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Equity Bank's Internationalization: Building an African Multinational

Chris Ogbechie and Nkemdilim Iheanachor

As Dr James Mwangi, the managing director and Chief Executive Officer (CEO) of Equity Group Holdings, walked over to the conference room in Equity Centre for a board meeting, he pondered how the bank would eventually enter the sophisticated Nigerian banking industry. The head of the project team charged with the task of developing a concept document for the establishment of the Nigerian subsidiary was Mary Wangari, who was also the director of corporate strategy. She had worked tirelessly with her team to establish possible entry options and evaluate the likelihood of success of each. James had reviewed the document highlighting their findings and recommendations and was set for an extensive debate during the board meeting on how they could best proceed with the Nigerian market entry.

Dr Chris Ogbechie and Nkemdilim Iheanachor prepared this as the basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation.

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With Equity's foray into other markets beginning to show promising results in the existing international locations of Rwanda, South Sudan, Uganda and Tanzania, Equity was now looking at growth opportunities in bigger African markets in fulfilment of the bank's vision to be the champion of socio-economic prosperity of the people of Africa. The Nigerian market was identified as a top priority given its strong fundamentals and similarities to Kenya, Equity's home country.

The decision to establish a Nigerian subsidiary was a bold one given the challenges of doing business in Nigeria. The project team recommended that Equity leverage on its various experiences from operating in other international locations as the Nigerian market would be similar in many ways. They had also established the pros and cons of each of the identified entry options.

The Nigerian banking industry had emerged from two reform phases that left questions about future policy directions and what the minimum regulatory establishment and existence requirements would be for existing players. The structure of the industry had also evolved, with the number of licensed commercial banks in the country decreasing from 89 to 25 at the end of the reforms in 2004. The competition for deposits and loans among Nigerian banks was intense as the licensed banks had well-developed portfolios of savings and loan products aimed at meeting the financial service needs of virtually all segments of the economy. The Central Bank of Nigeria had two major license categories for banks—commercial licenses and microfinance licenses. There were only two non-Nigerian banks with a presence in Nigeria as at December 2013.

The project team had established several entry options: establishment of a brand new commercial bank, acquisition of an existing commercial bank, entering into a partnership or joint venture with an existing commercial bank or establishing a national microfinance bank. Which was the most prudent option? Equity also had to decide on how to position the bank: Was it going to be a national bank or a regional bank? How many branches would they commence with at take-off? How were they going to recruit take-off staff? How would the board members be identified? Would the establishment of the Nigerian subsidiary put a further strain on management resources already stretched by the closure or letting go of 217 branches, 10,260 agents, 584 Automated Teller Machine (ATMs)

and 7788 employees in Kenya and other international locations? As James reflected on all these questions, he thought about Equity's position in Kenya and wondered if Equity would succeed in Nigeria, where several other non-Nigerian banks had failed.

About Nigeria

Nigeria is the 10th-largest country and has the largest economy in Africa.[1] It lies on the west coast of Africa, occupies about 923,768 km^2 of land, and borders Niger, Chad, Cameroon and Benin. The country is made up of 774 local governments and 36 states, including the Federal Capital Territory, Abuja.[2] The country is structured into six geopolitical zones: South South, South West, South East, North East, North West and North Central. Nigeria's population was about 160 million people in 2015, about 15 % of Africa's population. It is the most populous country in Africa and the whole black world; one out of every five Africans is Nigerian.[3] Nigeria, the seventh-most populous country in the world, has an age structure in which the largest segment is made up of individuals within the ages of 15 and 64 years (55.9 %), followed by individuals within the ages of 0 and 14 years (40.9 %); people aged 65 years and over represent 3.1 % of the country's population.[4]

Nigeria is a multi-ethnic state with over 250 different ethnic groups. The three largest and most influential ethnic groups in Nigeria are the Hausa, Igbo and Yoruba. Nigeria is roughly split half and half between Muslims and Christians, with a very small minority who practise African traditional religion.[5]

Nigeria's macroeconomic performance was on the upswing between 2000 and 2013. Nigeria's gross domestic product (GDP) of about $369 billion rose to US $567 billion in 2014,[6] a growth rate averaging more than 7 % between 2010 and 2014. Meanwhile, inflation trended downward to less than 10 % during the same period.[7] Substantial oil saving buffers, built before the 2008 global crisis, provided room for the implementation of countercyclical policies that minimized the impact of the crisis on the domestic economy. However, while Nigeria's growth has been among the highest in Sub-Saharan Africa, poverty still remains high.

Nigeria's is a heavily factor-driven economy diversified across agriculture, crude petroleum and natural gas, and wholesale and retail trade, with sectorial contributions to GDP of 39.49 %, 13.54 % and 19.87 % in 2011, respectively.[8]

Nigeria was structured as a federation, a structure inherited from her British colonial rulers. The country's 1999 constitution provides for a bicameral National Assembly consisting of a 360-member House of Representatives and a 109-member Senate.[9] The president and the governors and legislators in both the upper and lower houses are elected by the people for four-year terms. The president heads the executive arm of government, while the judiciary, including all courts (Supreme, Appeal, High and Magistrate) is headed by the Chief Justice of Nigeria.

Despite Nigeria's substantial natural resources, its infrastructure, particularly its road and electricity networks, remains inadequate, presenting a significant obstacle to economic growth. Only about 30 % of the population has access to electricity, and only about 31 % of the road network is paved.[10]

Owing to sectoral reforms, Nigeria has an advanced financial system relative to several other African countries. The cost of finance is still high, and access to medium- to long-term finance is limited. According to the Business Competitiveness Index (BCI) is from the Global Competitiveness Report in 2005 and 2007, Nigeria's level of competitiveness is declining, and the country is less competitive than South Africa and Kenya. After a slight improvement in the overall BCI Index in 2005, both the quality of the national business environment and the competitiveness of company operations and strategy declined yet again in 2007. Inadequate infrastructure, limited access to financing and high levels of corruption have been the key drivers of the decline in competitiveness. However, efficacy of corporate boards and access to the local equity market have improved.

Table 9.1 shows economic growth projections for the 32 largest economies in the world that collectively account for 84 % of global GDP. Nigeria's GDP was projected to rise from 20th in 2014 to ninth in the world in 2050 and to remain the largest in Africa from 2014 to 2050. This comparison further highlights the economic significance of Nigeria in Africa. Figure 9.1 shows Nigeria's rank in the ease of doing business index[11] compared to other Sub-Saharan African countries.

Table 9.1 Economic growth projections for the 32 largest economies in the world

	2014		2030		2050	
PPP rank	Country	GDP at PPP (2014 US$bn)	Country	Projected GDP at PPP (2014 US$bn)	Country	Projected GDP at PPP (2014 US$bn)
1	China	17,632	China	36,112	China	61,079
2	United States	17,416	United States	25,451	India	42,205
3	India	7277	India	17,138	United States	41,384
4	Japan	4788	Japan	6006	Indonesia	12,210
5	Germany	3621	Indonesia	5486	Brazil	9164
6	Russia	3559	Brazil	4996	Mexico	8014
7	Brazil	3073	Russia	4854	Japan	7914
8	France	2587	Germany	4590	Russia	7575
9	Indonesia	2554	Mexico	3985	Nigeria	7345
10	United Kingdom	2435	United Kingdom	3586	Germany	6338
11	Mexico	2143	France	3418	United Kingdom	5744
12	Italy	2066	Saudi Arabia	3212	Saudi Arabia	5488
13	South Korea	1790	South Korea	2818	France	5207
14	Saudi Arabia	1652	Turkey	2714	Turkey	5102
15	Canada	1579	Italy	2591	Pakistan	4253
16	Spain	1534	Nigeria	2566	Egypt	4253
17	Turkey	1512	Canada	2219	South Korea	4142
18	Iran	1284	Spain	2175	Italy	3617
19	Australia	1100	Iran	1914	Canada	3583
20	Nigeria	1058	Egypt	1854	Philippines	3516
21	Thailand	990	Thailand	1847	Thailand	3510
22	Egypt	945	Pakistan	1832	Vietnam	3430
23	Poland	941	Australia	1707	Bangladesh	3367
24	Argentina	927	Malaysia	1554	Malaysia	3327
25	Pakistan	884	Poland	1515	Iran	3224
26	Netherlands	798	Philippines	1508	Spain	3099
27	Malaysia	747	Argentina	1362	South Africa	3026
28	Philippines	695	Vietnam	1313	Australia	2903
29	South Africa	683	Bangladesh	1291	Colombia	2785
30	Colombia	642	Colombia	1255	Argentina	2455
31	Bangladesh	536	South Africa	1249	Poland	2422
32	Vietnam	509	Netherlands	1066	Netherlands	1581

Source: Adapted from The World in 2050 will the shift in economic power continue? PwC UK, February 2015
PPP – Purchasing Power Parity; GDP – Gross Domestic Product

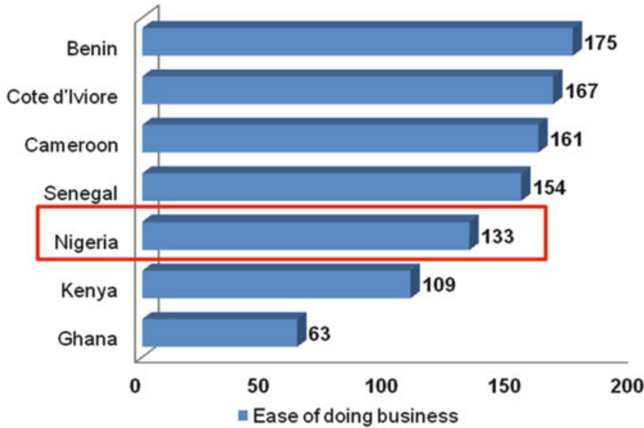


Fig. 9.1 Nigeria's rank in the ease of doing business index. *Source*: Doing Business in a more transparent world report by the International Finance Corporation, World Bank in 2012

Nigeria's Human Development Index (HDI)[12] value for 2012 was 0.471, positioning the country at 153 out of 187 countries and territories and firmly in the low human development category. However, between 2005 and 2012, Nigeria's HDI value increased from 0.434 to 0.471, an increase of 9 %, or an average annual increase of about 1.2 %. The rank of Nigeria's HDI for 2011 based on data available and methods used in 2012 was 154 out of 187 countries. In the 2011 HDI, Nigeria was ranked 156 out of 187 countries. Table 9.2 reviews Nigeria's progress in each of the HDI indicators. Between 1980 and 2012, Nigeria's life expectancy at birth increased by 6.8 years, mean years of schooling increased by 0.2 years and expected years of schooling increased by 2.4 years. Nigeria's gross national income per capita increased by about 34 % between 1980 and 2012.[13]

History of Banking in Nigeria

The first commercial bank in Nigeria, the Bank of British West Africa, was established in 1894 to serve British shipping and trading agencies in Nigeria. Draft legislation for the establishment of the Central Bank of

Table 9.2 Human development statistics for Nigeria as at 2013

	Life expectancy at birth	Expected years of schooling	Mean years of schooling	GNI per capita (2005 PP$)	HDI value
1980	45.5	6.6	-	1571	
1985	45.9	8.4	-	1202	
1990	45.6	6.5	-	1274	
1995	45.1	6.5	-	1303	
2000	46.3	7.9	-	1285	
2005	49.0	9.0	5.0	1540	0.434
2010	51.4	9.0	5.2	1928	0.462
2011	51.9	9.0	5.2	2017	0.467
2012	52.3	9.0	5.2	2102	0.471

Source: Human development report 2013 Nigeria
HDI–Human Development Index

Nigeria (CBN) was presented to the House of Representatives in March 1958. The Act was fully implemented on 1 July 1959 when the CBN commenced full operations.[14] The deregulation of the financial services industry in 1986 following the adoption of the Structural Adjustment Programme led to a rapid increase in the number of banks, from 41 commercial and merchant banks in 1985 to 115 by 1997. Through the liquidation of some banks by the Nigeria Deposit Insurance Corporation (NDIC), with the number of licensed commercial banks in the country decreasing from 89 to 25 at the end of the reforms in 2005.[15] Nigeria benefitted from the largest debt write-off in the history of the Paris Club, reducing its external debt from US $33 billion in 2003 to just US $3.5 billion in 2006.[16]

The Nigerian banking industry serves as the chief medium for financial intermediation in the economy. By 2005, earnings and total assets of the banking sector represented 5.9 % and 49 % of Nigeria's GDP, respectively. Key global banks with varying levels of investment in the sector include Citigroup, Standard Chartered Bank, the State Bank of India and Standard Bank of South Africa. The major offshore institutional investors (debt or equity) include the International Finance Corporation, Kingdom Holding Company of Saudi Arabia and Netherlands Development Finance Company (the Dutch FMO).[17]

To improve the financial base of the country's banking system, in 1997 the Central Bank of Nigeria increased the minimum paid-up capital requirement to N500 million (US$6 million), from N40 million and

N50 million for merchant banks and commercial banks, respectively.[18] The scope of services offered by banks was also expanded with the adoption of universal banking in 2000. The adoption gave banks the freedom to decide which activities they undertook (money, capital market, insurance, clearing house or any combination thereof) as long as they complied with the relevant guidelines.[19]

In January 2001, the minimum paid-up capital for new banks was raised again to N2 billion (US$20 million) from N 500 million to N1 billion (US$7.4 million) that it was raised from N 500 million to, while existing banks were required to raise their capital base to N2 billion (US$15 million) by the end of 2002.[20]

With the number of licensed commercial banks in the country decreasing from 89 to 25 at the end of the reforms in 2004. According to CBN, of the 89 operating banks in Nigeria in 2004, 10 banks accounted for over half of the sector's total assets and deposits, with many of the smaller banks operating at the margin of profitability. The Nigerian economy had a banking sector with credit to the domestic economy at 24 % of GDP, compared to the African average of 87 % and the average in developed countries of 272 %.[21]

Nigeria's Financial Sector

Pre-2004 Characteristics

By 2004, Nigeria's financial system was plagued by various structural problems that hampered its ability to financially intermediate. There was low aggregate banking credit to the domestic economy (about 20 % of GDP), there were various systemic risks as a result of which CBN had to frequently bail out ailing banks, and most banks were grossly undercapitalized and unable to lend to the real sector of the economy. In addition, there was an oligopolistic market structure, with 10 of the 89 existing banks accounting for over 50 % of total banking assets.[22]

Most banks had very weak corporate governance systems, and there was a very low banking population with only one bank branch for every 30,432 Nigerians.[23] The payments system was largely cash-based, and

the insurance industry, which was meant to serve as a buffer to banking system risks, was weak. The Nigerian equities market was also very weak, with less than 200 listed companies at the time.

There was an apathy of banks towards small savers, particularly at the grassroots level, which further compounded the problem of low domestic savings. Banks had also abandoned their main role of financial intermediation, resulting in high bank lending rates and crowding out of small savers, who required access to cheap and stable funds that could provide a reliable source of credit to the productive sectors.

In July 2004, the CBN launched a 13-point reform agenda with the broad objective of creating bigger banks with stronger balance sheets, ensuring safe and sound banking practices and enhancing the regulatory capacity to supervise the industry. A key element of the reform program was the increase in the minimum capital base of banks from N2 billion (US$15 million) to N25 billion (US$190 million) by December 2005.[24]

The reform programme was driven by the following factors:

- Small balance sheet size of Nigerian banks compared with their counterparts in emerging economies, which limited their ability to meet the funding requirements of the economy and also hampered their ability to contribute to the growth of the real sector;
- Narrow scale and scope of services provided by Nigerian banks, leading to a loss of business to foreign banks and resulting in low banking penetration and limited retail banking offerings;
- Fragmentation of the industry, with many banks operating as fringe players; and
- Dwindling level of confidence in the banking system as a result of poor corporate governance and sharp practices by some Nigerian banks.[25]

The CBN reforms were intended to strengthen the Nigerian banking system, with the objective of ultimately making Nigeria the financial hub of Africa. At the end of the consolidation exercise, 75 banks were consolidated through mergers and acquisitions into 25 new entities. The remaining 14 banks had their operating licences revoked, preparatory to formal liquidation. The 25 banks comprised 21 public listed banks, 3 foreign-owned banks and 1 locally owned bank. As at 2005, the banks

had a consolidated balance sheet size of over N4.5 trillion (US$35 billion) and shareholders' funds of N592 billion (US$4.6 billion).[26]

The consolidation resulted in fresh local investments totalling N350 billion (US$2.7 billion) and US$660 million in foreign direct investment into the industry. There was a significant dilution of ownership of the banks as substantial funds for the enhancement of their capital base was raised from the stock market. This increased the strength of corporate governance in the banks and also increased the number of regulators; the banks became public companies under regulation by the Securities and Exchange Commission and the Nigerian Stock Exchange.[27]

In 2005, following the conclusion of the consolidation exercise of the commercial banks, Central Bank of Nigeria (CBN) launched a new microfinance policy to reverse the prolonged sub-optimal performance of most of the existing 600 community banks. These banks had weak institutional capacity as a result of inadequate capital bases, poor corporate governance, lack of well-defined operations and restrictive regulatory/supervisory requirements.[28] The Nigerian market was also hugely underbanked, with a banking density of one financial institution outlet for every 32,700 inhabitants in urban areas and one outlet for every 57,000 inhabitants in rural areas, translating to less than 2 % of Nigerian households with access to financial services.[29] Aggregate microcredit facilities in Nigeria accounted for about 0.2 % of GDP and less than 1 % of total credit to the economy. The effect of not properly addressing the situation was expected to result in an accentuation of poverty and stunted economic growth.[30]

The new microfinance policy specified two categories of licenses—the unit microfinance bank with a minimum paid-up capital of N25 million and the state microfinance bank with a minimum paid-up capital of N1 billion. At the expiration of the deadline given by CBN for existing community banks to convert to microfinance banks and shore up their paid-up capital, to either N20 million or N1 billion depending on the category of license they sought, over 700 microfinance banks had emerged.[31]

A dramatic change in CBN's regulatory posture was occasioned by the appointment of Mallam Sanusi Lamido Sanusi as the governor of the Central Bank following the expiration of Professor Charles Chukwuma

Soludo's tenure. The Nigerian banking sector witnessed dramatic growth after consolidation. However, neither the industry nor the regulators were sufficiently prepared to sustain and monitor the sector's growth. Prevailing sentiment and economic orthodoxy encouraged this rapid growth while at the same time creating a blind spot to the risks building up in the system.[32]

CBN identified eight main interdependent factors that led to the creation of a fragile financial system after the 2005 consolidation, allowing the tip into distress by the global financial crisis and recession of 2008. The factors were macroeconomic instability caused by large and sudden capital inflows, major failures in corporate governance at banks, lack of investor and consumer sophistication, inadequate disclosure and transparency about financial position of banks, critical gaps in regulatory framework and regulations, uneven supervision and enforcement, unstructured governance and management processes at the CBN/weaknesses within the CBN, and weaknesses in the business environment.[33]

Following an industry-wide stress test carried out by joint examiners from the CBN and NDIC, nine out of the 25 commercial banks were adjudged to be in grave condition, prompting immediate intervention by CBN. Some of the problems identified in the nine banks included: non-performing loans totalling N1.7 trillion, representing 44.38 % of total loans; aggregate provisioning required amounting to N1.3 trillion; capital adequacy ratio ranging between 1.01 % and 7.41 %, which was below the minimum ratio of 10 %; and additional required capital injection of N495.83 billion.[34] The CBN immediately took steps to ameliorate the situation by injecting N620 billion into the nine banks, replacing the chief executives/executive directors of eight of the banks, reaffirming guarantee of the local interbank market to ensure continued liquidity for all banks, and guaranteeing foreign creditors' and correspondent banks' credit lines to ensure confidence and maintain important correspondent banking relationships. The capital injection enabled the nine banks to continue normal business operations and prevented a run on the banks. The Asset Management Corporation of Nigeria was established to stimulate the recovery of the financial system by acquiring non-performing loans from banks and assisting banks in improving their liquidity and capital positions.[35]

Post-2004 Reforms

The end of the banking industry consolidation saw a dramatic transformation in the nature and structure of banking in Nigeria. The minimum share capital of banks was raised by 1150 % from N2 billion ($15 million) to N25 billion ($200 million), and the number of banks shrank from 89 to 25.[36] The CBN adopted a risk-focused and rule-based regulatory framework. The CBN also introduced the electronic Financial Analysis and Surveillance System to facilitate online real-time monitoring of the activities of the Nigerian banks. There was strict enforcement of contingency planning and a strengthening of the corporate governance code of banks stipulating maximum tenures of 10 years for bank CEOs and 12 years for non-executive directors. Banks also enhanced their adoption and use of information technology (IT) in all their operations. The recapitalization of the banking industry saw the emergence and rise of Nigeria's equity market, the conversion of community banks to microfinance banks and the establishment of the Africa Finance Corporation.

At the end of the recapitalization exercise, 75 banks either merged or independently raised fresh capital to establish the 25 consolidated banks, and the NDIC employed a purchase and assumption mechanism for 11 of the 14 banks that failed to meet the minimum capital requirement.[37]

In 2007, a second self-induced wave of bank recapitalization took place in the Nigerian banking industry via a combination of rights issues and public offers by banks in pursuit of their domestic and regional expansion programs. The enhanced capital level of Nigerian banks heightened competition among them that manifested in the form of branch network expansion, new product offerings and investments in IT infrastructure. Six banks—Access Bank, First Bank of Nigeria, Guaranty Trust Bank, United Bank for Africa, First City Monument Bank and Diamond Bank—accessed the capital market and raised a total of US$2 billion through the Global Depository Receipts channel.

Key Outcomes of Nigerian Financial Sector Reforms: Systemic Risk Reduction

The Nigerian banking sector emerged from the turbulence with 25 strong banks with larger capital bases. International rating agencies like Fitch and Standards & Poor's rated Nigerian banks for the first time, and the overall number of bank branches in Nigeria increased from 3200 in 2004 to 3866 in April 2007.

About 919 community/microfinance banks were established (capital requirement about $156,000), and total non-performing loans/total loans decreased from 23 % to about 7 % in 2006. Longer-tenured deposits fuelled the increase in credit to the private sector. More than seven banks had over US$1 billion each in Tier-1 capital by the end of 2007.[38]

Financial Inclusion in Nigeria

Results from EFInA's 2010 financial access survey of Nigeria showed that only 30 % of the adult population had a bank account, equivalent to 25.4 million people. Of the adult population, 67.2 %, equivalent to 56.9 million people, had never been banked. Only 2.8 % of the adult population, equivalent to 2.4 million people, were previously banked. Of the 25.4 million adults who were banked, 23.6 million had savings accounts, 15.9 million had ATM cards and 6.5 million had current accounts. Overall, 30.7 million adults were financially included, while about 39.2 million adults were financially excluded, with no access to formal or informal financial services. When compared to other emerging markets like South Africa, Kenya and Botswana, these results showed that the estimated 46.3 % level of financial exclusion was high and presented opportunities.

The CBN's Cash-Lite Policy

CBN introduced a new policy on January 1, 2012 in Lagos cash-based transactions which stipulated a cash handling charge on daily cash withdrawals exceeding N500,000 for individuals and N3,000,000 for

corporate bodies. The new policy on cash-based transactions (withdrawals) in banks was aimed at reducing the amount of physical cash (coins and notes) circulating in the economy and encouraging more electronic transactions (payments for goods, services, transfers, etc.).

The policy was geared towards the development and modernization of Nigeria's payment system in line with the country's Vision 2020 goal of being amongst the top 20 economies by the year 2020. An efficient and modern payment system was positively correlated with economic development and was a key enabler for economic growth. A second aim was to reduce the cost of banking services (including cost of credit) and drive financial inclusion by providing more efficient transaction options and greater reach. Lastly, the policy aimed at improving the effectiveness of monetary policy in managing inflation and driving economic growth.

Equity's History

Equity Bank started operations in 1984 as the Equity Building Society, originally established to provide mortgage financing for Kenyans who were classified as low-income earners.[39] The bank's house-shaped logo was designed to communicate that Equity was an institution desirous of assisting them in building their own homes. The Kenyan government at the time significantly deregulated the economy in a bid to encourage private investment and economic development. The deregulation of the economy provided opportunities for proactive and discerning investors to start formal financial institutions, leading to an increase in the number of financial institutions in Kenya.

At the time Equity commenced its business activities, competition in the financial services industry was fierce among the big industry players, and the potentials were limited as stated. In addition, the mortgage sector was not well developed or well understood. This forced many of the smaller building societies to close shop.[40] Equity, however, managed to survive the onslaught by mobilizing customers and deposits through one-on-one marketing. The bank was at the time operated as an informal family business whose board members were largely friends of the

founders. The absence of disciplined processes and controls led to a gradual deterioration of the bank's loan book quality. In the absence of strong board oversight, Equity's financial health worsened. At the same time there was a gradual decline of interest and involvement in the affairs of the building society by three of the five founding owners/directors and a subsequent withdrawal of two of them from the business. This period of apparent board inactivity (1984–1992) resulted in the stagnation of and subsequent decline in the organization's performance. Customer deposits grew by only KSh1 million between 1986 and 1991. In the same period, loans and advances grew by only KSh7 million, from KSh2 million to KSh9 million. Accumulated losses also grew steadily from KSh5 million in 1986 to KSh22 million in 1991.[41]

Indeed, the first eight years of operations were hard for Equity. No staff member received a salary increase. Twenty staff members worked long hours in order to retain clients. Many other institutions were closing as a result of high costs coupled with the continuous loss of customers and increasing levels of loan default.

By December 1993, the Central Bank of Kenya (CBK) declared that Equity was technically insolvent. Equity's non-performing loans made up 54 %[42] of the total loan portfolio and its liquidity ratio stood at 5.4 %, well below the 20 % required by law. The CBK noted that supervision by the board was very poor. Accumulated losses were KSh33 million on a capital base of KSh3 million.[43] Deposits were being used at this time to meet operating expenses. However, limits to its powers meant the CBK could not request the closure of Equity. Only the Registrar of Building Societies, which licensed Equity for business, had the power to close the institution.[44]

At the start of 1994, Equity was technically bankrupt. It had only 17 staff members, who had extremely low morale, a loan portfolio of KSh12 million (54 % of it bad), and a deposit base of KSh25 million. Three main depositors accounted for 84 % of total deposits: the Kenyan Ministry of Water (KSh12 million), James Mwangi (KSh7 million) and the National Health Insurance Fund (NHIF; KSh2 million).[45] The board had not met between 1992 and 1994 and had performed no oversight functions. The company was grinding to a halt with an average annual loss of KSh5–7 million.[46] A court case was instituted by the Ministry of

Water and NHIF, who were seeking to liquidate Equity. James Mwangi, an accounting graduate from the University of Nairobi, was at the time the financial controller of Trade Bank.

When it became clear to James that his life savings in Equity were threatened, he opted to rescue Equity by joining the team. He resigned his job at Trade Bank and accepted a salary of US $300, compared to his salary of $5000 at Trade Bank. James' humble family background and desire to impact the low-income population in Kenya made him look beyond the fact that he had recently married and his wife had just been delivered of their first baby. After his graduation from the University of Nairobi at the top of his class, James had begun his career at Price Waterhouse, but after one month he had moved over to Ernst & Young, where he worked for three years. He then joined Trade Bank, where he rose to the position of group financial controller after three years.

James joined Equity Building Society as finance and operations director, and he, along with then managing director John Mwangi and chairman Peter Munga, constituted the board. Four independent directors were appointed from pre-eminent Kenyan organizations. James converted his KSh7 million deposit with the bank to ordinary shares, making him the majority shareholder, but John Mwangi remained CEO to allow for continuity and contact with the regulatory authorities.

Equity's Turnaround

James Mwangi also doubled as Equity's chief operating officer at the time, and he and the CEO were saddled with the responsibility of saving the company. He tackled this task in steps, starting with trying to raise the morale of staff. He subsequently ensured that the skill levels of Equity's staff in the technical and managerial areas were significantly upgraded. He was also very open to effective delegation of responsibilities to his colleagues. His vision was of a better future that would be achieved by teamwork, hard work and aspiration. According to James: "*We had to fight to save the bank or sink and lose all we had.*"

At the same time, James had to refocus Equity on microfinance since the existing mortgage market that constituted its primary business required

more capital and skill than Equity possessed at the time. The mortgage market was also more competitive than microfinance. The process involved a radical transformation of Equity's DNA; it underwent a company-wide visioning process through which the directional beacons were set. There was broad ownership among staff of what the organization would be about and how the audacious goals and objectives were to be achieved. James believed that poor people made transactions like any other group of people; the difference was in the size of the transactions. He believed a business model to deliver financial services to the Kenyan poor could be effectively executed. The training staff members received reinvigorated the Equity team by educating them on the needs and peculiarities of the microfinance market and the enormous benefit their work would bring to Kenyans.

In the early 90s, the political environment changed with the introduction of a multi-party political system that led to more freedom for the people. In addition, the government relaxed its requirement that state employees bank only at government-controlled banks. This change resulted in a flood of new deposits at Equity and other industry players. The board realized that if it wanted to turn Equity around, it needed more resources (capital and non-capital) to bring in new thinking, train staff to meet the dynamic challenges of the environment, and also expand its marketing thrust.

Gradually, a culture of customer service, hard work, dedication and devotion was institutionalized. James saw his main role as that of trainer/coach. He was very firm in institutionalizing the culture. During the initial stages there were strict deadlines, uncompromising customer service, long working hours and other such measures. Later on, he intensified staff training, encouraged on-the-job training and coaching and promoted a participative leadership style, all of which helped to galvanize the workforce.

By 1995, customer deposits had grown to KSh124 million from KSh31 million in 1993. Within the same period, the bank went from a loss of KSh5 million to profits of KSh9.7 million.[47] With the company showing signs of profitability, James successfully approached the International Finance Corporation and European Investment Bank in 1996 to invest in Equity through AfriCap (owned by both entities), and they were given a seat on the board. This international connection helped improve the image of the company and won customers' confidence.

In 1997, with this new focus, the company set a target of a KShs1 billion deposit base by 2000, which was achieved as planned. This burst of performance saw the deposit base of Equity grow by 40–50 % per year between 1995 and 2002. Profit margins also grew strongly. Equity had bounced back. Successes afforded access to international partners, such as the Micro Enterprises Support Programme funded by the European Union and UNDP's United Nations Development Programme MicroStart, followed by Swisscontact and MicroSave, the British Department for International Development and MasterCard.[48]

Remarkable evidence of Equity's recovery was the rating it was issued by the Central Bank of Kenya. Shortly after 1993, its rating moved to marginal, then to fair, and by 2002 it was satisfactory.[49] Capital adequacy was fair and asset quality was satisfactory, as were earnings and liquidity ratios. By 2002, Equity had become a highly profitable institution that operated through 12 branches and 18 mobile units, with 107,000 depositors whose deposits totalled KSh1.6 billion and a loan portfolio of 18,000 borrowers worth KSh1 billion.[50] The activities of the microfinance institution had also become computerized. It had about 190 staff members, 7 directors, and 2367 shareholders. By the end of 2005, Equity had become the biggest bank in Kenya in terms of customer base, 13th-largest by capitalization and 14th-largest in terms of deposit base, and it was rated among the top five banks in the country by the CBK.[51] By 2010, Equity posted a profit before taxes of KSh9.04 billion, a 71 % increase from the previous year.[52] Equity also massively grew its customer base from 4.4 million in December 2009 to 7.8 million by June 2012.[53] This made Equity home to 57 % of all bank accounts in Kenya. Customer deposits also grew from KSh69.8 billion in 2009 to KSh104.4 billion in 2010.[54]

The East African Financial Services Sector

Several East African banks had to some degree adopted a regional business model motivated by factors like client demand, their own corporate structures, or by regional trade corridor opportunities. Two types of factors influenced the internationalization of East African banks—push

factors and pull factors. Push factors are circumstances in the home country that explain why banks decide to move beyond the borders of their home countries. Chief among them are declining opportunities in the home jurisdiction and regulatory requirements. Pull factors, in contrast, are opportunities in host countries that made it attractive for a bank to enter the new market. In other words, pull factors are the expected benefits that banks hope to reap by exploring foreign markets.

One of the most powerful push factors that propels bank expansion beyond home markets is (perceived) declining profit opportunities in the home economy, especially relative to opportunities in potential host markets.

The East African banks displayed a fair degree of operational integration not just within East African markets but all the way along the trade corridors to South Sudan and the eastern Democratic Republic of Congo.

Kenya-based banks led the regional integration in the East African Country (EAC) banking sector. About 11 multinational and Kenyan-owned banks used Kenya as a hub to expand their operations into the EAC region.

About four indigenous Kenyan banks had branches within the region. Kenya Commercial Bank (KCB), Equity Bank, Fina Bank and Commercial Bank of Africa had a total of 63 branches outside Kenya (16 in Tanzania, 31 in Uganda and 16 in Rwanda) in 2012. Ugandan and Tanzanian banks had no regional presence and operated exclusively in their home markets.[55]

- Since 2006 KCB had been expanding in the EAC region. It had 164 branches in Kenya and 36 branches in other countries in East Africa—Tanzania (10), Uganda (11), Rwanda (9) and South Sudan (6). KCB's Tanzanian operation was established in 1997 and is the oldest of its regional subsidiaries.
- In March 2009 Commercial Bank of Africa merged with First American Bank's Tanzanian subsidiary, United Bank of Africa (the bank has since been renamed Commercial Bank of Africa–Tanzania).
- Fina Bank began its regional expansion into Rwanda in 2004, and by 2009 it had a presence in Uganda with five established branches. The bank had a total of 11 branches regionally.[56]

A survey conducted by the World Bank Group to gauge the operational integration of banks operating in the EAC revealed that 56 % of the banks interviewed had their operations concentrated mostly in Kenya. Most of the banks surveyed had yet to achieve full integration of their operations in the region, but partial integration had taken place in the areas of information and communications technology, risk management, customer service, and treasury operations.[57]

Two-thirds of the banks surveyed stated that regionalization had facilitated the introduction of financial products and services that would not have been possible in the absence of scale. Establishment of a single licensing regime (which would remove barriers to entry posed by separate capitalization requirements for each subsidiary and enable cross-border branching) was favoured by a majority of the banks as a measure to promote integration.

The major impediments to attaining full integration cited by banks included the lack of a common tax regime, resistance from bank supervisors (particularly supervisors in Tanzania and Uganda, who were averse to banks under their jurisdiction being managed by Kenyan parents), IT connectivity problems (caused by weak physical infrastructure), differing regulatory requirements, restrictions on the mobility of labour, and the existence of differing capital movement polices within the EAC.

Prior to the implementation of a common trading platform, cross-listing of shares in the EAC had already` increased private capital flows within the region. The total market capitalization for cross-listed shares in the EAC region stood at about US$2.88 billion, with 99.84 % taken up by the Nairobi Securities Exchange and 0.16 % shared between the Dar es Salaam Securities Exchange and the Uganda Securities Exchange. All companies cross-listed and traded regionally were from Kenya. As at 2013 there were no cross-listings of companies based in other EAC countries. Kenya defined a local investor as an EAC citizen and allowed foreign participation of up to 75 %. Tanzania allowed foreign participation of up to 60 % of shares in primary or secondary issues. There were restrictions in Uganda and Rwanda.[58]

Unlike Kenya, Tanzania did not allow foreign participation in initial public offerings (IPOs). Rwanda and Uganda required that citizens seek approval from their central bank to buy foreign IPOs. Sale or issue of shares by foreigners was not restricted in Kenya, Uganda or Tanzania, but Rwanda required central bank approval. There were no restrictions for foreigners to buy debt instruments in Kenya, Uganda, Rwanda or Burundi. Tanzania, however, restricted purchase of government bonds but allowed foreign participation for corporate debt instruments.

Participation in EAC stock and bond markets was usually dominated by institutional investors, national pension funds, fund management firms and insurance companies. Information provided by Kenyan investment banks suggested that the participation of Kenyan investors in other EAC markets was about 10 %, whereas that of Ugandan investors in other EAC markets was between 2 and 5 %, and that of Tanzanian investors reached a maximum of only 0.5 %. Due to the lack of restrictions on capital flows from Kenya, a greater number of its retail investors participated in EAC markets. This was in contrast to Tanzania and Uganda, where mainly institutional investors participated.

Several factors resulted in a regionalization of financial markets in the EAC. The signing of the Common Market Protocol and the initiatives of the private sector banks together created a favourable climate for integration, especially between the three original members of the EAC. However, several factors, like the harmonization of legal and regulatory frameworks, the adoption of a single licensing regime, mutual recognition among regulators, absence of a regionally compatible financial infrastructure and homogenous cross-border supervision practices, still constrained the growth and integration of the regional market. To enhance integration of financial markets in the EAC region, the World Bank proposed a Financial Sector Development & Regionalization Project I (FSDRP I), comprising a three-year US$16 million regional technical assistance grant to the EAC to support the move towards a single market in financial services. The project development objective of FSDRP I was to establish the foundation for financial sector integration among EAC partner states.[59]

Equity's Internationalization Experience

Equity's internationalization was driven by the integration of the EAC region, the bank's pursuit of its pan-African strategic intent to be the champion of the socio-economic development of Africa, the bank's vision of increasing accessibility to financial services to the people of Africa, and its salient desire to contribute to the socio-economic prosperity of the people of Africa through provision of inclusive financial services to the unbanked and underbanked. Equity Bank was, however, a late entrant in the cross-border banking business and had to grapple with the challenge of conquering competition in the various international locations. Domestic banks in the target countries already had high market shares established by subsidiaries of South African and Nigerian banks that commenced internationalization before East African banks. Equity's main strength was its unique high-volume, low-margin business model and strong brand in the region

Equity was also desirous of diversifying its country risk, which was increased by the 2007/2008 post-election violence, by generating earnings from other countries. The low levels of financial inclusion in the Sub-Saharan region, with about 88 % of households in the region unbanked, established strong demand for financial services in the region.[60] Equity was already an exceptionally successful bank with a huge capital base. It was a renowned brand riding on the platform of a stable and scalable core banking system. Equity had a strong management team reputed for deploying its products and services through the various established channels and an effective board with strong oversight capabilities that greatly reinforced management's efforts. Underlying macroeconomic fundamentals and projections suggested that East Africa's GDP would continue to grow at an annual rate of not less than 5 % for the next five years.[61]

Equity's Management had initial reservations when James sold the idea of going international, as they felt their rich culture and time-tested business model would be unreplicable across the international subsidiaries. The management team and entire staff eventually gave their full support when they realized that the pan-African vision of Equity was not realizable if they remained in Kenya only. They also saw internationalization as an opportunity for the growth and advancement of their

careers as most senior managers in Equity transited to director and CEO positions in the various subsidiaries. Cultural difference problems were resolved by staff induction programmes in Kenya for all newly recruited subsidiary staff members and rotational secondments to the various core head office units to get a better feel for Equity's operations and a better appreciation of the bank's corporate culture.

Equity's internationalization started with the establishment of the Ugandan subsidiary for the following reasons:

- Uganda had larger unbanked and underbanked populations than Kenya.
- There was a relatively lower degree of financial sector sophistication than in Kenya and hence room for the replication of Equity's existing business model.
- Uganda's GDP growth rate averaged 1.75 % between 2006 and 2015, reaching an all-time high of 5.83 % in the first quarter of 2008 and a record low of −2.29 % in the second quarter of 2014.[62]
- Uganda was Kenya's number-one trading partner and had several business ties with Kenya. Many Kenyans studied at Makerere University in Uganda.
- The close relationship between the vision of the acquired institution (Uganda Microfinance Limited) "to become the leading and preferred micro finance service provider in Uganda" and that of Equity Bank "to be the champions of socio-economic prosperity of the people of Africa" provided a good fit between the two organizations.
- The EAC integration and common use of English as an official language in both countries and Equity's customers required a Ugandan branch. Many of Equity's customers expanded their businesses into Uganda.

Project Team

In 2009, when Equity decided to go international, the Regional Expansion Unit within the Projects Management Office constituted a taskforce for the establishment of each subsidiary. This team had members from the information and communications technology, human resources, finance, procurement, legal, systems audit, facilities

management, treasury and shared services departments. Most members of the taskforce were based in the head office and were senior members of staff that had spent a minimum of five years with Equity and had a very good grasp of Equity's values, systems and business model. The taskforce centrally co-ordinated and managed all project-type activities in the bank's subsidiaries, and each country expansion had an independent project team and project manager that managed the day-to-day implementation challenges. All project managers reported to the senior program manager in charge of regional expansion.

Staffing

Initially, most subsidiaries had experienced Equity staff seconded to them for the first six months to help build culture, set up systems and address most of the teething and start-up problems. Following the success of this initial approach, Equity instituted a more structured 6- to 12-month induction course in Kenya for new officers recruited from the host countries in order to help them internalize Equity's unique culture and business model. This induction course included classroom lectures and secondments to Equity's business units on a rotational basis. Newly recruited officers were always inducted in Kenya prior to their resumption in their subsidiary locations. Equity encountered language problems in Tanzania and Rwanda as most staff members were not fluent in English. Rwandese were more fluent in French, and Tanzanians were more fluent in Swahili in spite of the fact that English was Tanzania's main language of instruction. Language was not much of a problem in Uganda. To overcome language problems, most customer-facing staff were recruited from the host countries and thoroughly prepared to handle the business.

The dearth of skilled manpower in the various international locations posed serious challenges to Equity. Most countries in the East African region had a deficiency of skilled banking staff. Tanzania had stringent labour laws that prohibited cross-border labour flow. Equity overcame the

challenge of skilled manpower in countries like South Sudan by recruiting graduates directly from colleges and training them thoroughly. With the exception of Uganda, where the managing director was recruited from Standard Chartered Bank Ghana, Equity deployed all subsidiary managing directors (experienced senior business and development managers and heads of departments) from Kenya, mainly because they understood well the Equity Bank model and had strongly internalized the organization's culture. However, Equity had to hire locals to fill other top management positions to localize the brand and give the citizens of the country a feeling of ownership. The aim was to eventually phase out expatriates once credible and competent local staff understood the Equity Bank model.

Differences in language, culture, flexibility of work hours, work ethic, lunch hours and national values led Equity to develop a course called "Leading Across Cultures". This course greatly helped new hires in subsidiaries and seconded Equity staff appreciate the various cultural issues they had to navigate in the course of their work in the international locations. Such issues as cultural integration and key imperatives for success in international locations were extensively discussed. The similarities in the work ethic and national management culture of Rwanda and Kenya made the establishment of the Rwandan subsidiary and integration of cultural issues relatively easier. Equity's staff incentive structure was replicated in all international subsidiaries.

Due Diligence

Equity's acquisition of Uganda Microfinance Limited was facilitated by PricewaterhouseCoopers (which was recruited to conduct the due diligence) and FSI Capital Ltd (which was recruited to conduct the detailed credit assessment study). Equity encountered several cultural difference problems arising from differences in the work cultures of the banks and in the national management culture of Ugandans. It also had to grapple with several integration issues. For

the establishment of subsequent subsidiaries—South Sudan, Rwanda and Uganda—all the due diligence and country viability studies were carried out by Equity's regional expansion team and the research and product development team. The taskforce used the PESTEL and SWOT analysis in Fig. 9.16 to establish market feasibility. The central banks of the respective countries were very supportive of the bank's initiatives to bring more unbanked individuals into formal banking. Telecom companies in the region also provided connectivity and mobile money services.

The research and product development team worked with the taskforce for each new international subsidiary to conduct comprehensive market research on existing products, customer needs and likely channels in the new country before establishment. They also established likely geographic areas in the country that would be most receptive to Equity and included a branch expansion plan in all the economically viable states of the country. The research team continuously conducted competitor intelligence exercises to establish the nature and character of competition in the various international locations with a view to improving Equity's positioning at all times (Figs. 9.2, 9.3, 9.4, 9.5, 9.6, 9.7, 9.8 and 9.9).

Equity's legal team researched and hired local legal teams if need be to facilitate licensing and other regulatory compliance issues of new subsidiaries. As the home regulator, CBK introduced cross-border supervision and liaised with other country regulators for cross-border regulation under Basel II standards. CBK and the Kenyan Ministry of Finance issued letters of no objection to the target country regulator and Equity Bank for the establishment of any subsidiary. The approvals were obtained after applications for company incorporation, bank license, investment authority registration and tax personal identification number registration were concluded.

With the exception of Uganda, where entry was by the acquisition of Uganda Microfinance, Equity adopted a greenfield entry strategy for the subsidiaries in South Sudan, Rwanda and Tanzania.

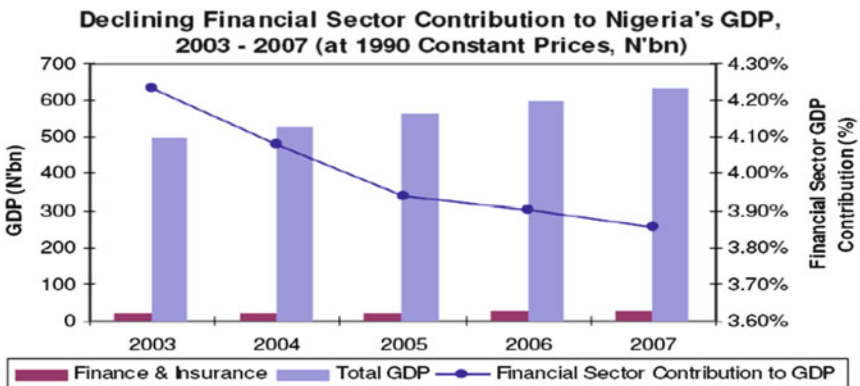


Fig. 9.2 Financial sector's contribution to Nigeria's GDP. *Source*: National Bureau of Statistics

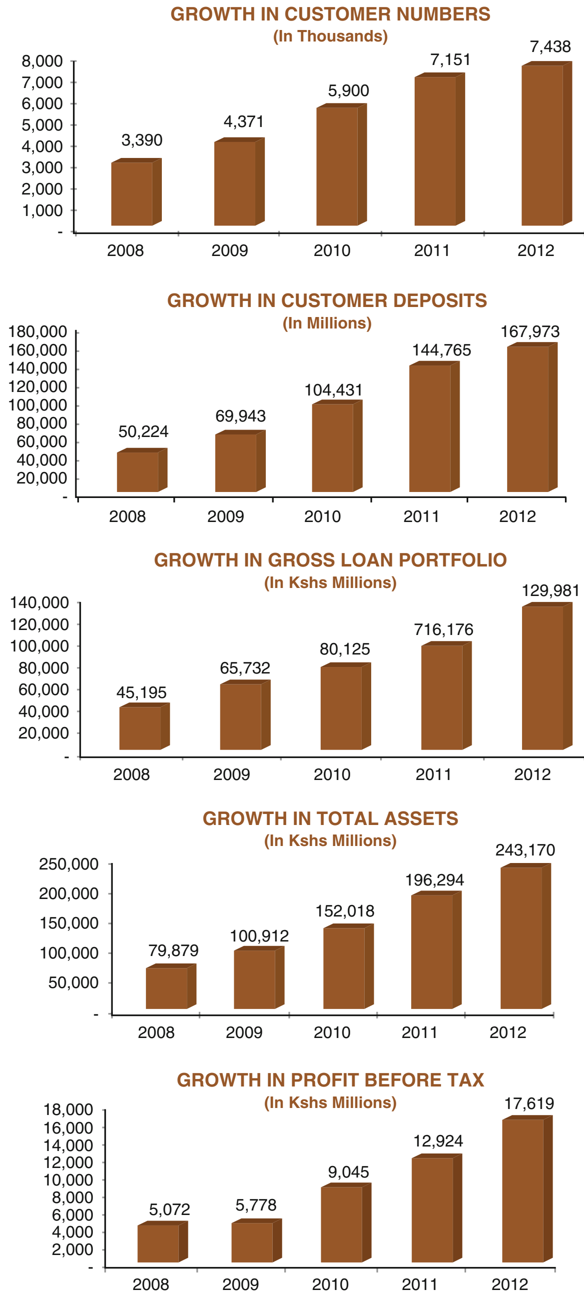


Fig. 9.3 Growth in customer numbers, deposits, gross loan portfolio, total assets and profit before tax. *Source*: Equity Bank Group Annual Reports and Accounts 2012

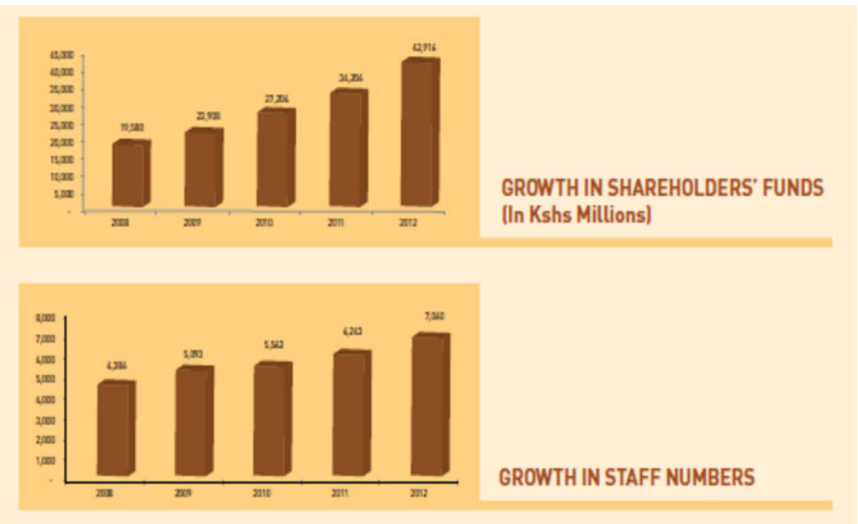


Fig. 9.4 Growth in shareholders' funds and staff numbers. *Source*: Equity Bank Group Annual Reports and Accounts 2012

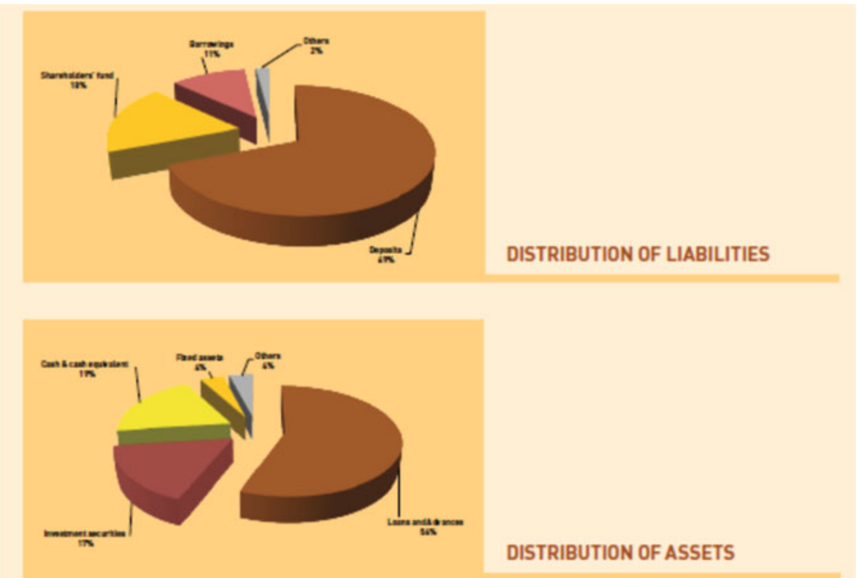


Fig. 9.5 Distribution of liabilities and assets. *Source*: Equity Bank Group Annual Reports and Accounts 2012

Purpose

We exist to transform the lives and livelihoods of our people socially and economically by availing them modern, inclusive financial services that maximize their opportunities

Vision

"…To be the champion of the socio-economic prosperity of the people of Africa.…"

Mission

"…..We offer inclusive, customer-focused financial services that socially and economically empower our clients and other stakeholders….."

Tagline

Your listening caring partner

Positioning

The Listening, Caring Financial Partner.

Motto

"… Growing together in trust…"

Core Values

- Professionalism
- Integrity
- Creativity and Innovation
- Teamwork
- Unity of Purpose
- Respect and dedication to customer care
- Effective Corporate Governance

Fig. 9.6 Equity Bank purpose, vision and mission

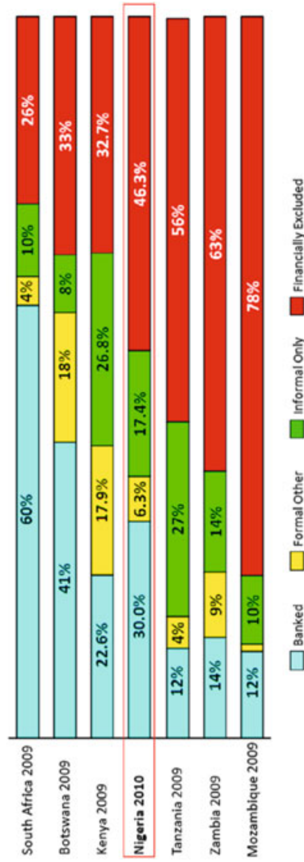
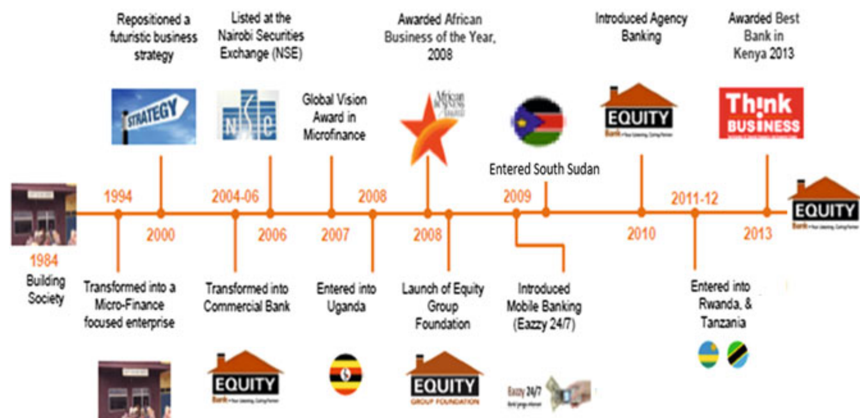


Fig. 9.7 2010 Financial Access Survey. *Source*: Adapted from EFINA's Financial Access Survey 2010—Cross Country Comparisons of Financial Inclusion



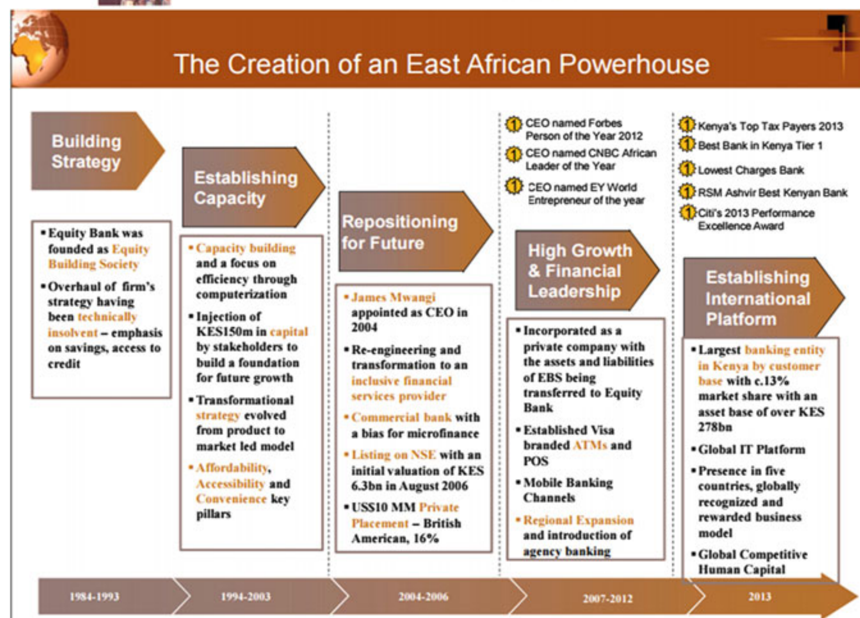


Fig. 9.8 Chronological evolution of Equity Bank. *Source*: Adapted from Equity's 2013 Investor Presentation

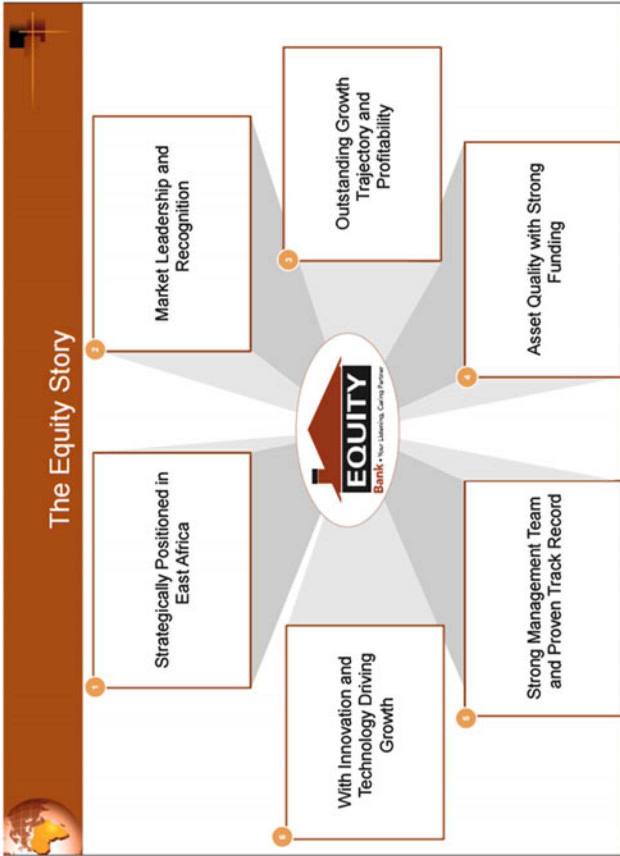


Fig. 9.9 The Equity story. *Source*: Adapted from Equity's 2013 Investor Presentation

Physical and Social Infrastructure

The quality of the physical and social infrastructures in other explored international locations was very similar to the situation in Kenya. Equity leveraged largely on its establishment experience for its Kenyan branches. Lack of a national identification system and land ownership titles in Tanzania affected delivery of credit services. Low gross literacy and financial literacy achievement levels required the bank to offer financial education programmes to its customers. In South Sudan, there was the need for credit guarantee mechanisms to crowd-in lending and effectively reduce the risk of lending. Financial intermediation was made more challenging in South Sudan by political instability; lack of effective treasury bill and bonds money markets; lack of a credit reference bureau; a small formal business sector (few companies registered); lack of a deposit insurance protection fund; and lack of regulatory guidelines for agency banking, mobile banking, and bancassurance. In Uganda there were relatively higher fraud levels as well as lack of regulatory guidelines for agency banking, mobile banking, and bancassurance. Rwanda and Tanzania had young credit reference bureaus.

Demand for Financial Services

There was a relatively high demand for financial services in East Africa as it was estimated that only 12 % of households in the region had access to such services.[63] The low levels of financial penetration and inclusion as well as very low percentages of loans to GDP in East Africa all provided strong evidence of the need for deepening financial services in East Africa.

Equity's skill in converting the unbanked helped it gain scale in every market it entered. This approach reduced time to market in all cases. Some competitor banks imitated Equity's product offerings but were unable to imitate Equity's ability to execute, and customer experience remained one of Equity's advantages.

Barriers to Entry

Most East African countries had relatively high minimum capital requirements. Zambia's high minimum capital requirement of KSh8 billion for a foreign subsidiary posed a difficulty for Equity in the establishment of a Zambian subsidiary.

Delays in processing and issuance of banking licenses in the various host countries hindered Equity's progress and substantially increased set-up time and time to market. In some extreme instances where delays were not anticipated, the Equity head office had to pay the salaries of over 100 staff members for over six months; these staff members were already trained and inducted but could not commence operations because issuance of the license was delayed for six months beyond the expected date.

Kenya was one of the most sophisticated economies in the region, and laws and policies for the conduct of agency banking were already in place. South Sudan had yet to enact an agency banking policy. Rwanda was able to issue guidelines in 2012, while Tanzania issued guidelines in 2013. This situation resulted in stunted growth of customer numbers and reduced profitability of the subsidiaries. A major regulatory hurdle Equity had to overcome was the labour law in Tanzania that restricted movement of labour into Tanzania. Equity sought and obtained the approval of the Bank of Tanzania to hire eight experienced managers to support the establishment of Equity Bank Tanzania. In South Sudan, United States sanctions on banking relations with Sudan (Khartoum) impacted Equity Bank negatively in areas such as delaying approvals for Citibank correspondent banking; SWIFT, Visa, American Express and MasterCard issuance; and customer acquisitions.

Products and Services

Equity at all times retained its microfinance model, which entailed standardized products customized to fit the circumstances of the international subsidiary. Equity typically started each subsidiary with payment products (cards, mobile money and internet payment channels), sav-

ings products and microloans. As the operations in a subsidiary gained scale with increased transaction volume and more customers, Equity introduced trade finance and treasury products. Equity had yet (as of 2014) to roll out insurance and investment banking services to customers outside Kenya.

The product development team constantly improved product bundles through market research results that revealed customer touchpoints and customer preferences in the various subsidiaries. Equity early on realized that a one-size-fits-all approach would be inappropriate because the circumstances, needs and peculiarities of each country required some form of customization of Equity's original model. There was also constant information flow between each subsidiary and the research and product development teams to fine tune product offerings and enhance their effectiveness.

Partnerships

Equity worked with the United Nations Capital Development Fund under the MicroLead programme to recognize milestone achievements and deepen financial inclusion and innovation in the subsidiaries. Other notable partners were Swisscontact and the Bill & Melinda Gates Foundation, both of which supported the various financial inclusion and corporate social responsibility initiatives of Equity Group in its various subsidiaries.

Equity's planned to roll out the Equity Foundation in all international subsidiaries to develop and implement the various host country corporate social responsibility (CSR) initiatives. The Equity Foundation also developed CSR programs that extended to other international locations.

Corporate Governance

Each subsidiary's board was well resourced with experienced executive and non-executive directors. Equity Group's board led the process of selection of directors for subsidiaries. Non-executive directors were typically sourced

from the host country's reservoir of business and community leaders who had distinguished themselves in their professional careers and proven their integrity. All board members were vetted before appointment, and the vetting took into account professional qualifications, integrity and track record. New board members had to pass the regulator "fit and proper test". Each board was relatively independent and was at liberty in some instances to undertake independent projects without recourse to the head office. An annual self-evaluation exercise of all directors in the subsidiaries was conducted, in line with international best practices. The evaluation focused on the role and responsibility of the board; its structure, composition, functions and processes; information and meetings; and other critical areas. The board structure and all relevant committees at Equity's head office closely resembled the board structure in each subsidiary, with slight customizations in line with the host country's code of corporate governance. Organization structures of the various subsidiaries were customized to meet the needs and circumstances of the host country and also to comply with local labour laws. Each subsidiary sent daily and monthly management and financial reports to Equity's head office. These reports complemented the monthly performance appraisals conducted by both internal and external auditors. Equity had to upgrade its management information systems infrastructure to enable it to monitor and manage the activities of the subsidiaries in real time.

Ownership

All subsidiaries were 100 % owned by Equity. Equity was cross-listed on the Nairobi Securities Exchangwe and the Uganda Securities Exchange. The future plan was to cross-list Equity's shares in established exchanges in countries hosting the international subsidiaries. Equity was instrumental to the injection of foreign direct investment into the different countries that hosted its international subsidiaries, with injection of over US$100 million in Uganda, Tanzania, South Sudan and Rwanda as at December 2013 (Tables 9.2, 9.3, 9.4, 9.5, 9.6, 9.7, 9.8, 9.9, 9.10, 9.11, 9.12, 9.13, 9.14 and 9.15). (Table 9.16 shows total foreign direct investment of Equity Group into all of its subsidiaries in 2013.)

Table 9.3 Macroeconomic indicators for Nigeria

Indicator	1990	1995	2000	2005	2010
GDP (current US$)	28,472,471,051	28,108,826,038	45,983,6000,313	112,248,609,250	193,668,738,107
GDP growth (annual %)	8.20	2.50	5.40	5.40	7.85
GDP, PPP (current international $)	99,836,294,288	127,142,551,468	161,081,163,566	244,642,093,041	377,146,064,036
GDP per capita (current US$)	292	256	372	803	1222
GDP per capita growth (annual %)	5.51	0.11	2.93	2.82	5.17
GDP per capita, PPP (current international $)	1023	1156	1302	1750	2381
Inflation, consumer prices (annual %)	7.36	72.84	6.93	17.86	13.72
Deposit interest rate (%)	19.78	13.53	11.69	10.53	6.52
Lending interest rate (%)	25.30	20.23	21.27	17.95	17.59
Interest rate spread (lending rate minus deposit rate, %)	5.52	6.70	9.58	7.42	11.06
Risk premium on lending (prime rate minus treasury bill rate, %)	0.00	7.73	5.77	10.32	13.74
Domestic credit provided by banking sector (% of GDP)	23.66	23.99	10.09	8.60	36.28
Official exchange rate (LCU per US$, period average)	8.04	21.90	101.70	131.27	150.30

(*continued*)

Table 9.3 (continued)

Indicator	1990	1995	2000	2005	2010
Exports of goods and services (current US$)	12,365,872,842	12,448,763,502	24,820,549,289	52,237,628,416	76,248,124,979
Imports of goods and services (current US$)	8,202,785,667	11,857,546,902	14,727,556,917	34,849,468,834	51,575,629,421
External balance on goods and services (current US$)	4,163,087,175	591,216,600	10,092,992,373	17,388,159,583	24,672,495,558
External balance on goods and services (% of GDP)	14.62	2.10	21.95	15.49	12.74
Market capitalization of listed companies (% of GDP)	4.81	7.23	9.21	17.24	26.27
External debt stocks, total (DOD, current US$)	33,438,924,000	34,092,471,000	31,354,920,000	22,060,054,000	7,882,519,000
Mobile cellular subscriptions	0	13,000	30,000	18,587,000	87,297,789
Mobile cellular subscriptions (%)	0.00	0.10	0.02	13.29	55.10
Internet users	0		79,261	4,962,548	45,039,711
Internet users (%)	0.00	0.00	0.06	3.55	28.43
Population, total	97,552,057	110,014,688	123,688,536	139,823,340	158,423,182
Rural population	83,116,181	67,218,974	71,120,908	75,224,957	79,528,437

Urban population	34,435,876	42,795,714	52,567,628	64,598,383	78,894,745
Population ages 0–14 (% of total)	44.81	43.94	43.13	42.82	42.81
Population ages 15–64 (% of total)	52.02	52.87	53.64	53.87	53.79
Population ages 65 and above (% of total)	3.16	3.19	3.22	3.31	3.40
Population growth (annual %)	2.51	2.36	2.38	2.48	2.52
Labour force, total	29,932,254	34,290,460	39,388,948	44,768,836	

Source: Adapted from World Bank macroeconomic indicators on Nigeria 1990–2010
GDP – Gross Domestic Product; LCU – Local Currency Unit

Table 9.4 Business growth and performance statistics of Equity Bank Uganda Limited in Ugandan shillings

Year	Dec 2009	Dec 2010	Dec 2011	Dec 2012
Deposits	71,568,612,233	138,882,063,052	167,284,801,451	178,879,223,930
Outstanding loans and advances	82,812,563,951	136,318,592,960	163,849,761,238	197,235,672,896
Total assets (net)	154,740,775,601	204,776,206,544	262,263,465,859	305,300,282,087
Pretax (profit/loss)	(6,978,719,661)	(22,861,827,563)	554,936,464	2,316,480,670
Cost to income ratio (%)	132.35	172.74	97.38	96.0
Return on equity (%)	–23.70	–49.88	2.50	4.13
Return on assets (%)	–7.10	11.68	0.42	0.57

Source: Equity Bank Group Annual Reports and Accounts 2012

Table 9.5 Business growth and performance statistics of Equity Bank South Sudan Limited in South Sudanese pounds

Year	Dec 2009	Dec 2010	Dec 2011	Dec 2012
Deposits	41,371,000	134,750,000	456,832,000	548,268,000
Outstanding loans and advances	5,366,000	21,850,000	61,597,000	135,970,000
Total assets (net)	75,262,000	201,359,000	621,707,000	675,710,000
Pretax (profit/loss)	(1,529,000)	11,540,000	12,827,000	37,882,000
Cost to income ratio	1.499	0.562	0.695	0.55
Return on equity (after tax, %)	−11	39	27	74
Return on assets (after tax, %)	−1.7	5	2.34	5

Source: Equity Bank Group Annual Reports and Accounts 2012

Table 9.6 Business growth and performance statistics of Equity Bank Rwanda Limited in Rwandan francs

Year	Dec 2011	Dec 2012
Deposits	4,341,315,000	15,889,958,000
Outstanding loans and advances	305,231,000	12,485,291,000
Total assets (net)	12,020,961,000	24,196,893,000
Pretax (profit/loss)	(419,096,000)	(1,690,345,000)
Cost to income ratio (%)	349	149
Return on equity (after tax, %)	−37	−34
Return on assets (after tax, %)	−21	−7

Source: Equity Bank Group Annual Reports and Accounts 2012

What Next?

Mary and her team had six months to come up with a market entry strategy document for Nigeria, but they had already submitted a preliminary findings report to the board. This report was going to form the basis for extensive deliberations at the board meeting. As her team began to get more information on the structure of banking in Nigeria, several key questions remained: What market entry strategy should Equity adopt for Nigeria? Was buying an existing bank more prudent, or was a greenfield entry preferable? Was a universal banking license better, or was a state microfinance

Table 9.7 Business growth and performance statistics of Equity Bank Tanzania in Tanzanian shillings

Year	December 2012
Deposits	38,323,905,000
Outstanding loans and advances	24,641,640,000
Total assets	76,218,766,000
Pretax (profit/loss)	(1,406,230,000)
Cost to income ratio (%)	116.90
Return on equity (after tax, %)	−4.43
Return on assets (after tax, %)	−1.50

Source: Equity Bank Group Annual Reports and Accounts 2012

Table 9.8 Equity bank operating segments

Operating segments	
Year	December 2012
Deposits	38,323,905,000
Outstanding loans and advances	24,641,640,000
Total assets	76,218,766,000
Pretax (profit/loss)	(1,406,230,000)
Cost to income ratio (%)	116.90
Return on equity (after tax, %)	−4.43
Return on assets (after tax, %)	−1.50

Source: Equity Bank Group Annual Reports and Accounts 2012

license more appropriate? How was Equity going to raise the required N25 billion required to open shop in Nigeria? What effects would the positioning in the industry have on Equity's brand? The Nigerian banking industry was more sophisticated than the Kenyan banking industry, so the innovation and product development teams would have to work harder to craft value propositions that would excite Nigerians. James stated:

> *The challenge in Nigeria is the banking culture is fairly strong. To operate in Nigeria, one requires a huge capital base in line with regulatory requirement. It's a huge market with a population of about 160 million people. But beyond meeting basic regulatory requirements, you need to open up a very big bank to be able to compete and in order to make business sense.*

Table 9.9 Equity Bank profit and loss as at 31 December 2012

2012						2011					
In millions of Kenyan shillings	Kenya	Uganda	Sudan	Rwanda	Tanzania	Total	Kenya	Uganda	Sudan	Rwanda	Total
Total assets	206,023	9978	19,656	3392	4122	243,170	167,587	9169	17,844	1694	196,294
Net interest income	22,123	985	488	167	201	23,964	15,659	853	(291)	2	16,223
Total operating income	32,181	1443	2425	423	355	36,827	25,642	21,351	1657	20	28,670
Total expenses	15,762	1386	1343	656	432	19,579	13,532	1332	1048	79	15,991
Profit before tax	16,591	57	1082	(233)	(77)	17,420	12,110	19	609	(59)	12,679

Source: Equity Bank Group Annual Reports and Accounts 2012

Table 9.10 Equity bank balance sheet as at 31 December 2012

		Group		Bank	
In millions of Kenyan shillings	Note	2012	2011	2012	2011
Interest income	8	30,848	19,339	28,497	18,376
Interest expense	8	(6884)	(3116)	(6385)	(2815)
Net interest income		23,964	16,223	22,112	15,561
Fee and commission income	9(a)	2301	2349	1809	2034
Net fee and commission income		2301	2349	1809	2034
Net trading income	9(b)	2090	2423	821	1274
Other operating income	10	8472	7675	7133	6598
Operating income before impairment losses		36,827	28,670	31,875	25,467
Net impairment loss on financial assets	11	(1608)	(1630)	(14,561)	(1533)
Operating income after impairment losses		35,219	27,040	30,419	23,934
Personnel expenses	12	(7172)	(6009)	(5905)	(5185)
Operating lease expenses	13	(1213)	(919)	(847)	(687)
Depreciation and amortization	14,15	(2316)	(1745)	(2018)	(1483)
Other operating expenses	16	(7269)	(5688)	(5589)	(4475)
Total operating expenses		(17,970)	(14,361)	(14,359)	(11,830)
Profit before tax and equity income		17,249	12,679	16,060	12,104
Share of profit of associates	17(a)	171	155	–	–
Profit before income tax		17,420	12,834	16,060	12,104
Income tax expense	18	(5340)	(2509)	(5063)	(2330)
Profit for the year		12,080	10,325	10,997	9774
Attributed to: Equity holders of the parent		12,080	10,325	10,997	9774
Earnings per share (basic and diluted)	29	3.26	2.79	2.97	2.64

Source: Equity Bank Group Annual Reports and Accounts 2012

Table 9.11 Equity Bank cash flow statement as at 31 December 2012

		Group		Bank	
In millions of Kenyan shillings	Note	2012	2011	2012	2011
Assets					
Cash and cash equivalents	19	45,134	35,282	35,467	
Loans and advances to customers	20(b)	135,692	113,824	122,410	106,486
Finance lease receivabl	20(c)	–	1	–	–
Investment securities	21	41,101	30,502	32,792	30,199
Amounts due from related parties	22(g)	2	124	983	1094
Other assets	23	7243	5038	6459	4707
Tax recoverable	18	5553	–	–	
Investment in associate	17(a)	1457	1366	1113	1260
Investment in subsidiary companies	17(b)	–	–	8204	6672
Property and equipment	9072	7592	6530	6044	
Prepaid leases	14(c)	292	29	4	4
Intangible assets	15	1415	1352	1123	1076
Goodwill	17(c)	887	887	–	–
Deferred tax assets	820	244	744	239	
Total assets	243,170	196,294	215,829	176,911	
Liabilities					
Deposits from customers	25	167,913	144,165	142,386	125,492
Tax payable	18	2365	487	2258	417
Other liabilities	27	3369	2565	2759	2186
Borrowed funds	26	26,569	14,792	25,755	13,769
Deferred tax liability	24	38	–	–	–
Total liabilities		200,254	162,009	173,158	141,864
Equity					
Share capital	28(a)	1851	1651	1851	1851

(*continued*)

Table 9.11 (continued)

		Group		Bank	
In millions of Kenyan shillings	Note	2012	2011	2012	2011
Share premium	28(b)	12,161	12,151	12,161	12,161
Retained earnings		25,088	17,719	24,308	17,974
Available for sale reserve	28(c)	(732)	(1062)	(732)	(1062)
Loan loss reserve	28(d)	603	521	454	420
Foreign currency translation reserve	28(e)	(603)	(529)	–	–
Revaluation reserve	28(f)	32	34	–	–
Other reserves	28(g)	(113)	(113)	–	–
Proposed dividends	28(h)	4629	3703	4629	3703
Total equity		42,916	34,285	42,671	35,047
Total liabilities and equity		243,170	196,294	215,829	176,911

Source: Equity Bank Group Annual Reports and Accounts 2012

Table 9.12 Loans and advances to customers as at 31 December 2012

		Group		Bank	
In millions of Kenyan shillings	Note	2012	2011	2012	2011
Cash flows from operating activities					
Net profit before taxation		17,420	12,834	16,060	12,104
Adjustments for:					
Depreciation	14	2016	1583	1734	1338
Amortization of intangible assets	15	300	162	284	145
Unrealized exchange (gains)/(losses)		(286)	63	(288)	(67)
Profit on disposal of property and equipment		(4)	(7)	(6)	(3)
Provision for non-performing loans	11	1608	1630	1456	1533
Share of profit of associates	17a	(171)	(155)	–	–
Dividends received	17a	(80)	(49)	–	–
Interest on term borrowings	8	1474	763	1508	806
Operating profit before working capital changes		22,277	16,824	20,748	15,807
Loans and advances		(23,476)	(37,159)	(17,380)	(36,118)
Other assets	(2205)		(1254)	(1495)	(1472)
Finance lease receivable		1	2	–	–
Customer deposits		23,748	39,734	16,893	30,289
Due from related parties		122	(16)	–	144
Other liabilities	804		(151)	573	(73)
Cash generated from operations		21,271	17,980	19,339	9577
Income taxes paid	18	(4002)	(2875)	(3728)	(2747)
Net cash generated from operating activities		17,269	15,105	15,611	6830
Cash flows from investing activities					
Purchase of property, equipment & prepaid leases	14	(3782)	(2225)	(2236)	(1689)
Purchase of intangible assets	15	(363)	(473)	(331)	(467)
Proceeds from sale of property and equipment	14	27	25	22	4
Investment in subsidiaries		–	–	(1532)	(1588)
Dividends received		80	49	–	49

(*continued*)

Table 9.12 (continued)

		Group		Bank	
In millions of Kenyan shillings	Note	2012	2011	2012	2011
Purchase of investment securities	21	(25,893)	(22,546)	(17,091)	(22,248)
Proceeds from sale of investment securities	21	15,625	23,959	14,829	23,888
Net cash generated from/ (used in) investing activities		14,306	(1211)	(6339)	(2051)
Cash flows from financing activities					
Dividends paid	28(h)	(3703)	(2962)	(3703)	(2962)
Proceeds from long-term borrowings		13,581	8096	13,745	7502
Repayment of long-term borrowings		(1804)	(1267)	(1759)	(1197)
Interest paid on long-term borrowings	8	(1474)	(763)	(1508)	(806)
Net cash flow generated from financing activities		6600	3104	6775	2537
Net increase in cash and cash equivalents		9563	16,998	16,047	7316
Effect of foreign exchange differences	323	(63)	290	67	–
Effect of foreign currency translation reserve on cash and cash equivalents	(34)	(156)	–	–	–
Cash and cash equivalents at the beginning of the year	19	35,282	18,503	19,130	11,747
Cash and cash equivalents at the end of the year	19	45,134	35,282	35,467	19,130

Table 9.13 Chronological evolution of the Nigerian banking industry

Year	Key events
1986	• 36 licensed banks • Inception of structural adjustment program
1990	• Entry of numerous small players • 109 registered banks • Introduction of prudential guidelines
1991	• 120 registered commercial and merchant banks • 45 % devaluation of the Naira • Minimum paid-up capital required for commercial banks: N20 million • Minimum paid-up capital required for merchant banks: N12 million
1992	• 6 banks distressed and taken over by the NDIC
1992 (cont'd)	• Minimum paid-up capital required for commercial banks: N50 million • Minimum paid-up capital required for merchant banks: N40 million • Official inflation at 57 % and yield on 90-day treasury bills at 18 % • 90 % gap between interbank foreign exchange market (official) and bureaux de change exchange rates • Establishment of Nigeria Inter-Bank Settlement System • Exchange rate of N17.3/US$1
1993	• 120 licensed banks: 80 solvent banks, 30 banks considered by CBN to be distressed, 4 banks in liquidation and 6 banks taken over by NDIC • Parallel market premium of 70 % over official exchange rate • Official inflation at 60 %; interbank rates top 100 % • Prime lending rates of commercial and merchant banks at 33 % and 66 %, respectively • Exchange rate of N22/US$1
1994	• 120 licensed banks: 4 banks in liquidation, 6 banks sold to the CBN for N1, 66 solvent banks, 44 financially distressed banks • Official inflation of 57 %; treasury bills issue rate fixed at 14.5 % • Exchange rate of N21.9/US$1

(continued)

Table 9.13 (continued)

Year	Key events
1995	• 115 licensed banks: 12 banks acquired, 43 financially distressed banks, 60 solvent banks • Official inflation of 73 %; lending rates fixed at 21 %; deposit rates range between 12 % and 15 % • Exchange rate of N70/US$1
1998	• 115 licensed banks: 26 banks in liquidation, 89 operational banks in the system comprising 51 commercial banks and 38 merchant banks • Minimum paid-up capital for all banks increased to N500 million with March 1999 set as deadline • Official inflation at 10 %; treasury bills issue rate at 20 %
1999	• New banks required to have minimum paid-up capital of N1 billion • Exchange rate of N95/US$1 • Capital requirement for existing banks remains unchanged at N500 million
2000	• Introduction of universal banking
2001	• 4 new licences and 2 approvals-in-principle issued • 8 banks recapitalized and restructured • minimum paid-up capital requirement increased to N2 billion for new banks; existing banks still have minimum capital requirement of N1 billion
2002	• 90 licensed banks: 79 solvent banks and 11 distressed banks
2003	• 90 licensed banks: 78 solvent banks and 12 distressed banks
July 2004	• Number of licensed banks drops to 89 with the revocation of the licence of Peak Merchant Bank; 11 of the 89 banks are distressed • Minimum capital requirement raised to N25 billion with 31 December 2005 deadline

Source: Agusto & Co. 2005 Industry Report (Banking)
NDIC – Nigeria Deposit Insurance Corporation

Table 9.14 Number of branches and outlets in Equity's international subsidiaries as at December 2013

Business drivers	Kenya	Uganda	S. Sudan	Rwanda	Tanzania	Totals
No. of employees	6484	580	258	278	188	7788
No. of branches	159	31	12	9	6	217
No. of agents	9557	0	0	570	133	10,260
No. of ATMs	516	31	18	12	7	584
No. of customer accounts	7,392,479	513,212	126,392	306,288	68,299	8,406,670

Source: Equity Bank Reports 2013

Table 9.15 PEST criteria grid

Political factors	Social factors
• EAC regional integration • Governance • Legislation and regulations • Country risk ranking	• Cultural differences • Management philosophy of the host country • Literacy level • Poverty level • Employment • Food security • Demographic profile
Technological factors	**Economic factors**
• Telecommunications: Mobile and internet penetration rates • Depth of telecommunication services supply • Mobile money penetration	• GDP per capita and GDP growth • Cost and ease of doing business • Currency exchange rate stability • Cost of capital • Interest rate regime (cr, Dr,interest spread) • Foreign exchange reserves/import cover • Balance of trade, current account deficit • Fiscal Policy and Budget Deficit • Credit rating of the country

Mobile Money Penetration refers to the percentage of adults who use the Mobile Money service compared to the total adult population
PEST – Political, Economic, Social and Technological Factors

Table 9.16 Equity's total foreign direct investment into subsidiary companies

Equity Bank foreign direct investment (FDI) as at 31 December 2013					
Country	Subsidiary	Cumulative capital injected by Equity Bank Group	Central bank or national regulatory authority	Central bank minimum capital/FDI requirement	% Equity Bank FDI above minimum capital
Uganda	Equity Bank Uganda Ltd	US$45,574,713	Bank of Uganda	US$9,601,814 (UGX25 billion)	374.65
South Sudan	Equity Bank South Sudan Ltd	US$29,160,920	Bank of South Sudan	US$3,000,000	872.03
Rwanda	Equity Bank Rwanda Ltd	US$16,988,506	National Bank of Rwanda	US$7,274,176 (RWF5 billion)	133.55
Tanzania	Equity Bank Tanzania Ltd	US$16,459,770	Bank of Tanzania	US$8,978,280 (TSh15 billion)	83.33

UGX – Ugandan Shillings; RWF – Rwandan Francs; TSH – Tanzanian Shillings

Notes

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