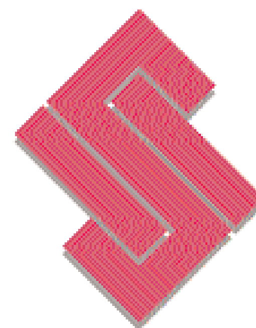
BANK OF NAMIBIA
RESEARCH DEPARTMENT

P O Box 2882, Windhoek, Namibia
Tel: +264-61-283 5111
Fax: +264-61-283 5231
E-mail: research@bon.com.na



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THE STRUCTURE AND NATURE OF SAVINGS IN NAMIBIA

by

Ebson Uanguta, Emma Haiyambo
Gerson Kadhikwa, Simana Chimana

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Enquiries related to this ppublication should be directed to:
The Chief Economist and Head of Research Department
P O Box 2882
WINDHOEK
NAMIBIA

Tel: +264 61 283 5111
Fax: +264 61 2835231
e-mail: research@bon.com.na
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http://www.bon.com.na

ABSTRACT

The main purpose of this study is to assess the structure of savings in Namibia and to examine how these savings could be translated into domestic investment. The preliminary analysis from this study reveals that the contractual savings which consist of pension fund contributions and life insurance premiums dominate the structure of savings in Namibia and are estimated to be around 60 per cent of the total private domestic savings. This is followed by commercial banks savings, which account for about 38 percent of the total private domestic savings.

Unlike many developing countries, contractual saving has been relatively high in Namibia. The saving level shows that domestic financial intermediaries have been successful in mobilising savings. However, the high savings mobilised in the economy do not seem to have been utilised sufficiently for domestic investment, particularly for the unlisted activities.

Having analysed the structure of saving in Namibia, one is inclined to conclude that the country is in a better position to use its current savings to finance long-term investments. This is based on the premise that the economy has well developed contractual saving institutions such as life insurance and pension funds, which have long-term liabilities on their balance sheets. This is usually in contrast with commercial banks that have mainly short-term liabilities. An institution that has short-term liabilities is prone to facing the risk of unexpected run against their assets that could generate liquidity problems, and potentially trigger solvency problems. As a result, the investment and lending strategies of commercial banks differ and are more risk averse to uncollateralised long-term financing than those of contractual savings institutions.

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1. INTRODUCTION

Domestic saving is of critical importance for the achievement and maintenance of sustainable growth and development. This is particularly so for developing countries where domestic borrowing is financing an increasing share of public sector expenditures as external capital flows to the private sector continues to decline.

Namibia is a country faced by four main development objectives namely to revive and sustain economic growth, to create employment, to reduce inequalities in income distribution, and to reduce poverty. The recent low GDP growth average of 3 per cent per annum recorded during the first decade of independence is far less than the average 5 per cent projected under the National Development Plan and 7 percent envisaged in Vision 2030. This low growth is partly attributed to a low level of investment activities. The ratio of gross fixed capital formation to GDP is a very important indicator of future economic growth as it is generally accepted that higher investment contributes to higher economic growth by making resources available for expansion of current and future production.

There is abundant evidence that countries that achieved high rates of economic growth also experienced corresponding high rates of saving and investment. While raising saving is not a sufficient condition for achieving sustained growth, it does appear to be a necessary condition for higher sustained growth. The economic research of the past decades, both theoretical and applied, cites that the development problem and lack of economic growth, has often been shown to be conditioned by inadequate savings.

According to the Bank of Namibia (2002) savings have an important role to play in the Namibian economy. Empirical evidence confirmed the postulation that countries with higher savings rate experienced higher rates of investment and growth. However, in Namibia the situation seems to be different. For the past years the country has generated a substantial amount of savings from pension and life insurance funds that resulted in a high domestic saving, although investment and economic growth have performed sluggishly.

This makes the country to present a paradoxical scenario with a high saving rate that does not seem to translate into high level of investment and economic growth. The excess of saving over investment has been reflected in continuous surpluses on the current account (Shiimi and Kadhikwa, 1999). As a ratio of GDP, gross national saving averaged 25.3 percent during the post-independence (1990-2001) period. However, the investment to GDP ratio averaged 21.1 percent during the same period. While the saving ratio is among the highest in sub-Saharan Africa, it is still low when compared to rapidly developing Asian countries, such as Singapore and Malaysia, where the ratios have been in excess of 30 percent.

Given this strong relationship between saving and investment, the concern is why investment should be low in Namibia, while there is enough saving to finance investment activities. It is against this background that this paper is assessing the nature and structure of savings in Namibia, and thereby suggests possible appropriate policies aimed at enhancing and utilising these savings. Therefore, the objectives of this paper are as follows:

- Analyse the structure of savings in the Namibian economy and assess as to what type of savings would be appropriate for financing productive and efficient domestic investment in the Namibian economy;

- Examine and analyse how savings could be translated into productive investment. Further, explore whether there are saving instruments with less risk aversion properties that could be channelled into productive investment. If these instruments are found viable, the study will suggest ways and means to encourage them.

This study is arranged as follows: Chapter 2 focuses on the review of the asset structure and nature of Namibian savings and the institutions that are responsible for the mobilisation and management of savings. Chapter 3 deals with the Financial Institutions and Investment regulation. Chapter 4 gives a brief summary of constraints on domestic investment. Chapter 5 provides some possible strategies to be followed, while the final chapter deals with conclusions, recommendations, and policy implications.

2. THE ASSET TREND AND STRUCTURE OF SAVING S INSTITUTIONS

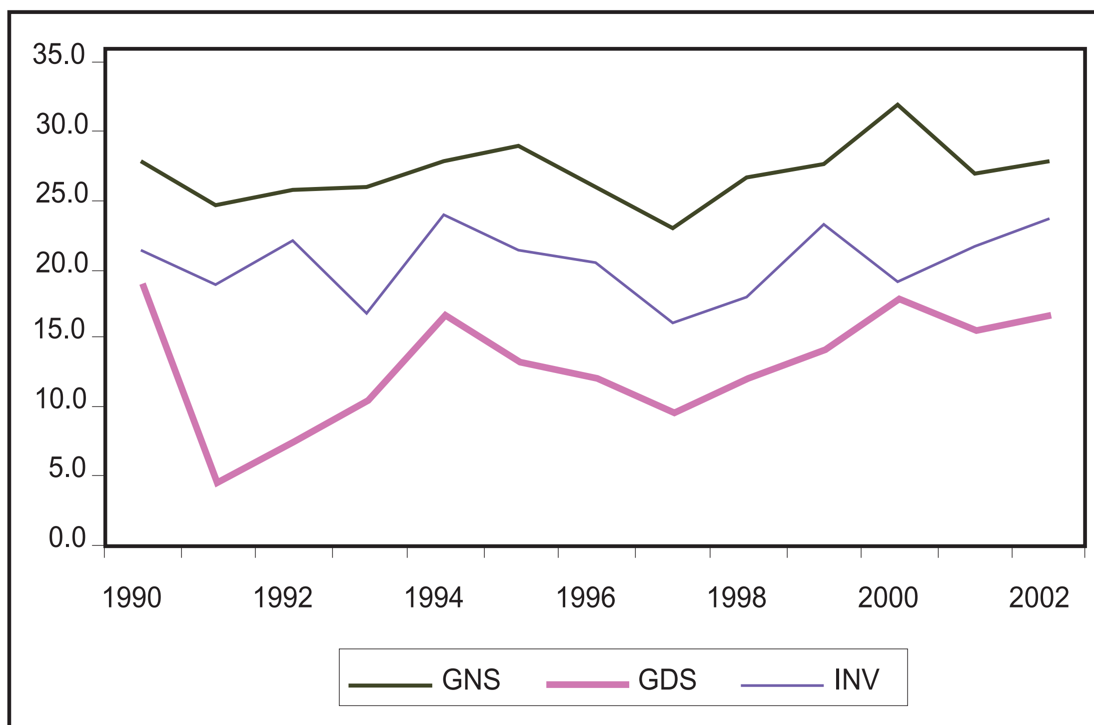
2.1 BACKGROUND

The Namibian economy is characterised by a robust and diversified financial sector and this makes it possible to mobilise savings from a large number of clients, largely in urban areas. A large part of domestic savings is considered to be linked to employment in certain sectors and is mobilised through life assurance policies and pension fund contributions. The key sectors include government, financial, real estate and business services, mining, and fishing. The section briefly discusses the aggregate savings and thereafter makes an in-depth analysis on the asset structure of various types of institutions that are responsible for savings mobilisation in the Namibian economy.

2.2 GROSS NATIONAL SAVING (GNS)

The Gross National Savings (GNS) is defined in the national income accounting context as net of gross national disposable income after accounting for consumption (GNDI-C). This definition is appropriate as it represents the national resources that feed in the monetary system as sources of funds to finance investment in the economy.

Chart 1 Savings and Investment (as percent of GDP)



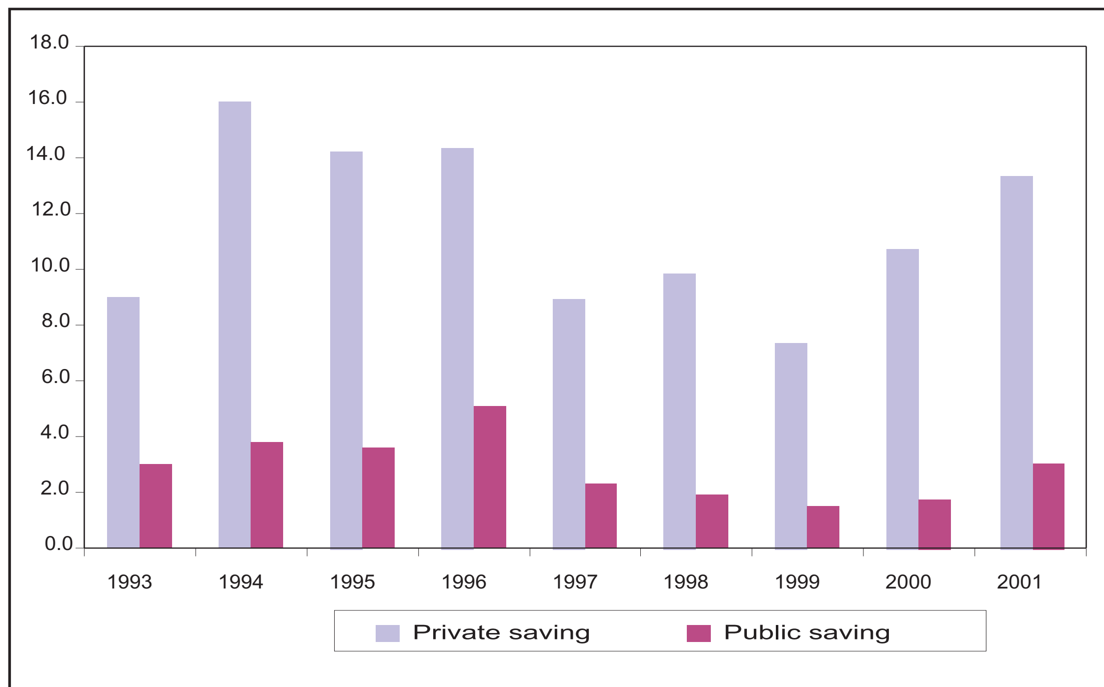
Source: World Bank and CBS

In the year 2000, investment as ratio of GDP was 19 percent, compared to savings, which were around 32 percent of GDP. The saving —investment gap improved slightly in 2001 whereby investment was at 22 percent of GDP and savings stood at 26 percent of GDP. The chart above confirms our earlier assertion that savings exceed investments that has been reflected in the current account surplus. On average, the saving / investment gap for the period 1990 - 2002 has been at around 5 percent.

2.2.1 Public and Private Savings

A public saving is defined as a saving by the general government, which is derived from the difference between government current revenue and expenditure. The government revenue consists mainly of tax receipts from the private sector, current non-tax revenue and current transfers received. The private saving in Namibia consists of personal and corporate saving. In the national accounts the two types of private savings are not separated, but it is generally known that personal savings are quite stable and growing consistently, while corporate savings exhibit a more volatile trend, but still represent a substantial source of private savings. A substantial amount of private saving is accounted for by contractual saving, which essentially involves individuals committing themselves to a series of payments such as premiums on insurance policies and contributions to pension funds. Low level of personal saving to a certain extent is attributed to absence of financial intermediaries in the rural areas where a large percentage of the population lives.

Chart 2 Private and Public Savings as a percent of GDP



Source: CBS

The private domestic saving, as a ratio of GDP, during the period under review has recorded an average of 12 percent. The highest share of 16 percent was recorded in 1994, while the lowest was 7.4 percent in 1999. On the other hand, public saving, as a share of GDP, averaged 4.1 percent. While the highest proportion of public saving was 5.1 percent in 1996 and the lowest was 1.5 percent in 1999.

2.3 REVIEW OF SAVINGS INSTITUTIONS

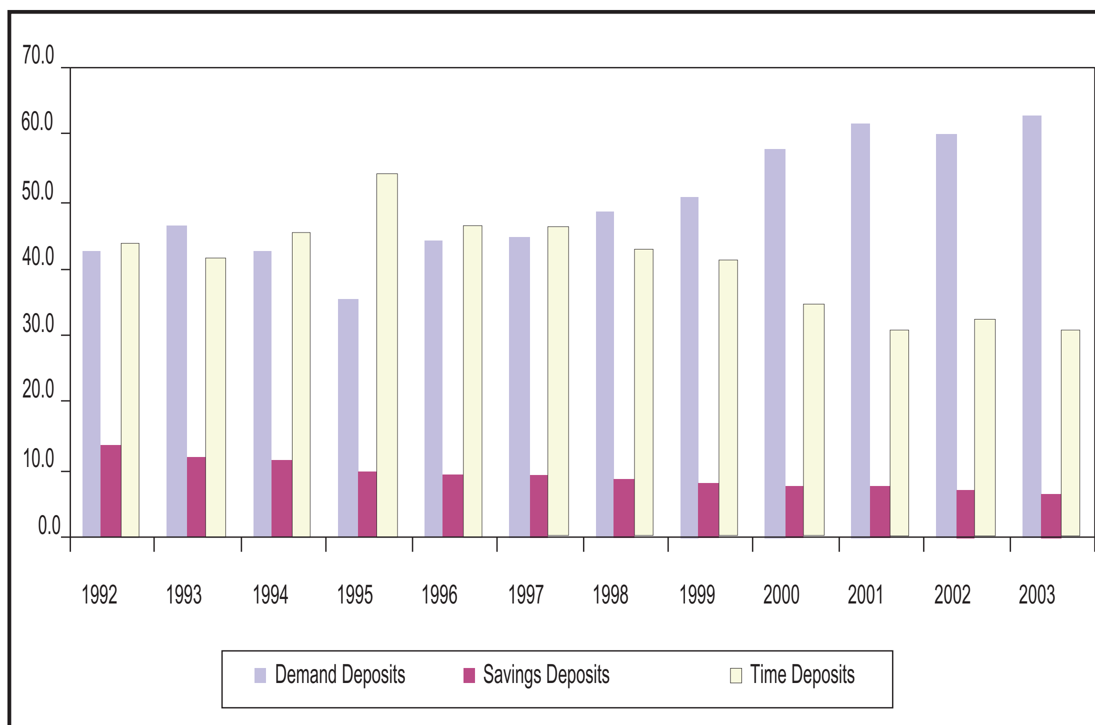
This section gives a brief account of the structure and assets position of the institutions responsible for savings mobilisation. This asset structure review gives an indication on the role various institutions play in savings mobilisation in the economy.

2.3.1 Commercial Banks

Commercial banks are one of the key savings institutions in Namibia. Deposits held at these banks increased at an average rate of 20.5 percent during the period 1993-1998, however, the growth rate slipped to a low of 12.9 percent during the period 1998-2000. The average growth rate for the period stood at 15.9 percent. This slide in the growth rate is partly attributable to the steep fall in the real rate of interest offered on the deposits. It is noteworthy that the real deposit rate recorded a steep decline from 4.6 percent in 1996 to 2.2 percent in 1999. Thereafter, it further declined and became negative in 2002.

This trend also resulted in a significant decline in the fixed and savings deposits over time. This implies that in order for the banks to sustain their deposit mobilisation efforts at levels achieved earlier, it becomes imperative that they should ensure a fair rate of return to the depositors.

Chart 3 Types of Commercial Banks Savings (as a percent of total banks savings)



Source: Bank of Namibia

Total savings held at commercial banks have been dominated by demand deposits for most of the period since 1998. Savings held at commercial banks between 1993 and 2002 grew by an average of 16 percent from N$2.5 billion to N$10.7 billion. The share of demand deposits has increased gradually from 43 percent in 1992 to 60.2 percent in 2002, while that of time and savings deposits declined from 44 percent to 32 percent and from 13.5 percent to 7.3 percent, respectively.

2.3.2 Long term Saving Industry

Namibia has a well-developed long term contractual saving industry. Some evidence can be seen from the discussion below on pension funds and insurance companies, which are regarded to be the key institutions responsible for the mobilisation of contractual savings. The development of contractual savings institutions is argued to have an indirect impact on the development of the domestic financial markets. Its presence can signal

to foreign investors a sound and stable domestic financial system. But, when a contractual saving is invested largely abroad, which appears to be the case in Namibia, the development of domestic financial system is not adequately stimulated. Total contractual savings as a share of total savings is estimated at 58 percent in 2001.

Table 1 Long term Savings[1] ratio to GDP (percent)

Countries	1990	1996	2001	2002
Netherlands	108.11	148.19	_	-
United Kingdom	86.90	141.72	_	-
South Africa	78.13	126.01	_	-
Namibia	_	53.0	84.0	76.0
Chile	29.28	50.61	_	-
Singapore	115.13	93.50	_	-

Source: Various sources

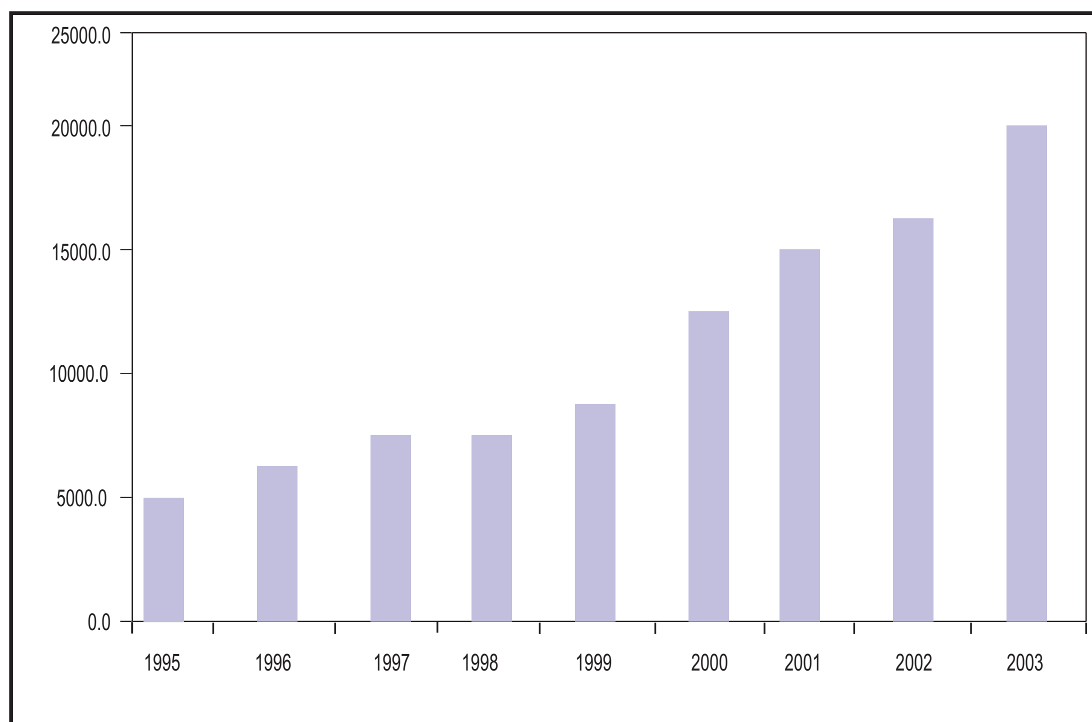
Namibia s long-term savings grew from 53 percent of GDP in 1996 to 84 percent of GDP in 2001. Countries vary considerably in the relative importance of their contractual savings institutions. A study by Vittas (1997) distinguishes three levels of development: countries where assets of contractual savings institutions are less than 10 percent of GDP, over 10 percent but less than 50 percent, and exceed 50 percent. Namibia seems to fall in a higher category with countries such as Netherlands, Singapore, and South Africa. The lowest category covers most of the Latin American countries (with the exception of Brazil, Columbia and most notably Chile).

2.3.2.1 Pensions funds

A pension fund is one of the most important contractual vehicles for savings mobilisation in Namibia. The saving by pension funds is mobilised through individuals and employers paying regular contributions into a pension, retirement and provident fund. The total number of registered pension funds has grown strongly since independence. By the end of 1992, the total registered funds were 176, but at the end of 2002, the number increased by 160 percent to 500. Namibia s ratio of pension assets to GDP in 2003 was an estimated 60 percent (approximately N$20 billion/N$30 billion).

[1] The saving includes pension funds and life insurance companies.

Chart 4 Namibian Pension Funds Assets (N$ Million)



Source: Namfisa

The total assets of pension funds in Namibia stood at N$20.0 billion at the end of 2003 compared to N$4.5 billion in 1995. This represents about 70 percent of all the assets of Non-Bank Financial Institutions (NBFI), or around 36 percent of all the assets of the financial system. The Government Institutions Pension Fund (GIPF) accounts for about 80 percent of the total assets of pension funds. This kind of savings in countries such as Chile has been used effectively for productive investment purposes. The challenge for Namibia is to utilise the abundant savings held by contractual savings institutions for productive investments in the country without compromising the returns on the invested savings.

Table 2 GIPF Portfolio allocation in (N$ Million)

Instruments	1999	2000	2001	2003
Derivatives	8,904	10,856	19,224	4,123
Bonds	1,158,991	1,549,437	1,668,349	1,991,197
Shares	3,142,294	4,475,112	4,829,069	5,490,821
Insurance Policy	113,169	91,674	97,002	125,920
Unit trust	1,295,840	1,432,105	1,474,255	2,074,975
Deposits	883,539	847,748	1,067,636	1,080,533
Unlisted companies	183,920	209,332	359,070	390,037
Debentures	22,837	44,722	96,543	77,713

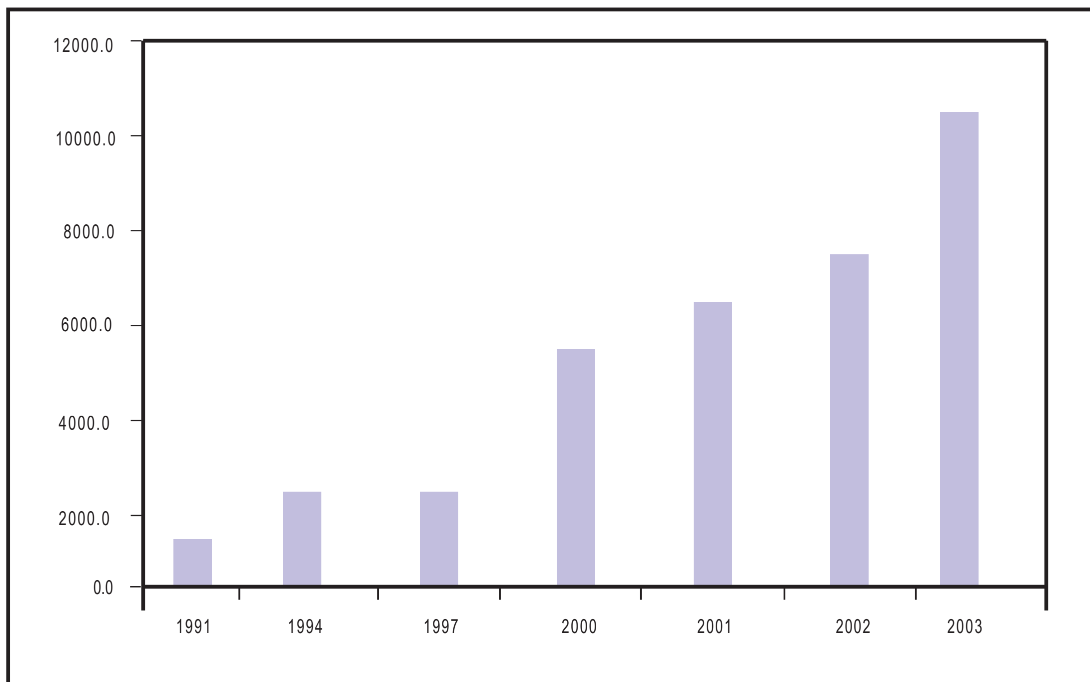
Source: GIPF Annual Reports

Using the investment portfolio of GIPF as proxy for the pension fund industry, it appears that the most popular instruments by pension funds are investment in equity, followed by bonds and unit trusts. Statistics show that around 80 percent of investments in equity are invested in South African companies. It is worthwhile to mention that pension funds still invest close to 60 percent of their portfolio in South Africa. This picture shows that the investment pattern of private pension funds may even favour South African s market more than the domestic.

2.3.2.2 Insurance companies

There are eight long-term insurance companies operating in Namibia. The majority of these insurance companies is wholly owned by parent companies in South Africa and, in addition to local prudential requirements, they are subjected to stringent measures by the parent companies.

Chart 5 Total Assets of the Long-term Insurance Companies (N$ Million)



Source: Namfisa

After pension funds, the long-term insurers are the largest group among non-bank financial institutions when measured by the size of total assets. The total assets of long-term insurers are estimated at around N$6.7 billion as at the end of 2002, representing about 20 percent of total assets of the financial system. The industry assets grew further by 46 percent from N$6.7 billion to N$9.8 billion in 2003.

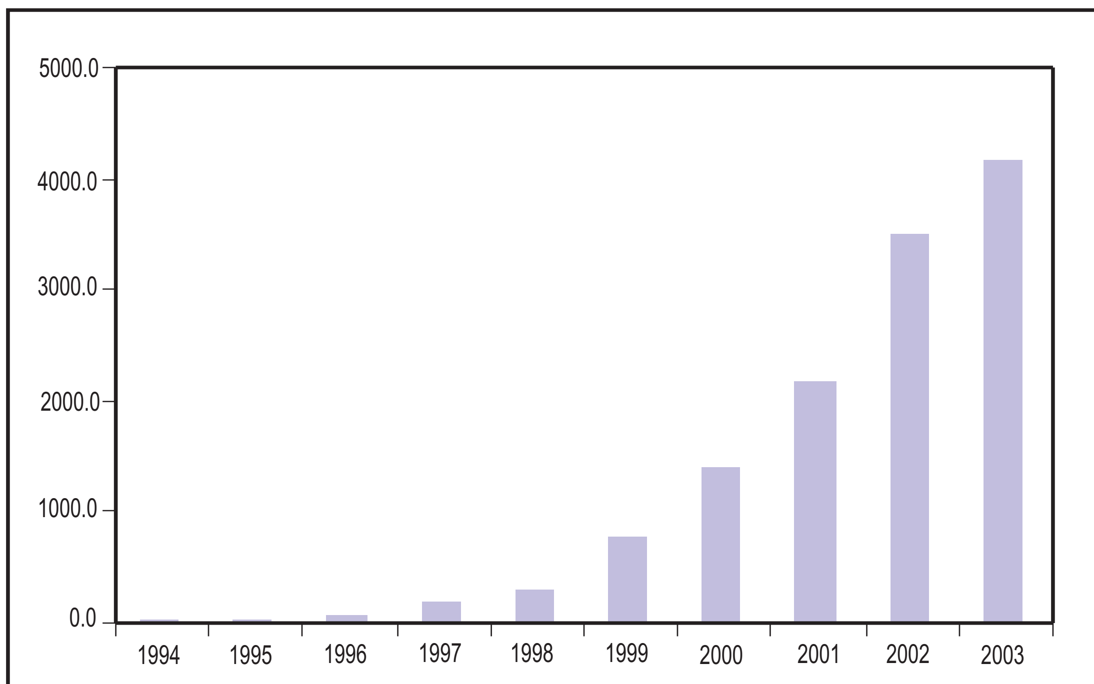
There are nine short-term insurance companies registered with the Namibia Financial Institutions Authority (NAMFISA). The total assets of short-term insurance companies doubled between 1993 and 1996 from nearly N$100 million to over N$200 million. At the end 1997, assets of short-term insurance companies totalled N$255 million, while they increased to N$973 million at the end of 2002. This represents about 1.3 percent of total assets of the financial system. In terms of concentration, this sector is dominated by three big companies (Mutual & Federal, Sanlam and FGI Insurance Namibia) that collectively account for about 80 percent of the total assets of short-term insurers.

2.3.3 Unit Trusts

A unit trust is a relatively new concept in Namibia that started in 1994 when Sanlam Namibia launched its first Namibian unit trust. However, at the end of 2002, there were eight registered Unit Trust Management Companies in Namibia. A unit trust is an investment mechanism that provides a large number of investors with means to participate in a diversified portfolio of investment. The main advantage of a unit trust lies in the mutual pooling of resources for investment under professional management. Even the small saver thus acquires all the advantages of equity/fixed interest investment, while liquidity is retained through the guarantee to repurchase units at prevailing market values.

Although unit trusts have not been in existence that long in Namibia, they have been doing relatively well and the industry as a whole has continuously increased its mobilised assets over the years. For example, in 1994 (the year when the first units trust was established), the total assets managed by unit trusts in Namibia were only N$24 million. These assets increased from N$213 million in 1997 to N$3.5 billion in 2002. This strong growth is essentially explained by the fact that returns from investments in unit trusts by individuals and companies are tax-free. Unit trusts also enjoy a much more liberal regulatory regime than commercial banks and other non-bank financial institutions. It was found, therefore, that the growth of assets managed by unit trust, was mainly at the cost of deposits held by commercial banks. This, in turn, has reduced the degree of intermediation by commercial banks and also diverted investments in real assets to investments in financial assets. The overall impact of utilising savings for investment and growth was therefore reduced.

Chart 6 Assets Development of Unit Trusts (N$ Million)



Source: BoN and Old Mutual

This development has shown that unit trusts are one of the effective vehicles for the mobilisation of savings in Namibia. By the end of 2000, total assets of unit trusts reached a level of N$1.4 billion representing 8.1 percent of the total assets of the non-bank financial institutions and 4.5 percent of the total financial assets. The assets managed by unit trusts grew further in 2001 to N$ 2.1 billion and doubled to N$4.1 billion in June 2003.

2.4 SUMMARY

Unlike many developing countries, savings have been relatively high in Namibia. The savings structure shows that domestic financial intermediaries have been quite successful in mobilising savings. However, the high savings mobilised in the economy do not seem to have been utilised sufficiently for investment, particularly in unlisted activities. This is evidenced by the fact that financial institutions are primarily concerned of maximising returns for investors (and themselves) over the short-term, with little regard to the long-term need to develop and grow the economy.

Having reviewed the structure of saving in Namibia, one is inclined to conclude that the country is in a better position to use its current savings to finance long-term investments. This is based on the premise that the economy has well developed contractual saving institutions such as life insurance and pension funds which have long-term liabilities on their balance sheets. This is usually in contrast with commercial banks that have mainly short-term liabilities on their balance sheets. An institution that has short-term liabilities is prone to facing the risk of unexpected run against their assets that could generate liquidity problems, and potentially cause solvency problems. As a result, the investment and lending strategies of commercial banks differ and are more risk averse to uncollateralized long-term financing than those of contractual savings institutions. Therefore, the country must design appropriate strategies to induce the contractual saving institutions to invest more in long-term investment with the view to grow and develop the economy.

3. FINANCIAL INSTITUTIONS AND INVESTMENT REGULATION

For the economy to grow and prosper, it is necessary that significant amount of savings must be translated into domestic investment, thus linking savings to economic growth. The purpose of this section, therefore, is to highlight the roles of some of the financial institutions in savings-investment translation. The main focus is on the experiences of some industrialised and developing countries.

3.1 FINANCIAL INTERMEDIARIES

Financial intermediaries provide the link between the financial and the real sector in the development experience of the developed and newly industrialised countries (Gold Smith 1969). In this respect, the most important agencies known to play a role in the process of savings mobilisation, facilitation and its translation into investment are commercial banks, Stock exchanges and more recently contractual savings institutions. Commercial banks, in particular, are regarded to be one of the most important agencies in linking those who have resources to save and invest with those who have the most promising uses for those funds, and are therefore willing to pay for their use. It is through these aforesaid institutions where decisions about how and where to invest funds are decentralised, just as production and consumption decisions are decentralised in the markets for goods and services. Therefore, this section would discuss briefly the roles of the aforementioned agencies in an economy. This would help to give a direction to Namibia as to how its savings could be translated into investment through these institutions.

3.1.1 Banks

Banks are well known for their role in gathering savings from households and invest them in loans to the private and public sectors. Moreover, banks have a comparative advantage in acquiring private information on borrowers and in monitoring their actions. A developed banking system implies lower monitoring costs in general due to the use of short-term debt, which reduces the scope for opportunistic behaviour, and thus reducing the cost of monitoring. A sound and efficient banking sector is obviously essential for firms especially those that do not have access to capital markets.

Generally, banks all over the world are also perceived to be risk averse to finance unsecured long term projects, which could be partly due to the nature of their balance sheets that consist mainly of short-term liabilities.

3.1.2 Stock Exchanges

Like the banking industry, stock markets play an important role in the national economies. In the process of financial development, equity markets across the world have become another important source of resource mobilisation and allocation. They help stockholders and other people to make investment decisions, evaluate how efficiently corporations are being run, and assess the general business climate.

This is done through the prices of thousands of corporate stocks that are traded daily on these exchanges, rising and falling in response to changing business conditions for individual firms, their competitors, and the overall economy. Stock markets, along with other sources of financing, can promote private enterprise expansion and thus stronger national economic growth.

Financing through the equity market has been observed to be relatively long term in nature as compared to the traditional intermediaries (commercial banks). The penchant for commercial banks towards short-term loans can be interpreted as a preference towards financing the variable cost needs of the firms. While on other hand firms tend to approach the equity markets to finance their fixed cost needs. Levine and Zervous (1998) confirmed this differentiation in their cross-country study of equity market and development.

3.1.3 Contractual Savings Institutions

Contractual savings institutions can play a very important role in the development of a country s financial system, and capital market in particular. This depends largely on the allocation of their assets, which varies considerably from country to country, reflecting both historical traditions and differences in regulation. The flow of funds into different types of asset is usually a matter of regulation (investment limits) and attitude toward risk. Investment limits are said to be necessary for economies with undeveloped financial market and poor supervisory agencies. However, the limits become more irrelevant for countries, with well-established financial markets and sophisticated supervisory agencies.

In Europe, for example, pension funds and life insurance companies used to place the largest part of their assets in government, corporate and mortgage bonds and in long term loans. This pattern of investment was attributed to investment regulations and partly as a result of traditional emphasis on conservative investment policies. Although pension funds and insurance companies are subjected to upper limits on their holdings of equities (as well as overseas securities) and although their managers were seeking either increases in these limits or their complete abolition, restricted investments were well below the specified limits. However, over the years, there has been a gradual shift of asset allocations of Dutch and Swiss pension funds in favour of equity investment and this had major implications for the size and liquidity of their respective national markets.

For the period (1980-1995) pension funds and life insurance companies in the Netherlands have invested 61 percent of their funds in long-term loans for the unlisted activities, 11 percent in shares, 14 percent in long term bonds, 2 percent in short-term loans and cash and 13 percent in other investments. Both pension funds and life insurance companies do not have any investments in short-term bills and bonds.

The pattern in other countries was similar to that of European countries, where investment rules have generally favoured bonds, except South Africa, where pension funds and life insurance companies have been free to invest in equities.

In other part of the world, for example in Singapore, the Central Provident Fund invests over 90 percent of its funds in specially-issued, non-marketable and floating rate government securities that earn a modest positive real rate of return. In Malaysia, the funds of the national provident fund are placed in government bonds, although investment in equities has increased in recent years.

In Chile, investments in corporate equities for the privately managed pension funds were less than 20 percent of total assets in the late 1980s, mainly because of the imposition of tight restrictions on their investment portfolios. The pension funds invested heavily in government, mortgage and corporate bonds, as well as bank deposits (Vittas, 1995). The investment regulations allowed up to 100 percent in government securities, up to 60 percent in corporate bonds. For other categories such as mortgage-backed securities and letters of credit or fixed term deposits, up to 70 percent investment in those instruments was allowed. As markets developed in Chile, regulations were relaxed to allow investments in shares, mutual funds, real estate funds, venture capital funds, securitised credit funds, foreign securities and hedging instruments. The limit on equities has been raised to 30 percent of assets in the 1990s while they were also allowed to invest in foreign securities.

In all these economies, pension funds did not only serve as a source of long term savings to support the development of bond and equity markets, they also served as a positive force for the innovation, corporate governance and privatisation process. In turn, capital markets offered pension funds the opportunity for better portfolio returns and risk management.

These countries were also having strict limits on foreign investment. Chile, for example, did not allow overseas investment until 1990. In the late 1990s, it raised the limit for investment in overseas securities to 9 percent of assets and 4.5 percent for foreign equities. This is justified by the argument that unrestricted foreign investment may institutionalise capital flight and prevent domestic markets from reaping the benefits of creating pension funds with long term financial resources.

3.2 LESSONS FOR NAMIBIA

Similarly, the Namibian government, recognising the role of appropriate regulation in the economy introduced regulation 28, which is aimed at retaining savings within the economy. The introduction of regulation 28 that requires 35 percent of the pension funds money to be invested in Namibia has resulted into a situation were at least a portion domestic savings is invested in local bonds, equities and cash. For prudential purposes Regulation 28 and 15 made the following investment provision for the contractual savings institutions.

Table 3 Investment Limits in Namibia

Assets	Pension fund and life insurance
Bonds per institution	20 percent
Unlisted activities	5 percent
Deposits per Banking Institution	20 percent
Property shares and units in unit trust	25 percent
Shares on a single company listed on any stock exchanges — CMA less N$ 2 billion	10 percent
Shares on a single company listed on any stock exchanges — CMA more than N$ 2 billion	15 percent
Shares on a single company listed on NSX less - N$ 500 Million	10 percent
Shares on a single company listed on the NSX - more than N$ 500 Million	15 percent

Source: Pension Funds and life insurance Act

The regulation has also a number of limitations, for example it limits investment in unlisted activities and property shares in Namibia to only 5 percent and 20 percent, respectively. Investment in a single company listed on the Namibian Stock Exchange with market capitalisation of less than N$500 million and more than N$500 million is limited to 5 percent and 10 percent, respectively. The regulation has succeeded in the development of the local asset management companies. However, the fact that asset managers invest more in the shares of dual listed companies at the Namibian Stock Exchanges render regulation 28 partially ineffective, because a portion of 35 percent required to be invested locally flows out in the form of investment in shares of dual listed companies.

From the global experience, investment limits are said to be necessary for economies with undeveloped financial market and poor supervisory agencies. However, as capital market developed, the investment limits or

regulations in more risky investment were relaxed and that has played a significant role in the growth prospects of those economies. It appears many countries in the early years of financial development were having stricter rules that were more prescriptive on where and how much to invest in various portfolios. For example, in Europe, pension funds and life insurance companies place the largest part of their assets in long term government, corporate and mortgage bonds. The experience in other countries such as Chile, Malaysia and Singapore is also not different from the one of Europe.

This pattern of investment is attributed to investment regulations and partly as a result of traditional emphasis on conservative investment policies. This implies investment in other portfolio such as equity was seen to be more risky, while returns on government bonds were more favourable with less hassles.

While investment in long-term government bonds seems to have been popular in most of the countries, Namibian pension funds and life insurance companies seem to prefer investing in short-term bonds or treasury bills. This could be on account of their perceived risk of the Government s credibility, but more importantly their reluctance to venture into long term commitments. This reluctance by domestic institutions to invest in long-term government bonds is in contradiction with world wide experience and therefore does not seem to be justifiable on these accounts. First, government bonds in Namibia have high premium relative to similar bonds in the neighbouring South Africa. Secondly, government budgetary performance has not been out of proportion to the extent government will not be in a position to honour its debt obligations.

Therefore, it is necessary to look at the effectiveness of the legislation, because empirical evidence has shown that appropriate legislation tends to facilitate the flow of savings to investment in productive sectors of the economy through financial markets and stock exchanges.

The assessment from this review shows that, although some of the institutions might have been ready to make investments in the so-called risk portfolios, they were constrained by stricter regulations and conservative investment policies. These policies were more in favour of bonds. As the policies were relaxed, contractual savings started featuring prominently in equity portfolios, i.e. Chile and Netherlands. It will be of crucial importance for Namibia design a mandatory measure for the contractual savings institutions to invest a certain portion of their funds into government bonds. This will clearly help the country in the long run to have a well developed capital market.

4. CONSTRAINTS ON DOMESTIC INVESTMENT

This section analyses factors that are constraining the saving-investment translation process from the perspective of fund holders. The interviews conducted with some of the key players in the financial institutions such as unit trust management companies, asset managers and insurance companies pointed to the fact that there are no quality investment instruments in Namibia. Furthermore, lack of relevant expertise and institutions such as private equity fund, Venture capital and Development Bank have also been cited to contribute to a low savings-investment translation process. Low level of liquidity and free float of shares in the NSX has been mentioned frequently as some of the impending issues. Generally, investors are interested in high yielding investment instruments, but in the absence thereof, could have contributed to a low level of saving-investment translation in the domestic economy. A number of relevant institutions or vehicles were suggested to play to a certain extent a role in the utilisation of funds in the domestic economy.

4.1 VENTURE CAPITAL AND PRIVATE EQUITY FUNDS

It emerged during the interviews with the key market players that lack of relevant institutions for investment such as venture capital fund and private equity fund might have restrained the savings-investment process in Namibia. Establishment of these institutions is hailed as one of the key steps towards addressing these gaps. A recent initiative on the establishment of the venture capital fund by IJG and a proposed private equity fund to replace the GIPF development capital portfolio will certainly address some of these impediments. Venture capital can play a significant role in long term financing due to its greater appetite for risk, than that of commercial banks. Venture capital is a specialised, professional investor, who provides funding and, in return, takes up equity in an enterprise, participates actively in the management of the enterprise and latter sells his stake after the start-up phase. Establishment of these relevant institutions would possibly enable institutions with long-term assets to avail their funds into productive investment.

4.2 SPECIALISED BANKS

It was also reported that the lack of specialised banks such as Development and Investment Banks could have hampered the process of savings-investment translation in Namibia. For example, a Development Bank is broadly seen as a vehicle that aims at financing long-term development projects, which could put an impetus to the development process of an economy. Like the venture capitalists, the establishment of specialised Banks in the domestic economy would help to accelerate investment-growth process. These banks would mobilise funds available in the domestic economy and use them for productive investment. Such mobilisation of funds could be done through the issuance of bonds to the public and thereby obtain needed funds to finance productive investments. This could also help reducing the outflow of capital. In this regard, it is of necessity for the Namibian authorities together with the active participation of the private sector to accelerate the process of setting up specialised banks.

4.3 OTHER INSTRUMENTS

The interviews revealed that a number of financial instruments such as real estate securities, inflation linked bonds, and derivatives are non-existent in the domestic market. This is partly to be blamed on the smallness of the domestic market and lack of capacity by local asset managers and stockbrokers. The players suggested that the introduction of more instruments would broaden the scope of investment, and possibly can go a long way in addressing the outflow of capital. The investors want higher or favourable long-term returns through appropriate and attractive investment instruments. It is our view that, if Namibia is to retain its savings to be utilised in the domestic economy, efforts must be geared towards development of locally based companies.

4.4 ROLE OF THE STOCK MARKET

The role of the stock exchange in mobilising funds for use in Namibia is still being questioned. The argument is that dual-listed companies could be used to transfer Namibian saving to South Africa. It can therefore, not be said with confidence that capital raised by these companies are indeed used in Namibia. In contrast, if it is in fact the case that funds are raised on the NSX for use in South Africa, then the NSX is simply a channel through which funds flow to South Africa or elsewhere, a situation that is not desirable.

5. STRATEGIES FOR NAMIBIA ON SAVINGS UTILISATION

The purpose of this chapter is to provide a number of savings utilisation options that could be considered by various economic agencies. In today s competitive financial services environment, there are many alternatives to conventional commercial bank finances. The following institutions or measures could either complement or compete with the existing structure and thus offer conducive environment for savings utilisation. The problem in Namibia is a lack of institutions with greater appetite for risk.

5.1 THE PRIVATE EQUITY FUNDS

Namibia is a country with abundant pension and life insurance funds, and has also potential projects that may not yet have been proven to be viable. In such situation commercial banks have a tendency of not financing or providing start-up capital to these initiatives. To that effect, one viable option to promote such initiatives is to form a venture capitalist funds.

The venture capital/private equity fund is a good vehicle to promote investment in the riskier productive sector, as it has a much greater appetite for risk. It is good in the sense that it does not only provide the necessary finances, but also the management skills required to run the business efficiently and effectively.

Their approach is described not as hands-off as with traditional commercial banking, but rather as hands-on . This institution has become an important outlet for the financial resources controlled by pension funds and other institutional investors worldwide. In this regard, it is recommended that further research be conducted to assess the performance of private equity fund in other countries and their viability in Namibia.

There are three possible channels for utilising contractual savings in the productive sector or unlisted activities in the domestic economy. One is for asset management companies to invest directly in unlisted activities. The second is for asset management companies to give the funds entrusted to them by the trustees of pension funds to a private equity fund. The third is for private equity funds to be entrusted directly with pension and life insurance assets.

With respect to asset management companies and looking at the mandate given to them by the trustees which strongly emphasises performance, it would be difficult for them to venture into something without a secure return. This implies that within the current setup the two first options do not seem to be feasible.

What appears to be feasible is the third option, which would enable pension funds and long term insurers to invest a certain percentage of their funds in private unlisted equity for long term investment. However, this can only be possible with the intervention of the government in providing some tax incentives to these institutional investors or by introducing appropriate investment regulations. Therefore, initiative between the Bank of Namibia and the Ministry of Trade and Industry aiming at establishing a venture capital fund in Namibia must be vigorously pursued.

5.2 TAX INCENTIVES

Tax incentives have played a key role in creating the enabling environment for fund holders to release part of their portfolio to productive or riskier investment purposes. This kind of incentive was used successfully in the mining industry in Canada. Investors were availing their funds in mining exploration exercise in the Northern Part of Canada and the government offered tax incentives for the short term return forgone on their assets.

A similar strategy can be used in Namibia, particularly for fund holders. The investors who invest their funds directly in private equity fund for long-term investment can be given tax incentives to compensate them for short-term losses they incur. This will be a small cost to government in the short term, but in anticipation of greater benefits in terms of tax revenue in the long run. The funds availed for productive investment will in the long run broaden the tax base through new companies and more activities in the economy.

5.3 DOMESTIC ASSET REQUIREMENTS FOR UNIT TRUSTS

Unit trusts have become important vehicles for the mobilisation of savings in Namibia. By the end of 2000, the total assets of unit trusts reached a level of N$1.4 billion representing 8.1 percent of the total assets of the non-bank financial institutions and 4.5 percent of the total financial assets. In absolute value the unit trusts grew further to N$ 2.1 billion in 2001, to N$3.5 billion in 2002 and to N$4.1 billion 2003.

This study has pointed out that unit trusts have started to compete unfairly with commercial banks in terms of returns offered to investors, mainly due to the tax-free status of returns on unit trust investments and the less restrictive regulatory regime of unit trusts vis- -vis that applying to banks. The growth of assets managed by unit trusts at the cost of bank deposits is not desirable, as it reduces the banks ability to intermediate in the market and as it diverts investments in real assets to investments in financial assets.

It is recommended that unit trusts be subjected to the same strict prudential regulations as applied to commercial banks and that the tax-free status on returns on unit trust investments be withdrawn in its entirety or, at least, for corporate tax payers.

5.4 SPECIALISED BANKS

Institutions that may play a role in ensuring that savings are utilised effectively for investments in the productive sector are specialised banks (such as development banks, investment banks and co-operative banks). These institutions could help to finance long term productive projects in the economy, particularly, infrastructural development that could support and sustain long term growth prospects. The co-operative banks are usually formed by farmers and other associations to provide credit to their members. They issue Co-op bonds to finance loan requirements of their members.

These banks mainly play a role in meeting financing needs of small-scale borrowers who may not have the necessary collateral required by the commercial banks. Community banks and credit unions and co-operative agencies must be encouraged and supported, but most importantly their viability must still be determined. In case they are found to be viable, the relevant authorities (i.e. MoF, BoN and MWARD) must strive towards strengthening existing institutions and establishing new ones of this kind.

5.5 REVISIT REGULATION 28 AND 15 FOR DOMESTIC ASSET REQUIREMENTS

The evidence shows that capital outflows through insurance and pension funds constitute a major portion of outflows from the economy. One of the objectives of the 35 percent local asset requirement imposed on these classes of institutions was to check capital outflow by compelling them to invest in the local market. Empirical evidence shows that only 10 percent of pension funds assets can be classified as true Namibian asset if dual listed shares and cash placed on deposit at local commercial banks are excluded from these portfolios (Nepru 2002). The same study also found that less then 5 percent of the 35 percent Namibian portfolio consists of local equity. The implication here is that only 20 percent of the total assets of the pension funds and life insurers are truly Namibian, while the rest is invested in dual listed companies.

To make the domestic asset requirement more effective, it is proposed that that the percentage of dual listed investment that qualifies as a domestic investment should be significantly reduced to 10 percent of the domestic portfolio. The reduction must be phased in over time.

This study has also found that regulations 28 and 34 does not prescribe minimum investments in Namibian government and government-backed securities, but instead prescribes limits to these instruments. It is recommended that these two Regulations are amended to prescribe a minimum percentage that pension funds and insurers must invest in government and government-backed instruments.

5.6 COMMERCIAL FINANCE COMPANIES

Specialised commercial finance companies are commonly known as asset-based lenders. Their specialisation is in making working capital or investment capital loans to small-scale businesses. The loans are secured by the business s accounts receivable and/or inventory. Often, banks participate with asset-based lenders in providing lines of credit. It is said that through this type of arrangement, banks have better monitoring capabilities, and it is particularly useful when lending to start-up business or to rapidly growing companies. These kinds of companies are not popular in most developing countries; they are more popular in developed economies such as United States and United Kingdom.

5.7 GOVERNMENT AGENCIES

Governments in other part of the world, as well as in Namibia offer financing assistance such as loan guarantees. In Namibia, it is still a new initiative, which has not yet been exploited to its maximum potential. This kind of assistance is designed to allow banks extend credit to business that might not otherwise qualify on grounds other than credit record. The average term of the guarantee is thirty-six months, but can be extended to 60 months if required.

Since the year 2000, Small Business Credit Guarantee Trust (SBCGT) has guaranteed loans amounting to N$42.9 million. From the beginning of the programme a total number of 2750 have benefited from this scheme. The minimum loan granted is N$ 3000, while the maximum is N$312,000. The scheme has paid a total amount of N$ 1.4 million to the commercial banks due to the defaulting borrowers. It is always necessary to ensure that loans backed by this scheme must meet the same credit criteria as all other loans. In such situation, it is imperative that for this scheme to remain sustainable to be accompanied by intensive training to equip the borrowers with the necessary basic skills in finance and business management.

5.8 APPROPRIATE SKILLS

One area of concern in the Namibian economy cited by players in the financial sector is the lack of appropriate skills and this has restrained to a great extent innovations and aggressive entrepreneurship. On this basis, it is advisable that the government and the private sector must make concerted efforts to enhance the country s human resource development with view to improve skills, especially in the areas of finance and entrepreneurship.

5.9 INFLATION LINKED BONDS

Taking into account that Namibia has an abundance of long term savings, mainly from pension funds and life insurers, the introduction of inflation liked bonds may help to retain more savings in the domestic economy. The literature clearly states that pension funds and life insurance do not necessarily have the same appetite for instruments as, say, commercial banks and hence cannot be expected to invest in similar assets all the time. The experience shows that pension funds are likely to have a return benchmark of average earnings, while life insurance companies at most seek to beat inflation. Therefore, an introduction of inflation linked bonds will to some extent reduce the outflow of life insurance funds and broadens the investment portfolios in the domestic economy.

6. CONCLUSIONS AND POLICY RECOMMENDATIONS

This study has assessed the structure of savings, mainly contractual savings in Namibia and to find out why most of these savings are not translated into investment. Having assessed the factors that impede savings-investment translation, the study is suggesting strategies to address some of the imperfections in the market. The study found that contractual savings which consist of pension funds and life insurers dominate the structure of savings in Namibia and are estimated to attract around 60 percent of total domestic savings. This is followed by commercial banks, which account for about 38 percent of total domestic savings.

The study further established that the lack of enough investment instruments and expertise in the Namibian economy has hindered the proper utilisation of savings. The lack of relevant institutions, such as venture capital fund and specialised banks, which can be outlets for financial resources, controlled by pension funds and other institutional investors, have restrained the process. These specialised institutions are mainly known for utilising resources for long-term and productive investment purpose.

Regarding the type of investment instruments, the study recommends that further research must be done to explore whether the kind of instruments proposed are feasible in the domestic economy. If found feasible, introduction of new instruments must be supported by investment limits or regulations that would help to stem the outflow of funds to outside world, particularly to South Africa. As such an outflow of capital, especially, if it is unidirectional could have serious implications to Namibia s long-term investment and growth prospects. Such unrestricted foreign investment may institutionalise capital flight and prevent domestic markets from reaping the benefits of creating pension funds and insurance companies with long term financial resources.

The study concludes that the dual listing of shares at the NSX has complicated the saving-investment process whereby funds invested through the companies find it way out of the economy to South Africa. To address this concern the study recommends that the Namibia Stock Exchanges must play an active role in identifying and grooming potential domestic companies and eventually list them. This process will help to facilitate the process of keeping funds invested through the NSX to remain in the economy and trickle down to productive investment, i.e. employment creation.

From the experience of both developed and developing economies, the study establishes that there is nothing wrong in introducing strict investment measures or limits to work in favour of the development of the domestic capital market. Therefore, the study proposes that in order to develop the domestic market and to ensure that the country benefits from its long term financial resources, there is a need to level the playing field. This suggests that regulatory measures must be put in place to limit the excessive outflow of funds via unit trusts and also to bring the tax and regulatory regime applying to unit trust investment on the same level as that applying to commercial banks. However, as mentioned earlier, these changes must be accompanied by aggressive exploration of new avenues of investment. As regulation without supporting market structures will lead to inefficiencies and might distort the market.

In addition in making the domestic asset requirement more effective, it is proposed that that the percentage of dual listed investment that qualify as a domestic investment should be significantly reduced to a lower percentage of the domestic portfolio. The reduction must be done gradually.

The study also recommends that necessary measures must be taken to induce pension funds and long term insurers to invest in government long term bonds. In addition, the government must put appropriate incentives in place to enable the contractual saving institutions to invest in the long-term projects where banks are not

willing to finance. This is supported by empirical evidence that shows that appropriate legislations have facilitated the flow of savings into investment in productive sectors of the economy e.g. Chile. The paper proposes some tax incentives to be introduced by government in order to enable the funds holders to avail their funds to relevant institutions such as private equity to boost investment in long term projects.

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APPENDIX

Table 1 Types of Commercial Banks Savings (N$ Million)

Year	Demand Deposits	Savings Deposits	Time Deposits
1992	1064.5	338.3	1101.3
1993	1333.1	347	1197.6
1994	1552.5	425.3	1657.8
1995	1641.6	466	2513.4
1996	2617.7	559	2744.6
1997	2929.14	592.82	2994.5
1998	3376.72	622.86	2953.99
1999	4174.03	667.32	3374.12
2000	5507.6	705.8	3295
2001	6095	748.7	2993.9
2002	6440.6	786.1	3472.5
2003	7705.8	906.3	4686.4

Source: Bank of Namibia

Table 2 Types of Commercial Banks Savings (as a percent of total banks savings)

Year	Demand Deposits	Savings Deposits	Time Deposits
1992	42.5	13.5	44.0
1993	46.3	12.1	41.6
1994	42.7	11.7	45.6
1995	35.5	10.1	54.4
1996	44.2	9.4	46.4
1997	44.9	9.1	46.0
1998	48.6	9.0	42.5
1999	50.8	8.1	41.1
2000	57.9	7.4	34.7
2001	62.0	7.6	30.4
2002	60.2	7.3	32.5
2003	62.7	6.5	30.5

Source: Bank of Namibia

Table 3 Namibia Pension Funds Assets (N$ Million)

Year	Total Assets
1995	4666
1996	5802
1997	7278
1998	8147
1999	9016
2000	12942
2001	16077
2002	16345
2003	20000

Source: Namfisa

Table 4 Total Assets of Long term Insurance (N$ million)

Year	Total Assets
1991	1068
1994	1525
1997	2179
2000	4830
2001	6296
2002	6798
2003	9800

Source: Namfisa

Table 5 Total Assets of Unit Trusts (in N$ million)

Year	Total Assets
1994	24
1995	52
1996	85.7
1997	213
1998	324.7
1999	776
2000	1393
2001	2198
2002	3532
2003	4172

Source: Namfisa