A Study of the Present State of Corporate Governance in Zimbabwe's Banking Industry

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Research paper presented to the Graduate school of Business leadership,
in partial Fulfillment of the requirements for the
Degree in Masters in Business Leadership
University of South Africa

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30 November 2005

Harare

Foreword

Poor corporate governance in Africa, Zimbabwe included, has been cited as one of the key problems preventing Africa from developing to its potential. Moreover corporate governance is an issue that has rocked business around the world over the past few years. There are limited studies written and published in Zimbabwe on corporate governance. The idea behind this research is to add to the body of knowledge available in Zimbabwe on corporate governance issues zoning in on the banking sector.

Acknowledgements

Firstly I would like to thank my study leader Professor Piet Nieuwenhuizen for his help. The successful completion of this research paper would not have been possible without his help and guidance. I would also like to thank the staff at Pricewaterhousecoopers library and the Zimbabwe stock exchange for their help.

Mom and Dad for always encouraging me to persevere when times were hard. I could never have asked for better parents. I would also like to thank my siblings, Tawanda, Junelle, Priscilla for their love and encouragement. Lastly but not least I would like to thank God for being my inspiration and giving me a reason to live.

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Abstract

The objective of this research paper was to examine and evaluate the contemporary state of corporate governance in Zimbabwe's listed private banking industry. This paper avails itself mainly to the case study method of research based on careful examination and evaluation of the relevant literature, inclusive of financial statements and reports on the matter. People knowledgeable about the subject were interviewed and a self administered questionnaire was completed in the presence of the researcher.

This research is of particular interest to Zimbabwe due to the turbulent socio-economic environment which has exposed banks to many risks and challenges requiring the continuous innovation of ways to manage business and its associated risks in order to not only remain competitive but to survive. After a series of corporate scandals and a general decline in the performance of banks in 2003/2004, the role of an empowered independent board has never been more important.

Prior to 2003 there was no capital market regulator in Zimbabwe but more recently the Reserve Bank of Zimbabwe has assumed that role. The Reserve Bank introduced corporate governance guidelines which were incorporated into the banking act in 2004, largely in response to a number of major corporate and accounting scandals. Prior to the act being introduced the listed banking institutions complied with the Second King Report of South Africa.

On paper the state of corporate governance in Zimbabwe's listed banks is of a good standard compared to other countries in Africa. Zimbabwe, however, has political and economic problems that affect the quality of governance. The government interferes with the market by pegging the Zimbabwe dollar at unrealistic rates. This has resulted in a parallel foreign exchange market that has caused hyper-inflation.

The areas surveyed by way of questionnaire and interviews to determine the state of corporate governance in Zimbabwe's listed banks were share ownership and responsibility to shareholders, board of directors' structure, composition, function and efficiency, external auditors function with respect to governance, communicating with stakeholders and financial performance in the five year period under review.

The following main issues came out of the investigation

- Investors should take a more active role in the governance of banks, as this would help with the maintenance of best practices in corporate governance. Shareholder activism is one such way of taking an active role.
- The compositions of the board of directors were quite impressive. The pool of directors is knowledgeable, educated and provide varied input in the running of the banks. All the boards had sub-committees to concentrate on identified risk areas as recommended by the King Report.
- The presence of executive directors in audit committees and remuneration committees was cited as affecting the quality of decisions taken in these meetings.
- The owner managed banking institutions (listed banks were CEO's had a significant shareholding i.e.10% or more) were cited as having more corporate governance problems than those that are not owner managed. The problem has been addressed by the Reserve Bank corporate governance guidelines which prohibit owners with a 10% shareholding or more from being directors of the bank.
- There appears to be a relationship between failed banking institutions and founder member, owner managed banking institutions.

Corporate governance and effective vigilance by the board is a critical component in dealing with problems that result in corporate failure, but in many

instances boards are inefficient. Another problem with boards is that there is often weak interaction between board members.

Banks are expected to identify and remedy deficiencies before material misstatements occur in financial statements. The capital markets regulator has increased resources to monitor the financial institutions more. Over time we will see fewer incidences of fraud. The Zimbabwean financial sector will emerge stronger from the present financial crisis. The banks that survived have built stronger internal controls and more effective corporate governance policies. The challenge they continue to face is a harsh economic, social and political environment, which is likely to continue to have a negative impact on profits.

CHAPTER ONE

Hypothesis and Method of Investigation

1.1. Background to the study

The objective of this research paper is to examine and evaluate the contemporary state of governance in Zimbabwe's listed private banking industry. This is of particular interest considering the turbulent economic, social and political environment which has exposed banks to new risks and challenges requiring the continuous innovation of ways to manage business and its associated risks in order to not only remain competitive but to survive. After a series of corporate scandals and a general decline in the performance of banks in 2003/2004 the role of an empowered independent board has never been more important. 'Corporate governance which can be defined as the system by which corporations are directed, controlled and held to account,'[1] has become an issue of great significance in Zimbabwe.

Similar studies have been done in many countries of the world inclusive of a number of African countries. However the studies done on Zimbabwe so far were more general in that they considered Zimbabwe in the African context. This paper expands on the existing literature on governance in Zimbabwe by zoning in more pertinently on the banking sector of the country.

Public confidence in the financial affairs of a country is the cornerstone of a stable banking system. As the custodian of the public funds, the management of a banking

[1] Corporate governance and the corporate sector in Zimbabwe, 2/5/2004, Financial Gazette, www.fingaz.co.zw

institution must exhibit impeccable integrity and professionalism in their conduct so as to engender public confidence in the safety of their deposits. With the broadening and deepening of a country's financial infrastructure, the need for an effective board of directors to assume full responsibility for the overall management of each and every banking institution is more crucial now than ever before.[2]

Because of a bank's special position of trust in the national economy, corporate governance is a matter of paramount importance. Banks are highly leveraged institutions, with most of their funds coming from depositors and creditors. They provide basic financial services to the public, financing to commercial enterprises, and access to the payments system. Increasing globalisation of financial markets, emergence of conglomerate structures, technological advances and innovations in financial products have added to the complexity of risk management in the banking sector. For these reasons, the quality of corporate governance expected of banking institutions is high.[3]

1.2. Socio- economic and political environment in Zimbabwe[4]

Zimbabwe had one of the most advanced and diversified economies in Sub-Saharan Africa. Per capita GDP in 1990 was nearly $2000(purchasing power parity equivalent), sixth highest in Sub-Saharan Africa. Zimbabwe's manufacturing sector accounted for 26% of GDP in 1990, a level comparable to that in South Africa and substantially higher than most other African countries. Other industrial activities, particularly mining, also contribute a substantial share of GDP (14% in 1990), while agriculture accounted for 13% of GDP in 1990. The manufacturing sector is quite diversified in Zimbabwe, producing about 7000 different products (Riddell (1998)).

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[2] Reserve Bank of Zimbabwe, Corporate Governance guidelines, 2005
[3] Reserve bank of Zimbabwe, Corporate Governance Guidelines, 2005
[4] The information, facts and figures have been obtained by the United Nations report of the fact finding mission to Zimbabwe to assess the scope and impact of "Operation Murambatsvina"

Less than one third of the labour force is employed in the formal sector (commercial agriculture, industry, government, trade and commerce, education, health and finance), with most of the remainder employed in agricultural activities in the communal areas. Incomes are substantially higher in the urban and formal sectors than in the rural and informal sectors.

Zimbabwe is currently going through an economic crisis which started in the late 90's and has continued to deepen. At independence in 1980 the country already suffered from a large fiscal deficit, low economic performance, unemployment, price controls, and a lack of foreign currency. The Smith regime was under economic sanctions during their reign and was heavily subsidized mainly by South Africa. It led to a relatively self-sufficient economy, which after independence and liberalization of the economy and the loss of the subsidy, became unsustainable.

The post –independence government realised that the extensive system of controls it used to regulate the economy was constraining its ability to realize its potential growth. Since most investments require imported capital equipment, spare parts and often imported raw materials, foreign exchange controls were a severe constraint on investment and production. Interest rate restrictions and the growing inflation led to negative real interest rates during most of the 1980's, limiting the ability of the financial system to mobilize savings and allocate capital efficiently. Wage and price controls contributed to unemployment and shortages of goods while investment regulations inhibited firms' ability and willingness to expand into potentially profitable areas. Rapid growth in government spending and the rising budget deficit contributed to growth in aggregate demand and in domestic credit, causing more inflation and crowding out of private investment by government borrowing. In response to these problems the government initiated a series of policy reforms beginning in 1988. In 1991 the government initiated a bold five year plan for liberalizing the economy. The plan provided for the fiscal and monetary policies, trade and foreign exchange liberalization, and deregulation of the domestic

economy. The plan sought to mitigate the adverse impacts of the adjustment program on vulnerable groups. By mid 1994, substantial progress had been made toward most of these goals but in large the Economic Structural Adjustment Program (ESAP) failed and led to massive retrenchment, closure of many manufacturing industries, general price increases and the deterioration of the social services [5].

The liberalization of the economy, led to the gradual but systematic decline of the formal economy and to the growth and emergence of the informal sector, especially in the rapidly growing towns and cities of Zimbabwe. There are mainly four factors that deepened the economic crisis in the late 90's, three of which were political;[6]

- The government embarked on an exercise to appease war veterans by giving them cash handouts. This caused run-away inflation which has never been contained since.
- Costly military intervention in the DRC war, which caused budgetary constraints to the government of Zimbabwe, and an ever increasing fiscal deficit.
- "Fast track" land redistribution program and persistent drought, which resulted in the agricultural production of the commercial farming being reduced by 80%. The country currently produces 20% of agricultural outputs it used to produce before the land redistribution program (Fingaz, 2005).
- Failed ESAP (Economic structural adjustment program).

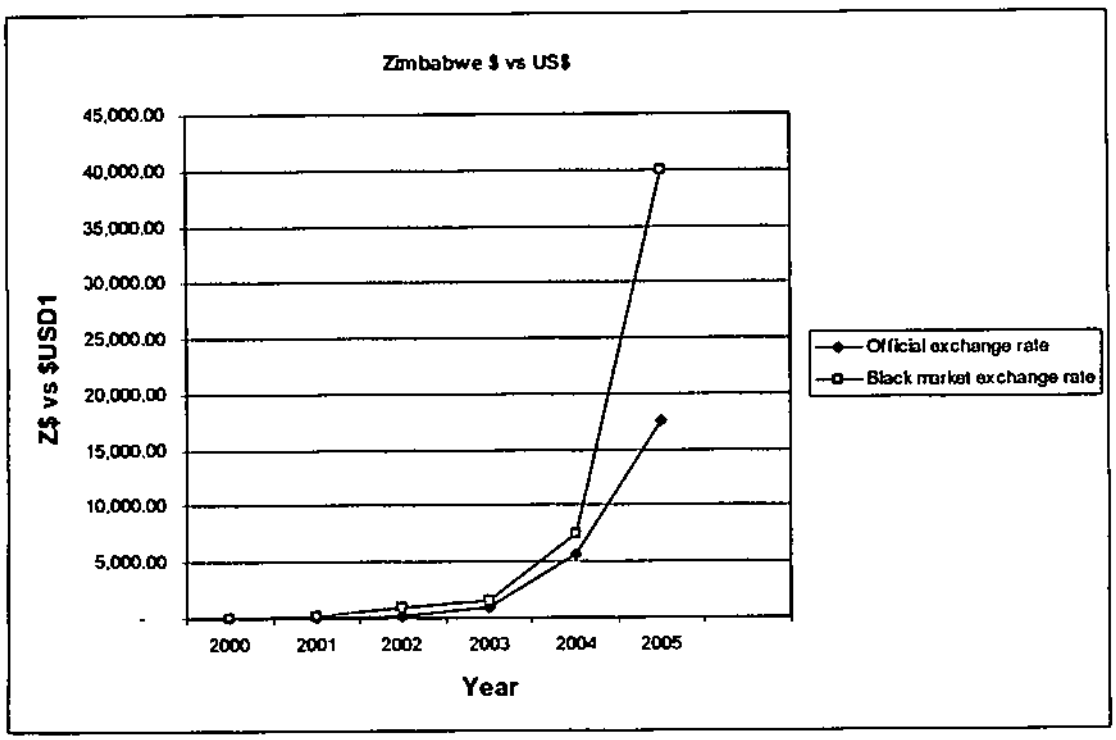
Some of these factors prompted sanctions, which affected the tourism industry. The economy has been on a downward spiral since then, registering growth of 0.9% in 1998 and -7% in 2004 and an expected -7% in 2005. Inflation is currently at 140 and a domestic debt of $1billion US. Unemployment is currently 75%.

[5] Tibaijuka, A (2005)
[6] Tibaijuka, A (2005)

The rise of the foreign currency parallel market is due to foreign currency shortages caused by the decline in agricultural, mining, and manufacturing exports, decline in tourism, and lack of foreign direct investment excercabated by the relunctance of the government to devalue the Zimbabwe dollar. The government pegged foreign currency exchange rates at unrealistically low levels. The parallel market is governed by market forces of supply and demand and is responsible for the free fall of the Zimbabwe dollar. Transactions were being carried at rates that are at least three times more than the official rate on the parallel market, in contravention of the law, but by 2001/2002, the currency parallel market was the only operating foreign exchange market. Banks began to participate in the parallel market especially the locally owned banks. The rate at which the Zimbabwe dollar was depreciating became an opportunity for many to profit from arbitrage. This unfortunately caused the dollar to depreciate even faster. Goods were priced according to the rate on the parallel market because all businesses procured their foreign currency on the parallel market. This contributed greatly to the upward spiral in inflation. By December 2003 inflation was 600%. It was impossible to procure foreign currency from the bank at the official exchange rate. In the meantime, the Reserve Bank of Zimbabwe continued to peg the Zimbabwe dollar at an unrealistic rate.

The graph below shows the disparity between the official and parallel market for the past five years. Also included below is a table showing inflation figures from 1985-2005 as well as the rate of growth/decline in the GDP. The exchange rate on the official market depreciated by 17892% in the five years between 2000 and 2005 on the official market. The depreciation on the parallel market was even more. This is the period of the greatest decline in the economy. Year on year inflation also rose from 55% to 140% in the same period and the economy shrunk by a cumulative 14%. The GDP per capital declined from USD1986 to below USD1000 in 2005 reflecting the magnitude of the economic decline in real terms. The GDP per capita is estimated at USD200 as at October 2005.

Figure 1 Greph showing foreign currency parallel market rate vs official market rate



Source is The Sunday Times, South Africa

Exchange rates, inflation and per capita income trends, Zimbabwe, 1985-2005

Table 1

	1985	*1990*	*1995*	*2000*	*2005*
Z$ to 1 USD	1.64	2.64	9.31	55.07	9896
Inflation %	8.49%	17.38%	22.59%	55.86%	140%
GDP per capita	1995	2099	1988	1986	<1000
% GDP growth Per capita	*3*	*4*	*-2*	*-7*	*-7*

Source: UNHABITAT, Global report 2003, Financial Gazette, IMF

A key function of The Reserve Bank is the maintenance of the internal and external value of the Zimbabwean currency. The Bank is responsible for the formulation and implementation of monetary policy, directed at ensuring low and stable inflation levels. The Bank has limited autonomy from Government. The Minister of Finance has wide powers to issue general policy directions to both the Board of the Bank and the Governor. The Reserve Bank Act specifies a number of functions which the Bank carries out. Chief among these is the maintenance of price stability, the formulation and execution of monetary policy and the fostering of a stable financial system. The formulation of exchange rate policy is a function of the Government.

The Reserve bank failed to control the foreign exchange market because there are some economic fundamentals that need to be addressed. For as long as there is insufficient exports and lack of foreign direct investment to deal with the balance of payments, there will always be a deficit on the current account. Demand for foreign currency will always exceed supply, because there are more goods being imported than being exported. The current account will bleed until exports and foreign direct investment increase significantly. As a result it is hard to get rid of the parallel market, for as long as people cannot get foreign currency on demand they will purchase it from the parallel market which is a ready market determined by market forces. On the other side of the coin the Reserve Bank of Zimbabwe cannot let market forces determine the official exchange rate as it will never stop sliding which can lead to a valueless currency and runaway inflation. Unfortunately this is exactly what is happening because of the existence of a parallel market.

The essence of Zimbabwe's monetary problem has its origin in the loss of the unit of account and asset functions of the currency, the Zimbabwe dollar, as a result of the rampant rate of inflation. Zimbabweans have only one dominant desire, namely to get rid of the currency by fleeing into real assets as fast as possible. The implications for the banking industry and the normal functions of money as a readily

acceptable medium of exchange are obvious. Monetization takes place when the non-bank sector sells assets which are not money to the banking sector, and a self liquidating process occurs as debt arrangement with the bank comes to fruition.

1.3. The banking industry in Zimbabwe

The range and number of financial institutions operating in Zimbabwe is impressive by African or even developing countries standards (Fafchamps, Pender &Robinson 1995).

The financial sector consists of several layers of institutions, inclusive of the the Reserve Bank of Zimbabwe, the commercial banks, the merchant banks (also called accepting houses), finance houses, discount houses, building societies, institutional investors, the development finance organizations, the Post office Savings Bank, and the Zimbabwe Stock Exchange. Financial activities are also assisted by credit insurance and credit reference institutions.

Prior to the sanctions in 2001/2002, the African development bank and the IFC were active in Zimbabwe. However, they have since scaled down their activity to almost nil. In the period after independence from 1980-1990 four commercial banks dominated the scene in terms of loans that they made to and from the public, Standard Chartered bank, Barclays bank, Commercial Bank of Zimbabwe, Zimbank. In the following decade many locally owned banks were founded, supported by the black empowerment drive which is typical in any African country after independence. Many locally owned listed banks emerged, Trust, NMB, Century, Kingdom, Barbican, Royal, Metropolitan, First Bank Corporation and a regional bank African Banking corporation and many smaller ones. By December 2003 there were 7 locally owned listed banks and they were dominating the retail banking sector, which was previously dominated by foreign owned banks like British Barclays Bank, and Standard Chartered Bank. Many more privately owned banking institutions also

emerged in this period. However this study is limited to the listed banks but reference will be made to the privately owned banks as well. There are some foreign owned banks that operate in Zimbabwe but are listed only in their countries of origin. These banks are outside the scope of this study.

The banking Act provides for the registration and regulation of persons conducting banking business and financial activities in Zimbabwe and establishes a deposit protection scheme to protect depositors in the event of the insolvency of a financial institution. The Act specifies "undesirable methods of conducting business " and provides for the cancellation of registration of the institution , inter allia, breaches any provisions of the banking act, misrepresents the facilities which it offers to the public, engages in banking activity that is not specified in its requisition certificate, or it can no longer provide adequate security for the assets entrusted to it.[7]

The Reserve Bank of Zimbabwe has a bank supervision function whose primary objective is to fulfill the responsibility relating to the safety and soundness of individual banks, placed on it by the Banking Act with the aim of strengthening, but not ensuring, the protection of depositors in banks. The Banking Act and The Banking Regulations of 2000 clearly set out the Bank's prudential supervisory task. The Act empowers the Bank to license banks, in concurrence with the Registrar of Banks and other Financial Institutions. The Act and the Banking Regulations 2000 specify minimum criteria which need to be fit and proper persons, that the business of banking can be conducted in a prudent manner and that it be carried out with integrity and skill.[8]

In September 2003, a new Central Bank Governor was appointed. In December 2003 he announced a monetary policy that was to rock the financial sector. Interest rates were increased from 150% to 600%. The exchange rate was devalued, and

[7] Code of Corporate Governance best practices in Zimbabwe 2001
[8] Reserve bank of Zimbabwe website, www.rbz.co.zw

new measures were put in place to bring back foreign currency into the official market. Banks were thrown into a liquidity crisis. The traditional banks that had good liquidity management and a conservative approach to business gained from the crisis. As rumors circulated of possible collapses of certain institutions, capital flights excruciated the liquidity situation at the younger trendy banks. Depositors fled in thousands and went to the traditional banks who where viewed as a safe haven. These banks were mainly foreign owned or government owned and were conservative and observed the law in terms of foreign exchange regulations. The newer banks were more daring and did not observe the foreign exchange act or the banking act scrupulously. The laws governing the banking industry especially the foreign exchange act was often perceived as unreasonable.

By early 2004, many of the banks were literally on their knees with acute cashflow problems and large interest burdens. Many banks were illegally investing in property and long term financial assets, resulting in a mismatch of assets and liabilities. Because of the investments in long term assets they were not liquid enough to meet short term obligations. Long term assets lost value, especially property and foreign currency assets as the exchange rate slipped resulting in losses in those banks. The traditionally conservative banks came out of this unscathed.

Prior to its collapse in 2004, Trust Bank had a 25% of the market share of deposits and had become the largest commercial bank in Zimbabwe. NMB, Century and Kingdom were doing well sharing a large stake of the remaining market share. By 2003, the local banks were dominating the retail banking sector. They were popular due to their ability to provide scarce foreign currency to companies to procure raw materials. These banks were not afraid to procure foreign currency of the parallel market which was an illegal market.

A shortage of Zimbabwe bank notes has been experienced since November 2002. Though official inflation to 30 April 2003 was about 270% (with the unofficial rate considered to be at least double this), Central bank has not been able to print sufficient money to satisfy the demand because of the shortage of foreign currency required to finance the printing of bank notes. Local currency shortages have had a ripple effect: the shortage of bank notes at the banks themselves meant that individuals and organisations were not depositing cash. The banks were in turn, compelled to solicit cash from individuals and organizations such as commuter transport operators, supermarkets and petrol filling stations and were prepared to pay a premium to get them. It is not realistic to expect banks that are involved in these sorts of activities to be at the centre of controlling good corporate governance. It is illegal in itself for banks to obtain bank notes at a premium and such transactions had to be concealed from the authorities. This becomes a predicate offense, especially in cases where the banks have to use the money in order to obtain scarce foreign currency on the illegal parallel market.

The turbulence that hit Zimbabwe's financial sector, which was flying at high altitude, started to subside towards the end of 2004 and in 2005. Banking institutions long considered to be conservative have shown that there is life after the crisis. The traditional banks released results that were excellent for the years ending December 2003 and December 2004. "The heady days of innovation and financial gymnastics that typified Zimbabwean finance sector were over and margins simply plummeted."[9] The hierarchy has been restored as depositors who had deserted the conservative traditional banks for the trendy indigeneous ones swung back in their thousands. While most indigeneous banks balance sheets which had swollen considerably particularly in the past two years were trimmed both at the instigation of the Reserve bank of Zimbabwe and as a result of depositor flight, traditional banks witnessed a significant growth in assets.

[9] Banya, N (2004)

Barclays in the last few years drastically reduced its branch network. The bank which is 64% owned by British Barclays Plc, posted a solid set of figures for the crisis years ended 2003 and 2004. All the banks that were liquid in 2003 and 2004 have posted hefty interest incomes. Barclays assets which stood at ZWD566billion at December 2003 rose further to ZWD900billion in January 2004, a reflection of the safe haven direction of deposits as the liquidity crunch and the attendant deposits as the liquidity crisis bit deeper into the newer banks.

The trend of conservative traditional banks restoring their hierarchy is confirmed by the exceptional results posted by Standard Chartered, Stanbic and Commercial Bank of Zimbabwe and Zimbank, for the years ended 2003 /2004. Traditional banks have consistently reflected cash and liquid assets to total deposit ratios exceeding 75%, which are indicative of strong liquidity positions. On the other end of the spectrum lie locally owned banks whose immediate history has suddenly been blighted by the evidence of imprudent banking conduct, questionable corporate governance and obscene insider loans.

A number of the indigeneous banks are still grappling to cover gaps created by mismatches in assets and liabilities. Daren King of the Johannesburg based Global credit rating company (GCR) believes Zimbabwe's financial system will emerge stronger from the crisis and one can't help but to agree with this statement. The banks who survived the crisis will emerge stronger in the long run.[10]

The banks play an important role in creating monetary capacity as the economy grows. The banks in Zimbabwe played an important role in the so called indirect financing system which implies that banks collect funds from individual investors in the form of deposits and lend them to non-financial firms. Banks have paid special attention to monitoring the performance of their borrowers and have acted as an

[10] Banya, N (2004)

important stakeholder in the Zimbabwean corporate finance system. Banks, however, have not been monitored adequately by public administration namely the ministry of finance and the Reserve Bank of Zimbabwe (RBZ).

There is a growing concern about the effect of corporate governance on the companies' performance in Zimbabwe. Such concern has previously concentrated on non-financial firms, such that banks monitor the non-financial firms to whom they lend money. No serious attention has been paid to financial institutions. In particular, no serious investigations have been done to identify the quantitative effects of corporate governance on financial firms' performance. This research will attempt to show some quantitative as well as some qualitative aspects of the listed banking institutions on the Zimbabwe Stock Exchange.

This research will endeavour to determine if poor corporate governance had anything to do with these banks collapsing. 'Globally, corporate governance has been recognized as a tool to fight, amongst other ills, corruption, corporate scandals, poverty and the agency problems.'[11] The research will determine if this tool is lacking in Zimbabwe's financial sector or the alternative which is that poor corporate governance did not contribute to the collapse of the financial sector.

1.4. Research design, instrument and questions

While the study was in part a replication if similar studies it is expected to contribute to the body of knowledge on corporate governance issues in Zimbabwe's banking industry. The study endeavours to establish whether or not these implications would be consistent with previous findings. The case study approach was used as the main method of study because of the depth and detail of the data that the researcher was expected to collect. According to Bless and Smith (1995:44), the case study is

[11] Corporate Governance and the corporate sector in Zimbabwe, 2/5/2004, Financial gazette, www.fingaz.co.zw

"A way of organizing social data and looking at the object to be studied as a whole. All the aspects are considered, which means that the development over time of the event or person constitutes an important dimension what were incidents and thought processes that led to these changes."

It was expected that a case study would draw the information required through questionnaires and interviews, the latter allowing for various forms. According to Cooper and Schindler (2003), the principal benefits of case studies are that they allow for the collation of various sources of information in order to bring about a comprehensive and reliable conclusion. To quote :-

"Case studies place more emphasis on a full contextual analysis of fewer events or conditions and their interrelations. Although hypothesis are used, the reliance on quantitative data makes support or rejection more difficult. An emphasis on detail provides valuable insight for problem solving, evaluation and strategy. This detail is secured from multiple sources of information."

Research questions

What is the present state of governance in the listed banks in Zimbabwe?

Are the best practices in corporate governance being applied in the financial sector?

What is the financial performance of the listed banks?

Is there a link between financial performance and good governance/ethical executive team?

Is there a link between the banks that survived the financial sector crisis and good governance/ethical executive team?

How does corporate governance in Zimbabwe rate against other comparable countries in the world?

1.5. Methodology

The objective of this paper is to examine and evaluate the contemporary state of governance in Zimbabwe's listed private banking industry. This paper avails itself mainly to the case study method of research based on a careful examination and evaluation of the relevant literature, inclusive of financial statements, and other publications on the subject. Information was also obtained from people knowledgeable about the subject by way of questionnaires and interviewing of such people. Questionnaires were completed in the presence of the researcher.

The literature involved is examined in chapter two followed by the analysis of the data obtained by the questionnaires, interviews and analysis of annual reports in chapter three. The findings and recommendations are being dealt with, respectively, in chapter four. The article for publication is documented in chapter five.

Leedy (1986) and Bell (1993) concur that "a questionnaire is an instrument used for observing data beyond the physical reach of the researcher." Data was analyzed in the form of tables and graphs. Questionnaires were summarized into tables for easier analysis. Results were explained based on the summary of tables. Raw data is provided in the appendices. The results are both in a quantitative format and in qualitative format. The quantitative results are in table format and the qualitative are written out in a results chapter. Questionnaire used in the investigation can be found in Appendix 1.

This study considered the years 2000, 2001, 2002, 2003 and 2004 except for the banks which fell out in 2003.

1.6. Limitations of the study

There are many factors which would have contributed to the collapse of some banks in Zimbabwe in 2004 which are economic, social and political which will not be analyzed in depth in this study. There is also a limitation on information in the sense that during the period in which the research is being conducted some of the banks folded up in 2004. This resulted in some of these banks not releasing annual reports for the year ended December 2004. For these banks the last year of review will be the year ended December 2003.

The subject of corporate governance is a sensitive issue in the banking sector in Zimbabwe at the moment, due to the numerous scandals that emerged in 2004. Many key people at the banks were not willing to be interviewed. Those who were willing to be interviewed were restraining some information due to the sensitive nature of the subject. The researcher is of the opinion that sufficient information was obtained from the respondents who were willing to cooperate.

CHAPTER TWO

Literature Review

2.1. Introduction

The objective of this chapter is to examine the existing, relevant literature on corporate governance in Zimbabwe, in other countries in Africa as well as globally. Historical literature as well as recent developments in corporate governance will be reviewed.

2.2. Corporate Governance structures in Zimbabwe

The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.[1]

An effective corporate governance framework needs an appropriate and effective legal, regulatory and institutional foundation in which all market participants can feel secure in establishing contractual relations. An effective corporate governance framework typically comprises elements of legislation, regulation, self-regulatory arrangements, voluntary commitments and business practices having an origin in country specific circumstances, history and tradition.[2]

The following is a description of the existing structures in Zimbabwe. Listed companies in Zimbabwe are regulated by the Companies Act and by the listing rules of the Zimbabwe Stock Exchange Act (under the ZSE Act). For many years there

[1] Agogu, M. (2003)
[2] Ayogu,M (2003)

was no capital market regulator, but recently due to the problems experienced in the capital markets the Reserve Bank of Zimbabwe has assumed the role of capital market regulator.

The increasing market orientation of banks has also necessitated changes in the approach to regulation and supervision. The responsibility for maintenance of the banking system and markets is being redefined, in one country after another. The Reserve Bank of Zimbabwe recently released a guideline of corporate governance principles that are to be used by all banking institutions monitored by the Reserve bank, including the listed banks surveyed in this study. These corporate governance guidelines were introduced in response to the financial crisis that occurred in 2003/2004 which caused the collapse of a significant number of financial institutions. The guidelines are mainly based on the Second King report and the Sarbanes Oxley Act which are discussed later in this chapter. Zimbabwe's listed banks previously complied with the Second King report recommendations. Recently, King two recommendations and some sections of the Sarbanes Oxley Act were incorporated into the Zimbabwean banking act. They are compulsory and punishable by the courts if not abided by. Of particular interest are the following issues which were not previously enforced.

No shareholder with a ten per centum (10%) or more shareholding in a banking institution or bank holding company shall form part of management of the banking institution or bank holding company. No shareholder with a ten per centum (10%) or more shareholding in a banking institution shall be appointed as Chairperson or Deputy Chairperson of the board of directors of a banking institution or bank holding company.[3]

[3] *Reserve Bank Corporate Governance Guidelines 2004*

One of the corporate governance problems which is cited as one of the main causes of the collapse of financial institutions is owner managed banks. There was a tendency by owners who were managing banks to ignore the corporate governance policies in place when it wasn't to their personal benefit. More is discussed under the data analysis section in chapter three. Bank regulators have recognized the importance of shareholders. In the modern market orientated approach to bank regulation, the emphasis on the fiduciary responsibility of shareholders has increased significantly. This is reflected in several ways, including the more stringent bank licensing requirements and standards that a bank's founder members should not be chief executive officers of the bank. This guideline should help alleviate the problem experienced in the past with owner managed banks. Directors may be penalised for any non-compliance with the provisions of the banking legislation and be removed from office if found to have acted against the interest of depositors and the banking institution and forbids directors and officers from participating in a competing enterprise unless a majority of the disinterested board members approve.

Directors and officers who have an interest in a transaction to which the banking institution is an actual potential party are required to disclose their interest to the Board.

This interest can come from being the other party to the contract; acting as representative of the other party; .owning stock or serving as a director or officer of the other party; .being a financier of the other party; or .having close relatives who are any of the above. For such a transaction to be valid, a majority of the disinterested directors must approve the transaction, upon disclosure of all the facts and circumstances surrounding the conflict of interest. If all the facts and circumstances surrounding the conflict are not disclosed, the Board or the shareholders may have the right to void the transaction and/or seek damages in court."[4]

[4] Reserve Bank Corporate Governance Guidelines (2004).

Another corporate governance problem cited as one of the causes the financial crisis of 2003/2004 is obscene insider loans, discovered only when the banks experienced problems. Loans were being granted to companies that directors had interests in without going through the proper approval channels. The introduction of this rule is expected to reduce this type of corruption and fraud by directors.

The Reserve Bank holds the chief executive officer directly responsible for the day-to-day operations of a banking institution. He/she must be conversant with the operations of the banking institution, the state of internal controls, requirements of statutes, directions, guidelines, regulations, as well as current issues and policies affecting the industry in general. He/she must also have the necessary knowledge and professional competence in the conduct of banking business. Given the strategic operational role of the chief executive officer, this function shall be separate from that of the chairperson. A banking institution is required to inform the Reserve Bank of the person who will be directly responsible for the overall running of the institution when the chief executive officer is unavailable, on leave or otherwise absent. The person so nominated should be fully acquainted with the affairs of the banking institution, and should be able to act promptly, with authority, on matters affecting the banking institution.

Particularly notable is the adoption of CEO and CFO accountability from Sarbanes Oxley act and incorporated into the banking act of Zimbabwe. CEO's and CFO's are now required to get certification as quote:-

"The appointment of a chief executive officer or chief accounting officer of a banking institution requires the prior written consent of the Reserve Bank as stated under section 20 of the Banking Act. Failure to obtain the prior written consent of the Reserve Bank constitutes an offence under the Act. In processing the applications for appointment of directors and chief executive of a banking institution, rigorous

vetting is conducted to ensure that the proposed chief executive officer or chief accounting officer is a fit and proper person. The sound operation of a banking institution depends critically on its chief executive. The chief executive officer must be suitably qualified with appropriate experience and possess a proven track record in the banking industry at senior management level. He must be a person of high calibre and impeccable integrity. The Reserve Bank will consider a candidate ineligible for the position of chief executive officer if he has been suspended for any reason while performing his duties in his previous employment or if he has been subject to investigation and compulsorily removed from his position by the Reserve Bank for doubtful transactions or misconduct during his career. Chief financial officer The Chief Financial Officer, along with the Chief Executive Officer, is generally regarded as an officer materially liable for the banking institution's operations."[5]

The tone at the top is critical and nothing related to financial reports can be taken for granted. Better corporate governance has been put in pace in many, if not most public financial institution. In a now-data survey conducted in Japan regarding perceptions of ownership and interests, presidents of major firms, senior executives, and middle managers were polled regarding perceptions of ownership. They were asked: On whose interests should corporations be run (80%) was almost as large as those mentioning stockholders (87%). And most company presidents indicated that the firm should belong to both groups, with society employees as whole getting many votes.

On the question of whose interests are being served, the most common answer was employees, with shareholders coming second. Again, most of the presidents mentioned both groups, but a full 20% indicated that shareholders' interests did not count in running the firm. With the growing interest worldwide in social

[5] *Reserve Bank of Zimbabwe Corporate Governance Guidelines, 2004*

accountability, it may be surprising to find that these views (in its many shades) are not limited to Japan.

Furthermore, to enable banking institutions to tap the expertise of lawyers and accountants, practicing lawyers and the Reserve Bank has allowed them to be appointed as directors of a banking institution provided that they are not employed by or are not partners in an accounting firm which is engaged to conduct audit of or consultancy work for the particular banking institution. Interlocking directorships in the banking industry is prohibited. The Reserve Bank will only allow common directorships for banking institutions which are related corporations. This is in line with the need to avoid conflict of interest situations in the management of two or more banking institutions. Consistent with this policy, a person with more than interest in the paid-up capital of a banking institution in his personal capacity (directly or indirectly) is also not allowed to be appointed to the board of another banking institution or banking group. In line with section 19(1) (b) of the Banking Act [Chapter 24:20], no person shall be appointed, or hold office, as a director of a banking institution if he is a director of another banking institution which carries on business in Zimbabwe in competition with the other banking institution. The chief executive officer or executive director of a banking institution shall not hold any executive position in another corporation. However, for companies within the same group, and family-owned companies of the chief executive or executive director, exemption may be ranted on a case-by-case basis. This is consistent with the Reserve Bank's requirement for a chief executive officer and executive director to devote his attention and commitment principally to the day-to-day operations of a banking institution. However, he may serve on the boards of other corporations in a non-executive capacity, subject to the limit specified in paragraph below.

Banking institutions must follow good corporate governance principles, which provide for the disqualification of a director or senior manager who: (i)has been involved in the directorship or management of a failed banking institution and or

bank holding company, unless that person shows to the satisfaction of the Reserve Bank of Zimbabwe that the person was not responsible for the insolvency, liquidation, composition with creditors, bankruptcy or other arrangement with creditors or other action with similar effect in Zimbabwe or elsewhere was a director of an institution that has been liquidated or is under liquidation or management of the Reserve Bank, or has taken part in or been associated with any other business practices as would, or has otherwise conducted himself in such manner as to cause doubt on his competence, integrity and soundness of judgment, or if he is under suspension or has been removed from office, or if he has been a director, chief executive officer, chief financial officer or manager of an institution that has been adjudged insolvent, entered into a composition with its creditors, gone into liquidation declared bankrupt or has entered into any other arrangement with creditors or taken any other action with similar effect in Zimbabwe or elsewhere unless that person shows to the satisfaction of the Reserve Bank of Zimbabwe that the person was not responsible for the insolvency, liquidation, composition with creditors, bankruptcy or other arrangement with creditors or other reaction with similar effect in Zimbabwe or elsewhere[6].

The introduction of this requirement will deter criminals from becoming directors of banking institutions; previously directors did not have to prove that they were not responsible for running down a company/bank as long as they had no criminal record. Shareholders are in a position to appoint the people in charge of the corporate governance process and should be carefully screened to ensure that they do not use the bank solely to finance their own enterprises. "Ultimate responsibility for the way in which a bank business is conducted lies with the board of directors. The board has to set strategic direction, appoint management, establish operational policies and most importantly take responsibility for ensuring the soundness of a

[6] Reserve Bank of Zimbabwe Corporate Governance guidelines, 2004

bank."[7] Shareholders play a key role in the provision of corporate governance. By electing the board of directors, which appoints management, the audit committee, and external auditors, shareholders are in a position to determine the direction of bank. Banks are different from other companies in that the responsibilities of management and the board are not only to shareholders but also to depositors, who provide leverage to owners' capital. Depositors are different from normal trade creditors because the entire intermediary function in the economy, including payments and clearance and therefore the stability of the financial system is at stake.

The Audit Committee members should elect a Chairman among them who is an indapendent non-executive director. The Chairman should not be the chairperson of the Board. Such review shall be by means of peer and self evaluation of the board as a whole, its committees and the contribution of each and every director, including the Chairman. The evaluations shall be conducted annually and the fact that they have been done should be disclosed in the annual report. The Chairman of the board shall report to the Reserve Bank annually on the board and directors' evaluations and effectiveness. The report shall be submitted 14 days after the year end. Every listed banking institution shall have a prohibition on dealing in its shares by directors, officers and other selected employees for a designated period preceding the announcement of its financial results or in any other period considered sensitive, and have regard to the listing requirements of the Zimbabwe Stock Exchange rules and/or any other applicable rules and legislation, in respect of dealings of directors [8]

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[7] Analysing Banking Risk , Hennie van Greuning, Sonja Brajovic Bratanovic, The world bank, 2000, the international bank for reconstruction., Washington, D.C, publisher is world bank.

[8] Reserve Bank of Zimbabwe, Corporate Governance guidelines, 2004

Audit committees and Boards of directors are more engaged in their responsibilities related to financial reporting. There is a new, stronger relationship between the auditor and the audit committee. The need to build good controls is front and center. Previously it was not enforced by law to have an audit committee though all the banks had an audit committee as recommended by the Second King Report. Now it is no longer an option but a requirement.

In addition to the Reserve Bank corporate governance guidelines the following governance structures exist in Zimbabwe.

Companies may not have more than a 40% foreign shareholding and no single foreign shareholder should hold more than 10% of a listed company. There has been many exceptions to this rule especially in the mining sector where foreigners own more than 50% of the company's shares. There are foreign exchange controls and offshore dividends are subject to a withholding tax. Zimbabwe is a common law country and despite the adverse publicity about political governance, the country's commercial law system is perceived to be efficient.

According to one respondent commercial regulation and stock market rules 'tend to be observed scrupulously.' A commercial arbitration centre was established in 1995 and is viewed as effective and speedy in resolving commercial disputes. The main commercial laws are the Companies Act (1951) and the Zimbabwe Stock Exchange Act (1996) which regulates activities of the self-regulating Zimbabwe Stock Exchange. For the banking sector there is also the banking act. The ZSE has adopted listing rules based on those of the London Stock Exchange and the Johannesburg Stock Exchange. The Institute of Directors has also been active in pushing for corporate governance standards derived from the UK Cadbury Report and the South African King Report. The Commonwealth Secretariat has also been

working with the Institute to provide training programmes to directors and shareholders. Current corporate governance practices include:[9]

By law, every company should have a minimum of two directors.

According to a survey conducted by the World Bank 'most companies have

Six or seven directors'. Boards are single tier and there are no specific rules on independent directors and committees. In practice many listed companies have independent directors and have appointed audit committees. The law also requires that at least one director be resident in the country. However, Anecdotal evidence suggests that the pool of directors is quite small and many companies have the same directors.[10]

As well as the other minority protection rules already detailed, an investor who reaches a 35% ownership threshold in a listed company is required to make an offer to minority shareholders. Shareholders must be informed and approve material transactions and related party transactions. Certain transactions including 'reduction of capital, issuance of shares at a discount, removal of directors and auditors, mergers and acquisitions, and voluntary wind up of a company' require a special resolution passed by a 75% majority (with a minimum quorum requirement of 25% of eligible votes and a 21-day notice period).

Companies are required to adhere to International Accounting Standards and must appoint an external auditor at the shareholders' general meeting. Local partners of KPMG, Deloitte & Touché, PricewaterhouseCoopers or Ernst & Young audit most major listed companies. Although there is no legal requirement to do so, most listed companies have appointed audit committees led by independent directors.

[9] Nganga, S.,Jain,V & Artivor, M (2003)
[10] Nganga, S., Jain, V., Artivoir,M (2003)

Prior to the recent political problems in the country, the Zimbabwe Stock Exchange was one of the leading stock markets in Africa and at one time was second only to the Johannesburg Stock Exchange. The stock market is dominated by institutional investors which include major multinationals like Old Mutual and Anglo American with small retail shareholders making up a small proportion of investors (estimated at 5%).

The finding of a study done by the London Business school show that ownership concentration by large blue-chip investors and the clarity and the efficiency of commercial law system makes governance among listed companies in Zimbabwe better than most of the other countries in Africa. However, the area of concern for a foreign investor in the country is that public governance problems may spill over into the commercial sector or foreign exchange controls may limit the ability to repatriate dividends.

The quality of corporate governance may not be independent of the quality of state governance; the quality of state governance provides the backbone (the "soft-core" infrastructure) upon which board of directors can govern, and upon which the shareholders can redirect the directors or monitor the monitor.[11]

2.3. Business Ethics and Corporate Governance in the Second King Report

The King Report on Corporate Governance for South Africa 2002 (also known as the second king report), named after the chairperson of the committee who drafted the report, Judge Mervyn King, is the successor code to the King Report on Corporate Governance for the South Africa of 1994.[12] Zimbabwean listed companies comply with the second King report which is the most recent development in Southern Africa on corporate governance. The Second King Report

[11] Ayogu, M (2003)
[12] Dean Roussour,G.J(2004)

gave particular prominence to business ethics. Corporate governance by its very nature is premised upon moral obligations. The four core values of corporate governance, fairness, accountability, responsibility and transparency at least create the impression that corporate governance imposes ethical obligations upon corporations. The ethical nature of corporate governance is, however, largely determined by how stakeholders are defined within corporate governance.[13] If by ethical we mean that one should only consider what is good for oneself, but also consider the good of others, then the question arises whether corporate governance by its very nature is premised upon moral obligations.

The King report makes it clear that the social, ethical and environmental performance of the corporation crucially determine whether the corporation will be able to sustain its financial performance. By social performance the report implies the moral obligations of corporations towards social transformation issues such as HIV/AIDS, poverty and human capital development in countries like Zimbabwe. In the case of South Africa one would add black economic empowerment. This detailed and explicit emphasis on social, ethical and environmental obligations has been recognised as a "world first" for corporate governance reports.

The stakeholder notion of the corporation is reflected in the report's option for an inclusive stakeholder approach as well as in its recommendation that the board of directors should take responsibility for the corporate governance of ethics. The following considerations that are explicitly mentioned in the report confirm this value orientation:

Stakeholders are defined in this report as "those upon whose co-operation and creativity it depends for its survival and prosperity." This implies that the ideal

[13] Dean Rousour, G.J (2004)

sustainability can only be achieved when a company succeeds in gaining and retaining the support of its various stakeholders.

The second king report further recognizes that a company needs more than legal approval to continue its operations. It also needs to be legitimized by its stakeholders and the community in which it operates. The ongoing process of being legitimized by its stakeholders is referred to as a company's "license to operate" (IOD, 2002:8). The license to operate is earned through responsible behaviour that demonstrates to its stakeholders that the company existence is to the mutual benefit of the company and all its stakeholders. According to the King report, the stakeholders from whom the company receives its license to operate includes, among others, groups like the state, investigative media, ethical pressure groups, consumers, employees and communities. In order to secure its license to operate, the report recommends that boards of companies engage regularly with these stakeholder groups.[14]

The report recognizes the fact that modern corporations often have a more immediate impact on citizens than the state, they often determine, to a greater extent than the state, the quality of individual and community life. The increased social power and influence of corporations yield added responsibilities for the boards of companies. Although not explicitly stated the second king report hints that if boards of companies do not take explicit charge of the added responsibilities that go with their social power will either be forced by the state to take responsibility, or they will have to bear the brunt of the resentment of special interest groups, the media or local communities. The report therefore opts for a pro-active approach where the boards of directors willing take responsibility for their social impact and engage with their stakeholders in order to ensure that the interests of all who are affected by the operations of the company are catered and cared for. In this regard the report

[14] Dean Roussour, G.J (2004)

sounds a warning to boards that "in the age of electronic information and activism no company can escape the adverse consequences of poor governance"

"Good corporate citizenship does not entail respecting laws and human rights and refraining from discrimination and exploitation. It also entails strengthening and developing the societies in which companies operate. This implies that companies should become involved in the most pertinent developmental issues in the contexts where they operate. This implies that companies should become involved in the most pertinent developmental issues in the contexts where they operate."[15] Those issues that have a direct bearing on the successes of companies should be addressed specifically. Within the Zimbabwean context one identifies at least three such areas that should figure prominently as part of the social responsibility of companies. They are

- health: HIV/AIDS
- human development
- Poverty

The commitment to good corporate citizenship advocated by the second king report this stems from the conviction that strong sustainable societies to survive and prosper. This is evident when the report justifies its options for an inclusive approach to corporate governance in contrast to an exclusively shareowner approach by stating that "any company's long term commercial success is inextricably linked to the sustainable development of the social and economic communities within which it operates."[16] Constructive responses to these developmental needs of the society require that companies should form partnerships with communities, local and national governments and other stakeholders in order to be effective. Once more the

[15] Dean Roussour, G.J. (2004)
[16] Dean Roussour, G.J (2004)

report implies that this responsibility for good corporate governance citizenship lies with the board of directors."

Every banking institution should report at least annually on the nature and extent of its social, transformation, ethical, safety, health and environmental management policies and practices. The board must determine what is relevant for disclosure, having regard to the company's particular circumstances.

Underlying this motivation is the assumption that there is no one universally valid corporate governance system. To the contrary, corporate governance systems should reflect the uniqueness of the societies in which they originate.

A final motivation for the second king report's inclusive stakeholder approach is based upon the importance of corporate reputation. This argument is based on the obligation of directors to protect company assets. These assets do not only include physical assets, but also the symbolic assets of the company as this not only impacts on its market valuation, but also on its ability to attract investments, clients and talented staff. Reputation is described in the report as a function of stakeholder perception of a company's integrity and efficiency. By implication this means that boards need to engage regularly with stakeholders in order to gauge what their current perceptions of the company are.

Unlike the previous five arguments that all maintained a balance between the interests of the company and those of its stakeholders, the last argument is merely concerned about the company's reputation in order to protect its own assets. Despite its lesser orientation on the interests of stakeholders, it nevertheless serves as a motivation for adopting an inclusive approach to corporate governance.

In order to compete successfully for capital, developing countries need to simulate the corporate governance systems and approaches of those developed economies where the capital is most likely to come from. In the case of Africa that means that the western style corporate governance models and practices of the USA and EU need to be adopted. On the other hand it can be argued that what matters is not the form of the corporate governance system, but whether it is true to the core values of good corporate governance, namely fairness, accountability, responsibility and transparency.

In order to ensure stable strong economies in which they can operate, companies in developing economies need to involve themselves in matters such as eradicating backlogs in education, training, health care etc., developing human capital and resourcing and reinforcing the legal system and its enforcing mechanisms.

The King report was devised for Southern Africa and is relevant in the Zimbabwean context. It has sound recommendations which if followed can help from sound ethical businesses. The King report places an emphasis on ethics which is really the basis of corporate governance. More recently however the King report has been criticized by those who support the African renaissance which is based on the Ubuntu theory. The argument is that the King report is derived from western ideas, culture and thinking and does not adequately capture the African culture and perspective of doing things. The ubuntu theory is further discussed in section 2.5.

2.4. The African Perspective(Ubuntu) on corporate governance

In the view of the Ubuntu perspective on corporate governance:

"The current Anglo-Saxon model popularly known as the king report, and which has been adopted as a model of institutional governance in both private and government institutions has been done more harm than good. Its emphasis on the significance of market forces and individual interests runs the risk of creating a mercenary culture in

our institutions, characterized by individual selfish interests at the expense of the common good. This is very alien to the African world view and where values as formed by the African philosophy of ubuntu."[17]

This view argues that in trying to please the West so that they can invest in the African countries by adopting western corporate governance models that do not consider African culture and values causes us to miss the mark.

The nature of representations that stakeholders can expect from boards of corporations depends on the social background of representatives, as well as on their consciousness or substantive orientations. In particular, a dimension of representation called "consciousness" is concerned with how representatives see the interests they represent and how they act on behalf of those interests. How they serve those interests is shaped by opportunities to influence events. These opportunities may in turn be shaped by the social, cultural and political settings of the economy. Africans believe that social orientations matter because culture- defined as a shared set of values, way of thinking, and beliefs about how things should be done – can be a powerful force.

The essence of African culture Ubuntu is centred around a strong culture of accountability," sense of shared destiny and legacy."(Mbigi, L 2005). Africa needs a leadership and governance system with a sense of legacy and a strong development orientation. The author is of the belief that Africa needs a long term vision whilst the King report provides a short term vision and a looting and mercenary mentality.

One can provide a strong argument that the King report does not have a short term orientation because it promotes sustainability in organizations and the environments in which they operate. On the other hand it can be argued that what matters is not

[17] Mbigi,L (2005)

the form of the corporate governance system, but whether it is true to the core values of good corporate governance, namely fairness, accountability, responsibility and transparency.

"The Anglo-Saxon model of institutional governance, with its bias towards downsizing and characterized by slash- and – burn policies destroys cultural capital in organizations. This increases the inequality in organizations and in society, which undermines the principle of democracy that aims to create a fair society whose institutions can accommodate the aspirations of every citizen, irrespective of race, tribe, class, gender, or political and religious affiliation. The principle of inclusion is the fundamental basis for creating a democratic society and organization, for it bestows citizenship."[18]

It appears that there are many similarities between the African model for institutional governance and the King Report, although the African model criticizes the King report for lacking a "sense of shared destiny and legacy" The ubuntu institutional governance model is characterized by "the principles of inclusion, consensus democracy and stakeholder accountability. This is expected to give rise to the development of robust and inclusive institutional governance structures, stability, long term orientation, as well as a sense of shared destiny, legacy and vision in African institutions."

Germany and Japan, who have institutional governance systems that emphasise stakeholder accountability rather than shareholder accountability which parallel the recommended ubuntu governance model.

"In contrast, Germany and Japan trumpet communication values; business groups, social responsibility for social skills, teamwork, firm loyalty, industry strategies, and

[18] Mbigi,L (2005)

active growth promoting industrial policies. Anglo-Saxon firms are profit maximisers. Japanese firms play a game that might be better known as 'strategic conquest'-they are more focused on market share than profit. These different visions of capitalism have profound effects on everything from labour relations to public education."[19]

The German social market governance model ensures that key stakeholders such as employees, local communities, bankers, and sometimes also suppliers and customers are considered. In large organizations employees are assured of representation on executive operations boards. Japan and Germany's inclusive capitalist systems give more emphasis to stakeholder accountability than shareholder accountability which resonates with the inclusive African cultural values of ubuntu.

2.5. Sarbanes Oxley Act

Without a doubt, the Sarbanes Oxley act is the single most important legislation affecting corporate governance, financial disclosure and the practice of public accountants since the US securities laws of the early 1930's and it is clear that public companies and the accounting profession have made great progress in meeting the vigourous requirements of the legislation.[20]

The Sarbanes Oxley Act was signed into law on July 30, 2002, largely in response to a number of major corporate and accounting scandals, the effects of which are still being felt throughout the economy. The Act, which has resulted in major changes to compliance practices at nearly 85% of large US multinational companies – requires executives, board of directors and auditors to take precise measures to bring about greater corporate accountability and transparency.

[19] Thomas Clarke et al
[20] Nally, D (2004)

However, in the years since its passage, many believe that the act may have imposed unnecessary complex rules and regulations on US businesses – rules that, while they have certainly created higher standards of corporate governance and responsibility, have done so at a cost. Businesses and the boards that run them, now face a plethora of ever –evolving, and often confusing complex policies

There are significant behavourial procedural and organizational changes across the spectrum of key roles in the capital markets network. For example with CEO and CFO accountability now required certification has become a major focus throughout the entire organization. The tone at the top is critical and nothing related to financial reports can be taken for granted. Better corporate governance has been put in place in many, if not most, public companies.

Audit committees and Boards of directors are more engaged in their responsibilities related to financial reporting. There is a new, stronger relationship between the auditor and the audit committee. The need to build good controls is front and center. Regulators have increased their resources to help make the entire process around Sarbanes-Oxley and section 404 work more efficiently. Audit firms have enhanced their audit approach to focus on the evaluation of internal controls, and to integrate the controls work with the performance of the financial statement audit work.

As companies continue to identify and remediate control deficiencies before material misstatements can occur in financial statements, I believe over time we'll see fewer major restatements, fewer SEC financial reporting cases, and ultimately fewer incidents involving accounting fraud.

Clearly companies and investors benefit from these efforts.

2.6. Shareholder activism

"Shareholder activism is about influencing the behaviour of companies so that shareholder interests are kept as the prime focus of their endeavors. It is about using the power of ownership to help companies develop and implement successful maximizing returns for the ultimate beneficiaries."[21]

Shareholder activism is an intervention used principally by institutional investors on behalf of individuals shareholders to engage with companies in which they have shareholdings. It is not simply a question of buying or selling shares, but one of seeking to influence behaviour in order to achieve a better performance by shareholders, using their voice.

Shareholder activism activities include:

-Direct negotiation with management

-Public targeting of a firm by using, for example, the media, and

-Trying to co-ordinate such activities with those of other shareholders.

"Activist investors say that they agenda is limited to specific issues of corporate governance, not intrusion into day to day operations. In other words, their goal is to keep a fire lit under boards and CEO's. Tell them what to do, not how to do it."[22]

2.6.1. The history of shareholder activism

It is believed that the history of shareholder activism dates back to the market crash of the late 20's which was caused in significant part by companies' lack of transparency. As a result the Securities and Exchange Commission (SEC) was formed through the securities act of 1933 and 1934 to create public disclosure and enforcement mechanisms to protect investors and promote dissemination of reliable

[21] Hendrikse J & Hendrikse L (2003)
[22] Frel, J. (2004)

corporate information to the marketplace. The SEC is the agency that regulates and promulgates rules governing shareholders resolutions in America. Changes in corporate governance in America then spilled over to the rest of the world. Shareholder activism is still a thing of the west. In Africa shareholders are fairly passive when compared to the shareholders described as ruling with "an iron fist in America" and in Britain. It is important to understand the culture in Africa in order to understand why shareholders are still passive when they are ruling with an iron fist elsewhere. [23]

Shareholders with a significant shareholding normally use their voting rights to appoint representation on the board, to appoint a chairman, who then appoints a CEO. This usually results in a situation were the majority shareholders run the organization and are involved in the day to day running of the organization. This usually prejudices the minority shareholders, because the majority shareholders become quite domineering and run the company according to their wishes. But as stated above, by Zimbabwean law shareholders must be informed and approve material transactions and related party transactions. Certain transactions including 'reduction of capital, issuance of shares at a discount, removal of directors and auditors, mergers and acquisitions, and voluntary wind up of a company' require a special resolution passed by a 75% majority (with a minimum quorum requirement of 25% of eligible votes and a 21-day notice period).

The only problem is that minority shareholders who are normally individuals are not that interested in how the organization is being run, etc, they are just interested in the bottom line. Only institutional investors employ people to watch and report on what is going on at the organizations they are invested in. When the share price starts falling or they get information that it may fall they simply disinvest.

[23]Frel, J(2004)

Even AGM's of large listed companies are normally very poorly attended, because of the lack of interest by the shareholders. Only institutions and individuals with significant shares turn up, and these are usually the same people who are involved in the day to day running of the organization. The minority shareholders do not show up and if they do they do not challenge the management as much as happens at AGMs of listed clients elsewhere in the world. If they perceive the company to be doing badly they simply disinvest.

2.6.2. Socially orientated shareholder activism

This type of shareholder activism was started in the 1970's by religious investors and started using the shareholder proposal process as a way for working peace and social justice. "They began organizing and filing resolutions on South African Apartheid, community economic development and global finance, environment, equality, international issues, health and militarism." Today shareholders and their allies are able to affect social change on a company-level.

The increasing shareholder activism has caused companies to be more socially responsible in order to keep all stakeholders happy. Socially irresponsible behaviour by some companies has led to large law suits, bad publicity and even bankruptcy.

In 1989, in the wake of the Exxon Valdez disaster, investors and environmentalists banded together to form the "coalition for environmentally responsible economics (CERES), which was built around elements of environmental disclosure. This investor –environmentalist alliance used power of share ownership to persuade companies to adopt a set of environmental principles and produce public standardized annual environmental reports."[24]

[24]Frel, J. (2004)

Socially orientated shareholder activism is the most prevalent in Africa, in Zimbabwe. Shareholders are proud to be associated with a socially responsible company. In many large corporations shareholders choose the manner in which they want to be socially responsible. They influence the board to support charities, schools, etc. For example Econet wireless is a telecommunications company listed on the Zimbabwe stock exchange and has one of the best social corporate responsibility policies influenced by shareholders who have a Christian background. They are involved in supporting various charities, orphanages etc. This actually has a positive impact on the image of the company. More people are more willing to support them by using their network because of their contribution in society. Being responsible socially is also beneficial to the bottom line, because image counts in attracting new customers and retaining old customers.

At the same time they have able to charge above market prices for the use of their network. Despite this they have not lost customers, instead their customer base has grown.

2.6.3. The need to increase shareholder activism in Zimbabwe

People in Zimbabwe generally do not respond to problems the way you would expect them. They are accepting of decisions made by superiors, and may be described as apathetic. This is so politically and in business as well. In the past few years shareholders/investors have lost billions of dollars to fraud, to the government etc, but I have not seen any strong activism against such action. It is a pity because people have lost their lifetime investments and savings due to political problems filtering into business. It may be because people somehow feel helpless because they have no faith in the justice system.

In recent years due to the political problems being experienced by Zimbabwe and the human rights violations, some large multinationals have been reducing their

investment by selling shares to locals and some have disinvested completely. Where some companies have had head offices in Zimbabwe they have moved them to neighboring countries. This is due to a combination of issues, the economic and political problems being the biggest motivational factor but considerations of the unethical conduct of business people and government also a factor.

In the countries of the West Socially responsible investing has been introduced. Growing attention and participation by socially responsible investors (SRIs) has been experienced, apparently 1 in 8 dollars under professional management is in social investments. Since many traditional financial firms now offer social funds, many social investment firms are now offering shareholder activism to set themselves apart.

Not only are socially responsible investors more likely to sponsor social resolutions, but they are more likely to vote for them as well. In contrast, traditional investors may require costly or time-intensive efforts to win their votes because social/environmental issues may be regarded as marginal or detrimental

3. Summary

Prior to the recent political problems in the country, the Zimbabwe Stock Exchange was one of the leading stock markets in Africa and at one time was second only to the Johannesburg Stock Exchange. The stock market is dominated by institutional investors which include major multinationals like Old Mutual and Anglo American with small retail shareholders making up a small proportion of investors (estimated at 5%).

The findings of a study done by the London Business school shows that ownership concentration by large blue-chip investors and the clarity and the efficiency of commercial law system makes governance among listed companies in Zimbabwe

better than most of the other countries in Africa. However, the area of concern for a foreign investor in the country is that public governance problems may spill over into the commercial sector or foreign exchange controls may limit the ability to repatriate dividends. It was also found that the quality of corporate governance may not be independent of the quality of state governance. The quality of state governance provides the backbone (the "soft-core" infrastructure) upon which board of directors can govern, and upon which the shareholders can redirect the directors or monitor the monitor[25]

Listed companies in Zimbabwe are regulated by the Companies Act and by the listing rules of the Zimbabwe Stock Exchange Act (under the ZSE Act). For many years there was no capital markets regulator, but recently due to the problems faced in the capital markets the Reserve Bank of Zimbabwe has assumed the role of the capital markets regulator.

The increasing market orientation of banks has also necessitated changes in the approach to regulation and supervision. The responsibility for maintenance of the banking system and markets is being redefined, in one country after another. The Reserve Bank of Zimbabwe recently released a guideline of corporate governance principles that are to be used by all banking institutions monitored by the Reserve bank, including the listed banks surveyed in this study. These corporate governance guidelines were introduced in response to the financial crisis that occurred in 2003/2004 which caused the collapse of a significant number of financial institutions. The guidelines are mainly from the Second King report and the Sarbanes Oxley Act. Zimbabwe's listed banks previously complied with the Second King report recommendations. Recently however King two recommendations and some sections of the Sarbanes Oxley Act have been incorporated into the Zimbabwean banking act making them compulsory and are punishable by the courts if not abided to.

[25] Corporate governance in Africa: The record and policies for good governance, Melvin D. Ayogu, Univeristy of Cape Town, South Africa

Without a doubt, the Sarbanes Oxley act is the single most important legislation affecting corporate governance, financial disclosure and the practice of public accountants since the US securities laws of the early 1930's and it is clear that public companies and the accounting profession have made tremendous progress in meeting the vigourous requirements of the legislation in the USA and all companies governed by the SEC.

The Sarbanes Oxley Act was signed into law on July 30, 2002, largely in response to a number of major corporate and accounting scandals, the effects of which are still being felt throughout the world economy. The Act, which has resulted in major changes to compliance practices at nearly 85% of large US multinational companies – requires executives, board of directors and auditors to take precise measures to bring about greater corporate accountability and transparency.

There are significant behavourial procedural and organizational changes across the spectrum of key roles in the capital markets network. For example with CEO and CFO accountability now required certification has become a major focus throughout the entire organization. Audit committees and Boards of directors are more engaged in their responsibilities related to financial reporting. There is a new, stronger relationship between the auditor and the audit committee. The need to build good controls is front and center. Regulators have increased their resources to help make the entire process around Sarbanes-Oxley and section 404 work more efficiently. Audit firms have enhanced their audit approach to focus on the evaluation of internal controls, and to integrate the controls work with the performance of the financial statement audit work.

In Zimbabwe the adoption of some of these policies is still to bear fruit, as this is a development effective in 2004. The Reserve bank has taken significant strides in

addressing corporate governance issues in the banking sector in response to the scandals and collapses of 2004 just as the SEC also responded to the Worldcomm and Enron debacle by introducing the Sarbanes Oxley Act.

Particularly notable is the adoption of CEO and CFO accountability which now requires certification as adopted from Sarbanes Oxley Act and incorporated into the Banking act of Zimbabwe. The tone at the top is critical and nothing related to financial reports can be taken for granted. Better corporate governance has been put in place in many, if not most, public companies.

Although not explicitly stated the second king report hints that if boards of companies do not take explicit charge of the added responsibilities that go with their social power will either be forced by the state to take responsibility, or they will have to bear the brunt of the resentment of special interest groups, the media or local communities. The report therefore opts for a pro-active approach where the boards of directors willing take responsibility for their social impact and engage with their stakeholders in order to ensure that the interests of all who are affected by the operations of the company are catered and cared for. In this regard the report sounds a warning to boards that "in the age of electronic information and activism no company can escape the adverse consequences of poor governance"

Good corporate citizenship does not entail respecting laws and human rights and refraining from discrimination and exploitation. It also entails strengthening and developing the societies in which companies operate. This implies that companies should become involved in the most pertinent developmental issues in the contexts where they operate. In the case of Zimbabwe, companies need to get involved in tackling issues such as HIV/AIDS, as Zimbabwe has one of the highest incidence of HIV/AIDS in the world. The commitment to good corporate citizenship advocated by the second king report stems from the conviction that strong sustainable societies to

survive and prosper. This is evident when the report justifies its options for an inclusive approach to corporate governance in contrast to an exclusively shareowner approach by stating that "any company's long term commercial success is inextricably linked to the sustainable development of the social and economic communities within which it operates. Once more the report implies that this responsibility for good corporate governance citizenship lies with the board of directors."[26]

Companies, countries need to adjust corporate governance systems so that they reflect the uniqueness of the societies in which they originate. In order to ensure stable strong economies in which they can operate, companies in developing economies need to involve themselves in matters such as eradicating backlogs in education, training, health care etc., developing human capital and resourcing and reinforcing the legal system and its enforcing mechanisms. It is not the governments problem only, at the end of the day it is everyone's problem.

The King report places an emphasis on ethics which is really the basis of corporate governance. More recently however the King report has been criticized by those who support the African renaissance which is based on the Ubuntu theory. The argument is that the King report is derived from western ideas, culture and thinking and does not adequately capture the African culture and perspective of doing things. On the other hand, in order for developing countries to compete successfully for capital they need to simulate the corporate governance systems and approaches of those developed economies where the capital is most likely to come from. In the case of Africa that means that the western style corporate governance models and practices of the USA and EU need to be adopted.

[26] Dean Roussour, G.J (2004)

The essence of African culture Ubuntu is centred around a strong culture of accountability," sense of shared destiny and legacy."(Mbigi, L 2005). Africa needs a leadership and governance system with a sense of legacy and a strong development orientation. The author is of the belief that Africa needs a long term vision whilst the King report provides a short term vision and a looting and mercenary mentality.

One can provide a strong argument that the King report does not have a short term orientation because it promote sustainability in organizations and the environments in which they operate. On the other hand it can be argued that what matters is not the form of the corporate governance system, but whether it is true to the core values of good corporate governance, namely fairness, accountability, responsibility and transparency.

CHAPTER THREE

Data Analysis

3.1. Introduction

An analysis of the data obtained by the survey was done through exploratory data using descriptive tables and simple and multiple factor graphs and charts.

Nine banks were listed on the Zimbabwe stock exchange in December 2003. As at December 2004 two of these banks had been de-listed and put under curatorship. The two banks were Trust merchant bank and Century bank(also known as CFX Bank). These were the largest locally owned banks in the country. Three of the banks were affiliated with foreign companies the remaining six were local banks. A survey of the annual reports was conducted and interviews with people knowledgeable about corporate governance who are also employed or were employed at these institutions were conducted and questionnaires were filled in the presence of the researcher. A list of the 9 listed banks surveyed can be seen on the table in the shareholders framework below. Results were analysed under four main headings, shareholder framework, board of directors, disclosure in the financial statements and financial analysis.

3.2. Share ownership and responsibility to shareholders in Zimbabwe's listed banks

An analysis of these banks shows that they are owned by pension funds, large insurance companies like South African insurance giant Old Mutual and local insurance giants like First Mutual. There are three listed banks, namely ABC, CBZ and Barclays where the major shareholders are foreign based. Barclays major shareholder being Barclays plc, UK, and CBZ's major shareholders is ABSA bank, South Africa. ABC is owned by local and regional companies based in Botswana. The remaining 6 banks are owned by local pension funds, local insurance companies and management share schemes.

Table 2: Listed Banks end their shareholding as at 31 December 2004

	Name of the bank	Top 5 shareholders
1	African Banking Corporation	Old mutual-12.5%, HIB holdings 8% Heritage investment bank 6%, Barclays Botswana nominees 6%
2	Barclays of Zimbabwe	Barclays plc 60%
3	Commercial Bank of Zimbabwe	Absa group-26% Government of Zimbabwe-17% NSSA-8% FML-6% Libyan Arab foreign bank-5% International finance corporation-4%
4	Century Bank	Campion investments (pty)LTD Camphill investments (pty ltd)
5	First Bank Corporation	Zimre Holdings ltd AM Tregar Ukumbana-Kubatana Investments and NSSA
6	Zimbabwe Financial Holdings	National social security authority Government of Zimbabwe
7	Kingdom bank	Meikles Africa -25% Old Mutual Assurance Life -12% Fornside investments -10% Valleyfield investments -10% Melbar investments-10%
8	NMB Holdings	National merchant bank investments Old mutual life assurance Local authorities pension fund
9	Trust Holdings	Trust employees share ownership-10.75% NRZ contributory pension fund-9.3% Zesa Staff pension fund-8% Oldmutual-7%, Ludham investments -8%

Source: Zimbabwe stock exchange

Research shows that the directors own significant shares in the companies through investment vehicles or companies. This is revealed in the section where directors disclose the shares they own in the annual reports. The major shareholders are represented on the board. Minority shareholders however are the ones who don't seem to have a voice in Zimbabwe.

Reporting to shareholders should be in a regular transparent manner and the annual report is one such way of communicating with shareholders. The development of reporting standards that factually measure performance and supply shareholders periodically with accurate, meaningful and understandable information is necessary. This should enforce the duty of directors to be accountable to their shareholder. The focus should be measurable performance and wealth indicators.

An analysis of the annual reports showed that the listed banks in Zimbabwe all provided performance measures and wealth indicators to shareholders information. The disclosure of the top ten shareholders was not consistent. 33% of the banks did not disclose this information in their annual reports. Generally the annual reports were informative with the exception of 20% of the banks not providing adequate information to communicate effectively with shareholders.

The researcher filled in a questionnaire in the presence of selected individuals from each of the listed banks and former listed banks. The questions asked and the responses obtained are tabulated below.

Table 3: Institutional investors

Institutional investors	Yes	No
Do you believe that institutional investors should take a more active role than they already have in the company's affairs?	55.5%	44.4%
Do you believe that this would contribute to the adoption and maintenance of best practices of corporate governance in your bank?	67%	33%

Source: Self Administered Questionnaire

55.5% of the respondents believe that institutional investors should take a more active role than they already have in the company's affairs, whilst 44.4% did not think this was necessary. 67% of the respondents said that they believed that this would contribute to the adoption and maintenance of best practices of the corporate governance of their banks, whilst 33% believed that it would not have an effect.

3.3. Survey of the Board of Directors of listed banks

The major duties and responsibilities of the board of directors of a banking institution are as follows: To ensure that there are adequate policies in place that are aimed at improving the banking institution's profit performance and ensuring fulfillment of the banking institution's strategic plans; to identify, measure, monitor and manage key risks facing the banking institution; who are qualified and competent to administer the affairs of the banking institution effectively and soundly; staffed with qualified personnel to perform internal audit functions, covering the traditional function of financial audit as well as the function of management audit; and approve the bank's compliance policy, including a charter or other formal document.

3.3.1. Board composition of listed banks

The board of directors is elected by shareholders and are empowered to hire and fire management and make or ratify all major decisions and thereby shareholders indirectly affect the decisions that are made. If the directors do not follow the wishes of the shareholders, the shareholders can replace them, at least in principle. In practice however it is questionable how well this has worked. In modern corporations separation of ownership rights and control rights is supposed to increase efficiency in organizations. There has been many studies done on agency problems which have been well accepted but satisfactory solutions remain to be found. In this research, the board composition was analysed as disclosed in the annual financial statements. All the banks had a reasonable mix of executive versus non executive directors. An Executive director is "a director who is not only a member of the board, but also a full-time employer of the company involved in the management and running of the business, for which he or she receives remuneration. An executive director's focus is on the operational, tactical and day-to-day performance of the business."(Hendrikse, J &Hendrikse L. 2003)

Non executive directors are directors who are only members of the board, are not involved with the management of the company and are paid directors' fees. A non-executive director's focus is on the strategic direction and the overall governance of the business. (Hendrikse, J & Hendrikse L. 2003)

In an increasingly complex banking environment, the presence of suitably qualified independent directors can contribute effectively towards achieving the main tasks of the board. Further, independent directors should provide the necessary checks and balances on the board of the banking institution so as to ensure that the interests of minority shareholders and general public are given

due consideration in the decision-making process. Independent directors should not be brought in as a mere formality as this would be tantamount to deceiving the minority shareholders and the public. (Reserve Bank Corporate Governance Guidelines, 2004)

All the boards had sub-committees to concentrate on identified risk areas as recommended by the King report. Some of the local banks however did no have enough sub-committees to effectively govern and control the bank. Too much power and control was being given to the executive committees. The independence of the chairperson's was sometimes questionable as they appeared to be relationships between the chairperson's company and the bank in question. Independence of many of the non-executive directors appeared impaired as they had significant business dealings with the bank in question. In the local banks it appeared as if founding member directors were forming most of the executive directors committee. This resulted is a very powerful and domineering executive team, which the non-executive directors could not effectively challenge. Especially is cases where the founder member CEO's had celebrated success. It appears that the board were not adequately informed about some of the unethical dealing that went on.

The code of best practices in corporate governance requires that the annual financial statements of a listed company disclose the executive directors and the non-executive directors and the background of directors. Sub committees of the board should be detailed and number of meetings that took place during the year should also be documented.

Information on directors was generally scanty. With exceptions of a few of the banks that provided full background information on the directors. A lot of the directors are good corporate citizens drawn from a variety of sectors in the economy. The pool of directors is knowledgeable, educated and seem to provide varied input in the running of the banks. The problem arose at local banks were founding members were CEO's and executive directors. As a result they

overpowered the rest of the board and were able to do bad dealing, break the law and fail to comply with regulatory requirements.

The banks were found to have an acceptable mix of non executive directors to executive directors. One bank had 10 non executive director s versus 4 executive directors. Non executive directors were ranging from 5-10 non executive directors. The results of the mix of directors is shown in the table below.

Table 4 : Board of Directors of listed banks

Board of directors	**Bank1**	**Bank2**	**Bank3**	**Bank4**	**Bank5**	**Bank6**	**Bank7**	**Bank8**	**Bank9**
Executive directors	1	3	3	4	4	1	2	4	4
Non executive directors	5	8	7	6	10	6	8	5	6
Total directors	**6**	**11**	**10**	**10**	**14**	**7**	**10**	**9**	**10**

Source: researcher's compilation from annual reports of the listed banks

Two of the nine banks had a deputy chairman. Three of the banks had founder member CEO. Two of these banks have since folded up and one had a going concern problem as at 31 December 2004. Four banks out of nine listed banks investigated did not have details of board meetings held during the year in their annual reports.

Table 5 : Average Board size per firm financial services sector

	Botswana	Ghana	Kenya	Mauritius	Namibia	Nigeria	SA	Swaziland	Zambia	Zimbabwe
Finance, insurance and real estate	11	9	8	10	12	9	9	8	9	10
CEO's as chairperson	n/a	5(23)	5(24)	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Modal board size										

Source: Corporate governance in Africa, Ayogu, M.

The table above shows the distribution of size of board of directors of firms by sectors across countries. The data for Nigeria and South Africa are relatively more current (based on statistics as at year end 1998). John and Senbet (1998) summarise an empirical study by Yermack (1996) on board size. The main findings are that, the market penalizes large board sizes between 4-10 beyond which no systematic relationship appears to exist; profitability ratios and asset utlilisation ratios deteriorate rapidly over board sizes between 4 and 10, and less discernable beyond; CEO incentives from compensation and the threat of dismissal operate more strongly on firms with small boards. The study has also found that that the market rewards the separation, within the same company, of the positions of CEO and chairperson of the board.

The researcher filled in a questionnaire in the presence of selected individuals from each of the listed banks and former listed banks. The questions asked and the responses are tabulated below.

Table 6: Board of Directors

Board	Yes	No
Does the chairman/person have effective control over the board including the CEO?	78%	22%%
In your opinion is there a clear division of responsibilities at the executive level of the company with no individual having unfettered powers of decision making?	67%	33%
Does the board have a formal schedule of matters specifically reserved to it for decision making?	88%	12%
Is there an agreed upon procedure for directors in the execution of their duties to take independent professional advice if necessary, at the company's expense?	67%	33%

Source: researcher's compilation from self administered questionnaire

One expects the standard of corporate governance in banking institutions to be very high as they are regulated institutions. For the questions above one would have expected a yes answer by all the individuals questioned. 78% of respondents believed that the chairperson had effective control over the board including the CEO whilst 22% believed that the chairperson didn't have effective control. Similarly 67% of the respondents said that there was a clear division of responsibilities at the executive level. 88% of the respondents said that the board had a formal schedule of matters specifically reserved to it for decision making. 67% agreed that there was an agreed upon procedure for directors in the execution of their duties to take independent professional advice if necessary, at the company's expense, leaving 33% of the respondents saying that there was

no formal procedure in their organizations for directors to get professional independent advice. There appears to be wide acceptance of the corporate governance best practices, as the majority of the respondents believed that their institutions had good corporate governance practices as recommended by the code.

Table 7: Executive Directors

Executive directors	**Yes**	**No**
The directors report discloses the composition of the remuneration committee	100%	
The chairman of the remuneration committee is available to answer questions at the annual general meeting	100%	
Do you think that the executive directors are of a sufficient caliber to run a listed bank successfully?	88%	12%

Source: researcher's compilation from self administered questionnaire

All the respondents said that the directors' report disclosed the composition of the remuneration committee and that the chairman of the remuneration committee was available to answer questions at the annual general meeting. 88% said that they were of the opinion that the executive directors were of a sufficient caliber to run a listed bank successfully, whilst only 12% believed that they were not of sufficient caliber. These results are quite impressive as they reflect generally good corporate governance practices.

Table 8: Non-executive directors

Non-Executive directors	Yes	No
Are the majority of the non-executive directors independent of management without any business or other relationships with the company, apart from their fees and shareholding?	78%	22%
Non-executive directors do not participate in share option schemes	100%	
Non-executive directors are appointed for specific terms and reappointment is not automatic.	100%	
Does the board include non-executive directors of sufficient caliber and number for their views to carry weight?	88%	12%

Source: researcher's compilation from self administered questionnaires

78% 0f respondents said that the majority of the non-executive directors are independent of management without any business or other relationships with the company, apart from their fees and shareholding. 22% of the respondents were of the opinion that only a minority of the non-executive directors were independent of management.

The Zimbabwean economy is fairly small therefore there is a lot of interaction between the few businesses in the market making it difficult to have truly independent directors. There is likely to be business dealings between the director in his personal capacity and the bank of between the company were the director works and the bank.

It was said that all the non-executive directors do not participate in share options and that all the non-executive directors were appointed for specific terms and

reappointment was not automatic. 88% of the respondents were of the opinion that the board included non-executive directors of sufficient caliber and number for their views to carry weight. 12% believed that they were of insufficient caliber.

There was a wide acceptance of the with respect to recommendation of the King report on non-executive directors.

3.3.2. Sub-committees of the board of directors

3.3.2.1.Role of the auditors and the audit committee

The primary objectives and roles of the external auditors are to report to the shareholders on the performance of the directors and to report to the shareholders on the performance of the company.

Table 9: Audit committee

	Bank1	Bank2	Bank3	Bank4	Bank5	Bank6	Bank7	Bank8	Bank9
Executive directors	0		1						1(fd)
Non executive directors	3	4	4	3	4	4	2	4	2
MD/CEO	0		1	1		1		1	

Source: researcher's compilation from self administered questionnaire

The purpose of the audit committee is to assist the board in discharging its duties in relation to financial reporting, asset management, risk management, internal control systems, processes and procedures, and to measure the quality of both the external and internal audit functions.

The audit committee should consist only of independent non-executive directors

The chairperson of the audit committee should not be the chairperson of the board. The committee should consist of at least three members.

Findings of Audit committee compositions

Only five of the nine banks had audit committees that comprised only on on-executive directors. All the banks had an audit committee. This is commendable as it is not compulsory in Zimbabwe to have an audit committee but most listed companies have an audit committee as recommended by the king report. Four of the boards had at least one executive director sitting on the committee, most of them being the Chief executive officer or the managing director. In my view this is a disadvantage because the executive director will always be defensive when sensitive issues come up and may impede certain discussions in order to cover up internal control weaknesses. Usually there is a conflict between internal audit and executive directors, as internal audit is seen as exposing their weaknesses.

However the code says that if executive directors are to sit on the audit committee the majority of the directors should be non executive directors. Therefore all the banks met this criterion as they all have a majority of non executive directors on the committee.

It also worth noting that of the two banks that fell out they both had an executive director sitting on the audit committee one of them being the FD. The directors of these banks managed to conceal irregularities from the audit committees.

The audit committee is not the board, neither is it the auditors – it is there as the boards' watchdog to report to and guide the board; and the intervention egency

between the board and the auditors by providing an easy and accessible channel of communication.[1]

Table 10: Reporting and Control

Reporting and control	**Yes**	**No**
Is membership of the audit committee confined to non-executive directors?	44.4%	55.5%
Do the financial director, the internal audit head and the external auditor attend audit committee meetings?	77%	23%
Does the audit committee have discussions at least once with the external auditors, without the executive board members present?	100%	0%

Source: researcher's compilation from self administered questionnaire

44.4% of the respondents said that audit committee membership was confined to non-executive directors. This was consistent with the analysis of annual reports done. It was found that a 77% majority said that the FD, internal audit and external auditors attended the audit committee meetings. 100% said that there is a meeting held without the executive directors present.

[1] Hendrikse, J & Hendrikse L (2003)

Table 11: External Auditors

External auditors	Yes	No
Do the external auditors review the company's statement of compliance with the code in so far as it relates to		
-the board having a formal schedule of matters		100%
-the procedure for directors to seek independent professional advice		100%
-the terms of appointment and selection of the non-executive directors	33%	67%
-the tenure of executive directors' contracts, the disclosure of emoluments and adherence to the recommendations for a remuneration committee	88%	12%
-the directors assessment of the effectiveness of the internal controls and their going concern statement.	88%	12%
Do you think the external auditors should have adequately considered corporate governance issues in previous years	12%	88%
Would your company accept increased audit fees in order that your external auditors are in a position to comment competently on corporate governance issues?	12%	88%

Source: researcher's compilation from self administered questionnaire

The survey done in respect of external auditor revealed that most of the auditors do not review the board's formal schedule of matters, the procedure for directors

to seek independent professional advice and the terms of appointment and selection of the non-executive directors.

88% of the respondents said that the auditors had reviewed the tenure of executive directors contracts the directors emoluments and adherence to the recommendations from the remuneration committee. 88% of the respondents also said that auditors reviewed assessment of the effectiveness of internal controls and their going concern statement.

23% of the respondents were of the opinion that external auditors should have adequately considered corporate governance issues in previous years and would be willing to accept increased audit fees in order that their external auditors are in a position to comment on corporate governance issues.

3.3.2.2. Remuneration committees in listed banks

All the banks had a remuneration committee. However newspaper articles post the 2003 financial crisis reveal the executive directors were remunerating themselves over and above what was being disclosed. This was particularly a problem with founder member directors who always felt that they owned the business and were entitled to more at the expense of the depositors and investors

The purpose of a remuneration committee is to provide an independent and objective body that will recommend policy on remuneration of the executive directors. This procedure needs to be transparent and at an arms length.

Functions of the remuneration committee

- To review the remuneration arrangements of the chief executive officer and other executive directors;
- To review the remuneration policies and practices for the company generally;
- To review the recruitment and termination policies and practices for the company including employment contracts
- To review the incentive scheme for executives, including share options and
- To reflect the linkage between directors remuneration and the company's performance. It is essential that there be full disclosure of directors' remuneration in the annual financial statements.

The committee should be chaired by an independent, non executive director, and all the members of the committee should be non executive directors.

Remuneration committees are there to ensure that executive directors are appropriately rewarded and that these rewards are substantially related to the performance of the company, and in the best interests of the shareholders. To ensure true independence, the remuneration committee should consist only of independent non-executive directors.[2]

Six of the nine banks had the managing director or the chief executive officer plus three non executive directors. Only three banks had a committee comprising only of non executive directors. The recommendations are the committee comprises of non executive directors only so that it can be "truly independent."

[2] Hendrikse, J & Hendrikse L (2003)

Table 12: Remuneration committee

	Bank1	Bank2	Bank3	Bank4	Bank5	Bank6	Bank7	Bank8	Bank9
Non executive directors	4	3	3	3	3	3	3	3	3
MD/CEO	0	1	1		1	1		1	1
Total	**4**	**4**	**4**	**3**	**4**	**4**	**3**	**4**	**4**

Source: researcher's compilation from annual reports of listed banks

Of the banks that folded one had all non executive directors and the one had the chief executive as well as three non executives. The other bank which almost folded up also had CEO in the remuneration committee. Two out of the three failed institutions did not have a truly independent remuneration committee. There may or may not be a relationship between banks that folded up and a remuneration committee which is not truly independent.

3.4. Communication with stakeholders in annual report.

An essential complement to sound corporate governance is the implementation of robust financial disclosure requirements for corporations and banking institutions. Financial disclosure is essential as a means of strengthening the accountability of directors and senior management and enhancing the incentives for risk management. It is also essential for market participants and observers particularly the larger creditors of banks, news media, financial analysts and rating agencies to effectively monitor the performance and soundness of banking institutions and to exercise appropriate discipline on those institutions which do not perform well or fail to meet acceptable prudential standards.

3.4.1. Disclosure on corporate governance in annual reports and financial statements[3]

The code of best practices and conduct in the King report, states that the directors should report on certain matters in their annual report, including "the maintenance of adequate accounting records and an effective system of internal controls'

Internal control can be divided into the following aspects

- effectiveness and efficiency of operations
- internal financial control
- compliance with applicable laws and regulations

Directors' statements should contain as a minimum

- acknowledgement by the directors that they are responsible for the company's system of internal financial control:
- Explanation that such a system can provide only a reasonable and not absolute assurance against material misstatement or loss.
- description of the key procedures that the directors have established and which are designed to provide effective internal financial control
- Confirmation that the directors (or a board committee) have reviewed the effectiveness of the system of internal financial control.

It was found that most of the listed banks in Zimbabwe had a director's statement which stated the responsibility of the directors in respect of the actual figures as well as the internal controls. Of the nine banks analysed four did not include the statement that limits the review of systems to providing only "reasonable and not

[3] The guidelines on research objectives have been obtained from "Corporate governance in South Africa,' DeloitteTouche, 1995.

absolute assurance". Generally the disclosure was very good and in compliance with the king report.

3.4.2. Disclosure of material weaknesses in internal controls

Directors are required to disclose material weaknesses in internal controls in their director's statements. In addition they are required to describe corrective action being taken or intended to be taken or explain why no changes are considered necessary.

The banks all had a disclosure as stated above. All did not admit to any material weaknesses or breakdown in internal controls, though it was discovered later that some of the banks did have a material weakness internal controls that the directors were aware of but did not disclose.

3.4.3. Reporting on Going Concern

The code requires that the directors' report on going concern basis of the company and that forecasts and budgets be prepared in trying to evaluate the going concern of a company.

All except one of the banks had a going concern statement in the directors' report.

3.4.4. Regulatory compliance and ethics

Five of the listed banks are known to have violated foreign exchange regulations which resulted in hefty fines by the Reserve Bank. This information was gathered from the newspaper. After this occurred only one of the five banks disclosed the

non compliance and the resulting fine. The other bank did not disclose the non-compliance.

Two of the three listed foreign owned banks scored high in terms of complying with the law and regulations. They did not violate foreign exchange control regulations and showed commitment to observing the law and regulations even when everyone else was not complying with the law and regulations. They are now reaping the benefits of their high ethical behavior, because after the financial crisis they are viewed as safe havens for deposits and they both have a combined, market share of 40% of deposits in 2005.

3.4.5. Corporate social responsibility

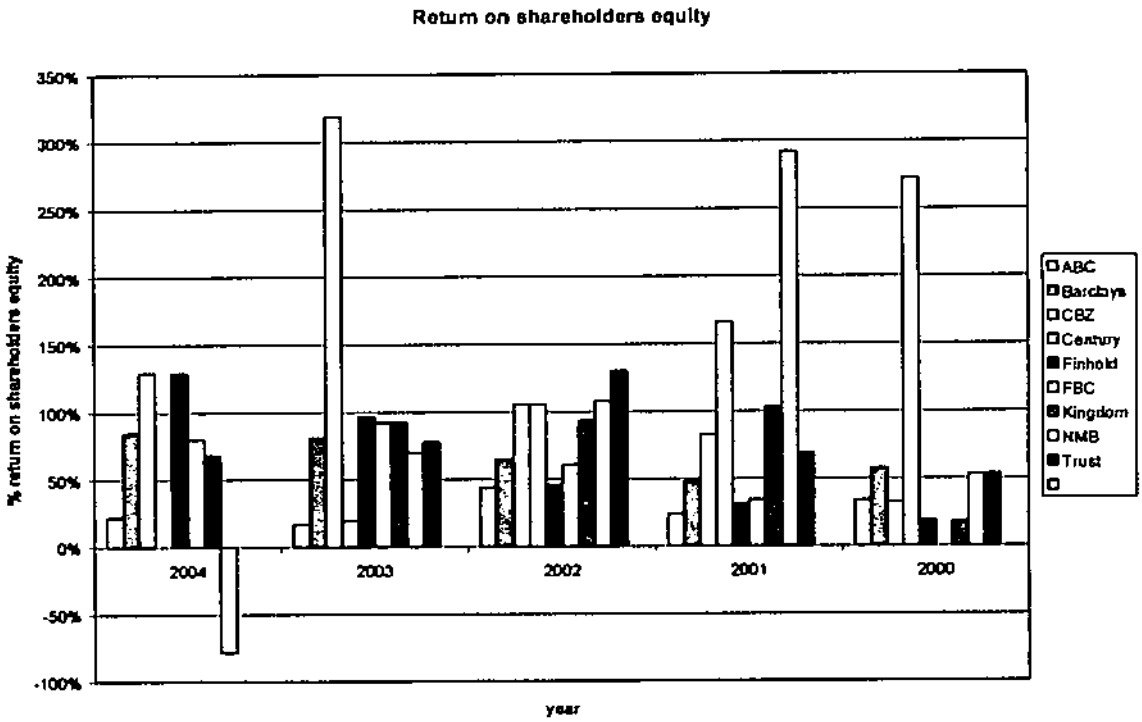
All the banks had some corporate social responsibility activity, however at varying degrees. The foreign owned banks were very conservative and spend as little money as possible in their respective communities. The local banks showed a lot more commitment to their communities. They spend more money on corporate social responsibility and spend more pages in their annual reports detailing the activities there are involved in the community and the money spent during the year. Of particular concern is Barclays bank which spent only 900 pounds in their community. Particularly commendable is Kingdom bank which was very involved in the community and spend a decent amount to support health education, and various charities.

The foreign owned banks need to realize the importance of investing in their communities to show commitment to the community that they are operating in. They appear to milk the community and give back nothing in return

3.5. Financial Analysis

3.5.1. Return on shareholders equity over a five year period

Figure 2



Source: researcher's compilation from the listed banks annual reports

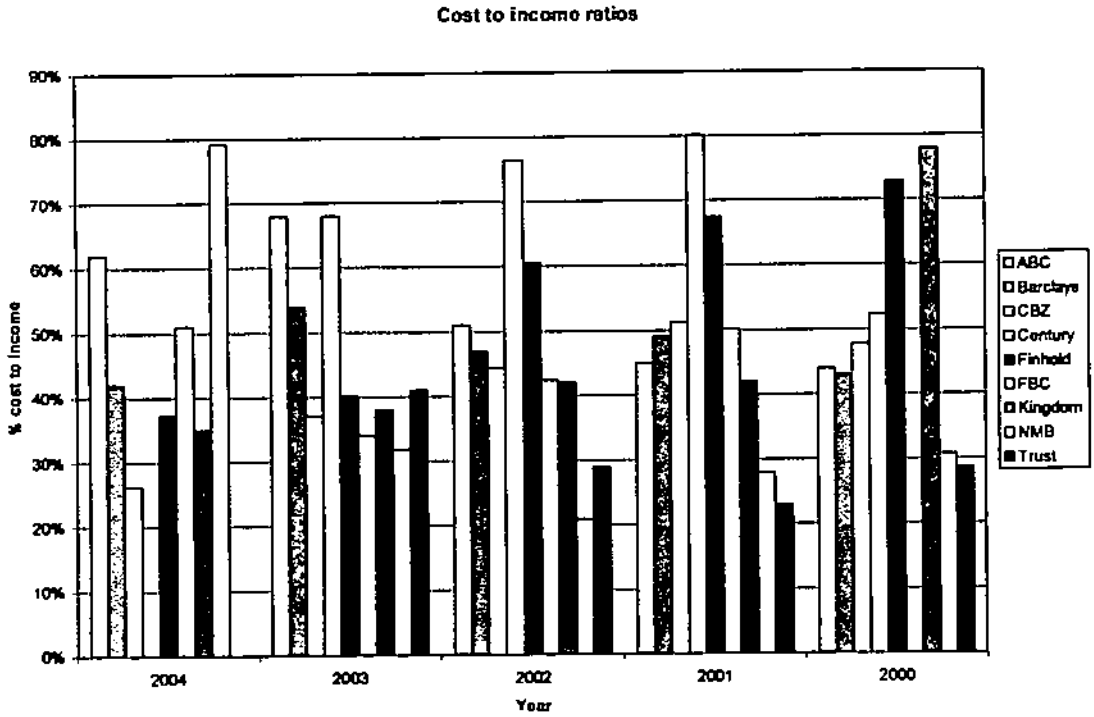
The table above shows the return on equity to shareholders of all the banks listed on the Zimbabwe stock exchange for five years from 2000-2004. As observed earlier the return on investment for shareholders was generally high in the financial sector. This explains the large number of entrants into the sector. By 2004, the general return on investment was declining. These figures are before adjusting for the inflation factor. The inflation adjusted figures in many cases show a negative return on investment which is probably a better reflection of the financial performance as inflation in Zimbabwe is very high. Banks that have a significant foreign shareholding appear to have been consistent in delivering a

good return on equity. These are the same banks that have sound corporate governance practices as they are not only governed by local practices but also by governance codes of more developed countries, like South Africa and United Kingdom. For the local banks, in the time of turmoil in the financial sector, the return on shareholders equity decreased significantly as can be seen in the bar graph below. The banks were shaken due to loss of interest income caused by capital flight, as well as large foreign exchange losses.

Century and Trust are the banks that fell out in 2003/2004 and NMB had going concern problems as at 31 December 2005. These banks were the top performing banks in 2000, 2001, 2002 year yielding the highest return on shareholders equity. In 2004 section on the bar graph above, Century and Trust bank have disappeared as they had collapsed. NMB bank has a negative return on shareholders equity and has going concern problems.

3.5.2. Cost to income ratio

Figure 3



Source: researcher's compilation from the listed banks annual reports

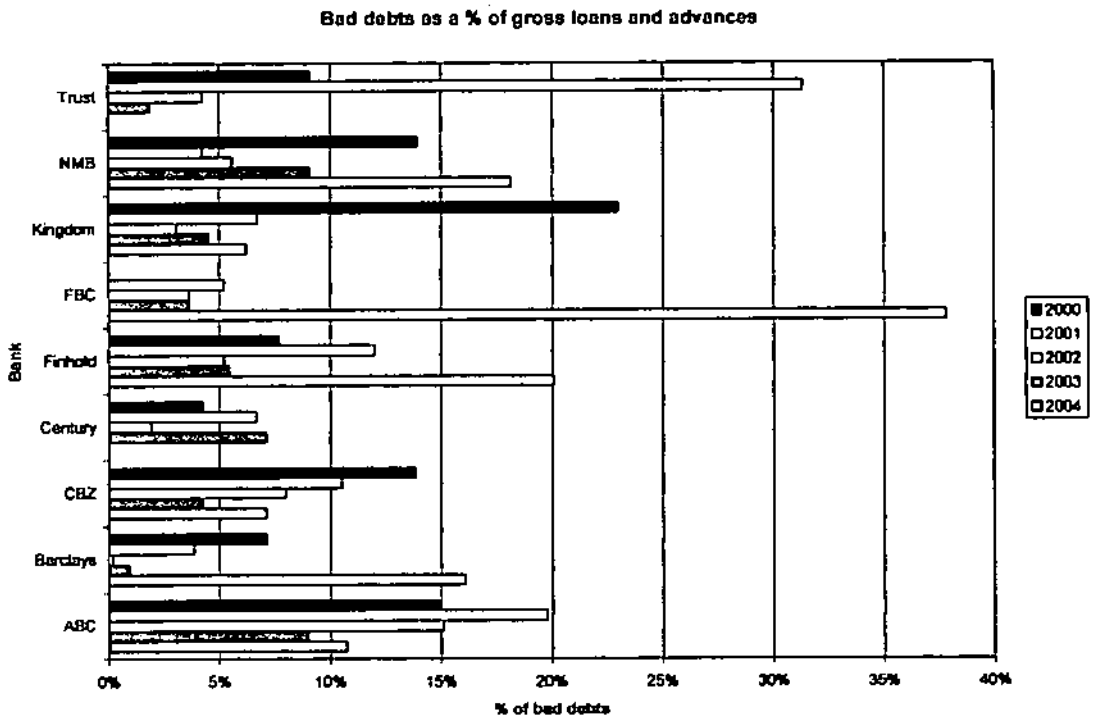
Cost to income ratios in the financial sector are generally higher than most other places in Africa and the developed world due to high inflation rates it is very difficult to contain the ever rising costs.

The banks who seem to have managed their costs quite well are Barclays, CBZ, Finhold and Trust bank before its collapse appeared to have a good cost management considering a hyperinflationary economy. Trust also had a good corporate governance structure and framework

Cost to income ratio is equal to costs as a percentage of total income. It is a reflection of management ability to manage costs. In 2000, 2001, 2002, 2003 Trust, NMB had the best cost management. Century to have had a high cost to income ratio in those years. In 2004 Century and Trust disappeared. NMB bank had the highest cost to income ratio.

3.5.3. Bad debts provision as a percentage of total loans and advances

Figure 4



Source: researcher's compilation from the listed banks annual reports

An analysis of the above graph shows that in the 2004 there was a significant increase in bad debts as a percentage of total loans and advances. Some other years showing a significantly high percentage are 2000 and 2001. This was due to the agrarian reform which resulted in an enormous increase in bad debts as the farmers lost farming assets to the war veterans who invaded farms. As a result they were unable to pay back their loans.

In 2004 many banks had liquidity problems and two listed banks were put under curatorship. As a result banks that were exposed to the banks that were put

under curatorship had to provide for bad debts as chances of recovering the money were slim.

3.6. Summary of findings

Banks in Zimbabwe are owned mainly by pension funds, insurance companies and some foreign investors. Individuals own shares through investment vehicles. The areas surveyed to determine the state of corporate governance in Zimbabwe's listed banks were shareholder framework, board of directors structure, composition, function and efficiency, external auditors function, communication with stakeholders including shareholders, financial performance in the five year period under review. These were investigated using annual reports from the years 2000 up to 2004. Interviews were conducted with people knowledgeable about corporate governance in the banks. These people comprised of employees and partners in the audit firms. Questionnaires were filled in the presence of the researcher.

In the shareholder sections it was found that communication of financial performance and wealth indicators was of an acceptable standard at most of the banks. Interviewees were of the opinion that investors should take a more active role in the banks, as this would help with the maintenance of best practices in corporate governance. Shareholder activism is one such way of taking an active role.

The structure, functions, efficiency of the board of directors was investigated. The results show that on paper and in principle the corporate governance policies are in place and that boards meet at least once quarterly. The pool of directors is knowledgeable, educated and seem to provide varied input in the running of the banks. All the boards had sub-committees to concentrate on identified risk areas as recommended by the King report. Some of the local banks however did no have enough sub-committees to effectively govern and control the bank. In these

institutions too much power and control was being given to the executive committees. The King report recommends that the audit committee and the remuneration committee comprise only of non-executive directors and that they be chaired by independent director who is not the chairperson of the board. The majority of the remuneration committees had the CEO as a member. The majority of the audit committees had at least one executive director as a committee member. These situations impair independence and affect the quality of decisions made in these meetings. There also appears to be a relationship between failed banks and deviation from the King two recommendations especially of independence. There also seems to be a relationship between failed banks and founder member CEO's. All three banks that had going concern problems, two that later collapsed were being run by founder members who had a significant shareholding in the bank. This has been cited world wide as a problem, and the RBZ has forbidden a director with a significant shareholding to be am executive director.

The survey done in respect of external audit work revealed that most of the auditors do not review the board's formal schedule of matters, the procedure for directors to seek independent professional advice and the terms of appointment and selection of the non-executive directors. The banks are not willing to pay more fees to auditors for them to comment on corporate governance issues. They are of the opinion that the Reserve Bank does enough monitoring in those respects.

Two of the three foreign owned banks scored high in terms of complying with the law and regulations. They did not violate the exchange control regulations and showed commitment to observing the law and regulation even when everyone else decided that they would not comply with the regulations as they were unreasonable. These banks are now reaping the benefits of their ethical behaviour, as they both have a combined market share of 40% of deposits in

2005. The market rewards ethical behaviour especially in banks and penalizes unethical behaviour.

Banks were found to be responsible social citizens, with most of them involved in the key areas of health, education and poverty. The foreign owned banks were not very active and spend as little money as possible in their communities. This is against the King Two Report recommendations to work with the community to address problems in the community because strong, sustainable companies are built in successful communities.

The financial analysis revealed that in the years 2000,2001,2002, the younger banks were making super profits mainly from dealing profit resulting from arbitrage profits gained by illegally dealing on the foreign currency parallel market. Prior to this period the traditional banks dominated the scene as they enjoyed a large market share. As new banks that were viewed as trendy emerged in the market the traditional banks lost their market share. This hierarchy was restored in 2003 and 2004 as depositors fled the younger banks as some of them folded up and the market lost confidence in the new locally owned banks. The analysis also shows that banks were affected at a large scale by inflation and struggled to keep cost to income ratios down. In the period of the agrarian reform when war veterans invaded commercial farms, banks experienced large increase in bad debts as farmers fled their farms and failed to repay loan. The banking sector has experienced many challenges in the period under review including a shrinking economy, high inflation and shortages of foreign currency which impact on real returns. Real returns for most of the banks are negative.

CHAPTER FOUR

Findings and Recommendations

4.1. Discussion

The banking sector in Zimbabwe experienced a high growth rate with numerous entrants emerging into the market in the decade from 1995 to 2005. The capital requirements up until 2003 were quite low in relative terms as they were not being adjusted according to the rampant rate of inflation. This resulted in many owner managed financial institutions. Some of these owners retained more than 10% of shares even after listing on the Zimbabwe stock exchange. The problems which arose were that the banks appeared to have good corporate governance policies in place but in practice many of them were overridden for the benefit of the owners in their personal capacity.

The two banks which have completely collapsed due to misconduct are Century bank and Trust Bank. NMB Bank is struggling to keep its head above the water and had a going concern problem as at 31 December 2004. These banks have one thing in common; they were being run by an executive team that were founding members and holders of a substantial portion of shares held through investments vehicles.

The core of a banking institution is its loan book. In owner managed banks it was found that an obscene insider loans were being granted without going through the proper approval channels. Directors are required to declare their interests in material transactions in board meetings. The directors of banking institutions were not declaring their interests in material transactions. This resulted in large bad debts when the economy experienced major changes in interest rates, foreign exchange rates in 2003.

The third problem cited is the competence of directors. The directors as mentioned earlier are from a pool of knowledgeable, educated , experienced citizens but often not effective in board meetings, especially were directors had founding member CEO's who had significant shareholding tended to be domineering and because theyhad celebrated success in the past the other board member felt intimidated and would not question their decisions.

The executive teams were domineering and used the company as a personal fiefdom. These banks required CEO's who took time to listen and account to the board. When the situation got untenable the board should have got rid of the CEO's.

It can be argued that it is a challenge for a chairman to bring a CEO down to size, especially if the CEO is successful. The board is not likely to have the confidence to confront and address the issues. When an executive team of directors is jointly corrupt they will do everything in their power to conceal the corruption and it is difficult for anyone else from the outside to discover what is going, including no-executive directors.

A study done in South Africa on corporate failures reveals that corporate governance and effective vigilance by the board is a critical component in dealing with many of the problems that result in corporate failure. But in many instances boards are inefficient. The biggest problem with boards that were studied was that there was weak interaction between board members.[1]

There are so many examples were CEO' s are so domineering that the management team is incidental to what happened. You'd like to think that very senior executives would be able to disagree with the direction the CEO is taking. But the truth of the

[1] Nelson, J (2005), Sunday times

matter is that in most instances they didn't and that in itself had serious consequences.

The boards of the banks that collapsed comprised of people who were highly competent, extremely busy and enthusiastic. This is the weakness and strength of many boards. Usually the non-executive directors nominated to the board are very busy and are usually executive directors of other companies. Despite them being competent if they cannot give time to the company which they are non-executive directors, this renders them useless. They sit through board meetings and are usually accepting of the decisions made, especially if the CEO is a domineering one

The chairpersons of the boards and the non-executives should have more of a grip on the executive directors. They should not have let the domineering nature of the executive team intimidate them. This is one of the biggest challenges in corporate governance. Normally the CEO and executive directors have more knowledge about the organization and the industry than the chairperson or non-executive directors. In a recent debate held in Johannesburg, attended by CEO's of various large corporations it was agreed that it is necessary for the chairperson to have a very good understanding of the organization and the industry in which it is operating in order to be able to control wayward CEO's.

4.2. Conclusion

The Reserve bank corporate governance guidelines were incorporated into the banking act in September 2004, largely in response to a number of major corporate and accounting scandals, the effects of which are still being felt throughout the economy. The Act, which has resulted in major changes to compliance practices at banking institutions – requires executives, board of directors and auditors to take precise measures to bring about greater corporate accountability and transparency.

There are significant behavourial, procedural and organizational changes across the spectrum of key roles in the capital markets. For example CEO and CFO accountability now requires certification. The tone at the top is critical and nothing related to financial reports can be taken for granted. Better corporate governance has been put in place in many of Zimbabwe's surviving banking institutions.

Audit committees and Boards of directors are more engaged in their responsibilities related to financial reporting. It is expected that there will be a new, stronger relationship between the auditor and the audit committee. The need to build good controls is front and center. Regulators have increased their resources to monitor the financial institutions more. Audit firms have enhanced their audit approach to focus on the evaluation of internal controls, and to integrate the controls work with the performance of the financial statement audit work.

As banks continue to identify and remediate control deficiencies before material misstatements can occur in financial statements, over time we'll see fewer incidents involving accounting fraud. Clearly companies and investors benefit from these efforts.

The Zimbabwean financial sector will emerge stronger from the financial crisis. The banks that survived have build stronger internal controls and corporate governance policies. The correct balance between conformance with governance principles and performance must be found in order to survive, but this will be specific to each bank. The number of banks operating in the market is fewer but they are stronger after the crisis. The challenge that they continue to face is a harsh economic and political macro environment, which is likely to continue to shave real profits.

4.3. Recommendations

The Reserve bank has taken commendable strides to rectify the corporate governance situation in Zimbabwe's banking sector. The economic situation however poses as the biggest threat to the banking industry at the moment.

Zimbabweans need to rise up and take charge of their economy. Why should foreign owned banks and government owned banks be the only banks to dominate the retail banking sector. These banks combined have an 80% market share as at 31 October 2005. Prior to 2003 the younger banks were dominating the retail banking sector and had taken over most of the market share. The traditional banks (defined as the foreign owned banks and government owned banks) have taken back their position at the top after the younger banks did not survive the financial crisis. There is something that the traditional banks have gained with experience which has staying power. As stated earlier the market penalizes unethical behaviour so banks should seek ethical behaviour over and above to observing regulations and the law.

As a race we should learn a lesson from the traumatic events of slavery and colonialism. African people need to attain a high degree of economic confidence and independence. There is a need to establish our individual, community and state companies that are players in the global economy. If we do not do this as a black race we shall never be free, and our economic dependency and slavery will continue.

The ubuntu values of human dignity, respect, interdependence, compassion, solidarity, taking care of our own should be incorporated into our governance systems. There should be no unjust treatment of African people by their governments. There should be freedom of expression.

Political stability and effective governance are essential. The essence of sustainable development lies in the ability to build effective institutions informed and nourished

by cultural values and beliefs. The rapid political, economies and social development of Japan can serve as a historical example in this regard, but the assimilation of western and eastern practices in our institutions has to be anchored by African Culture. Indigenous impetus (Ali Mazrui)

The essence of sustainable development lies in the ability to build effective institutions informed and nourished by cultural values and beliefs. The rapid political, economic and social development of Japan can serve as a historical example in this regard, but the assimilation of Western and Eastern practices in our institutions has to be anchored by African culture.

CHAPTER FIVE

Article for Publication

The Present State of Corporate Governance in Zimbabwe's listed banking industry

The objective of this research paper is to examine and evaluate the contemporary state of governance in Zimbabwe's listed private banking industry. This is of particular interest in Zimbabwe due to the turbulent economic, social and political environment which has exposed banks to new risks and challenges requiring the continuous innovation of ways to manage business and its associated risks in order to remain competitive. After a series of corporate scandals and a general decline in the performance of banks in 2003/2004 the role of an empowered independent board has never been more important. 'Corporate governance which can be defined as the system by which corporations are directed, controlled and held to account,'[1] has become an issue of significance in Zimbabwe.

Public confidence is the cornerstone of a stable banking system. As the custodian of public funds, the management of e banking institution must exhibit impeccable integrity and professionalism in their conduct so as to engender public confidence in the safety of their deposits. With the broadening and deepening of the country's financial infrastructure, the need for an effective board of directors to assume full responsibility for the overall management of each and every banking institution is more cruciel now than ever before.[2]

Because of a bank's special position of trust in the national economy, corporate governance is a matter of paramount importance. Banks are highly leveraged institutions, with most of their funds coming from depositors and creditors. They provide basic financial services to the public, financing to commercial enterprises,

[1] Corporate governance and the corporate sector in Zimbabwe, 2/5/2004, Financial Gazette, www.fingaz.co.zw
[2] Reserve Bank of Zimbabwe, Corporate Governance guidelines, 2005

and access to the payments system. Increasing globalisation of financial markets, emergence of conglomerate structures, technological advances and innovations in financial products have added to the complexity of risk management in the banking sector. For these reasons, the quality of corporate governance expected of banking institutions is high.

Apart from South Africa Zimbabwe had one of the most advanced and diversified economies in Sub-Saharan Africa. Per capita GDP in 1990 was nearly $2000(purchasing power parity equivalent), sixth highest in Sub-Saharan Africa. Zimbabwe's manufacturing sector accounted for 26% of GDP in 1990, a level comparable to that in South Africa and substantially higher than most other African countries. Other industrial activities, particularly mining, also contributed a substantial share of GDP (14% in 1990), while agriculture accounted for 13% of GDP in 1990. The manufacturing sector was quite diversified in Zimbabwe, producing about 7000 different products (Ridell (1998)).

Less than one third of the labour force is employed in the formal sector (commercial agriculture, industry, government, trade and commerce, education, health and finance), with most of the remainder employed in agricultural activities in the communal areas.

Zimbabwe is currently going through an economic crisis which started in the late 90's and has continued to deepen. At independence in 1980 the country already suffered from a large fiscal deficit, low economic performance, unemployment, price controls, and a lack of foreign currency. The Smith regime was under economic sanctions during their reign and was heavily subsidized mainly by South Africa. It led to a relatively self-sufficient economy, which after independence and liberalization of the economy and loss of subsidy, became unsustainable. The post –independence government embarked on an economic structural adjustment program (ESAP) which failed and led to massive retrenchment, closure of many manufacturing industries, general price increase and the deterioration of social services.

There are four factors that deepened the economic crisis in the late 90's, three of which were political factors;

- The government embarked on an exercise to appease war veterans by giving them cash handouts. This caused run-away inflation which has never been contained since.
- Costly military intervention in the DRC war, which caused budgetary constraints to the government of Zimbabwe, and an ever increasing fiscal deficit.
- "Fast track" land redistribution program and persistent drought, which resulted in the agricultural production of the commercial farming being reduced by 81%. The country currently produces 20% of agricultural outputs it used to produce before the land redistribution program. The country has been experiencing drought for the past five years with below average rainfall. This has exacerbated the decline in the agricultural production
- Failed ESAP (Economic structural adjustment program).

These factors, combined with the liberalization of the economy, led to the gradual but systematic decline of the formal economy and to the growth and emergence of informal sector, especially in the rapidly growing towns and cities of Zimbabwe. These factors also prompted sanctions, which affected the tourism industry. The economy has been on a downward spiral since then, registering growth of 0.9% in 1998 and -7% in 2004 and an expected -7% in 2005. Inflation is currently at 140 and a domestic debt of $1billion US. Unemployment is currently 75%.[3]

A key function of The Reserve Bank is the maintenance of the internal and external value of the Zimbabwean currency. In this regard, the Bank is responsible for the formulation and implementation of monetary policy, directed at ensuring low and stable inflation levels. The Bank has limited autonomy from Government. The Minister of Finance has wide powers to issue general directions of policy to both the

[3] Tchibaiki, United Nations report.

Board of the Bank and the Governor. The Reserve Bank Act specifies a number of functions which the Bank carries out. Chief among these is the maintenance of price stability, the formulation and execution of monetary policy and the fostering of a stable financial system. The formulation of exchange rate policy is the function of Government.

The rise of the foreign currency parallel market is due to foreign currency shortages caused by the decline in agricultural, mining, and manufacturing exports, decline in the tourism industry, lack of foreign direct investment excruciated by the refusal of the government to devalue the Zimbabwe dollar. The government pegged foreign currency exchange rates at unrealistically low levels. The parallel market is governed by market forces of supply and demand and allows the Zimbabwe dollar free fall. Transactions were being carried at rates that are at least three times more than the official rate on the parallel market, in contravention of the law, but by 2001/2002, the illegal foreign currency parallel market was the only existing foreign exchange market. The parallel market for foreign currency began to thrive. Many banks began to participate in the parallel market especially the locally owned banks. The rate at which the Zimbabwe dollar was depreciating became an opportunity for many to profit from arbitrage. This unfortunately caused the dollar to depreciate even faster on the parallel market. Goods were priced according to the rate on the parallel market because all businesses procured their foreign currency on the parallel market. This contributed greatly to the upward spiral in inflation. By December 2003 inflation was 600%. It was impossible to procure foreign currency from the bank at the official exchange rate. In the meantime, the RBZ continued to peg the Zimbabwe dollar at an unrealistic rate.

The Reserve bank failed to control the foreign exchange market because for as long as there is reduced exports and no foreign direct investment there will always be a shortage of foreign currency. Demand will always exceed supply. As a result it is hard to get rid of the parallel market, for as long as people cannot get foreign currency on demand they will purchase it from the parallel market which is a ready

market determined by market forces. On the other side of the coin the RBZ cannot let market forces determine the official exchange rate as it will never stop sliding which can lead to a valueless currency and runaway inflation. Unfortunately this has still happened because of the existence of a parallel market.

The range and number of financial institutions operating in Zimbabwe is impressive by African or even developing countries standards. The financial sector consists of several layers of institutions: The Reserve Bank of Zimbabwe, commercial banks, merchant banks (also called accepting houses), finance houses, discount houses, building societies, institutional investors, development finance organizations, The Post office Savings Bank, and the Zimbabwe Stock Exchange. Financial activities are also assisted by credit insurance and credit reference institutions.

Prior to sanctions in 2001/2002, African development bank and IFC were active in Zimbabwe. However they have since scaled down their activity in Zimbabwe to almost nil. In the period after independence from 1980-1990 four commercial banks dominated the scene in terms of loans that they make to and from the public, Standard Chartered bank, Barclays bank, Commercial Bank of Zimbabwe, Zimbank. In the following decade many locally owned banks were founded, supported by the black empowerment drive which is typical in any African country after independence from colonial rule. Many locally owned listed banks emerged, Trust, NMB, Century, Kingdom, Barbican, Royal, Metropolitan, First Bank Corporation and a regional bank African Banking corporation and many smaller ones. By December 2003 there were 7 locally owned listed banks and they were dominating the retail banking sector, which was previously dominated by foreign owned banks like British Barclays Bank plc, and Standard Chartered Bank. Many more privately owned banking institutions also emerged in this period. However this study is limited to banks listed in Zimbabwe but reference will be made to privately owned banks as well.

The banking Act provides for the registration and regulation of persons conducting banking business and financial activities in Zimbabwe and establishes a deposit protection scheme to protect depositors in the event of the insolvency of a financial institution. The Act specifies "undesirable methods of conducting business " and provides for the cancellation of registration of the institution , inter allia, breaches any provisions of the banking act, misrepresents the facilities which it offers to the public, engages in banking activity that is not specified in its requisition certificate, or it can no longer provide adequate security for the assets entrusted to it.

The RBZ has a Bank's supervision function whose primary objective is to fulfill the responsibility relating to the safety and soundness of individual banks, placed on it by the Banking Act with the aim of strengthening, but not ensuring, the protection of depositors in banks. The Banking Act and The Banking Regulations of 2000 clearly set out the Bank's prudential supervisory task. The Act empowers the Bank to license banks, in concurrence with the Registrar of Banks and other Financial Institutions. The Act and the Banking Regulations 2000 also specify minimum criteria which need to be fit and proper persons, that the business of banking can be conducted in a prudent manner and that it be carried out with integrity and skill.[4]

In September 2003, a new Reserve Bank governor was appointed. In December 2003 he announced a monetary policy that was to rock the financial sector. Interest rates were increased from 150% to 600%. The exchange rate was devalued, and new measures were put in place to try and bring back foreign currency into the official market. Banks were thrown into a liquidity crisis. The traditional banks that had good liquidity management and a conservative approach to business gained from the crisis. As rumors circulated of possible collapses of certain institutions, capital flights excruciated the liquidity situation at the younger trendy banks. Depositors fled in thousands and went to the traditional banks who where viewed as a safe haven. These banks were mainly foreign owned or government owned and were conservative and observed the law in terms of foreign exchange regulations.

[4] Reserve bank of Zimbabwe website, www.rbz.co.zw

The newer banks were more daring and did not observe the foreign exchange act or the banking act scrupulously. The laws governing the banking industry especially the foreign exchange act was often perceived as unreasonable.

By early 2004, many of the banks were literally on their knees with acute cashflow problems and large interest burdens. Many banks were illegally invested in property and long term investments, resulting in a mismatch of assets and liabilities. Because of investments in long term assets they were not liquid enough to meet short term obligations. Long term assets lost value especially property and foreign currency slipped resulting in losses in those banks. Foreign currency purchased on the parallel market lost value as the official rate was devalued. The banks traditionally conservative came out of this unscathed.

Prior to its collapse in 2004, Trust Bank had a 25% of the market share of deposits and had become the largest commercial bank in Zimbabwe. NMB, Century and Kingdom were doing very well sharing a large stake of the remaining market share. By 2003, the local banks were dominating the retail banking sector. They were also popular due to their ability to provide the scarce foreign currency to companies to procure raw materials. These banks were not afraid to procure foreign currency of the parallel market which was an illegal market. A shortage of Zimbabwe bank notes has been experienced since November 2002. Though official inflation to 30 April 2003 was about 270% (with the unofficial rate considered to be at least double this), Central bank has not been able to print sufficient money to satisfy the demand because of the shortage of foreign currency required to finance the printing of bank notes. Local currency shortages have had a ripple effect: the shortage of bank notes at the banks themselves meant that individuals and organisations were not depositing cash. The banks were in turn, compelled to solicit cash from individuals and organizations such as commuter transport operators, supermarkets and petrol filling stations and were prepared to pay a premium to get them. It is not realistic to expect banks that are involved in these sorts of activities to be at the centre of controlling good corporate governance. It is illegal in itself for banks to obtain bank

notes at a premium and such transactions had to be concealed from the authorities. This becomes a predicate offense, especially in cases where the banks have to use the money in order to obtain scarce foreign currency on the illegal parallel market.

The turbulence that hit Zimbabwe's financial sector, which was flying at high altitude, started to subside towards the end of 2004 and in 2005. Banking institutions long considered to be conservative have shown that there is life after the crisis. The traditional banks released results that were excellent for the years ended December 2003 and December 2004. The heady days of "innovation" and financial gymnastics that typified Zimbabwean finance sector were over and margins simply plummeted. The hierarchy has been restored as depositors who had deserted the conservative traditional banks for the trendy indigeneous ones swung back in their thousands. While most indigeneous banks balance sheets which had swollen considerably particularly in the past two years were trimmed both at the instigation of the Reserve bank of Zimbabwe and as a result of depositor flight, traditional banks witnessed a significant growth in assets.

Barclays in the last few years drastically reduced its branch network, the bank which is 64% owned by British Barclays Plc, posted a solid set of figures for the crisis years ended 2003 and 2004. All the banks that were liquid in 2003 and 2004 have posted hefty interest incomes. Barclays assets which stood at 566billion at December 2003 rose further to 900billion in January 2004, a reflection of the safe haven direction of deposits as the liquidity crunch and the attendant deposits as the liquidity crisis bit deeper into the newer banks.

The trend of conservative traditional banks restoring their hierarchy is confirmed by the exceptional results posted by Standard Chartered, Stanbic and Commercial Bank of Zimbabwe and Zimbank, for the years ended 2003 /2004. Traditional banks have consistently reflected cash and liquid asset to total deposit ratios exceeding 75%, which are indicative of strong liquidity positions. On the other end of the spectrum lie locally owned banks whose immediate history has suddenly been

blighted by the evidence of imprudent banking conduct, questionable corporate governance and obscene insider loans.

A number of the indigenous banks are still grappling to cover gaps created by mismatches in assets and liabilities. Daren King of the Johannesburg based Global credit rating company (GCR) believes Zimbabwe's financial system will emerge stronger from the crisis and one can't help but to agree with this statement. The banks who survived the crisis will emerge stronger in the long run.

The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.

To ensure an effective corporate governance framework, it is necessary that an appropriate and effective legal, regulatory and institutional foundation is established upon which all market participants can rely in establishing their private contractual relations. This corporate governance framework typically comprises elements of legislation, regulation, self-regulatory arrangements, voluntary commitments and business practices that are a result of a country specific circumstances, history and tradition.

The literature review provided various arguments with respects to corporate governance. In Zimbabwe the Code of best practices has been devised from the South African King Report and the UK Cadbury report. Hence it incorporates views from abroad as well as Africa. The criticism however is that the King report of South Africa has too much of a western approach which will not work for the African people in our case for Zimbabweans.

Prior to the recent political problems in the country, the Zimbabwe Stock Exchange was one of the leading stock markets in Africa and at one time was second only to the Johannesburg Stock Exchange. The stock market is dominated by institutional

investors which include major multinationals like Old Mutual and Anglo American with small retail shareholders making up a small proportion of investors (estimated at 5%).

The findings of a study done by the London Business school shows that ownership concentration by large blue-chip investors and the clarity and the efficiency of commercial law system makes governance among listed companies in Zimbabwe better than most of the other countries in Africa. However, the area of concern for a foreign investor in the country is that public governance problems may spill over into the commercial sector or foreign exchange controls may limit the ability to repatriate dividends.

The quality of corporate governance may not be independent of the quality of state governance; the quality of state governance provides the backbone (the "soft-core" infrastructure) upon which board of directors can govern, and upon which the shareholders can redirect the directors or monitor the monitor[5]

In Zimbabwe the commercial sector appears to have good governance and laws to support that good governance. However the state of governance in the government itself is not good and tends to spill over into the private sector. Corruption and poor governance is the order of the day in government run institutions. It is certainly possible that politicians use nominee companies to stake their interests in corporations. Hence the widespread incidence of crony capitalism and lackluster enforcement of the Rule of Law.

The responsibility for maintenance of the banking system and markets is being redefined, in one country after another. This approach reconfirms that the quality of bank management and especially the risk management process as the key concerns

[5] Corporate governance in Africa: The record and policies for good governance, Melvin D. Ayogu, University of Cape Town, South Africa

in ensuring the safety and stability of both individual banks and the banking sector as a whole.

The Reserve Bank of Zimbabwe recently released a guideline of corporate governance principles that are to be used by all banking institutions monitored by the Reserve bank. This includes the listed banks surveyed in this study. Of particular interest is the guidelines incorporate King 11 Report recommendations and the recent Sarbanes Oxley Act and has enforced them as a law punishable by the courts if not abided to.

Without a doubt, the Sarbanes Oxley act is the single most important legislation affecting corporate governance, financial disclosure and the practice of public accountants since the US securities laws of the early 1930's and it is clear that public companies and the accounting profession have made tremendous progress in meeting the vigorous requirements of the legislation in the USA and all companies governed by the SEC.

The Sarbanes Oxley Act was signed into law on July 30, 2002, largely in response to a number of major corporate and accounting scandals, the effects of which are still being felt throughout the world economy. The Act, which has resulted in major changes to compliance practices at nearly 85% of large US multinational companies – requires executives, board of directors and auditors to take precise measures to bring about greater corporate accountability and transparency.

However in the years since its passage, many believe that the act may have imposed unnecessary complex rules and regulations on US businesses – rules that, while they have certainly created higher standards of corporate governance and responsibility, have done so at a cost.

There are significant behavourial procedural and organizational changes across the spectrum of key roles in the capital markets network. For example with CEO and

CFO accountability now required certification has become a major focus throughout the entire organization. The tone at the top is critical and nothing related to financial reports can be taken for granted. Better corporate governance has been put in place in many, if not most, public companies.

Audit committees and Boards of directors are more engaged in their responsibilities related to financial reporting. There is a new, stronger relationship between the auditor and the audit committee. The need to build good controls is front and center. Regulators have increased their resources to help make the entire process around Sarbanes-Oxley and section 404 work more efficiently. Audit firms have enhanced their audit approach to focus on the evaluation of internal controls, and to integrate the controls work with the performance of the financial statement audit work.

As companies continue to identify and remediate control deficiencies before material misstatements can occur in financial statements, I believe over time we'll see fewer major restatements, fewer SEC financial reporting cases, and ultimately fewer incidents involving accounting fraud. Clearly companies and investors benefit from these efforts.

In Zimbabwe the adoption of some of these policies is still to bear fruit, as this is a development effective in 2004. The Reserve Bank has taken significant strides in addressing corporate governance issues in the banking sector in response to the scandals and collapses of 2004 just as the SEC also responded to the WorldCom and Enron debacle by introducing the Sarbanes Oxley Act.

Particularly notable is the adoption of CEO and CFO accountability which now requires certification as adopted from Sarbanes Oxley Act and incorporated into the Banking act of Zimbabwe

The appointment of a CEO or CFO of a banking institution requires the prior written consent of the Reserve Bank as stated under section 20 of the banking act. Failure

to obtain the prior written consent of the Reserve Bank constitutes an offence under the Act. Failure to obtain the prior written consent of the Reserve Bank constitutes an offence under the act. *In processing the applications for appointment of directors and chief executive of a banking institution, rigorous vetting is conducted to ensure that the proposed chief executive officer or chief accounting officer is e fit and proper person. The sound operetion of a banking institution dapends critically on its chief executive. The chief executive officer must be suitably qualified with appropriete experience and possess a proven track record in the banking industry at senior management level. He must be a person of high caliber and impeccable integrity. The Reserve Bank will consider a candidate ineligible for the position of chief executive officer if he has been suspended for any reason while performing his duties in his previous employment or if he has been subject to investigation and compulsorily removed from his position by the Reserve Bank for doubtful transactions or misconduct during his career. Chief financial officar The Chief Financial Officer, along with the Chief Executive Officer, is generally regarded as an officer materially liable for the banking institution's operations.*[6]

The tone at the top is critical and nothing related to financial reports can be taken for granted. Better corporate governance has been put in place in many, if not most, public companies.

King report makes it clear that the social, ethical and environmental performance of the corporation crucially determine whether the corporation will be able to sustain its financial performance. By social performance the report implies the moral obligations of corporations towards social transformation issues such as black economic empowerment and human capital development. By ethical performance it alludes to the obligation to protect the natural ecology. This detailed and explicit emphasis on social, ethical and environmental obligations has been hailed as a "world first" for corporate governance reports.

[6] Reserve bank guidelines

The stakeholder notion of the corporation is reflected in the report's option for an inclusive stakeholder approach as well as in its recommendation that the board of directors should take responsibility for the corporate governance of ethics. The following considerations that are explicitly mentioned in the report confirm this value orientation:

Although not explicitly stated the second King Report hints that if boards of companies do not take explicit charge of the added responsibilities that go with their social power will either be forced by the state to take responsibility, or they will have to bear the brunt of the resentment of special interest groups, the media or local communities. The report therefore opts for a pro-active approach where the boards of directors willing take responsibility for their social impact and engage with their stakeholders in order to ensure that the interests of all who are affected by the operations of the company are catered and cared for. In this regard the report sounds a warning to boards that "in the age of electronic information and activism no company can escape the adverse consequences of poor governance"

Good corporate citizenship does not entail respecting laws and human rights and refraining from discrimination and exploitation. It also entails strengthening and developing the societies in which companies operate. This implies that companies should become involved in the most pertinent developmental issues in the contexts where they operate. This implies that companies should become involved in the most pertinent developmental issues in the contexts where they operate. Those issues that have a direct bearing on the successes of companies should be addressed specifically. Within the Southern African context the report identifies at least three such areas that should figure prominently as part of the social responsibility of companies. They are
-black economic empowerment
-health: HIV/AIDS
-human development

In Zimbabwe the first point is irrelevant. The next two points are crucial points in the communities in Zimbabwe. Zimbabwe has one of the highest incidence of HIV/AIDS in the world. The pandemic has even contribute to a very low population growth rate. The commitment to good corporate citizenship advocated by the second king report stems from the conviction that strong sustainable societies to survive and prosper. This is evident when the report justifies its options for an inclusive approach to corporate governance in contrast to an exclusively shareowner approach by stating that "any company's long term commercial success is inextricably linked to the sustainable development of the social and economic communities within which it operates. Constructive responses to these developmental needs of the society require that companies should form partnerships with communities, local and national governments and other stakeholders in order to be effective. Once more the report implies that this responsibility for good corporate governance citizenship lies with the board of directors."

All the banks surveyed had some corporate social responsibility activity, however at varying degrees. The foreign owned banks were very conservative and spend as little money as possible in their respective communities. The local banks showed a lot more commitment to their communities. They spend more money on corporate social responsibility and spend more pages in their annual reports detailing the activities there are involved in the community and the money spent during the year. Of particular concern is Barclays bank which spent only 900 pounds in their community. Particularly commendable is Kingdom bank which was very involved in the community and spend a decent amount to support health education, and various charities.

The foreign banks need to realize the importance of investing in their communities to show commitment to the community that they are operating in. They appear to milk the community and give back nothing in return

All banks can do more in terms of HIV/AIDS for their employees and their communities. HIV/AIDS is an issue affecting southern Africa as cited by the King report and companies need to address it as a critical issue that affects the success of their organizations. Companies should emulate Anglo American Corporation in South Africa which was the first company to provide excellent support to employees by providing Anti retroviral drugs, staff clinics and counseling to support those affected and to raise awareness to employees so that they can practice safer behaviour.

Companies, countries need to adjust corporate governance systems so that they reflect the uniqueness of the societies in which they originate. In order to ensure stable strong economies in which they can operate, companies in developing economies need to involve themselves in matters such as eradicating backlogs in education, training, health care etc., developing human capital and resourcing and reinforcing the legal system and its enforcing mechanisms. It is not the governments problem only, at the end of the day it is everyone's problem.

A final motivation for the second king report's inclusive stakeholder approach is based upon the importance of corporate reputation. This argument is based on the obligation of directors to protect company assets. These assets do not only include physical assets, but also the symbolic assets of the company as this not only impacts on its market valuation, but also on its ability to attract investments, clients and talented staff. Reputation is described in the report as a function of stakeholder perception of a company's integrity and efficiency. By implication this means that boards need to engage regularly with stakeholders in order to gauge what their current perceptions of the company are.

In our Zimbabwean banking industry the obligation of directors to protect company assets was evidently missing prior to the financial crisis. Directors were neglecting their fiduciary duties to act in good faith and prevent the interests of the banks which they worked for and their own interests from clashing. Directors are required to

declare their interests in a board meeting for a transaction that requires board approval. Instead directors of banks were loaning money to companies in which they had interests, but were not declaring these interests in the board meetings. In addition loans were being granted to friends and relatives of the directors without going through the proper vetting and authorization processes that a loan is supposed to go through. In many cases the authorization processes were being overridden.

This was a frequent occurrence in the banks prior to the financial crisis, as gathered from the interviews done with people knowledgeable about the subject. With the Reserve bank act now placing more responsibility on CEO and CFO this should now improve because these were the very people who were compromising the governance systems in the banks. Fear of the law which has been tightened to punish wayward directors should act as a deterrent. This is not to say that misconduct will be done away with in Zimbabwe's banking industry but it will definitely decrease, because previously the law was not air tight on certain company law issues, especially those to do with governance issues of accountability and transparency.

"In order to compete successfully for capital developing countries need to simulate the corporate governance systems and approaches of those developed economies where the capital is most likely to come from. In the case of Africa that means that the western style corporate governance models and practices of the USA and EU need to be adopted. On the other hand it can be argued that what matters is not the form of the corporate governance system, but whether it is true to the core values of good corporate governance, namely fairness, accountability, responsibility and transparency."

The King report places an emphasis on ethics which is really the basis of corporate governance. More recently however the King report has been criticized by those who support the African renaissance which is based on the Ubuntu theory. The argument

is that the King report is derived from western ideas, culture and thinking and does not adequately capture the African culture and perspective of doing things.

The essence of African culture Ubuntu is centred around a strong culture of accountability," sense of shared destiny and legacy."(Mbigi, L 2005). Africa needs a leadership and governance system with a sense of legacy and a strong development orientation. The author is of the belief that Africa needs a long term vision whilst the King report provides a short term vision and a looting and mercenary mentality.

One can provide a strong argument that the King report does not have a short term orientation because it promote sustainability in organizations and the environments in which they operate. On the other hand it can be argued that what matters is not the form of the corporate governance system, but whether it is true to the core values of good corporate governance, namely fairness, accountability, responsibility and transparency.

The listed banks in Zimbabwe comply with the King report of South Africa. Banks whose holding companies are based in the United Kingdom also comply with the UK Cadbury report and the combined code. Zimbabwe Stock Exchange also has a code of best practices in corporate governance which was based on king report as well as Cadbury report. This was put together by the World Bank and a local management services company. There were nine banks listed on the Zimbabwe stock exchange in December 2003. Three of the banks were affiliated with foreign companies the remaining six were local banks. A review of the annual reports shows that generally in Zimbabwe the standard of corporate governance information and annual report information is of good standard. As at December 2004 two of these banks had been de-listed and put under curatorship. The two banks were Trust merchant bank and century bank. These were the largest locally owned banks in the country. A list of the 9 listed banks analysed can be seen on the table below. Market capitalization is also shown below as well as who the major shareholders are.

An analysis of these banks shows that they are owned by pension funds, large insurance companies like South African insurance giant Old Mutual, local insurance giants like First Mutual. There are three listed banks namely ABC, CBZ and Barclays where the major shareholders are foreign based. Barclays major shareholder being Barclays plc, UK, and CBZ's major shareholders is ABSA bank, South Africa. ABC is owned by local and regional companies based in Botswana. The remaining 6 banks are owned by local pension funds, local insurance companies and management share schemes. Research shows that the directors also own significant shares in the companies through investment vehicles or companies. This is revealed in the section where directors disclose the shares they own in the annual reports. The major shareholders are represented on the board. Minority shareholders however are the ones who don't seem to have a voice in Zimbabwe.

Reporting to shareholders should be in a regular transparent manner and the annual report is one such way of communicating with shareholders. The development of reporting standards that factually measure performance and supply shareholders periodically with accurate, meaningful and understandable information. This should enforce the duty of directors to be accountable to their shareholder. The focus should be measurable performance and wealth indicators.

The research results showed that the listed banks in Zimbabwe all provided performance measures and wealth indicators for the shareholders information under the financial highlights section. The disclosure of the top ten shareholders was not consistent. 33% of the banks did not disclose this information in their annual reports. Also generally the annual reports were informative with the exception of 20% of the banks not providing adequate information to communicate effectively with shareholders.

All the boards had sub-committees to concentrate on identified risk areas as recommended by the King report. Some of the local banks, however, did not have

enough sub-committees to effectively govern and control the bank. Too much power and control was being given to the executive committees. The independence of the chairperson's was sometimes questionable as they appeared to be relationships between the chairperson's company and the bank in question. Independence of many of the non-executive directors appeared impaired as they had significant business dealings with the bank in question. In the local banks it appeared as if founding member directors were forming most of the executive directors committee. This resulted is a very powerful and domineering executive team. Which the non-executive directors could not effectively challenge. Especially in cases where the founder member CEO's had celebrated success. It is also my belief that the board was not adequately informed about some of the unethical dealing that went on.

Information on directors was generally scanty. With exceptions of a few of the banks that provided full background information on the directors. A lot of the directors are good corporate citizens drawn from a variety of sectors in the economy. The pool of directors is knowledgeable, educated and seem to provide varied input in the running of the banks. The problem arose at local banks were founding members were CEO's and executive directors. As a result they overpowered the rest of the board and were able to do bad dealing, break the law and fail to comply with regulatory requirements. These banks were NMB, Trust, and century. Other smaller merchant banks which were not listed at the time of this study also experienced similar problems with founder members. At the time when economic fundamentals changed this unearthed rot which was being guised by profits and good shareholders return. In the past five years many of the banks made a lot of dealing profit from illegally participating on the parallel market. Shareholders did not mind the illegal activities, they were interested in a high return on equity and a performing share price.

However, when the law turned on these banks, large fines, lawsuits and bankruptcy faced some of the them, and this became the shareholders problems as profits turned into losses and assets turned into liabilities. In the 2004 shareholders lost

billions of Zimbabwe dollars which translate into millions of US dollars. Only when this happened did they start to point fingers

The banks were found to have an acceptable mix of non executive directors to executive directors. One bank had 10 non executive director s versus 4 executive directors. Non executive directors were ranging from 5-10 per board.

The two banks which have completely collapsed due to misconduct are Century bank and Trust Bank. NMB Bank is struggling to keep its head above the water due to misconduct as well. These banks have one thing in common, they were being run by an executive team that were founding members and holders of a substantial portion of shares held through investments vehicles. In the case of Trust Bank, The CEO, the FD, the Operations and marketing Director and Retail Banking Directors were all founder members with substantial shares. The Chairman was also the founding Chairman. The bank listed about four years after starting operations. During these four years it was very successful. The executive team was very powerful and was credited with the success of the company, which at times rendered the chairman and the board docile. It became very difficult for the board to curtail powers of the executives, often this accumulation of power is "insidious in nature, it is something that happens over time."

The executive teams were domineering and used the company as a personal fiefdom. The challenge here was to maintain a healthy balance between having assertive CEO and having those that ride roughshod over everyone else. Trust like all companies required CEO's who took time to listen and account to the board. When the situation got untenable the board should have got rid of the CEO.

It can be argued that it is a challenge for a chairman to bring a CEO down to size, especially if the CEO is successful. The board is not likely to have the confidence to confront and address the issues.

The boards of these companies comprised of people who were highly competent, extremely busy, enthusiastic management team." This is the weakness and strength of many boards. Usually the non-executive directors nominated to the board are very busy and are usually executive directors of other companies. Despite them being competent if they cannot give time to the company which they are non-executive directors, this renders them useless. They sit through board meetings and are usually accepting of the decisions made, especially if the CEO is a domineering one.

The chairman and his non-executives should have had more of a grip on the executive directors. They should not have let the domineering nature of the executive team intimidate them. This is one of the biggest challenges in corporate governance. Normally the CEO and executive directors have more knowledge about the organization and the industry than the chairperson or non-executive directors. In a recent debate held in Johannesburg, attended by CEO's of various large corporations it was agreed that it is necessary for the chairperson to have a very good understanding of the organization and the industry in which it is operating in order to be able to control wayward CEO's.

Conclusion

The Reserve Bank corporate governance guidelines were incorporated into the banking act in September 2004, largely in response to a number of major corporate and accounting scandals, the effects of which are still being felt throughout the economy. The Act, which has resulted in major changes to compliance practices at banking institutions – requires executives, board of directors and auditors to take precise measures to bring about greater corporate accountability and transparency.

There are significant behavourial, procedural and organizational changes across the spectrum of key roles in the capital markets. For example CEO and CFO accountability now requires certification. The tone at the top is critical and nothing related to financial reports can be taken for granted. Better corporate governance has been put in place in many of Zimbabwe's surviving banking institutions.

Audit committees and Boards of directors are more engaged in their responsibilities related to financial reporting. It is expected that there will be a new, stronger relationship between the auditor and the audit committee. The need to build good controls is front and center. Regulators have increased their resources to monitor the financial institutions more. Audit firms have enhanced their audit approach to focus on the evaluation of internal controls, and to integrate the controls work with the performance of the financial statement audit work.

As banks continue to identify and remediate control deficiencies before material misstatements can occur in financial statements, over time we'll see fewer incidents involving accounting fraud. Clearly companies and investors benefit from these efforts.

The Zimbabwean financial sector will emerge stronger from the financial crisis. The banks that survived have build stronger internal controls and corporate governance policies. The correct balance between conformance with governance principles and performance must be found in order to survive, but this will be specific to each bank. The number of banks operating in the market is fewer but they are stronger after the crisis. The challenge that they continue to face is a harsh economic and political macro environment, which is likely to continue to shave real profits.

Zimbabweans as Africans need to rise up and take charge of their own economies. Why should foreign owned banks and government owned banks be the only banks to dominate the retail banking sector. These banks combined have an 80% market share as at 31 October 2005. Prior to 2003 the younger banks were dominating the retail banking sector and had taken over most of the market share. The traditional banks (defined as the foreign owned banks and government owned banks) have taken back their position at the top after the younger banks did not survive the financial crisis. There is something that the traditional banks have gained with experience which has staying power. As stated earlier the market penalizes unethical behaviour so banks should seek ethical behaviour over and above to observing regulations and the law.

As a race we should learn a lesson from the traumatic events of slavery and colonialism. African people need to attain a high degree of economic confidence and independence. There is a need to establish our individual, community and state companies that are players in the global economy. If we do not do this as a black race we shall never be free, and our economic dependency and slavery will continue.

The ubuntu values of human dignity, respect, interdependence, compassion, solidarity, taking care of our own should be incorporated into our governance systems. There should be no unjust treatment of African people by their governments. There should be freedom of expression.

Political stability and effective governance are essential. The essence of sustainable development lies in the ability to build effective institutions informed and nourished by cultural values and beliefs. (Ali Mazrui)

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APPENDIX 1

Corporate Governance questionnaire 2005

This questionnaire is required for the completion of a Research paper as partial fulfillment of the degree of Masters in Business Leadership (UNISA)

Please answer the following questions by ticking yes or no.

	Board	**Yes**	**No**
1	Does the chairman/person have effective control over the board including the CEO?		
2	In your opinion is there a clear division of responsibilities at the executive level of the company with no individual having unfettered powers of decision making?		
3	Does the board have a formal schedule of matters specifically reserved to it for decision making?		
4	Is there an agreed upon procedure for directors in the execution of their duties to take independent professional advice if necessary, at the company's expense?		

	Executive directors	**Yes**	**No**
5	Directors service contracts do not exceed 3 years unless there is shareholder approval		
6	The directors report discloses the composition of the remuneration committee		
7	The chairman of the remuneration committee is available to answer questions at the annual general meeting		
8	Do you think that the executive directors are of a sufficient caliber to run a listed bank successfully?		

	Non-Executive directors	**Yes**	**No**
9	Are the majority of the non-executive directors independent of management without any business or other relationships with the company, apart from their fees and shareholding?		
10	Non-executive directors do not participate in share option schemes		
11	Non-executive directors are appointed for specific terms and reappointment is not automatic.		
12	Does the board include non-executive directors of sufficient caliber and number for their views to carry weight?		

	Reporting and control	**Yes**	**No**
13	Is membership of the audit committee confined to non-executive directors?		
14	Do the financial director, the internal audit head and the external auditor attend audit committee meetings?		
15	Does the audit committee have discussions at least once with		

	the external auditors, without the executive board members present?		

	Institutional investors	Yes	No
16	Do you believe that institutional investors should take a more active role than they already have in the company's affairs?		
17	Do you believe that this would contribute to the adoption and maintenance of best practices of corporate governance in your bank?		

	External auditors	Yes	No
18	Do the external auditors review the company's statement of compliance with the code in so far as it relates to -the board having a formal schedule of matters -the procedure for directors to seek independent professional advice -the terms of appointment and selection of the non-executive directors -the tenure of executive directors' contracts, the disclosure of emoluments and adherence to the recommendations for a remuneration committee -the directors assessment of the effectiveness of the internal controls and their going concern statement		
19	Do you think the external auditors should have adequately considered corporate governance issues in previous years		
20	Would your company accept increased audit fees in order that your external auditors are in a position to comment competently on corporate governance issues?		
[21	You are invited to comment briefly on the general state of corporate governance in your institution of employment. --- --- --- --- --- --- ---		

APPENDIX 11

GLOSSARY OF GOVERNANCE TERMS AND CONCEPTS

All the definitions are obtained from the Buiness Governance Handbook, principles and Practice, John and Leigh Hendrikse, 2004.

A

Accountability	• Involves the periodic and regular reporting of appropriate information in the respective three areas of responsibility – economic, social/safety/health and environmental. • To account to someone on performance and results that are communicated. • Relates to the act of reporting of accounting for ones actions, ones performance, and ones results; an obligation to account for ones actions and performance.
Accounting Framework	A statement of interrelated objectives, and theoretical principles, which forms a reference for the underlying discipline. In the case of financial reporting, it concerns the provision of information that is useful in making economic decisions. The accounting framework, therefore, should establish the basis for determining which events should be reported, how they should be measured and the format on which they should be communicated to users.
Accounting Policies	Specific principles, bases, conventions rules and practices adopted by an enterprise in preparing and presenting financial statements.
Accounting Standards	Desirable accounting disclosure practices relating to the financial position and financial performance of the business
Agency Relationship	The mandate given to directors to manage the shareholders funds invested in the business in the best interest of the shareholders and the company.
Annual General Meeting	An arranged meeting of shareholders held after the company releases its annual report to be used as a forum to discuss the financial statements, the reports of directors and auditors, corporate governance and other ordinary and special resolutions.
Annual Report	The statutory report prepared by companies to inform shareholders and other interested parties of results and operations over the reporting period, which is usually twelve months.
Arms length transaction	A transaction in which the parties to the transaction are financially unconnected and in which no preference of any is shown in the trading

	terms and application.
Audit Committee	A board committee that should comprise only non-executive independent directors to evaluate the effectiveness of the external and internal auditors and to make recommendations regarding the appointment of external auditors.
Auditing	A public interest activity that provides assurance to the users of financial statements, that an independent professional has performed sufficient work to express an opinion on the fair presentation of those financial statements.
Auditor	The person appointed to perform the relevant auditing functions, provided that where a firm is so appointed, it means the person nominated by the firm to perform such functions.
Auditor Independence	The relationship of the auditor and the audit client in respect of non-audit services that ensures that the auditor maintains independent, impartial and objective position in fulfilling his auditor duties. See Independence

B

Balance Sheet	It is a statement of the assets, liabilities and the owners' funds at a specific point in time. Also referred to as the Statement of Financial Position.
Benchmark	A standard against which a share, bond, portfolio, operating activity can be measured in terms of performance.
Board	A board of directors, audit committee of such boards, head of an agency or legislative body to whom internal auditors report, board of governors or trustees of a non profit organization, or any other designated governing bodies of organisations.
Board Composition	The respective number of independent non-executive directors, and executive directors that makes up the board of directors.
Bottom Line	The net profit after taxation and after paying dividends to preference

	shareholders.
Board of Directors	A board that effectively controls the company, directs and controls the management of the company and is involved in all material decisions affecting the company. May consist of executive directors (full-time employees) or non-executive directors (not full-time salaried employees) and independent non-executive directors.
Bribery	Voluntary gift or receipt of anything of value in corrupt payment for an official act already done and to be done or with the corrupt intent to influence the action of a public official.
Business Governance	Is the force that controls and maintains the balance of interest of shareholders, stakeholders and society. The controlling force in business governance is based on a framework of strategy, structure, systems and synergy.
Business Interest	A shareholders' interest in a company, or a member's interest in a close corporation or a partner's interest in a partnership.
Business Risk	The basic risk inherent in a firm 's operations. It essentially measures the risk of doing business profitably. Business risk plus financial risk resulting from the use of debt equals total corporate risk.

C

Capital	The amount invested in an asset or a business or a financial institution for the purpose of earning income or appreciation. Capital takes the form of owners capital (e.g. ordinary shareholders) and borrowed capital (e.g. preference shareholders, debentures), collectively referred to as fixed capital, working capital (e.g. funding of stocks and debtors) and intellectual property capital which has generated intellectual property assets (e.g. goodwill, trade marks).
Capitalism	The economic system that is based on a market economy where one has the freedom to make decisions, the freedom to choose, and the freedom for business, to operate in competition
CEO	An executive director responsible for the running and management of the

	business, and the performance of individual top management members. Chief executive officer; also known as managing director.
CFO	An executive director responsible for the financial, accounting and administrative function of the business. Chief Financial Officer is also know as financial director.
Chairman	A non-executive director responsible for running the board of directors and the overall management and control of the performance of individual directors
Checks and Balances	The regulatory framework including the applicable legislation, the company's memorandum and articles of association, the internal controls of the business, including policies, procedures and all the contractual documentation of the business.
Code of Ethics	A company 's code of ethics sets out its standards for an ethical organisational as well as individual ethical conduct, and consists of two essential components, namely, a value statement and code of conduct (See Ethics)
Compliance	• The ability to reasonably ensure conformity and adherence to organisation, policies, plans, procedures, laws, regulations and contracts. • To act in accordance with the rules and to conform in practice with the laws, rules and regulations, checks and balances that applies to the company.
Committees	Part of the organisational structure representing an advisory body specialising in particular issues, e.g. Board committees are, inter alia, Nomination, Remuneration, Audit, Strategy, and Environmental.
Conformance	To follow the laws, rules and regulations
Control Procedures	The policies, procedures and activities that are part of a control framework, designed to ensure that risks are contained within the risk tolerances established by the risk management process.
Currency Risk	Risk associated with fluctuating currencies and impacts on whether the business is importing or exporting
Corporate and business governance	The system that maintains the balance of rights, relationships, roles and responsibilities of shareholder, directors and management to direct,

	conduct, control the sustainable performance of the company and the business with honesty and integrity in the best long-term interest of the company, shareholders, business and community stakeholders.
Corporate Citizenship	The commitment of business to contribute to sustainable economic development working with employees, their families, the local community and society at large to improve their quality of life.
Corporate Code of Conduct	The definitive business constitution that governs relationships and behavior of the company, its directors, management and employees and the interrelationship between the company, shareholders, business stakeholders and community stakeholders. It represents the external and internal governance blueprint and benchmark for honest business behavior and best practices.
Corporate Social Responsibility	The balancing of the company activities of productivity, profitability, quality and equity with the sustainability goals of economic, social and environmental benefits to shareholders, business stakeholders and society for the present and the future.
Corporate Strategy	Is a plan of action that encompasses the mission, objectives and goals of the company and identifies various alternatives open tot the company, and a selection of what appears to be the optimum course or sources of action to achieve these objectives and goals
Credit Risk	• The risk of financial loss to the company as a consequence of default by a counter party to a transaction. • The economic, legal and political risk inherent in a particular obligation, or more succinctly, the default risk it embodies.
Currency Risk	Risk associated with fluctuating currencies and impacts on whether the business is importing or exporting.

D

Director	A director is defined by the Companies Act, as including any person

	occupying the position of director or alternate director of the company and an officer includes a managing director, manager or secretary.
Directors' Code of Conduct	A directors code of conduct also represents the Corporate Code of Conduct and incorporate the companies code of ethics
Directors' Duties	Directors have three principal duties – to comply with the Companies Act, Memorandum and Articles of Association; fiduciary duties of loyalty and good faith to company; duty of care diligence and skill.
Directors' Rights	The authority and powers to act, make decisions and enter into contracts on behalf of the company in the best interest of the shareholders.
Disclosure	The extent to which directors communicate the activities and results of the company's performance to shareholders and stakeholders.
Duty of Care	Is doing the things a prudent man would do in the circumstances and refraining from those things he would not do

E

Ethics	A set of moral principles. • The principles and standards that it espouses to guide a company in the day-to-day business activities and its relations with internal and external stakeholders in accordance with its established corporate values. Ethics is the practice of aligning human life, individually or collectively, or institutional structures and practice, according to basic standards of conduct; generally speaking, human conduct, practices and institutions are judged to be good or bad, right or wrong, in the light of such standards of conduct; standards of conduct take the form of values/principles, obligations, rights, and consequences, and meeting those standards emanate from good character or virtues
Executive Director	Directors who are not only members of the board, but are full-time

	employees of the company involved in the management and running of the business, and for which they receive remuneration. Executive directors focus on operational, tactical and the day-to-day performance of this business.
External Audit	• An independent and objective check on the way in which the financial statements have been prepared and presented by the directors taken exercising their stewardship to the shareholders. • A statutory duty to report their independent opinion to the shareowners, on the company 's financial statements, and to consider statutory requirements and standards for financial reporting, and auditing.

F

Fair Presentation	The appropriate application of GAAP statements with additional disclosures where necessary results in financial statements that achieve fair presentation. Compliance with GAAP statements ensures fair presentation.
Fiduciary Duties	A director stands in a fiduciary relationship to his or her company, i.e. they control the assets of another and holds the power to act on behalf of another. The result is that the director has the duty to act in good faith towards the company, to exercise his or her powers as a director for the benefit of the company and to avoid a conflict between his or her own interests and that of the company.
Financial Position	The state of financial affairs represented by assets, liabilities and owner 's equity of a business entity at a specified date
Financial Statements	• A structured representation of the financial position of an enterprise and the financial performance of the business during a period. • Accounting information regarding the financial position of a firm, the results of operations and the changes in financial position. Four

	statements constitute the basic set of financial statements: The balance sheet, the income statement, the statement of shareholders' equity, and the statement of cash flow.
Fraud	• Intentional and unlawful misrepresentation that is to the detriment of the business. • Intentional deception and attempted deception of an individual with the promise of goods, services, or things of value that do not exist or in other ways are misrepresented. For example, false advertising, tax evasion and accounting lies. Two principal types of fraud are theft and false accounting. • Any illegal acts characterised by deceit, concealment or violation of trust. Frauds are perpetrated by individuals and organisations to obtain money, property or services; to avoid payment or loss of services; or to secure personal or business advantage.

G

Gearing	The proportion of funding that is geared or borrowed by companies. Also known as dent/equity and leverage financing.
Globalisation	Is he mobility of capital, skilled knowledge workers, new technology, information and knowledge and growth of multinationals
Going Concern	• An operating business enterprise. • It is a business in operation with the prospect of continuing so in the foreseeable future. It is not a start-up nor a wind down, i.e. the business is operating and systems and people are in place with the prospect of continuing so for the foreseeable future. Assets and liabilities are valued on the assumption that there is no intention or necessity to liquidate or curtail significantly the scale of operation.
Governance, Business Governance, Corporate Governance	• Is the guiding principle for directors and management to operate in the best interest of all stakeholders, to optimize effective leadership, optimize returns, and minimize risk as well as the abuse of power by leaders.

	• It is the framework by which directors can manage effectively carry out the functions of business. • It relates to the way a business is directed and governed. • It deals with the strategy, policies, procedures that directly impacts on organizational performance, stewardship and its capacity to be accountable to its various stakeholders. • It is the exercise of economic, political and administrative authority to manage a business affairs at all levels. It comprises the mechanisms, processes and institutions through which shareholders, stakeholders and leadership articulate their interests, exercise their legal rights and meet their obligations and mediate their differences. • Can be viewed as the control mechanism that ensures the right checks and balances are in place to prevent the risk of mismanagement from conflicting priorities, misallocation of resources, conflicts of interest, misaligned incentives and some of the business weaknesses associated with excessive power. BUSINESS GOVERNANCE HANDBOOK DEFINITION OF CORPORATE AND BUSINESS GOVERNANCE: Corporate and business governance is the system that maintains the balance of rights, relationships, roles and responsibilities of shareholders, directors and management to direct, conform, control the sustainable performance of the company and the business with honesty and integrity in the best long-term interest of the company, shareholders, business and community stakeholders.

H

Human Capital	The capital of a successful business enterprise is composed of working capital, fixed capital and intellectual capital of which human capital is a component. Human capital is the collection of experience, skill and education of a company's employees.

IAS	International Accounting Standards
Independent Director	A director who is a non-executive director who has no existing or prior business, employment or consultancy and other relationship with the company.
Inflation Rate Risk	The unanticipated changes in the inflation rate
Innovation	Any process of change that expands a business' know-how and make it more competitive. The development of new products or processes and the entry into new markets both national and international is part of that change.
Insider Trading	A market abuse where investors have been unreasonably disadvantaged by others who have used information that is not publicly available to others. The idea is to deal in the shares before, confidential and price-sensitive information becomes public and impacts on their price, and in the process to make a proper avoid making a loss.
Integrated Sustainability Reporting	Reporting on the social environmental and economic performance of the business. Also referred to as sustainable reporting and triple bottom line reporting.
Internal Audit	An independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate the effectiveness of risk management, control and governance processes.
Internal Control	A process effected by a company 's board of directors, management and other personnel designed to provide reasonable assurance regarding the

	achievement of objectives in the categories of: • Economy, efficiency and effectiveness of operations • Internal financial controls, and • Compliance with applicable laws and regulations
Investors	Shareholders who invest in a portfolio of shares in different companies.
Irregularities	Intentional misstatements or omissions of amounts or disclosures in financial statements.

K

King II Report	A recommended code of corporate conduct produced under the auspices of the Institute of Directors of Southern Africa for use by listed companies, banks, insurance companies and public enterprises.

L

Legal Liability	The legal sanction of directors, officers and employees for acts of omission or commission as a result of a break of duty or wrongful acts.
Legal Risk	It arises when inadequate documentation and legal controls exist.
Legislation	An act of parliament; a statutory power or law.
Liquidity	Liquidity is used to describe the nature of a company 's asset holdings or mix, i.e., their nearness to cash. Secondly, it is used to describe the relationship between a company's, liquid assets and its short-term liabilities, i.e. the ability of a firm to meet its short-term financial obligations when and as they fall due.
Liquidy Risk	• It arises in the course of the company's general funding activities and the management of the balance sheet, • The risk associated with the company's ability to meet its commitments in respect of financial instruments and short-term

	obligations.
Listed Company	A public company that trades its shares on a stock exchange.
Listing Requirements	The requirements of a stock exchange which may be amended from time to time that aims to ensure that companies listed conduct their business with due regard to the public interest and particularly in relation to the principals of corporate governance.

M

Managing Director	See Chief Executive Officer
Minority Shareholders	Shareholders who do not have a controlling interest or shareholding in the company.
Misconduct	Includes fraud, negligence, default, breach of trust, and breach of duty.
Money laundering	An activity which has or is likely to have the effect of concealing or disguising the nature, source, location, disposition or movement of the proceeds of unlawful activities or any interest which anyone has in such proceeds.

N

Non – Executive Director	Directors who are only members of the board, are not involved with the management of the company and each fixed director's fees. Non-executive directors focus is on the strategic direction and the overall governance of the business.

O

Operating risk	It relates to the potential for losses arising from internal and external fraud, systems failures, incomplete data and inadequate internal control procedures.
Options	This gives one the right, but not the obligation, to buy or sell a specified asset at a set price within a fixed period of time.
Ordinary Resolutions	They are passed by a simple majority of those present in person or by proxy voting at the meeting for the resolutions, i.e. requires a simple 51% majority of votes cast.
Ordinary Shares	The most commonly traded security in South Africa. Holders of ordinary shares are part-owners or ordinary shareholders of a company and may receive payments in cash, called dividends, if the company trades profitably,..
Ownership	Rights over property, including rights of possession; exclusive enjoyment; destruction; etc.

P

Public Company	A company which, in terms of its articles of association: a) Is permitted to invite the public to subscribe for its shares b) Places no limitation on the number of its members c) Places no restriction on transfer of its shares Only the shares of a public company may be listed on a stock exchange

Q

R

Reckless Trading	Directors or managers that run a company irresponsibly and without due

	care and consideration of the interests of the financiers, creditors, shareholders and what is in the best interest of the company. Results in financial loss, and the dilution of the net worth of shareholders, and/or prejudices the creditors claims against the company.
Regulations	Rules created by bodies below Parliament, i.e. does not have legislative or statutory authority.
Regulatory Framework	Statutory legislation (e.g. Companies Act), and non-statutory including regulations and governance codes of conduct to guide corporate and business behaviour.
Reputation Risk	Is the risk that the organisation might be exposed to negative publicity due to the contravention of applicable statutory, regulatory and supervisory requirements by the organisation itself or by its staff members during the conduct of business
Resolutions	Decisions of the board, or indeed of any executive or other committee meeting are referred to as resolutions. Resolutions may either be ordinary resolution or special resolutions. Unless the shareholders' agreement in the case of a private company, the company 's articles of association, or the Companies Act expressly provides otherwise, all matters at board and general meetings may be decided by ordinary resolution.
Responsibility, or Business Responsibility	Involves both an attitude and an action. • It is the act of doing something in terms of ones position and function; the act of attending to ones duties, ones action and results, ones performance. • It is also an attitude – a duty to act responsibly, to apply ones mind responsibly in relation to decisions and actions; an attitude of being trustworthy and being entrusted with duties to perform.
Return	The expectation of future benefits based on the risk profile of the investment. These future benefits are the ability of the business to generate income, the degree of future income stream certainty, future cash flow stream, current levels of profitability, and capital appreciating potential of the asset and the wealth creation of the business.
Risk	• The uncertainty of an event occuring that could have an impact on

	the achievement of objectives. • Risk is the possibility of suffering harm and loss as a result of something happening. • The threats and uncertainties that undermine a business. Risk is measured in terms of probability of occurrence and consequences

S

Shareholder Rights	The rights under the Companies Act, which in the main, are the right to information, to vote, to call general meetings, to appoint directors and auditors.
Shareholders	Owners of the shares in an incorporated business such as a company or close corporation.
Shareholder Value	The net worth of the business based on the market value of the tangible assets and intangible assets attributed to the shareholders of the company.
Share Options	Share options or share warrants are rights to acquire or subscribe for specified shares in a company, usually at a stated price at some future date.
Share Price	The price traded on the stock market.
SHE Responsibility	The social (safety), health and environmental responsibilities of the business.
Solvency	The total financial state and position of the business, and relates to the net worth or net value of the business where assets are valued on the basis of their market values and realisable values. Solvency is a reflection of the ability to realise all the assets (by sale or mortgage) within a relatively short time. This is referred to as a commercial solvent business.

Special Resolutions	They are passed by at least 75% of the votes cast by members entitled to vote on the resolution
Stakeholders, Business	Non-shareholders who have a direct and economic interest in the acts of the business, viz. directors, management, employees, creditors, financiers, customers and South African Revenue Services.
Stakeholders, Community	Non-shareholders who have an indirect interest in the company which relates to social and environmental issues, e.g. public at large, and the community that the company forms part of.
Strategy	- Is leadership that balances the interest of shareholders, stakeholders and society. - Translating a business vision into a business mission.
Structure	Is the organisation that has to be put in place in 3 structural areas: i) Board of Directors, ii) Management, executives and employees, and iii) Board Committees
Sustainability	• The role of business is to create value for shareholders, business stakeholders and community stakeholders by considering the impact of business decisions on social and environmental activities. • Sustainability integrates economic, social and environmental performance into one triple-bottom line benefit for the company, shareholders, business stakeholders and society.
Sustainability Reporting	Reporting on the social and environmental performance of the enterprise, as well as on the financial and economic achievements. Also referred to as triple bottom line reporting.
Systems	Is part of the checks and balances of a business that represents the compliance and control of the business. This takes the form of policies, procedures and systems and is supported by the internal audit function and external auditor's review. It includes various information, accounting and reporting standards and practices.

T

Transparency	Is the ease with which an outsider is able to make a meaningful analysis of a company 's actions.
Triple Bottom Line	Reporting on the social including safety and health, environment and economic performance of the business. • Economic covers financial and non-financial information (Economic prosperity) • Environmental, the effect of the products and services on the environment (Environmental stewardship) • Social, covers values, ethics, relationships with various stakeholders (Social responsibility) Also referred to as integrated sustainability reporting.

U

Unitary Board Structure	The company has only one board of directors consisting of both executive and non-executive directors.

V

Value Reporting	Reports on the value drivers that creates and grows wealth for the shareholders and other stakeholders.
Values, Corporate Values	• The guiding moral principles for personal and corporate behaviour, e.g. fairness, honesty. • Standards of human conduct to which one should aspire.