A REVIEW OF THE ROLE OF THE BANCO NACIONAL DE ANGOLA

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DEDICATION

I dedicate this research to all the Angolan youth, to encourage them to contribute to the increase of Angolan academic literature.

DECLARATION

I, the undersigned, Rosa de Fatima Silverio Carneiro Mangueira, hereby declare that "A Review of the Role of the Banco Nacional de Angola", is my own work. It has never been submitted before, and that the sources used and quoted have been indicated and acknowledged by means of references.

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The success of this research paper is a blessing from God, the One who believed that I was capable of writing this report.

I am grateful for having and feeling the Soul and Spirit of my mother, Helena da Costa Carneiro Mangueira there for me, consoling my pain by giving me the strength to carry on with that long journey.

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ABSTRACT

The object of this study is to examine and analyse the dynamics of central banks. The central bank in any country has a great impact on the economic and monetary issues within its jurisdiction. This research is based on a case study of the economic and monetary crisis in the Republic of Angola resulting from the prolonged phases of civil war.

The study will focus in particular on the role of the Banco Nacional de Angola, the central bank of Angola. This bank has a very important role to play in the post-war phase, since it is the only institution capable of inspiring confidence in national and international markets. In this period the country has been closely observed by foreign investors who are believed by this researcher to be the only guarantee for an immediate development of the country.

The study points out the main periods of economic crisis, emphasising their main causes and origins, and suggests ways of overcoming these problems on the path to economic recovery from the ravages of the war. Furthermore it examines the manner in which monetary policies are monitored and implemented within the Angolan framework.

Emphasis is given to the fact that the Angolan central bank was highly controlled by the state. This is due to the lack of financial resources at the state's disposal. It is believed by this researcher that the main problem of central banking in Angola is inefficiency in terms service delivery, which has had a significant impact on the quality of its functioning. This study gives some suggestions for possible tools for better performance of the central bank, so that Angola can move towards a better future.

This researcher has used qualitative data from secondary sources, exploring and analysing existing information from resources such as journals, reports, legal documents, as well as banking and government sources. This researcher has also collected and analysed national and international laws and legislative policies regarding central banks in general, and the Banco Nacional de Angola in particular.

ABREVIATIONS

BNA – National Bank of Angola (Banco Nacional de Angola)

BPA – Popular Bank of Angola (Banco Popular de Angola)

CCBG – Committee of Central Bank Governors

COMESA - Common Market for Eastern and Southern Africa

IMF – International Monetary Fund

MEFMI – Macro-economic and Finance Monetary Institute

SEF – Programme of Economic and Financial Rectification (Saneamento Economico e Financeiro)

SADC – Southern Africa Development Community

ZEP - Preferential Trade Area of Eastern and Southern Africa

CHAPTER ONE

Introduction

1.1 Background to the Study

Since the beginning of 2002, the Republic of Angola has attracted renewed attention from foreign countries and companies interested in investment. This is because of its potential, particularly in terms of the exploration of its natural resources. It is therefore important to consider the role of the Banco Nacional de Angola (the National Bank of Angola) acting as the central bank, since, through monitoring its performance, potential investors can gain confidence in investing in the Angolan economy.

This study provides the reader with an overview of the concept of a central bank, with emphasis on its relationship with the government. This is illustrated by a case study focusing on the levels of dependence and independence of the Banco Nacional de Angola (BNA) with respect to the government in power.

The civil war in Angola from 1975 to early 2002 had a great impact on the role of the BNA. The war resulted in a lack of technical and human resources, and consequent inefficiency and ineffectiveness. During this period the government acted as owner of the central bank, so the BNA was totally dependent on the government and had no say in major decisions made concerning itself.

This research paper has been written in a period of transition from war to a free and democratic environment within Angola, so it discusses the role of the central bank, based on an international standard, and examines how close the performance of the BNA is to that point.

1.2 Problem Statement

Central banks around the world could be classified as the 'heart controllers' and regulators of economic and financial issues within a given country. In Angola it may be time for structural changes in the role of the central bank. Such changes could be made possible by adopting international standards for central banks.

The banking system is a key instrument in economic growth all over the world, and especially in the establishment of national and international market-economic relations. In addition, as the main institutions for designing monetary policies, central banks have particular functions and responsibilities, such as being regulators of the balance of payments, controlling price fluctuations and stabilising currencies. In summary a central bank should function as the coordinator of all activity of commercial banks and other financial institutions within a country.

However, in Angola the situation is different. The National Bank of Angola (BNA) does not function as a fundamental player in terms of the establishment of market prices in the domestic economy. Decision making is still performed by the central government, through its major ministries such as the Planning and Finance. This precludes the BNA from functioning as a central banking institution well-designed monetary policy based on a liberalised economy. In addition, the BNA is facing a problem of inefficiency within its banking system, which has had a negative impact on the Angolan market economy. Consequently the bank's capacity for competing with other financial partners has been reduced, in particular within the Southern African Development Community (SADC) region.

The BNA is unable to perform as a central bank should, for a number of reasons. These include:

- a high degree of control by the government over the BNA;
- an unclear definition of the role of the BNA;
- the public perception of the role the BNA;
- inefficiency and ineffectiveness in the functioning of the BNA.

1.3 Research Assumptions

1. The high degree of interference by the government in the functioning of the BNA has impacted negatively on the manner in which the bank performs.
2. The high degree of interference by the government in the functioning of the BNA is primarily due to its over-reliance on BNA funding for meeting public needs and interests.
3. The lack of sound policies with regard to the banking and financial systems has led to weaknesses in the practice and functioning of the BNA.

1.4 Objectives of the Study

This study does the following:

- examines the relationship between the BNA and government;

- examines the BNA as a source of funding of the government;
- identifies the main obstacles that the Angolan central bank faces;
- aims to prove that the Angolan central bank is a key instrument for positive financial and economic development of the country.

1.5 Methodology of the Study

The researcher relied heavily on secondary sources of data. This method was adopted to circumvent the limitations associated with gathering primary data within the time frame and available resources for the project. It also allowed this researcher to be guided by or use the sources as a gateway to new information that might meet the needs of this study. These sources included books, journals, reports, conference proceedings documents, government publications and the Internet.

1.6 Significance of the Study

The circumstances of the National Bank of Angola are not ideal and its achievements do not fulfil those expected of a central bank with respect to internationally recognised standards. Thus this research paper performs a critical analysis with the aim of identifying problems, in order to inform academics and other experts in the field, as well as governments and other institutions. These constitute a key group influencing policy-making designed to repair the unstable Angolan economy, particularly in respect of monetary issues. This paper should thus help the Angolan government to review the situation, and hence correct mistakes and provide solutions with regard to the way policies have been designed and implemented in the light of central bank standards.

1.7 Literature Review

Central banks exist in more than 170 countries, to "regulate their economies".[1] Their functions vary from one country to another. This can be explained on the basis that the theory and system of central banking was not clearly defined when central banks first began to appear, although in several countries there was a unique and specific bank which issued money and was therefore known as a "Bank of Issue" or "National Bank" (de Kock, 1974, 8).

Rapid changes within the structure of financial systems worldwide have attracted enormous attention in academic and policy circles. Berger and Humphrey (1998, 175-212) conducted a survey of 130 papers analysing the level of efficiency of central banks within 21 countries. Most of the existing studies are, however, devoted to the financial sector of developed economies, the only exception being recent special issues of the Journal of Banking and Finance (2000) that give an overview of topics related to the development of the financial system in transition economies.

There has been an increasing interest in the study of central banks and their independence from government. Eijffinger (1997, xi) shows that in recent years academics and policy makers have shown a greater interest in the independence of central banks with respect to the formulation of monetary policy. They stress that a high level of central bank independence, together with an explicit mandate to aim for price stability, forms an important institutional device for maintaining price stability.

Numerous theoretical and empirical studies have stressed that lack of autonomy of the central bank and a high level of inflation are negatively related. Even though some writers, such as

[1] http://www.law.nyu.edu/centralbankscenter (Miller)

Goodhart (1995, 60-67) and Eijffinger (1997, xi-xv), specialise in this subject they do not provide a clear definition of what central bank independence entails. It is therefore important for this researcher to reiterate that central bank autonomy should be seen as referring to the relationship between the central bank and government.

There is limited literature on the role of the central bank in Angola. Available literature deals strictly with comparing the Angolan central bank with the international standards, or demonstrates its specific functions as agent, adviser and banker for the government and other financial institutions. Some sources available to this researcher, such as the Report of the BNA (May 2001, 1-6) and the BNA Law of 1997 (ibid., 15), show that the Angolan central bank is dependent on the government in the sense that most monetary policy decisions are taken by the government through the Council of Ministers, even though the BNA constitutes the major monetary policy adviser in the country. This researcher is of the opinion that the central bank could perform a more independent function if the country itself were run within a stable political and economic situation. Government interference in personnel, financial and policy matters within the central bank has reduced its level of autonomy, making it difficult for the bank to achieve its aims and objectives.

Concerning independence in personnel matters, namely the appointment of the governing body of the central bank, Eijffinger (1997, xii) argues that it is quite impossible to exclude government influence. This is because the governing body must be able to guarantee the interests of the state, since the bank is administrator and manager of the economic reserves of the country. Downes and Vaez-Zadeh (1991, 103) support this line of thought by stressing that the head of the central bank, the Governor, is appointed by the State President, and the State President has the right to remove the Governor in case of illness or on the "request of the Board". The BNA Law of 1997 also stresses that the Board of Directors, including the Governor, has to be appointed by the Head of State. However, the issue of concern appears to be related to the amount of state involvement in central bank matters. Scholars such as Alesina and Tabelini (1987, 619-625), and Cukierman (1992, 353-370) for example, acknowledge the importance of state intervention but at the same time emphasis the importance of independent functioning of the central bank. Factors such as unclear definitions of dependence contained in laws and documents as well as the political and economic instability that the country went through have impacted on central bank functioning. Most of the literature related to the financial autonomy of the central bank shows that it is not independent of government.

Eijffinger (1997, xii) observes that it is in the government's interest to exert an influence over the central bank's activities. He states that this is particularly the case when the government needs to finance its own expenditure directly or indirectly through the central bank. In the Angolan case, the government is sometimes unable to finance its own expenditure and therefore it does not simply influence the central bank, but is in fact the main player in decision-making regarding financial and monetary policy. This should normally be the responsibility of the BNA.

In terms of policy independence, the BNA Law 6 /97 (1997, 3) gives some independence to the bank in the designing and conducting of monetary policy, since the bank is the formulator, administrator and supervisor of the national Angolan financial system. This point is underlined by Eijffinger (ibid), who also emphasises that the formulation and execution of monetary policy has been put in the control of the central bank. In many countries the dominant conceptual analysis of central banking, from after World War II until today, is associated with an economic vision that might be defined as a Keynsian system of monetary policy (Downes & Vaez-Zadeh 1991, 121). Economic and financial programmes in Angola are based on foundations of neo-liberal policy.

Todaro (1997, 608) suggests that monetary policy focuses on two fundamental economic variables: the aggregate supply of money in circulation, and the level of interest rates. A greater money supply induces the expansion of economic activity by giving people the capacity to purchase more goods and services. This is called the monetarist theory of economic activity. Some scholars of economics believe that, by controlling the growth of the money supply, the governments of industrialised countries can regulate their economic activity and inflation. On the other hand, Keynesian economists believe that an expanded supply of money in circulation increases the availability of loanable funds. According to this perspective, a supply of loanable funds in excess of demand leads to lower interest rates. Private investment is assumed to be inversely related to prevailing interest rates, and thus business people will have the capacity to expand their investments as a consequence of the fall in interest rates, which will in turn allow credit to become more readily available (Downes & Vaez-Zadeh 1991, 121-123).

Furthermore, Todaro (1997, 609) stresses that the description of monetary policy in industrialised countries illustrates its complex nature. He gives two important features that developing countries need if they are to implement a model policy. The first is related to the ability of the governments of developed countries to expand and contract their money supply in order to create conditions for raising and lowering the costs of borrowing in the private sector. Secondly, the financial system in developed countries is economically highly organised and is based on interdependent systems, thus facilitating the existence of efficient and well-functioning money and credit markets. This situation does not, however, hold in developing countries, since the markets and financial institutions in these countries are in most cases disorganised, externally dependent and fragmented. The International Monetary Fund (IMF) and the World Bank have encourage many developing countries to embrace structural and institutional reforms of their financial systems.

Other financial components such as inflation, exchange rates and balance of payments must be taken into account when considering reform of monetary policy. The major structural reform proposed is the financial functioning of the central bank as an institution autonomous from government, in order to achieve accountability and transparency in a free market economy. This reform of total autonomy in most developing countries, particularly in Africa may be unattainable as central banks do not operate in a decentralised system; most of them are attached to the government. Their function must be understood in terms of the framework of regulation which may decrease the ability of the market to function competitively, and this is the case in Angola according to the Angolan legal framework of 1997.

Economic reform in Angola has resulted in some very important achievements such as the transformation of most of public enterprise into private enterprise, transparency of public expenditure, and control of fiscal taxes. Nevertheless, gaps remain in the efficiency of the implementation of reform in legal and economic policy frameworks, as well as in administrative areas influencing the regulation of the economy. Given the dramatic improvement in its economic performance, the Angolan government remains firmly committed to consolidating and accelerating the reform process through monetary policies under which the central bank has the major responsibility of ensuring that these policies are implemented (Relatorio Annual do BNA 1999, 6).

Scholars such as Heffernan (1996, 109) and Roux (1999, 123-127) support the notion that the scope and space of reform differs from country to country. They focus on two main areas: liberalisation and balance sheet restructuring, which concentrate mainly on removing interest rate ceilings and other controls. It is important to stress here that in the case of Angola most of these reforms are currently ongoing and seem to be successful, with new management of the central bank and a new government economic team, although the highest level of achievement has not yet been met.

Increased access to financial services is essential in improving the performance of banking systems in developing countries. In addition, special attention should be given to improving the quality of and access to services, in order to increase competition.

1.8 Outline of the Chapters

This study is organised as follows:

Chapter 1: - Organisation of the research paper; explanation of how the research was conducted; aims and objectives of the study; basic assumptions; methodology of analysis; significance of the research paper, and related literature.

Chapter 2: - An introductory framework for the reader: a brief history of the central bank and its role within a country, emphasising the relationship between state and central bank in terms of the bank's dependence on or independence from government.

Chapter 3: - The role of the BNA (the Angolan central bank). This chapter is also an attempt to analyse the political transition within Angola from 1975 to 1992 and to explain its impact on the dynamics of the BNA. The chapter examines the manner in which monetary policies are monitored and implemented.

Chapter 4: - This chapter sets out some of the challenges which have been facing the Angolan central bank since 1992, when, for the first time, the Angolan people went to the polls to vote for democratic political change. This has impacted on economic and financial institutions within the country, and on the whole social environment. The intent of the chapter is to illustrate the strengths and weaknesses of the BNA, based on the findings of this research study, by giving emphasis to the relationship between the central bank and the government. It will also show the need for confidence in the banking system in Angola on the part of the public and possible foreign investors.

Chapter 5: - This chapter summarises and concludes the study by highlighting the main points of the paper for further research. This researcher is of the opinion that the BNA has a very important role to play at this stage in the reconstruction and development of Angola, and so this chapter puts forward some recommendations for new practice which could lead to better performance by the BNA.

1.9. Limitations of the Study

The study was severely limited by a lack of literature on the topic. There was, however, relevant material that this researcher was able to collect through the World Bank and the IMF, because these institutions are still monitoring the Angolan financial system and conducting studies designed to serve their own interests. There are no textbooks or academic literature specifically concerned with the functions of the central bank in Angola. The shortage of literature on Angola does not always reflect the reality of the country.

DELIMITATION OF KEY WORDS

1. Central Bank – Refers to a financial institution responsible for issuing currency, managing foreign reserves, implementing monetary policy, and providing banking services to both the government and commercial banks.

2. Efficiency – Can be understood as the measure of production performed by a designated person in a competent or proficient manner.

3. Financial liberalisation – The condition for eliminating various forms of government intervention in financial markets. This for example allows for, supply and demand to determine the level of interest rates.

4. Foreign investment – Overseas investments by private multinational corporations.

5. Inflation – The term is used here as defined by Archer (1990, 7) to describe a situation where movement in the average price level of goods and services is upward. A period of above-normal general price increases as reflected, for example, in the consumer and wholesale price indexes. More generally: the phenomenon of rising prices.

6. Investment – Refers to that part of national income or national expenditure devoted to the production of capital goods over a given period of time.

7. Money – Any currency legally recognised and used as a trading medium.

8. Monetary Policy – Practices and procedures designed to regulate and influence financial variables such as money supply, interest rates, prices etc., within a nation.

9. Macroeconomic –Refers to the economy as a whole within a nation, concerning the total amount of goods and services produced, total income earned, level of employment of productive resources, and the general behaviour of prices.

10. Reform – The moral, political or social changes that occur in a society, in order to amend or correct wrong doings.

CHAPTER TWO

The Evolution and Development of Central Banks

2.1 Introduction

This chapter provides a brief history of central banks, as recognised in the international arena, and illustrates the role of a central bank within a country, giving emphasis to the relationship between the functions of government and central bank. In addition the chapter discusses theories regarding the independence of the central bank, based on different schools of thought. The chapter concludes with a summary of the main points discussed.

2.2 Reasons for the Appearance of Banks

At this stage it is important to give a brief idea of what economics is about, because it is through the ideas of economics that central banks came into being. Roux (1999, 4) defines economics as the study in which "mankind employs scarce resources to satisfy its many needs". In other words economics is a subject that deals with people and their behaviour within a society, in response to their financial capacity and according to their desires – as buyers and consumers – for goods and services. Together with these go those who produce the goods and services, based on the demands of the public they serve.

In order to fulfil this type of exchange, argues Salomon (1997, 31), there was a need to create money as a trade regulator and as an acceptable mode of payment for goods and services, especially in the period of transition from subsistence economy to the era of specialisation and exchange. Drake (1980, 57) underlines this by arguing that the increasing number of goods available to people led to a "rise in the utility of money". It is within this perspective that banks were introduced, as safe-keepers of gold and silver, which can be translated as "money standard fit", according to Salomon (1997, 15-21).

Today money is presented in different forms such as notes, coins and cheque deposits, representing standard measures of value. The increasing development of industrial firms has greatly influenced the expansion of banks and concomitantly the administrative banking system worldwide. Banks play the role of intermediaries between depositors and borrowers (Heffernan, 1996, 15).

2.3 The Origins and Operation of the Banking System

It is believed that banking systems were established as far back in time as ancient Greece. One of the main functions of banks at that time was making loans, testing and exchanging coins, and providing credit transactions and deposit facilities. At this time the only forms of money were coins and bullion; a note currency did not exist (Chamber's Encyclopaedia, 1966, 99).

At that time the responsibility for the money in the market was in the hands of two groups, known as brokers and "scriveners". The scriveners were mostly lawyers, who specialised in drawing up commercial contracts and thus came into contact with those people who had money to lend and others who wished to borrow (Encyclopaedia Britannica, 1974, 699).

In this tradition, in 1694 the Bank of England was the first to perform in a way similar to today's central banks by being the only bank legally responsible for issuing money. The Riksbank of Sweden is also considered one of the oldest. The English banking system is the direct ancestor of modern commercial banks, and at that time (17^{th} century) acted as custodian of private cash and gold reserves of the country (de Kock, 1974, 1-3). England still plays an important role in the creation and development of the monetary system of banking. In fact, up to today, as Roux (1999, 96) argues, a large portion of the world's foreign reserves consists of gold, whose value is dictated by the London Stock Exchange on its gold price fixing, process that occurs every month.

Banking outside London developed later, but most banks were created during the second half of the 18^{th} century, and the 19^{th} century. One of the major banking systems was the merchant banks, which dealt with goods and exchange bills by lending money and monitoring payment accounts (Encyclopaedia Britannica, 1974, 700).

2.3.1 The Role of Commercial Banks

Ordinary 'commercial' banks function as intermediaries between the producers and the consumers of goods. They fulfil functions such as being custodians of much of the public's money, and they provide a system for easily-made payments that eliminates the need to pay in 'hard' cash. They also advance funds to credit-worthy customers, for personal or business purposes, in the form of overdrafts, fixed-term loans, mortgages, instalment sales (hire purchase) and lease agreements. These banks invest funds, and trade in various types of assets, mainly of a monetary nature. In addition they provide sundry financially-oriented services to customers, including the purchase and sale of foreign currencies (Jacquillat & Feiger 1982, 1-6).

Central banks, however, do not deal with the public directly, but work with governments, commercial banks and other financial institutions, acting as an institution for the accumulation of money reserves (De Kock 1974, 2-3). A central bank must monitor organisational structures such as the relationship between the central bank and other institutions in the financial market, and the manner in which government policy decisions are taken. It must also take note of the strategies of commercial banks in terms of the development of the banking system as a whole.

2.3.2. Central Banks and their Relationship with Commercial Banks

Commercial banks are profitable institutions whose major source of income is the interest they charge on advances to people and firms who need their services, to borrow or to save through depositing money. Kelly (1988, 3) describes their activity as a business which consists mainly of "acceptance of deposits of money withdrawable by cheque", and Heffernan (1996, 16), says that commercial banking consists of "wholesale and procedure retail" banking activities.

Unlike central banks, commercial banks provide the means of making payments and loans to individuals or companies. Central banks on the other hand (which mostly came into being around the 1940s) are mainly bankers to government and lenders to commercial banks or to other financial institutions (Chamber's Encyclopaedia, 1966, 96-98). The money they hold is in the form of metal – usually gold and silver – with a value which they attempt to maintain at stated levels over time. In other words, central banks are responsible for maintaining currency convertibility under the gold standard.

According to Miller,[2] more than 170 countries today regulate their economies through central banks. Despite many deficiencies, the Bank of England, established in 1694, was the first bank which could be characterised as a 'central' bank, as seen from a modern perspective. In several countries, such as England and Sweden, a unique and specific bank issued money and was therefore known as a "Bank of Issue" or "National Bank". However, as de Kock (1974, 8) mentions, the theory and system of central banking were not yet clearly defined. By the beginning of the twentieth century the concept and purpose of central banks was fully accepted, and led to many independent nations establishing their own central banks. By 1950 there were 59 of these, and 161 by 1990. The increase in the number of central banks reflects the main means of business settlement and transaction within the global financial system.[3]

Central banks have two distinct roles: the macroeconomic one of establishing and regulating price fluctuations in order to avoid inflation, and the microeconomic functioning through which the stability of the banking system is enforced. It is important to point out that central banks are not private institutions; they depend on the government and its policies, based on consensus between government and the central bank.

Commercial banks are out in the market, therefore they are fundamentally competitive, in order to attract customers. Central banks, however, act as sponsors of governments (BIS Policy Papers 1999, 80-83). This researcher is of the opinion that one of the most important functions of central banks is providing a degree of balance and security to commercial banks, especially in a period of liquidity crisis.

[2] http://www.law.nyu.edu/centralbankscenter
[3] ibid.

2.4 Central Banks Acting as Government Agencies

Since government has certain welfare functions, it needs a degree of power over the central bank, in order to prioritise the demands of the essential public services it has to provide.

The central bank acts as a controller of currency and monetary policies, especially in periods of war or crises. In a period of political instability therefore, the nature of financial crisis is complex – influenced by the environment which has a negative impact on the political, economic and legal systems of the country. There is a tendency for greater and more complex difficulties to exist in the conditions that the central bank has to deal with (Downes & Vaez, 1991, 215).

Conflicts can also arise between central banks and governments because the central bank may have no clearly designated function, nor independence from the government. In cases such as Angola and Nigeria, the responsibility of the central bank, in terms of the formulation and execution of monetary policy, is to prescribe by legal act. Because of the power of the government, and as a result of the ambiguity in the delimitations of its powers and functions, situations might occur in which government interferes with and violates what has been declared as law. As Emenuga (1996, 417) points out, the Nigerian Federal Minister of Finance "personalised the policies of the central bank, by using the personal pronoun 'I' when referring to intended policies and actions of the bank." (This is nothing new, because even the Bank of England, before being established as a central bank, had been run with some influence and even interference from government.[4]) However recent views express the opinion that "if central banks were less susceptible to government pressure, they would maintain lower inflation" (Goodhart 1995, 61). The independence of central banks is the current approach used by some governments such as South African.

Governments are the biggest borrowers from central banks. This arises partly due to the privilege and right of central bank to issue notes (De Kock, 1974, 38). Another way in which the central bank contributes money directly to government is the outright purchase of government bills.

Central banks today play six major roles:

- Monopoly issuer of currency: for example foreign exchange reserves consist of gold and foreign currency stock (the latter translated into dollars). One method used by central banks to avoid inflation and to control the national currency in their favour is to sell dollars in the market in order to prevent devaluation or depreciation (Roux 1999, 107-110);
- Bankers' bank: central banks are the main producer of new bank notes and coins and the safe-keeper of all banks' reserves;
- Regulator of commercial banks, price of credit and the amount of money available in the economy;
- Lender of last resort: commercial banks may face "insufficient funds to conduct their daily business" in which case they may borrow money from the central bank, paying interest in the same way as individuals who borrow money from a commercial bank;

[4] http://patriot.net/~bernkopf/

- Conductor of monetary policy: different measures are implemented by the central bank in order to achieve its economic objectives, such as establishing equilibrium in the balance of payments.
- International transactions: central banks are involved in the international transactions of a country relating to assets, liabilities, gifts and services. These involve the so-called balance of payment accounts, which have several sub-accounts. In terms of foreign direct investment, these transactions constitute part of the financial or capital account. Therefore in one way or another the central bank has to be involved, because it is required intervene in a meaningful way for the management of assets (Carbaugh 2000, 353). For example, the Coca-cola company and its relationship with its subsidiary in Angola.

2.5 Central Bank Independence

This section deals with the principles of measurement of independence of central banks, as used by some schools of thought.

Eijffinger (1997, 68) asserts that the key elements in the status of central bank independence entail five principles:

- prohibition of lending to public sector authorities;
- independence of instructions from governmental authorities;
- determining the exchange rate;
- provisions for the personal independence of board and council members, and
- constitutional status for the central bank's statutes.

Eijffinger considers these five elements to be fundamental in assessing the extent of a central bank's independence. He emphasises the first principle, focusing on the existence of a broad consensus in terms of the objective of price stability – which requires a free monetary policy – without the traditional obligation of financing public sector budget deficits. This demonstrates his view that there are often insufficient measures to rule out direct lending, but he believes that it is essential to reduce or eliminate the loan link between central bank and government.

The second principle refers to the fact that a central bank cannot exist independently if it must obey instructions from government or other authorities. This principle calls for the governing body of the central bank, or the central bank council (which might need to be explicitly provided with full authority), to decide on the target of monetary policy, mechanisms, means and implementation procedures, as well as details of the bank's internal organisation and, last but not least, on the budget (Eijffinger, 1997, 69). Formal independence from any government instructions might be considered as an important step in determining the level of independence of a central bank.

Goodhart (1995, 69) argues that an independent central bank has some advantages in that government ministers and treasury officials may "lose the power to control short term monetary policies, and fiscal policy itself may become more disciplined". This cannot occur if the statutes governing the bank entail an obligation to support general economic policy. Such an obligation would give a government the right to ask for an expansionary course of monetary policy at any time, although it might not be possible for the central bank to comply fully with such a request.

The third key principle is based on the idea that the major objective of price stability is not really in conflict with exchange rate stability. A price stability objective means that the central bank must be provided with full power to decide on all exchange rates and to intervene in matters of monetary and financial regulation. If the central bank is required by government to fix the exchange rate permanently at a certain currency value, it would obviously lose its ability to control the domestic price level over the medium to long term.

This opinion is supported by Goodhart (1995, 67) who argues that governments have never been willing to delegate to central banks the "right to take strategic decisions on exchange rate regime" in the context of monetary affairs. He states that such delegation occurs in most countries with formally independent central banks, and also in countries where central banks are not independent – although he believes that it can also occur if influential public opinion can demonstrate that changes in the exchange rate regime are not favourable to the public's needs and priorities. Thus flexible exchange rates are more acceptable than fixed rates. Once again this underlines the importance and power of law when it prescribes the functions of the central bank.

The three principles enunciated are fundamental, but not sufficient to assure a status of independence for a central bank. Another importance factor influencing independent functioning of a central bank relates to the competence of members of the bank council. If the members of the bank council lack professional competence, knowledge and expertise effective implementation of monetary policy could be jeopardised. Therefore professional competence within the governing body and the central bank itself are necessary in order for council members to fulfil their responsibility.

Goodhart (1995, 68) states that central bank statutes can be changed by a simple majority in parliament, but he carries on to say that most politicians across the world have never supported or trusted the independence of central banks. The reason for this is that, by keeping their influence over the functions of the central bank, they accommodate their own interests, such as the budget. As politicians, they base their interests on their desire for re-election. Despite the negative influence on price stability, they are able to use their power to respond to the demands of public or particular interest groups, especially those of the financial sector. It appears therefore that, although central banks are not allowed to choose their objectives, they can nevertheless be autonomous in choosing the manner in which government-defined objectives for the banks will be achieved. Eijffinger (1997, 104-105) suggests that those governments which require only a bare majority to modify the statutes of their central bank may threaten the integrity of the bank if it does not comply with basic government requests. It is therefore important for the central bank to have constitutionally enshrined statutes.

Cukierman et al (1992, 353-360) have developed broad measures for estimating the independence of a central bank. These can be fruitfully used in analysing the level of independence of the BNA. Cukierman et al uses three guidelines: the legal index, the rate of turnover of central bank governors, and the rate of inflation.

As regards the legal index, the legal independence of a central bank is based on laws that explicitly confer such status on the bank. This would entail four major factors:

- The set of objectives of the central bank;
- Limitations on a central bank's ability to lend to government;
- Policy formulation, mainly as regards mechanisms for conflict resolution between the executive arm of government and the central bank on monetary policy issue, and also the role of the central bank in budgeting;

- The terms and conditions of employment of the Governor, including the right to appoint and dismiss him/her, or to determine his/her term of office.

Objectives of the central bank would include price stability, stable banking, full employment, and the provision of services to allow the bank to act as government agent in the commodities market. The level of central bank independence is measured mainly against a listing of such objectives, which should be stated in its charter. One of the main purposes in applying these objectives as a measurement of legal independence would be to ascertain the degree of freedom of the bank in the pursuit of price stability and similar macroeconomic objectives, without recourse to other arms of government. Using such criteria, the degree of independence is considered higher when the bank has a mandate to achieve price stability than when it does not. Independence is also rated as being higher when this is a major or even a sole mandate, rather than when it is one of many others, such as higher economic growth and full employment.

In the case of multiple objectives, the pursuit of full employment, for instance, provides a ready excuse for inflation, when in fact inability to control inflation may be a symptom of the bank's eroded authority in monetary control. It is suggested by Cukierman et al (1992, 57) that the degree of a central bank's independence is considered to be greatest when it has sole authority in the formulation of monetary policy. They also say that independence will be low where the bank is a partner of the government and its only function is that of adviser, so that it has little influence on other government agencies. Finally, independence is zero if the central bank has no effect on monetary policy.

With regard to the terms of employment of the bank governor as a measure of independence, there are four important factors.

- His/her term of office should ideally be at least four years. If the length of the term of office is left to the discretion of the state, independence ranges from a low point where the governor's tenure is short, through growing degrees of independence, up to a case of full independence if the statutory term of office is more than eight years.
- Another important measure is based on the authority to appoint the governor, again ranging from a low point if the executive arm has the authority to appoint him/her, to a high one where the central bank appoints its own chief executive.
- The third factor lies in the case of dismissal of the central bank governor, where a provision for unconditional dismissal constitutes prejudice of the bank's degree of independence.
- The level of independence could be said to be low if the governor is legally restrained from holding other political office (Eijffinger, 1997, xv-xxv).

It seems very difficult to determine the level of independence necessary to allow for the effective and efficient functioning of a central bank because of the variety of opinions and assumptions about central bank independence. This researcher is of the opinion that the State must exercise a level of control over the central bank. This opinion is influenced largely by two interrelated factors. The first is the state's role in ensuring that public interests are met. The second, related to the first, is the state's role in the economic and financial stability in the country. Therefore, as Eijffinger argued (1997, 104-105), "making the central bank an agency with a mandate to maintain price stability constitutes a means by which a government can choose the strength of its commitment to price stability".

According to Eijffinger (1997, 214-216), economists and practitioners in the area of monetary policy mainly support the idea that the degree of independence of the central bank from government affects the rates of expansion of money and credit through important variables such as inflation and the size of the budget deficit. However, the central bank's authority and its scope of action may depend on the government. Nonetheless, in many cases governments pass laws or pursue policies that grant to their central banks authority and autonomy to ensure price stability, even in cases when this conflicts with other government objectives. Thus price stability constitutes a key factor – though not necessarily a sufficient factor – in the development of the local capital market where government and business can borrow conveniently and cheaply in the long term.

Pursuing price stability may compete with at least some of the other tasks assigned to the central bank; tasks which it can and must fulfil: mainly managing government's financial transactions, and financing government deficits with money issue.

Considering the various issues raised concerning the quality and degree of independence of the central bank, the independence of the central bank not only depends on the law but must also include other structured factors such as informal arrangements between the bank and other government institutions (ibid).

Analysts such as Eijffinger and Goodhart limit their focus of central banks on the law. This gives rise to two problems. Firstly, in most cases the law does not clearly specify limits on the balance of authority between the central bank and the government. A second problem is that, even where the law is explicit, practices frequently deviate from those prescribed by law. Even when the law prescribes a clear mandate in terms of the level of independence and scope of authority of the central bank, there is a tendency for government to violate this authority in the interests of political gains. However this does not mean that legal independence is not an essential element in measuring the degree of central bank independence. But laws differ in focus, scope and degree of detail and this sometimes results in unclear laws or the misinterpretation of laws regarding central bank independence.

This researcher believes that the degree of independence of a central bank cannot solely be measured according to legal stipulations. One should examine the relationship between the state and the central bank by taking into account the scope and authority of the central bank functions. It is quite impossible for a central bank to enjoy complete independence from government, although the best way to ensure that status would be through legislation on the limits of authority of the central bank.

Halme et al (2000, 34) assert that the field of law-and-economics provides a background for examining the economic effects of legislation. Thus, they say, the normative viewpoint goes beyond a positive analysis of economic effects and takes a position either for or against various regulations, in order to achieve the most effective legislation. Here the law should be seen as an important instrument that establishes rules which are complementary to economic activity. Without these parameters it would be impossible for any economic agent to operate within the framework of the real world of business.

At this point it is important to bear in mind that central bank independence has its positive side in that this independence encourages more fiscal discipline, improvement in the bank's performance, and reduces the level of politicians' interference. Goodhart (1995, 66-68) despite his focus being limited to that of the law, expressing views on central bank independence which extends to issues of inflation. He argues that the more the central bank is autonomous from the government, the more a country will experience lower inflation rates.

2.6 How Central Banks Conduct Monetary Policies

In examining the relationship between governments and central banks the issue of monetary policies and the way in which they have been conducted arises. Downes & Vaez-Zadeh (1991, 11-15) believe that the central bank should be guided by a monetary policy, normally designed by monetary authorities in a qualitative manner. This allows for two things: First that public demands are appropriately responded to. Second, that the financial structure of the country is developed as a whole. They argue that this is also one way of bringing about monetary control, especially as regards the issuing of money, which is the responsibility of central banks alone. They emphasise that the design of any monetary policy should be based on sound public finances, especially if the desire is to maintain price stability and avoid conflict between the public sector and monetary discipline.

In this context Roux (1999, 123) gives some elements on which monetary policy should be based in order to achieve a country's economic objectives within a sound economic environment. These are: regulating price fluctuation through economic activities and money circulation; regulating the payments system; guaranteeing the international value of the currency; and keeping inflation low. He believes that these are preconditions for the short term performance of a stable economy which will lead to long term growth within a country.

Goodhart (1995, 61) believes that governments should see monetary policies as an important instrument to control inflation in the medium-term. This cannot, however, be implemented in isolation, but it should rather be enforced by other measures such as fiscal and counter-inflationary policies, in order to achieve price stability. Sundararajan, et al (1997, 11) point out that inflationary finance has in most cases originated in order to enforce "explicit or implicit tax expenditures and subsidies for distressed production sectors of the economy".

Monetary policies can be controlled by legal provisions of bank supervision and regulatory functions related to certain specific activities. Sundararajan et al (1997, 167) argue that this control and supervision should be directed towards objectives which will allow financial strength. The process should, however, follow normative procedures in order to permit analysis of the manner in which the work was "gathered, processed, evaluated and acted upon". The information collected should be supervised in such a way that priority can be given to those areas where attention is most needed. Here the objective is to provide adequate and quality information to policy-makers for use in decision making. Goodhart (1995, 93) emphasises this point by indicating that monetary policies are normally primarily exercised through reserve requirements, since the central bank is the institution which keeps the currency and deposits of other banks, to "refinance facilities that are mainly market based, and to a limited extent [permit] auctions of treasury bills or central banks liabilities."

2.7 The Influence of International Banks on Central Banks

In the mid 1940s two powerful monetary institutions, the International Monetary Fund (IMF) and the World Bank – also known as the International Bank for Reconstruction and Development – were created, and came into official existence in 1946. They arose from an idea conceived during the United Nations Monetary and Financial Conference in 1944 in Bretton Woods, United States of America (Kelly, 1988, 158-159). The World Bank had great success after the Second World War in helping European countries to resuscitate their economies.

Some the objectives in the creation of the IMF were:

- To promote international monetary cooperation and stable international credit facilities;
- To promote exchange rate stability;
- To assist in the establishment of a multilateral system of payments;
- To make general resources temporarily available to members experiencing balance of payments difficulties (under adequate safeguards);
- To shorten the duration and lessen the degree of disequilibria in the international balance of payments deficits of its members.

(Kelly, 1988, 158-159)

The World Bank on the other hand deals exclusively with economic and development programmes in countries which are considered poor, by broadening and strengthening their economies and preventing them from collapse. It works with governments, and also with non-governmental organisations (NGOs).[5]

Although the IMF and the World Bank were designed for different purposes, they have similar objectives, viz. to help countries in economic need – as long as those countries are members of these institutions – and they work together in close coordination. In practice almost all members of the IMF are also members of the World Bank, although the IMF has 182 member nations, while the World Bank has 180.[6]

In a sense, the IMF and the World Bank are cooperative institutions, which lend money and at same time give economic advice directly to governments through a process of negotiation between institution and government, based on consensus. With some exceptions, they also

[5] http://www.cftech.com/BrainBank/FINANCE/IMFHistory.html
[6] ibid.

assist selected private sectors in financial trouble. As part of the contract, those receiving aid have to adhere to certain conditions, such as having a sound macro-economic policy.[7]

These two institutions collect and exchange information on the monetary and financial problems of the country in need, in order to be able to give advice on the formulation of corrective policies. Their relationship with central banks, argues Kelly (1988, 159), is mainly concerned with exchange rate stability, which should "reflect the true tendency of the balance of payments". He/she continues by saying that in relationships with international institutions, the central bank acts as adviser, agent and representative of the government with respect to financial and monetary issues.

Every IMF or World Bank member country pays a membership 'quota'. If a country borrows back more than 25% of its quota, this must be repaid within a period of three to five years, during which time these institutions require governments to implement political and economic reforms.[8]

The world-wide establishment of central banks can be attributed to the growing realisation that, under modern conditions of banking and business, it is a great advantage to any country, irrespective of its stage of economic development, to have centralised monetary reserves, with the control of currency and credit vested in one bank which has the support of the state and is subject to some form of state supervision and participation.

[7] http://www.cftech.com/BrainBank/FINANCE/IMFHistory.html
[8] ibid.

2.8 Chapter Summary

This chapter gives an overview of the development of central banks across the World. These banks originally appeared merely to regulate the flow of money as an acceptable mean of payment for goods and services. The Riksbank of Sweden and the Bank of England – created in the middle of the 16th century – are considered to be the oldest central banks with characteristics similar to those of modern central banks.

There are differences between central banks and commercial banks. Central banks deal with financial institutions and particularly with governments, acting as their banker, agent, adviser and lender of last resort, but commercial banks are profitable institutions, which deal directly with individuals.

Central banks are not entirely independent since, some of their functions are influenced by government's monetary policies. In other words, some of their functions are determined by the power of politicians. It seems to be quite impossible for a central bank to become an institution truly independent of government. Even if a central bank is independent in terms of its functions, it cannot be independent of government decisions made in terms of monetary policy, nor be independent of the laws determining its authority. Thus the role of central banks is not fully determined by any theoretical framework, because in practice such a framework could not always be complied with. Nevertheless the central bank does enjoy exclusive privileges relative to other banks and financial institutions.

CHAPTER THREE

History of the Banco Nacional de Angola

3.1 Introduction

The aim of this chapter is to provide an overview of the banking system of Angola, more specifically in the post-independence uniparty-ruled period, when the central bank was first introduced (November 1975). It is an attempt to analyse the role and dynamics of the Banco Nacional de Angola (BNA) as the central bank, in relation to the political, social and economic environment at the time.

3.2 The Birth of the Central Bank in Angola

The government that came into power after the independence of Angola in 1975 had confiscated and nationalised commercial farms, private businesses and the banking sector as a whole. In 1976 the socialist system resulted in the government's direct intervention in the finances and economics of the country. This had a negative influence on the economy of the country: it created an imbalance in macroeconomic terms, affecting the balance of payments, inflation, and so forth.[9]

All economic activities were controlled by the state which at that time was not subordinate to a parliament, but rather to the party in power – the Movimento Popular de Libertação de Angola - Partido do Trabalho or MPLA (PT) (World Bank Country Study 1991, 8). This was according to the provision of Angolan Law 69/76 of 5 November 1976. The national

[9] http://www.1upinfo.com/country-guide-study/angola/angola52.html

currency, the Kwanza, was also created at that time (by Law 71-A/76) and put into circulation on 8 January 1977, from which time the old colonial currency was no longer valid.

In 1976 the new Angolan government created a banking structure by reconstituting the old Commercial Bank of Angola (SARL) as the Banco Popular de Angola (BPA), which was defined as a bank of capitation and savings. In addition, the Bank of Angola was transformed into the National Bank of Angola or Banco Nacional de Angola (BNA), a central bank, based in the capital, Luanda. By Law 69/76 of 5 November 1976, the BNA took on its role as issuing bank, government treasurer, and commerce banker.[10] Angola had been one of the few countries without a properly defined central bank, so the creation of the BNA changed the functioning of the entire Angolan financial system.

The main macroeconomic function of the Angolan central bank is to preserve the value of the currency, in other words to maintain price stability in the banking system. A special statute (number 69/76), characterised the BNA as a public enterprise of finance and credit, subordinated to the Ministry of Finance.[11]

From 1978, based on Law 4/78 (of 25 February), banking activity in Angola was regarded as the exclusive domain of the state banks, and private commercial banks were closed. This allowed the BNA to extend its activities across the whole country.

As described in the World Bank Report of 1991 (13-14), the Angolan economy was heavily dependent on imports up until late 1988, and thus required foreign currency. The central bank, in coordination with the Ministry of Foreign Trade, licensed foreign exchange for enterprises and special interest groups, by draft on the Kwanza equivalent. The only business that earned

[10] http://www.bna.ebonet.net//bnahis.htm
[11] In addition there was the regulation of insurance activity, which was given solely to the state-owned company, the Angolan National Insurance Company (ENSA), established in 1978. Later, in 1981, all private insurance companies were liquidated and their activities transferred to ENSA.

foreign currency through exports was the ENDIAMA, which exports diamonds, and the Sociedade Nacional de Combustiveis de Angola (SONANGOL), which exports oil. These companies held their earnings in the BNA in foreign currency. Most of the money collected as revenue was based on crude oil and diamonds, as the government was the only legal exploiter of these natural products. In fact diamonds and oil functioned as a direct source of income and payment (Cilliers & Dietrich, 2000, 119-121). During that period, there was no other significant industrial activity, and agricultural activity was minimal because of innumerable and uncontrolled land mines.

According to Cilliers & Dietrich (2000, 8-9), the government sometimes paid its accounts directly through the above-mentioned companies during the war period in Angola. This resulted in expenditures without discussion and approval from the Ministry of Finance or the central bank. These authors point out that, in a politically unstable period, levels of accountability and transparency in government payments and expenditure are not likely to be as high as they would be in peace time. This is because the government budget itself is not "unified" and is sometimes even mismanaged as demonstrated above (ibid, 9).

3.3 Effects of the War on the Functioning of the Angolan Central Bank

The Angolan war began as far as back as 1961. However, its effects on the normal functioning of the central bank were only visible from 1975, the year in which the country achieved independence from Portugal. The political transition from one government to another was not peaceful, with ongoing-armed conflict between the various political parties and the armed forces of the former Portuguese colony. At independence, the MPLA came into power, but this was disputed by belligerents such as the Força Nacional de Libertação de

Angola (FNLA) and the Unidade National de Independencia Total de Angola (UNITA). The war continued between the new government and the UNITA rebels until 2002.

The post-1975 period had a great negative impact, not only on the financial economy of Angola, but also on the political and social arenas. Cilliers & Dietrich (2000, 26-30) classify the Angolan war as a "resource war". They state: "abundant natural resources can motivate conflicts to secure state control or secede, and involve foreign intervention." This researcher contests this point because the war in Angola was not, in the primary stages, based on the control of resources, but was related to the struggle for political power after the decolonisation of the country. It is important to note that UNITA had been mobilised to war on ethnic grounds rather than to gain "resources".

The period between 1975 and 1992 witnessed heightened interference and control in the activities of the BNA by the state. During the 27 years of war, the banks and banking system of Angola were gradually weakened, and the demand for borrowed money was very high. The Gross Domestic Product (GDP) was low or even non-existent, with very few loans available to individuals or state-owned enterprises. As this researcher has already remarked in Chapter 1, war has a negative impact on the economy of a country, and in the Angolan case, it had a huge influence on the central bank in terms of monetary policy making, the management of those policies, and their implementation (BNA Relatorio Anual, 1999, 6).

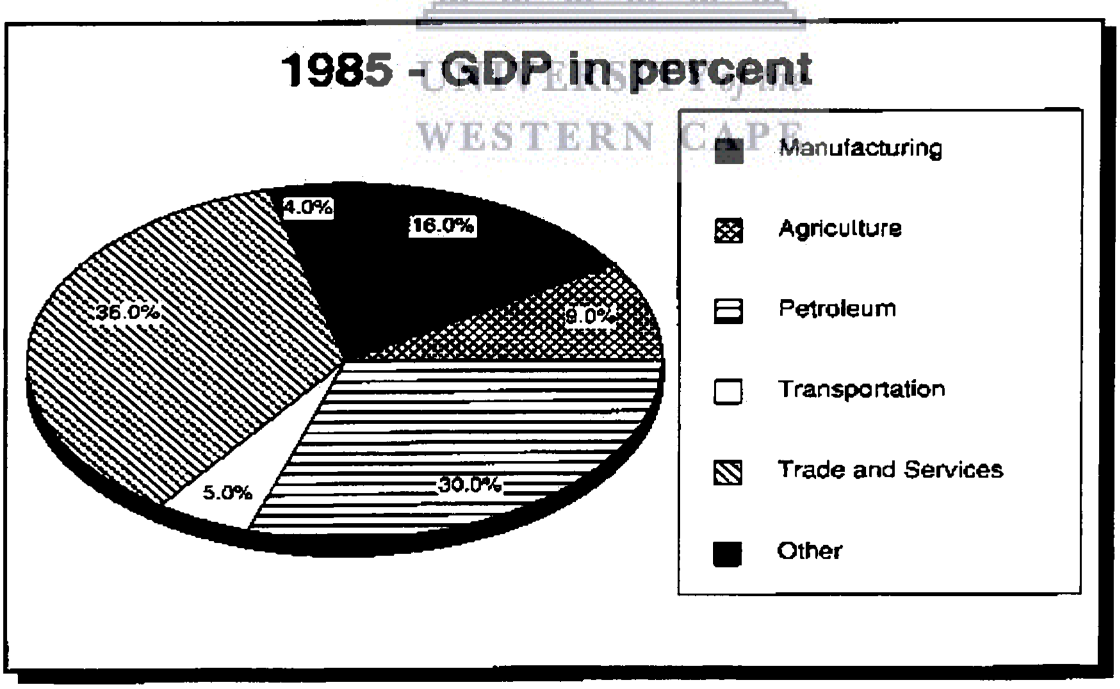
The over-dependence on oil and diamonds as a means of obtaining foreign income resulted in the lack of attention on other sectors. There was, for example, a complete absence of agricultural and industrial production. Most durable and non-durable goods were imported, especially from Europe and Brazil. For many years after independence, because of the lack of competition in the market, the state owned at least 60% of the value output of goods produced within the country, i.e. 60% of its GDP. The Angolan state was the largest proprietor, the greatest exporter and importer, and the largest employer in the economy. It was the largest consumer of resources, the largest debtor and the largest investor (Cilliers & Dietrich 2000, 8).

Since the dollar is internationally recognised and used on the monetary exchange standard market, the demand for dollars was several times higher than the BNA could afford, and on top of that the government had no real control of its own expenditure. This provoked instability in the banking and economic systems within the country. Downes & Vaez (1991, 16) argue that there is an invisible positive impact on the role of the central bank in the economy of a country if it is unable to implement adequate development within the financial system in terms of "both size and diversity". This is especially true in developing countries such as Angola where illegal activities such as the exchange of foreign currency in the 'informal sector'[12], has had a great impact on the formal sector. For example the BNA was the only legal institution authorised to deal with foreign currency. It functioned as a bureau of exchange, with certain restrictions, especially for enterprises. During this period the financial system was not efficient enough and credible, in the public eye, in other words, there was no culture of savings through the banks, because of the rapid and increasing devaluation the Kwanza. Furthermore the increased demand for foreign currency and the inability of the central bank to meet the demand encouraged the development of a "parallel foreign currency market"[13], namely the foreign black market. This period also reflected unhealthy state intervention in the determination of exchange rates.

[12] The informal sector, also known as the parallel market or *kadonga*, is those self-employment activities exercised by people who "earn a living" outside of the parameters of legal economy system (Adamu, 1996, 309).
[13] http://www.state.gov/www/about_state/business/com_guides/1999/africa/angola99_08.html

The impact of political instability on the economic activity of the country led in particular to the government's inability to supervise and control the economy effectively. For example, the supervision and control of fiscal policies resulted in a higher level of government expenditure on imported military equipment The lack of internal industrial capacity and very low economic productivity meant that the country relied increasingly on the import of machinery and food. Because of the populist economic policy that the country had embraced, there was a lack of clear monetary policy, and thus no clear role for the central bank. The political instability led to a non-functional economy which affected the transportation and distribution network available to the population as a whole, especially in 1980s.

The graphic on the next page[14] demonstrates how the Growth Domestic Product (GDP) was accessed in 1985.



[14] http://lcweb2.loc.gov/frd/cs/angola/ao03_01a.jpg

This graphic shows that, during 1985, oil made up 30% of the GDP, whereas agriculture contributed only 9%. Agriculture, although considered a traditionally significant sector of the Angolan economy, was not able to perform adequately, as a result of the impact of the political instability that the country was undergoing at the time. As a consequence, the growing parallel market increasingly undermined the government's efforts to implement measures for achieving better production and distribution of goods. The researcher believes that the factors mentioned above negatively affected banking activity which, in various ways, constitutes one of fundamental elements of the economy. This was particularly significant in regard to price stability which, in the context of this discussion, was remarkably important, because of difficulties encountered by the general population in the accessing of goods.

3.4 Dominance of the State over the Central Bank

Because the banks were owned, controlled and dominated by the state, it was difficult, if not impossible, for the BNA to perform its role properly as a central bank. After independence, the MPLA government decided to centralise the entire economy. Until the late 1980s, the National Bank of Angola and the Popular Bank of Angola (BPC) were the only banks with branches in all provinces (World Bank Country Study 1991, 20-21). Banks were very remote, and were not computerised. Because of the war, a great 'brain drain' of bank clerks and other personnel occurred, as many rural people fled to towns, especially to the capital Luanda. The performance of those bank employees remaining in country areas was of a very low standard. On top of that, most of the Portuguese citizens who abandoned the country transferred their accounts and deposits to banks in Portugal, and thus escaped repaying their loans.[15]

[15] http://www.bna.ebonet.net//bnahis.htm (A Banca de Angola: sua Criacao, Historia e Desenvolvimento p. 3)

In some areas where employees had fled to the cities because of the war, branches of the BNA and BPC had to be closed. Consequently the accounts of the BNA did not reflect their real assets: the bank was unable to control its finances because large amounts of information were lost, or transmission of information was delayed, making it impossible to trust the given figures. To keep better control of its foreign currency, the BNA created a special branch, named Direcção de Operações Internacionais (DOI). This later became the Bank of External Commerce, and was used for national and foreign exchange operations. However that form of "bank" was not organised and did not follow central banking standards in controlling foreign accounts and exchange (BNA Relatorio Annual 1999, 6-7).

The war also had a great effect on the delivery and quality of essential services to the population. In a normal situation, the Angolan government would have acted as provider of essential public services such as education and health, for the benefit of all Angolans. As Riruako (2002, 45-46) argues, it is the responsibility of government to ensure quality of service, which should be accessible to all. During the war period, such services were subsidised in full by government. However, the lack of infrastructure made it difficult, if not impossible, to monitor the quantity and quality of services like water. Hence, water and electricity charges were not paid for by the consumers. This was not only attributed to the lack of or poor infrastructure but also to a lack of technical resources and trained staff. Furthermore not everyone could afford to pay rates and taxes because the standard of living was so low. Cilliers & Dietrich (2000, 119-121) estimate the average income in Angola in the mid-1990s as being equivalent to US$10 per month.

The BNA, especially between 1975 and 1992, acted as a commercial bank as well as functioning as the central bank. Although there were few private enterprises, they were in some sense dependent on government decisions, which limited their autonomous economic activity as profitable enterprises. There was no open market competition; the lending process was decentralised, and administrators at BNA headquarters determined interest rates. Government and commercial enterprises were required to make their deposits in the BNA, while other organisations and individuals had to make use of the Banco Popular de Angola (BPA) for depositing. In any case the public did not on the whole use banks for depositing money, since the instability of the Kwanza had led to rampant inflation, which did not encourage saving. The BNA had also to deal with constant financial losses, mainly caused by:

- A high degree of interference from the government;
- Fluctuation of the exchange rate because of the depreciation of the national currency, the "New Kwanza" (earlier "Kwanza");
- Non-payment of revenues from the pendent operations and transactions that the bank assumed on behalf of the state
- Non-payment of credit security granted to the state and other financial institutions.

During that period the central bank was the sole player in the determination of money supply and also the only source of credit for most enterprises (World Bank Country Study, 1991, 21).

We see that the government tended to abuse its powers of control over the central bank, increasing money creation and, therefore, inflation, because government spending usually exceeded its reserves. Downes & Vaez (1997, 371) state that this often occurs when central bank gives credit to government, especially when this is done at a low interest rate, thus leading government to "increase expenditure, jeopardising macroeconomic stability and deteriorating the financial position of the central banks."

Thus conflicts arise between the government and the bank. The government has both the power and the incentive to force the central bank to give priority to their immediate needs. For more than ten years, during the war in Angola, the function of the BNA was not properly defined (this will be discussed in more detail in Chapter 4). Capie [16] argues that tensions arise between state and central bank in its functioning as "lender of last resort". In such a case, the government will have failed to find other ways to finance its plans or policies and, as a last resort, have to use its assets at the central bank. During the period 1975 to 1992 the Angolan government did not have any visible source of revenue or funds – which would normally have come from taxpayers, either directly or indirectly. This had a great negative impact and influence on the Kwanza and on exchange rates, bringing uncontrollable and continuing inflation to the market.

3.5 Monetary Policy in the Period 1975 - 1992

The crisis in the Angolan economy can be attributed in part to a lack of sound economic policies and to high-level government decisions controlling and interfering in monetary matters. In most cases government monetary policies were well designed but bank officials lacked the capacity and resources (as stated elsewhere) to properly implement such policy. This meant that the expected output could not be realised. Most of the government's economic plans were incomplete or did not achieve fulfilment, and this affected the performance of the central bank in areas such as price control for goods and services, and foreign exchange rates, with a great negative impact due to external (international) factors. In many cases monetary policy was designed to fit government needs and "the fluctuation in the net foreign assets of the BNA" (World Bank Country Study, 1991, xviii-xix).

[16] http://patriot.net/~bernkopf/ - The Evolution of Central Banking

The BNA had control over its branches around the country; for example all credit limits for commercial enterprises had to be approved by the governor of the central bank. The BNA was the only source of credit available to these enterprises, to be used exclusively for wage payments and the acquisition of commercial goods. Most BNA loans were made to the government to benefit state-owned enterprises, or were used to cover government expenditure when government exceed its receipts. In fact there were no credit limits on government and public enterprises before 1990.[17]

3.5.1 Foreign Exchange Control through Ministries

The foreign exchange budget was drawn up by members of the Ministry of Foreign Trade and the Ministry of Energy and Petroleum, with assistance of the BNA. The Ministry of Planning also had a major role to play in the process. The BNA did not, however, have much influence in the implementation and outcome of this document. It was, nevertheless, the responsibility of the BNA to enforce the implementation by ensuring that each ministry produce a report related to its "foreign exchange expenditure" (World Country Study, 1997, 14).

Foreign exchange used to be allocated according to economic and social priorities pre-established by the government and reflected in the annual foreign exchange budget through the Ministry of Foreign Trade. In fact there was lack of coordination between the Ministry of Foreign Trade and the central bank, especially concerning the availability of foreign exchange for import enterprises. In some cases these enterprises were refused access to foreign currency (dollars expressed in kwanzas) by the BNA unless they obtained a licence from the referring ministry. This was not necessarily a fully effective measure, but it was one way that

[17] www.angola.org/business/b_mon.htm (Monetary Policy)

government could limit the number of goods being imported. It also acted as a step towards overcoming the balance of payments crisis – although not necessarily the most effective measure – and towards protecting foreign exchange reserves.[18]

3.6 The First Structural Economic and Financial Reform in Angola

In 1987 the programme of Economic and Financial Rectification (Saneamento Economico e Financeiro - SEF) was first introduced. The objective of this plan, which was monitored by the World Bank and the International Monetary Fund (IMF), was to restructure the banking system in Angola, in order to overcome the economic crisis that the country had been going through.

The SEF was a very encouraging programme as it was a set of reform measures whose goals were to adjust and control prices, especially those of goods and services. Its objective was also to reduce inflationary pressures, bring exchange rate stability, reduce the budget deficit, and improve accounting systems and administrative controls. This was to be accompanied by personnel training programmes. Thus it would increase efficiency in the use of "scarce financial resources" and better control the money supply by basing it on adequate policies (World Bank Country Study, 1991, 21-23).

The SEF was a monitoring programme designed by the IMF in collaboration with the World Bank (which had distributed guideline manuals). It was a programme which could have been successfully implemented in a stable political environment. This however, was not the case in Angola; although at the time the programme was implemented positive signs regarding the end of war were quite visible. The main objective of the SEF was to reduce budget

[18] http://www.state.gov/www/about_state/business/com_guides/1999/africa/angola99_08.html

expenditure, especially regarding the allocation of subsidies and defence costs. Other issues to be addressed were the stimulation of agriculture, which was unviable due to the uncontrolled number of anti-personnel land mines, dating from the time when farming areas were used as battle fields.[19] However the programme was not effective in bringing about economic and financial stability in Angola. Williams (2000, 245) believes, that in most cases foreign donors tend to ignore the political and economic environment of a country. This, in his opinion, results in the failure of programmes like the SEF, that could quite possibly bring about change in a politically stable environment.

Not much has improved since the implementation of the SEF programme in 1987. It appears to have failed in its main purpose of dealing with the economic and financial crisis. One of the major causes of its failure has been attributed to unsound policy measures.

Despite the inability of the SEF programme to bring about complete economic and financial stability in Angola it did have certain positive effects on the functioning of the central bank. Firstly, the programme led to the closure of the commercial functions of the BNA, allowing its establishment exclusively as a central bank, and thus acting as an incentive to competitive commercial banking. The intent was also to give authority to banks to borrow money with a guarantee of repayment, thus reducing the level of inflation. This meant however, that the BNA needed to increase its investment in human resources, through training and development programmes which would lead to an improvement in its administrative banking control (World Country Study 1997, 158-164).

[19] www.ebonet.net.bna

Secondly, the BNA was able to achieve some level of independence from government in areas such as credit decisions and interest rate measures, thus increasing confidence in bank services. Commercial enterprises had also reduced their dependence on government by becoming more financially independent. There were however certain requirements that they had to follow in order to be allowed to borrow from the central bank. These included guaranteed "prospects for repayments" of loans (ibid.).

Thirdly, better performance by the BNA would increase the confidence of domestic economic agents and their foreign partners in the future of the Angolan economy. This could impact significantly on international trade collaborations. And hence enhance economic growth of the country.

3.7 Chapter Summary

The National Bank of Angola lost its power, control and special privileges because of the political and military upheaval, and the consequent economic instability within the country. In particular, the central bank could not be expected to play its role and conduct its responsibilities according to international standards at this time. Although some countries are able make an economic recovery after such circumstances, this was not the case in Angola. The intent of this section was to provide some insights into the political instability created by the war on the economy of Angola, and more specifically on its monetary system.

There was an attempt to rectify the economic and financial mistakes registered in the Angolan banking system, and in the economy as whole, in 1987. The SEF was the first programme with a significant impact on economic change in Angola. It was monitored by the IMF and the World Bank but failed to achieve its goals regarding the strength of the Angolan currency, reduction of the budget deficit, better control of public finances and prices in the market. Most of the objectives of the programme were not accomplished because of the lack of a political and social environment suitable for applying such an ambitious reform plan.

It is important to understand that, in such a period in a developing country such as Angola, the national bank acts mainly according to the dictates of the government in power and its interests, instead of being complementary to the government's economic development policies. This is partly because accountability and transparency are not practised, and the power of parliament is stronger than it would be in a democratic environment.

CHAPTER FOUR

The Banco Nacional de Angola within a Democratic Environment

4.1 Introduction

The purpose of this chapter is to analyse the role and functions of the Banco Nacional de Angola (BNA) after Angola's first democratic elections in 1992. It analyses the functioning of the central bank as a key operator in the economic and financial development of Angola. Finally the chapter attempts to demonstrate the actual level of autonomy of the BNA in the post-transformation period.

4.2 The Role of the BNA in Economic and Financial Development

This section deals with the key role played by the BNA, and its impact on the economic growth of the country. The beginning of the 1990s witnessed dramatic changes in the functioning of the BNA. The economic, social and cultural environmental changes in the country led to the central bank adopting a more efficient, effective and competitive system, based on modern banking strategies. In fact, international pressures from institutions like the IMF and World Bank, together with the challenges of globalization, demanded a more effective, efficient and competitive banking system.

The transition from a central planning economy to a market economy in Angola was not the easiest, since it had to incorporate the transition from a single political party

system of governance to a multi-party democratic system. Accelerating institutional change in both sector and market transition was recognised as a fundamental aspect of such a transition. Economic and political uncertainty placed a heavy load on social arrangements in the past (because of the civil conflict). It is this researcher's view therefore that economic reform should include the introduction of new institutional mechanisms and structural changes necessary to stabilise the economy and take a further important step towards recovery. These changes will be discussed below.

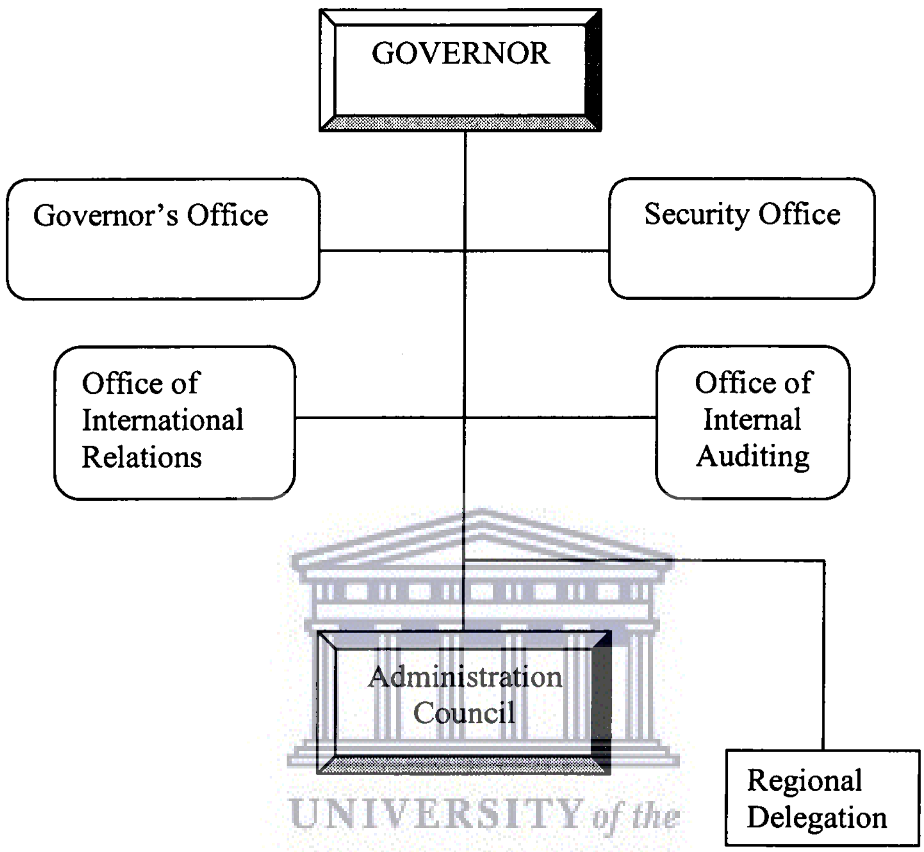
4.2.1 Organic Structure of the Banco Nacional de Angola

The process of change within the BNA started in 1991 with its functions being likened specifically to that of an internationally recognised central bank. The BPA, on the other hand, became a department of the BNA. From that time on, the government began to implement reforms of the financial sector. The Organic Law of the National Bank of Angola and the Law of Financial Institutions created a banking system with two main levels. The installation of the central bank at the one level and separate commercial banks at the other level. This brought to an end the monopoly of the state in the financial sector.

The new Board of the BNA consists of a Governor, who is head of the institution and chairman of the Board of Directors, a Deputy Governor, and five Executive Directors, as shown in the following diagram.[20]

[20] http://www.bna.ebonet.net//breve.htm

BNA organic structure



The governor of the central bank and his/her deputy are appointed by the President of the Republic of Angola, on the recommendation of the Prime Minister, for a term of office of five years, which can be renewed. The President has power to remove them on grounds of illness, or for other reasons that might put at risk the running of the bank. Although the Governor and the Deputy are not members of the Cabinet they participate in its meetings, and are expected to attend parliamentary sessions if there is a need for clarification regarding financial or economic issues. Furthermore it is the responsibility of the Governor, as the head of the Board, to ensure the implementation and effectiveness of economic and monetary policies, as well as to conduct relations with the Ministry of Finance, the Ministry of Planning and the Council of Ministers, and to represent the central bank in international forums. The Executive

Directors, who form the Board, are appointed by the Council of Ministers, on the recommendation of the Governor, with a five-year renewable mandate.

By Law 6/97, BNA Act of 1997, Article 38, the Governor of the BNA is accountable to the Council of Ministers, and must issue opinions and prepare reports for and on all matters relating to its dealings. This means that the central bank is accountable to government, and not to parliament or any other political institution. However, in the event that a matter pertaining to the central bank has to be explained or clarified it is the Governor of the BNA that has to appear before parliament.

The non-interference from politicians and subsequent independent functioning of the BNA only became apparent in 1997. In fact, the period after 1999 was known as the "New Era" of the banking system in Angola. This was also the first time that the Angolan central bank opened itself to a form of transparency in its accounting by allowing external auditing of its records and documents. This signified a tendency towards greater ideals of transparency, openness and accountability.

4.3 Legal Guidelines for the Financial and Economic Activities of the BNA

For a country to be part of the modern world-market economy, its central bank must be seen as a fundamental element of the financial system in general and the banking system in particular. The availability of finance for enterprises, and the potential to restructure and improve competitiveness in transition economies, depend critically on the level of the efficiency and capability of the banking system.

The New Organic Law, promulgated for the BNA in 1997, was drawn with that perspective in mind. The central bank acts in two main ways:

1) As monetary agent of the exchange authority, separate from commercial functions;
2) As authoriser for the formation of the following financial institutions:
   - Financial institutions such as commercial banks and banks of investment or development;
   - Special institutions of credit, such as designated cooperatives and mutual credit holdings for insurance institutions.

The Law of Financial Institutions has regulated the exercise of credit functions and the constitution of other institutions of private capital, both national and foreign. Besides the BNA, Angolan national banking was composed of two commercial banks, constituting a shareholders business using public capital. These were the Bank of Insurance and Credit (BPC) (previously the BPA) and the Bank of Commerce and Industry (BCI). The BCI was created to support the expansion of productive capacity in the piscatorial and agriculture sectors, as well as for increasing production of other essential goods.[21]

By the end of 1991, therefore, the BNA no longer allowed individuals to open deposit accounts, in either local or foreign currency. In addition, a programme was approved suspending commercial activities by the central bank in Luanda, and this was later applied to its branches in the rest of the country. These changes allowed the BNA to start functioning as a central bank is intended to function and was hence in line with international practices.

Having an open economy in a liberalised market system has led to the need for profound adjustments in the BNA philosophy. These changes in the economic management of the

[21] http://www.angola.org/internet/

country, resulted in the redefining of the executive and functional duties of the BNA as central bank, issuing bank and exchange authority.

Central banks are needed because of the unique nature of the banking business. Commercial banks hold deposits that are redeemable for money on a first-come-first-served basis. Therefore to ensure sustainability of a commercial bank there has to be a constant flow of funds. To prevent a run, bank assets should be marked to market. But this is impossible in the case of the BNA, because of the nature of its assets.

Under the new 1997 BNA law, the BNA is able to delegate to commercial banks and exchange houses the authority to engage in exchange operations. This is based on fixed rates dictated by the BNA, since the BNA has the responsibility and authority to act in the primary foreign exchange market. But there are still other functions that remain within the responsibility of the BNA. For example, all imports and exports are subjected to a previous licence from the BNA, as is capital transfer. Essentially the BNA halts administrative price fixing in the exchange and monetary market, and uses the market to determine equilibrium prices.

The profound change in driven monetary policies and exchange had an immediate positive impact.[22] The central bank has been able, over the last few years, to drop the level of inflation, which had stood at triple digits for most of the past decade. It was running at well above 200 percent per year in 1999 and 2000, before moderating to 'only' 116 percent in 2001. With spiralling inflation, the Angolan currency, the Kwanza, depreciated 97 percent between January 1999 and the end of 2001.[23] Indeed, the main function of the central bank is ensuring

[22] http://www.angola.org/internet/
[23] http://biz.yahoo.com/ifc/ao/ (Country fact sheet)

local currency stability so that this can bring economic stability, with a sound and prudent monetary policy in place.

The decentralisation of some operations in the BNA and the loss of its commercial character as a banking system also positively influenced the banking and financial system as a whole. Increased responsibilities of commercial banks, awareness amongst the public of a culture of savings, increased borrowing to the public, among other things, demonstrated the changes in the banking industry. But the banking system seemed not to have found a solution to the financial problems facing the country because of the huge crisis in the finance arena. The crisis which the financial system of Angola faces now cannot be attributed solely to a lack of organisation in the system of the central bank: international shocks in the financial market should also be taken into consideration.

4.4 The Relationship between the Central Bank and the State

The relationship between the central bank and the state is based on two fundamental forces. The BNA is the banker of the government, and is, at same time, a credited monetary institution authorised to act on behalf of the state. This means that it has competence to create conditions for the stability of the monetary system and solutions for financial matters within or outside the country. De Kock (1974, 35-36) argues that the central bank operates as government banker because this is convenient for the government and because of its ability to establish a connection between public finance and public affairs. The relationship between the BNA and the state is, therefore, characterised by the following:

4.4.1 Government Banker

As government banker the BNA executes its duties and responsibilities in a similar fashion as does commercial banks with their ordinary customers. It has the following responsibilities and powers:-

- keeping the accounts of all government ministries and government institutions;
- safe-keeping of funds proceeding from any international financial organisation of which the country is a member;
- allowing the state an overdraft facility up to a limit equivalent to 10% of current receipts of the state collected in the previous year;
- accepting government deposits of cash, cheques or drafts;
- undertaking transactions drawn on other banks, and can transfer government funds from one account to another; and
- supplying government ministries and institutions with money for salaries or for other payments (BNA Law, Article 34).

In addition to these functions the BNA law also allows the bank to make foreign currency available to the state for its expenditures abroad, either to service debts on loans provided by foreign countries or institutions, or for purchasing goods – Angola is still importing more goods and services than it exports. These transactions should be based on an agreement between the central bank and the state, as foreign exchange is the only means of paying accounts from outside the country (Law 6/97, Article 32).

According to Article 35 of the 1997 BNA Act, the central bank may grant credits to the state, but these should not exceed the amount approved by parliament. If this amount is exceeded, however, the central bank should (i) inform the government accordingly; and (ii) advise the government on how to prevent future over expenditure.

Despite the clearly defined relationship and role of the BNA as government banker the history of central banking in Angola has witnessed a tension between the banks' function as maintainers of the value of the currency and their function as bankers to the government. According to its Organic Law (1997), the BNA acts as a "sole banker of the state." It therefore has a duty to advise the state on monetary and financial policies in particular, as well as in matters within the country in general. Article 16 of Law 6/97 gives power to the central bank to intervene on behalf of the government in its international monetary relations as well, and ensures the bank's function as a lender of last resort. The government should, in turn, protect the economy of the country in all possible ways.

4.4.2 Agent of the Government

The BNA, as agent for the government, administers the treasury's account, for which the bank effects payments "up to the limit of funds in its custody" and collects tax revenue on behalf of the government (Law 6/97, Article 36, 14). The BNA is co-responsible for the formulation of monetary and exchange rate policies and is largely responsible for the execution of these policies. However, in fiscal matters the bank only assists the government in collecting its tax income through the treasury account (BNA Estrategia de Desenvolvimento do Sistema Financeiro 2001, 1). The BNA also acts as representative of the government at financial institutions, namely the International Monetary Fund, the World Bank group and the African Development Bank.

4.4.3 Economic Adviser to the Government

The BNA assists the government in the design of the budget by providing consultancy services to the Finance Minister. This situation is extended to central and local departments of state administration in their credit operations. Abroad, the central bank participates in international negotiations dealing with loan contracting and consequently in debt-servicing arrangements. In the event that government holds accounts in banking branches internationally, or to use the services of other financial institutions, the BNA is responsible for advising government on the management of such accounts (Law 6/97, Articles 37-39).

The BNA does not only act as an economic advisor to the state but is also responsible for implementing new policies aimed at bringing about stability to the Angolan economy. The decentralisation of some commercial operations has therefore allowed the BNA to perform its correct role as central bank, especially in relation to economic agents.

A significant difference in the relationship between the commercial banks and their customers and the relationship between the BNA and the state rests in the fact that the government account is run free of charge. This, however, should not be so if there is to be a free market system. A free market system in the true sense would require the government being treated as a customer of the BNA. This would avoid any kind of abuse of power by the government in relation to the central bank, and would reduce the level of government interference into to the affairs of the bank.[24]

[24] http://www.angola.org/internet/

The relationship between the BNA and government appears to be clearly defined when reflecting upon the three dimensions just discussed. However, the existing arrangements still allow for a certain degree of political interference. Eijffinger (1997, 2) states that the government can exercise its influence on the central bank, for example, if the government finances its expenditure directly or indirectly through central bank credit. In such circumstances it seems that the bank has no financial independence. Granting direct access to central bank credit suggests that monetary policy is subordinated to fiscal policy. Indirect access may result if the central bank is cashier to the government or if it handles the management of government. This case scenario was apparent in the previous Angolan economic system (a central planning economy) in which the central bank was highly controlled by the government. And it still continues into the democratic dispensation where the BNA extends credit to the government when a fiscal debt occurs. The Treasury Department of the Ministry of Finance issues treasury bills for the amount required and remits them to the BNA. Government borrowing from the BNA may be granted up to the limit approved by parliament, namely ten per cent of the government's previous fiscal year revenue.

To ensure the independent functioning of the BNA its relationship with government should follow the path of accountability and transparency towards a real free market economy. This will allow for the central bank to perform its function as a complementary instrument of the government on monetary policy, without any kind of interference. Although such transparency and accountability are not yet reflected in reality, the changes in the financial systems of the country have been supported by the IMF and the World Bank. Reforms are aimed at achieving sound macroeconomic and microeconomic policies for economic growth, in which the bank will be the most important institution for ensuring economic stability.

4.5 The Impact of Institutional Reform on the International Economy of Angola

The institutional change in the BNA since 1992 has significantly impacted on Angola's ability to attract foreign direct investment. Most banks are still owned by the state, despite the processes of transformation and the importance of privatisation of the banking industry. This does not imply that the banking industry is not being privatised. It simply implies that privatisation is an ongoing process that will not happen simultaneously with political transformation. This phase of restructuring follows the reforms required by the World Bank and the IMF. Reduced interference by the state in banking matters and the consequent privatisation of the banking industry may also lead to the adoption of an acceptable monetary policy.

The remaining outdated legislation pertaining to investment is being reformed, and a wide range of policy measures has been undertaken to attract and protect foreign investment enterprises. At the end of 1999 the BNA was authorised by law (not yet published at that time), to begin permitting insurance activities by foreign and national private investors, with such activity no longer being a state monopoly (BNA Relatorio Annual 1999, 21-23). These incentives, coupled with low wage rates, and a stable social and political environment, make Angola an attractive prospect for potential investors. Its central location between southern and central Africa gives Angola a comparative advantage in the trade sector, as it provides easy access to some of the fastest-growing economies on the continent.

As financial markets develop and mature in Angola, a two-way interaction between financial and non-financial policies should emerge. The recent discoveries of oil fields and the world's biggest kimberlite pipe (rich diamond-bearing rock) have brought more capital investment into the country. A new era with peace and stability in the Angolan market would expose its economy to global financial systems, with the central bank fulfilling its responsibilities as a key operator in encouraging the new financial and entrepreneurship industries. These responsibilities call for continuous structural change within the financial system of the country – in particular of the central bank as it relates to currency confidence and stability – to make the Angolan market more attractive for investment.

4.6 Factors determining BNA Autonomy

Reflecting on the 'tools for measuring central bank independence' discussed in Chapter two of this dissertation one can determine the level of autonomy of the BNA in the democratic dispensation by focusing on these three key areas: legal provisions, the turnover rate of governors and the inflation rate.

4.7 Legal Provisions Relating to the BNA

Governments worldwide have controlled their economies through central banks, and the case of Angola is no different. Although the Organic Law (4/91) gives the BNA authority to guide, co-ordinate and supervise monetary policy, the bank is far from being effectively independent. Despite the political transformation and accompanying changes in the structure and focus of the BNA, the government still maintains control over the banking system, although the bank does have a certain level of autonomy to conduct its own activities. There is, nevertheless, co-operation between the central bank, the Ministry of Planning and the Ministry of Finance in determining monetary and foreign exchange policies, either privately or collectively.

However, some reforms have resulted in increased autonomy in the functioning of the BNA. More responsibility has also been placed on improving its performance and functions with regard to monetary issues and exchange within the country. This was as a result of the New Organic Law 6/97 of the BNA, passed and approved by Parliament in July 1997, and the Exchange Law 5/97, of the same date.

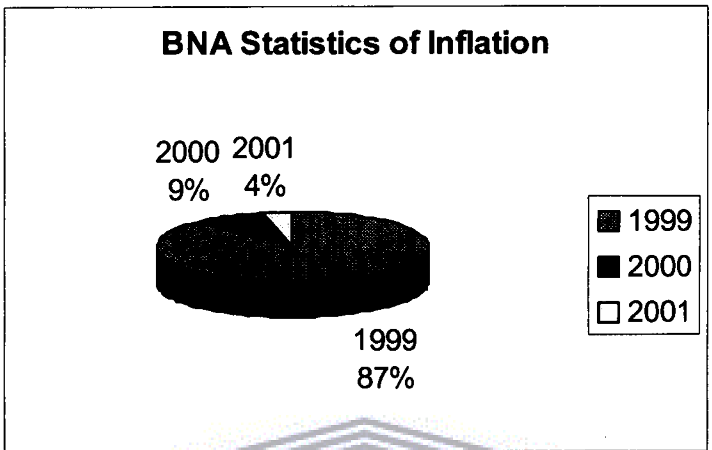
4.8 Appointment of Governor and Members of the Board to the BNA

An overview of the available documents about the Angolan central bank show that the BNA is not an independent institution. The way in which the board of the central bank is nominated is an example of this, because most decisions remain in the hands of government decision makers, who are, in turn, influenced by the legislative and political environment of the country. The outputs of the central bank are the result of its own policies, imposed by international institutions, and influenced by globalisation and the capital market. The BNA is however independent to the extent that it has its own budget and decides on how to manage its own finances.

4.9 Inflation Rate

Another measure of central bank independence is the inflation rate, with an inverse relationship to be expected between the rate of inflation and the independence of the central bank. The problem of growing inflation in Angola is still not under the control of the central bank, in part due to the existence of a huge informal finance sector. This especially involves informal currency exchange, which has significantly supported the informal market economy (BNA: Estrategia de Desenvolvimento do Sistema Financeiro 2001, 25).

A breakdown of inflation rates for the period 1999 - 2001 is shown in the graph below.[25]



As this graphic shows, the fall in inflation over these three consecutive years is a result of the government and the BNA implementing measures to bring monetary growth under control, and as means of attracting investors. An example of inflation in Angola is that in September 1999 it increased by 28.85%. Inflation in Angola might be considered as having a great influence on the informal market since in only three months it could increase by more than 50% against the exchange rate from the US dollar to the Kwanza. The level of discrepancy between formal and informal sectors was referred to in the Annual Report of the BNA, (Relatorio Annual do BNA 1999, 22-23). The fluctuation and increases in the prices of goods and services can be attributed to the fact that public demand is greater than availability.

Since central banks are more concerned with price stability than governments are, central bank independence should result in lower rates of inflation (Alesina and Tabellini 1987, 23,

[25] http://www.summitreports.com/angola2/introduction.htm

619). A mandate that allows the central bank to pursue price stability constitutes one of the indicators of legal independence, and also contributes – to a certain extent – to the lowering of inflation rates. Thus an absence or lack of central bank independence can be associated with a high rate of inflation. In addition, an inability to control growing deficits can result in a lack of central bank independence too.

It is important also to point out that the inflation rate in Angola has also been influenced by the pre-conditions for loans set by the IMF and the World Bank for the Angolan government. Those international institutions maintained that Angola must implement better "fiscal, monetary and structural reforms", in particular in the banking sector, to achieve economic growth and poverty reduction. The government has therefore continued designing and implementing measures to achieve that goal. In fact in this period, 1999-2001, oil production by well-known international oil companies, in partnership with SONANGOL, was increased. This, together with increased oil export, was a considerable help to the country both in reducing the national account debt and in increasing foreign exchange reserves (World Bank.org/afr/ao2.htm).

Some improvement in the banking system was registered, and in 1999 the Angolan economy presented two remarkably different images. On the one hand there was the negative impact of the resurgence of war, when the UNITA party refused to accept the results of the 1992 election, and decided to continue the military war, thus bringing economic uncertainty because of the continuing destruction of infrastructure. On the other hand the increase in the price of oil on the international market, influenced by the Asian economic crisis[26], had a positive impact. Since oil is one the main sources of Angolan income – as an export product

[26] East Asian countries were considered to be the fastest growing capitalist economies, but in late 1998 fell into crisis. Michie and Smith (1999, 18) consider the main reasons for this crisis to be misallocation of foreign capital inflows and over-investment.

and principal public revenue – this was a good period for the economy, and the cost of basic products fell.

4.10 Chapter Summary

The new democratic environment in Angola has allowed the BNA to set out on a course of continuing reforms, aimed at achieving the most appropriate policies for overcoming the economic crises that the country has been put through because of political instability.

The increasing independence from government interference which the central bank has been gaining should result in the effective implementation of economic policies. This is a step enforced by the BNA Law of 1997 which gives the central bank more autonomy, including the authority to perform as much as possible in conformity with international standards for central banks. It would involve the BNA being the banker's bank and advisor to the government and guaranteeing the value and stability of the Kwanza. The reforms are being monitored by IMF and World Bank, especially on issues such as decrease in government expenditure, transparency and better allocation of public finance resources, privatisation, liberalisation of the market and adjustment of prices.

Angola has undergone a social and political transformation in recent years which has created a new optimism within the country, especially now that it is politically stable. It is now poised to capitalise on its comparative advantage through greater cooperation with private sector investors.

CHAPTER FIVE

Findings, Summary and Recommendations

5.1 Introduction and Hypotheses

This chapter summarises and concludes this study by highlighting and discussing the major findings. The main objective of the study was to demonstrate the importance of the performance of the BNA as a central bank facilitating the economy of Angola in a period of transition, reform and foreign investment attraction.

The study hypothesised that:-

4. The high degree of interference by the government in the functioning of the BNA has impacted negatively on the manner in which the bank performs.
5. The high degree of interference by the government in the functioning of the BNA is primarily due to its over-reliance on BNA funding for meeting public needs and interests.
6. The lack of sound policies with regard to the banking and financial systems has led to weakness in the role of the BNA.

As stated in Chapter 1, the aims and objectives of the study were to:

- examine the relationship between the BNA and government;
- examine the BNA as a source of funding of the government;

- identify the main obstacles that the Angolan central bank faces;
- aim to prove that the Angolan central bank is a key instrument for positive financial and economic development of the country.

5.2 Findings

Angola is classified as a developing country which, for about 27 years, was ruled under political-military instability. The country has been facing huge economic and financial problems, of which high government interference in the functioning of the BNA and the bank's resulting inability to establish sound monetary policies have been identified as major factors.

Government spending in Angola grew over time, due to many and diverse factors. In addition to military and defence costs due to the civil war, there were inadequate economic policies (which led to a loss of transparency in government accounts), mal-administration of government revenue, and a lack of accountability. Authors like Dietrich, Cilliers and Eijffinger argue that it was quite impossible for the central bank to play its full role in the unstable political environment, and become independent of the government. They draw attention to this last point by classifying it as an unrealistic expectation in third world countries. The central bank had to supply money and lend to government and state-owned enterprises, even though their expenditure exceeded their means. The situation also permitted an excess of money in the market, thus increasing the level of inflation in an uncontrolled manner.

This section gives a summary of the research findings, under headings relating to the three assumptions made at the start of the work.

5.2.1 Findings Regarding the Relationship between the BNA and Government

The first assumption of this study was that there was a high degree of interference by the government in the functioning of the BNA, which has impacted negatively on the bank's performance. The BNA started acting out its functions as a banker's bank, agent and adviser of the government, issuer of currency and lender of last resort after 1992. In the period from 1975 to the early 1990s, the BNA did not function according to the delimitations of a normative central bank.

The ongoing civil war allowed the government to exercise an abnormal degree of control over the BNA. After the nationalisation of the banking industry – based on the socialist economic system adopted after independence – the BNA, besides acting as a central bank, took on the functions of a commercial bank, and was thus the only bank in the Angolan banking system.

During the war, production of oil and diamonds were the major sources of income for the government and agriculture was almost nonexistent. Furthermore fiscal control, including a proper system for payment of taxes, was lacking. A fixed exchange rate, the issuing of money by the BNA beyond planned government expenditure, and a lack of transparency in government management of public finance all disrupted the banking system and led the country into parallel markets. The overall effect has been an economic and financial crisis that requires a total reform.

It is the opinion of this researcher that the BNA is not yet independent from government interference, nor is it functioning fully as an autonomous bank. This conclusion was reached on the basis of the bank's level of independence (as measured according to the criteria of Effinger and Cukierman), taking into account what is legally prescribed in terms of its functions and roles, and also the continued involvement of government in the appointment of governor of the BNA.

The state of war in particular allowed government to exercise extra control over the BNA. As the war spread, the BNA was forced to close its branches in certain provinces and to concentrate most of its activities in the capital, Luanda. Its functions became fully controlled by the government.

The World Bank Country Study of 1991 suggests that before the early 1990s the government did not give adequate support to economic reforms. It was not accompanied by political reforms, and thus was not sustainable in the long run. After 1992 conditions started improving slowly, but there is still much work to be done. The lack of reform is visible in the relationship between the Angolan government and the BNA. However, no literature clearly indicates the actual level of interference from government in BNA affairs.

5.2.2 Findings Regarding the BNA as a Funder for the Government

The second assumption of this thesis was that the political environment in Angola resulted in the over-reliance of government on funding from the BNA in meeting the public interests and needs. The lack of income from other sources resulted in financial shortfalls, which naturally impacted on government's ability to respond to the needs, demands and interests of the public. This in turn led government to source funding from the BNA.

During the period from 1975 to the late 1980s, the government was based on a socialist economic system, and considered itself responsible for the provision of basic public needs, such as food, education and health, by subsidising their costs. Education and health were fully subsidised, despite the fact that most of government expenditure was invested in the military defence of the country. In most cases, monetary policies were designed according to government priorities rather than with regard to any economic or financial benefit to the country as a whole.

5.2.3 Findings Regarding the Main Obstacles Faced by the BNA

The third research assumption was that the lack of sound policies with regard to the banking and financial systems has led to weaknesses in the role and functioning of the BNA. One of the weaknesses of the BNA appears as a lack of independence in monetary management. The liberalisation of bank licensing allowed many new companies into the country, which increased industrial competition and showed the need for deep and continuous structural reforms within the BNA. The liberalised banking environment also brought about increased banking problems, which required of the BNA a higher level of operational capacity, and efficiency in regulation and supervision mechanisms.

A general overview of the state of the human and technical resources available in Angola during the period of war has led the researcher to conclude that there was a scarcity of skilled personnel in the BNA at that time. Little information or data has been accessible about this specific issue, however. The World Bank Country Study (1991, 14) refers to a "shortage of skilled personnel" in the BNA, but does not analyse this in detail. It gives no information about the central bank's plans for training and development programmes to overcome this problem. The Study does however give an example of problems experienced in the allocation of foreign exchange, which was based on priorities incorrectly established by under-experienced BNA employees. This example reflected the general inefficiency of the bank and the need to seriously invest in staff development programmes.

5.2.4 Findings Regarding to BNA as a Key Instrument for Positive Financial and Economic Development of Angola

The data reviewed for the purpose of this research paper has proved that the BNA, as the central bank of Angola, is an institution, which has great positive impact on the financial and economic development of the country. It has proved that the Angolan central bank is the only institution with the ability and authority to control the financial environment, maintain price stability and inflation control.

This is attributed due to the fact that the central bank is an institution designed to perform as agents, adviser's and banker's of the of the governments. The central bank , therefore, has special and particular responsabilities, such as the only bank authorised to issue money.

This basically means that the government has been given more autonomy to the BNA, especially with regards to the economic policies that has to be accompanied by the political reforms under going in the country. As an example is the reforms on the programme of Economic and Financial Rectification (Saneamento Economico e Financeiro – SEF) - monitored by the World Bank and the IMF - to give the public, and possible foreign investors, an increased confidence in the banking system. In view of this progress, the government now hopes to achieve annual economic growth and development. Development strategy has been slowly improving – especially over the past three years. This improvements include:

1. Level of macro-economic stabilisation
2. Development of essential infrastructure
3. Financial institutions to mobilise and allocate savings
4. privatisation on the banking industry
5. Reform of public administration and legal institutions.

These all contribute towards the effectiveness and organisation of the entire banking system.

5.3 Recommendations

Under headings relating to the three initial assumptions the researcher suggests recommendations to be considered for improving the functioning of the BNA.

5.3.1 The Relationship between the Central Bank and Government

Interference by the government was a form of power during the Angolan civil war. At this time of economic transition, the government should provide the enabling political and financial environment for the bank to develop its new identity to function and meet the needs of the country and the economy. This would entail a reform of the legislation regarding the relationship between the government and the bank. To this end the BNA should be allowed to function fully as the issuer of currency, the banker's bank, the lender of last resort, the conductor of monetary policy and finally be involved in international transactions of Angola.

Even though the central bank is still undergoing in-depth transformation in order to be the major key operator of the Angolan economy, some of the functions that apply to most central banks as independent banks are already being put into practice. It is, however, still too early to say that the BNA has achieved the desired level of autonomy. The government should be more transparent in its economic activities and allow the BNA to act according to its basic functions, and create stability of its currency. The BNA must have a level of independence from the state in order to make decisions according to the needs of the country, based on international banking standards.

One of the new challenges for the BNA is the need to be assigned constitutional responsibilities independently of the goals and responsibilities of the executive arm of government. The bank should also be constitutionally charged with the pursuit of macroeconomic goals that include price stability, equilibrium in the balance of payments, and a stable exchange rate. With these mandates, and with freedom to pursue them without recourse to government, the bank would be at liberty to choose its monetary tools and set policy targets to fulfil its objectives.

The level of autonomy will be achieved only when the reforms have had a real impact on the free market economy, so that the bank can fulfil its major role in price stabilisation and monetary policy without interference from the government or other political influences

The government should acknowledge the autonomy of the bank, and conditions should allow bank policies to be implemented. The bank needs an operational scope and autonomy to meet the challenges of a deregulated financial sector effectively. There is a need to promote development and sustainability, both in Angola and in the continent in relation to the world at large. Sundararajan at el (1997, 4-5 and 48) suggest that, in the process of restructuring strategies, it is important to consider the need for a competitive and profitable framework in the banking system.

5.3.2 Executive Selection of the Bank

When clear constitutional responsibilities of the BNA have been defined, the choice of Board members should be made with a view to enabling the bank to achieve its mandate. Appointment to the Board must be based on professional competence with minimal influence of candidate's political affiliation. This is especially important for appointment of the Governor of the BNA.

5.3.3 Managing Monetary Policy Instruments

The BNA is facing a growing challenge on how to manage the indirect monetary policy instruments which may have to be introduced in line with a liberalised financial environment. Such measures will have to be accommodated in the strategic vision and mission of the bank. Government should facilitate the implementation of changes in macroeconomic policies such as fiscal control and supervision of expenditure and tax management, plus efficient allocation of human and financial resources.

The interactions between the economy and the banking system are influenced by the banks' organisational structures and their technical operating methods, as well as by the way in which government policy decisions are taken.

5.3.4 Provision and Future Control of Expenditure

Better control of government expenditure and reform of the balance of payments system is needed. From 1987 until today, however, the central bank has been implementing a set of reforms, such as the SEF – monitored by the World Bank and the IMF – to give the public, and possible foreign investors, increased confidence in the banking system. In view of this progress, the government now hopes to achieve annual economic growth and development.

5.3.5. Promoting Foreign Investment

Government and the BNA should promote greater foreign investment. Through the BNA, the government should intensify efforts to encourage foreign currency funds in bank accounts set up within Angola by residents and non-residents according to prescribed laws of the country. Foreign investment plays a major role in the development of the economy, and the BNA plays an important role concerning both inflows and outflows of foreign currency and the exchange rate.

Reforms in legislation and monetary policies, coupled with transparency, should provide investors with sufficient confidence and trust to invest in the economy.

5.3.6. Improving Overall Functioning of the BNA

Improvement of the banking system, particularly as regards the role and performance of the BNA, would lead to greater financial and economic development of the country. It must be empowered to decide on all exchange rates and to intervene in matters of monetary and financial regulation. It must be given authority to borrow money from the government with a guarantee of repayment. Finally, all commercial functions of the BNA should be transferred to commercial banks.

5.3.7 Promoting Transparency

An administrative structure capable of enforcing the legal framework that promotes transparency in its activities should be instituted. Such a structure would prevent or reduce the abuse of power, the mismanagement of public funds as well as the possible recovery of BNA losses. This appears to be one of its major challenges, since government over-expenditure is currently funded by the BNA, without the possibility of recovery.

5.4 Further Study

A lack of investment in human resources and modern technology has resulted in a crisis in the central banks of African developing countries. A more general study could be undertaken concerning these problems. High quality staff training and development programmes are needed in order for the banks to perform effectively and adapt to changes in the world economy. It is important to note the level of banking skills required. Among other things, these involve accounting procedures, credit analysis and computing.

5.5 Concluding Remarks

Despite the problems still being experienced in Angola, it is important to recognise that the BNA structures and strategies are being reformed to enable it to perform its functions and activities in an independent manner. However, the desired level of independence is still wanting.

Policies that promote the role of the BNA as banker's bank, adviser of the government and lender of last resort will contribute towards greater independence. A central bank with appropriate autonomy and skilled human resource and modern electronic systems is crucial for economic growth in the post-war period of Angola.

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