Learning objectives

This chapter aims to provide a better understanding of the workings of finance and the economy. After reading through this chapter you should:

- Know where to find financial and economic data and source indicators such as inflation, gross domestic product and unemployment, and interpret them to write articles;
- Know the difference between monetary and fiscal policy, and the role of these in the economy;
- Understand some of the issues around trade;
- Understand some of the main issues around banking and access to financial products for economic development;
- Have a knowledge of basic terms for writing about companies and markets;
- Understand the relative roles of the public and private sectors in the economy;
- Know where to find statistical indicators for country comparisons;
- Have an overview of the institutions that regulate the economy and financial sector;
- Handle the kind of calculations needed to be able to report accurately.
Financial journalism

Many journalists seem to fear numbers. Yet numbers are often central to a story and understanding them can help you when you are working on an article. However, while numbers are important, they are not enough on their own. Interpreting them, putting them in context, seeing how they affect people, in short finding the story in them, is the real skill.

We live in a time of data journalism but we still need journalists to make sense of data. Financial data is no different, and financial journalism will become even more important as African economies develop, the private sector grows and there is more financial data to explore. If you don’t speak the language of finance and money you will be excluded from what is happening.

This chapter aims to introduce you to basic economic and financial ideas. It is an introduction to a vast topic. You can’t be expected to know everything. You are a journalist – not a financial expert. What you need know is how and where to find the answers, who you can ask to help you interpret the figures, and especially how to ask the right questions.

Basic Economics: Overcoming the fear of finance

Many journalists seem to fear numbers. Yet numbers are often central to a story and understanding them can help you when you are working on an article. However, while numbers are important, they are not enough on their own. Interpreting them, putting them in context, seeing how they affect people, in short finding the story in them, is the real skill.

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Economic and financial indicators

This section takes a closer look at three main indicators that affect policy: gross domestic product (GDP), inflation and the consumer price index (CPI), and unemployment.

Basic Economics: Measuring the economy

Open almost any newspaper and somewhere you will find those three familiar letters: GDP.

Global GDP will grow by less than 3% in 2016
Rwanda’s GDP grew by 7% in the second quarter of 2015
South Africa’s debt could surpass 50% of GDP
Agricultural activity represents 40% of African GDP
IMF revises projections of Kenya’s GDP

The letters GDP are often not even spelt out, underlining an assumption that most people understand gross domestic product and know what it means.

What is GDP?

GDP is a way of measuring the economy. It is one of the main statistics that governments compile. At its simplest level GDP is the total value of all the goods and services produced in a country in a given period. It measures the overall economic activity of a country.
It is important to understand what GDP is because it is used to measure a range of indicators. It is used to measure the growth (or lack of growth) of a country’s economy. Government debt is measured as a percentage of GDP (Ghana’s public debt climbed to 71% of GDP in 2015). It is used as a sign of whether a country is in recession. The sizes of the different economic sectors in a country are measured as a percentage of GDP. South Africa’s finance, real estate and business services sector is now 24% of GDP compared to mining at 11%; Zambia’s mining sector is less than 10% of its GDP – but accounts for 80% of its exports (Figures from 2015). GDP is also used to compare the economic health of different countries. It has become the figure used to measure a country’s success.

The importance that people place on GDP is seen in the reaction to news in 2014 that Nigeria passed South Africa as the biggest economy in Africa. Overnight the Nigerian economy grew from US$264 billion to US$510 billion, overtaking South Africa’s US$384 billion. Media coverage of this was at times quite emotional, such as describing this as a win for Nigeria because South Africa had lost its position as Africa’s largest economy to Nigeria. There is, however, a logical reason why Nigeria’s economy should be bigger than South Africa’s.

Consider these three possible reasons and think about which you believe fits:

1. **Nigerians are more hard-working than South Africans.**
2. **Nigeria has a stronger entrepreneurial culture than South Africa.**
3. **There are more people in Nigeria than South Africa.**

While 1 and 2 are possible contributing factors, the reason is simply that Nigeria has a population more than three times that of South Africa. With a population of 170-million compared to South Africa’s 52-million, Nigeria’s GDP should be more than three times the size of South Africa’s.

The article below (edited for length) from the US publication *The Atlantic* investigated this high-profile event and what it meant on a number of different levels.

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How Nigeria became *Africa’s biggest economy overnight*

**Does the continent’s most-populous country deserve its new title?**

Something strange happened in Nigeria on Sunday: The economy nearly doubled, racking up hundreds of billions of dollars, ballooning to the size of the Polish and Belgian economies, and breezing by the South African economy to become Africa’s largest. As days go, it was a good one.

It was, in fact, a miracle borne of statistics: It had been 24 years since Nigerian authorities last updated their approach to calculating gross domestic product (GDP), a process known as “rebasing” that wealthy countries typically carry out every five years. When the Nigerian government finally did it this week, the country’s GDP – the market value of all finished goods and services produced in a country – soared to $510 billion.

Nigeria’s overnight transformation raises two distinct but interconnected questions. First: What do we miss about countries when we don’t have accurate economic data about them – and what are the practical implications of that blindness?

In computing its GDP all these years, Nigeria, incredibly, wasn’t factoring in booming sectors like film and telecommunications. The Nigerian movie industry, Nollywood, generates nearly $600 million a year and employs more than a million people, making it the country’s second-largest employer after agriculture. As for the telecom industry, consider that there are now some 120-million mobile-phone subscribers in Nigeria, out of a population of 170-million. Incorporating the film and telecom industries into Nigeria’s GDP made a huge difference in the services sector, rendering the country’s economy not just bigger but more diversified.

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**2013 Nigerian GDP: old vs new estimates**

<table>
<thead>
<tr>
<th>Nominal GDP, in millions of Nigerian naira</th>
<th>2013 (old)</th>
<th>2013 (new)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>20 000 000</td>
<td>20 000 000</td>
</tr>
<tr>
<td>Industry</td>
<td>40 000 000</td>
<td>40 000 000</td>
</tr>
<tr>
<td>Services</td>
<td>60 000 000</td>
<td>60 000 000</td>
</tr>
<tr>
<td>Total</td>
<td>80 000 000</td>
<td>80 000 000</td>
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</tbody>
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Agriculture | Industry | Services | Total

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*Source: The Atlantic*
Cases like Nigeria’s indicate that “Africa as a whole probably is not as poor as we’ve long thought, the economist Diane Coyle writes in her well-timed new book, GDP: A Brief but Affectionate History.

“In many African, Asian, and Latin American economies, the GDP calculations take no account of phenomena such as globalization, or the mobile phone revolution in the developing world... There are fundamental weaknesses with the collection of basic statistics such as what businesses there are, what they are selling, or what goods and services households spend their incomes on. The surveys needed to collect this information are carried out only infrequently.... [O]ne estimate suggests that for twenty years sub-Saharan African economies have been growing three times faster than suggested by the ‘official’ data.”

And these economic indicators are not mere abstractions – they have real-world consequences. Coyle notes that when Ghana rebased in 2010, its GDP increased by 60 percent, transforming it instantly from a “low-income” country into a “low-middle-income” country. Aid organizations use these categories to determine levels of financial assistance.

All this brings us to the second question: Are we too obsessed with GDP as a measure of countries’ economic strength and health? As Coyle wrote, this week’s GDP overhaul will likely make investors and entrepreneurs more confident in Nigeria. And yet, “Nothing real has changed, the economic problems like poverty and inequality and a poorly-functioning state remain.”

South Africa’s GDP numbers are three times larger than Nigeria’s on a per capita basis. South Africa has a diverse, modern economy, while Nigeria remains heavily dependent on oil.... The good news is that the Nigerian government now has a better system for measuring its economy. The bad news? Knowing Nigeria has a $510-billion economy doesn’t reveal a whole lot about the welfare of its citizens.

Uri Friedman, THE ATLANTIC, APRIL 2014
Full article available at www.theatlantic.com

What is GDP per capita?

GDP per capita is what you get when you take the gross domestic product of a country and divide it by the number of people in the country. The higher the GDP per capita is, the higher the general standard of living in a country.

South Africa has a GDP per capita of $6 477. However, averages don’t tell the full story either, such as that income levels in South Africa are extremely unequal. While many of its citizens are well off many are still living in poverty.

And as the chart below shows, Botswana has a higher per capita GDP than South Africa.

<table>
<thead>
<tr>
<th>POPULATION 2014</th>
<th>GDP 2014 (US$ millions)</th>
<th>GDP PER CAPITA 2014 (US$)</th>
</tr>
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<tbody>
<tr>
<td>NIGERIA</td>
<td>177 475 986</td>
<td>568 508</td>
</tr>
<tr>
<td>SOUTH AFRICA</td>
<td>54 001 953</td>
<td>349 817</td>
</tr>
<tr>
<td>BOTSWANA</td>
<td>2 219 937</td>
<td>15 813</td>
</tr>
</tbody>
</table>

For some context on the size of the economies of these countries, compare them with the United States and China, the first and second largest economies in the world. China is expected to overtake the US and become the biggest economy in the world sometime in the next few years. However, as with Nigeria and South Africa, the GDP per capita of the US is likely to remain much higher.

Note, however, that the US does not have the highest per capita income in the world. Countries with a higher GDP per capita than the US include Australia (US$61 887), Norway (US$97 361), Singapore (US$56 286.8) and Qatar (US$97 518).

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<tr>
<td>UNITED STATES</td>
<td>318 857 056</td>
<td>17 419 000</td>
</tr>
<tr>
<td>CHINA</td>
<td>1 364 270 000</td>
<td>10 360 105</td>
</tr>
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</table>

Source: World Development Indicators, World Bank
Other indicators for country comparison include life expectancy; the percentage of the population living below the national poverty line; literacy levels; income inequality levels in a country; and the percentage of the population who are banked, a measure that has become important because of the acceptance that without access to financial services people may have difficulty doing business or engaging in trade.

The Human Development Index is a move to include broader measures of the quality of life rather than income alone. This United Nations Development Programme is a composite statistic to measure a country’s social and economic dimensions, based on health, education and standard of living.

Consumer Price Index:
Measuring the cost of living and inflation

Inflation – increasing prices of goods and services – is part of daily life. We can all remember when bread was cheaper, and when it cost less to get around. The opposite of inflation is when prices of goods and services fall. This is known as deflation and is also bad for economic growth because it causes the economy to stagnate.

Consider this example:
If five brothers are given a gift of R1 000, how much does each get if shared out equally? The answer is clearly R200.
Now imagine that the brothers have to wait for one year to get their share of the R1 000 and inflation that year is 6%. Will they be able to buy:

A. The same amount?
B. Less than they can buy today?
C. More with their share of the money than they could buy today?

While the amount of money they receive will be the same, prices would have increased by 6% so they will be able to buy less than they can buy today.

The only way the money would have increased in value is if it was put in a bank and the interest on this was more than 6%.
This is why annual wage increases are often linked to the inflation rate. If workers get an increase that is the same rate as inflation, this means the buying power of their money stays the same. If they want a real increase in what they are earning, the increase needs to be above the inflation rate.

Essentially inflation eats your money and high inflation means that the cost of living is increasing rapidly. It affects everyone, but it affects poor people more, as well as people living on a fixed income.

Deflation is the opposite of inflation, and while it may sound benign that the buying power of money increases rather than decreases, this is bad for a country. The economy shrinks because people put off buying goods while they wait for prices to come down. This has a ripple effect on the production of goods and is a sign that an economy is in trouble.

Prices rise for different reasons. When demand for products and services increases, suppliers can raise their prices. One reason for inflation is summed up in the phrase “too much money chasing too few goods”. This is known as demand-pull inflation, when demand is growing faster than supply. It can happen when central banks print too much money, either literally or through too-low interest rates creating too much credit or borrowing in the economy.

Another reason is “cost-push” inflation. The cost of producing goods may increase, pushing prices up. This can be internal such a bigger wage bill or the costs of materials or transport costs – or it can be caused by external forces, such as an increase in the price of oil, which would make transport cost more, or if the value of the currency falls. If a company is importing materials for a product and its currency falls, it will have to pay more for the imported goods.

Measuring inflation

Millions of goods and services are traded every day, and almost all these transactions have a price. The inflation rate shows the rate at which prices change from one period to the next, usually on an annual basis, but also on a monthly basis. It measures the changes in the level of prices compared to the previous year or part of a year. The rate of inflation is measured by using a price index known as the Consumer Price Index, or CPI. It is important to remember that CPI measures the rate of the increase not the price increases.

An index is a number that starts at 100 in a certain year, known as the base year. It changes over time compared with the base
year and can be converted into a percentage since the base year starts at 100. For example, if the Consumer Price Index is said to start at 100 in the year 2010 and then the index increases to 103 in 2011, the prices in that economy have risen by 3%. That means the inflation rate is 3% and that R1 will buy 3% fewer goods and services than it did at the end of the previous year.

How is the CPI calculated? This is done through indexing a basket of goods and services that are bought by households. What goes into the basket is different for different countries and is usually reviewed every few years to take into account changing consumer buying patterns.

Many countries have inflation targets and you will learn more about how government tries to keep inflation in check under the Monetary Policy section.

At present a number of African countries have double-digit inflation rates, including Malawi, where it was 24.9% in December 2015, and Ghana, where it was 17.7% at the end of 2015.

When inflation is out of control is becomes hyperinflation. Hyperinflation is rapid inflation and can lead to the breakdown of a country’s monetary system, such as in Zimbabwe.

**Things to remember about inflation**

Inflation is the phenomenon of rising prices; the inflation rate measures how much the retail prices of a basket of goods and services rise over a period; the Consumer Price Index (CPI) is used to calculate the inflation rate.

So if the inflation rate went from 5% to 6%, don’t write, “Inflation rose last month,” or “The CPI rose last month.” It’s the inflation rate, measured by the Consumer Price Index, that increased.
When inflation goes up, the buying power of money goes down. Inflation affects rich people more than poor people because they have more money. Deflation is bad for an economy because money loses its value. Many people in Brazil lost all their savings after hyperinflation in the 1980s. Unemployed people don’t have to worry about inflation because they aren’t earning a regular income. Hyperinflation in Zimbabwe was fuelled by the government printing too much money. Deflation discourages consumers from spending because they want to wait for prices to fall further. Owning your own house can be a hedge against inflation as the price of property also rises when there is inflation. Deflation is good for an economy because prices decrease. Deflation can lead to job losses because demand for goods decreases. The use of price freezes has been successful in stopping hyperinflation. Hyperinflation makes it impossible for families to afford the basic commodities they need every day. When the interest rate offered by banks is less than the inflation rate, people have no incentive to save because their money is reducing in real terms. If food prices continue to rise more people will be pushed into poverty. People living on fixed pensions are affected by inflation because the amount of money they get each month stays the same while prices increase. Governments have the power to control the price of goods including the cost of imports. If your bank pays 5% interest a year on the money you are saving it will keep its value even if inflation is 6% a year. Hyperinflation is a sign that people in a country have lost faith in their currency. A decrease in the global oil price is likely to push up prices and increase inflation in those countries that import oil. Deflation is a sign that a country’s economy is beginning to strengthen.

Brazil is another country that has suffered hyperinflation – but found a way out of it. In the early 1990s, Brazil’s inflation rate hit 80 percent a month. What this meant was that if, say eggs costs $1 one day, they’ll cost $1.80 a month later. Over a year that would mean that they would cost more than $1 000. In practice, this meant that shops had to change their prices every day. Someone had the job each day of going up and down the aisles in the shop putting new prices on the items on the shelves. When people came to shop they would look for him and then run ahead, so they could buy their food at the previous day’s price. Inflation started to rise in Brazil back in the 1950s, when the government printed money to build a new capital in Brasilia. By the 1980s, inflation was out of control. The country first tried a price freeze to end this. This failed and the president lost his job as a result. Four economists then came up with the idea of creating a parallel currency. This was done and eventually the new Real was introduced in 1994. For more on this story listen to the Planet Money Podcast, How Fake Money Saved Brazil (http://www.npr.org/sections/money/2010/10/04/130329523/how-fake-money-saved-brazil). Brazil managed to keep its inflation low for more than two decades. Recently, however, inflation has begun to rise again and at the end of 2015 was more than 10% for the first time in 12 years.

Exercise #1

Understanding inflation

Which of these statements about inflation, deflation and hyperinflation are true and which are false?

1. When inflation goes up, the buying power of money goes down.
2. Inflation affects rich people more than poor people because they have more money.
3. Deflation is bad for an economy because money loses its value.
4. Many people in Brazil lost all their savings after hyperinflation in the 1980s.
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18. Hyperinflation is a sign that people in a country have lost faith in their currency.
19. A decrease in the global oil price is likely to push up prices and increase inflation in those countries that import oil.
20. Deflation is a sign that a country’s economy is beginning to strengthen.
Job creation is one of the biggest economic issues of our time— not only in the developing world but also increasingly in countries in the developed world, where unemployment shot up after the 2008 global financial crisis. Countries such as Greece, Spain and even Ireland have reported figures as high as 40% youth unemployment in recent years. And keeping the population employed is seen as a political victory— even in the United States, where during President Barack Obama's time in office he scored political points for having the lowest unemployment figures in years.

Unemployment statistics for a country are calculated by the statistics office of the government. In South Africa the unemployment figures are reported every quarter. But how is unemployment defined? What does this figure include?

The first thing to understand is who is included in the labour force. Obviously pensioners and retired people as well as children are excluded. Full-time students are also excluded as they are regarded as not having yet entered the labour force. Adults staying at home to look after children are also excluded.

In theory then, the labour force should cover all people of working age who are either employed or want to work and are looking for employment—it is the total number of people who are working or unemployed. However, many countries exclude those they call “discouraged workers”. A discouraged worker is someone who was looking for work but has given up. They would like to have a job but have stopped looking and therefore do not get counted in the unemployment figure. This is one reason why some economists believe the unemployment rate underestimates the actual level of unemployment in a country.

This skews the picture. In South Africa for example, the official unemployment rate is around 25%; but if discouraged workseekers were included the rate would be more than 40%.

It is therefore crucial to know what has been included in the unemployment figure when you are writing about this and trying to make sense of it. Consider the figures in the paragraph below, extracted from an article printed in a South African newspaper in 2015, as an example.

SOUTH Africa’s unemployment rate - 25 percent at the most recent count — is among the highest in the world. It is the highest among nations that could be considered “competitor economies” or significant trading partners. Unemployment in Nigeria, Africa’s largest economy and South Africa’s putative partner for continental economic development, stands at 6.4 percent. It averages 9.7 percent in the European Union, South Africa’s largest trading partner bloc. South Africa’s unemployment is higher than all the other BRICS nations combined (Brazil - 6.7, Russia - 5.5, India -3.6, China - 4.1). In Southern Africa, Swaziland, Lesotho and Namibia have worse numbers, and Botswana, at 17 percent, comes close to South Africa. But the size and population profile of those economies is very different, and Lesotho’s horrific 42 percent still translates to small numbers of jobless adults.

This article frames the serious unemployment problem in South Africa by comparing it with other countries, such as Nigeria and its partners in BRICS, Brazil, Russia, India and China, which all seem to be managing job creation much better—at least according to the figures.

A number of things make it difficult to know if this is accurate.

For starters the article fails to source the figures. There are a number of different data sets for unemployment figures. Have these all come from the same data source? Are they from the same year? Without knowing this it is difficult to know if you are comparing like with like.

Also, what is included in the figures to make them so low? Has Nigeria included its sprawling informal sector to have an unemployment rate as low as 6.4%? Has India included its massive public employment programme, the National Rural Employment Guarantee Programme, which is providing work for 50 million households, to have the exceptionally low unemployment figure of 3.6%? Again, without being able to answer these questions it is not possible to know if the comparison is accurate.

The other thing this article highlights is the problem of working with averages. According to this the European Union has average unemployment rate of 9.7%. There are 28 countries—so what does that average tell you about all these countries? In Greece, for instance, according to Trading Economics, the youth unemployment rate increased to 48.6% in July from 48.1% in June of 2015. Averages rarely tell the full story.

What the story does highlight, though, is the need to be careful in making country comparisons based only on percentages—indeed, 42% of Lesotho’s population is far fewer people than 42% of South Africa’s population.
Monetary and fiscal policy are used to drive the outcomes of a country’s economy. How they are used has a direct effect on GDP, inflation and unemployment.

Monetary policy is the management by the central bank of a country’s money and interest rates. Fiscal policy is the government’s use of its spending, taxation and borrowing to influence the economy.

It’s easy to feel that these policies are far removed from your own daily life. But they have everything to do with your life. If inflation increases dramatically, you may find that your pension is now worth only half what it was before. If interest rates are too low, you may find that it is not worth saving as the returns are so low. If interest rates go up you may find that your mortgage bond is now too expensive, and you may even lose your house because you can no longer afford the repayments. A business that took out a loan to set up may find it is no longer profitable and have to close. If personal tax increases, you will have less money in your pocket every month. If government raises too much debt to finance programmes such as infrastructure or education, it may have to cut other things such as social grants or providing health care.

One of the reasons people feel dislocated from monetary and fiscal policy is that the language used to talk about these is often obscure and jargon. The regular announcements by central banks are a good example and have even been dubbed “central bank-speak”. This section aims to help you understand the language that central banks and economists use so that you will feel less excluded and more empowered and through this write about these policies with insight. And know what questions to ask.

One of the main roles of the central bank is ensuring price stability in a country, which means protecting the value of a country’s money by controlling inflation. It does this through setting interest rates. Other functions include foreign exchange control, supervision of commercial banks, and the issuing of bank notes and coins.

The main instrument for controlling inflation is the setting of interest rates. Interest is the money you pay to use money that does not belong to you — for loans, mortgages, hire purchase for cars and household goods. It is also the amount paid to people for saving. If interest rates are too low — especially if they are below the inflation level, the incentive to save is removed.

The ripple effect through the economy of interest rates is captured in this quote from John Lanchester in his book How to Speak Money:

If I had to pick one term that summed up my reason for wanting to write this, it would be interest rates. I must have heard interest rates mentioned in the news thousands of times before I found out why they were so important. When the financially literate talk about interest rates, they’re bringing to bear a whole set of linked ideas about inflation, unemployment, the cost of borrowing, the exchange rate, the political impact of rising mortgages, the conditions of trade for business, the price of exports, the balance of payments and the growth or contraction of the economy — all packed into two words, “interest rates.”

…To people who don’t speak finance, the language can seem impenetrable and the interlocking ideas too complex to grasp or unpack at the necessary speed. The reason interest rates matter so much is because the interest rate is the cost of money at any given moment. It’s also the rate at which it is possible to invest risk-free, because you can buy a government bond at the prevalent interest rate, and it’s guaranteed to pay you back. This means that when interest rates go up:

1. Life is harder for businesses, because money is more expensive, and
2. people will tend not to invest in companies, preferring to invest in risk-free bonds, and
3. the stock market will fall for that reason, so
4. confidence in general will fall. In addition,
people with mortgages will find it harder to make their repayments, and those who are coming off fixed-rate deals may suddenly have a dramatic increase in their monthly repayments. That means mortgage defaults will rise, so there will be downward pressure on house prices, and some people will be in negative equity, which will stop them spending money. Also, the currency will rise, because higher guaranteed rates of investment will attract money into buying the country’s debt, so life will become harder for manufacturing businesses, because their exports will be more expensive. Not only that, but inflation will fall – remember, inflation means money is worth less, whereas a rise in interest rates means money is more expensive.

There’s more, too, but these 11 things are a starting point for all the things that are completely taken for granted by people who speak money when they hear “interest rates”.

**Basic Economics:** Central banks and interest rates

The public face of monetary policy is the governor of the country’s central bank, who makes the regular announcements about interest rates. In South Africa the central bank is the South African Reserve Bank; in Nigeria it is the Central Bank of Nigeria; in Uganda it is the Bank of Uganda.

The setting of interest rates is influenced by a number of things including the inflation rate. Most countries have a desired range for inflation, and this is known as “inflation targeting”. In South Africa this is between 3% and 6%; in Nigeria it is between 6% and 9%; and in Kenya it is between 2.5% and 7.5%.

The central bank interest rate is usually known as the bank rate. In South Africa it is known as the repo rate, which stands for repurchase rate and is the rate the central bank lends to commercial banks.

In South Africa, the commercial bank rate is known as the prime rate, and is 3.5 percentage points above the repo rate. Note that African countries are used to high interest rates. In the US and Europe rates are low. Ghana has one of the highest interest rates in the world.

When the governor announces a rate increase or decrease he or she speaks about basis points and percentage points. There are 100 basis points in one percentage point.

- If the repo rate is increased from 5% to 6%, this is an increase of 100 basis points or one percentage point.
- If repo rate is increased from 5% to 5.5%, this is an increase of 50 basis points or half a percentage point.

If the repo rate is decreased from 5.5% to 5.25%, this is a decrease of 25 basis points or a quarter of a percentage point.

**Regional central bank**

The eight members of the West African Economic and Monetary Union have a common central bank, the Central Bank of West African States (La Banque Centrale des Etats de l’Afrique de l’Ouest – BCEAO). The Union has adopted the CFA Franc as a common monetary unit, which has been pegged to the Euro. The bank is based in Dakar and members are Benin, Burkina Faso, Ivory Coast, Guinea-Bissau, Mali, Niger, Senegal and Togo. However, being pegged to a strong currency has its problems, such as making exports expensive.

**Basic Economics:** Exchange rates

The exchange rate is the rate at which one country’s currency can be traded or exchanged for another country’s currency. It determines how cheap or how expensive it is for you to buy imported goods, such as television sets, clothes, and tyres for your car. A high exchange rate against the US dollar makes the currency more expensive, which increases the price of imported goods and services. This means you can buy fewer things that have been imported such as electronics for every Rand or Naira you make. If a company uses the services of a foreign consultant, this becomes more expensive.

Central banks sometimes try to protect the country’s currency by using their foreign exchange reserves. A number of countries in Africa did this in 2015 as many currencies have been in free fall against the dollar. Nigeria, for instance, decided to use its reserves to support the local currency in 2015. This was after the Naira has fallen by about 25% against the US$ in the previous year. And Angola’s central bank also used a third of its foreign exchange reserves, US$10bn, in 2015 to hold the kwanza’s depreciation against the dollar at about 30%.
**Exercise #2**  Who loses from a weakening currency?

One of these does not fit. Which one?

1. Companies that are exporting goods.
2. People who are being paid in foreign currency.
3. People receiving remittances from abroad.
4. People living in Zimbabwe receiving money from family working in South Africa.

**ANSWER**

4) The Rand-US$ rate has moved from R8 in 2012 to more than R15 in 2015 and the US$ is now the official currency in Zimbabwe so people there receiving money from South Africa are getting almost half of what they received before.

**Exercise #3**  Who gains from a weakening currency?

One of these does not fit. Which one?

1. Consumers of imported goods such as electronic goods.
2. Countries that rely on importing oil as this increases costs such as transport, both for individuals and also for companies moving goods around.
3. Farmers who are selling their produce abroad.
4. Local retailers who import food products from abroad.

**ANSWER**

3) Farmers selling produce abroad are now getting more for their goods.

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**Basic Economics: Fiscal policy**

Monetary policy and fiscal policy are complementary. While monetary policy focuses on the way the central bank of a country manages a country’s money supply, fiscal policy focuses on how government raises money and spends it to manage a country’s economy – government’s income and expenditure, as reflected in the budget.

Income is raised mainly through taxes, and through borrowing or government debt. Sometimes government will move something off its balance sheet and try to fund it differently. Toll roads are an example of this, where the user rather than government pays for the use of the road. However, some people see this as another way of taxing people and this can become unpopular.

Fiscal policy, announced through the annual budget, is always a juggling act – decreasing taxes means more money in the economy for people to spend, and more economic activity. When the government lowers your taxes through fiscal policy, it puts more income in your pocket. This means more money to spend, usually resulting in overall increased demand for goods and services. It also means that the government has, at least in the short term, less money to spend unless it borrows.

How government decides to allocate its expenditure is essentially a political matter. For instance, a government can raise taxes to provide more social welfare, or free education, or public health care. It must decide how much to spend on what, depending on how much money it has and its policy priorities. Providing free higher education, for example, may mean that more money cannot be spent on social welfare. When government presents its budget, the amounts it devotes to particular programmes and projects tells us what its actual political priorities are, as opposed to what it may say at election time.

Budgets are instruments of government accountability to the citizens. For this reason, budget transparency is important and there is growing pressure on governments to release more and reliable budget data. The International Budget Partnership (www.internationalbudget.org) Open Budget Index compares countries and measures budget transparency. Of countries in Sub-Saharan Africa, South Africa scores highly on the Open Budget Survey index 2015, coming third in the index after New Zealand and Sweden. Sierra Leone was listed as 43, followed by Ghana at 45, Kenya at 51 and Botswana at 53.

When the government wants to grow the economy, it is known as expansionary policy. To do this, the government can reduce taxes or spend more to stimulate the economy. Contractionary policy, which is characterised by a decrease in government spending
or increases in taxes, has the opposite effect.

A government budget resembles a household budget but is not the same. You would probably like your household budget always to balance, in other words not to spend more than you earn, and always to have money left over to save. However, a balanced budget achieved through simply matching spending and revenue is not necessarily a good thing for a country. Sometimes it is necessary to borrow, particularly for large infrastructure projects, to facilitate economic growth.

Governments can try to manage economic growth through spending and borrowing less or more. They do this by increasing spending, and borrowing more to do so, when the economy faces headwinds, and spending less than is raised in revenue when the economy is booming, to rein in economic activity to control inflation and also save money for the proverbial “rainy day”.

So a government can run a budget deficit, spending more than the revenue, mainly from tax, that it brings in. And they can achieve a budget surplus, which can be put aside for tough economic conditions.

The budget deficit
A government can do a number of things to balance its budget, such as:

- Raising more income from taxes, including indirect taxes such as VAT (value added tax).
- Freezing government posts and cutting the wage bill.
- Placing a ceiling on spending for items such as old age pensions and other items of social welfare, health and education.

The other way government can find money to balance its budget is by raising debt.

Government debt
There is always political pressure on government to spend money, since the demands of society are almost infinite. Why not always borrow as much as possible? The answer is that interest has to be paid on loans, and if too much is borrowed, the interest can overwhelm the ability of the government to pay. In any case, borrowing means that interest payments divert spending from other areas.

Government debt is measured as a percentage of GDP. The Greek debt in 2015 was 200% of its GDP. South Africa’s is 48% and rising. In the 2015/2016 financial year its total net debt was set to be R1.78-trillion. This meant the government will have to spend about R350-million a day on servicing its debt. If it becomes too big, it will eventually have to cut other spending in the budget to pay the interest on the debt and to pay the actual debt.

How much governments borrow is both intensely political and technically important. Opposition parties may accuse cautious governments of not doing enough for the voters. Lenders will demand higher interest rates on government debt if they think a government is being irresponsible in its borrowing and may not pay back the borrowed money. Governments perceived to be too zealous in cutting spending to bring down deficits are accused of austerity finance. How much or how little to borrow is contentious.

Not all economists agree about how much debt is good or bad. In this, and other areas of economic policy, it is wise to seek a range of voices to deepen and broaden your news or feature item.

The most common way for government to raise extra money (debt) is through the issuing of government bonds. The amount that government pays for its debt is affected by the Credit Rating Agencies.

Credit ratings agencies
Ratings agencies pronounce on the likelihood that a government will not pay back, or default on, its debt. Their ratings, on a scale from investment grade to junk, determine how risky the government is supposed to be as a borrower, and therefore how much interest governments must pay to raise money, usually through issuing bonds. If the ratings agencies believe that a government is spending too freely and borrowing too much, they may downgrade the government’s debt rating.

Exercise #4
Monetary policy or fiscal policy?

This exercise will assist you in distinguishing the difference between monetary and fiscal policy. Which of the following statements, taken from news articles in 2015, are linked to monetary policy and which to fiscal policy?

1. Nigeria kept interest rates unchanged even as inflation accelerated to 9.3% in August 2015, exceeding the central bank’s 6% to 9% target band for a third month.

2. At the end of 2014, taxpayers owed the Rwandan government Rwf122 billion ($168 million) in unpaid taxes spanning many years, highlighting the poor culture of paying taxes in Rwanda.

3. Linking the Namibian dollar to the South African Rand has helped stabilise inflation, which has generally remained at a lower average than the average inflation in Sub-Sahara Africa.

4. The Kenyan central bank governor said that higher interest rates had helped to curb inflation.

5. The Zambian government has promised public servants pay increases even though the public service bill makes up about 52% of the country’s budget.
In September 2015, the Bank of Ghana raised its main rate by 100 basis points to 25%, the highest rate in over a decade, to offset the risk of inflation, which reached 17.9% in May before declining to 17.3% in August.

Kenya’s shilling has weakened 14% against the dollar this year (2015), prompting the central bank to raise borrowing costs by 300 basis points since June.

Ghana moved to control government spending as a decline in oil revenues threatened its budget.

The interest bill is one of the fastest growing items on the South African government’s budget as government debt continues to rise.

Kenya will hire a director-general to be in charge of debt as the International Monetary Fund (IMF) pushes the country to manage its ballooning public debt.

Bank of Mozambique left its benchmark lending rate unchanged at 7.5%, saying the impact of the fall in commodity prices on the country’s balance of payment posed risks to the economy.

Botswana plans to finance a projected budget deficit by drawing down on government reserves and issuing bonds.

Angola’s currency fell to a record low after the central bank devalued the kwanza as the drop in oil prices cut the main source of government revenue and export earnings.

Nigeria’s central bank has turned to foreign-exchange controls to stabilise the naira after the currency fell almost 10% against the US dollar in the first two months of 2015.

South Africa’s tax revenue has grown significantly due to economic growth with the income tax register expanding from three million taxpayers to almost 20 million.

Zambia’s kwacha firmed after the central bank sells dollars to support the currency.

Government debt in Angola is expected to jump above 40% of GDP in 2015 from 23.1% in 2013.

Plunging copper prices means Zambia’s government is now facing a budget deficit.

Nigeria is considering doubling the VAT (value-added tax) rate to 10%.

Botswana’s government said that while economic growth and employment creation remain a top priority it will, in its next national budget, allocate a large sum of funds to water and electricity.

ANSWERS
1, 3, 4, 6, 7, 11, 13, 14, 16 are monetary policy;
2, 5, 8, 9, 10, 12, 15, 17, 18, 19, 20 are fiscal policy

Writing about banking provides an opportunity for a wide range of stories. Some are specific to the industry, such as the launch of a new bank or new banking product. Some deal with regulation – how and why government is regulating the industry. Some are more universal, such as what role did banks and other financial institutions play in the global recession of 2007-2008? Some focus on the bank itself as an investment.

Some recent banking stories from Africa worth investigating include following up on the rescue of African Bank in South Africa after it almost went under because of its bad debt levels; Nigeria’s Ecobank Transnational Incorporated, one of Africa’s leading regional banks, posting a 52% growth in profit in 2015; South Africa’s First National Bank (FNB) following its expansion into select African countries with the launch of an Islamic banking product in Zambia and Tanzania; Kenya’s central bank ordering Imperial Bank to be put under judicial management following fraud of more than US$335-million; Kenya’s Equity Bank chairman citing social media as an effective tool for expanding access to banking; and an estimate from the Reserve Bank of Zimbabwe that Zimbabweans in the diaspora are remitting between US$1.7-billion and US$2-billion back into the country each year.
Like other economic and financial topics, banking has its own language. The banking terms below are an introduction to some of the most common.

**Interest**: The money you pay to use other people's money, whether informal lenders or formal banks, charged by the lender to the borrower. Also refers to the amount you make on funds that you have invested. The interest rate is a percentage of the debt or investment over a period of time.

**Interest rates**: The interest rate is the percentage charged or earned on money borrowed or invested. Interest rates often change because of inflation and central bank policies (see monetary policy, inflation targeting, central bank rate and commercial bank rates).

**Credit rating**: A ranking applied to people or businesses that is based on their credit history and is used as a measure of the likelihood that the debt will be repaid.

**Credit history**: A report on a person's or business's record in handling their credit arrangements, such as whether they made regular payments or defaulted on the debt. A credit history is often used by a lender to assess a loan application.

**Housing bubble**: An increase in housing prices that is fueled by demand, speculation and the belief that prices will always rise. Housing bubbles usually start with an increase in demand in the face of limited supply. Speculators enter the market, believing that profits can be made through short-term buying and selling. This further drives demand. At some point, demand decreases, or stagnates at the same time supply increases— and the bubble bursts, often meaning that many paid more for their properties than they could realistically be sold for.

**Underwater – mortgage**: An “underwater” mortgage is when the outstanding balance of the mortgage loan is higher than the money the property can fetch if it were sold.

**Reserves**: Money the banks hold as cash in their vaults or as deposits with the central bank.

**Money supply**: The entire stock of currency and other liquid instruments in a country’s economy at a particular time. The money supply can include cash, coins, and balances held in cheque or current and savings accounts. The central bank monitors the country’s money supply.

**Regulatory environment**: It is important to understand the regulatory environment that banks work in. This includes international regulation, regional regulations and country regulations, which are different for different countries.

**Payments systems**: A system that allows banks to exchange the debits and credits of their customers with customers of other banks.

**Collateral**: Any asset or property that a borrower puts up as security for a loan, to be forfeited if the borrower defaults. Necessary for “secured credit”.

**Unsecured credit**: Loans granted without collateral. The lender has to take legal action to get money back if the borrower defaults, and does not have prior claim on assets.

**Commercial Bank**: A financial institution that offers a broad range of services from banking to savings, credit and payments.

**Development Finance Institution**: DFIs are government-funded financial institutions that provide finance for investments that promote development. Examples of DFIs include South Africa's Industrial Development Corporation and the Development Bank of Southern Africa, which services the Southern African Development Community; the Bank of Industry and the Bank of Agriculture in Nigeria; and the East African Development Bank, which has its headquarters in Uganda.

**Financial capability**: People's knowledge and skills to understand their own financial circumstances, along with the motivation to take action. Financial capability is a broader concept than financial literacy, which is essentially people's ability to understand finance and economic issues.

**Access to finance**: Access to finance refers to the availability of financial services, including deposits, credit, payments, or insurance, to individuals or enterprises. In Africa, on average, less than 20 percent of households have access to formal financial services, with low population densities, poor transport and limited communications infrastructure contributing to this lack of supply. Even where such services are available, low-income individuals and small and medium businesses often have difficulty accessing these as they do not have the required documentation or collateral. The aim is to find ways to lower these barriers to access and offer suitable financial products, also known as financial inclusion (see next section).

**Informal finance**: Financial services that are unregulated by central banks or other supervisory and regulatory bodies. This type of financing is generally not arranged through formal agreements and is not enforced by law. Informal lending and savings schemes remain common in Africa.

**Microfinance**: This covers the provision of a range of financial services to low-income households, including loans, savings, money transfers and insurance, often at high interest rates.
**Key terms (cont.)**

**Microinsurance:** Insurance that protects low-income people against specific perils, such as the costs of funerals.

**Mobile banking:** The use of mobile phones to transfer money and access other banking services. Increased mobile phone ownership has changed the economics of providing financial services, particularly in remote areas. This has dramatically increased the number of people who can access these services.

**SME financing:** The small and medium-sized enterprise (SME) sector is now recognised as important for economic development, and is a significant sector in many African countries. SME financing are services specifically created for small and medium-sized enterprises, such as access to loans and leasing.

**Branchless banking:** Delivering financial services through non-bank outlets, such as, in South Africa, supermarkets.

**Banked population:** The percentage of the population with a bank account. This indicator is increasing used as one of the measures of the economic development of a country.


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**Basic Economics: The big African story – financial inclusion**

The banking sector is useful for looking at the relative roles of the private and public sectors. While the banking sector is mainly in the hands of private companies, regulating the sector is the work of government. Many believe that inadequate regulation of the banks fueled the financial crises in the United States in 2007-2008, which precipitated a global financial crisis, the effects of which are still being felt throughout the world.

Adequate regulation is essential to protect the banking system, but much intervention threatens innovation in the sector. Innovation in banking became a catchphrase in the first decade of this century as the idea of financial inclusion became tied to economic growth.

Lack of access to affordable banking services, credit and insurance was identified as hampering trade and the growth of key areas such as small business. The main reasons identified was that people, and emerging businesses, remained unbanked because of costs, travel distances to reach banks, and the often-burdensome requirements, such as ID documents, proof of residence and income, needed to open an account.

Banking Africa’s unbanked population has been on the agenda since then. Evidence, however, is that while financial inclusion has been successful on many levels, significantly increasing people’s access to services, it has increasingly been accompanied by growing debt levels.

This push for financial inclusion has raised concerns that increasing access to products such as credit is exposing low-income people and emerging entrepreneurs to predatory lending, and needs to be backed by greater economic literacy so that people are better able to manage their financial affairs as well as appropriate market regulation to ensure that the industry behaves responsibly.

The article below (edited for length) by Illana Melzer of Eighty20 Consulting takes a hard look at the link between financial inclusion and economic growth, and who is benefiting, and also the increasing problem of debt.

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**Rising star or red flag**

**South Africa’s financial inclusion growth raises questions for the entire industry**

South Africa was placed second in a recent Brookings Institute study comparing financial inclusion in 21 developing countries – surpassed only by Kenya. But though this has occasioned a number of glowing headlines, there’s a troubling aspect to these findings.

According to the report, financial inclusion refers to “both access to and usage of appropriate, affordable and accessible financial services.” The report suggests that “having greater access to financial services promotes entrepreneurship, lifts people out of poverty and gives them greater hope for a brighter economic future.” Its first key takeaway is that “access to and use of formal financial services provide opportunities for facilitating individual prosperity and economic development.”

This may sound like unalloyed good news, but the report fails to support these assertions. It simply presents them as fact, or articles of faith: It’s a given that financial inclusion delivers demonstrable developmental dividends. Indeed, the framework used to assess financial inclusion makes absolutely no mention of the impact of increased access to and usage of financial services on the lives of the newly included. Surely we need to ask whether this focus on financial inclusion is a helpful approach, and whether it furthers the important agendas of the developmental organisations and donors involved.
Rising star or red flag (cont.)

**Do More Accounts Equal Greater Social Impact?**

Let’s explore the South African data in a little more detail. According to the report, “Financial inclusion in the country increased from 61 percent in 2004 to 86 percent in 2014.” That is no small change. Admittedly, we have no counterfactual, but given the expectations for financial inclusion set out in the report, we would expect to see some visible impact on entrepreneurship or poverty levels in light of this very significant improvement. In that regard the data is somewhat disappointing. According to the Labour Force Survey of 2004 there were 1.4 million black African business owners in South Africa. In 2014 there were 1.5 million (Eighty20 data). This is hardly an achievement given South Africa’s staggering levels of unemployment – there are 7.4 million unemployed black South Africans, including so-called discouraged workseekers, who by definition have lost hope of a brighter economic future. The connection between financial inclusion and entrepreneurship is clearly less direct than anticipated.

With poverty, South Africa has seen significant improvements in living standards and a reduction in hunger and deprivation over the past 10 years. But this is a result of direct assistance provided by the state. By way of example, in 2004 there were 7.9 million recipients of government grants, receiving a total of around R45 billion a year. By the end of 2014 there were over 16 million beneficiaries receiving R120 billion.

These grants are paid electronically into bank accounts established precisely to facilitate a more efficient grant payment system. Grant recipients have become financially included because they are poor enough to receive government grants. Likewise, their levels of poverty have been reduced because they receive grants, not because they have bank accounts. Overwhelmingly, it appears that grant beneficiaries cash out their benefits in full – jettisoning financial services in favour of hard currency, as do many wage earners who are paid their salaries directly into a bank account. While this calls into question the impact of increased banking penetration for the poor, there is one clear beneficiary: The financial inclusion agenda, for which more accounts apparently mean greater success, no matter how they are used.

**More Opportunity – or Just More Debt?**

Of all the statistics celebrated in the report, it is the one related to increased credit usage that is most perturbing. Yes, there has been a significant increase in the number of South Africans using formal credit products. According to the latest Credit Bureau Monitor (Q1 2015) by the National Credit Regulator (NCR), there are 23.1 million credit-active South Africans, up from 17.1 million in Q4 2007, when the first Credit Bureau Monitor was published by the regulator. Using data from the Labour Force Survey for the corresponding periods, the proportion of credit-active South Africans has increased from roughly 57 percent of the adult population to 70 percent.

However, there is clearly a significant problem with borrowers’ ability to repay – a basic indicator of impact. According to the Credit Bureau Monitor, just 43 percent of borrowers who are credit active are current on all of their accounts. Thirteen percent are one or two months in arrears, while almost a quarter are behind by 90 days or more. A further 10 percent have adverse listings (that is, their debts have been written off or handed over for collection). And in retail credit, according to credit bureau data over 40 percent of borrowers with open accounts are 90 days or more in arrears on their worst performing account in that category. What’s more, a staggering 11 percent – or 2.5 million borrowers – have a judgment against them, typically an attachment order compelling an employer to deduct outstanding repayments directly from payroll. This mechanism is blatantly abused by debt collectors.

Aside from the high levels of arrears, the application of borrowed funds is also worthy of scrutiny. According to the NCR, two percent of South Africa’s gross debtors book comprises developmental credit. This category includes loans granted for housing, education and small business development. By far the most significant category of credit is retail credit.

**Important Truths – and Dangerous Risks**

The data clearly show that the problem is not one of access to credit. There is plenty of credit – possibly too much. The challenge is to somehow direct available credit toward promoting entrepreneurship, lifting people out of poverty and giving them greater hope for a brighter economic future rather than funding, at great expense, the purchase of new clothes and cars.

Indeed, given the high default rates, high cost of borrowing, high levels of indebtedness and limited mortgage lending in South Africa, it may be fair to say that access to and usage of credit entrenches patterns of inequality and exacerbates poverty. It would appear that financial inclusion has delivered far greater benefits to providers and officials than it has to the intended beneficiaries.

-- NEXT BILLION, SEPTEMBER, 2015

Complete article is available at www.nextbillion.net
The Brookings Institute study mentioned in the previous article placed South Africa second in a comparison of financial inclusion in 21 developing countries. Kenya was first. The main reason for this is the widespread use of mobile money in Kenya, which does not require people to have a bank account, in particular the phenomenal success of the M-Pesa product.

In contrast, the attempt to launch M-Pesa in South Africa has twice failed. The reason tells you a lot about the different banking environments in the two countries, including the regulatory environment.

**M-PESA IN KENYA**

The International Monetary Fund, in its 2014 Financial Access Survey reported a dramatic increase in the number of active mobile money accounts in Kenya. The number of mobile money transactions increased by more than 130 times, from 5.5-million in 2007 to more than 700-million in 2013.

This statistic is not surprising given the incredible uptake of M-Pesa, a mobile-phone money transfer and micro-financing service launched in Kenya by Vodafone in 2007. Upwards of 75 percent of Kenya's adult population now use M-Pesa to process payments for a range of goods and services.

> From Banking Africa’s unbanked population is not the solution to improved inclusion – Niyi Aderibigbe, Venture, February 2015.

**M-PESA IN SOUTH AFRICA**

A second attempt by Vodacom to launch the M-Pesa mobile payments platform in South Africa has flopped. On Monday, the mobile operator conceded that since it relaunched M-Pesa in the local market last July (2014), it has signed up only 72 000 active customers. It had been hoping for 10-million sign-ups in the first five years.

Vodacom first introduced M-Pesa to South Africa in 2010 and, although initial take-up was strong, it failed to take off as it has in other markets. Last July's relaunch was meant to spur renewed interest and demand for M-Pesa in the South African market and address the problems it faced after it was first launched in 2010.

As part of the relaunch of the service in South Africa, Vodacom ended its relationship with Nedbank, with which it launched M-Pesa locally, choosing to work instead with Bidvest Bank and Visa.

The relaunched service offered customers a chip-and-Pin Visa card and a voucher system to upload cash as well as giving customers access to 27 000 ATMs and 240 000 merchants. Despite rewards offering consumers double airtime when purchasing airtime via M-Pesa and free airtime to activate the Visa card, it's now clear that the relaunch has failed to live up to expectations.

> From Vodacom’s M-Pesa relaunch is a flop — Duncan McLeod

To find the answer to the question of why M-Pesa succeeded in Kenya and failed in South Africa, you need to consider three aspects:

- The regulatory environment
- The business environment
- The M-Pesa product itself

**The regulatory environment:**
The Central Bank of Kenya remains actively involved in the regulation of mobile money services in Kenya. However, it has taken an open approach to allowing telecom operators to offer mobile money services without the requirement of bank partnership. This is not possible in South Africa, where Vodacom had to partner with a registered bank to launch M-Pesa.

**The business environment:**
The business environment in Kenya was highly conducive at the time of the launch in 2007. In Kenya 38% of people didn’t use any form of financial service, formal, semi-formal or informal before the launch of M-Pesa, and only 19% of the population had access to formal financial services. The demand for this kind of service was high – due to lack of competitive money transfer services. Also, transferring money is a common practice in Kenya especially among urban migrant workers wishing to send money back to their families in the villages. Before M-Pesa people would resort to sending money with someone (possibly a stranger) who was travelling to their village.
By contrast, in South Africa, the banking sector is highly developed and has been working on financial inclusion and access to services since the voluntary Financial Sector Charter came into effect in 2004. This set targets for inclusion and drove the launch of a number of products aimed at the low-income market, including money transfers. This meant that M-Pesa was launched into a market in which potential consumers already had choice – including being able to send money from local supermarkets all around the country.

The M-Pesa product:
As M-Pesa agents need to have cash on hand, the feeling is that, with the high crime in South Africa, this product model would have made them vulnerable to theft.

One of the main lessons to learn from the M-Pesa experience in Kenya and South Africa is that it is not possible to cut and paste solutions from one country to another. Understanding local conditions is important – and, as a journalist, finding out about these is where you will find your stories.

Trade – imports from and exports to other countries – of both goods and services is at the heart of the modern global economy. The flow of goods and services is central to globalisation, increasing interconnectedness of world economies. Over the decades, countries have been moving towards freer trade, and signing trade agreements to bring about greater flows of goods and services between and among them.

Trade agreements are of two types: bilateral trade agreements between two countries, and multilateral trade agreements between three or more countries. These agreements supposedly ensure that benefits of trade are fairly negotiated between countries. An example is the South African-European Union Preferential Trade Agreement. Regional trade agreements are also multilateral.

Unilateral trade arrangements are also common, where one country either gives another country or countries greater access to its market, for example the United States under the African Growth and Opportunity Act (AGOA) which benefits a number of African countries; or unilaterally acts to make it harder for a country to trade with it.

Vested interests in countries try to fend off competition from abroad with various forms of protectionism. Also, freer trade does not necessarily benefit everyone in a country equally: consumers may get cheaper clothing but workers in clothing companies put out of business by cheaper imports will lose their jobs and may not be able to get new jobs.

Governments can take action, if they have the money, to soften the blow for vulnerable groups, but have to steer clear of subsidies that break the rules of world trade agreements. In South Africa, the government introduced support programmes for South African clothing manufacturers to try to salvage jobs lost to Chinese clothing imports.

Domestic producers often argue that they need actual protection from what they see as unfair global competition. The government has to weigh the advantages of introducing or increasing tariffs on particular imported goods against the possibility of revenge protectionism.

Free trade agreements may also contain elements that are not directly about trade, such as new and onerous protections for intellectual property like software or commercial brands, or provisions for settling trade and investment disputes that may militate against a country’s sovereignty.

It is a journalist’s duty to keep the public informed about the pros and cons of particular trade deals, and particular cases of new protection, such as onerous safety regulations, or the removal of existing protection.

Trade also features in a country’s national accounts, showing how well or badly the country is faring in selling goods and services abroad to buy goods and services that the country needs, and to save in the country’s gold and foreign exchange reserves.

Much is often made of an unfavourable balance of trade between countries, such as between South Africa and China in 2014 of R73-billion. A counter argument would be that a trade deficit or surplus with one country is not as important as the general trade balance.

In Africa, the big problem has been the imbalance in the kind of trade. African countries tend to export low-value commodities such as iron ore, and import high-value finished goods, such as motor vehicles. The call to change this through beneficiation of local commodities and have more manufacturing in Africa is an ongoing source of stories.

All commodities have a value chain, whether it is a mineral such as platinum or a crop such as tomatoes. The raw commodity is at the lower end of the chain and the manufactured goods higher up the value chain.

Nigeria grows vast amounts of tomatoes yet imports tomato puree from China. The announcement in 2016 that the Dangote Group in Nigeria is opening a tomato processing plant outside the northern city of Kano to manufacture tomato puree is an example of moving up the value chain in a way that keeps the jobs in the country. The announcement that a company in South Africa is going to locally manufacture fuel cells, whose key component is platinum, is another example of moving up the value chain and keeping the jobs in the country where the platinum is mined.
Finding the story

What are the most important commodities in your country? What is their value chain? Are the jobs up the value chain being kept in the country or are they in another country? These are all possible stories for you to explore.

Another problem in Africa is the low level of trade among countries on the continent, hindered by problems such as poor infrastructure, inadequate rail and road networks, and bureaucratic issues that make crossing borders difficult, with controls that delay trucks sometimes for days. The Tripartite Free Trade Area is an attempt to boost intra-African trade. The deal, which was signed in Egypt in 2015, aims to create a free-trade zone that covers 26 countries and goes from Cape Town to Cairo. This deal is still in the early stages. It involves three existing African trade blocs: the Southern African Development Community (SADC), the East African Community (EAC) and the Common Market for Eastern and Southern Africa (Comesa). The first step is for each country’s parliament to approve the deal.

Finding the story

How would your country benefit if the Tripartite Free Trade Area is successful? Has the deal been approved in your country? If not, what is holding it up? All of these are potential stories for you to explore.

Key terms: Some other terms important for trade

The two main terms you need to know are the trade deficit and surplus and the surplus or deficit on the current account of the balance of payments.

The trade balance (deficit or surplus) is the difference between a country’s export and import revenue.

The current account is an important indicator of economic health. It is the sum of the balance of trade, which is goods and services exported minus imports, net income from abroad and net current transfers.

A positive current account balance (a surplus) shows that a country is saving more than it is spending and that it is providing more commodities, goods and services to other economies and is owed money in return.

A negative current account balance (deficit) indicates that a country is a net borrower from the rest of the world and is spending more than it is saving.

The balance of trade is often the biggest component of the current account. A trade deficit means that the value of imports is greater than the value of exports. A trade surplus means that the country is selling more goods and services abroad than it imports.

Some other terms important for trade

Dumping: The export of a product at a price that is lower than the price in the country where it is being produced. The effect in the receiving country is that the lower price threatens local producers who can’t compete and lose sales or go out of business.

Trade protection: Legal measures a country imposes on goods entering the country, such as tariffs or outright bans on certain goods being imported, to protect domestic industry. South Africa, for example, bars the import of second-hand motor vehicles to protect its motor industry.

Subsidies: Subsidies for companies or sectors, particularly the agricultural sector, are a form of protectionism. The subsidising of agricultural products in developed countries continues to be controversial as this makes it difficult for developing countries to compete.

Import duties: A tax collected on imports by the customs authority of a country and goes towards state revenues.

Tariffs: Basically taxes imposed on goods entering a country, usually to grant a form of protection to local industry by making imports more expensive.

Non-Tariff Barriers: A barrier to trade other than a straight import tariff, such as the use of safety regulations and standards. Frequently used by developed areas, such as the European Union and Australia to make it difficult for exports from developing countries to gain entry.
Company and market reporting

Basic Economics: Writing about companies

Making reporting about companies and markets interesting is a challenge that many journalists seem to find difficult. Most company news is interesting to investors and investors only. Market reports are often a list of detailed and hard-to-digest facts.

Companies get away with having their press releases reproduced verbatim by reporters who do not understand enough to ask any questions. Examples abound of press releases being reprinted with a journalist’s byline on them. Of course press releases most often present “spin,” a flattering picture that journalists are duty bound to take a hard look at.

Be aware that public companies listed on a stock exchange are more forthcoming with information than private companies. It is often hard to find out much about private companies without a source inside the company.

Listed companies do release, according to stock exchange rules, a great deal of information, though it might not be easy to interpret. Buried in the details of profit and loss, assets and liabilities, and cashflow in company financial reports lie story gems – or at least indications of where those story gems may lie.

One item of interest is always the total remuneration of the executives, particularly the CEO, in relation to the company’s performance. Somehow CEOs always seem to be well rewarded, even on their way out the door, through a “golden handshake”. Yet scrutiny of the annual report should not end there. With the help of good contacts, sources inside the company, industry experts, sector analysts, friendly accountants, and even just the willingness to read carefully, a financial report can yield good stories.

Financial reports for publicly listed companies should contain:

- An income statement,
- A balance sheet, and
- A cashflow statement.

Journalists often focus on the income statement, which tells us whether the company has made a profit or a loss. Arguably the most important part of a financial report remains the “bottom line”, or net income, or after-tax profit, as it sometimes also known, because this affects the share price. The bottom line is what is left of the top line, the turnover, after subtracting all expenses, including tax. Companies will sometimes want to direct the public’s attention to an increase in turnover, or some version of pre-tax profit or operating profit, if they tell a better story than the bottom line.

Apart from the income statement, the balance sheet, however, is crucial in assessing the financial health of the company. It tells us the relationship between the assets and liabilities of the company. When liabilities exceed assets, a company is insolvent.

The cashflow statement tells us an important story about the ability of the company to generate “money in the bank”. The saying is, “Turnover is vanity, profit is sanity, cash is reality.”

Pay close attention to debt. Debt itself is not bad, but bad management of debt can be the undoing of a company.

Really juicy bits of information are sometimes hidden in small print in the notes to the financial statements. Look especially for provisions for paying legal bills for lawsuits against the company.

Basic terms

**Gross profit**: The money the company makes from selling something.

**Operating profit**: The money the company makes from selling something, after deducting the costs of selling that thing.

**Pre-tax profit**: The money the company makes after it has deducted the costs of selling its product or service, and paid any interest on any debt it may have, but added in any income from any other investments it might have – before it pays any tax.

**Net or after-tax profit**: How much money the company makes after all the above as well as paying tax.

**Retained profit**: The money the company keeps to put back into the company for future investment and spending.

**Turnover (or sales)**: All the money a company rakes in before items like tax are deducted.

**Earnings per share**: calculated by dividing the earnings of the company by the number of shares the company has issued.

**Dividend**: The money distributed to shareholders of a company, usually once a year, that is decided on depending on the net profit it makes for the year.

**Asset**: Anything on the balance sheet with value to the company. In banking, this includes loans, which can be a little confusing since loans involve money that a bank has parted with for the benefit of a borrower. But because that money is lent out with the expectation that it will return to the balance sheet eventually, it’s an asset, just like the securities (such as Treasury bonds) that a bank might own.
**Basic terms (cont.)**

**Capital:** All of the equity in a firm; for banks this generally means ordinary and preference shares, surplus capital and profits.

**Capital markets:** Markets where companies or governments can raise long-term funds, i.e. debt and equity. An alternative to bank borrowings for companies that are not self-financed.

**Financial year:** A 12-month period that may or may not follow the calendar year. At the end of the financial year, companies calculate their year-end profit and loss.

**Financial statement:** A summary of a business' financial position for a given period. Financial statements can include a profit and loss, balance sheet and cash flow statement.

**Fixed asset:** A physical asset used in the running of a business.

**Fixed cost:** A cost that cannot be directly attributed to the production of a good or service.

**Fixed interest rate:** When the interest rate of a loan remains the same for the term of the loan or an agreed timeframe.

**Equity:** The value of ownership interest in the business, calculated by deducting liabilities from assets.

**Equity finance:** Money provided to a business in exchange for part ownership of the business. This can be money invested by the business owners, friends, family, or investors like business angels and venture capitalists.

**Investment:** The purchase of items of value to earn income and/or increase capital, i.e. putting money to work to make more money. Investments can include income-producing vehicles such as bonds, equity vehicles such as ordinary and preference shares (which may or may not provide income) and other assets such as real estate.

**Liabilities:** The debts and financial obligations of a company either current (payable within one year) or long-term (payable after one year) such as salaries, taxes and money owed. The concept also applies to pension plans and reflects the benefit promises of the plan (i.e. future pension payments).

**Capital:** Wealth in the form of money or property owned by a business.

**Capital cost:** A one-off substantial purchase of physical items such as plant, equipment, building or land.

**Capital gain:** The amount gained when an asset is sold above its original purchase price.

**Capital growth:** An increase in the value of an asset.

**Cash:** Includes all money that is available on demand including bank notes and coins, petty cash, certain cheques, and money in savings or debit accounts.

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**Numbers for journalists**


It focuses on specific calculations around percentages and the difficulties people may have in knowing the difference between percentage points and percentages – and how to use them in common financial and economic stories.

Most stories involving statistics, from news about interest rates to unemployment figures, include percentages to show increases or decreases. These can be described as percentage points or percentages.

- If the central bank increases its interest rate from 5% to 6% this is an increase of one percentage point, but a 20% increase.
- If unemployment increases from 20% to 25%, this is an increase of five percentage points, but a 20% increase.

The following multiple choice exercise will help you gauge your general financial literacy. Exercise 6 focuses on percentages.

**Exercise #5**

1. If you give your mother R2 000 to keep and the annual inflation rate is 3%, after a year the money will be worth:
   - A. The same amount
   - B. More
   - C. Less

2. High inflation means that the cost of living is increasing rapidly
   - A. True
   - B. False
**Exercise #5 (cont.)**

3. South Africa’s exports to the rest of Africa last year grew by 10% from R300 billion to:
   - A. R310 billion
   - B. R330 billion
   - C. R400 billion

5. It is less likely that you will lose all your money if you save it in more than one place.
   - A. True
   - B. False

**Numbers**

4. The IMF global growth forecast for 2015 is down 0.2 percentage points from an expected 3.8%. What is the expected growth now?
   - A. 3.6%
   - B. 4%
   - C. 5.8%

**Answers**

1) C
2) A
3) B
4) A
5) A

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**Exercise #6  Numbers – understanding percentages**

1. Assume inflation was increasing by 3% a year. There is a sudden jump to 6% a year. By how much has inflation increased in percentage terms?
   - A. 3%
   - B. 50%
   - C. 100%

2. Economic growth is expected to slow to 1.8%, down from the predicted 2.8% last month, a decrease of:
   - A. 1%
   - B. 50%
   - C. One percentage point

3. Unemployment in Greece skyrocketed from 10% in 2010 to 25% in 2015, an increase of:
   - A. 15%
   - B. 150%
   - C. 250%

4. The public sector wage bill swallows 40% of gross national revenue, compared with 20% a decade ago, an increase of:
   - A. 20%
   - B. 60%
   - C. 100%

5. The Namibian economy is projected to grow by 5.5% and 5% in 2015 and 2016 respectively, an improvement from the 4.5% recorded in 2014. What is the projected increase from 2014 to 2015?
   - A. 1%
   - B. half a percentage point
   - C. one percentage point

6. A statistical report showed that one in three people are now unemployed, compared to one in six last year, a percentage increase of:
   - A. 100%
   - B. 50%
   - C. 25%

7. OECD analysis shows that Spain’s unemployment rate is expected to remain high, at 21.5% this year, falling to 19.7% at the end of 2016, a drop of:
   - A. 1.8%
   - B. 1.8 percentage points
   - C. 2%

8. Economic growth in Angola is forecast to slow to 3.9% this year from 5.8% in 2013 because of a decline in oil output, according to the IMF – a decrease of:
   - A. 2.1%
   - B. 1.9 percentage points
   - C. 2.1 percentage points

9. If the Bank of Botswana increases the bank rate from 5% to 7% this is an increase of:
   - A. 2%
   - B. two percentage points
   - C. 4%

10. Prime interest rates have dropped to 9% from 12% three years ago. How much have they decreased in percentage terms?
    - A. 4%
    - B. 25%
    - C. 75%
### Exercise #6

<table>
<thead>
<tr>
<th>Percentage</th>
<th>Summarised</th>
<th>In One or Two Words</th>
</tr>
</thead>
<tbody>
<tr>
<td>100%</td>
<td>All</td>
<td>All</td>
</tr>
<tr>
<td>99%</td>
<td>Practically all</td>
<td>Most</td>
</tr>
<tr>
<td>95%</td>
<td>Almost all</td>
<td>Most</td>
</tr>
<tr>
<td>90%</td>
<td>Nearly all / nine out of 10</td>
<td>Most</td>
</tr>
<tr>
<td>80%</td>
<td>The greater part of number / eight out of 10</td>
<td>Most</td>
</tr>
<tr>
<td>70%</td>
<td>The greater part of number / seven out of 10</td>
<td>Most</td>
</tr>
<tr>
<td>60%</td>
<td>More than half / six out of 10</td>
<td>Most</td>
</tr>
<tr>
<td>55%</td>
<td>Just over half</td>
<td>Most</td>
</tr>
<tr>
<td>50%</td>
<td>Half / five out of 10</td>
<td>Half</td>
</tr>
<tr>
<td>45%</td>
<td>Nearly half</td>
<td>Many</td>
</tr>
<tr>
<td>40%</td>
<td>A large part / four out of 10</td>
<td>Many / a significant minority</td>
</tr>
<tr>
<td>35%</td>
<td>Quite a large part or number / just over a third</td>
<td>A significant minority</td>
</tr>
<tr>
<td>30%</td>
<td>Around a third / roughly one in three</td>
<td>A minority (a significant minority will depend on context)</td>
</tr>
<tr>
<td>25%</td>
<td>A quarter / one in four</td>
<td>A minority</td>
</tr>
<tr>
<td>20%</td>
<td>A fifth / one in five</td>
<td>A small minority</td>
</tr>
<tr>
<td>15%</td>
<td>A small part</td>
<td>A few</td>
</tr>
<tr>
<td>10%</td>
<td>A tenth / one in 10</td>
<td>Not much / not many / a few</td>
</tr>
<tr>
<td>5%</td>
<td>A twentieth / one in 20 / a small number</td>
<td>Few / very few</td>
</tr>
<tr>
<td>1%</td>
<td>A hundredth / one in a 100</td>
<td>Very few / a small minority</td>
</tr>
<tr>
<td>0%</td>
<td>None</td>
<td>None</td>
</tr>
<tr>
<td>0.something%</td>
<td>A minute part of / fewer or less than one in 100</td>
<td>Almost none</td>
</tr>
</tbody>
</table>
Glossary of financial institutions

INTERNATIONAL
- **Bank for International Settlements (BIS):** Headquartered in Basel, Switzerland, the BIS is a bank for central banks. Founded in 1930, the BIS is the oldest global financial institution and operates under international law. The BIS seeks to make monetary policy more predictable and transparent among its 60-member central banks, except in the Eurozone countries which forfeited the right to conduct monetary policy in order to introduce the Euro.
- **Basel Committee on Banking Supervision:** An international forum for banking authorities that work to strengthen the regulation, supervision and practices of banks and improve financial stability worldwide. Administered from Basel, Switzerland.
- **Basel Accords:** Basel III is a global, voluntary regulatory agreement that covers aspects such as bank liquidity and capital requirements for banks. Basel III, the third installment of the accord, is part of the ongoing attempt to set international rules for the banking sector. Basel III was developed in response to gaps in the financial regulation landscape that became obvious during the global financial crisis of 2007-2008. African countries implementing Basel III include South Africa and Botswana.
- **International Monetary Fund (IMF):** An international organisation mainly funded by developed countries that provides funds to countries with debt or balance of payment problems. However, these come with strict conditions, sometimes resulting in countries losing control of being able to direct their own policies.
- **World Bank:** International financial institution that provides loans to developing countries. The bank compiles data on a range of topics including agriculture, climate change, energy, debt, trade and urban development and can be a good first stop when looking for statistics. It also produces research reports on various topics. (www.worldbank.org).
- **World Trade Organization (WTO):** The main aim of the WTO is to deal with the global rules of trade between nations. It aims to ensure that trade flows as smoothly and freely as possible. Based in Geneva, Switzerland. (www.wto.org).

REGIONAL
- **Southern African Customs Union (SACU):** Comprising five countries in Southern Africa, Botswana, Lesotho, Namibia, South Africa and Swaziland, the union is headquartered in Windhoek. The aim of the union is to facilitate regional integration and development; however recently it has been mired in controversy over disagreements on how to share revenue between the five countries.
- **Southern African Development Community:** An inter-governmental organisation based in Gaborone, Botswana comprising 15 member states: Angola, Botswana, Democratic Republic of Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe. Its aim is to further regional cooperation and integration on issues such as trade and financial services.
- **Committee of Central Bank Governors in SADC:** Made up of the 15 governors from the SADC central banks. The CCBG deals with issues such as co-operation around financial flows in the region, making it possible to move money around the region and foreign exchange policies.
- **Committee of SADC Stock Exchanges:** A collective body of the stock exchanges in the region.
- **Common Market for Eastern and Southern Africa (COMESA):** The largest regional economic grouping in Africa, with 19 member countries and a population of about 390 million. COMESA has a free trade area and launched a customs union in 2009. Members include: Burundi, Comoros, DRC, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia and Zimbabwe. (www.comesa.int)
- **East African Community:** The regional intergovernmental organisation of Burundi, Kenya, Rwanda, Tanzania and Uganda, with its headquarters in Arusha, Tanzania.
- **West African Monetary Union:** The union has a common monetary unit, the Franc of the African Financial Community (CFA F), which is issued by the Central Bank of West African States (BCEAO). WAMU comprises: Benin, Burkina Faso, Guinea Bissau, Cote d’Ivoire, Mali, Niger, Senegal and Togo.

SOUTH AFRICAN BODIES REGULATING THE ECONOMY AND FINANCIAL SECTOR
- **National Treasury:** The National Treasury is responsible for managing South Africa’s national government finances including fiscal policy, coordinating macroeconomic policy, managing the budget preparation process and directing policy on matters such as financial inclusion.
- **South African Reserve Bank:** Responsible for monetary policy as well as the regulation and supervision of banks and banking groups.
- **Financial Services Board:** The regulatory agency responsible for the non-banking financial services industry. An independent body that supervises and regulates financial services in the public interest. This includes the regulation of the Johannesburg Stock Exchange.
Glossary of financial institutions (cont.)

**SOUTH AFRICAN BODIES REGULATING THE ECONOMY AND FINANCIAL SECTOR (CONT.)**

- **National Credit Regulator:** Responsible for the regulation of consumer credit and consumer information. Oversees matters such as reckless credit granting, providing for debt re-organisation in cases of over-indebtedness, registration of credit bureaux, credit providers and debt counseling services, and sets standards relating to consumer credit.
- **Competition Commission of South Africa:** The Competition Commission is a statutory body empowered to investigate, control and evaluate restrictive business practices, abuse of dominant positions and mergers with the aim of achieving equity and efficiency in the South African economy.
- **Competition Tribunal of South Africa:** The commission is the investigation and enforcement agency. The Tribunal is the adjudicative body, like a court. The Competition Appeal Court considers appeals against decisions of the Tribunal.
- **Banking Association of South Africa:** An industry body representing all banks registered and operating in South Africa. It has numerous committees that advise on issues pertinent to the sector.
- **South African Insurance Association:** The voice of the short-term insurance industry. It represents the industry at all levels and with all stakeholders.

Useful links

- **BBC News – Country Profiles:** Provides a range of socio-economic indicators and well as general background information. [http://news.bbc.co.uk/2/hi/country_profiles/default.stm](http://news.bbc.co.uk/2/hi/country_profiles/default.stm)
- **Centre for Affordable Housing Finance in Africa:** Information about housing finance in Africa, with a focus on affordable housing. Produces an annual yearbook with detailed profiles of African countries. [http://www.housingfinanceafrica.org/](http://www.housingfinanceafrica.org/)
- **FinScope:** National surveys of how people source their income and how they manage their financial lives, including statistics on access to financial services, banked population and debt. Surveys have been conducted in 15 African countries. [www.finscope.org](http://www.finscope.org)
- **Investopedia:** Economic and financial definitions. [www.investopedia.com](http://www.investopedia.com)
- **Library of Congress Business Reference Services:** A list of African government banking and financial institutions. It includes links to the official web sites of central banks, ministries of finance, capital markets, and sub-regional financial institutions that provide financial and technical assistance to promote private investment. [http://www.loc.gov/rr/business/african/banks.html](http://www.loc.gov/rr/business/african/banks.html)

Further reading

- How to speak money. John Lanchester. (Faber & Faber, 2014)

PODCASTS

- The giant pool of money. This American Life Episode 355. [www.thisamericanlife.org/radio-archives](http://www.thisamericanlife.org/radio-archives)
- How four drinking buddies saved Brazil. Planet Money Episode 216. [www.npr.org/sections/money](http://www.npr.org/sections/money)
- The invention of the economy. Planet Money Episode 522. [www.npr.org/sections/money](http://www.npr.org/sections/money)