

REFORMS IN THE NIGERIAN BANKING SECTOR: IMPLICATIONS, ISSUES AND CHALLENGES

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Abstract

The focus of this paper is on the implications issues and challenges of banking industry reforms from 1986-2009 and beyond. This is the era of banking deregulation or expansionary banking era, which incorporates government policy thrust and adopted by the Regulatory authorities towards healthy financial system in Nigeria. In pursuit of the focus of this paper: it treats numerous issues. It did an overview and ex-ray in detail the nature of the banking reforms in Nigerian between 1986 -1995 Structural Adjustment Programme Era (SAP), PostSAP Era (the guided Deregulation and Globalization Ear 1996 and beyond). Furthermore, it critically examines the current banking reforms since 2004 and its development implications on the economy. The paper concludes that if the current reform is well implemented, it will positively impact on meeting the development challenges facing the country and could strengthen the operational efficiency of the financial system which could accelerate the pace of sustainable economic development.

Introduction

Countries embark upon government economic plan, programme and reforms in order to enhance the growth and development of their economies. According to Onwumere, (2005) economic growth refers to increase over time in a country's real out put per capita conveniently measured by increases in a

country's per capita gross national product (GNP), while economic development can be viewed as a process of growth which should be reflected in a high degree of self-reliance in the abundant utilization of natural resources.

Banking reforms generally have been undertaken in countries especially those in African and Asia within the preview of guided, deregulation and globalization through some forms of financial liberalism. The objectives of reforms have largely been: to improve the financial strength and lending capacity of bank through re-capitalization; to promote real banking activities; to strengthen prudential regulations (i.e. guidelines or rules and regulations designed to control and prevent banks from taking risks with depositors fund beyond their capacities); to promote competition while avoiding market failures and to evolve a sound banking industry and by extension, a more efficient financial system.

Osemeke (2008) opined that the following could necessitate the above:

Occasional bank distress that cause serious hardship to depositors; dependence on public sector funds by a majority of domestic banks; weakness of the domestic private sectors while the public sectors is very strong. to the extent that lending favours public institutions promoting sustainable growth and development of the economy.

Generally, banking reforms comprise some of the reasons usually advanced for government intervention in economic activities, an issue that has been controversial and may be as old as economics itself. Furthermore, banking reforms in Nigeria, took the form of regulation, deregulation and supervision in order to preserve the stability of the National economy (Cameron, 1972)

Thus, whatever happens in the banking sector attracts more than a cursory attention of most economic agents. Accordingly, since the Central Bank of Nigeria initiated this current banking reforms on July 6, 2004 lost of interest have been shown on the banking industry. Indeed, economic agents appreciating the imminent significant changes in the Banking environment have started posting for post reform operations (Ogunbunka, 2005). According to Sanusi (2010), the critical challenge that Nigeria faces today as a nation is how to create some irreducible minimum standards of financial system stability that will promote strong financial institutions and the emergence of budding banking system, and hence ensure sustained growth and development in Nigeria and indeed in the rest of Africa.

The focus of this paper is on the Nigerian experience in developing, over time, an efficient and sustainable banking sector for economic activities to thrive. The vision is for a system that integrates the domestic, foreign, short and long term sources, where banks can exploit each others' comparative advantages in cost-effective financial services delivery.

The prime objective of this paper is to qualitatively examine the developmental implications, issues and challenges of banking sector reforms from 1986 to 2010. The choice of the review period was informed by the need to afford us the hindsight pre-reform and post-reform performance of the sector in the last decades for a better judgment. It is hoped that the recommendations deduced from the findings would form veritable inputs for the improvement and fine-tuning of the current reform process.

To make the discussion lucid, the rest of the paper is structured as follows: following the introduction is section two which attempts to review the evolution of banking sector reforms in Nigeria, eliciting the salient features of the reform policies already implemented between 1986 - 1995 structural adjustment programme (SAP) era; Post SAP era (the guided de-

regulation and globalization era 1996 and beyond); current banking reforms since 2004, as well as the achievement of the sector reform objectives. Section three considers the developmental implications, issues and challenges of the banking reforms. Section four concludes the paper.

An Overview of Nature Of Banking Sector Reforms In Nigeria.

This section will focus on the banking reforms in Nigeria from 1986-1995. Though, historical reference might be made to period outside the time framework with a view to assessing the impact on the period. This period was legally the beginning of the structural adjustment programme (SAP) Era, which was characterized by federal government major economic reforms including banking industry reforms.

The Structural Adjustment Programme (SAP) Era 1986- 1995.

The Federal government in 1986 introduced the SAP in order to open up the country with the objectives of: achieving balance of payment viability in the short to medium terms; laying foundation for sustainable non inflationary growth; and improving the efficiency of the private and public sectors.

Policy measures adopted to achieve these objectives include: the setting up of a second tire foreign exchange market (SFEM); adoption of appropriate fiscal/monetary policies; dismantling of price controls trade and exchange regulations (liberalization policy) revision of the tariff structure; elimination of petroleum subsidy; commercialization of public enterprise; and over hauling of administrative structure (Nnanna, 1990)

Notable regulatory reform measure in the banking industry, in line with SAP was deregulation. With this the number of entrants into the banking industry increase significantly such that by 1993, the number of commercial banks and merchant banks were 66 and 54 respectively as against 28 commercial bank and 12 merchant banks operating in the country in 1985 (Onwunere 2005). Other measures include:

- i. The promulgation of the central bank of Nigeria (CBN) degree no 24 of 1991 (which had to be amended in 1993, giving more teeth to the CBN to bite harder), and the banks and other financial institution decree (BOFID) No. 25 also of (1991)

meant to effectively control the industry and ensure soundness.

ii. The Nigeria deposit insurance corporation (NDIC) decree was promulgated in 1988 (Decree 22 of 1988), though the corporation commenced operations in 1989 with the functions which included insuring deposits liabilities of license banks providing technical and financial assistance to the bank and assisting in the quest for a healthy banking environment.

iii. Initial rationalization and eventual removal of credit ceiling for sound banks and shift to indirect approach to monetary management with open market operations (OMO) as main instrument.

iv. Enhance interest rate management: Removal of all control on interest rates in August 1987 with CBN fixing only its minimum rediscounting rate (MRR) to indicate its desired direction of interest rates. Prescription in 1991 of a maximum margin between each banks average cost of funds and its maximum lending rate with a later prescription of savings deposit rate and minimum lending rate. Restoration of partial de-regulation in 1992 banks only required to maintain a specified spread between their average cost of funds and their minimum lending rates. Removal of maximum lending rate ceiling in 1993 and Restoration of direct interest rate control in 1994.

v. Improvement in payment system which started with implementation of the magnetic ink character recognition (MICR) involving phased adoption of MICR technology for processing of inter bank transfer and in-house cheque, promotion of automation of payment system by banks.

vi. Establishment of the people's bank in 1989 and the community bank in 1990 was in order to ensure grass root reach/development (by way of extension of credit and to mobilize more funds outside the banking industry and inculcation of banking culture.

vii. The introduction of prudential regulation-prudential guidelines in 1990. This has been described by many as significantly sanitizing banking operations in the country and has been very useful in stemming financial distress (Ojo; 1994, Ekpenyong, 1993).

viii. The establishment of the Nigeria Export and

Import Bank (NEXIM) in 1991 to promote export of non-oil goods through the provision of credit and risk bearing facilities. This was in addition to an earlier established National Economic Reconstruction Fund (NERFUND) and Bureau exchange 1989 by decree in order to provide easier access to a variety of credit for small and medium scales enterprises.

ix. The setting up of the fail banks (recovery of debt financial malpractices tribunal) which came into force in 1994 with a view to checking and punishing insider excesses and other associated factors that underline the health of the banking industry and the financial sector.

A review of this SAP period (1986-1995) revealed that the banking industry witnessed court - throat competition with many, especially the new entrants, adopting all kinds of strategies to outwit each other, branch network of banks increased astronomically. The merchant bank branches for example increased from 26 in 1985 to 144 in 1994 while commercial banks branches increased from 1297 to 2541. Competition leads to innovations in products and service delivery leading to a critical overhaul of the banking industry.

However some banks created risk assets at incredibly low interest rates with or without collaterals or adequate cover while some others generated liabilities at incredibly high rates (the extreme case being 100%). In all insider abuse manifested in several dimensions (granting loans secured and unsecured to dummy organizations and individuals out right stealing etc) high rate of loan repayment default especially by states governments, federal ministries and parastatals, management incompetence, the general economic down turn and adverse macro economic condition; policies like the dual exchange rate regime (started with SFEM in September, 1986) the use of stabilization securities with debited funds not made available to banks in the face of problems, withdrawal of government funds without prior notice and non-payment of contractors who had executed projects for government and inadequate regulatory supervisory capacity among others were major contributory factors that brought about crisis in the banking industry which reached an epidemic proportion in 1994 when 55 out of the 120 operating banks were distressed (CBN,2006).

This period also witnessed a gradual return of

confidence and sanity in the banking industry through government action that came belatedly. For instance, the establishment of the NDIC was to ensure industrial safety and soundness. The money and capital markets witnessed some vibrancy (Onwumere, 2005). The failed banks (recovery of debts) and financial malpractices decree which despite its post event enactment was meant to check and punish insider excesses and associated crime. Many bankers received wide-ranging punishment under this decree.

Nevertheless, Sobodu and Akiode (1994) observed that the banking environment that emerged from the reform was inefficient, undercapitalized, riskier, and less liquid and generated lower returns on assets relative to the pre-reform period. Ikhide and Alawode (2001) added low human capital in terms of the dearth of qualified management personnel to meet the challenges of the sudden growth in the industry as another weak feature of the system.

Post SAP Era (The Guided Deregulation and Globalization Era 1996 and Beyond).

No doubt, the world is inextricably linked by globalization. Thus, the economic and financial crisis, which started in the United States, destabilized markets and economies (developed, developing and underdeveloped) around the globe and has continued to dominate discussions on the global economy. These days one would hardly watch the television or browse through national and international newspapers, magazines and journals without stumbling upon headline news of how political leaders are scrambling for strategies to mitigate the impact of the financial crisis on the domestic and global economy.

The major banking reforms of this period were to ensure that banks in Nigeria became globally competitive while implementation of many past reforms measures with a view to ensuring stability in the system was continued.

The major policies of this era include:

Total deregulation of interest rates in October 1996; upward review of minimum paid up capital of banks in 1997 to N500m and later to N2.0bn; adoption of universal banking system in 2001 to create a level playing field for all financial operators; re-introduction of Dutch auction system (DAS) in July 2002 with a view to realigning the Naira exchange

rate, enhancing transparency and curbing capital flight from the country. Under the system, there is intervention by the CBN twice weekly and end-users bought foreign- exchange at their bid rates through authorized dealers; guidelines rolled out by the CBN in 2004 on electronic banking (e-banking) practice in Nigeria in line with global trend. Banks were encouraged to install ATM machines for cash withdrawals specific guidelines on standards and use of e-money products such as credit cards, debit cards, digital cash, etc were spelt out by CBN in line with international best practices; CBN's promotion of automated payment system in order to reduce delays in clearing of payment instruments, reduces cash transaction and enhances monetary policy's transmission mechanism.

Implementation of Real Time Gross Settlement (RTGS) System in order to eliminate risk in large value payments and increase efficiency of the payment system, this involves

Appointment of 7 banks (that met CBN's requirements) as settlement banks to perform clearing and settlement functions for other banks; introduction of National saving certificate and variations of cash reserve requirement (CRR) and the MRR to enhance liquidity management.

Further to liquidity management by CBN, withdrawal of public sector funds from banks when necessary (upon two week's notice) and return of same when liquidity conditions improved.

The Current Banking Reforms Since 2004

This subsection is treated in two parts: (i) current banking reform 2004- 2008 (ii) 2009-date.

(i) Current Banking Reform 2004- 2008

As observed by Nwankwo, (2003), banking is an industry in transition. The Financial industry of the millennium will look very different from the way it looked in the 1990s. According to the author, "the dynamics of this change are rooted in several fundamental transition forces; government deregulation, technological change, cultural and demographic change, changes in the economic climate, industry consolidation, and new competitive challengers (Kolawole, 2006).

Individually, each of these transition forces has influenced the financial industry. When they converge, these forces will more dramatically affect

the industry's competitive force in the years ahead. It was no accident that the current changes in the banking sector constituted the most pervasive of the reform programmes of the Federal Government of Nigeria.

Banking plays a pivotal role in any economy and remains the catalyst for economic growth and development. It is so important that most countries in attempts to reform their economies for growth and development, turned first to it. The soundness of a country's economy is therefore inextricably intertwined with the health of her banking system. As Nigeria moved into the millennium, the preponderance of opinion among stakeholders in the economy favoured strengthening the Banking sector. Quite easily, the main driver of happenings in the Nigeria banking environment is the Central bank of Nigeria induced capitalization enhancement and consolidation of banking institution. This policy has brought with it a banking land scope characterized by the following (Ogubunka, 2006):

Aggressive fund raising by banks to meet the N25 billion naira new minimum capital base; unprecedented patronage by banks, of the capital market offering their shares for public investment; bombardment of the investing public with bank's private placements and rights issues; redirection of investable funds towards banks with consequences for either sectors of the economy.

Further to the above, the answer to that call came in the mode of an all-embracing policy for the reform of Nigeria's banking industry, released by the Central Bank of Nigeria (CBN) on July 6, 2004. The reform outlined a thirteen point agenda aimed at recapitalizing, consolidating and strengthening the banking institutions in Nigeria in order to make them more supportive of the economy.

The main thrust of the policy was the increase in minimum capitalization of banks defined as aggregate shareholders funds unimpaired by losses from N2 billion to N25 billion with full compliance by 31st December, 2005. Other elements/tents of the banking reforms are as follows: (CBN, 2004).

- (i) Phased withdrawal of public sector funds from banks, starting in July, 2004
- (ii) Consolidation of banking institutions through

mergers and acquisitions;

(iii) Adopting of a risk focused and rule based regulatory framework;

(iv) Adopting of zero tolerance in the regulatory framework, especially in the area of data/information rendition/reporting

(v) Automating the process for the rendition of returns by banks and other financial institutions through the enhanced financial analysis and surveillance (e- FASS)

(vi) Establishment of a hotline, confidential internet address (governor@cenbank.org) for all those wishing to share any confidential information with the governor of the Central Bank on the operations of the banks or the financial system.

(vii) Strict enforcement of the contingency planning framework for systemic bank distress.

(viii) Establishment of Assets Management Company as an important element of distress resolution.

(ix) Promotion of the enforcement of dormant laws, especially those relating to the issuance of dud cheques and law relating to the various liabilities of the board members of banks in cause of failings of the banks.

(x) Revision and updating of relevant laws and the drafting of new ones relating to the effective operations of the banking system.

(xi) Collaborating closely with the Economic and Financial Crimes Commission (EFCC) in the establishment of the financial intelligence unit (FIU) and the enforcement of the anti-money laundering and other economic crime measures and;

(xii) Rehabilitating and effectively managing the Nigeria Security Printing and Minting (NSPM) Plc to meet the security printing needs of Nigerian, including the banking system, which constitutes over 90% of the NSPM's business.

It is pertinent to state that prior to these current banking reforms, the Federal government of Nigeria has in 2004 identified problems confronting the

financial sector to include the following: the inability of the sector to play a catalytic role in the real sector; shallowness of the capital market; dependence of the banking system on public sector funds as a significant source of deposits and foreign exchange trading; inaccurate information; Non harmonization of fiscal and monetary policies and non-prompt repayment of bank loans (National planning commission 2004).

In order to resolve the above-identified problems, the Federal Government Policy thrust was to build and foster a competitive and healthy financial system, to support development and to avoid systemic distress; deepening the financial system in terms of assets volume and instrument diversity; drastically reduce and ultimately eliminate the financing of government deficits by the banking system in order to free up resources for lending to the private sector; review capitalization of financial institutions in the system, and develop a structure of incentives to enable the financial system to play developmental role by financing the real sector of the economy.

Nothing the impact of effective financial intermediation in the economy, the following strategies were incorporated into the monetary policy framework and adopted by the regulatory authorities:

embark on a comprehensive reform process aimed at substantially improving the financial infrastructure (Legal codes, information system); restructure, strengthen and rationalize the regulatory and supervisory framework in the financial sector; addressing low capitalization, the poor governance practices of the intermediaries that submit inaccurate information to the regulatory authorities and the consequent costs to the financial system; in collaboration with banks and other financial institutions, workout a structural financing plan to ensures less expensive and more accessible credit to the real sector; directing government policy towards financial deepening (establishing links between rural and urban banking and non banking and formal and informal financial systems) and financial product diversification (filling the missing gap for commercial financial services for small and medium size enterprises with the new services based on best practice technologies for cash flow financing, leasing e.t.c (National Planning Commission 2004).

Commenting further to the above, the banking industry's operational performance was not in the best of states when the reforms were introduced as could be observed from table 1 below.

Table 1: Rating of Banks Using the "Camel" Parameters

Category	Number			
	2001	2002	2003	2004
Sound	10	13	11	10
Satisfactory	63	54	53	52
Marginal	8	8	14	16
Unsound	9	9	9	10
Total	90	90	87	87

Source: CBN (2004:15)

The above Table shows the rating of licensed banks by CBN using the capital adequacy, asset quality, management, earnings and liquidity (CAMEL) parameters. The marginal and /or unsound banks exhibited weakness such as under capitalization; liquidity, weak/poor asset quality and poor earnings, among others (CBN, 2004). There is no doubt that marginal and unsound banks will not play any meaningful role in meeting the country's development challenges. It was not surprising therefore that the reforms announced by then CBN Governor (Professor

Charles Soludo) are geared towards having a sound banking industry with operations that can compete globally and of course, meaningfully aid Nigeria's economic growth and development.

There is no doubt that the consolidation exercise had some positive impacts on the banking sector. The banking system was transformed from 89 banks to 25 through regulatory merger and acquisition and latter to 24 through market-induced merger and acquisition. Bank branches grew from 2,900 in 2005

to almost 5,500 in mid-2009. Besides deepening of the capital market, the banks were positioned to actively participate in a wider range of activities, including financing of infrastructure and the oil sector.

However, while the consolidation exercise lasted, certain developments in the economy and within the banking system itself put the banking sector at serious risk. Between 2004 and 2008, Nigeria enjoyed unprecedented increase in oil price which resulted in huge inflow of foreign exchange and robust economic growth. This, coupled with appreciable level of foreign direct investment inflows, resulted in huge liquidity in the economy which the real sector of the economy could not absorb (Adedipe, 2010).

The excess liquidity found its way into the stock market as shown in the unprecedented rally in the stock prices on the Nigerian Stock Exchange between 2006 and March 2008. The excess liquidity also allowed banks to raise capital. Fresh capital raised between 2006 and first quarter of 2008 amounted to N1, 603 billion. The increase in capital supported banks' balance sheet growth with banking sector assets as percentage of GDP increasing rapidly to 60 per cent from about 30 percent in 2004. With significant capital and greater liquidity, banks were increasingly under pressure to create risk asset amidst limited product innovation and diversification. This, coupled with poor risk management practices, ultimately led to a concentration of assets in certain areas, in particular margin lending and oil trading/marketing. As at end-December 2008, banks' total exposure to oil industry stood at over N754.0 billion, representing over 10.0 per cent of the industry total and over 27.0 per cent of the shareholders' funds.

Thus, in mid-2008 when the global financial and economic crisis set in, the domestic financial system was already engulfed by several interdependent factors that led to the re-emergence of an extremely fragile banking system similar to pre-consolidation era. These factors included macroeconomic instability caused by large and sudden capital inflows, major failures in corporate governance at banks, lack of investor and consumer sophistication, inadequate disclosure and transparency about financial position of banks, critical gaps in regulatory framework and regulations, uneven supervision and enforcement, unstructured governance and management processes at the CBN/ weaknesses within the CBN, and

weaknesses in the business environment.

According to Sannusi (2010), it is clear, that when the global crisis hit Nigeria, the banking sector was ill-equipped to weather the storm in spite of recapitalization. As we are all aware, the financial crisis had an adverse effect on both the oil and gas sector and the capital market where the Nigerian banks were exposed to the tune of N1.6 trillion as at December 2008. The result was a sharp deterioration in the quality of banks' assets which immediately led to concerns over banks' liquidity. Indeed, the Nigerian banking sector was thrown into severe crisis as many of the banks became distressed.

An assessment of the health of the banking sector between 2008 and 2009, using CAMEL parameters, indicated that no bank was rated A. However, one (1) bank was rated B, eleven (11) C, three (3) D, while nine (9) were rated E, compared with zero (0), three (3), eighteen (18), two (2) and one (1) respectively in 2008. The assessment indicated that twelve (12) banks did not exhibit serious weakness that necessitated supervisory concerns. However, twelve (12) banks, as against three (3) in the preceding year, manifested debilitating conditions that required supervisory attention. This is illustrated in table two (2).

Table 2: Rating of banks using "CAMEL" Parameters in 2009

Rating	2008	2009
A	0	0
B	3	1
C	18	11
D	2	3
E	1	9
Total	24	24

Source: CBN 2009 Annual Reports and Accounts

The computed average Capital Adequacy Ratio (CAR) of the banks indicated that eleven (11) did not meet the stipulated minimum ratio of (0.0) per cent, compare with two (2) as at end- December 2008, the asset quality of the Banks, as measured by the ratio of nonperforming loans to industry total, deteriorated as it increased from 6.3 per cent in 2008 to 32.8 per cent. This ratio was above the industry threshold of 20% maximum prescribed in the contingency plan for systemic distress. The development was attributed to the CBN requirement that banks make full provisions

for all non-performing, off-balance sheet engagements under the new supervisory regime. The average industry liquidity ratio of 35.3% was above the 25% minimum requirement. Three (3) banks, however, failed to meet the stipulated ratio, as against two (2) in the preceding year (CBN, 2009).

Furthermore, it was discovered that nine banks were the main users of the Expanded Discount Window (EDW) over a nine-month period ending June 2009. Accordingly, when the CBN eventually closed the EDW in July 2009, and in its place, guaranteed interbank placements, it was observed that these nine banks were the main net-takers under the guarantee arrangement. At this point it was clear that the issue was far beyond the liquidity problem and if drastic actions were not taken, the financial system could collapse.

(ii) Current Banking Sector Reforms 2009 till Date

Given the precarious state of the Nigerian banks, the CBN in June 2009, took a three pronged approach to assess the financial condition of the 24 banks. The first was the special examination exercise jointly conducted by the CBN and the Nigerian Deposit Insurance Corporation (NDIC)

According to (Sanusi 2010) this exercise highlighted inadequacies in capital asset ratios and liquidity ratios as well as weaknesses in corporate governance and risk management practices in Nine (9) banks. These banks were found to be in a grave situation as a result of capital, liquidity and corporate governance concerns. They failed to meet the minimum 10 per cent capital adequacy ratio and 25 per cent minimum liquidity ratio. Apart from accumulating high non-performing loans, these banks were seriously exposed to the oil and gas sector as well as the capital markets. Poor risk management practices in the form of absence of necessary controls measures were prevalent as the board and management of the banks had failed to observe established controls. The remaining 14 banks were found to be in a sound financial state and did not require the CBN to take any action.

The second approach was to carry out diagnostic audit through independent consultants. The report of the audit exercise revealed greater magnitude of weak financial condition of the nine banks. All of them were "technically" insolvent with significant negative asset value. It also exposed several illegal activities that had

been taking place in five of the affected banks.

It was against this background that the CBN moved decisively to strengthen the industry, protect depositors and creditors, restore public confidence and safeguard the integrity of the Nigerian banking industry.

The initial measures/ initiative taken by the CBN in conjunction with NDIC and the Federal Ministry of Finance (MOF) included injection of N620 billion into the nine banks; the replacement of the chief executives /executive directors of eight of the nine banks with competent managers with experience and integrity; reaffirmation of the guarantee of the local interbank market to ensure continued liquidity for all banks; and guaranteeing of foreign creditors and correspondent banks' credit lines to restore confidence and maintain important correspondent banking relationships. When the new management of the banks took office, it became necessary to also carry out further detailed and independent assessment of the financial conditions of the banks. Thus, the third approach was to carry out management account audit of the affected banks by their new management. The outcome was very much in line with that of the audit report. Consequently, the management took numerous actions under the CBN guidance to ensure that the banks operated effectively with particular emphasis on improving transparency and operations (Sansui, 2010).

To improve operations, the new management took steps to: (i) improve reporting infrastructure, internal governance and risk management procedures; (ii) increase transparency and disclosure; (iii) ensure effective and continuous communication with all stakeholders; (iv) ensure weekly reporting between the MDs and the CBN on financial performance, loan recoveries, and; (v) immediate report of any material developments to the CBN. Measures taken to improve operations included continued focus on loan recovery to improve NPL ratios; reducing cost to income ratio; avoiding unnecessary costs; focus on de-risking and de-leveraging the balance sheet and liquidity management. There is no doubt that these initiatives enabled the nine banks to continue normal business operations and prevented a total collapse of the banking sector.

It is pertinent to state here that this present reform is a continuation of the 2004-2005 Thirteen (13) point

agenda articulated by the former governor of the apex bank Professor Chukwuma Soludo, while Soludo's main focus was on consolidation and recapitalization of banks, his successor, Sanusi Lamido Sanusi is using the four (4) pillars to reposition the banking sector. The focus of the Central Bank of Nigeria is first of all to ensure that there is financial sector stability and, secondly, that the financial system assists in growing the real sector of the economy. It is important to note that any economy that cannot create jobs on a continuous basis, reduce poverty, and guarantee its citizens functional and qualitative education as well as world class infrastructural facilities is not only unsustainable but would remain globally uncompetitive. Attainment of this fit goes beyond short term palliative measures. It requires a strategic medium to long term measures. This explains why the focus of the recent CBN reforms is in the following four areas (pillars) namely: enhancing the quality of banks, establishment of financial stability, enabling healthy financial sector evolution, and ensuring that the financial sector contributes to the real economy (Sanusi, 2010).

Implications of Banking Reforms

The happening in the Nigerian Banking environment today has implications for the economy of the country going forward. The implication of this current reform is that at the end of the first phase of the reform programme on December 31, 2005, the number of Banks in the country reduced from 89 to 25 Mega/large banks, which are now stronger and have enormous financial resources at their disposal, thereby helping to restore confidence in the industry. By the Central Bank of Nigeria's account, the exercise double the aggregated capitalization from N384 billion (US\$3 billion) in 2004 to N755.2 billion (US\$5.5 billion) in 2006, with N64 billion (US\$500 million) of this amount representing inflows from foreign direct investment (Soludo 2006).

Another implication is that a high level, new competitive phase had ensured in the industry, thus engender quite a number of things. For example, they have been increase in the development of new products, seeking of opportunities outside the country by opening off- shore branches. Guaranty Trust Bank Plc, for instance commenced its off shore branch in Ghana. The Guaranty Trust Bank (Ghana) Ltd, commenced operations in March, 2006 in its purposely built head office in Accra, the Ghanaian Capital (GTB Annual Report, 2006). UBA Plc also

has its presence in the United State, being the only bank in African to have off shore branch in United State (UBA Annual Report, 2006). In addition, Zenith Bank Plc, has on 30th March, 2007 opened a subsidiary called Zenith Bank UK in the United Kingdom (Abiodun, 2007).

Furthermore, the current banking reforms have enhanced the capital base of consolidated banks; which initially improved lending to the various sectors of the economy. The banks had sufficient funds to advance credit facilities to both individuals and cooperative bodies engaged in business in all sectors of the economy.

Innovations in the banking products/services delivery is due to improvement in technology and globalization of operations in the industry thereby aiding modernization in the Nigeria economy. Gone are the days that banks resort to round tripping to remain afloat. This is because of the very recent introduction of a central IT system to monitor daily activities of banks. Thus banks are largely restricted to carrying out core banking functions (Ekanem 2006).

The Banking reforms have led to the development of new framework for monetary policy implementation in the country. CBN recently replaced the minimum rediscount rate (MRR) with the monetary policy rate (MPR). The MPR will now serve as an indicative rate for transactions in the interbank money market as well as other banks interest rate. Also CBN came up with the Real Time Gross Settlement (RTGS) system, which replaces the Nigerian Inter-Bank Settlement System (NIBSS) due to the growing need to automate the existing settlement process within the Nigeria financial system. The introduction of the RTGS is aimed at increasing the efficiency of the payment system thereby reducing settlement risk and lead time for reconciliation (Oronsaye, 2007).

There has been an increase on employment generation especially at the middle and lower levels of the industry in the short and long runs. The increase in branch Networks of banks aided employment of both capital and labour. For instance, UBA Plc which as at today is one of the largest financial services group in Nigeria and West Africa with a balance sheet size in excess of N2.24 trillion has retail network of over 711 as at end- December 2009; compared with 460 business offices at end of

September, 2005 and 360 business offices as at end of September, 2004. The number of persons employed by the banks as at 31st September, 2006 was 4659 compared with 3787 as at 31st March, 2005. This represents increases of 28 percent and 23 percent respectively, while as at December 31st, 2009 the total number of employees and directors increased to 11,791 (UBA, 2009).

Besides the above, it is expected that interest rates regime will return to single digit while foreign exchange rate will become more stable. Furthermore as a result of competition, banks operating margins will fall against rising operating cost trends. The regulatory Authorities and security Agencies have intensified their surveillance on banks over unethical practices, money laundering, economic and financial crimes. This entails more challenges on the supervisory authorities especially in terms of capacity and capability, thereby aiding better management of the banking/financial aspect of the economy (Ogubunka, 2005, Onwumere-2005). The effect of this is enhanced economic growth and development of the economy as more funds are channeled into productive investments with increased vibrancy of the money and capital market.

Central to healthy financial sector evolution is the establishment of the Asset Management Corporation of Nigeria (AMCON) as part of a broad banking sector crisis resolution strategy. The AMCON Act 2010 was signed into law on July 19, 2010. When fully operational, AMCON would serve as a vehicle to free the banks from the weight of their non-performing assets and accelerate the process of financial revitalization of the banking sector. Besides, the CBN is currently reviewing the basic one-size-fits-all model of banking that has emerged since consolidation. In addition to reviewing the universal banking model, The CBN considers it appropriate to introduce greater diversity in bank mandates. In the near-term, it should be possible to have international, national, regional, mono-line and specialized banks such as Islamic banks in the country. Already the guidelines for specialized institution have been fixed as follows: non-interest bank (regional), N5 billion, noninterest bank (National), N10 billion, and primary mortgage institutions, N5 billion. The commercial banks have also been restructured into regional, national, and international banks with paid-up share capital of N10 billion, N 25 billion, and N 50 billion, respectively. These and several other measures have

positively impacted on the banking sector.

Another implication of the reform is that the CBN has taken concrete measures to finance the real sector of the economy. Some of these measures include:

(I) N500 Billion Critical Infrastructure Fund: The Infrastructure Intervention Fund was introduced in April 2010 by the CBN to provide long-term support to finance critical infrastructure projects. The Fund is a 15-year debenture investment in the Bank of Industry (BOI) for on-lending to all eligible DMBs and Development Finance Institutions (DFIs) at 1% interest rate. These DMBs and DFIs will in turn lend to promoters of the projects at a maximum of 7.0%, (a) N200 Billion Refinancing/Restructuring of SME/Manufacturing Fund: Out of the N500 billion Critical Infrastructure Fund approved, N200 billion was set aside for refinancing/ restructuring of SME/Manufacturing Fund in April 2010 to enable banks refinance and restructure their existing loan portfolio to SMEs and manufacturing. The 15-year facility has a 3-year moratorium with loan amounts ranging from N5 million (minimum) to N1 billion (maximum) to single obligor at an interest rate of 7.0 per cent annually repayable quarterly. According to Sanusi, (2010) on July 28, 2010, the N130 billion programme for refinancing and restructuring of loans to SMEs and manufacturing sector was launched. Already, 317 beneficiaries have been screened for the disbursement of the money. (b) N300 billion for long term funding of Power and Aviation. The balance of N300 billion was also approved to provide long term funding: Power (N250 billion) and Aviation Industry (N50 billion).

Furthermore, Inter-bank rate and other key money market rates have moderated significantly compared to the pre-reform period. Weighted average inter-bank call rate and other key money market rates fell to below the end-December 2008 level by end-August 2009 after the sharp increase between January and July 2009. As at 28 July 2010, the inter-bank rate had fallen to 1.12 per cent while the Open Buy-Back (OBB) rate stood at 1.10 per cent. In response to the increase in MPR of September 21, 2010, both the Inter-bank call rate and OBB have trended upward averaging 10.56 and 8.23 percent, respectively by November 15, 2010.

In spite of the fluctuation in money market rates, the lending rates have remained consistently high. The

prime lending rate stood at between 18 and 19 per cent while the maximum lending rate hovered between 22.56 and 23.91 per cent over March 2009 and May 2010. The average prime lending rate remained at 16.66 per cent in both October and September 2010, declining from 16.89 per cent in August 2010. The average maximum lending rate, however, declined to 21.85 per cent in October 2010 from 22.20 per cent in September 2010 and 22.31 per cent in August 2010. The weighted average savings rate equally declined marginally to 1.48 per cent in October, 2010 from 1.49 per cent in September, 2010 and 1.41 per cent in August, 2010 while the consolidated deposit rate increased to 2.31 per cent in October 2010, up from 2.07 per cent in September and 2.27 per cent in August 2010. The spread between the average maximum lending rate and the consolidated deposit rate, however, narrowed to 19.54 per cent in October, 2010 from 20.14 per cent in September 2010, and 20.04 per cent in August 2010 (Sanusi, 2010)

On the whole, the immediate effect of the banking reform is the rebound of public confidence in the banking system on account of enhanced capital strength. Major producers of goods and services in Nigeria now look with rekindled hope that banks are in a better state to provide necessary financial supports for their businesses, to enhance their contributions to the National Economic Growth. The dividend of the banking industry consolidation would become more apparent as complementary initiatives are being taken toward sustainable economic development of the country. The recently launched micro financial policy, the enhanced capital base and consolidation of Insurance Companies (Insurance reforms policy), Re- capitalization of stock broking firms, are some of such initiatives.

Issues and Challenges

Banking reforms entails the assumption of the private sector as the driver of economic activities and growth, while the role of government is aligned to that of providing a healthy competitive level playing environment for players for the delivery of quality services and products at minimal cost. So far, several reform measures had been undertaken in Nigeria to meet the immediate challenges of evolving a virile and competitive environment that would stimulate greater resource mobilization, improved financial intermediation, deepen and widen the money and capital markets and develop the private sector in the process. Though the current reform measures have no

doubt yielded significant benefits there still stare in the face of managers of the economy some fundamental challenges. Some of these challenges are-highlighted below:

The widening interest rate spread, which is suggestive of poor competition, mirroring the Oligopolistic structure of the industry, remains a discretionary factor in the market. Government's recent ability in the elimination of the spread in the foreign exchange market is an indication that a similar feat could be achieved in the narrowing of interest rate spread if appropriated.

Complementarily, the achievement of price stability must be pursued with Vigor as a stable inflation rate is a precursor for investment and growth. Here government's intention to migrate from monetary targeting to inflation targeting deserves some commendation. In addition, there is need for monetary authorities to ensure that growth in money supply is in consonance with the output projection with a view to curbing inflationary pressures.

Another issue of concern is the short-term nature of banking system funds which had greatly hamstrung bank's ability to lend long-term. It was established that domestic funds are indispensable in a country's quest for development and that savings growth rate was sluggish. In order to mobilize long term savings, government must, as a matter of priority, resuscitate the dilapidated infrastructural facilities for the efficient and low cost operations of business, especially the small scale enterprises. Given the quantum of informal activities in Nigeria, the provision of infrastructural facilities would not only boost productivity (increased GDP), but also increase income and savings of individuals and corporations. A reduced operational cost would mean more profit (wealth) and business expansion which would lead to more employment generation and increased demand for credit.

Another challenge before the government is the holistic implementation of economic reforms. Hitherto, banking sector reforms were undertaken in isolation without complementary reforms of the other sectors, more so, such reform measures were incongruently sequenced. This had led to the grave erosion of the successes of banking sector reform and the distortion of policies. Emenuga (2002) succinctly captures the reform process then as being hasty in the

execution of the approved measures, partial in scope, destitute of other concomitant adjustment measures, and inconsistent. It was not surprising that it did not yield the desired results. Bearing in mind the inter-linkages of the sectors, it becomes expedient that reform measures must not only cut across all sectors but must be properly sequenced.

In addition, while commending government for undertaking fiscal reform measures such as the benchmark pricing of oil, constitution of the cash management committee, due process, budget deficit limits, etc, the passing into law of the Fiscal Responsibility Act by the National Assembly need to be fast-tracked. The passage of the bill will not only stem expansion in money supply but also reduce inflationary pressures in the economy as government is statutorily restrained from resorting to the CBN for its expenditure financing even in the face of dwindling revenue, among other benefits. Furthermore, the CBN's intention to establish a financial crime court in conjunction with the EFCC is long overdue. This will not only discourage malpractices in the industry but also ensure the early arbitration of cases brought before it; this will restore sanity and boost confidence in the industry and hence promote savings and deposits as well as credit facility for the promotion of investment in the economy (Lemo, 2005).

That notwithstanding, credit must not be taken away from the government on the current reform measures so far, especially in the banking sector and the re-engineering of the process of governance. In recognition of the fact that a liberalized banking sector without a corresponding supportive surveillance arrangement might result in anti-social behaviour by the banks, the CBN's supervisory and surveillance apparatuses had been strengthened with the deployment of sophisticated and customized information technology applications such as the Electronic Financial Analysis and Surveillance System (EFASS), Real Time Gross Settlement (RTGS) system and Consolidated supervision, etc. The Bank is in addition pursuing vigorously the attainment of full autonomy to enable it adequately face the challenges of the emerging banking sector and the economy at large, in addition, in appreciation of the dearth of human capacity in the financial sector, the Bank went into capacity building alliance with the DMBs especially in core area like risk management to forestall a repeat of the crises of the 1990s.

The federal government should pursue with transparency the current reforms in the pension sub sector to a logical conclusion in order to fully harness the potentials of the sector for economic growth. The dominance of the banking sector could be detrimental to the overall objectives of development, given the peculiarities of the industry and the short-term nature of its funds. The sector could serve as a veritable source of long term funds for sustainable investment. However, the greatest challenge in this direction remains the gaining of confidence of the people in terms of the sustenance of the reforms beyond the current administration.

In the same vein the conversion of community banks into microfinance companies is an innovative scheme that would in no small measure stimulates savings for long term investment, as well as explore the many ways of financing needs of the small and micro enterprises in the poor urban and rural areas. Hulme and Mosley (1996) opined that such microfinance organizations should be designed to cope with the problems entailed in lending to small scale borrowers without collateral and ... are likely to need some form of public subsidy to cover the very high administrative costs involved. Effort must therefore be made to avoid a repeat of the "draining" activities of the erstwhile rural banking system in which rural branches were used as conduit for siphoning rural resources to finance urban activities.

One of the pillars of the reform blue print is ensuring that the financial sector contributes to the real economy. Rapid financialisation in Nigeria did not benefit the real economy as much as had been anticipated. Development financial institutions set up for specific purposes such as housing finance; trade finance and urban development have not fulfilled their mandates. Many successful emerging markets have witnessed proactive government actions to ensure that the financial sector contribute to the real economy. Nigeria can learn from countries with successful track records in creating financial accommodation for economic growth through initiatives such as development finance, foreign direct investment, and venture capital and public-private partnerships

Although, economic growth has been robust but a major challenge is how to sustain and translate this into new employment opportunities. The link between the major growth drivers, particularly

agriculture and manufacturing, continue to be weak. Hence, the manufacturing sector remains an insignificant contributor to growth. There is urgent need to address all binding constraints to growth. Inadequate or absence of basic economic and social infrastructure remains a major binding constraint on Nigeria's growth and development. There are needs to fast-track the proposed reforms in some key sectors of the economy, notably power and oil/gas sectors, to attract the much-needed investment and reduce the huge import bills on refined petroleum products. There is absolutely no reason why our refineries should not be functional.

Resumption of credit to key productive sectors of the economy is crucial because of the obvious medium-to-long term implications for the real economy. This requires adequate regulatory interventions to develop all sectors of the credit market from microfinance to larger corporations. While acceleration of credit market reform such as dispute resolution mechanism, credit bureau regulation, and leasing laws are very critical, adequate attention must also be given to development of public-private partnership framework, legal framework for rental markets, etc.

A major challenge also lies in reducing the high lending interest rate in the face of low money market rates. Growing banking system liquidity is still desirable and, hence, the need to quickly bring the banking system reforms to closure. There is urgent need to inject fresh funds into the banks affected by regulatory actions in addition to the removal of the "toxic assets". This is where AMCON is very critical. A major challenge remains how to strike an appropriate balance between monetary, fiscal and other policies. There is a limit to what monetary policy can do to deliver economic growth. Other complementary policies must be in place. Banking sector reforms is a necessary but not a sufficient condition for economic growth and development. Complementary reforms in other areas of the economy, particularly in agriculture (in addition to energy sector mentioned above) to curb high import bills on food (rice) and reduce demand pressure in the foreign exchange market, are absolutely necessary.

Conclusion and Recommendations

Conclusion

The history of the Nigerian financial system is replete

with several reform measures articulated to meet the challenges of the economy. While some of the reform objectives were met, others were far from being realized. This paper thus objectively examined the banking sector reforms in Nigeria vis-a-vis the issues and challenges. The result of banking reforms implemented in Nigeria in the last two decades is mixed.

In spite of several challenges, it is gratifying to note that no single bank in Nigeria has collapsed since year 2005 and no depositor has lost his/her money as a result of the banking sector crisis. Furthermore, the stress test conducted recently on the twenty four banks by CBN has shown that the financial soundness of the banks (both intervened and non-intervened) has improved significantly compared to the crisis period. The banking system has been stabilized and the nine most affected banks have continued normal operations while modalities for injecting fresh capital into them either by shareholders or through acquisition and merger arrangements are being finalized. To a large extent the reforms have succeeded in returning macroeconomic and banking system stability.

Growth in real savings had not risen as expected. Interest rate spread persistently widened owing largely to rising inflation. Too much emphasis was placed on interest rates and savings mobilization while the precursor to these (real income) was discounted. Credits to the private sector which the industry demand was not made available to it. There is therefore the need to engender competitiveness among the financial institutions. The study noted the significant development in the banking sector and bond markets but call for further deepening and widening of the bond market to brace up with the global challenges. Specialized financial institutions need to be encouraged for the market segment that might not be attractive to the banking industry. There is great need for the rejuvenation of social and economic infrastructural facilities given its potential in improving productivity create wealth and increase the much needed savings for long term investment. The paper noted and commended current efforts of government in strengthening the prudential supervision of the banking institutions.

The main aim of the current banking reforms is to rise a new generation of banks with large capital base comparable to what is obtainable in the international

financial markets. The institutions should have enough muscle to compete effectively in the global financial markets. They must also practice banking ethically and efficiently, and command high public confidence. It is hoped that if the current reforms are well implemented, it will positively impact on meeting the development challenges facing the country.

Recommendations

The apex bank should ensure that governance best practices are embedded in the banking industry including the CBN as well as ensuring that risk-based supervision (RBS) principles, methodology and processes are established across the CBN and NDIC. Under the RBS, the CBN should establish a programme management structure within the CBN to ensure that there is a high level of communication with the industry, implementation quality is measured and examiners acquire the necessary skills. A monitoring mechanism to measure the programme's impact and ensure a high level of responsiveness to issues raised by the industry could also be established. The regulation and regulatory framework reform programme should review the regulations and guidelines around the key causes of the crisis by industry regulators; harmonization and raising to world-class standards of the supervision processes, technology and people within the various financial regulators; and establishment of a centre of competence for international financial Reporting Standard (IFRS) and N-GAAP+ implementation.

Also the CBN should be transformed to ensure good corporate governance, stronger information management system, people development, and enhanced disclosure to levels expected in major investor countries such as the United States, the United Kingdom, South Africa, China and India.

There is urgent need to check the excessive costs in the banking system which is attributable, in the main, to infrastructure cost, high salaries/emoluments for executives and poor operational efficiencies. The CBN should encourage the development of electronic channels to drive down industry cost structure while working with the banks to improve on the quality of service delivery in order to improve customer confidence. Nigeria presently has a large informal sector which has been estimated by the World Bank to constitute about 57.9 per cent of Nigeria's Gross National Product (GNP). This is higher than what obtains in Brazil, Ghana, Turkey, Malaysia and South

Africa. Developing a financial system that will take care of this large segment of the economy is of utmost necessity.

To ensuring that the banking sector contributes to the real economy the CBN should through the reforms: evaluate on continuous basis, the effectiveness of existing development finance institutions and initiatives in agriculture, manufacturing, and import-export credits; take a public lead in encouraging the examination of critical issues for economic development, such as the impact of infrastructure e.g power, port and railway; lead further studies on potentials of venture capital and private-public partnership initiatives in Nigeria, and cooperate with State governments in running pilot programmes that are aimed at directing the financial sector's contribution to the State's socio-economic development.

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