

TOWARDS A NEW MONETARY AUTHORITY AND FINANCIAL SYSTEM: Interim Progress Report

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Outline

- Introduction
- Core Mandate of the CBN
- Financial System as Pillar of the New Economy: The Vision, the Reforms
- Key Outcomes of the Reforms
- Challenges and Next Steps
- Conclusions

Core Mandate of CBN

- Issuance of legal tender currency in Nigeria
- Maintenance of external reserves to safeguard the international value of the legal tender currency
- Promotion of monetary stability and a sound financial system in Nigeria
- Acting as banker and financial adviser to the Federal Government

THE VISION, THE REFORMS...

- Where Were We?
- 89 fragile, small and uncompetitive banks tainted by corruption and mismanagement
- A system with low depositor confidence
- Banks that could not support the economy
 - (bank credit as % of GDP in 2003 only 24% compared to over 100% for SA; and 57% as African average)
 - 3 of Nigerian banks used to be among top 500 banks but none was among top 1000 in the world in June 2004

The Vision, The Reforms...

- “Nigeria as Africa’s Financial centre, and CBN as one of the best in the world”
 - Within 10 years, Nigerian bank(s) should be among the top 50—100 banks in the world.
- A New Banking System that depositors can trust, and investors can rely upon: to usher in a new economy
 - Recall the 13- Point Reform Agenda on July 6, 2004

The Reform Agenda

- Recapitalization of banks to N25 bn shareholders' fund by December 31, 2005
- Consolidation of the banking sector through mergers and acquisition
- Zero Tolerance on misreporting and infractions
- Stricter enforcement of corporate governance principles
- Payments System Reforms
- Etc, Etc.

Key Outcomes of the Reforms

Outcomes

- Larger capital base: (from under \$3bn to over \$5 bn)
 - About N350.2 bn new investment (nearly US\$3 bn)--- largest in non-oil sector in one year
 - FDI inflows at about US\$500 million
 - Share of NSE doubled from 24% to almost 50%
 - Deepening of capital market; consciousness about capital market among population
 - Capital market becomes more liquid, capitalized
- Greater depositor confidence
- About 24- 25 banks to emerge (compared to 89)

Outcomes

- ALL 4 foreign banks recapitalized despite initial hesitation
- Liquidity in the system induced interest rate to fall drastically....
- Lending to private sector rose by 40% (unprecedented) and non-oil sector grew by est. 8.5% in 2005
- More banks now have access to credit lines from foreign banks (one received \$250 million from two foreign banks---
- never received more than \$25 m before).
- Economies of Scale
 - Unit costs of operations reduced as overlapping functions scrapped
 - Staff costs of post-merger smaller than pre-merger over time
 - Lower interest deposits due to ‘safety in bigness’ in minds of depositors

Outcomes

- Increased potential to finance big transactions--- (higher single obligor limits)
- Dilution of ownership--- as most banks become PLCs; and more regulators oversee them---- SEC and NSE.
- More effective supervision---- focus on fewer (25) banks rather than 89 mostly sick banks
- No more wholly regionally/ethnically based banks
- No Government dominant ownership by 2007
- Depositors as king in liquidation process
- About 11 banks likely to be liquidated compared to 25 that were somewhat 'dead' in June 2004

Outcomes

- Short-run Employment issues---
 - Massive lay-offs as feared have not occurred
 - Relative to counterfactual– if previously weak banks were liquidated, more jobs to be saved under consolidation than if it did not happen
 - More SUSTAINABLE jobs emerging rather than ‘bubbles’ as previously
 - Larger credit to the non-oil sector creates more jobs than the entire banking industry
 - Offer of SMEEIS facility to staff that might lose their jobs
 - Banks required to fulfill their contractual obligations to staff that leave

Challenges and Next Steps

Challenges and Next Steps

- Revocation of Licenses of Unhealthy banks
- Liquidation Process to Begin After Verification and Valuation
- List of heavy and Chronic debtors to the system; Asset Strippers; and Mismanagers handed to EFCC and Police for prosecution under Failed Bank Act.
- Liquidation Options
 - Selective Purchase and Assumption (Assumption of liability and Cherry-picking of assets by Healthier Banks)
 - CBN issuance of bonds and payments of private depositors within 3 months of liquidation----- a record compared with previous liquidation schemes
 - Bridge bank to take some of the weak banks

Next Steps

- What Happens to Public Sector Deposits trapped?--- After sale of Bank Assets, less private sector deposits and other confirmed creditors (ie, if CBN issues Bonds)
- Cost of Liquidation Options?----- Likely lowest in the world
 - Under Purchase and assumption?-----
 - CBN issuance of Bonds? -----
 - (Breakdown into NDIC insured and non-insured components)
 - Bridge Bank to take ‘sick’ banks

Who Bears the Cost of Final Resolution?--- IMF recommends
Treasury should bear it---- Budget appropriation

CBN to issue instrument--- and gradually write it down as assets are disposed off.

Next Steps

- Due Diligence on ALL Banks in the system--
--(re-verification of capital) to prevent 'Bubble capital'.
 - Contingency Plan in case any 'Bubble' bursts (CBN as lender of last resort!)
 - Getting Stronger Banks Ready to Acquire any shaky bank(s)
- Zero tolerance regarding infractions; misreporting; transparency; etc...

Next Steps

- IT and New Ways of Doing Business
eFASS; RTGS; --- no place to hide— for banks to lie about their state of affairs
- CBN and BOFIA amendments to strengthen CBN in enforcement
- Restructuring/Strengthening Banking Supervision Department (risk-focused; skills)
 - New robust Code of Ethics and Conduct
 - Incentive and Sanctions Regime--- supervisors who fail to find what they should, would be penalized; and those who succeed are rewarded!

Next Steps

- **TRAINING:** Intensive and extensive training for:
 - CBN Staff--- re-orientation and skills
 - Board members of commercial banks and MFBs
 - Staff of banks--- on critical skills in the industry and managing Change/transition in the 'new' industry
- **Decentralization of CBN Supervisory Infrastructure---** Zonal Structure especially for Microfinance Banks; Agric Schemes; SME programmes
- **Getting CBN Branches and Currency Centres to ALL States**

Next Steps

- Locking-in Reforms through International Benchmarking for Nigerian banks...
 - Partnership with foreign banks in reserve mgt leapfrogs internationalization of processes and global integration
 - International Rating Agencies for Nigerian banks

Managing Internal integration processes of newly merged banks--- people and IT issues

Next Steps

- Managing the next phase of consolidation---
market driven
 - Bank(s) with US\$1 billion in capital base to receive at least US\$500 million reserves to manage

Road Show for the New Face of Banking in
Nigeria/Africa!

Key Lessons

- Political Commitment as key success factor—many expected reversal of policy due to ‘Nigerian factor’
 - President’s Commitment and Courage critical
 - Received about 17 threat letters
- Many banks were empty shells
 - Huge non-performing portfolios
 - Large insider-related loans
 - Huge negative shareholders’ funds
- Regulators and Auditors have share of blame: Provided room for banks to ‘play games’
 - Need to revolutionalize processes especially IT
 - Skills and capacity of regulators to be strengthened
 - New incentive/sanction regime and Code of Conduct for staff

Banking Sector Revolution Not Enough:

- More focused, efficient and effective CBN--- Project EAGLES
- Getting Back to Basics: CBN as Monetary Authority--- Meeting the IMF challenge!
- Currency, Payments System and Reserve Management Reforms
- Microfinancing and Developmental Roles of CBN
- Other Complementary Reforms--- Mortgage; Infrastructure; Agriculture; Legal/institutional; etc
 - African Investment Bank

Conclusions

CONCLUSIONS

- We are on course to achieve Objectives
- Consolidation is not an Event, it is a Process---- a long one to serve Nigerian economy
- A new, focused, effective and efficient CBN is emerging
 - More effective Monetary and exchange rate mgt
- Complementary Reforms in other sectors required.
- CBN is committed to the emergence of a ‘new Nigerian economy’!
- TOGETHER, We Can Build Nigeria that Claims the 21st Century