



MACROECONOMY:

Progress Report on Monetary and Exchange Rate Policies and the Financial System

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Outline

- I: Introduction
- II: Issuance and Management of Currency
- III: Management of Foreign Reserves
- IV: How Sound and Stable is the Banking System?: Unfinished Business
- V: Monetary and Exchange Rate Policies?
(Is the new Forex Policy working?)
- VI: Institution Building and Reforms
 - NSPM, Plc Restructuring
 - Africa Finance Corporation in-formation
 - Payment System Reforms– e-payment systems!
- Conclusion

Introduction

Focus of Presentation?

Not on banking sector reforms---ideally not more than 10% of CBN effort should be on regulation/supervision

Focus mainly on Core mandate:

macroeconomic management--- key prices (interest rate, exch. Rate, inflation), credit and payment systems---- to ensure non-inflationary economic growth and efficient payments system.

Tangentially on Institutional Reforms, including Banking system reforms.

a) Issuance and Management of Legal Tender Currency

- Objective:
 - To promote efficient payments system through CLEAN, COST-EFFECTIVE, SECURE, AND RESPONSIVE currency Notes and Coins
 - Promote the Use of Coins in the payments system

Context:

- On the average, central banks review the currency structure every 5 – 8 years.
- No restructuring of the Nigerian currency since 1984.
- The CBN carried out a comprehensive review of Nigeria's currency structure in 2005.

Currency Management...

Activities/Outcomes?

- Redesign of the lower banknote denominations (N5, N10, N20 & N50), new coin series (50k & N1) and introduction of a N2 coin.
- N20 to be introduced in Polymer substrate
- Effective cost of currency notes down by 41- 58%
- Effective cost of coins down by about 60%
- New banknotes and coins will be issued by the end of 2006.

- The CBN will outsource currency processing and distribution to free the Bank from non-core currency management functions

Currency Management...

- Reforming Nigerian Security Printing and Minting, Plc:
- Context:
 - Loss making as at 2004; owed about N8.5b
 - Only country with Mint but importing banknotes
 - NSPM, Plc never produced up to 1 billion notes in any year in over 10 years
 - Employed about 1800 workers, but needed about 900
- Objectives?
 - A world-class MINT to meet banknote and security documents requirements of Nigeria and West Africa in medium term
 - To stop importation of currency notes after December 31, 2006

Currency Management....

■ Activities/Outcomes?

- CBN's shareholding increased from 2.35% to 77.0% in February 2005
- New Board constituted in March 2005
- New 5-member Magt replaced 14-member team in June, 2005
- Retrenched about 846 staff in Sept 2005
- Output increased by over 30% by Dec. 2005 (1.27b notes--- first time since over 10 years)
- Company was profitable in 2005
- Comprehensive plant restructuring and heavy investment to meet targets of self-reliance
- New Corporate Governance and Procurement Systems
- On Course for Mint Privatization early 2007

Currency Management...

(iii) Promotion of Clean Notes Policy:

To improve the quality of banknotes in circulation,

- Embarked on a campaign to stop the abuse of the naira.
- Major investment to address crisis in our strong-rooms: capacity to process currency notes.
- If Nigerians cooperate and as e-payment system takes root, clean notes will be back in circulation.

b) Management of External Reserves

- Goal: To safeguard the international value of the nation's currency--- (safety, return, and build-up of reserves)
- What is External Reserves? (IMF Balance of Payments Manual, 5th Edition)
 - “those external assets that are readily available to and controlled by monetary authorities for direct financing of payments imbalances, for directly regulating the magnitude of such imbalances through intervention in exchange markets to affect the currency exchange rates and/or other purposes”.
 - (Excludes private sector assets or encumbered external assets)

Growth of Nigeria's Reserves

■ Year	US\$ billions
■ 1999 (May)	4.99
■ 1999 (end)	5.44
■ 2000	9.39
■ 2001	10.27
■ 2002	7.68
■ 2003	7.47
■ 2004	16.96
■ 2005	28.28 (debt pmt)
■ 2006 (June 30: with debt pmt)	36.628

Composition of Reserves as at June 30, 2006

- . CBN Reserves = \$23.563 b
- Government = \$13.065

- TOTAL = \$ 36.628 b

- Caution:
- If you are in doubt, contact CBN before making unsubstantiable statements about reserves, capable of causing financial crisis.
- CBN responded promptly by providing the facts and clarifications to the public who were being confused.
- 7 Nigerian banks in partnership for managing reserves

c) Price and Monetary Stability

- Focus on price stability as the core function: Moving towards inflation targeting – pro-active policy stance!
- Effective Liquidity management framework and new framework for implementing Monetary Policy for launch in July, 2006
- MRR and tight policy against inflation

Comparative Average Lending Interest Rates (%)

	Average Lending Rate	Inflation Rate	Real Lending Rate
GHANA	26	10	16
SOUTH AFRICA	10.5	4.3	6.2
USA	8.25	3.7	4.55
NIGERIA	16.97	10.5	6.47

Price and Monetary stability...

Outcomes?

- 2004 and 2005 met monetary targets
- Met PSI monetary targets (Reserve money) for Q1 and Q2, 2006
- Inflationary pressures contained: now 10.5%

Pressure Points?

Measurement of Inflation (core or headline) when food constitutes 63% of CPI?

Liquidity challenge in the face of possible supplementary budget.

Exchange rate and Forex Management

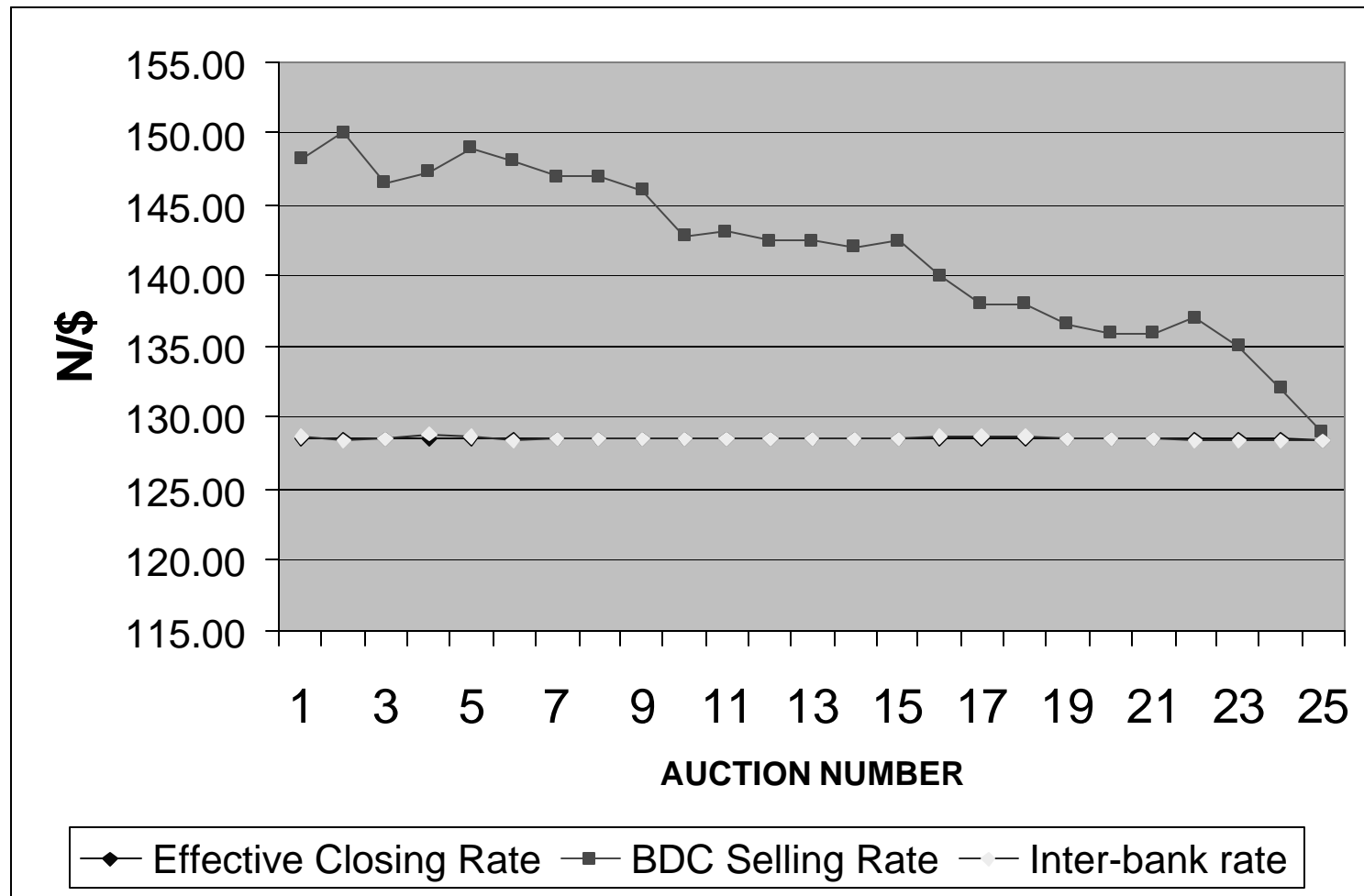
Focus on maintaining a stable exchange rate

- Exchange rate has remained stable for the past two years (appreciating)
- Exchange rate stability was maintained around the pre-determined exchange rate band of plus/minus 3% in 2005
- WDAS system introduced in Feb. 2006 to further stabilize the exchange rate and eliminate the gap between the official window and the inter-bank rate

Exchange rate and Forex Management

- Further liberalisation of foreign exchange market on March 27, 2006 as parallel market rate diverged significantly from official (N151 = \$)
 - Bureau de change brought into the official foreign exchange market as brokers
 - CBN sells forex to BDCs twice weekly
 - Maximum disbursement for BDCs per transaction reviewed upwards from US\$2500 to US\$5000
 - Sale of forex to the BDCs is decentralised to allow branches of the CBN to sell to BDCs within their areas of operation
 - OUTCOME?:
 - (Naira is the currency to hold, not forex)

WDAS, INTER-BANK, AND BDC RATES (March 27- July 3, 2006)



Issues and challenges?

- Is the Policy sustainable? Yes:
 - (Accretion to reserves growing, and CBN marginal player-- \$1.6b surplus Jan-June)
- Is the appreciation faster than predicted by fundamentals?
No.
- Threat: impacts on exports and foreign investment/tourism?
- Messages?
 - We promised; we delivered!
 - Convergence of three rates achieved first time since 1986 (0.8% premium)– efficiency of economy; avoid distortions!
 - Continued progress towards Naira convertibility
 - CBN is studying the market keenly and continue to deepen reforms

 - Appreciation:
 - The President; CBN Team– BDC operators and Licensed dealers

d) Sound Financial and Payments System: What's New?

- 1. 9 Nigerian banks in top 1000 (none in 2003)
- 2. De-listing by FATF: Congrats to Mr. President and all Nigerians.
- Banking sector strongest it has ever been in our history

Sound Financial and Payments System

BANKS: Key indicators	Dec 2003 N'b	March 2006 N'b
Shareholders' Fund	292	811
Total Assets	2,768	4,974
Total Gross Credits	1,162	2,056
Total Deposits	1,409	2,835
Unsound banks	11	0
Net Profit	9	41

Summary

- Assets growth rate = 79.7%
- Capital growth rate = 177.74%
- Deposit growth rate = 101.21%
- Credit growth rate = 76.94%
- Earnings growth rate = 355.56%
- Liquidity growth rate = 75.78%

- CBN had carried out a post consolidation due diligence on banks to ensure the absence of bubble capital
- Post consolidation integration, people, processes, system etc being monitored by the CBN
- New code of corporate governance had been issued on march 1, 2006
- Moving to Risk-based supervision and re-training/re-orientation of banking supervision Department
- Microfinance policy and SME financing

- Challenges
- Concluding liquidation of the 14 failed banks
 - NDIC has obtained final court order to wind up only four banks- Allstates, Lead bank, Assurance bank and Trade bank
 - Provisional order had been obtained for three banks- Afex bank; Hallmark and Fortune bank
 - Two other banks for which orders were granted have appealed judgement
 - Total deposits of private sector in these banks = 78%
- Training for Commercial banks staff and Directors of Banks---compulsory!

- Private depositors of Allstates bank (in liquidation) taken over by Ecobank under the purchase & assumption arrangement
- Lead Bank, Assurance Bank and trade Bank will follow next

Payments System Reforms

- Started the reform of the payments system:
Inaugurated the National Payments System Committee
- Commenced implementation of enhanced cheque clearing system; developed cheque standards; approved Nigerian Cheque Printers Accreditation Scheme; extended Nigeria Automated Clearing System infrastructure to Abuja.
- Promotion of Electronic Modes of Payment
 - (7 banks have international credit card facilities)
 - Soon payment transfers by GSM phone

Africa Finance Corporation in- Formation (AFC)

- A private-public sector partnership with private sector having majority shareholding
- Strong interests on the AFC from within and outside Nigeria
- An international investment bank to be appointed soon as issuing house for private placement
- All Nigerians, Africans and international investors will have opportunity to invest
- AFC expected to take-off last quarter 2006

CONCLUSION



- Thanks for Listening!