February 2007
IMF Country Report No. 07/83

Namibia: Financial System Stability Assessment, including Report on the Observance of Standards and Codes on Banking Supervision

This Financial System Stability Assessment on Namibia was prepared by a staff team of the International Monetary Fund and the World Bank as background documentation for the periodic consultation with the member country. It is based on the information available at the time it was completed on February 27, 2006. The views expressed in this document are those of the staff team and do not necessarily reflect the views of the government of Namibia or the Executive Board of the IMF.

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International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

NAMIBIA

Financial System Stability Assessment

Prepared by the Monetary and Financial Systems and African Departments

Approved by Ulrich Baumgartner and Abdoulaye Bio-Tchané

February 27, 2006

Key macro-relevant findings are:

- **The financial system appears healthy, well-run, and resilient to plausible macroeconomic shocks.** Namibia has one of the most sophisticated and highly developed financial systems in Africa. It comprises a diverse range of institutions, which are mostly private. The banking sector is mature, very profitable, and well-capitalized. The NBFI sector is also well-developed. Some macro risks arise from exposure to the real estate sector (for banks), and financial markets (pension funds and insurance companies). Conclusions regarding the NBFI are more tentative given supervisory weaknesses (see below).
- **Close ties with South Africa have significantly benefited financial institutions but also entail some risks.** Financial institutions are able to diversify their risks while strong ownership ties and common good practices with reputable financial institutions in South Africa help mitigate weaknesses in domestic supervision and regulation as well as limited domestic skills. The peg with the rand also provides predictability in the exchange rate. Possible risks relate to limited avenue for independent monetary and financial policies, more limited options for global diversification given the need to conform to South African exchange control practices, and the possibility that shocks in South Africa can be quickly propagated to Namibia.
- **While the regulatory and supervisory frameworks for the financial sector are broadly satisfactory, there is a significant shortfall in implementation by the regulatory agencies, especially for the NBFI sector**. Urgent action is needed to address supervisory shortcomings, which relate mainly to limited analytical capacity. Failure to do so could harm the interests of pension fund members and insurance policy holders, and in the case of the government pension fund, could have direct consequences on the government's finances.
- **Access to finance is better than in other Sub-Saharan African countries but is still very limited, reflecting pervasive rural poverty and widespread unemployment which limit savings and demand for services.** At the same time, limited access makes efforts to reduce unemployment and poverty more difficult. This is a key problem even if solutions go beyond the financial sector.
- **Investment opportunities in domestic financial markets and avenues for diversification are very limited.** As a result, capital outflows have put pressure on the capital account and reserve levels. Steps to develop domestic markets may reduce such flows and are preferred to investment restrictions.

The FSAP therefore recommended steps to (a) upgrade supervisory and regulatory frameworks, especially those for NBFIs; (b) expand the reach and affordability of financial services; and (c) create more domestic investment opportunities and deepen financial markets.

The authorities broadly concur with the FSAP assessment and recommendations.

FSAPs are designed to assess the stability of the financial system as a whole and not that of individual institutions. They have been developed to help countries identify and remedy weaknesses in their financial sector structure, thereby enhancing their resilience to macroeconomic shocks and cross-border contagion. FSAPs do not cover risks that are specific to individual institutions such as asset quality, operational or legal risks, or fraud.

This Financial System Stability Assessment (FSSA) is based on the work of a joint IMF/World Bank Financial Sector Assessment Program (FSAP) mission to Windhoek from October 12 to November 2, 2005. It has also benefited from discussions with the authorities from February 9–10, 2006 under the Article IV consultations.

The FSAP team comprised Messrs. Teo (Team Leader, IMF), and Soylemezoglu (Deputy Team Leader, World Bank); Mmes. Chang, Chivakul, Mulatu (assistant), Messrs. Dwight, Phelan, and Yokobori (all IMF); Mmes. Grose and Guven, Messrs. Goldblum, Hassler, Mousset, Vittas, (all World Bank). A four-person World Bank team led by Ms. Isabelle Schoonwater and consisting of Messrs. McDowell, Wang, and Yikona also visited Windhoek in late October 2005 to conduct an AML/CFT assessment.

The main authors of this report are Leslie Teo, Yuji Yokobori, Mali Chivakul with contributions from the rest of the FSAP team.

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GLOSSARY

Agribank	Agricultural Bank of Namibia
AML/CFT	Anti-Money Laundering and Combating the Financing of Terrorism
AUM	Assets Under Management
BCP	Basel Core Principles of Effective Banking Supervision
BIA	Banking Institutions Act
BON	Bank of Namibia
CAR	Capital Adequacy Ratio
CMA	Common Monetary Area
CISNA	Committee of Insurance, Securities and Nonbanking Authorities
DBN	Development Bank of Namibia
FSAP	Financial Sector Assessment Program
FSSA	Financial System Stability Assessment
GAAP	Generally Accepted Accounting Principles
GIPF	Government Institution Pension Fund
ICA	Institute of Chartered Accountants
IFRS	International Financial Reporting Standards
IRS	Internal Registered Stocks
LOLR	Lender of Last Resort
MOF	Ministry of Finance
MOU	Memorandum of Understanding
MDGs	Millennium Development Goals
Namclear	Electronic Clearinghouse
NAMFISA	Namibia Financial Institutions Supervisory Authority
Namib Re	Namibian National Reinsurance Corporation
NBFIs	Nonbank Financial Institutions
NEPRU	Namibia Economic Policy Research Unit
NGO	Nongovernmental Organization
NHE	National Housing Enterprise
NHAG	Namibia Housing Action Group
NII	Net interest income
NISS	Namibian Interbank Settlement System
NPLs	Nonperforming Loans
NSX	Namibia Stock Exchange
PAAB	Public Accountants and Auditors Board
PG	Prosecutor General
PostBank	NamPost Savings Bank
ROA	Return on Assets
ROAA	Return on Average Assets

ROAE	Return on Average Equity
ROE	Return on Equity
RTGS	Real Time Gross Settlement System
SACCOs	Savings and Credit Cooperatives
SACU	Southern African Customs Union
SARB	South African Reserve Bank
SBCGT	Small Business Credit Guarantee Trust
SCAs	Savings and Credit Associations
SDFN	Shack Dwellers Federation of Namibia
SME	Small- and Medium-Sized Enterprises
SSA	Sub-Saharan African Countries

I. Overall Assessment and Key Recommendations

Introduction

1. **Namibia has one of the most sophisticated, diverse, and highly developed financial systems in Africa.** Most financial institutions are private, with strong ownership links to South African institutions. Access to the South African market fills in any gaps.

2. **The performance of the financial system has been shaped by the structural characteristics of the economy.** Namibia suffers from very high economic inequality and from a huge disparity between its formal and informal sectors. The financial system serves the formal sector very well, but has been unable to achieve a satisfactory level of access for the urban poor and the rural population. Owing to limited domestic investment opportunities, institutional investors invest heavily overseas. In addition, Namibia seems to have an acute deficit of skilled financial professionals. Given the structure of the economy, solutions to the policy challenges facing the financial sector go beyond the sector itself and include "real" sector policies such as education, land reform, and rural development.

Major risks to systemic stability

3. **The commercial banking sector is mostly exposed to credit risk.** Credit risk arises mainly from banks' exposure to the real estate sector, mostly in the form of mortgages. In addition, given the concentration of large institutional depositors, banks are vulnerable to their simultaneous withdrawal. More fundamentally, Namibia's size and narrow economic base means that borrowers' performance, even if they are in different sectors of the economy, are highly correlated.

4. **At the same time, the banking sector is mature, very profitable, and well-capitalized**. In addition, key financial soundness indicators suggest that the banking sector's resilience has strengthened in recent years. Stress tests confirm the system's ability to withstand extreme but plausible macroeconomic shocks. These include shocks on credit, interest rate, exchange rate, and liquidity risks as well as scenarios examining the impact of higher interest rates, increasing nonperforming mortgage loans, and further appreciation of the rand and therefore the Namibian dollar.[1]

5. **Available data indicate that major macro risks faced by pension funds and insurance companies include interest rate, equity, and country risks.**[2] Equity allocation appears high in comparison to other emerging market countries but is in line with practice in developed countries. Equity investments increase volatility of investment performance but

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[1] Stress testing did not explore implication of de-pegging with the rand because (i) data required for such a test does not exist; and (ii) such an event would be so traumatic that economic relationships and assumptions embodied in any stress tests would be invalid.

[2] Pension fund and insurance companies also face technical and re-insurance risks. Stress testing on pension fund and insurance companies was not possible due to incomplete data.

have also resulted in rather good long-term performance. Pension funds and insurance companies also invest heavily abroad given the lack of suitable domestic investment opportunities. Pension funds and insurance companies appear to manage these risks appropriately. However, given weaknesses in data and supervision, more detailed and definitive conclusions regarding the solvency and performance of these institutions are not possible.

Cross-border and regional Issues

6. **Close ties with South Africa have significantly benefited financial institutions but also entail some risks.** Benefits include: (i) access to regional and global financial markets that enable pension funds and insurance companies to diversify their risks; (ii) more efficient capital allocation within the Common Monetary Area (CMA); (iii) strong ownership ties and common good practices with reputable financial institutions in South Africa which help mitigate weaknesses in domestic supervision and regulation (see below) as well as limited domestic skills; and (iv) a peg that provides predictability in the exchange rate. Nevertheless, there are possible risks that need to be managed including (i) limited avenue for independent monetary and financial policies given the CMA; (ii) more limited options for global diversification given the need to conform to South African exchange control practices for countries outside the CMA; and (iii) the possibility that shocks in South Africa can be quickly propagated to Namibia.[3]

Regulatory and supervisory frameworks

7. **The regulatory and supervisory frameworks for the financial sector are broadly satisfactory but there is a significant shortfall in implementation by the regulatory agencies, especially for the Nonbank Financial Institutions (NBFI) sector.** One of the shortcomings of Namibia Financial Institutions Supervisory Authority (NAMFISA) is the failure to compile, verify, analyze, and disseminate accurate and reliable data on the financial soundness and performance of the NBFIs that come under its authority. Another is to carry out effective off- and on-site supervision as well as implement solvency requirements for insurance companies and pension funds. For banking supervision, major gaps include the lack of supervision of bank holding companies and financial groups, and the absence of regulatory requirements on market and country risks. Significant weaknesses were also found in the conduct of supervision, as too much emphasis was placed on compliance with regulations and too little on the analysis of banks' risk profiles. These shortcomings are primarily caused by a lack of knowledge and skills among supervisors.

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[3] This risk is mitigated by the requirement for foreign-owned financial institutions to be set up as subsidiaries. Furthermore, banks have little direct cross-border exposures as they fund and invest mostly domestically. Nevertheless, risks remain given strong and deep links with South African institutions. Pension funds and insurance companies also invest a significant proportion of their assets in South Africa. More generally, Namibia's economy is closely integrated to that of South Africa.

Access to financial services

8. **While access to finance in Namibia is better than in other Sub-Saharan African countries, it is still very limited.** This reflects pervasive rural poverty and the growing population of urban shack dwellers, who suffer from widespread unemployment. The situation is aggravated by relatively high fees for the use of banking services, especially checking accounts. Nonetheless, a range of microfinance institutions has evolved. Government efforts to broaden access to specific financial products by way of specialized financial institutions, aside from PostBank, have had very limited success.

Domestic investment

9. **There are limited investment opportunities in domestic financial markets, as well as limited avenues for diversification.** This has resulted in capital outflows with Namibia having increasingly large net claims on its neighbor, and putting pressure on Namibia's reserve levels.

Anti-Money Laundering and Combating the Financing of Terrorism[4]

10. **Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) policies and practices are nascent and do not yet meet international standards.** Legislation that would provide an AML/CFT framework is in draft form and will take some time to be enacted.

Recommendations

11. The FSAP recommends measures to (a) upgrade supervisory and regulatory frameworks, especially those for NBFIs; (b) expand the reach and affordability of financial services; and (c) create more domestic investment opportunities and deepen financial markets (Box 1).

- **The most urgent and important recommendation is to improve NAMFISA's effectiveness to ensure the NBFI sector is well-supervised.** Failure to do so will harm the interests of pension fund members and insurance policy holders. The appointment of a CEO with relevant experience is an immediate priority. NAMFISA has to put in place a comprehensive plan to build its capacity by providing targeted training for its staff and proactively managing public perception of its credibility. In banking supervision, the priority should be to fully comply with the Basel Core Principles (BCP) before implementing Basel II.

- **Action is also needed to address gaps in the provision of financial services to the majority of the population.** The authorities should foster greater competition among banks by making the structure of fees and charges clearer, continuing to remain open to

[4] The AML/CFT assessment is currently being prepared by the World Bank team. The ROSC would be issued in spring 2006.

new reputable entrants, leveraging on PostBank's reach, and supporting the establishment of credit unions. At the same time, banks should be encouraged to introduce products targeted at low-income groups, as their parent banks are doing in South Africa. The usury act is not protecting the poor and should be replaced with a consumer-credit act with truth-in-lending provisions. Finally, a comprehensive re-examination of the role of specialized financial institutions should be carried out to ascertain how their policy objectives can be best achieved. Given their small size, it may be better to consolidate or transform them into wholesale institutions.

- **The authorities should also revisit the decision to tighten domestic investment requirements and to require investment in unlisted Namibian securities.** The case for tightening domestic investment requirements is not convincing. The requirement to invest 5 percent of assets in unlisted Namibian securities, in particular, is highly risky. Available information indicates that the performance of domestic instruments has so far been less than satisfactory. Such a requirement could lower investment returns and channel funds to unworthy projects. Instead, the authorities should take steps to develop domestic investment opportunities through asset securitization, leasing and factoring, and further development of private equity as well as domestic money and foreign exchange markets. The Bank of Namibia (BON) should move ahead with efforts to develop its capacity to manage systemic liquidity.

- **An AML/CFT framework that is consistent with international good practice should be put in place as soon as possible.** This includes a set of laws, appropriate regulations and procedures, and enforcement capacity.

12. **Over the medium-term, the authorities should strengthen their capacity to monitor and assess emerging threats to systemic financial stability.** While financial institutions appear to be healthy, there is a need to monitor risks especially those that might arise from outside Namibia. In this regard, there is a need for closer coordination with South African regulators in order to deal with any problems that might arise from potential contagion or South African ownership. For example, Namibian regulators should follow developments with parent institutions closely. In many countries, such monitoring is carried out by a dedicated group or department, usually in the central bank or regulator.

Box 1. Key FSSA Recommendations [1]

Upgrading the Regulatory and Supervisory Framework

(Immediate)

- Strengthen NAMFISA by appointing an experienced and respected CEO. NAMFISA should (i) collect, compile, and analyze data from the NBFI sector; (ii) carry out effective on- and offsite supervision; (iii) and fully implement current solvency frameworks.
- Address weaknesses in banking supervision to fully comply with BCP.
- Supervise deposit taking specialized financial institutions on the same basis as commercial banks.
- Update laws to regularize money market unit trusts and unit-linked insurance products, regulate asset managers, and introduce an "appointed actuary" concept.
- Give NAMFISA a clear mandate to regulate market conduct.

(Medium to Longer-term)

- Build capacity to monitor systemic financial stability as well as more general developments in the sector.

Improving the Reach and Effectiveness of the Financial System

(Immediate)

- Improve transparency of banks' fees and charges.
- Encourage banks to introduce products targeted at low income and rural customers as has been done by their parent banks in South Africa.
- Foster greater competition in the sector by continuing to be open to new reputable entrants, leveraging on PostBank's reach, and supporting the emergence of credit unions.

(Medium to Longer-term)

- Abolish the usury act or raise the usury ceiling substantially; instead introduce a consumer credit act with truth-in-lending provisions.
- Examine effectiveness and revisit role and rationale of specialized financial institutions.

Creating Domestic Investment

(Immediate)

- Revisit proposals to tighten requirements to invest in domestic assets; do not implement the proposal to require 5 percent investment in unlisted Namibian securities.
- Promote asset securitization by enacting the appropriate legal framework.
- Move ahead with plans for more active systemic liquidity management.

(Medium to Longer-term)

- Examine and remove any impediment to the development of asset managers who specialize in private equity investment.
- Promote leasing and factoring by enacting an appropriate legal and regulatory framework.

AML/CFT

(Immediate)

- Put in place an AML/CFT framework which is consistent with international best practice.

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[1] More detailed recommendations were provided in the FSAP Report and associated technical notes.

II. Macroeconomic Environment

A. Macroeconomic Background

13. **Namibia has enjoyed macroeconomic stability since independence in 1990.** Underpinned by a credible exchange rate peg with the South African rand and generally prudent fiscal policies, Namibia has developed a market-oriented economy with a sophisticated physical infrastructure. A stable political and legal environment has also been conducive to economic growth. Real GDP growth has averaged 4.5 percent in the last five years driven by construction, diamond and other mining, and transport and communications. During the same period, consumer price inflation has declined from 9 to 4 percent as the Namibian dollar has appreciated with the rand. Namibia's current account has registered a surplus (averaging 6.75 percent of GDP in the last five years) as the trade deficit has been offset by customs union revenues.

14. **Economic growth, however, has been insufficient to generate a reduction in unemployment and poverty.** While Namibia's per capita GDP is among the highest in Africa, per capita growth lags behind that of other countries in the region. The income distribution is highly skewed, reflecting an uneven distribution of land and rigid segmentation between highly developed services and primary production industries and a large informal sector. The lack of labor-intensive industries, together with labor market rigidities and a shortage of skilled labor, has kept the unemployment rate above 30 percent. These problems have been compounded by the high incidence of HIV/AIDS.

15. **Namibia's economic structure—its narrow economic base, small population, vast geographical expanse, and unequal distribution of wealth and capital—limits policy options that might be available to address challenges in the financial sector.** Put another way, other real sector policies must also be in place to effectively address financial sector concerns. Key challenges relate to the need for increased employment and income generation, the lack of skills especially in finance, the shortage of entrepreneurs, and the creation of the appropriate environment to facilitate doing business.

B. Common Monetary Area[5]

16. **Membership in the CMA provides Namibia's financial institutions with significant benefits but also entails some risks.** Free capital flows allow for more efficient allocation of capital among the CMA member countries. Access to South Africa's financial markets helps financial institutions diversify risks. Similarly, the peg to the rand has helped reduce inflation and provide predictability in exchange markets. However, membership in the CMA means that Namibia's monetary policy must follow South Africa's and capital can

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[5] The CMA is the term used to describe the area of coordination of the monetary and exchange rate policies of Lesotho, Namibia, South Africa, and Swaziland under the Multilateral Monetary Agreement of 1992. Under the CMA, the Namibian dollar is pegged one-to-one to the South African rand. The rand is also legal tender. The CMA guarantees free capital flows among member countries and access for the Namibian government and financial institutions to South Africa's financial markets. South Africa also compensates Namibia for lost seigniorage due to the rand circulating in Namibia. (See Appendix I)

flow rapidly in response to macroeconomic or exchange rate shocks. The open capital market also limits how "independent" financial policies can be from South Africa.

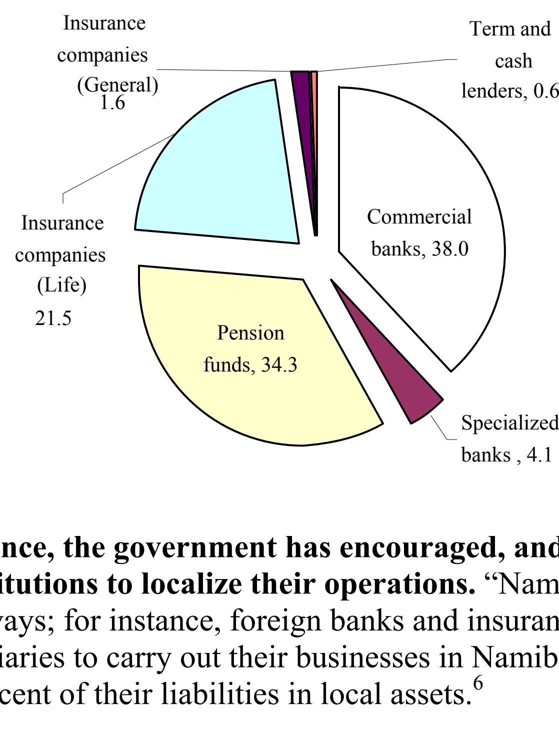
17. **The CMA arrangement requires Namibia to conform to South African exchange control practices for countries outside the CMA.** This requirement limits options for global diversification and hence constrains the investment options of pension funds and insurance companies. Further South African account liberalization should, however, minimize distortions imposed by exchange controls.

III. Financial Sector Stability and Performance

A. Introduction

18. **Namibia has one of the most sophisticated and highly developed financial systems in Africa.** Total financial system assets are about 170 percent of GDP. This system consists of four private commercial banks, about 30 insurance companies, 500 pension funds, a stock exchange, a number of asset management and unit trust management companies, several specialized lending institutions, and a large number and variety of microlending insitutions (Figure 1 and Appendix II). Most of these institutions are private with strong ownership links to South African institutions.

Figure 1. The Namibian Financial System
(percent of total assets)



19. **Since independence, the government has encouraged, and in some cases required, financial institutions to localize their operations.** "Namibianization" has been effected in a variety of ways; for instance, foreign banks and insurance companies are required to set up subsidiaries to carry out their businesses in Namibia and banks have to maintain at least 100 percent of their liabilities in local assets.[6]

[6] Banks are required to maintain not less than 100 percent of the amount of the liabilities in Namibian dollars (excluding capital funds) in local assets situated in Namibia.

B. Commerical Banks and Specialized Financial Institutions

20. **The commercial banking sector is mature and well-established.** Financial intermediation, as measured by private sector credit to GDP, is high at slightly over 50 percent. About 40 percent of the banks' loans is in the form of individual mortgages. Other important borrowers are the finance, real estate and business service sectors. However, lack of collateral and distance between rural villages and urban centers, where most commercial banks are located, limits access to credit for small- and medium-sized enterprises (SMEs) and rural borrowers. Deposits comprise more than 90 percent of total liabilities and is highly concentrated (Figure 2).

21. **Commercial banks in Namibia are well-capitalized and very profitable**. Key financial soundness indicators suggest that the banking sector has become more resilient in recent years. The reported sector-wide capital adequacy ratio (CAR) was 15 percent at end 2005, NPLs at 2 percent, and return on equity (ROE) at 28 percent (Figure 3).

22. **Namibian banks' performance compares well with other banks in Sub-Saharan Africa (SSA).** For instance, while the average ROA and ROE for SSA countries were 1.9 percent and 16.3 percent, respectively, in 2004, Namibian banks recorded 2.0 percent and 21.6 percent. These indicators are comparable with banks in South Africa, although they are less favorable than those for banks in other Southern African countries (Table 1).

Table 1. Banks' Performance in Selected Countries, 2004 [1]

	Total Assets	Return on Average Equity (ROAE)	Return on Average Assets (ROAA)	Net Interest Margin	Cost to Income Ratio	NPL	CAR
	Mil USD	Percent	Percent	Percent	Percent	Percent	Percent
Namibia	1,045	21.6	2.0	4.3	61.8	2.4	15.4
South Africa	52,979	30.6	1.5	3.8	59.9	1.8	13.5
Botswana	510	56.6	4.8	7.2	41.5	2.8	20.6
Lesotho	169	27.9	2.9	4.5	58.1	…	…
Swaziland	154	40.7	3.4	6.5	61.8	…	…
Sub-Saharan Africa	…	16.3	1.9	…	…	14.7	16.1

Sources: Bankscope, Bank of Namibia, and Staff estimates.
1/ Simple average of largest banks in each region.

23. **Stress tests confirm the system's resilience, although exposures to the real estate sector and large institutional depositors could lead to risks (Table 2, Appendix III).** The system's main vulnerabilities are credit and liquidity risks while exchange and interest rate risks are negligible. Credit risk arises mainly from banks' exposures to household mortgages. However, even under the worst case scenario, which focuses on credit risk, only one bank's CAR falls to 6 percent.[7] Given the concentration of large institutional depositors, all banks

[7] The minimum required CAR is 10 percent.

would be adversely affected by the withdrawal of large depositors. However, this risk is mitigated by banks' deposits and credit lines with their parent banks in South Africa.

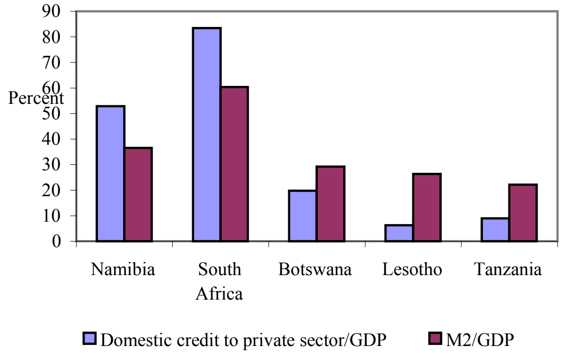
24. **Government efforts to broaden access to specific financial products by way of specialized financial institutions have had very limited success, with the exception of PostBank.** These institutions have suffered from problems related to economies-of-scale. They incur large operational costs compared with outputs that they are expected to deliver. Moreover, decreasing interest rates have reduced their margins. Relatively large NPLs[8] have exacerbated the situation. While these problems are more acute in Agribank, efficiency is a major issue for all of these institutions. Widespread efficiency and effectiveness problems and emerging prudential concerns necessitate revisiting the role and effectiveness of these institutions.

[8] NPLs in Agribank and National Housing Enterprise (NHE) are both about 12 percent.

Figure 2. Balance Sheet of the Banking Sector, 2004–05

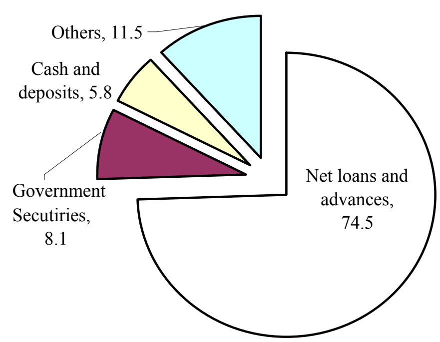
Financial intermediation is relatively high...

Financial Intermediation
(Selected African countries, 2004)



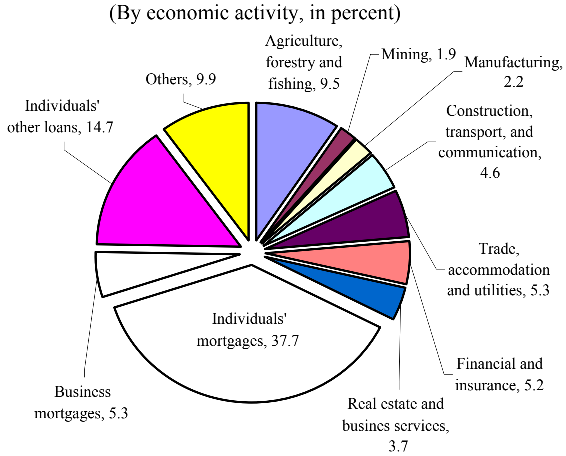
...and banks are actively lending.

Banking System Assets
(Percent of total)



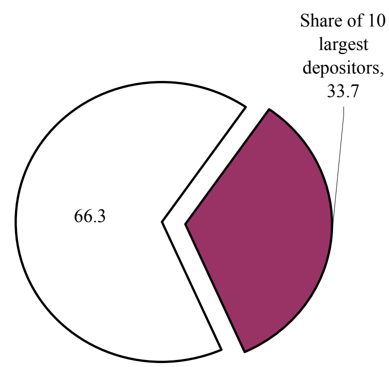
Exposure to individual mortgages is high.

Loans and Advances
(By economic activity, in percent)



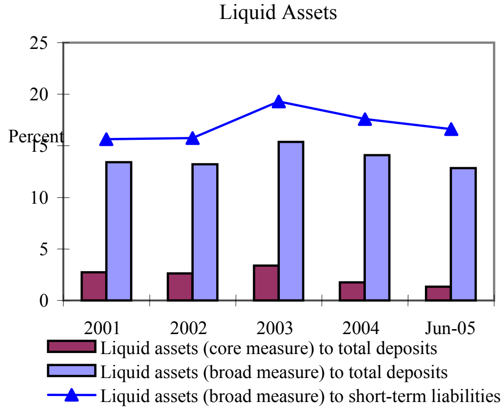
Deposits are highly concentrated.

Deposits
(Percent of total)



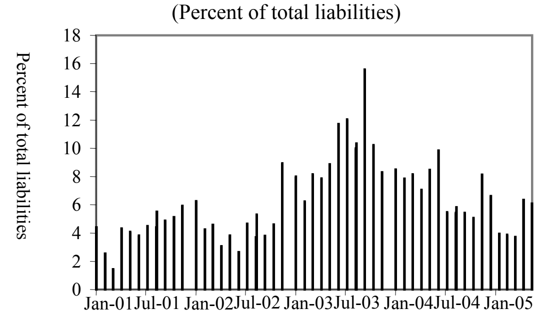
Liquidity remains stable...

Liquid Assets



...and banks have strong ties with South African banks.

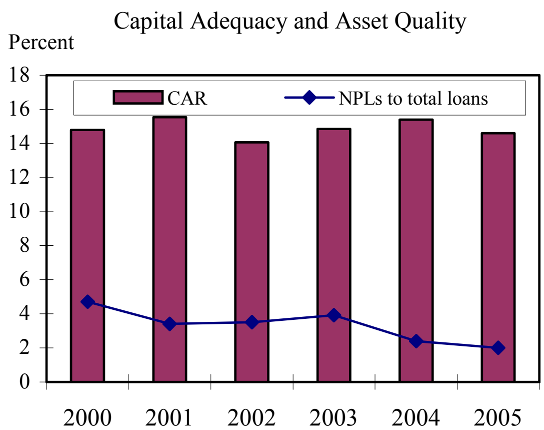
Banking System's Intragroup Funding
(Percent of total liabilities)



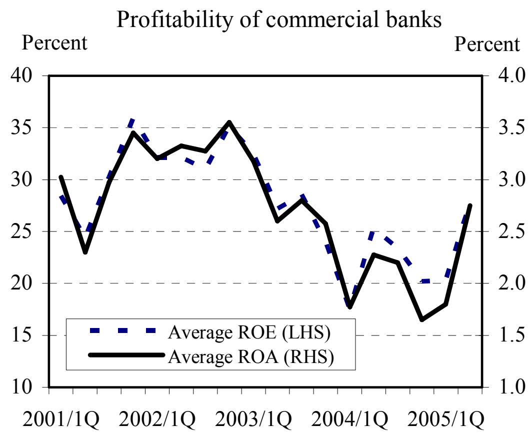
Sources: BON and staff estimates.

Figure 3. Recent Performance of the Banking Sector, 2004-05

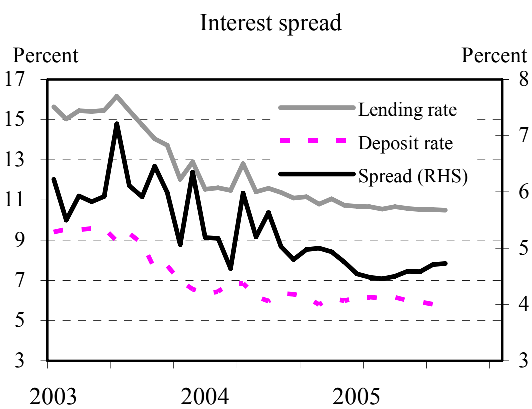
Banks are well-capitalized with low NPL ratios.



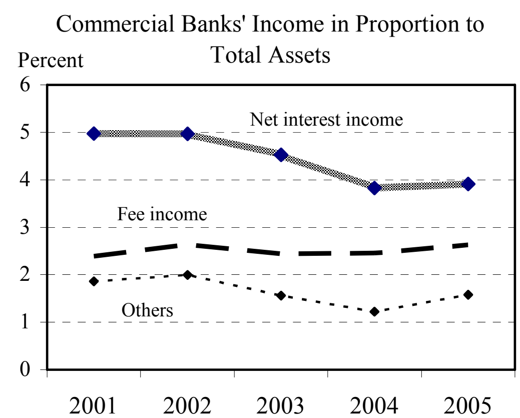
Profitability remains high.



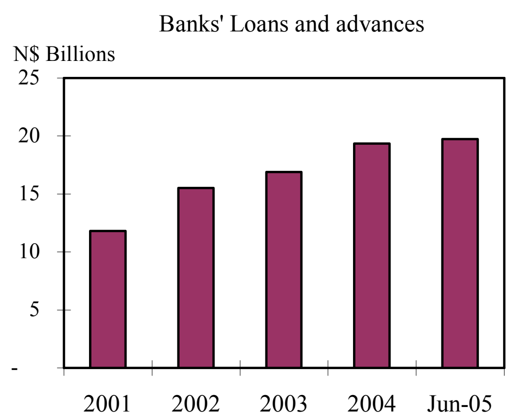
Spreads have fallen...



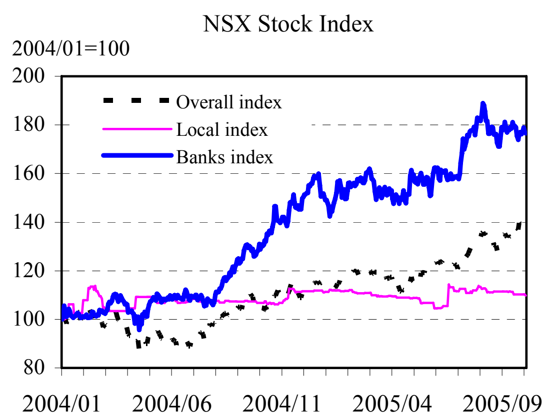
...leading to a decline in net interest income.



Growth remains robust...



...while market valuations are healthy.



Sources: BON and staff estimates.

Table 2. Stress Testing Results

Test	Bank 1	Bank 2	Bank 3	Bank 4	Total
Baseline CAR	13.1	18.6	15.5	11.6	14.7
Baseline Liquidity Ratio	13.8	10.2	10.7	8.7	11.1
I. Sensitivity analysis					
Credit Risk			(Change in CAR)		
1. Overall increase of NPLs by 100 percent	-1.4	-1.6	-4.8	-1.1	-1.4
2. Overall NPLs equal to historic high	n.a.	n.a.	n.a.	n.a.	-4.2
3. 10 percent of mortgages become NPLs	-1.6	-2.7	-1.4	-1.9	-2.0
4. 20 percent of mortgages become NPLs	-3.3	-5.7	-2.9	-3.9	-4.2
5. 30 percent of mortgages become NPLs	-5.1	-8.8	-4.4	-6.0	-6.4
6. 30 percent of loans in agriculture and fish sector become NPLs	-1.5	-0.9	-3.0	-1.1	-1.4
7. Default of large exposures to each bank					
The largest exposure	-1.0	-1.4	-1.6	-1.5	-1.3
Three largest exposures	-2.7	n.a.	-4.3	-3.8	n.a.
Five largest exposures	-4.0	n.a.	-5.9	-5.3	n.a.
8. Default of large exposures to the sector as a whole					
The largest exposure	-0.8	-1.4	0.0	-1.5	-1.1
Three largest exposures	-2.4	-1.4	0.0	-2.7	-1.9
Five largest exposures	-3.4	-1.4	0.0	-3.8	-2.5
Liquidity Risk			(Change in Liquidity Ratio)		
1. Withdrawal of 5 largest depositors	-31.6	-22.8	-25.3	-30.8	-27.8
2. Withdrawal of 10 largest depositors	-52.0	-30.8	-41.2	-60.9	-45.2
Interest Rate Risk			(Change in CAR)		
1. Reduction in rate by 500 bps	-2.1	-4.0	-4.7	-3.2	-3.3
2. 50 percent drop in government securities yield	-0.4	-0.1	-0.1	-0.3	-0.2
Exchange Rate Risk			(Change in CAR)		
1. Depreciation of 30 percent	0.0	0.0	1.2	0.0	0.1
2. Depreciation of 90 percent	0.0	0.0	3.6	0.0	0.4
3. Appreciation of 30 percent	0.0	0.0	-1.2	0.0	-0.1
4. Appreciation of 90 percent	0.0	0.0	-3.6	0.0	-0.4
II. Macroeconomic Scenario			(Change in CAR)		
Scenario I	-2.9	-4.4	1.8	-2.6	-2.8
Scenario II	-3.6	-4.9	-5.7	-4.3	-4.8

Source: Staff estimates.

C. Nonbank Financial Institutions

25. **The NBFI sector is, by and large, under-supervised.** Although NAMFISA is authorized to regulate and supervise it, it has not been able to develop the capacity to analyze and respond to developments in the sector. One aspect of this is the lack of comprehensive and reliable data. This impedes a thorough analysis of the performance of pension funds, insurance companies and unit trusts. The analysis in this section should therefore be interpreted with caution.

Pension Funds

26. **The pension fund sector is well developed in terms of total assets size and has also reached an advanced stage of maturity, having effectively been established many years before independence**. The stage of maturity is highlighted by the ratio of benefits, including net transfers, to contributions at higher than 60 percent which is comparable to mature systems (Figure 4).

27. **Pension funds have been able to return reasonable nominal returns that have exceeded the rate of inflation by a significant margin, although available data only cover a very short period and mostly the Government Institution Pension Fund (GIPF).** While equity allocation appears high in comparison to other emerging market countries, it is similar to allocations in developed countries. Several factors have contributed to this outcome:

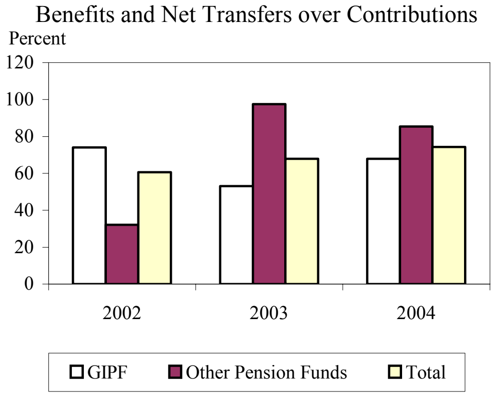
- Data show that about 60-70 percent of assets are invested in equities and unit trusts, and these have so far performed well. Holdings of government bills and bonds have fluctuated between 10-20 percent.

- Under regulation 28, pension funds are required to invest a minimum of 35 percent in local assets but its flexible implementation to include the dual listed equities on the Namibia Stock Exchange (NSX) as local assets has allowed continued diversification and good performance.

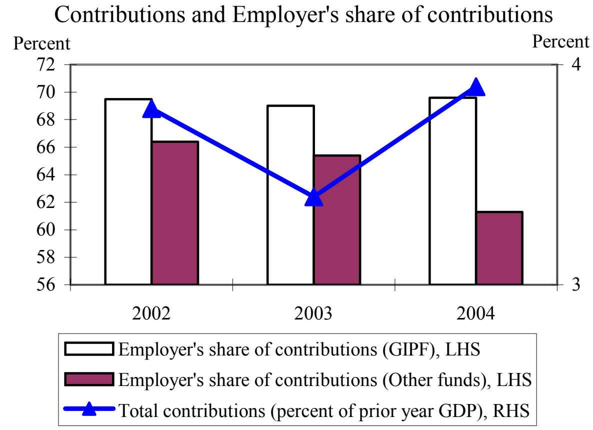
- In contrast, the GIPF has suffered large losses—over 50 percent—in its Development Capital Portfolio investments, aimed at domestic unlisted companies.

Figure 4. Recent Performance of Pension Funds and Insurance Companies, 2001–05

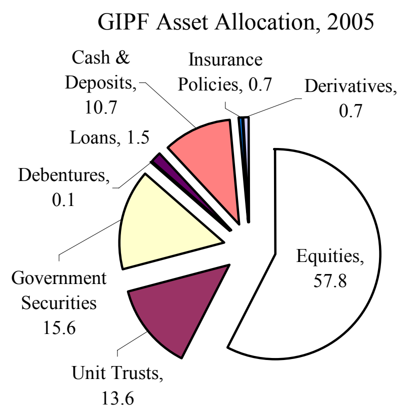
Pension fund sector has reached an advanced stage of maturity...



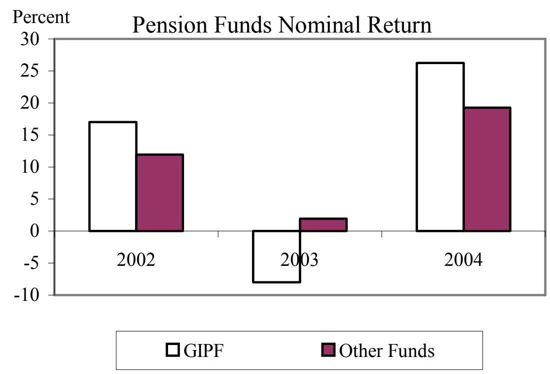
...with sizable contributions as a share of GDP.



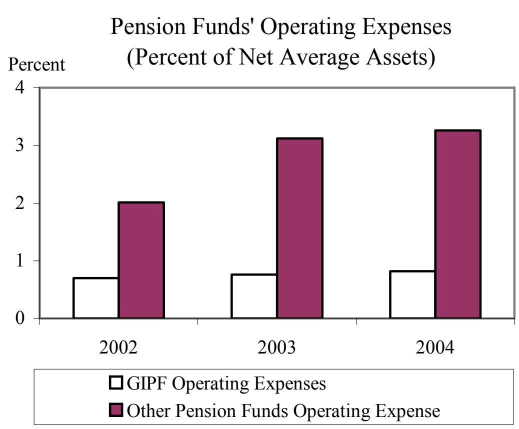
Asset allocation is similar to developed systems.



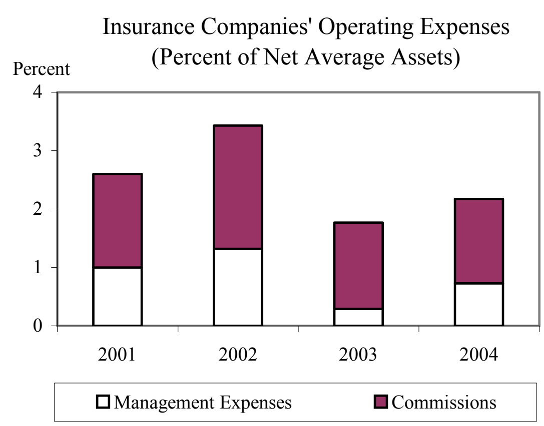
Pension funds have been able to earn satisfactory returns.



Besides GIPF, other pension funds' operating expenses appear relatively high...



...while insurance companies' are low by international standards.



Sources: NAMFISA, GIPF, and staff estimates.

Insurance

28. **Growth in long-term insurance assets as well as premiums have been volatile, although this may have been caused, at least in part, by errors in statistical coverage.** Total assets of long-term insurers were equivalent to about 40 percent of GDP as of March 2004. Annual premiums of long-term insurers corresponded to nearly 6 percent of GDP for the 12 months ending in March 2004. However, no meaningful analysis of the solvency and investment performance of the sector is possible given data constraints. Nevertheless, the close ties between the pension and life insurance industries would suggest that their investment performance follows closely that of the major pension funds.

29. **Short-term insurance is less well-developed.** The level of annual premiums for short-term insurance amounts to 2.6 percent of GDP. This is partly explained by the absence of compulsory third-party motor liability.[9] In addition, large industrial and commercial risks are often insured in overseas markets, mainly South Africa, while product and personal liability lines are not yet well-developed. Local firms claim to be engaging in fierce competition, although loss ratios are low at 55 percent.

IV. Regulatory and Supervisory Frameworks

A. Commercial and Specialized Financial Institutions[10]

30. **The regulatory and supervisory frameworks for banking supervision are broadly satisfactory.** There is a good legal and regulatory environment, while the BON has adequate supervisory powers, although its current remit is too narrow (see below).

31. **However, there are significant weaknesses in implementation.** Major gaps identified in the BCP assessment include the lack of supervision of bank holding companies and financial groups, and the absence of regulatory requirements on market and country risks. Significant weaknesses were also found in the conduct of supervision, as too much emphasis was placed on compliance with regulations and too little on the analysis of banks' risk profiles, taking into account materiality. This hampers BON's ability to identify and prevent banks' problems at an early stage. These shortcomings are primarily caused by a lack of necessary knowledge and skills among supervisors and, to a lesser extent, by the inadequacy of their own risk-based supervision methodologies.

32. **All deposit-taking institutions should be supervised by the BON, regardless of their ownership.** The BON regulates and supervises the four commercial banks. However, the four specialized financial institutions are established under separate legislation, which exempts them from BON supervision. Yet reduced margins and liquidity problems are forcing the National Housing Enterprise (NHE) and Agribank to seek more deposits. These trends are

[9] Compensation for loss of life and bodily injury from car accidents is provided by a fund operated by the Department of Motor Vehicles and is financed from a tax assessed on sales of gasoline.

[10] See Annex for the BCP ROSC.

likely to continue given the funding problems of these institutions and the maturity profile of their lending. As these institutions take more and more deposits, the urgency of competent prudential oversight becomes more apparent. In addition, operational risks due to outdated systems are important as well.[11] On the other hand, the BON should supervise smaller deposit-takers (e.g., large Savings and Credit Cooperatives (SACCOs) or credit unions) with a lighter touch.

33. **Following its October 2005 decision in principle to implement Basel II, the BON should assess the impact of Basel II on the Namibian banking system and its supervision before setting any timeframe.** The priority should be to fully comply with the BCP before implementing Basel II. The BON should also ensure that it remains fully on top of the technical issues involved. It could consider phased implementation of Basel II, starting with pillars 2 and 3 (respectively supervisory review and market discipline) and possibly the standardized approaches of pillar 1 (capital adequacy), before allowing any bank to use internal rating based approaches for supervisory purposes. This will take a number of years, and require signficant enhancement of BON's supervisory capabilities.

34. **The authorities should also strengthen their capacity to monitor and assess emerging threats to systemic financial stability.** While banks appear to be healthy, they are still exposed to risks such as the credit risk arising from household mortgages. At the same time, supervisors will need to be aware of developments outside Namibia given possible contagion to Namibian institutions (see paragraph 70). In many central banks, such monitoring is carried out by a dedicated group or department. Such a group would also be well placed to formulate policies required to respond to changes in the sector as a whole.

B. Nonbank Financial Institutions

35. **It is important to strengthen NAMFISA so it will be able to regulate and supervise NBFIs effectively.** As a matter of priority, NAMFISA has to put in place a comprehensive plan to build its capacity by providing targeted training for its staff and proactively managing public perception of its credibility. The appointment of a CEO with relevant experience is an immediate priority. NAMFISA's Board needs to be independent, equipped with the requisite financial sector expertise, and be accountable to both industry and government. It would also be important to appoint a qualified and experienced actuary to assist NAMFISA. As an interim measure, NAMFISA could also engage an actuarial consultant to assist in implementing current solvency regimes, and, over the medium-term, to help in developing a risk-based solvency framework.

36. **One of the fundamental shortcomings of NAMFISA is the failure to compile, verify, analyze and disseminate accurate and reliable data on the financial soundness and performance of NBFIs that come under its authority.** This reflects the lack of systems and skills to compile and analyze data. The implementation of the Bank Supervision Application is a step in the right direction, but more would need to be done to collect relevant regulatory data and improve NAMFISA's capacity to verify and analyze that data.

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[11] For example, the auditors' qualified opinion on Agribank's last audit report indicates that it is impossible to determine whether stated figures are accurate due to lack of reliable record keeping processes.

37. **Another important task is to verify that pension funds and insurance companies are solvent, well run, and managing risks appropriately.** Off-site in-depth analysis of financial statements and quarterly returns is the first step to identifying financially weak institutions for regulatory interventions. NAMFISA would also need to carry out on-site examinations and implement solvency regimes for insurance companies and defined benefit pension funds. As actuarial evaluations have significant impact on the solvency of insurers and pension funds, NAMFISA should introduce "appointed actuaries"[12] under the insurance legislation as soon as practicable. Insurers and pension funds meeting certain criteria (such as size) should be required to have an "appointed actuary" to report and advise on all matters affecting their financial condition.

38. **A few immediate and straightforward legislative amendments are required to close the gaps in the law.** Asset management services, money market unit trusts and unit-linked life policies should be regularized under the law as soon as possible. Strengthening of NAMFISA's powers should be implemented in conjunction with modernizing Namibia's financial services laws to bring them in line with international best practices and to provide a conducive framework for the financial sector to further develop. This will ensure that NAMFISA has the ability to enforce the new legislation and sanction those who contravene the laws.

39. **In the medium term, NAMFISA should rationalize its current supervisory approach and move to a risk-based supervision framework.** Such a framework encourages institutions to adopt robust corporate governance and risk management practices. A risk-based supervisory approach would help NAMFISA prioritize its limited supervisory resources according to the risk profile and impact of institutions. This should be supplemented by risk-based solvency or capital regimes to provide the appropriate regulatory incentives for institutions to adopt sound market practices. There are merits to entrenching the broad corporate governance principles in legislation, supplemented by a code of corporate governance to facilitate updating. Recent scandals involving alleged misappropriation of funds emphasize the importance of strong corporate governance to complement the regulatory framework.

40. **The current gap in NAMFISA's mandate for market conduct regulation and supervision could be addressed by working closely with industry associations to develop market conduct rules**. These would cover best practices to safeguard clients' funds (e.g., separating client and firm accounts), know-your-client rules, fact-finding on clients' protection and investment needs as well as disclosure of risks, fees, and commissions. NAMFISA should be given an explicit mandate for market conduct regulation.

C. Anti-Money Laundering and Combating the Financing of Terrorism[13]

41. **Namibia does not have an AML/CFT framework in place.** The Prevention of Organized Crime Act, which criminalizes money laundering, was passed in parliament in

[12] See for example "The Role of the Appointed Actuary" at http://www.actuaries.org.uk/files/pdf/life_insurance/apptdact.pdf

December 2004, but has not been put into effect by the Ministry of Justice. The Financial Intelligence Bill was recently tabled in parliament. The Anti-Terrorism Activities Bill is still in draft form and there is no time frame as to when it will be tabled before parliament.

42. **Given the absence of an AML/CFT framework, the BON has exercised its powers under the Banking Institutions Act (BIA) to issue general anti-money laundering related determinations and circulars to address aspects of money laundering, but with limited success.**[14] They, nevertheless fall short of compliance with the international standards and are not sufficient to ensure industry compliance. Meanwhile, all South African owned banks and larger insurance companies have adopted home office AML/CFT policies to some degree.

D. Legal, Judicial, and Accounting Frameworks

43. **Creditor rights are reasonably well established and the accounting framework is set to comply with International Financial Reporting Standards (IFRS).** However, the current arrangements for oversight of the accounting profession are not effective. The Public Accountants and Auditors Board (PAAB) is chiefly responsible for authorizing chartered accountants, supervising their activities, receiving reports relating to irregularities on their clients' financial statements and, where appropriate, taking disciplinary actions and /or alerting the Namibian authorities. As some of its members have not been replaced, the PAAB has not been able to operate since March 2005. Moreover, although the PAAB has transmitted to the Prosecutor General (PG) three to five reports concerning irregularities on financial statements each year since 1990, it seems that no action has been taken by the PG.

V. Access to Financial Services

A. Affordability

44. **While access to finance in Namibia is better than in other SSA countries, it is still very limited, due to the structure of the Namibian economy.** On the one hand, there is pervasive rural poverty, a growing population of urban shack dwellers who suffer from widespread unemployment, and low population density. On the other hand, the existence of a considerably affluent population segment and a corporate business sector provides steady profit opportunities for existing institutions. Consequently, the financial system has organized itself to serve these segments of the economy and has so far not ventured away from the existing clientele.

45. **Lack of access may be aggravated by basic banking services fees that appear high to most of the population.** Available estimates indicate that less than 15 percent of the population use transaction, credit or insurance services.[15] The use of savings products is

[14] The BON has issued in June 1998, Determinations on Money Laundering and "Know Your Customer Policy" BID-3, which requires banks to keep records relating to their customers. A complimentary Circular, BIA 2/02 was issued in June 2002 to provide guidance regarding the prevention, detection, and control of possible money laundering activities.

[15] The proportions reported in the FinMark Trust Research Paper No.3 of 2003, which was prepared by Genesis Analytics, are respectively 9.8 percent, 11.8 percent and 12.8 percent (Genesis Analytics 2003).

relatively high at 45 percent of the population although even this is low by international standards. Other access indicators suggest that Namibia is outperforming other SSA countries, but it is lagging behind other countries with comparable levels of per capita income (Table 3).

Table 3. Loan and Deposit Access Indicators in Selected Countries

Country	Loan accounts per 1,000 people	Loan-income ratio	Deposit accounts per 1,000 people	Deposit-income ratio	GDP per capita
Namibia	80.7	5.2	423.0	1.3	2,312
Brazil	49.6	6.2	630.9	0.4	2,788
Kenya	...	...	70.0	6.3	434
Mauritius	207.1	2.8	1,586.0	0.5	4,265
Turkey	264.5	0.7	1,114.2	0.7	3,365
Uganda	5.8	10.7	46.6	3.9	245
Zimbabwe	...	...	173.6	8.0	634
Median	80.6	3.8	528.9	0.7	...
LIC Median	75.5	4.2	423.0	0.8	...
HIC Median	482.1	2.2	1,986.0	0.4	...

LIC: low-income countries; HIC: high-income countries
Sources: Beck et al (2005) and staff estimates.

B. Banking Services

46. **The high fees applied by Namibian banks reflect the apparently high service levels as well as limited competition.** One way to foster competition among banks is to improve transparency regarding fees and charges. Commercial banks are disclosing only maximum fees for their services and no one knows what actual fees are. Furthermore, the structure of fees is complicated and difficult to compare across banks.

47. **Another promising avenue is to encourage banks to introduce products that target low-income groups.** This is currently being done by the South African parents of commercial banks. It would not be difficult for these institutions to introduce similar products in Namibia.

48. **In the longer-term, allowing more entrants is the best way to foster greater competition.** This could be achieved by the following:

- As is current practice, the **BON should remain open to new reputable entrants.**

- **A strong and efficient PostBank could provide affordable services and compete with banks.** The fees charged by the postal savings bank are already significantly lower than those levied by banks for similar services. Automation and cross-selling of services could achieve a further reduction.

- **The emergence of credit unions, especially among civil servants or employees of large companies, should be encouraged.** Credit unions can operate with low spreads since they do not need to spend heavily on marketing and advertising or to build large branch networks. They can also avoid exposure to credit risk by initially focusing on savings mobilization and short-term loans. As they acquire managerial expertise and sound management, they could expand into longer-term loans.

C. Microfinance

49. **Expanding the supply of microcredits in both urban and rural areas is the main challenge facing the authorities in promoting micro and rural finance.** The supply of microcredit can also be expanded by stimulating the spread of Savings and Credit Associations (SCAs) throughout the country and by taking steps to increase the number of commercial lenders engaging in microcredit activities (such as by changing the usury act). The emergence of credit unions could also go a long way toward filling this gap.

50. **The usury act should be replaced because it is not protecting the poor.** Indeed, microlenders charge rates higher than the usury ceiling, reflecting their lending risks. Some term lenders charge interest rates within the usury ceiling but require the purchase of expensive credit life insurance that brings the total cost to 3 or 4 times the prime rate. The cap on charges is therefore not binding. At the same time, the act inhibits competition because it discourages entry by reputable institutions, thus restricting supply and therefore supporting higher interest rates.

51. **A consumer credit act with truth-in-lending provisions can most effectively protect the consumers.** Charges and costs will be more transparent to borrowers. Meanwhile, as has occurred in many countries, lifting the cap will likely lead to more entrants, greater competition, and lower rates.[16] A consumer credit act should emphasize transparency and disclosure and should grant the regulator the power to take prompt action against cases of serious misconduct. Establishing an ombudsman office for investigating and resolving complaints and disputes, not only on microlending operations, but over the whole gamut of consumer financial services—including banking, insurance and pensions—should also be considered.

D. Housing Finance

52. **Mortgage lending for high- and medium-income households is well-developed, but there is not enough housing (especially low-cost housing) to meet growing urbanization.** This fairly well developed market has been fostered by strong property administration system. Foreclosure proceedings are also efficient. The level of arrears is fairly low, in the range of 1–3 percent, except in NHE's case (12 percent). Nevertheless, with urban immigration, there is not enough supply to meet housing demand, especially in low- to moderate-income groups.

53. **Legal uncertainties attached to some forms of land tenure impede housing finance.** A significant proportion of land in the country still remains under customary or informal possession, including in some urban developments,[17] and this largely excludes

[16] For example, see CGAP Occasional Paper No. 9, 2004, available at http://www.cgap.org.

[17] In these areas, "Permissions to Occupy," which were not full titles, were delivered until 2002.

"owner" occupants from housing finance.[18] A first and easy step to channel resources toward housing, is to clarify the legal status of long term leases so they can be collateralized. The government is well aware of this issue, and new legal provisions are being considered.

E. SME Finance

54. **SME access to finance is limited.** Important reasons for the lack of access include commercial banks' preference for collateral, the underdevelopment of leasing and factoring services, the nascent state of development of private equity and venture capital funds, and the ineffectiveness of specialized financial institutions and the Small Business Credit Guarantee Trust (SBCGT). In particular, the guarantees issued by the SBCGT suffer from poor credit appraisals and monitoring, as well as weak loan recovery efforts by participating banks, resulting in a limited amount of small firm operations. Two commercial banks have only recently established specialized divisions to serve (SMEs).

F. Specialized Financial Institutions

55. **Widespread efficiency and effectiveness problems and emerging prudential concerns require revisiting the role and effectiveness of specialized financial institutions.** These institutions have by and large had limited value-added. Moreover, their products, business models, and policies make them similar to other financial institutions, which may carry out the functions of the specialized financial institutions more efficiently. The review of these specialized institutions should not only include appropriate measures of efficiency to judge historical performance but should also question their current business models. In this context, the review should explore whether other options exist to pursue the policy goals that these institutions were set up to meet.

G. Informational Infrastructure

56. **The usefulness of the two credit reference bureaus could be improved by collecting positive information.** The availability of information on the credit record of prospective borrowers promotes competition, reduces credit risk and lowers collateral requirements. However, the bureaus should be encouraged to collect and disseminate both positive and negative information on the payment and credit record of credit applicants. Currently the two credit reference bureaus are not overseen by any official agency. Their operations should be covered by future consumer protection legislation.

VI. Creating Opportunities for Domestic Investment

A. Capital Flows

57. **The limited investment opportunities in domestic financial markets have led to sizable outflows of Namibian savings into the liquid and relatively developed markets in neighboring South Africa.** Namibia has increasingly large net claims on its neighbor, putting

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[18] Banks have however started to lend in these areas with a lien on pension fund accounts.

pressure on its reserve levels.[19] This situation has been a central concern for the Namibian authorities. The main contributors to the capital outflows are net outflows in both portfolio investment and other investment, which offset net inflows in direct investment.

58. **The authorities have tried to stem these outflows by requiring institutional investors to invest a portion of their pension or life insurance funds in domestic instruments.** However, these regulations are not likely to be effective since individuals remain free to invest directly in other CMA countries. Indeed, if such regulations were to make Namibian pension funds or life insurance companies less competitive compared to other institutions in the CMA, individuals would have even more incentive to invest outside the country. In addition, as Namibia is a small country, Namibian investors benefit significantly from access to markets that allow them to diversify their risk.

59. **A positive interest rate differential with South Africa and more attractive investment opportunities are likely to be more effective as a means of increasing reserves or attracting capital flows.** If the level of reserves is too low, the authorities should stand ready to incur the costs of obtaining those reserves.[20] However, the cost of such a policy will eventually be reflected in the BON's financial position. Hence, the long-term solution to this problem requires significant structural changes in the Namibian economy, in order to attract capital.

B. Enhancing Domestic Investment Opportunities

60. **The Namibian financial sector can help create domestic investment opportunities by focusing on its role in allocating, assessing and managing risks as well as in market development.** This requires establishing a critical mass of asset managers who are skilled in entrepreneurial development (i.e., various forms of private equity or venture capital), expanding information sharing and monitoring so there is greater awareness of risks and returns, and strengthening corporate governance and risk management in insurance companies and pension funds.

61. **Strengthening the financial sector's role is preferable to requiring institutional investors to invest in particular assets.** Indeed, if successful, strenghtening the financial sector could even lead to capital inflows. In any case, regulations to "control" flows are not likely to be effective because they are easily circumvented, especially within the CMA. Some suggestions include: (i) establishing a vibrant private equity industry with asset managers who specialize in investing in the industry, to create more opportunities for domestic investment; (ii) promoting leasing and factoring companies, which could help develop the private securities markets; and (iii) developing asset securitization.

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[19] Persistent and continuous capital outflows that averaged around N$1.8 billion per year from 1990 to 1994 have accelerated to about N$2.4 billion per year since 1995.

[20] The BON could raise interest rates it pays on its deposit facilities or make direct foreign exchange purchases and then sterilize the operation.

62. **In addition, the BON could further develop local money and foreign exchange markets by improving information flows and actively participating in these markets.** First, the BON should more actively manage domestic liquidity conditions. Second, it could foster foreign exchange market development by (i) facilitating price discovery; (ii) welcoming participation by other large institutions such as NBFIs; and (iii) participating more actively in the market by buying and selling foreign exchange, if consistent with broader monetary policy. Third, the BON should keep up efforts to develop a liquid secondary market for government securities. Finally, it should ensure that its lending facilities do not discourage financial institutions from trading with each other.

63. **The case for tightening domestic investment requirements is not convincing.**[21] Such a change has to weigh the macroeconomic impact, potential costs to beneficiaries in terms of returns and solvency given the smaller investment universe, and take into account the availability of domestic investment opportunities.

64. **Available information indicates that the performance of domestic instruments has so far been less than satisfactory, and this casts doubt on the government's proposal to compel institutional investors to invest large amounts of their resources in domestic securities.** Such a requirement could lower investment returns and channel funds to unworthy projects. It would be preferable to let institutional investors refine and streamline their private equity operations and to seek voluntary participation by institutional investors in their projects only when they have created a strong track record and can credibly offer the prospect of high returns at a tolerable level of risk.

65. **In particular, the requirement to invest 5 percent of assets in unlisted Namibian securities is highly risky** On a purely technical level, depending on how it is calculated and imposed, this requirement could lead to continuous losses on the part of institutional investors. The main concern, however, is the high level of risk that institutional investors could be carrying. After all, for prudential reasons such investments are currently limited to a maximum of 5 percent. In addition, in an environment where such investment opportunities are rare, a requirement to invest in unlisted assets could lead to asset price inflation, risky behavior, and efforts to circumvent regulation.

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[21] In July 2004, the Namibian cabinet approved a tightening of these requirements. This would (i) reduce the percentage of dual-listed companies on the Namibia Stock Exchange (NSX) that qualify as a domestic investment to 10 percent from the current 100 percent, (ii) require all institutional investors to place a minimum of 5 percent in unlisted Namibian securities, and (iii) subject unit trust management companies to a domestic asset requirement and remove the tax holiday on income from unit trusts. No detailed proposal to implement this decision was available at the time of the mission.

VII. Systemic Liquidity and Crisis Management

A. Liquidity Management

66. **Money and foreign exchange markets are essentially extensions of the South African markets.** Given the close institutional ties with South Africa, the CMA, and the lower costs associated with transacting in a more liquid market, it has been much easier and cheaper for financial institutions to use regional financial markets than local domestic markets. This has limited activity in local markets and BON's scope for conducting monetary operations, although local markets trading has slowly picked up with growing income and the development of domestic payment systems (Figure 5).

67. **In line with the development of the national payment system, the BON should continue to develop its capacity to manage short-term liquidity through open market operations by using repos and reverse repos.** The BON's main policy instruments have been rather passive; it currently has an overdraft and a deposit facility. As payments are increasingly settled domestically (rather than in South Africa), domestic liquidity management will increase in importance. More market-based and active monetary operations—using repos and reverse repos—would also help develop local money markets.

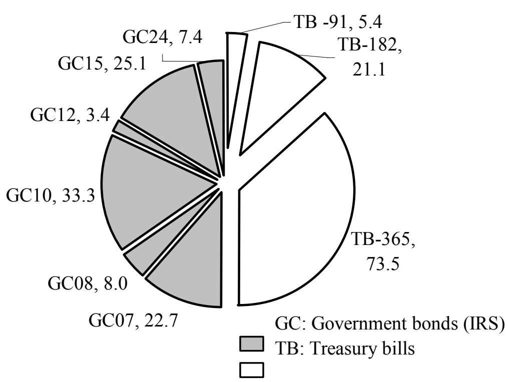
68. **More active liquidity management could entail additional costs for the BON.** The BON would need to improve its own liquidity forecasting as well as set up a transparent and efficient means for conducting operations, including establishment of criteria for its counterparts and a master repurchase agreement. In addition, since the BON does not currently hold enough government securities, it will need to build up a stock of securities to be used in monetary operations. The BON could purchase government securities in the secondary market, and consider raising the call deposit rate to offset the liquidity injection. Monetary operations may lead to losses for the BON so the Ministry of Finance (MOF) and the BON should agree on arrangements to ensure that any such losses are compensated from the budget where necessary. Meanwhile, the BON should also carefully review banks' automatic access to the overnight liquidity facility for settlement purposes and make sure that a penalty rate is applied for its use.[22]

[22] While interbank and electronic funds transfer, which represent the bulk of the total, are settled by 6.00 p.m., check clearing is not settled until 10.00 p.m. Banks have automatic access to collateralized overnight repos to cover any shortage at the end of the day in their settlement accounts at BON. For this purpose, banks are required to pledge enough eligible securities as collateral to avoid the rejection of any settlement request. Currently, there are no 'failure to settle' rules in place, but in practice, banks have been keeping sufficient collateral to cover any possible shortfalls.

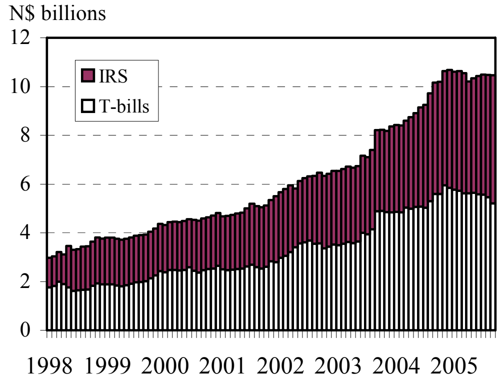
Figure 5. Financial Markets

There is a well-developed government securities market.

Distribution of Outstanding Government Securities
(Percent of total)

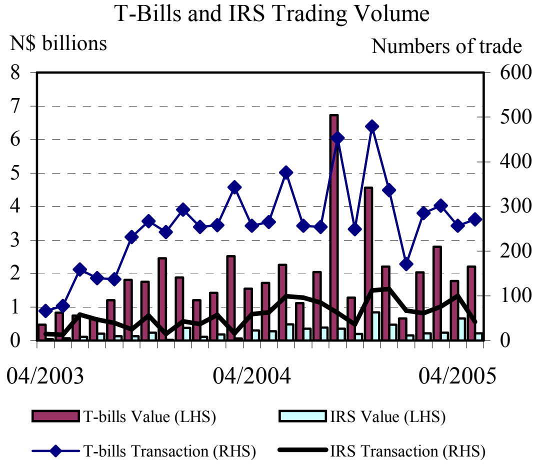


Size of the Government Securities Market



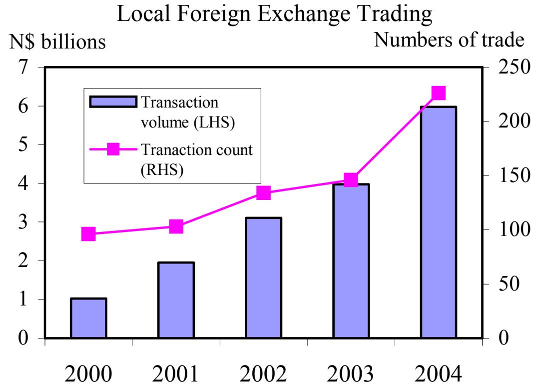
And active trading in T-bills.

T-Bills and IRS Trading Volume



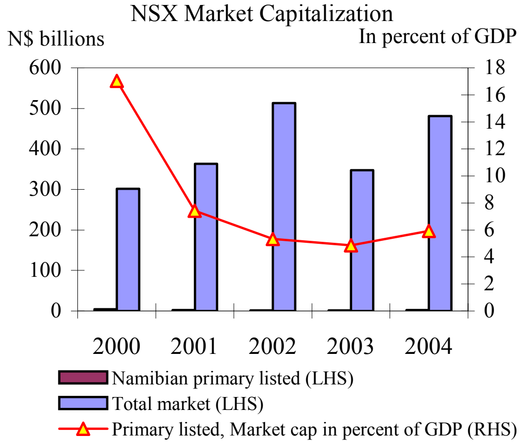
Local foreign exchange transactions are steadily growing from a very low level.

Local Foreign Exchange Trading



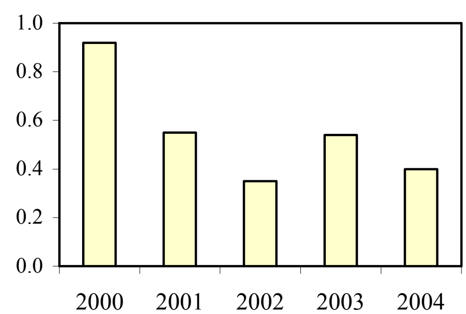
The NSX is dominated by dual-listed companies.

NSX Market Capitalization



Trading in NSX is not active.

Turnover Ratio in NSX



Sources: BON, NAMFISA and staff estimates

B. Safety Net and Crisis Management

69. **The BON has the legal authority under the Banking Institutions Act (BIA) to take an appropriate range of remedial actions against banks.** Its powers range from requiring corrective actions such as restricting the extension of credit or the payment of dividends, and removing directors and officers from office, to assuming control of entire banking activities or appointing a person to conduct the business of the Banking Institutions (BI).[23] The BON can also apply to the courts to wind up a bank, although at present it has no power to ensure that the liquidator is someone it approves of. Planned amendments to the BIA will, however, remedy this.

70. **Given that the major financial insitutions are South African-owned, crisis management will require good communication with regulators in South Africa.** While there is no formal crisis management framework for banks and the major NBFIs, the legal powers accorded to the BON and NAMFISA to take remedial action against weak insitutions are broadly satisfactory.[24] The challenge for regulators, however, is to deal with any potential problems that arise from potential contagion (e.g., problems with parent institutions) or South African ownership (e.g., if the local subsidiaries require remedial actions). In this regard, the BON should start holding regular meetings with the South African Reserve Bank (SARB) as agreed under an Memorandum of Understanding (MOU) that already exsits. At the same time, Namibian regulators have to be vigilant and follow developments with parent institutions in order to react quickly if problems arise.[25]

[23] In its procedure manual for supervisory actions, the BON defines the way it intends to exercise its powers (both formal and informal) and to deal with banks' weaknesses.

[24] The BON has a lender of last resort (LOLR) facility. There is also a guarantee fund to cover stock broker's liabilities.

[25] In this regard, the policy of requiring foreign-owned financial institutions to be set up as a subsidiary rather than a branch helps minimize potential contagion and other risks. It does not, of course, mitigate reputational risk and contagion. The BCP assessment has recommended that the BON should require a formal commitment from South African parent banks to support their Namibian subsidiaries.

Observance of Financial Sector Standards and Codes—Summary Assessments

This Annex contains summaries of the assessments of compliance with the Basel Core Principles for Effective Banking Supervision (BCP). The assessment of the BCP was performed by Mr. Peter Phelan, formerly of the Bank of England and Financial Services Authority, U.K., with over thirteen years supervisory experience, and Mr. Cedric Mousset of the World Bank with over eight years supervisory experience, from October 12 to November 2, 2005. Detailed assessments were also prepared and presented to the authorities.

The assessment takes into account both the basis for regulation and supervision, such as the institutional framework, laws and guidelines, and implementation by the authorities as well as in the supervised institutions.

A. Basel Core Principles For Effective Banking Supervision

General

71. **The assessment of the Basel Core Principles (BCPs) was conducted in accordance with "The Basel Core Principles for Effective Banking Supervision" (1997) and the "Core Principles Methodology" (1999).** The assessment takes into account both the basis for regulation and supervision, as well as the implementation by the authorities and the supervised institutions.

72. **The management committee of the BON has decided that it will implement Basel II, but no details have yet been worked out.** Full compliance with the BCP should constitute a prerequisite to the implementation of Basel II. It is important that, before implementation, the BON carries out a full assessment of the impact that Basel II would have both on the banking system and its own activities and resources, as well as ensuring that it remains fully on top of the technical issues involved here. The BON should also consider a phased implementation of Basel II, starting with pillar 2 and 3 (respectively supervisory review and market discipline) and possibly the standardized approaches of pillar 1 (capital adequacy), before allowing any bank to use internal rating based approaches (IRB) for supervisory purposes. This will take a number of years, and require a very significant enhancement of BON's supervisory capabilities.

Institutional and macroprudential setting, market structure—overview

73. **Namibia has enjoyed good macroeconomic stability since independence in 1990.** A stable political and legal environment has proved conducive to economic activity and real GDP growth has averaged 4.5 percent in the last five years.

74. **Namibia has one of the most sophisticated and highly developed financial systems in Africa.** This comprises four commercial banks, around 30 insurance companies and many pension funds, asset management companies, unit trust management companies, plus some specialized lending institutions and microfinance organizations. All the banks have

strong links to South Africa, with three of them having majority South African ownership. The banks appear all well-capitalized, profitable and well-managed.

General preconditions for effective banking supervision

75. **There is a general consensus among market participants and the legal profession that the legal system is noncorrupt, fair and impartial, as well as being reasonably rapid in processing straight-forward cases.** The existence of 'unproclaimed' land, where Western-style rights do not apply, does mean, however, that in large parts of the country collateral for banks is not available.

76. **IFRS will be directly applicable in Namibia with effect from 1 January, 2006.** All registered companies have to have an external auditor and the major international accounting firms are all present in Namibia.

77. **Namibia has a real time gross settlement system (RTGS), the Namibian Interbank Settlement System (NISS), which has been fully operational for both large payments and retail transactions since mid-2004.** All domestic payments are routed through this system, save for credit and debit card clearing which is still routed through South Africa, but which will be taken over by the local clearing house, Namclear, in March, 2006. The system is currently working in a broadly satisfactorily manner, although there are no 'failure to settle' rules in place. The banks currently ensure that they have adequate collateral for repos to cover any shortfall. An oversight framework for payment systems is currently being developed by the BON.

78. **There is no deposit insurance system in place** in Namibia and none is currently contemplated.

Main findings

79. **The assessment of Namibia under the BCPs was carried out by two experienced assessors** and was based on a self-assessment carried out by the Namibian authorities and on discussions with the supervisors, all four Namibian banks, lawyers, accountants and the MOF.

80. **The Namibian Authorities chose to be assessed against both the essential criteria (EC) and the additional criteria (AC) of the Core Principles**, which meant that they were assessed against international standards of best practice.

81. **The structure of banking supervision in Namibia (both legal and operational) is broadly satisfactory**, but some tidying up is necessary even here. This would cover the supervision of government-owned specialized institutions as well as micro-depositors.

82. **There are more significant shortcomings in operational practice**, with, in particular, much to be done to enhance the skills and knowledge of supervisory staff as well as supervisory methods which still place too much importance on compliance with

regulations and not enough on banks' risks profile. Namibia is Compliant with three of the BCPs, Largely Compliant with ten (including the overall assessment of CP.1), Materially Non-Compliant with nine, and Non-Compliant with three. The assessment of CP.15 (anti-money laundering) is Materially Non-Compliant, but a full assessment is being done by the AML/CFT team.

Summary assessment

- Objectives, Autonomy, Powers, and Resources (CP 1)

  The BON is the only authorized banking supervisor in Namibia and its powers are enshrined in legislation which is broadly satisfactory. However, neither specialized institutions (some of whom are taking deposits) are covered by the BON, nor are small micro-deposit-takers. This should be remedied in a timely manner. The BON is de facto independent of government in operational matters, but there is a potential ambiguity in the law which should be put right.

  The BON has MOUs with other supervisors, both at home and abroad, reports on its supervisory activity through its Annual Report, website and ad hoc meetings with ministers, and has the necessary financial resources to perform its function. Staff numbers are adequate, but turnover is higher than ideal, and there are skills deficiencies. The Bank and its staff are protected against suit when carrying out their duties in good faith, and the Governor and his senior staff can only be dismissed for cause.

- Licensing and Structure (CPs 2–5)

  BIs are clearly defined in law, as are their permitted activities, and the use of the term 'bank' is controlled. Criteria for the licensing of BIs are set out in law, a minimum amount of capital is set, and the criteria applied for licensing are consistent with those for ongoing supervision. Although the BON has the power to control the acquisition of shares in a BI directly, as well as the BI's own acquisitions, the lack of consolidated supervision covering bank holding companies means that these powers can be, and are, frequently circumvented.

- Prudential Regulations and Requirements (CPs 6–15)

  Capital adequacy rules are broadly Basel compliant, save that there is no market risk regime of any kind. Credit policies, loan loss and provisioning are reasonably well handled, although the BON will have to look urgently at how consistent its provisioning rules are with IFRS and make any necessary adjustments. Large exposure rules are broadly satisfactory, but the adequate connected lending rules are not enforced. There is no country risk regime, nor, as mentioned above one for market risk. Liquidity, interest rate and operational risks are inadequately covered. The law requires only one person to direct the BI, rather than the two required to ensure proper check and balances as well as business continuity, and more needs to be done, both in regulation and in supervision, to ensure that the internal control environment of BIs is satisfactory.

- Methods of Ongoing Supervision (CPs16–20)

  On-site and off-site supervisors liaise reasonably well and a reasonably comprehensive set of returns is required of banks. Some of these are audited both by on-site examiners and (when they carry out their audit) by external auditors. However, the analysis by off-site staff is superficial, and many areas are not covered by the returns (e.g., operational, market and country risk). On-site work is also far from comprehensive, with, for example, no real analysis of the control environment of the bank, nor of its management. There are contacts with BI's managements, but not with their Boards of Directors, nor with the external auditors. Meetings are not held according to a coherent plan, nor are they minuted. There is no consolidated supervision regime for banking groups, including their holding companies in Namibia, and financial conglomerates.

- Information Requirement (CP 21)

  Banks will have to comply with IFRS from January 1, 2006. The BON must approve the appointment of a bank's external auditor and, in practice, all four banks are audited by a major international firm. There are no direct links between the BON and the external auditors.

- Formal Powers of Supervisors (CP 22)

  There are comprehensive powers in the law regarding the remedial actions that the BON can take. Little occasion has arisen to use these, but restrictions on one bank in difficulty were imposed a number of years ago ahead of a market resolution of the problem by merger.

- Cross-Border Banking (CPs 23–25)

  There are as yet no foreign activities by Namibian banks, but one is contemplating establishing a subsidiary of its holding company abroad. In the absence of consolidated supervision, including bank holding companies, it is unclear that the BON will be able effectively to supervise these activities. It does have links with foreign supervisors of parents of banks in Namibia, where again the necessary legal powers are available. Contacts are, however, limited to general issues rather than institution specific ones.

Table 4. Recommended Action Plan to Improve Compliance of the Basel Core Principles

Reference Principle	Recommended Action
CP.16: On-site and off-site Supervision	Ensure that the full range of risks in banks is examined and prepare guidelines to help examiners in this.
CP.1.2: Staffing and remuneration	Review training arrangements and need for expert staff. Review arrangements for key staff to ensure that financial and non-financial incentives are in place to reduce turnover and promote staff's motivation.
CP.20: Consolidated Supervision	Introduce a regime for banking groups, including their Namibian holding companies, and financial conglomerates.
CP.12: Market Risk	Introduce a regime.
CP.13: Other Risks	Issue detailed risk management requirements for operational, interest rate and liquidity risks, and set disclosure requirements for these.
CP.14: Internal Control and Audit	Issue detailed internal control requirements and ensure that examiners cover these Require banks to have two principal officers.
CP.11: Country Risk	Introduce a regime.
Introduction and Methodology: Basel II	Ensure full compliance with the BCPs and carry out an assessment of the impact of Basel II on both the system and the BON, before setting any timeframe for implementing Basel II.

Authorities' response

83. The authorities concurred with the assessment and are taking steps to implement the recommendations.

The Common Monetary Area and Regional Links

84. **The CMA encompasses Lesotho, Namibia, South Africa and Swaziland**. The CMA is the result of a long history of monetary cooperation in southern Africa. After the South African Reserve Bank (SARB) was established in 1921, the South African pound became the common currency of the territories that are now Botswana, Lesotho, Namibia, South Africa, and Swaziland. In 1974, Lesotho, South Africa, and Swaziland signed the Rand Monetary Agreement while Botswana decided to pursue an independent monetary policy with a flexible exchange rate. The Rand Monetary Agreement was replaced by the CMA Agreement in 1986 and the Multilateral Monetary Agreement in 1992 when Namibia joined the CMA as an independent state.

The MMA contains a number of important provisions:

- Each country has its own central bank and currency but may allow the rand to circulate as legal tender.
- The CMA countries agree not to restrict capital flows within the CMA except for domestic investment requirements.
- The governments and financial institutions of the CMA countries have a right to access the South African capital and money markets and the CMA countries have agreed to harmonize their exchange controls with South Africa's.
- South Africa compensates the other CMA countries for lost seignorage due to rand circulating within their borders.
- CMA members may conclude bilateral agreements with South Africa on monetary policy and exchange rate policy.

85. **Aside from the CMA, there are a number of other agreements on economic cooperation in southern Africa**. The Southern Africa Customs Union (SACU) was established in 1910 and includes the CMA countries plus Botswana. This agreement was revised in 2002 to give Botswana, Lesotho, Namibia, and Swaziland more say in policy. The agreement calls for free trade within SACU and a common external tariff. In addition, SACU members agree to adopt common policies in agriculture, industry, competition, and unfair trade practices. The SACU members agree to share customs and excise revenue. Customs revenue is allocated in proportion to intra-SACU imports while the excise revenue is allocated 85 percent according to each member's weight in SACU GDP and 15 percent is allocated according to deviations of per-capita GDP versus the average.

86. **The Southern Africa Development Community (SADC) was established in 1992 and includes Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia, and Zimbabwe**. The purpose of SADC is to promote development and growth and alleviate poverty in member states through economic

and political cooperation. The SADC agreement consists of general objectives rather than specific obligations. The key policy objective is to strengthen trade and investment linkages among SADC countries. In 2000, the SADC Protocol on Trade was implemented, which aims to establish Free Trade Area by 2008.

87. **Namibia is a member of the Committee of Insurance, Securities and Nonbanking Authorities (CISNA), a committee of the SADC**. CISNA aims to promote (i) sound regulatory frameworks, (ii) harmonized regulation of capital markets, investment services, insurance and retirement funds; and (iii) eventually, free flows of capital across the SADC region.

Financial System Structure

A. Introduction

88. **The current features of Namibia's financial system were laid during the preindependence period.** Its commercial banks were either controlled by South African parents or had strong ties with South Africa. While Namibia was still a protectorate of South Africa, its pension funds and insurance companies benefited from the strong emphasis of mining companies on adequately protecting and securing retirement income for their employees. The civil service was also covered by a funded pension scheme. Since independence, the growth of private companies and the civil services has provided additional impetus to the rapidly expanding role of pension funds and insurance companies. As a result, Namibian pension funds and insurance companies have sizeable assets under management (AUM), about 100 percent of GDP. This is one of the highest ratios among emerging market economies, and almost three times as large as Namibia's domestic debt and local equity markets.

89. **Since independence, the government has encouraged, and in some cases required, financial institutions to localize their operations.** "Namibianization" has been effected in a variety of ways; for instance, foreign banks and insurance companies are required to set up subsidiaries to carry out their businesses in Namibia and banks have to maintain at least 100 percent of their liabilities in local assets. Pension funds and insurance companies are also required to invest at least 35 percent of their total AUM in Namibian assets. The objective is to ensure important decisions and operations are carried out in Namibia.

B. Commercial Banks and Specialized Financial Institutions

90. **There are four commercial banks in Namibia, with two banks controlling more than 60 percent of the total assets, loans, and deposits.** Three of four commercial banks are subsidiaries of South African banks and the fourth, Bank Windhoek, has a South African bank (ABSA) as its largest shareholder (36 percent). Moreover, although Bank Windhoek makes a point of stressing its status as the only truly 'Namibian' bank, there have been suggestions that ABSA's new owner (Barclays) may be interested in increasing its stake. Most of the banking groups are financial conglomerates (e.g., two management companies controlled by banks have a 60 percent market share of assets under management in Namibia). Nevertheless, banking remains in all cases their main source of revenue.

91. **All banks engage in a broadly similar business**, offering commercial banking services (deposits, transmission services and loans) to corporates, standard retail services to the private sector (defined as those in regular employment or who have a steady income) and mortgages, sometimes for periods as long as twenty years. Mortgages are the largest single part of banks' loan portfolios (43 percent). Delivery is through a branch network in the major towns.

92. **There is little or no investment banking activity**, although some project loans are made in the primary and industrial sectors. All banks hold government securities and treasury bills and there is some trading in the latter. Much risk management is either handled in South Africa or according to policies and regulations laid down by the South African parents, and the existence of the rand peg whereby the rand is treated as a domestic currency means that foreign exchange exposure is very limited.

93. There are four state-owned specialized financial institutions—PostBank, Agribank, DBN, and the NHE—that act as financial institutions. Their total assets are about N$2.5 billion (7 percent of GDP). These institutions are tasked to support specific public policy objectives.

- **PostBank provides basic saving and remittance services through 120 outlets dispersed all over the country.** PostBank has by far the largest geographical outreach among all financial institutions. Over 40 percent of households have savings accounts with PostBank and its charges are substantially lower than those of commercial banks. It enjoys a fiscal advantage because, unlike bank deposits, interest income on postal accounts is exempt from tax. It does not engage in lending activities. PostBank's deposits are currently about N$600 million (1.6 percent of GDP).

- **Agribank supports agricultural activity through short term loans for crop production and medium- and long-term loans for investment in farmland and equipment.** It is the largest specialized financial institution with assets of about N$1.2 billion (4 percent of GDP). Agribank also provides special loans including affirmative action programs, national agricultural credit programs, and the government tractor scheme. Agribank is not currently taking deposits from the general public but could do so upon approval of the minister of finance. However, it is currently taking deposits from other parastatals, as well as its staff without explicit authorization.

- **DBN has only recently started operations.** It provides funding to new investment activities for development either directly or through lines of credit to other financial institutions. It does not take deposits.

- **NHE was set up to address housing needs.** It makes loans for the purchase of homes and builds houses for sale. NHE is authorized to take deposits and currently has over N$5 million in deposits and N$500 million in total assets.

94. **The BON regulates and supervises the four commercial banks.** However, the four specialized financial institutions are established under separate legislation, which exempts them from BON supervision. They are audited by external auditors hired by them or by the Auditor General.

C. Nonbank Financial Institutions

95. **Namibia has a well-developed contractual saving sector (pension funds and life insurance companies) with total assets of around 100 percent of GDP**. Contractual savings institutions have close links with South African institutions, but they have also been able to develop considerable local expertise. There are many other nonbank financial institutions, such as unit trusts, brokers of various vocations, asset managers and fund administrators, as well as a growing presence of microlenders. The Namibian stock exchange lists and trades both equities and bonds.

96. **Pension funds are the largest institutional investors, with AUM of N$21 billion in March of 2004, equivalent to 57 percent of 2003 GDP.**[26] There are over 500 pension funds, but are small and are administered by external fund administrators that provide basic record keeping as well as more specialized legal and actuarial services. Alexander Forbes is the largest pension fund administrator with about a 60 percent market share. There is also a small number of pension funds that are administered and insured by life insurance companies. These funds have total assets of N$2.4 billion that are included with insurance company assets in published statistics.

97. **The largest pension fund is the GIPF that covers civil servants and employees of other government agencies and operates as a defined benefit plan.** Its net assets amounted to N$15.1 billion in March 2004, representing 73 percent of total pension fund assets.[27] The remaining N$5.6 billion was held by various smaller funds, the bulk of which are based on defined contribution plans. The average size of private pension funds is less than N$12 million, implying that pension fund operations may be suffering from small scale diseconomies. However, several plans belong to umbrella funds in an attempt to lower operating costs and enhance investment performance.

98. **The insurance industry is well developed but is highly concentrated.** While there are 16 long-term insurers and 12 short-term insurers (including one reinsurer), the top 3 companies in each segment of the market accounted in 2004 for 85 percent and 86 percent respectively of total gross premiums written for long-term and short-term insurance. The total assets of long-term insurers amounted to N$13.3 billion in March 2004, corresponding to 39.2 percent of 2003 GDP. Adding the assets of short-term insurers raises total insurance assets to 42.3 percent of GDP.

99. **Pension funds and insurance companies invest extensively in overseas assets.** These are placed mostly in South Africa, because of the close economic links between South Africa and Namibia and the existence of the CMA that eliminates currency risk. Investments in non-CMA countries are subject to the exchange control limits applied by the South African Reserve Bank. This is currently set at 15 percent of assets.

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[26] Total pension fund assets likely exceeded N$25 billion in March 2005, corresponding to 68 percent of 2004 GDP.

[27] Total GIPF net assets rose to N$19 billion in March 2005.

100. **Pension funds and insurance companies are subject to a minimum local investment requirement of 35 percent.** This can be satisfied by investing in domestic government bonds, bank deposits, securities of domestic companies and in shares of foreign companies that are dual-listed on the NSX. Since dual-listed companies qualify as a domestic investment, pension funds and insurance companies are still able to invest in fairly diverse assets and earn satisfactory rates of return.

101. **The Namibian National Reinsurance Corporation (Namib Re), the only registered reinsurer, is wholly owned by the government.** Namib Re has a market agreement with short term insurers under which it has the option to underwrite up to 20 percent of their treaty and facultative reinsurance. This market agreement is due for review in 2006.

102. **There are 29 registered asset managers that mainly provide services to pension funds and insurance companies.** Asset managers include both affiliates of South African entities and some local groups. Because of the small size of the local market, asset managers undertake balanced mandates. There are no managers that specialize in particular segments of the financial market. There are also firms that specialize in monitoring the performance of asset managers and helping pension funds and other investors in selecting asset managers.

103. **Driven by money market portfolios and the tax free status, the unit trust industry has grown rapidly.** While there is no requirement for localization of investments in unit trust schemes, management companies generally observe the 35 percent domestic asset requirement in order to attract investments from institutional investors. Corporate investors also invest in money market unit trusts, mainly for tax reasons. There are eight registered unit trust management companies which have AUM of N$8 billion, N$7 billion in money market portfolios and the balance in equity and balanced portfolios. Management companies controlled by two domestic commercial banks have a 60 percent market share of AUM.

104. **There appear to be limited leasing and factoring activities.** Most are carried out by retailers or auto companies. There are few specialized or independent factoring and leasing companies, and there is no specific consumer credit legislation that governs these activities.

105. **NAMFISA was created in 2001 to regulate the NBFI sector.** This includes pension funds, insurance companies, assets managers, capital markets, and microlenders. Prior to 2001, the responsibility for regulating and supervising the sector rested with the MOF. While laws regulating short and long-term insurance were updated in 1998, legislation governing pensions, unit trusts and securities markets have not been updated for many years. However, these laws are appropriate in the short-term although changes are necessary to close gaps and take into account developments in financial markets. In particular, there are no laws covering asset managers, money market unit trusts, unit-linked insurance policies and products.

106. **Several types of institutions are active in microlending and cater to different groups of people with limited access to services from the commercial banks.** These include term and cash lenders, SACCOs, SCAs, and stokvels. However, the total size of

outstanding loans is still small (only 0.9 percent of GDP). The annual volume of disbursed loans is slightly greater (at 1.1 percent of GDP) because a big part of the business consists of loans repayable monthly. Term and cash lenders are required to register with NAMFISA. They are allowed to apply financial charges up to a usury ceiling of twice the prime rate (currently 11.75 percent).[28] SACCOs and SCAs are registered with the Department of Cooperative Development of the Ministry of Agriculture and are allowed to take deposits from, and make loans to, their members. Stokvels are highly informal and are not required to register as long as they have fewer than 20 members and less than N$500 thousand in deposits. There is no data on these, nor on those which exceed the legal requirements and have yet to be identified.

107. **The Namibia Housing Action Group (NHAG), an NGO, is active in low-cost housing and helps shack dwellers build and move into houses.** NHAG cooperates with the SDFN[29] and the Twahangana Fund.[30] It prepares plans for the layout of blocks of land, the installation of basic services, and the construction of low-cost houses. The Twahangana Fund allocates funds obtained from international donors and government sources (the Ministry of Regional, Local Government and Housing as well as the Building Together Loans Fund of municipalities around the country) to local groups. These funds are supplemented by member savings.

108. **Household and SME finance providers are supported by two credit reference bureaus.** ITC is mainly used by the banks and has information on both individuals and companies. Compuscan, on the other hand, caters to the microlending industry. Both bureaus have headquarters in South Africa and have a combined database for Namibia, South Africa, Botswana, Zimbabwe, and Lesotho. The credit bureaus are computerized, compile only negative information on users of credit services, and claim that they correct mistakes with little delay.

D. Financial Markets

109. **Money and foreign exchange markets in Namibia are essentially extensions of the South African markets.** As most banks manage their liquidity with banks in South Africa (especially their parent banks), there is little interbank trading in Namibia. Banks

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[28] The usury ceiling for institutions that are not registered with NAMFISA is equal to 1.6 times the prime rate.

[29] The SDFN was established in 1998. It is a network of housing saving schemes that aims to improve the living conditions of low income groups living in shacks. There are 312 savings groups under SDFN mostly from urban areas throughout the country. Each group manages its own project and once they start saving, they can apply for a loan from the revolving fund that provides micro enterprise loans, housing and service loans. Housing loans account for the major part of the total loans disbursed.

[30] The Twahangana Fund, which is associated with the SDFN, is presented as a development fund but comprises groups that operate like stokvels. It has been successful in mobilizing member savings and allocating housing loans to local groups.

usually have access to liquidity through their parent banks, while stringent position limits imposed by their parent banks have also served as an impediment for active local interbank transactions. However, transactions are picking up, in tandem with development in the domestic payment and clearing systems. Similarly, there is a limited amount of local foreign exchange trading, partly owing to the limited demand for such transactions.[31] Nevertheless, the volume has been growing steadily since 2000 reflecting declining dependence on parent banks.

110. **There is a relatively well-developed government securities market with a reasonably active secondary trading in Treasury-Bills.** Government and the BON have taken steps to create liquid and deep government securities market, including (i) issuance of longer term bonds, and (ii) consolidating small issues and introducing switch auctions. The outstanding amount of Namibian government securities has steadily increased, reaching N$10.5 billion in September 2005 (28 percent of GDP), shared equally between treasury bills and bonds, which are called Internal Registered Stock (IRS). Treasury-Bills are issued on a discount basis, with maturities of 91, 182, and 365 days, while IRS go from 1 year to 20 years. The primary market is functioning well with participation from banks, NBFIs, and a few individuals, although most individuals bid through financial institutions. All Treasury-Bills are held in the book entry system administered by the BON. Issuance of IRS is done on delivery versus payment. The secondary market transaction are active for treasury bills while IRS are generally held to maturity.[32] In an effort to facilitate and improve pricing, the government has benchmarked its IRS against the most liquid South African government benchmark bonds. In addition, in early December 2005, Fitch Ratings has assigned Namibia a sovereign long-term foreign currency rating of BBB.

111. **The NSX plays a relatively small role in the country's economy.** It lists nine local companies with a market capitalization of only 5.9 percent of GDP in 2004 and a turnover ratio of 1.9 percent.[33] The value of traded local equities was 0.3 percent of GDP. The exchange also lists several dual listed, mostly South African, companies with operations in Namibia. Trading of these dual listed issues is much greater, but still only corresponded to

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[31] Limited demand for foreign exchange transactions are due to the following factors: (i) one to one convertibility between Namibian dollar and South African rand is ensured without any fee under the CMA arrangement; (ii) over 80 percent of Namibia's imports are invoiced in rand which is also a legal tender in Namibia so there are no foreign exchange transactions resulting from this side of the trade balance; (iii) the diamond export proceeds are received centrally from De Beers in South Africa and are paid in rand, much of them initially being reinvested in rand in South African banks; (iv) foreign exchange proceeds from other exports that are received in non-rand currencies must be converted within 90 days by the exporters through a foreign exchange transaction, and in many cases, the local commercial bank offload the resulting foreign exchange position through South African banks and receive rand; and (v) residents are not allowed to transact business in foreign currencies but may use the rand.

[32] The average monthly turnover is around 40 percent for the treasury bills while it is only around 8 percent for IRS.

[33] Based on data from NAMFISA. Data from NSX show local market capitalization of 3.5 percent of GDP in 2004 and a turnover ratio of 9 percent. Trading value data are from NSX.

7.4 percent of GDP in 2004. There is also a small number of listed corporate bonds. The exchange has reasonably modern rules on listing and an efficient infrastructure for trading and settlement but because of its small size it operates with minimum nonnegotiable commissions. These are higher than commissions charged by brokers of the Johannesburg Securities Exchange, although the difference is small. The economic contribution of the NSX has remained small because of the lack of interest by most local companies to list on the exchange.

E. Payment Systems

112. **Namibia introduced its RTGS, the NISS, in June 2002.** At first, the system only covered high value transactions, with retail transactions being handled from mid-2004. The BON requires that all types of domestic transactions be settled in Namibia through the NISS, specifically, (i) high value single transactions (interbank); and (ii) retail transactions through the electronic clearing house (Namclear). The former represents roughly 70 percent of all transactions by value. The latter consists of retail clearing (8 percent) and check clearing (22 percent) via electronic funds Transfer system. Credit and debit card clearing is still settled in South Africa via correspondent arrangements between Namibian banks and their South African counterparts. This will be taken over by Namclear in March 2006. However, credit cards represent a very small part of the transactions.

113. **A framework for the effective oversight of the payment systems is currently being developed.** The Payment System Management Act, 2003, provides the legal basis on which the BON will oversee Namibian payment systems to ensure their financial and technical integrity. This includes their overall robustness and capacity to deal with shocks as well as their efficiency and cost effectiveness. The BON will establish standards and rules, including those on disclosure, and will also carry out monitoring, analysis and enforcement. Under this BON oversight umbrella, the Payments Association of Namibia, a statutory payment system management body, is responsible for the technical management and regulation of national payment systems.

F. Systemic Liquidity and Crisis Management

114. **The primary objective of monetary policy is to maintain the fixed peg with the rand as required by the CMA arrangement.** Operationally, the BON targets an adequate amount of foreign reserves to cover currency in circulation. The BON's two main policy rates are the bank rate which applies to overdraft facilities that are available to commercial banks and the call rate on bank's call (deposit) accounts with the BON. The reserve requirement is set at one percent of a bank's total liabilities and is not remunerated. Banks are required to hold 10 percent of their liability base in liquid assets. Currently, there is no open market operation, although the BON does repo transactions with commercial banks to provide intraday and overnight liquidity for settlement purposes. This facility is available for intraday liquidity without any charge while the bank rate is applied for overnight borrowing.

115. **The BON has the legal authority under the Banking Insitutions Act (BIA) to take an appropriate range of remedial actions against banks.** Its powers range from requiring corrective actions such as restricting the extension of credit or the payment of dividends, and removing directors and officers from office, to assuming control of entire banking activities or appointing a person to conduct the business of the BI.[34] The BON can also apply to the courts to wind up a bank, although at present it has no power to ensure that the liquidator is someone of whom it approves. Planned amendments to the BIA will, however, remedy this.

G. Legal, Judicial, and Accounting Frameworks

116. **Creditor rights are reasonably well established.** There is a general consensus among market participants and the legal profession that the legal system is noncorrupt, fair and impartial, as well as being reasonably rapid in processing straight forward cases. There are some 350 lawyers and about five law firms that carry out significant commercial business. Banks cannot realize collateral without going to court, but in uncontested cases (the vast majority) banks can obtain and auction off property within a matter of months. Contested cases (whether involving collateral realization or other matters) can take a number of years.

117. **Current Namibian GAAPs are closely linked to South African GAAPs, which have been progressively modified during the last five years to comply with IFRS.** The accountants' professional organization, the Institute of Chartered Accountants (ICA), is responsible for setting accounting standards in Namibia. According to a decision made by the ICA, IFRS will be applicable to Namibian companies from January 1, 2006. According to the Companies Act, all registered companies have to appoint external auditors. There are currently about 100 chartered accountants active in Namibia, and the major international accounting firms are represented. Accounting firms face a shortage of accounting professionals in Namibia, which is addressed through in-house training.

[34] In its procedure manual for supervisory actions, the BON defines the way it intends to exercise its powers (both formal and informal) and to deal with banks' weaknesses.

Stress Testing Methodology and Results

Sensitivity analysis

118. **Credit risk.** The system as a whole is resilient to a 100 percent increase in overall NPLs.[35] However, with mortgages comprising about 40 percent of total loans, the banking system is vulnerable to a shock that affects households' ability to service mortgages. One bank's CAR falls below the regulatory CAR of 10 percent if 10 percent of mortgages become nonperforming while three of the four banks are vulnerable if 30 percent become nonperforming. In addition, the sector is moderately exposed to large borrowers. For most banks, simultaneous defaults of their top five large exposures would bring CAR below 10 percent. However, both shocks are extreme and have no historical precedent.

119. **Liquidity risk.** Given the high concentration of large institutional depositors, the sector's resilience to a large withdrawal of deposits from commercial banks was tested. The result suggests that the withdrawal of the largest five depositors would bring the liquidity ratio of the sector down from 11.1 percent to–16.7 percent, much lower than the required level of 10 percent.[36] All banks are sensitive to such a shock.

120. **Interest rate risk.** Based on a repricing model,[37] the FSAP team simulated an interest rate shock that reduces net interest income. The banking sector is robust to a downward parallel shift in the yield curve of 5 percentage points. The sector as a whole would see a reduction in the CAR of almost 3 percent with one bank experiencing a fall in its CAR of 4.7 percent. A decline in interest income from government securities was also tested. The impact of a 50 percent cut in such income is limited due to small government securities holdings.

121. **Exchange rate risk.** Under the CMA, South Africa's exchange controls limit Namibian investment in non-CMA countries. As a result, Namibian banks' direct exposure to nonrand foreign exchange risk is negligible. A test that simulates a de-pegging between the rand and Namibian dollar is not possible. First, data required for such a test does not exist. Second, such an event would be so traumatic that economic relationships and assumptions embodied in the stress tests would be invalid.

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[35] The test assumes additional provisioning of 50 percent for all new NPLs, and 100 percent for old NPLs.

[36] Liquid assets to total deposits.

[37] The repricing model measures the effect of a change in interest rates on the future net interest income of banks (i.e., the cash flow gains/losses of a bank over a given period). The test was conducted for one year horizon taking into account of differences in cash flow timing with four maturity buckets.

Scenario analysis

122. **Macroeconomic scenarios.** Two extreme scenarios were tested.[38] The first one is similar to the rand crisis of 1998/99. In this scenario, the Namibian dollar depreciates 30 percent against the U.S. dollar, and domestic interest rates increase by 5 percent.[39] It is assumed that the high interest rate leads to a 30 percent increase in mortgage NPLs. The stress test results suggest that one bank is vulnerable to a shock in this scenario with its CAR falling below the minimum required CAR of 10 percent. The second scenario involves a sharp appreciation of the rand against the U.S. dollar. In this scenario, the Namibian dollar appreciates 25 percent, and domestic interest rates fall by 5 percent. The appreciation causes 30 percent of loans in the agriculture and fishing industries, important export sectors of the country, to become nonperforming. The results suggest that the banking system is vulnerable to this shock, with the CAR of three banks falling below 10 percent. However, in both cases, all banks remain solvent.

[38] The scenarios were designed in consultation with the BON.

[39] An interest rate decline of 5 percentage points is considered an extreme case given that between 1992–2005, the largest fall in interest rates in one year was about 3.3 percent.

Table 5. Selected Financial and Economic Indicators, 2000-04

	2000	2001	2002	2003	2004
	(Annual percentage change, unless otherwise noted)				
National income and prices					
GDP at constant 1995 prices	3.5	2.4	6.7	3.5	6.0
GDP deflator	10.7	14.1	11.4	-0.6	2.9
GDP at current market prices (N$ million)	23,690	27,686	32,907	33,841	36,905
GDP per capita (U.S. dollars)	1,857	1,698	1,603	2,225	2,764
Consumer price index (period average)	9.3	9.3	11.3	7.2	4.1
Consumer price index (end-of-period)	10.8	8.3	12.5	2.6	4.3
External sector					
Exports (U.S. dollars)	10.7	-13.7	-6.1	16.3	53.8
Imports (U.S. dollars)	-5.9	1.8	-4.6	33.7	30.9
Export volume	-0.9	-4.5	-8.0	18.3	22.2
Import volume	-5.2	4.0	20.4	5.2	6.0
Terms of trade	12.5	-7.8	28.8	-22.6	-7.7
Real effective exchange rate	2.9	-1.6	-5.1	12.6	4.3
Central government finance 1/					
Revenue and grants	13.6	9.1	16.8	-6.8	20.6
Expenditure and net lending	10.7	19.7	12.8	6.6	1.3
Money and credit 2/					
Credit to the private sector	17.0	16.3	20.2	12.4	19.4
Broad money	13.0	4.5	6.9	9.6	16.2
	(In percent of GDP, unless otherwise noted)				
Investment and savings					
Gross investment	19.5	23.4	19.7	29.8	25.5
Public	6.1	8.7	6.2	7.0	7.2
Private	13.4	14.7	13.5	22.8	18.3
Gross domestic savings	15.5	17.8	14.9	23.3	22.9
Gross national savings	29.2	26.7	25.2	34.8	35.7
Public	3.6	1.5	2.4	-0.7	2.1
Private	25.6	25.1	22.7	35.5	33.6
Central government finance 1/					
Revenue and grants	33.3	30.9	31.6	28.2	31.3
Of which: SACU receipts	11.7	9.1	7.8	8.8	11.2
Expenditure and net lending	34.7	35.4	34.9	35.6	33.3
Of which: personnel expenditure	15.1	14.9	14.2	14.8	14.4
capital expenditure and net lending	5.3	5.3	6.3	5.6	5.3
Primary balance (- deficit)	0.7	-2.4	-0.8	-5.0	0.7
Overall government deficit including grants	-1.4	-4.5	-3.3	-7.5	-2.0
Public and publicly guaranteed debt outstanding/GDP	34.1	39.0	33.7	39.4	39.9
Public debt outstanding/GDP	23.1	25.9	23.9	29.5	33.4
External sector					
Current account balance					
Including official transfers	9.7	3.2	5.4	5.0	10.2
Excluding official transfers	-2.6	-7.1	-3.0	-4.8	-1.0
Gross official reserves					
In millions of U.S. dollars	268.5	224.0	336.2	318.9	295.2
In months of imports of goods and services	2.0	1.7	2.7	2.0	1.5
External debt/GDP (in percent)	23.3	18.5	29.6	24.7	…
Exchange rate (Namibia dollar/U.S. dollar, end-of-period)	7.6	12.1	8.6	6.6	5.6
Exchange rate (Namibia dollar/U.S. dollar, period average)	6.9	8.6	10.5	7.6	6.4

Sources: Namibian authorities; and Fund staff estimates.
1/ Figures are for fiscal year, which begins April 1.
2/ Data for 2003 onwards reflect new monetary data.

Table 6. Financial System Structure, 2000–05

	2000	2001	2002	2003	2004	Jun-05
	(Number)					
Commercial banks	...	5	5	4	4	4
Private commercial	...	2	2	1	1	1
State-owned	...	0	0	0	0	0
Foreign-owned subsidiaries	...	3	3	3	3	3
Specialized banks 1/	...	...	...	4	4	4
Pension funds	...	...	...	482	513	530
Insurance companies (Long term)	8	10	11	12	14	16
Insurance companies (Short term) 2/	8	10	9	13	14	12
Term lenders and cash lenders 3/	...	...	34	74	105	170
SACCOs	...	...	...	...	19	...
	(Assets, billions of Namibian dollars)					
Commercial banks	...	13.7	17.8	20.0	23.4	25.7
Private commercial	...	3.7	5.7	4.3	5.2	6.1
State-owned	...	...	...	...	...	...
Foreign-owned subsidiaries	...	10.0	12.1	15.7	18.2	19.6
Specialized banks	...	...	...	...	2.5	...
Pension funds 4/	...	...	16.3	15.8	21.1	...
Insurance companies (Long term)	4.8	6.3	9.3	10.3	13.3	...
Insurance companies (Short term)	0.6	0.8	1.0	1.0	1.0	...
Term lenders and cash lenders 5/	...	...	...	...	0.3	...
SACCOs 6/	...	...	...	...	0.0003	...
SCAs	...	...	...	...	0.0004	...
	(Assets, in percent of GDP)					
Commercial banks	...	49.5	54.1	59.1	63.4	64.9
Private commercial	...	13.4	17.3	12.7	14.1	15.4
State-owned	...	...	...	...	...	...
Foreign-owned subsidiaries		36.1	36.8	46.4	49.3	49.5
Specialized banks	...	...	...	...	6.8	...
Pension funds			49.6	46.7	57.2	...
Insurance companies (Long term)	20.4	22.7	28.1	30.5	36.0	...
Insurance companies (Short term)	2.4	2.9	2.9	2.9	2.7	...
Term lenders	...	...	...	...	0.8	...
Cash lenders	...	...	...	...	0.1	...
SACCOs	...	...	...	...	0.001	...
SCAs	...	...	...	...	0.001	...
Memorandum items:	(In billions of Namibian dollars)					
Commercial Banks' Deposits		9.9	12.7	14.3	19.1	21.5
Private commercial	...	3.0	4.7	3.5	4.4	5.2
State-owned	...	...	...	...	...	...
Foreign-owned subsidiaries	...	6.9	7.9	10.7	14.7	16.3

Sources: Bank of Namibia, NAMFISA, and Staff estimates.

1/ Includes Agribank, Development Bank of Namibia, the NHE and Nampost Savings Bank. For Nampost, the size of deposits was used as a proxy for asset size.
2/ Includes primary insurers and reinsurers.
3/ Lenders that are registered with NAMFISA.
4/ Insured funds' figures are available only from 2003, and are included in insurance companies' data. Their size is 5.6 and 6.4 percent of GDP for 2003 and 2004, respectively.
5/ Staff estimate using ECI Africa study and data from NAMFISA.
6/ Figures show total savings of SACCOs.

Table 7. Cross-Country Comparison of Selected Indicators

	Namibia	South Africa	Botswana	Lesotho	Swaziland	Kenya	Tanzania	Mozambique
Size of financial intermediaries 1/								
Domestic credit to private sector (% of GDP) 1/	52.8	83.4	19.7	6.3	16.2	23.2	9.0	2.3
M2/GDP	36.5	60.4	29.2	26.3	19.3	38.0	22.1	27.0
Banking industry 2/								
Number of banks	4	20	4	3	4	23	10	7
Assets (% of GDP)	63.4	108.8	30.6	50.2	24.1	34.6	16.8	36.9
Capital Adequacy Ratio	15.4	13.3	20.6	...	...	16.5	21	18.7
NPLs to total loans	2.4	1.8	2.8	...	...	22.9	4.5	6.4
Return on Assets	2.0	1.2	4.0	...	...	2.1	2.1	1.4
Return on Equity	21.6	16.2	36.0	...	...	22.7	20.7	18.7
Capital and insurance markets 3/								
Number of companies listed	35	403	18	...	6	47	6	...
Stock market capitalization to GDP	1305.0	214.1	29.4	...	9.3	24.9	6.2	...
Stocks traded, turnover ratio (%)	0.4	45.0	2.1	...	0.0	8.0	2.5	...
Insurance premiums to GDP	7.61	14.38	3.75	...	...	2.81	...	...
Enforcing contracts								
Procedures (number)	31	26	26	49.0	...	25	21.0	38.0
Time (days)	270	277	154	285.0	...	360	242.0	580.0
Cost (% of debt)	28.3	11.5	24.8	23.9	...	41.3	35.3	16.0
Credit markets								
Public registry coverage (% adults)	0.0	0.0	0.0	0.0	...	0.0	0.0	0.8
Private bureau coverage (% adults)	35.2	63.4	30.8	0.0	...	0.1	0.0	0.0
Closing a business								
Time (years)	1	2	2.2	2.6	...	4.5	3	5
Cost (% of estate)	14	18	14	8	...	22	22	9
Recovery rate (cents on the dollar)	45.4	34	54.4	35.9	...	15	22.4	13.3
Starting a business								
Procedures (number)	10	9	11	9	...	13	13	14
Time (days)	95	38	108	92	...	54	35	153
Cost (% of income per capita)	18.8	8.6	10.9	56.1	...	48.2	161.3	95
Development indicators								
GNI per capita (US$)	2370	3630	4340	740	1660	460	330	250
Agriculture, value added (% of GDP)	10.8	3.8	2.4	16.2	11.9	16.4 ..	..	
Improved water source (% of population with access)	80	87	95	76	52	62	73	42
Percent rural population	67.0	42.6	48.0	81.9	76.3	59.5	63.5	63.2

Sources: World Development Indicators, World Bank's Doing Business databases, Swiss Re, and NAMFISA. Data are for 2004 unless otherwise noted.

1/ Data for Namibia and Swaziland are from 2003.
2/ End-2004 data except Kenya (June 2004) and Tanzania (end-2003).
3/ Data for Namibian capital markets is from NAMFISA

Table 8. Financial Soundness Indicators for Banks, 2001– 2005
(In percent, unless otherwise indicated)

	2001	2002	2003	2004	2005
Capital adequacy					
Capital to assets	8.7	7.5	8.3	8.8	7.8
Regulatory capital to risk-weighted assets	15.5	14.1	14.8	15.4	14.6
Regulatory tier I capital to risk-weighted assets	12.4	11.0	12.2	12.7	11.2
Nonperforming loans net of provisions to capital	8.3	11.1	11.8	20.2	20.0
Asset quality					
Large exposure to capital	146.0	179.0	186.0	183.9	182.8
Nonperforming loans to total gross loans	3.4	3.5	3.9	2.4	2.0
Sectoral distribution of loans to total loans					
Agriculture	9.0	8.6	5.5	3.1	3.9
Mining	0.7	1.5	2.6	2.0	2.8
Manufacturing	5.4	5.4	3.8	2.3	1.8
Construction	3.9	4.5	4.1	5.5	1.5
Electricity and water	0.3	4.4	3.4	0.7	0.8
Trade and accommodation	4.8	5.2	2.6	3.7	4.1
Transport and communications	3.7	3.6	4.6	2.3	3.1
Finance, real estate, and business services	15.5	11.1	9.6	11.4	13.2
Other services (including government)	11.6	7.0	8.6	8.2	6.8
Individuals	44.1	47.1	47.1	51.2	54.9
Other	1.1	1.8	8.3	9.4	7.1
Earnings and profitability1/					
Trading income to total income	10.6	11.5	10.9	6.7	5.0
Return on assets	2.9	3.3	2.8	2.0	2.8
Return on equity	29.7	32.6	28.0	21.6	27.8
Net Interest income to gross income	49.0	53.0	51.3	57.0	52.3
Noninterest expenses to gross income	51.3	49.3	58.1	69.2	44.1
Spread between reference lending and deposit rates	7.3	6.2	6.0	4.4	4.4
Personnel expenses to noninterest expenses	50.0	48.4	43.8	47.1	61.9
Liquidity					
Spread between highest and lowest interbank rate	...	4.0	0.8	0.2	5.3
Liquid assets to total assets	9.6	9.2	11.0	10.4	9.5
Liquid assets to short-term liabilities	15.6	15.7	19.3	17.6	16.6
Customer deposits to total (non-interbank) loans	88.0	84.0	87.0	87.1	94.6
Exposure to foreign exchange risk					
Net open position in foreign exchange to capital	0.2	0.1	0.0	0.5	1.4
Foreign currency-denominated loans to total loans	6.0	5.0	3.0	1.9	0.7
Foreign currency-denominated liabilities to total liabil	5.1	5.2	4.5	2.0	1.2

Sources: Bank of Namibia; and Fund staff estimates.

1/ Figures are average of the period. 2005 figures are for the first half of the year.

Table 9. Balance Sheet and Income Statement of the Banking Sector, 2001–05
(In percent)

	Dec-01	Dec-02	Dec-03	Dec-04	June-05
Assets	*In percent of total assets*				
Financial Assets	97.9	98.0	98.5	98.7	98.5
Cash, balance with BON, and deposits	3.2	2.8	3.2	4.6	5.8
Gross loans and advances	85.5	87.3	84.5	82.8	76.9
Net loans and advances	82.6	84.4	81.7	80.2	74.5
Total provisions and interest in suspense	2.9	2.9	2.8	2.5	2.4
Debt securities	8.3	9.4	8.7	9.3	13.2
Nonfinancial Assets	2.1	2.0	1.5	1.3	1.5
Other assets	3.8	1.4	4.9	4.5	5.0
Liabilities	*In percentage of total liabilities and capital*				
Deposits	82.9	84.3	83.9	83.0	84.0
Customer deposits	71.6	71.3	71.3	71.9	76.0
Borrowings	0.6	0.7	0.3	1.4	2.0
Intragroup funding	5.9	8.9	8.3	8.1	6.1
Interbank funding	1.6	1.2	1.5	2.2	3.2
Debt securities	1.1	0.9	0.8	1.0	1.0
Other liabilities	5.8	5.8	3.5	3.7	3.1
Capital and Reserves	9.6	8.4	11.5	11.0	10.0
Income structure	*In percent of total income (annual figure)*				
Net interest income	53.9	51.8	53.1	51.0	48.2
Charges, Fees, and Commissions	25.9	27.5	28.6	32.7	32.4
Other income	20.2	20.8	18.3	16.3	19.4
Overhead costs	49.7	48.8	53.0	61.8	52.6
Of which personnel costs	25.6	24.0	24.9	29.8	26.9
Other costs	24.1	24.8	28.1	32.1	25.7
Tax	17.4	14.8	13.0	11.1	12.8
Net income after tax (NIAT)	30.9	33.1	29.3	23.0	28.8

Source: Bank of Namibia

Table 10. Pension Funds Statement of Funds and Net Assets
(In millions of Namibia dollars)

	2002	2003	2004
Funds			
Accumulated funds	15,149.4	14,698.9	19,360.9
Pension	14,928.0	14,469.4	18,943.9
Provident	103.7	109.3	222.7
Retirement annuity	117.7	120.1	30.0
Preservation	0.0	0.0	164.3
Reserves	899.4	736.0	1,300.7
Total funds and reserves	16,048.8	15,434.9	20,661.5
Net assets			
Fixed assets	36.0	38.7	50.3
Investments	15,667.5	15,289.0	20,399.5
Loans	92.3	109.5	125.8
Current assets	522.3	357.8	535.9
Total assets	16,318.1	15,795.0	21,111.6
Liabilities	269.3	360.1	450.0
Long-term liabilities	0.0	0.0	0.0
Current liabilities	269.3	360.1	450.0
Total net assets	16,048.8	15,434.9	20,661.5

Source: NAMFISA.

Table 11. Pension Funds Revenue Account
(In millions of Namibia dollars)

	2002	2003	2004
Contributions received	1,039.0	1,132.6	1,325.5
Members' contributions	326.8	364.9	442.7
Normal	326.5	364.7	425.8
Additional voluntary	0.3	0.2	16.9
Employer's contributions	712.1	767.6	882.8
For retirement funding	683.6	733.0	783.3
For costs	28.5	34.7	99.5
Buyback of past service	0.0	-0.1	0.0
Benefit fund	0.1	0.2	0.0
Transfers received	234.6	30.2	57.2
Unclaimed benefits forfeited	0.2	0.6	0.3
Waiver from insurance	0.0	0.0	0.0
Other income	3.8	1.1	1.3
Reinsurance recoveries	69.6	72.3	81.1
Investment income	1,087.0	1,180.1	1,509.5
Less: Administration expenses	181.2	220.2	268.5
Revenue net of expenses	2,253.1	2,196.6	2,706.5
Adjustment to fair value of assets	1,375.3	-2,019.2	2,882.5
Accumulated funds- beginning	12,687.1	15,235.2	14,783.0
Accumulated funds- transferred to fund	0.4	13.0	152.9
Accumulated funds- before benefits	16,315.9	15,425.6	20,524.8
Less: Benefits and transfers out	865.6	799.1	1,042.9
Transfers to/from reserve accounts	-203.1	156.6	199.4
Accumulated funds-end	15,247.2	14,783.0	19,681.3

Source: NAMFISA
1/ Figures are for fiscal year ending in March every year.

Table 12. Long Term Insurer's Consolidated Financial Statements 1/
(In millions of Namibia dollars)

	2001	2002	2003	2004
Income				
Net premium	1,693.0	1,987.8	1,833.9	1,969.4
Investment income	875.6	108.7	879.4	351.7
Other income	0.1	6.7	1.1	3.9
Total Income	2,568.7	2,103.3	2,714.4	2,325.0
Expenditure				
Individual policy benefit	647.8	1,045.0	900.0	1,054.7
Group policy benefit	230.0	767.6	385.8	402.7
Reinsurance outflow	44.1	88.8	75.4	71.5
Management expenses	55.3	101.8	28.3	85.9
Commission	88.4	163.1	144.4	170.1
Total Expenditure	1,065.7	2,166.3	1,533.9	1,722.0
Total Assets	6,188.2	9,255.6	10,307.0	13,274.7
Policy liabilities	5,067.0	7,705.4	8,697.9	6,948.3
Total liabilities	5,609.7	8,531.6	9,091.1	11,701.8

Source: NAMFISA
1/ Figures are for fiscal year ending in March every year.

Table 13. Selected Indicators for the Insurance and Pension Sector 1/
(In percent)

	2001	2002	2003	2004	2005
Pension Funds					
i. All pension funds					
Asset growth	...	0.3	-3.8	33.9	...
Benefits to contributions	...	60.7	67.9	74.4	...
Cost					
Administrative expense to average net assets	...	1.13	1.40	1.48	...
Administrative expense to contribution	...	17.4	19.4	20.2	...
Investment performance					
Total investment income to average net assets	...	15.4	-5.3	24.3	...
ii. GIPF					
Asset growth	12.1	20.7	-5.6	35.1	26.5
Benefits to contributions	42.9	74.0	53.1	68.0	73.0
Cost					
Administrative expense to average net assets	0.21	0.24	0.32	0.35	0.30
Asset management fees to average net assets	0.49	0.46	0.44	0.47	0.44
Administrative expense to contributions	2.9	3.7	4.9	5.4	5.7
Asset management fees to contributions	7.0	7.1	6.6	7.2	8.3
Investment performance					
Total investment income to average total assets	8.1	17.0	-8.0	21.9	21.6
Life Insurance					
Asset growth	28.1	49.6	11.4	28.8	...
Benefits to net premiums	51.9	91.2	70.1	74.0	...
Cost					
Management expense to average net assets	1.0	1.3	0.3	0.7	...
Commission to average net assets	1.6	2.1	1.5	1.4	...
Management expense to net premiums	3.3	5.1	1.5	4.4	...
Commission to average net premiums	5.2	8.2	7.9	8.6	...
Investment performance					
Investment income to average total assets	15.9	1.4	9.0	3.0	...

Sources: NAMFISA, GIPF and Staff estimates.
1/ Figures are for fiscal year ending in March every year.

Table 14. Activity and Turnover in the Namibia Stock Exchange, 2000–04
(In billion of Namibia dollars)

	2000	2001	2002	2003	2004
Local market					
Market capitalization	4.0	2.1	1.8	1.6	2.2
(In percent of GDP)	17.0	7.4	5.3	4.9	5.9
Turnover ratio	4.6	6.0	1.5	0.7	1.9
Index (end year)	146	80	57	52	62
Overall market					
Market capitalization	301.1	363.1	513.0	347.4	481.6
(In percent of GDP)	1,271.0	1,311.7	1,559.0	1,026.5	1,304.9
Turnover ratio	0.92	0.55	0.35	0.54	0.4
Index (end year)	263	314	393	263	365

Sources: NAMFISA and BON.