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The Impact of Regulatory Framework on the Conduct of Credit Providers in the Consumer Credit Market in South Africa

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Abstract:

The size of the consumer credit market has grown at a faster rate catalysing the development of the South African economy. Robust economic regulation is viewed as a necessary intervention that fosters a developing credit market environment. The dynamic nature of the consumer credit market requires a regulatory architecture that is flexible enough to adapt and respond to institutional and market circumstances. The reason for promulgating the National Credit Act, 34 of 2005 in South Africa was fivefold: to promote equity, to regulate the consumer credit in such a manner that it promotes economic development, to remedy regulatory deficiencies caused by an inadequate regulatory regime, to curb abusive practices, and provide remedies for those prejudiced. The research design involves an empirical study presented in an exploratory and descriptive fashion using a qualitative research approach. The investigation also utilises modern methodologies like the Regulatory Impact Analysis and Cost Benefit Analysis and Content analysis tailored for evaluating regulatory frameworks across jurisdictions. The National Credit Act, 34 of 2005 regulatory architecture has played a salient role in pioneering a new culture and enhancing the development of the credit market. However, there are challenges around the implementation thereof by credit providers especially when considering aspects of volatility, interconnectedness of the global financial markets and dynamic nature of the market spurred by technological changes. The current architecture of the National Credit Act is not adequate to effectively impact the conduct of credit providers in South Africa.

Keywords: Credit, consumer, market, risk, regulatory, framework, debt

1. Introduction

The South African (SA) consumer credit market is central to the development of the economy because it has the ability to stimulate the credit industry and improve livelihoods. Thomas (2009) states that consumer lending is a 'sleeping giant' of the financial sector that has experienced phenomenal growth over the past 55 years. Moodley (2007) ascertains that consumer spending has for a long time driven South Africa's (SA's) economic growth. The National Credit Regulator (NCR) quarterly Consumer Credit Market Report (December 2013) shows the total outstanding gross debtor's book on consumer credit to be at R1.53 trillion. This indicates how huge the consumer credit market is in the SA economy. The size of SA's credit market is therefore enormous and any challenge to the credit industry poses a threat to the wellbeing of the country's economy. The threat is more eminent if there is a lack of adequate regulatory mechanisms in place to mitigate any potential inherent or residual risk.

The 2008 global credit crisis and developments on the consumer credit regulation have shown that risks emanating from one part of the global financial system can be rapidly transmitted across continents with disastrous consequences for the global economy. The SA economy, which forms part of the interrelated global economy, did not elude the global financial crisis in that, it was plunged into a recession (SA exiting recession: 2010) thereby affecting the credit market. The above submission shows that there is a need to evaluate the impact of the regulatory framework as designed by the National Credit Act (here after the NCA), 34 of 2005 on the conduct of credit providers in SA since they are the key role players in the consumer credit market.

Since the consumer credit market is important for the economic development of SA, it is important that the industry remains competitive, well regulated and stable. In line with the ongoing regulatory reforms the NCA and its Regulations were promulgated on 1 June 2006. This was done against the backdrop of an ineffective and outdated regulatory framework (distorted market, high cost of credit, rising levels of over-indebtedness, reckless behaviour by credit providers and exploitation of consumers and the need to modernise the credit laws as well as harmonising them against the best international jurisdictions). The NCA was designed to achieve a number of objectives, most of which are intended to;

- Regulate the consumer credit market;
- Promote the development of a credit market that is accessible to all South Africans; and

- Promote equity in the market by balancing the respective rights and responsibilities of credit providers and consumer rights. This is meant to ensure that the credit market operates in a balanced manner.

There is, therefore, a need to investigate the impact the NCA has on credit providers against the policy objectives *visa-vis* bankruptcy, over-indebtedness, reckless lending, arbitrary informal lending, manipulative and misleading abusive practices, interest rate ceilings, investments-disincentive, extent and severity of regulation as highlighted in the objectives of the NCA.

The consumer credit landscape has been tilted by the introduction of the NCA to regulate the consumer credit market in SA. However, there is a need to determine if this policy has a meaningful impact on the behaviour of credit providers. Furthermore, there is also limited research that enhances the understanding of the NCA on its influence on credit providers since it's a fairly new legislation.

2. Statement of the Research Problem

The current regulatory architecture, even though considered to be one of the espoused modern regulatory mechanisms, is inadequate in influencing the conduct of credit providers effectively in a dynamic environment so as to develop a stable and developing consumer credit market.

3. Research Hypothesis

This investigation thus hypothesizes that there are loopholes in the current NCA regulatory framework that make it inadequate to effectively impact the behaviours of the credit providers in the dynamic consumer credit market.

4. Aims and Objectives of Research

The main objective of the research was to investigate the impact of the current regulatory regime, the adequacy of the current system in influencing the behaviours of the credit providers and assess how the developments in the credit market will affect the regulation of the consumer credit market. The investigation sought to find out how effective the SA regulatory framework is influencing the behaviour of credit providers in promoting a fair, transparent, competitive, sustainable, responsible, efficient, effective and accessible credit market and industry, and the protection of consumers.

5. Research Questions

To achieve the primary objectives, the following four questions are to be investigated:

- What is the rationale and benefits of regulating the conduct of credit providers in the consumer credit market?
- How effective is the current model of credit regulation?
- How effective is the SA regulatory framework in ensuring that credit providers promote a fair, transparent, competitive, sustainable, responsible, efficient, effective and accessible credit market and industry, and the protection of consumers that contributes to SA's economic growth?

6. Importance of the Study

Kelly-Louw (2007) states that the fundamental purpose of the NCA is to achieve integrity in the market. Therefore an understanding of this dynamic market is necessary in employing an effective regulatory framework so as to positively effect on the economic development of SA. Interest in this study was sparked by the realization that credit market regulation is an important function of the economy, especially against a backdrop of the global credit crisis. The credit market is a dynamic field and therefore there is a need to review the current regulatory framework. The study is important in that it will:

- Heighten the analysis and evaluation of the regulatory framework provided for in terms of the NCA and its impact on credit providers against international regulatory practices;
- Contribute to the body of knowledge on the development of effective regulatory framework for credit providers;
- Provide a review of the impact of the current regulatory framework on credit providers, thereby increasing the understanding of the challenges experienced in implementing the requirements of the Act;
- Also help in benchmarking the impact of the South African regulatory framework on credit providers against international standards perceived as best practices.

7. Literature Review

The size of the SA credit market is huge with the quarterly Consumer Credit Market Report (March, 2014) released by the National Credit Regulator (NCR) showing the total outstanding gross debtor's book on consumer credit to be at R1.55 trillion by 20,2 million credit active consumers. The FinScope Consumer Survey SA (2012) defines active credit consumers as those who have an obligation to pay a credit provider and/or have an account with a supplier of goods or services. These obligations are then registered on the consumer's credit record with credit bureaus. The NCA (2005) loosely defines credit when used as a noun, to mean a deferral of payment of money owed to a person, or a promise to defer such a payment or a promise to advance or pay money to or at the direction of another person.

Ramsey (2003) submits that credit is increasingly the driver of world economies. A policy framework for consumer credit by the Department of Trade and Industry (DTI) (2004), states that, in developing countries without a welfare state the increasing availability of credit may provide access to credit services. The World Bank (2008) views the access to credit as not necessarily a 'human right' but as a method of reducing income inequality and poverty. Although access to consumer credit is seen as providing benefits to

consumers by credit providers in smoothing income fluctuations over the household life cycle and addressing short term liquidity crises, it brings with it the risk of over-indebtedness and social costs (Employment Social Affairs and Equal Opportunities, 2008). Ferk (2007) views debt as an instrument used to sustain consumption over time. The benefits of access to credit as viewed by DTI (2009) can be significant if the credit market works well where individuals are empowered to accumulate assets, exploit economic opportunities, grow businesses and create new jobs.

7.1. Regulation of the Consumer Credit Market

The volatility of the consumer credit market as discussed above shows that the case of regulation is a necessary intervention. Bar-Gill and Warren (2008) submit that credit can be a dangerous product, as such, regulation may be justified to protect against the risks associated with it as it will have the effect of stimulating confidence in the use of consumer credit markets. Giddens (2000) submits that markets and credit providers in particular are embedded in society as such, they cannot function without a social and ethical framework.

For the purposes of this research there is a need to conceptualize the theory of regulation. As already stated, Khemani and Shapiro (1993) define the term regulation as the imposition of rules of government, backed by the use of penalties that are intended to modify the economic behaviour of individuals and firms in the private sector. From this definition, it can be understood that there are different rationales that exist for economic regulation. The purpose of regulation may be to curb the potential market power and increase efficiency, protect consumers, maintain quality, promote employment and equitable distribution of income, prevent excessive competition and protect suppliers from unstable output and low price conditions.

Falkena et al (2001) argues that it is the role of financial regulators to set minimum standards that all organizations in the sector must adhere to and ensure that these will be applied equally to all competitors. Thus, "regulation could have the positive and beneficial effect of breaking the gridlock by offering a guarantee that all participants will behave in accordance with certain standards" (Llewellyn, 1999). Falkena *et al* (2001) admits that what is imperative to the success of any regulation is the ability to seek regulatory institutions, structures and mechanisms that maximize the explicit objectives of the regulations whilst minimizing the imposed costs.

7.2. Who is supposed to Regulate and how is it Supposed to be done?

Globally, there seems to be no agreement on who is supposed to be responsible for regulation. There are different viewpoints on whether regulation is supposed to be through legislation by central banks, or through meta-regulation in the form of internal bureaucracies of creditors. Self-regulation by credit providers is through the use of industry codes of practice and the work of Ombudsmen whereas governmental regulation is usually through legislation enacted by parliament. There is however no agreement among the literature as to which of the two models of regulation is the most effective in regulating the conduct of credit providers in the credit market.

Cowton (2002) submits that not all lenders are interested in following the prescribed and responsible lending practices, regulation through legislation rather than by self-regulation should be more desirable. This notion is supported by Williams (2007) who states that most governments seem to favour the empowerment of consumers through mandatory credit disclosures and financial literacy initiatives. Whereas Black (2001) states that contemporary approaches to regulation recognize regulatory strategies that combine government and non-governmental actors who have to be involved in the structuring and influencing market interactions rather than merely policing infractions of rules.

The SA credit market can be contextualized through the use of NCR information. NCR was established as a result of the provisions of the provisions of section 12 in the NCA on 1 June 2006 for the regulation of the South African credit market (Otto: 2006:7). The roles of the NCR are mainly centered on education, research, policy development, registration of industry participants, including credit providers, investigating complaints, prosecuting violations through the National Consumer Tribunal or Courts and compliance with the NCA. The NCR's role in terms of the preamble of the NCA is to promote the development of an accessible credit market, particularly for the needs of those historically disadvantaged as well as marginalized persons and low income persons. Thus, it is the policeman of the credit market in SA.

7.3. Credit Providers

According to the NCR website as of 20 June 2014 the SA credit market has 4417 registered credit providers offering a mix of credit products described as a small, intermediate, or large agreement as provided for in terms of section 8 of the NCA. Section 1 of the NCA defines a credit provider, in relation to the types of credit agreements to mean:

- The party who supplies goods or services under a discount transaction, incidental credit agreement or instalment agreement;
- The party who advances money or credit under a pawn transaction;
- The party who extends credit under a credit facility;
- The mortgagee under a mortgage agreement;
- The lender under a secured loan;
- The lessor under a lease;
- The party to whom an assurance or promise is made under a credit guarantee;
- The party who advances money or credit to another under any other credit agreement; or
- Any other person who acquires the rights of a credit provider under a credit agreement after it has been entered into.

Section 40 of the NCA makes it mandatory for a person or entity who wishes to operate as a credit provider to register with the NCR. If that person, alone or in conjunction with any associated person, has offered at least 100 credit agreements, other than incidental credit agreements; or if the total principal debt owed to that credit provider under all outstanding credit agreements, other than incidental credit agreements, exceeds the threshold prescribed for in terms of section 42 (1) which is currently R 500 000.00.

7.4. *The National Credit Act, 34 of 2005*

The NCA is the most critical literature on the regulation of consumer credit market. Kelly-Louw (2007:150) states that, the fundamental purpose of the NCA is to achieve integrity in the South African credit market. Otto (2006:2) says the NCA is in essence the legal instrument for consumer credit legislation. According to Renke *et al* (2007:239) parties to be affected by the NCA are not limited to, consumers, but include credit providers, credit bureaus and debt counsellors. Clayton (2006:19) stated the following as the ten most important aspects of regulating the consumer credit market by the NCA

- a) Better disclosure - The NCA places specific obligations on lenders to disclose aspects like fees and interest rates. Durkin (2002) speculates that as a result of disclosure, consumers may act in one of the following;
 - use less credit as the disclosure highlights that credit is expensive;
 - not change their use of credit patterns, as the disclosures may confirm their perceptions that credit is affordable;
 - Increase their credit use due to increased confidence that credit is a desirable option.
- b) Consumer information held by the Credit Bureaus - lenders are required to register all credit in the national register to enable lenders to do an affordability assessment. The credit bureaus are regulated with regard to how they handle the consumer credit information for the purposes of protecting consumers. The credit bureau and NCR are obliged to investigate the accuracy of the information at no cost to the consumer. Consumers are entitled to have right of access to their records from the credit bureaus at no cost once a year. Mohan and Sahu (2005) argue that information held by credit bureaus seeks to analyse data on actual and potential clients, with the goal of understanding the client's capacities and performance potentials so as to develop credit scoring models. The benefits of this information would be sharing best practices, generating early warning signals and credit scoring in the absence of collateral, thus enabling the expedient decision making and product development based on customer needs and aspirations.
- c) Unsolicited marketing or selling - the NCA prohibits this practice;
- d) Marketing practices - the NCA prohibits misleading advertising and negative option marketing;
- e) Reckless credit - the NCA puts mechanisms to deal with debt and create a safety net for those burdened with debt. The Act also prohibits reckless credit granting, by placing an obligation on the lender to conduct an affordability assessment;
- f) Contract terms - the NCA contains mechanisms to enable the consumers a right to receive a contract in an understandable manner;
- g) Interest rates - the NCA requires the disclosure of interest rates and other charges. It prescribes the maximum rate of interest that can be charged on credit;
- h) Fees - the NCA requires that charges be disclosed upfront before the consumer enters into an agreement;
- i) Cost of insurance - the NCA seeks to regulate packages of insurance offered by credit providers together with the credit; and
- j) Complaints - the NCA has enacted a dispute resolution body in the form of the National Consumer Tribunal and Provincial Consumer Courts.

Gryffenberg (2007:1) states that all credit providers had to adapt their operational procedures to incorporate the requirements of the NCA in the following respects: granting of credit in a manner that does not amount to reckless, setting the acceptable or proper interest, fee ceilings as well as the establishment of the credit register. According to Finlay (2008:13) credit providers competing in the consumer credit market to accomplish their objectives if they are capable of predicting and controlling the behaviour of their customers. From the literature surveyed there was no investigation on the effectiveness of the current regulatory framework for the conduct of credit providers in the country which leaves a gap in the field of research which this study seeks to fill.

8. Research Design

The research involves an empirical study and would be presented in an exploratory and descriptive manner using a qualitative research approach. Flick (2002:17) states that, the qualitative research design allows for the conceptualization of how subjects under study relate to the context within which they are studied in different ways. Zikmund (2003) states that, "more often than not, an exploratory research provides a greater understanding of a concept and crystallise a problem instead of providing precise measurement". Furthermore, exploratory research does not involve extensive mathematical analysis; therefore the researcher's focus should be on words and observations to clarify ambiguous problems. This submission is further supported by Collins and Hussey (2003) who state that, an exploratory study looks for patterns, ideas, rather than testing or confirming a hypothesis. Thus, the literature selected allows the researcher to conceptualise aspects of the credit market, regulation, behavior of credit providers and the impact played by the NCA in influencing the behavior of credit providers.

8.1. *Data Collection Techniques*

The investigation utilized documents, records, court judgments among other sources for the purposes of extracting opinions of experts in policy making, regulation, Tribunal members, consumer court officials and those charged with implementing the Act. The

documents and records are assumed to have been compiled by experts with a deeper understanding of the NCA and the consumer credit market industry. The opinions expressed were then utilised to evaluate how the objectives of the NCA are championed by the credit providers in the development of South African consumer credit market. The use of documents, records and court judgements were chosen as it allows the researcher flexibility to select relevant data.

8.2. Sampling

Diamantopoulos and Schlegelmilch (2006) broadly define population as the totality of entities in which the researcher is interested in, the collection of individuals, objects or events about which the research wants to make inferences. Zikmund (2003) defines sampling as obtaining units which are most conveniently available. From the above submissions it can be explained that sampling is a process of choosing data or information from the population for the purpose of investigating that particular area of interest. During this investigation the population from which the investigation was undertaken was sampled from the data that relates to the regulation of the conduct of credit providers in the credit market industry.

Information was collected from various sources and a more justifiable manner of evaluating the conduct of the credit providers was to look at court judgments grouped according to different themes that aid in evaluating the different aspects of the NCA policy to be complied with. Also, the courts are tasked with the role of interpreting and explaining the NCA while applying to different cases brought to them. This helped in explaining acts of compliance and non-compliance by credit providers, thereby giving a view as to whether the NCA is effective in influencing the behavior of the credit providers in the consumer credit market. The sample population for the purposes of this investigation only involved relevant data on consumer credit industry.

The criteria used to select the participants was determined by their role and understanding of the NCA and consumer credit markets, the diversity of opinions that were gathered and the level of strategic insight. The focus of the data was on the behavior or conduct of credit providers who are key role players in implementing the NCA.

8.3. Analysis of Data

Irvine and Gaffikin (2006) define data analysis as the organization, selection, interpretation and representation of data to build a theoretical version of reality. Such an analysis included the positive and negative impacts that are distributed on the conduct of credit providers (Lee, 2002). This is because regulation entails trade-offs in which some gain and others lose as a result of implementation of a new law (Kirkpatrick and Parker, 2003; Financial Services Authority, 2000a). A mix of data analysis techniques were utilised, these include triangulation, Cost Benefit Analysis (CBA), interpretive paradigm and case study with the major technique being a qualitative content analysis. The mix of techniques was utilized to ensure absolute objectivity in qualitative research.

9. Findings and Analysis

The findings and analysis of this research were mainly based on the objectives of the NCA which states that the purpose of the NCA is to promote and advance the socioeconomic welfare of South Africans. This entails promoting a fair, transparent, competitive, sustainable, responsible, efficient, effective and accessible credit market and industry, and to protect consumers. As such a case study of 24 small, medium and large credit providers ranging from banks, motor financiers, pawnbrokers, retailers, developmental credit providers and micro lenders among others offering various credit products was assessed to evaluate the impact of the regulatory framework on the conduct of credit providers.

Qualitative content analysis as a selected methodology enabled the researcher to assess attitudes or themes on the effectiveness of the impact of the NCA regulatory framework on the conduct of credit providers in the consumer credit market. From the population of 4467 registered credit providers a sample of 24 credit providers of varying sizes ranging from banks, motor financiers, pawnbrokers, retailers, developmental credit providers and micro lenders among others operating at local, provincial or nationwide and offering various credit products and different amounts of credit loans were selected and analyzed for patterns so as to conceptualize a wide range of aspects on the NCA in influencing the behaviour of credit providers in the credit market.

The sample deals with various aspects of the NCA as they aid in evaluating the impact of regulatory framework on their conduct of the credit providers in the South African consumer credit market. The following detailed two case studies of some of the major credit providers Capitec Bank Limited and African Bank Limited and other numerous credit providers highlighting the extent of the effectiveness of the regulatory framework as underpinned by the NCA. These credit providers were selected because they have been investigated by the NCR as also they highlight the impact of the regulatory model on the conduct of credit providers.

A close study of Capitec Bank Limited, one of the biggest credit providers with 574 branches countrywide extending to remote rural settlements revealed that it has grown its customer base from 350000 in 2005 to 4, 7 million in 2013. The bank staff is tasked with the responsibility of ensuring compliance with the Act and Regulations and attending to consumer complaints and a dedicated debt review unit to deal with debt counsellors. Thus, the training of the staff on compliance goes a long way in ensuring compliance with the NCA over and above leveraging on IT systems. Furthermore, the credit provider regularly engages with the Banking Council of South Africa on issues of compliance with the NCA and Regulations. This constant engagement with a voluntary industry body with codes of conduct around the integrity of the banking sector shows a drive to operate the credit market with ethical standards.

The consumer complaints redress mechanism employed by the credit provider highlights the due processes in place to resolve consumer complaints at all levels from branch to industry and ultimately by forums created by the NCA thereby affording them their rights. The case study of Capitec Bank Limited shows that, there is an increase in the access to credit even in remote areas, technology

is being optimized to mitigate business risks and credit costs thereby complying with NCA and benefiting consumers. The credit provider has measures in place to ensure risk management and compliance with the NCA is of high priority.

The NCR as part of its mandate to regulate credit providers appointed Gobodo Forensic and Investigative Accounting (Pty) Limited in July 2011 to conduct an investigation into the alleged unsecured and micro-lending practices of the Capitec Bank so as to assess compliance with the NCA. In its investigation a random sample of 60 credit agreements from the following categories: 20 short-term credit agreements; 10 small credit agreements; 10 intermediate credit agreements; and 20 credit agreements were consumers had defaulted on their repayments. The forensic report alleged that the credit provider had contravened the NCA in that;

- Credit agreements had unlawful standard terms and conditions in respect of short-term, small and intermediate credit agreements;
- The credit provider unlawfully entered into intermediate credit agreements with consumers without furnishing the consumers with pre-agreed statements and quotations;
- Charging interest in excess of what is prescribed in the NCA;
- Charging excess withdrawal fees;
- Inadequate assessment of the consumers' ability to repay the loan

The NCR approached the National Consumer Tribunal to prosecute the credit provider for contravention of the NCA. The Tribunal found that the NCR had merely instructed Gobodo to conduct an investigation and did not properly designate them to be investigators with the requisite authority to conduct an investigation into the conduct of the credit provider as such the application to prosecute the credit provider based on a report obtained unprocedurally was dismissed. This case highlights an improper application of the NCA by NCR and the abdication of duty by an industry regulator which is supposed to champion the development of the credit market. The material error and failure by the NCR to properly vest Gobodo with lawful powers to investigate Capitec Bank meant that the findings of a forensic report, though pointing to non-compliance with the NCA do not stand. As such, if the NCR had procedurally investigated and prosecuted the credit provider and the findings were proven to be true, there was going to be consumer redress and punishment of the credit provider for contravening the NCA. This case portrays the error of the NCR in a negative light and can potentially raise doubts and lack of confidence in its capabilities.

9.1. African Bank Limited

The African Bank Limited, under the African Bank Investment Limited (Abil) has 3,2 million customers and 630 branches nationwide and additional contact points through Elleries Furniture Stores. Thus, African bank has a gross of R60 billion in the forms of credit extended as loans and furniture this having increased from R18 million in 2009. The bank is South Africa's micro-lender with a banking model that was hailed for introducing a new way of banking in Africa by targeting the mass market of previously unbanked South Africans. The target market of the credit provider is from poor and working class background that were previously excluded from the formal economy because of apartheid. This served the purpose of inclusivity and accessibility to the credit market. The credit provider has bondholders like Investec Asset Management, Momentum Asset Management and Nedbank among the local institutions and the Public Investment Corporation that funds Abil's short and long term debts which in turn are extended as credit to the consumers.

The credit provider was investigated by NCR in 2012 and prosecuted before the National Consumer Tribunal for having contravened the NCA. In 2011 one of its branches at Dundee in the Kwa-Zulu Natal province granted 700 loans recklessly to 397 consumers who could not afford to repay them to the capital value of R15, 5 million. The employees of the credit provider are alleged to have fraudulently granted loans by manipulating the affordability calculation assessments. In the majority of the loan applications the consumers colluded with employees and made illicit payments to the agents in return for granting the loans. The credit provider reacted by dismissing 3 employees involved in the issue. It is also interesting to note that a consumer from Ekurhuleni in Gauteng had their identity document used to fraudulently obtain a loan of R83 000.00 from the credit provider.

In the prosecution before the National Consumer Tribunal the NCR sought to have the credit provider pay an administrative penalty of R300 million, which was the 10% of its 2012 annual turnover for reckless lending. However, the NCR decided to withdraw the matter from the National Consumer Tribunal and settled with the credit provider in October 2013.

In as much as the parties are entitled to settle outside the National Consumer Tribunal the withdrawal of the prosecution from the National Consumer Tribunal appeared to have been questionable in this instance, when assessed against the other credit providers that were prosecuted for similar incidences of contravening the NCA and deregistered with hefty penalties issued against them whereas African Bank was treated differently. This may be viewed as an unfair application of the NCA as small and large credit providers are treated differently by the NCR. Part of the condition of the settlement merely states that the credit providers will develop an active engagement process with the NCR perhaps a compliance process with the NCA instead. The general conditions of registration of credit providers require them to comply with all applicable legislation relating to all their business operations. It is noteworthy that not all credit providers are required to register with the NCR, only if they have at least 100 credit agreements. Any credit provider that has at least the number of credit agreements in terms of the prescribed threshold and is not registered with the NCR is prohibited by the NCA from offering, making available or extending credit.

The credit providers are supposed to have procedures in place to protect all consumers' confidential information and only utilise it for its intended purpose and forward reports to the credit bureaus. The credit providers are supposed to have measures in place to ensure increases in credit limits, in respect of credit facilities, are made with the permission of the consumer. The credit providers are to have

procedures in place to combat over-indebtedness and prevent reckless credit granting by conducting pre-assessments. From the assessment of the credit providers' practices around curbing reckless lending the following was observed:

- Smaller credit providers do not have training programs for their staff or management, procedures and systems in place to combat over-indebtedness and reckless lending.
- Most of the smaller credit providers did not conduct pre-assessment of the consumer's debt repayment history or the consumer's financial means and obligations.
- Most smaller credit providers would extend credit to consumers under administration or debt review this act defeats the purposes of aiding debt stressed consumers to from becoming over-indebted. This act is automatically deemed by the NCA to be recklessly lending.
- Some credit providers would return or have permanent customers in their books. This highlights how some consumers are caught in the vicious cycle of debt.
- Agreements relating to the small credit loans were not recorded or there were no credit agreements. As such, additional credit would be given to the consumers since there was no information registered with the credit bureaus. This leads to over-indebtedness and reckless credit granting.
- Most of the small credit providers would extend credit without an insurance cover. This is a factor that can also be attributed to the voluntary closure of smaller credit providers that falter due to non-repayment by consumers.
- Most of the smaller credit providers were charging consumers interest, fees or unlawful fees in excess of the prescribed rates.

From the above observations when evaluated against the NCR statistics which show that at least 9 million of the 20, 2 million credit active consumers have impaired credit records. This could be attributed to the non-compliance by credit providers who are to train and monitor their staff members and have mechanisms in place for combating over-indebtedness and reckless lending.

The credit providers are to ensure that they have procedures in place to ensure that they do not conclude unlawful credit agreements with consumers or that their credit agreements do not have unlawful terms.

Section 92 (1) (2) and 93 (1) of the NCA states that a credit provider is supposed to provide a consumer with pre-agreement statement and quotation before concluding a credit agreement. Furthermore, a credit provider is supposed to provide a credit agreement to the consumer without a charge. From the case studies most of the small credit providers did not provide any pre-agreed statements or quotation and some did not even furnish the consumers with credit agreements. Thus, there was non-compliance by many smaller credit providers.

Section 100 of the NCA outlines charges or liabilities that may not be imposed on a consumer who enters into a credit agreement as defined in the NCA. These are, any fee or charge prohibited by the NCA; any fee or charge that exceeds the limits set by the NCA and Interest that exceeds the limits set by the NCA. The following was observed to be another means of manufacturing additional costs for the credit providers; Most of the small and intermediate credit providers would give numerous smaller loans to the same consumer within a day (splitting of loans) whilst charging administrative costs in respect of each credit agreement every time they gave out the loan. They were also charging consumers third party fees which are not categorized as credit fees in terms of the NCA.

The credit providers are required to submit statistical returns, annual financial statements, annual disbursements and assurance engagement report to the NCR on an annual basis. From the case studies on the credit providers the level of compliance among bigger credit providers is high, whereas in smaller credit providers the extent of non-compliance is high. From the case studies, it appears that bigger credit providers have procedures and controls in place and defined roles and responsibilities to ensure compliance, whereas in smaller it appears to be non-existent. In considering the efficacy of the NCA only Capitec bank expressly stated that the NCA and its Regulations are complex, sometimes obscure and even contradictory. The assertion by the credit provider about the challenges around the efficacy of the NCA is attested to by the growing volume of jurisprudence highlighting interpretation and application challenges encountered by credit providers in the credit market in that there are conflicting court decisions and complaints about how poorly the legislation was drafted. Most of the smaller credit providers appear to be struggling to interpret or apply the NCA as such this may increase the incidences of non-compliance and ultimately the cost of regulation.

10. Summaries of Findings, Research Questions and Recommendations

The triangulation and saturation of findings showed similar patterns on the NCA regulatory framework thereby confirming the findings this was further validated and verified through discussion with industry regulators and further augmented by external public debates of the Debt Counselling Industry, South African Communist Party (SACP) and public conference debates by industry experts, evaluation of the literature through various techniques. Saturation about the impact of regulatory framework on the conduct of credit providers in the consumer credit market in South Africa was reached on the following aspects:

The NCA has made significant strides in the consumer credit market in advancing the socio-economic welfare of South Africans by establishing standards for promoting a fair, transparent, competitive, sustainable, responsible, efficient, effective and accessible credit market and industry and protection of consumers. The realization of this is premised on the effectiveness of the NCR and co-operation by all the role players especially the credit providers. Thus, regulation has introduced a culture of discipline from credit providers through pre-assessment of consumers applying for credit and the consequences of reckless credit granting that often act as deterrence against non-compliance. The consequences of non-compliance, which entails, among others prosecution of offenders, financial penalties, deregistration, loss of business and ultimately criminal prosecution raises the standard of compliance and awareness about the importance of compliance with the NCA. Regulation has brought a culture of consumer protection as part of the corporate social responsibility by credit providers.

Regulation has enabled some of the credit providers to remain financially solvency and sound, but some like African Bank have not been able to do so due to non-compliance that has further raised questions about the role of the NCR. This highlights that the regulation has catalysed the growth and development of credit market industry in South Africa.

a. How effective is the current model of credit regulation?

The following aspects of;

- The volatility that requires the adaptation of best international standards to local conditions were appropriate,
- The risks created by the interconnectedness nature of the global credit market facilitate connection of capital markets create a conducive environment for systematic financial failure,
- Gaps and overlaps with other regulatory frameworks within the South African context, current levels of compliance with the NCA especially by smaller credit providers
- The SA credit market is characterised by high and opaque credit costs and unfair treatment of consumers, especially the vulnerable old, poor and illiterate. The malpractices of reckless lending must be curbed in order to better protect the consumers and reduce the systemic risk.
- Continued high cost of credit and rising levels of over-indebtedness of consumers caused by reckless conduct of credit providers.
- This interconnectedness of credit market exposes the country to significant risks, therefore SA financial systems ought to be made safer through a regulatory architecture that is competitive whilst pursuing best global practice since it operates in a globalised environment where crisis in one economy can be rapidly transmitted with devastating speed and impact.

This raises a lot of questions about the adequacy of the current regulatory framework in its current format. This casts a shadow of doubt about the future of the NCA architecture playing a critical role in driving the credit market and conduct of credit providers. There is no doubt that the model has pioneered an ideal path for defining the standards and levels of compliance for all the role players, especially the credit providers, however the glaring gaps of monitoring and the corresponding compliance levels highlight the inadequacies of the current system. As such the model in its current form is not robust enough to effectively regulate the consumer credit market.

b. How effective is the SA regulatory framework in ensuring that credit providers promote a fair, transparent, competitive, sustainable, responsible, efficient, effective and accessible credit market and industry, and the protection of consumers that contributes to SA's economic growth?

Overall there has been an increase in access to credit, and competition through the increased number of credit providers distributed across the country offering diverse credit products there is still a prevalence of non-compliance with the NCA among the smaller credit providers adverse impact caused by unfair or unlawful credit agreements, non-disclosures through deceptive credit agreements, unlawful collection practices, levels of over-indebtedness and reckless lending and blatant disregard of the NCA that severely prejudices the rights of the consumers thereby undermining the development of the consumer credit market. The gaps in the compliance are glaring yet the level of monitoring is still inadequate due to the size and capacity constraints of the NCR. This raises a lot of questions about the capability of the NCA framework to effectively regulate the market. Notwithstanding the above there is a drive towards compliance as complemented by other frameworks this is seen in the level of compliance among the bigger credit providers that high as such it somewhat mitigates the risk caused by the non-compliance among smaller credit providers. This may however not be adequate towards effectively contributing to the economic growth of SA.

c. Most of the compliance requirements of the current model has gaps and must be changed to ensure that there is meaningful regulation that promotes a stable credit market, improves consumer protection, mitigates against systemic risk and ensures that credit providers behave with integrity.

d. What is the impact of the SAs regulatory system in influencing credit providers' compliance with NCA?

From the case studies it appears that credit providers offering large and intermediate credit are compliant with the NCA whereas smaller credit providers registers as close corporations offering mainly small credit are non-compliant. There appears to be a lot of gaps and inadequacies caused by the framework itself, the application, supervision and monitoring by the NCR, the fast paced development of the credit market which often leaves regulatory framework lagging behind. The regulatory system has established rules of trade and so has the credit providers devised new means to comply or avoid compliance. The varying levels of compliance highlight different levels of impact as it appears that there is more incentive to comply for bigger credit providers whereas smaller ones tend to contravene the NCA. The impact designed by the framework has paved a new culture but there are still challenges with regards to compliance.

10.1. Recommendations

- The global financial stability is yet to be secured due to the risks associated with increasing unsustainable public debt ratios and volatile capital flows. There must be balance when promoting access to credit as unrestrained credit access may appear desirable, but excessive household lending creates financial instability risks with dire economic consequences. In seeking to promote access to credit the NCA must not be in contempt of promoting the explosion of lending and unsound household debt rise. Some of the lessons from the 2008 credit crisis taught us that scant regulation led to a proliferation of products such

as subprime mortgages driven by indiscriminate credit extension as amplified by the innovation of sophisticated financial products and inadequate risk management systems.

- To achieve this equilibrium between the competing objectives a regulatory architecture that can anticipate the rise in systemic risks must be developed by the regulators and also NCA must promote access to credit for small and medium enterprises must be promoted this will in the long run translate into meaningful economic growth rather than fuelling unsustainable levels of debt financed consumption.
- Regulation has not yet effectively levelled the playing field between consumers and credit providers and there is still a prevalence of abusive tendencies from some of the credit providers. Furthermore, there is still a prevalence of inadequate disclosures and increasing levels of indebtedness and reckless lending by credit providers. This will be effectively combated by improving financial literacy.
- The gaps of monitoring and the corresponding compliance levels highlight the inadequacies of the current system as such the current model is to be modified so as to enable it to be robust and effectively regulate the consumer credit market.
- The balance of bargaining power is far from being even as it appears that credit providers have more bargaining power and in dictating the terms of the credit agreement as such it is proposed that standard contracts and templates should be developed for usage by credit providers so as to help incidences of unlawful contracts. This must be balanced with the need to promote competition and not curtail it. Standard credit agreements will minimise unlawful incidences created by unlawful terms and supplementary agreements. Alternatively the credit agreements must form part of the application process for registration of the credit provider.
- There must be general pre-assessment standards that will provide uniform criterion for all the credit providers to assess the consumer credit applications. This will ensure that all aspects of the consumer's credit profile are considered before extending credit. This will help curb over indebtedness and reckless lending.
- The criteria for registration as set by the threshold creates a gap in the regulation of the consumer credit market as credit providers with under 100 credit agreements are not required to register. As such, some especially small credit providers may utilise this gap so as not to evade the radar of regulation opening up room for abuse of consumers by unregistered credit providers who do not have to account to the NCR on an annual basis about initiatives or processes they have put in place to comply with the NCA for the development of the consumer credit market. To close this gap in the regulation it is recommended that all credit providers are to be required to register irrespective of the number of credit agreements they have. Furthermore to mitigate compliance and business costs especially for small credit providers, innovative tailored compliance mechanisms that will be best suited for small credit providers without complex systems can be devised.
- Unregistered credit providers are also to be required to submit compliance reports on their conducts as it appears that the NCR had challenges obtaining information from small or unregistered credit providers. This will help in monitoring the credit market as there appears to be a lot of abusive practices by small credit providers. The case of Werlan Cash Loans trading as Lebathu Finance an unregistered credit provider operating in a remote area of Free State province shows the extent of gross violation of the consumer rights as such much must be done to protect consumers from unregistered credit providers.
- The supervision of the credit market must be strengthened through domestic and international coordination by regulators. The NCR must reinforce its monitoring mechanism and supervision of the market participants. Co-ordination in terms of legislative development, enforcement, and market conduct is necessary. The financial sector regulation ought to be coordinated with monetary, fiscal and other economic policies so as to take into account systematic risks. Regulation must be focusing on the entire system as opposed to one institution. There must be extension of regulation of private pools of capital credit rating agencies including the currently excluded credit providers falling outside the threshold. There must be no credit provider falling outside the perimeter of regulation.
- The impact has been meaningful to some limited extent in developing the credit market but the framework has to be modified so as to stimulate further development and compliance by smaller credit providers.

10.2. Conclusion

The selected methodology has enabled the researcher to effectively assess and evaluate the salient role played by NCA framework in impacting the conduct of credit providers in the South African consumer credit market. The NCA regulatory architecture has played a salient role in pioneering a new culture and enhancing the development of the credit market. There is however still a lot of challenges around the implementation of the NCA by credit providers as evidenced by the levels of compliance. It was evident that NCA on its own is not adequate formula for influencing the conduct of credit providers and developing the credit market especially when considering aspects of volatility, interconnectedness of the global financial markets, dynamic nature of the market spurred by technological changes, and volatile the credit marketing highlighting the constant need for urgent reform to retain its competitiveness.

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