

SAVINGS MANAGEMENT IN DEVELOPING COUNTRIES

BY
CHIEF (DR) J.O. SANUSI
GOVERNOR
CENTRAL BANK OF NIGERIA

An Address Delivered at the Banking and
Financial Services Symposium, organized
by the Commonwealth Business Council,
London, 3-4th July, 2002

Mr. Chairman,
Distinguished ladies and gentlemen,

I feel delighted and honoured to be invited by this August body to speak on the topic, "Savings Management in Developing Countries". Your choice of this topic must have been informed by the importance of savings in the development process of any nation. The distinction between the rich and the poor nations of the world is evidenced in the level of savings that could be generated and made available for investment. In the advanced countries, the income per capita is high enough to allow the accumulation of savings, which translates to higher investment. Savings and investment are closely related, with financial institutions playing the intermediation role of mobilising and allocating financial resources from savers to investors. The soundness of financial institutions determines the magnitude of savings and the efficiency of its allocation. The weak institutional framework, as well as low income level significantly inhibit effective savings mobilisation in the developing countries, resulting in low savings, low investment and low growth.

2. I have attempted in this paper to discuss the fundamental issues involved in savings mobilisation and management in the context of the developmental aspirations of developing countries in general, and Nigeria in particular. The paper is structured into four sections. The importance of savings mobilisation in economic

development is highlighted in section one. Section two discusses efforts at savings mobilisation and management in Nigeria, while section three reviews the strategies to encourage savings. Section four concludes the paper.

I. IMPORTANCE OF SAVINGS MOBILIZATION AND MANAGEMENT IN ECONOMIC DEVELOPMENT

3. Savings represents that part of income that has not been consumed. This provides resources for investment purposes. There are three broad types of savings at the level of the domestic economy. These are voluntary savings, involuntary savings and policy induced savings generated to increase output in a situation of less than full employment.

4. The importance of savings in the developing economies can be discussed from two main perspectives. The first relates to the resource gap which needs to be bridged through enhanced savings culture amongst the population. As a result of low per capita income, most developing countries have low savings rates relative to their counterparts in the advanced economies and this has affected the level of capital formation in those countries.

5. Among the developing countries, savings rates vary considerably. Studies have shown that East Asian countries save more than 30 per cent of their Gross National Disposable Income, while savings GDP ratio in Sub-Saharan Africa is less than 15 per cent. Regional disparities have been on the increase over the past three decades as savings rates have doubled in East Asia and

stagnated in Sub-Saharan Africa, Latin America and the Caribbean. Studies have, however, shown that the poor are capable of saving more where the environment is conducive. In a United Nations workshop on savings in 1999, it was concluded that the importance of savings lies in its potential to reach the poorest of the poor.

6. In many developing countries, more capital is held in the informal economy than in the formal economy. A large part of this capital is held in small amounts by those living near or below the poverty line. Developing countries can bring these numerous small capital holdings into the formal sector by providing poor households with savings services that can meet their needs and made readily accessible to them. This assertion provides the impetus for the establishment of micro finance institutions (MFIs), such that access to savings services could be enhanced. This has lifted the pace of economic development in some of those countries. In spite of the imperfect financial environment in most developing countries, studies have shown that micro finance institutions have succeeded in some countries in South Asia and part of Africa notably Zambia, Tanzania and Uganda. Bangladesh is often cited as the model for successful implementation of the MFIs for the poor.

7. Another perspective is that with sound macroeconomic environment, supported by a stable and honest government, the environment for resource mobilization and its effective utilization would have been created. These pre-conditions have been lacking in most developing countries and this explains the low saving

capacity among these countries. The challenges facing most of these countries, therefore, centre around the need to ensure popular participation in both governance and economic activities, which could generate incomes for the vast majority, and thus enhance savings and investment. This would accelerate the pace of economic development.

8. The importance of putting institutional framework in place to provide avenues for savings and investment must also be recognised. While formal institutions have worked efficiently in the developed economies, the outcomes in the developing countries have been less than satisfactory. The financial dualism that characterise most developing economies and the need to put the informal sector in proper focus pose serious challenges for savings mobilisation in these economies. Cross country experiences in Africa, Asia and Latin America have shown that savings can be harnessed from the poor given the right institutional arrangements and efforts at reaching the population with innovative products that meet their needs.

II. SAVINGS MOBILIZATION AND MANAGEMENT IN NIGERIA

9. Savings mobilization and management is at the core of financial intermediation. In Nigeria, formal banking activities began in 1894 with the establishment of a branch of a foreign bank. The developments since then have resulted in extensive network of bank branches in various locations in the country, with most of them concentrated in the urban centres, as in other developing countries.

The post office savings outlets that were inherited from the colonial era could not be efficiently operated to meet the aspirations of the population. In addressing this problem, Central Bank of Nigeria initiated a number of policy actions to encourage growth in domestic savings, especially among the rural and the urban poor. The institutional arrangement for the mobilization of savings in Nigeria is discussed under two main broad headings: the formal sector and the informal arrangement.

Formal Institutional Framework

10. Formal institutions that have been established to encourage financial savings include the deposit money banks, insurance companies, pension funds and the capital market, as well as innovative institutions like the Peoples Bank and the Community Banks. The ratio of institutional savings relative to Gross Domestic Product (GDP) was 10.0 per cent in 2001.

(i) Deposit Money Banks

11. The deposit money banks constitute the main formal channels through which financial savings are mobilized in Nigeria. Currently, there are 89 banks with 2,965 branches located all over the country. The banks provide services and offer various types of products which give some returns to savers. Of the total amount of institutional savings in Nigeria more than 95 per cent was accounted for by banks. Attempts were made in the past through the rural banking scheme to encourage banks to locate in the rural areas. However, with progress

made in financial sector reform other innovative institutions have been promoted to encourage rural savings.

(ii) Insurance Companies and Pension Funds

12. Insurance companies and pension funds have contributed to savings mobilization. There are 118 insurance companies currently in operation. Life insurance premium constituted the main channel through which resources are pooled by insurance companies to finance economic development. Pension funds represent money set aside to provide for employees when they retire from service. The funds which is largely contributory provide an avenue for making resources available to enhance economic development.

(iii) The Capital Market

13. The Lagos Stock Exchange, established in 1961, is the prime operational institution in the Nigerian capital market. It has six trading floors located in various parts of the country, on which equities and government stocks are traded. As at the end of 2001, market capitalisation amounted to ~~N~~662.6 billion. A commodity exchange was commissioned in Abuja in 2001.

iv. Innovative Financial Institutions

14. Following financial reforms since 1986 and the need to expand the scope of financial intermediation to meet the developmental aspirations of the Nigerian economy, community banks and the Peoples Bank were established to operate at the community level in the urban and rural areas. A community bank is a unit bank, which is established through the efforts of the various groups in the community. The performance of the community banks, however, suffered a

setback following the distress in the financial sector in the recent past. At the end of 2001, there were 747 community banks in operation. With the current involvement of the CBN in the regulation and supervision of community banks, the institutions are being strengthened to perform their expected functions of financial intermediation in the rural economy. The Peoples Bank of Nigeria was established in line with the Bangladesh's Grameen Bank experience, with branches located in both the urban and rural areas of the country. The Peoples Bank accepted deposits from clients who were mainly self-employed, artisans and traders who did not have access to conventional banking facilities. It also extended credit to its clients and provided advisory services that could help in the development and expansion of such trades. The recent restructuring and recapitalisation of development financial institutions (DFIs) led to the merger of the Peoples Bank with the Nigerian Agricultural and Cooperative Bank (NACB) and the Family Economic Advancement Programme (FEAP) to form the Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB). The main objective was to streamline the institutional arrangement within the development finance sub-sector and enhance the performance.

(v) Finance Companies and Primary Mortgage Institutions

15. These institutions operate within the financial sector to provide various services to their clients. Finance companies are time-deposit-taking institutions, that contribute to the deepening of the financial system. They were, however, not regulated or supervised until recently. Most of the institutions, therefore, collapsed during the

banking crisis of the early 1990s. The primary mortgage institutions operate at the retail end of the housing finance sub-sector. Their operations are targeted towards mortgage financing and they take deposits of various maturities in furtherance of the objective of housing financing. At the end of 2001, 98 finance companies and 74 primary mortgage institutions (PMIs) were in operation in Nigeria.

Informal Institutions in Savings Mobilization

16. There are still various institutional arrangements in the informal credit market in spite of the progress that has been made in the liberalization of the financial sector. These include the Cooperative Societies, the Rotating Savings and Credit Associations (ROSCAS), otherwise called Esusu, Credit and Town Unions, which serve as a vehicle for pooling small savings. The shortcomings of these arrangements notwithstanding, they provide veritable sources of investible funds for their members. The challenges facing the monetary authorities are not only that of integrating these institutions into the formal financial system, but largely that of ensuring adequate monitoring of their activities in order to plug the leakages, which their operations constitute to the monetary policy framework.

III. STRATEGIES FOR SAVINGS MOBILIZATION AND MANAGEMENT IN NIGERIA

17. Strategies to enhance savings mobilization and management must recognize the importance of the small savers and the need to

encourage them. The strategies for savings mobilization and management as they relate to the Nigerian economy are as follows:

(i) Poverty Reduction Initiatives

18. Poverty must be addressed in order to put a larger population in the category of savers. For poverty reduction initiatives to succeed, the beneficiaries must be empowered and made to contribute to the wealth of the economy through their involvement in viable business or trade. There is also the need to streamline the various poverty reduction programmes to ensure the achievement of the desired objectives. In recognition of the need to empower the poor and involve them in nation-building, the present Government has made the poverty reduction strategy the cornerstone of its economic policy.

(ii) Competitive Financial Environment:

19. The current efforts at ensuring a sound and stable financial system, through sanitisation and strengthening of the supervisory framework, are expected to provide a conducive financial environment that engender greater competition. This is expected to facilitate the introduction of new savings products that could enhance the mobilization of resources for development.

(iii) Capital Market Reforms:

20. The capital market is expected to play a pivotal role in the mobilization of long-term resources for development. The current reform efforts in the Nigerian capital market provide opportunities for both public and private organisations to access the market for investible funds. Efforts will be sustained to make the market more efficient in order to attract foreign investments into the country.

Presently, the introduction of the National Savings Certificates (NSC), a medium to long-term savings instrument, is being finalised. Its introduction is expected to pool savings for productive investment.

(iv) Growth in Output:

21. The economy has to grow in order to allow for savings mobilisation. The current efforts at rehabilitating the existing infrastructural facilities are aimed at increasing the productive capacity of the economy, which is expected to raise per capita income and thereby enhance savings.

(v) Stable macroeconomic environment:

22. The pursuit of sound macroeconomic policies is considered important in savings mobilization and management. Sound economic policies will ensure the achievement of low inflation which facilitates the savings-investment process. In Nigeria, more emphasis is being placed on improved co-ordination of fiscal and monetary policies, as well as other economic policies in order to achieve macroeconomic stability which is essential for sustainable growth.

IV. CONCLUDING REMARKS

23. Distinguished Ladies and Gentlemen, the challenges confronting most developing countries include the need to integrate the various informal savings institutions into the mainstream of the formal financial system and thus, harness such resources for development, as well as the need to reduce poverty and increase per capita income. Also, there is a need to encourage the growth of pension funds as a veritable instrument for long-term investment and sustainable growth.

More importantly, it is very pertinent to stress the importance of political stability and good governance, as savings mobilization can hardly be sustained in a chaotic and unstable environment. Finally, there is no viable alternative to institutional reforms in enhancing allocative efficiency of financial savings. Developing countries should embrace it.

Thank you for your kind attention.

July 4, 2002