CENTRAL BANK OF NIGERIA

FINANCIAL STABILITY REPORT

DECEMBER 2013

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LIST OF ABBREVIATIONS

AIPs	Approvals-in-Principle
AMCON	Asset Management Corporation of Nigeria
AML/CFT	Anti-Money Laundering and Combating the Financing of Terrorism
ASI	All Share Index (Nigerian Stock Exchange Index)
ATMs	Automated Teller Machines
BCEAO	Banque Centrale des Etats de l'Afrique de l'Ouest (Central Bank of West African States)
BDCs	Bureaux de Change
BOA	Bank of Agriculture
BOFIA	Banks and Other Financial Institutions Act 1991 (as amended)
BOI	Bank of Industry
BRICS	Brazil, Russia, India, China, and South Africa
CACS	Commercial Agricultural Credit Scheme
CAR	Capital Adequacy Ratio
CBN	Central Bank of Nigeria
CIBN	Chartered Institute of Bankers of Nigeria
CIFTS	CBN Inter-bank Fund Transfer System
CR6	Concentration Ratio (of the six largest banks)
CRMS	Credit Risk Management System
DFIs	Development Finance Institutions
DMBs	Deposit Money Banks
DvP	Delivery versus Payment
EBAs	Eligible Bank Assets
EDC	Enterprise Development Centre
eFASS	Electronic Financial Analysis and Surveillance System
FATF	Financial Action Task Force
FCs	Finance Houses
FCT	Federal Capital Territory
FGN	Federal Government of Nigeria
FMBN	Federal Mortgage Bank of Nigeria
FMF	Federal Ministry of Finance
FSIs	Financial Soundness Indicators
FSRCC	Financial Services Regulation Coordinating Committee
GDP	Gross Domestic Product
GIZ	Deutsche Gesellschaft fur InternationaleZusammenarbeit (German Society for International Cooperation)
HHI	Herfindahl-Hirschman Index
ICFA	Implied Cash Flow Analysis
IFRS	International Financial Reporting Standards
IFSB	Islamic Financial Services Board
IMF	International Monetary Fund

KYC	Know Your Customer
L/C	Letter of Credit
M_1	Narrow Money Supply
M_2	Broad Money Supply
MCP	Microfinance Certification Programme
MENA	Middle East and North African Countries
MFBs	Microfinance Banks
ML/FT	Money Laundering and Financing of Terrorism
MoUs	Memoranda of Understanding
MPR	Monetary Policy Rate
NAICOM	National Insurance Commission
NDIC	Nigeria Deposit Insurance Corporation
NERFUND	National Economic Reconstruction Fund
NEXIM	Nigerian Export-Import Bank
NFIU	Nigerian Financial Intelligence Unit
NGAAP	Nigerian Generally Accepted Accounting Principles
NIBSS	Nigeria Inter-bank Settlement System
NIRSAL	Nigerian Incentive-based Risk Sharing System for Agricultural Lending
NMRC	Nigeria Mortgage Re-finance Company Plc
NPLs	Non-Performing Loans
NSE	Nigerian Stock Exchange
OBB	Open Buy Back
OFIs	Other Financial Institutions
PAIF	Power and Aviation Infrastructure Fund
PCBs	Private Credit Bureaux
PENCOM	National Pension Commission
PFAs	Pension Fund Administrators
PFCs	Pension Fund Custodians
PMBs	Primary Mortgage Banks
PoS	Point of Sale
PSV 2020	Payments System Vision 2020
RDAS	Retail Dutch Auction System
ROA	Return on Asset
ROE	Return on Equity
RTGS	Real-Time Gross Settlement System
SEC	Securities and Exchange Commission
SMEs	Small and Medium Enterprises
SMECGS	Small and Medium Enterprises Credit Guarantee Scheme
WAMZ	West African Monetary Zone
WDAS	Wholesale Dutch Auction System
WEO	World Economic Outlook

FINANCIAL STABILITY

'Financial stability' is the resilience of the financial system to unanticipated adverse shocks, while enabling the continued smooth functioning of the financial system's intermediation process. A stable financial system contributes to broader economic growth and rising living standards. The financial system performs one of the most important functions in the welfare of citizens by supporting the ability of households and firms to hold or transfer financial assets with confidence. Thus, the stability of the financial system and its adequate analysis and reporting are important policy goals of the CBN.

GOVERNOR'S STATEMENT

During the second half of 2013, while the global economy sustained its recovery, fiscal and monetary authorities focused on measures that would further enhance growth and curb unemployment. In the emerging economies, a decline in commodity prices contributed to the dampening of the significant growth in GDP experienced in recent years. In Nigeria, the efforts to diversify the economy achieved results, as the real GDP growth was mainly driven by growth in the non-oil sectors of the economy.

With respect to monetary policy, rates remained low in most advanced economies. In Nigeria, the policy thrust was to rein in inflation. Thus, the monetary policy rate was retained at 12.0 per cent throughout the review period. Inflationary pressure was, therefore, contained as year-on-year inflation rate was 8.0 per cent at end-December 2013. Money markets and foreign exchange rates were relatively stable. In the near term, we expect to continue the tight monetary policy stance in order to maintain price stability.

For the Central Bank of Nigeria, it was critical to ensure that the shocks noted in the global environment did not threaten the stability of the domestic banking system. Regulatory actions were, therefore, focused on ensuring that the banks maintained healthy loan portfolios by creating high quality assets that would ensure sustainable growth. Meanwhile, the proactive actions taken to resolve the distress situation in the system have achieved the desired results and contributed to the overall stability of the financial system.

Following the successes recorded in the pilot scheme of the cash-less policy, its implementation was extended to five additional states and the Federal Capital Territory in the second half of 2013. The expected reduction in the cost of cash handling in the country was already being achieved. The implementation of the policy has also contributed to the achievement of the Bank's financial inclusion targets. We believe that the inclusion of the economically active but poor people into the formal financial system would enhance the ability of the financial system to contribute to economic growth and development.

With the Federal Government's continued commitment to implementing measures to address security challenges and tackle the disruption in crude oil production, it is expected that the success achieved in these efforts would enhance both economic growth and government's revenue base.

Sanusi Lamido Sanusi (CON)
Governor, Central Bank of Nigeria

EXECUTIVE SUMMARY

Global output was estimated to have grown by 3.0 per cent in 2013, compared with the 3.1 per cent achieved in 2012. However, in the second half of the year, growth achieved was higher than the 2.9 per cent projected for the half year, driven mainly by growth in advanced economies. In Nigeria, real GDP growth was estimated at 6.7 per cent in 2013, compared to 6.6 per cent in 2012. In advanced economies, inflation decreased in 2013 owing to declining commodity prices caused by improved supply and reduced demand from major consuming nations, such as China. In Nigeria, headline inflation decelerated to 8.0 per cent at end-December 2013, from 8.4 per cent at end-June 2013.

In 2013, most advanced economies maintained a stable monetary policy stance. Among the BRICS, only Brazil and India reviewed their policy rates upwards.

The CBN maintained its policy rate at 12.0 per cent in the review period. However, lending rates in the banking industry trended upwards. On the fiscal side, the Federal Government operated at a deficit of 6.3 per cent of GDP, which was financed through domestic borrowings and privatization proceeds.

The CBN examined 21 banks and 14 foreign subsidiaries of Nigerian banks. The results showed that most banks had a stable outlook in their composite risk rating and improvements in their internal audit and financial analysis functions. In addition, the stress test conducted, based on their end-December 2013 call reports indicated that the banking industry was stable and resilient.The key challenges in the industry, however, remained corporate governance and risk management practices.

The Other Financial Institutions sub-sector witnessed several developments, including the establishment of the Nigeria Mortgage Refinancing Company Plc to provide liquidity in the mortgage market and promote availability and affordability of housing in Nigeria.

The Bank continued to promote financial inclusion during the review period in line with its Financial Inclusion Strategy.The geo-spatial mapping of financial services' access points and the Micro Small and Medium Enterprises Development Fund were launched. The Bank also commenced financial literacy/enlightenment programmes through public workshops, secondary schools' outreach, road shows and engagement of the media.

Meanwhile, matured AMCON bonds, as at December 2013 were redeemed in line with the terms of the indenture.

The cash-less policy, earlier launched in Lagos, was extended to five additional States and the FCT.

The Nigerian economy is projected to remain strong, driven largely by increased growth in agriculture, trade and services, while activities in the oil sector are projected to recover in 2014. Although inflation is projected to decline, the 2015 electioneering activities would pose some threat.

This edition of the *FSR* is divided into five sections. Section one reviews global and domestic economic and financial developments, highlighting key stability issues. Section two chronicles developments in the domestic economy, while section three covers regulatory and supervisory activities. Key developments in the payments system are highlighted in section four. Finally, section five provides the outlook for financial stability.

1.0 MACROECONOMIC DEVELOPMENTS AND FINANCIAL SYSTEM STABILITY

1.0 MACROECONOMIC DEVELOPMENTS AND FINANCIAL SYSTEM STABILITY

1.1 Global Economic and Financial Developments

1.1.1 Output

Global output was estimated to have grown by 3.0 per cent in 2013, compared with the 3.1 per cent achieved in 2012[1]. The lower growth rate was attributed to the continued fragility and persistent downside risks in some economies. The growth in the second half of 2013 was stronger than the 2.9 per cent projected in the October 2013 *World Economic Outlook* (WEO). The stronger growth during the second half of 2013 was due to improved macroeconomic and financial conditions in most economies. Global output in 2013 was driven mainly by growth in advanced economies as growth in emerging markets and developing economies slowed down.

Output in advanced economies was projected to improve to 2.2 per cent in 2014, due to higher inventory demand aimed at filling the large output gaps.

The US economy was estimated to have grown by 1.9 per cent in 2013, due to upward surprises to inventories in the second half of 2013. This was expected to improve to 2.8 per cent in 2014, given the carryover effects of final domestic demand supported by reduction in the fiscal drag following the recent agreement on the budget. Japan's growth was estimated at 1.7 per cent in 2013, up from the 1.4 per cent achieved in 2012. It was projected to remain unchanged at 1.7 per cent as the temporary fiscal stimulus was expected to partly offset the drag from the consumption tax increase in early 2014.

Real GDP growth of the Euro area improved to negative 0.4 per cent in 2013, compared with the negative 0.7 per cent recorded in 2012, and is projected to strengthen to 1.0 per cent in 2014 in spite of the uneven recovery within the area. High private and public debts and financial fragmentation were expected to hold back domestic demand, while exports were projected to further contribute to growth, with the improvement in growth being more modest in economies under stress.

The emerging market and developing economies were estimated to grow by 4.7 per cent in 2013, compared with the 4.9 per cent achieved in 2012. The marginal decline in 2013 was attributed to low commodity prices and weak internal and external demand. Growth was projected to strengthen to 5.1 per cent in Sub-Saharan Africa in 2013. Growth in the BRICS countries (Brazil, Russia, India, China, and South Africa) was mixed in 2013. While Brazil improved from a growth rate of 1.0 per cent in 2012 to 2.3 per cent in 2013, Russia slowed down from 3.4 per cent in 2012 to 1.5 per cent in 2013. India[2] grew by 4.4 per cent in 2013, compared with the 3.2 per cent recorded in 2012. China grew by 7.7 per cent in 2013, the same as in 2012, and South Africa recorded a growth of 1.8 per cent in 2013, down from the 2.5 per cent achieved in 2012.

[1] World Economic Outlook (WEO) January 2014 Update

[2] For India, the IMF WEO Report noted that, "all data and forecast are presented on a fiscal year basis in the July 2013 WEO, whereas data were presented on a calendar year basis in the April 2013 WEO." It added that the difference between the April 2013 WEO and the July 2013 WEO Update was adjusted to a fiscal year basis.

Real GDP growth in Latin America and the Caribbean slowed down from 3.0 per cent in 2012 to 2.6 per cent in 2013. Growth in Mexico declined to 1.2 per cent in 2013 from the 3.7 per cent recorded in 2012. In the Middle East and North Africa (MENA) region, growth slumped to 2.4 per cent in 2013, from 4.0 per cent in 2012, due mainly to social and political instability.

Output growth in Sub-Saharan Africa strengthened from 4.8 per cent in 2012 to 5.1 per cent in 2013, and was projected to rise to 6.1 per cent in 2014. The increase in growth in 2013 was supported by domestic demand. In Nigeria, real GDP grew by 6.9 per cent in 2013, higher than the 6.6 per cent achieved in 2012 and is projected to grow by 6.7 per cent in 2014[3].

Table 1.1: Real GDP Growth of Selected Countries and Regions

	2012	2013 (Est.)	2014 (Proj.)	2015 (Proj.)
World Output	**3.1**	**3.0**	**3.7**	**3.9**
Advanced Economies	**1.4**	**1.3**	**2.2**	**3.0**
United States	2.8	1.9	2.8	3.0
Euro Area	-0.7	-0.4	1.0	1.4
Germany	0.9	0.5	1.6	1.4
France	0.0	0.2	0.9	1.5
Italy	-2.5	-1.8	0.6	1.1
Spain	-1.6	-1.2	0.6	1.1
Japan	1.4	1.7	1.7	1.0
United Kingdom	0.3	1.7	2.4	2.2
Emerging and Developing Economies	**4.9**	**4.7**	**5.1**	**5.4**
Sub-Sahara Africa	**4.8**	**5.1**	**6.1**	**5.8**
China	7.7	7.7	7.5	7.3
India	3.2	4.4	5.4	6.4
Brazil	1.0	2.3	2.3	2.8
Mexico	3.7	1.2	3.0	3.5
MENA	**4.1**	**2.4**	**3.3**	**4.8**

Source: IMF World Economic Outlook, January Update 2014

[3]World Bank: *Global Economic Prospects* January 2014

1.1.2 Inflation

A downward trend was observed in the inflation figures of advanced economies in 2013 due to declining commodity prices, amid improved supply and lower demand growth from key emerging market economies, especially China[4]. In addition, weak economic growth in the Euro area, alongside a downward pressure on wages in the periphery, worked together to reduce inflation within the region. However, in emerging market economies, despite a drop in commodity prices, the presence of capacity constraints, weakening exchange rates as well as strong domestic demand pressures in some of the countries, led to a marginal rise in prices relative to 2012.

Overall, inflationary pressures in advanced economies were contained around 1.4 per cent in 2013, down from 2.0 per cent in 2012; on the other hand, emerging and developing countries witnessed a marginal rise in inflation to 6.1 per cent in 2013, from 6.0 per cent in 2012 (Table 1.2).

Inflation declined in France, Germany and USA to 0.99, 1.60 and 1.48 per cent in 2013, from 2.23, 2.14 and 2.08 per cent in 2012, respectively. However, inflation in Japan, Brazil, Russia and South Africa increased to 0.30, 6.21, 6.78, and 5.76 per cent in 2013, from -0.04, 5.41, 5.07, and 5.65 per cent in 2012, respectively (Table 1.3).

Table 1.2: Global Inflation (Consumer Prices)

Consumer prices	2012	2013	2014 (proj.)
Advanced Economies	2.0	1.4	1.7
Emerging and Developing Economies	6.0	6.1	5.6

Table 1.3: Inflation Rates for Selected Countries

Country/ Region	2012 %	2013 %	2014* %
Africa			
Nigeria	12.24	8.00	8.80
South Africa	5.65	5.76	5.70
Egypt	8.60	6.91	9.90
Ghana	9.16	11.65	9.90
North America			
United States	2.08	1.48	1.60
Canada	1.52	1.00*	1.50

[4] http://www.imf.org/external/pubs/ft/weo/2013/02/pdf/text.pdf

Latin America			
Brazil	5.41	6.21	5.80
Argentina	10.03	10.61	12.15
Mexico	4.11	3.81	3.70
Colombia	3.17	2.02	2.90
Europe			
United Kingdom	2.84	2.57	2.10
France	2.23	0.99	1.20
Germany	2.14	1.60	1.50
Russia	5.07	6.78	5.40
Asia			
Japan	-0.04	0.30*	2.40
China	2.65	2.63	3.10
India	11.44	9.01	8.84

- **Sources:** All figures were sourced from Bloomberg except those for India which were from the IMF, *World Economic Outlook* (WEO) October 2013 and January 2014 update;
- (*) Bloomberg estimates

1.1.3 Oil prices

Average crude oil prices declined marginally to US$104.10 in 2013, from US$105.00 in 2012. The decline was attributed to increased supply from new oil discoveries in China and the U.S. as well as the return to the market by Libya and Iran. Furthermore, increasing U.S. production arising from innovations in shale oil technology placed her as the largest non-OPEC producer of liquid hydrocarbons.

Global demand for crude oil was projected to grow at less than 1.5 per cent annually, with the growth coming from non-OECD countries. OECD oil consumption was expected to remain subdued in the light of sluggish economic growth and sustained general energy efficiency.

1.1.4 Monetary Policy Rates

Monetary policy rates remained low in most advanced economies for the greater part of 2013. The U.S. Federal Reserve, the Bank of Japan, the Bank of England and the Bank of Canada maintained their rates at 0.25, 0.10, 0.50, and 1.00 per cent, respectively, while the European Central Bank maintained its rate between 0.25 and 0.75 per cent. The Reserve Bank of Australia reduced its policy rate from 2.75 per cent at end-July 2013 to 2.50 per cent by December 2013.

In the BRICS countries, monetary policy rates remained unchanged, except in Brazil and India where the rates were reviewed upward at end-July 2013 to 10.00 and 6.75 per cent, from 8.50 and 6.25 per cent, respectively (Table 1.4).

Table 1.4: Summary of Policy Rates Across Selected Countries (Jan 2013 – Dec 2013)

Monthly Policy Rate												
Country	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Developed Economies												
Japan	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Europe	0.75	0.75	0.75	0.75	0.50	0.75	0.75	0.75	0.75	0.75	0.25	0.25
UK	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
US	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Canada	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
South Korea	2.75	2.75	2.75	2.75	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50
New Zealand	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50
Australia	3.00	3.00	3.00	3.00	2.75	2.75	2.75	2.50	2.50	2.50	2.50	2.50
ASEAN												
Indonesia	5.75	5.75	5.75	5.75	5.75	6.00	6.50	7.00	7.25	7.25	7.50	7.50
Malaysia	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00	3.00
BRICS												
Brazil	7.25	7.25	7.25	7.50	8.00	8.00	8.50	9.00	9.00	9.50	10.00	10.00
Russia	8.25	8.25	8.25	8.25	8.25	8.25	8.25	8.25	8.25	8.25	8.25	8.25
India	6.75	6.75	6.50	6.50	6.25	6.25	6.25	6.25	6.50	6.50	6.75	6.75
Hong Kong Base	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
South Africa	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00
Other Emerging Economies & South America												
Mexico	4.50	4.50	4.00	4.00	4.00	4.00	4.00	4.00	3.75	3.50	3.50	3.50
Chile	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00	4.75	4.50	4.50
Colombia	4.00	3.75	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25
Africa												
Egypt	9.25	9.25	9.75	9.75	9.75	9.75	9.75	9.25	8.75	8.75	8.75	8.25
Ghana	15.00	15.00	15.00	15.00	16.00	16.00	16.00	16.00	16.00	16.00	16.00	16.00

Source: Bloomberg

1.2 Domestic Developments

1.2.1 Output

Despite the slowdown in some emerging market economies, including the BRICS, the Nigerian domestic economy remained strong in the second half of 2013 as growth in output rose by 1.2 percentage points above its level of 6.5 per cent in the preceding period. The development was attributed to the increase in the contribution of the non-oil sector, reinforced by the relative stability in monetary and fiscal policies. The non-oil sector, in the fourth quarter, recorded a growth of 8.73 per cent, in real terms, and contributed 88.27 per cent to real GDP, compared with the growth of 7.95 and 8.21 per cent in the third quarter of 2013 and the corresponding quarter of 2012, respectively. The growth in the non-oil sector was driven by activities in the telecommunications and postal services (26.73%), building and construction (14.96%), solid minerals (13.61%), hotels and restaurants (13.48%), wholesale and retail trade (11.33%), real estate and business services (11.02%), manufacturing (8.81%), and agriculture (4.29%) (Table 1.5).

The oil sector recorded a real growth rate of 0.30 per cent and contributed 11.73 per cent to GDP in the fourth quarter of 2013, in contrast to the negative growth of 1.15 and 0.53 per cent recorded in the second and third quarters of 2013, respectively. Its contribution to GDP was, however, lower than the 12.50 per cent recorded in the second quarter of 2013.The rise in the growth rate of the oil sector was attributed to improved production levels.

Figure 1.1: Gross Domestic Product

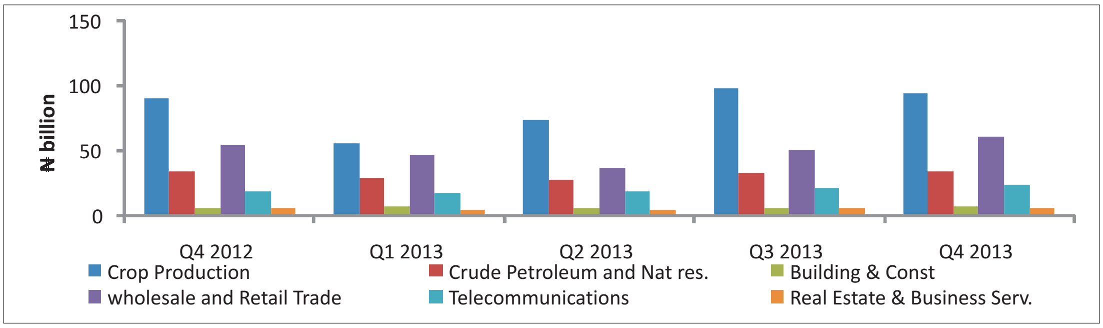


Table 1.5: Percentage Changes in Real GDP by Sector

Sector	Q4 12	Q1 13	Q2 13	Q3 13	Q4 13
Telecommunication and Postal Services	32.44	24.53	22.12	24.42	26.73
Building and Construction	12.55	15.66	14.87	14.31	14.96
Solid Minerals	13.59	12.00	11.84	12.67	13.61
Hotels and Restaurants	-3.12	13.61	13.69	13.66	13.48
Wholesale and Retail Trade	11.19	8.22	7.44	9.03	11.33
Real Estate and Business Services	5.58	9.81	10.58	10.15	11.02
Manufacturing	7.70	8.41	6.81	8.16	8.81
Agriculture	3.62	4.14	4.52	5.08	4.29
Crude Petroleum & Natural Gas	-0.79	-0.54	-1.15	-0.53	0.3

Figure 1.2 : Shares of Oil and Non-oil Sectors in Real GDP

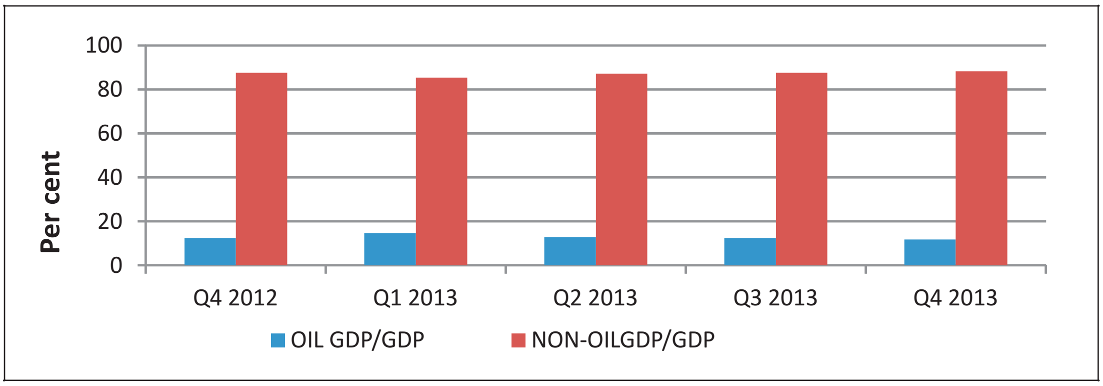
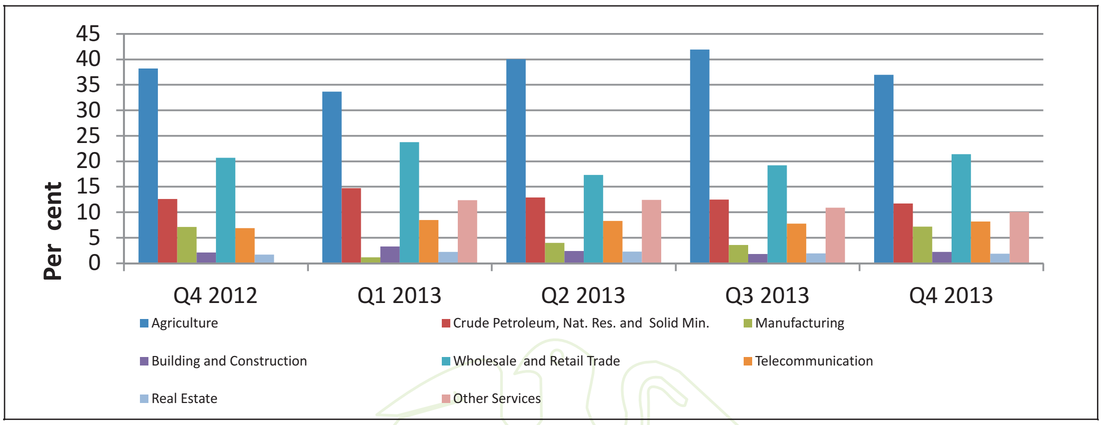


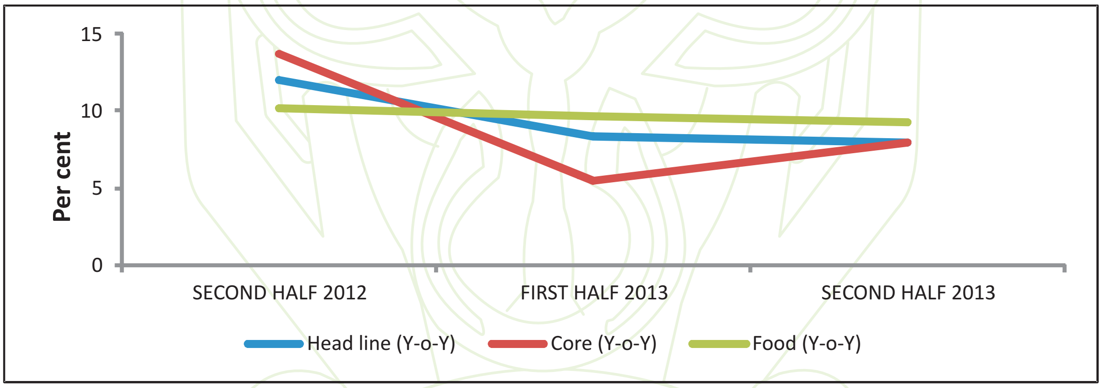
Figure 1.3: Share in Total GDP (%)



1.2.2 Inflation

Inflation was generally mild in the second half of 2013, due largely to price moderation in both food and non-food commodities classification. Year-on-year headline inflation stood at 8.0 per cent in December 2013, down from 8.4 per cent at end-June 2013, and a decline of 4.0 percentage points from the level in December 2012. Furthermore, core and food inflation declined to 7.9 and 9.3 per cent at end-December 2013, from their respective levels of 13.7 and 10.2 per cent in December 2012.

Figure 1.4: Inflationary Trend (Year-on-Year)



1.2.3 Interest Rates

Rates generally trended upwards with the exception of the Inter-bank Call and the Open-Buy-Back (OBB) rates. The development was largely attributed to the continued monetary tightening stance of the CBN. During the review period, the Bank maintained its policy rate at 12.00 per cent. Consequently, the average term deposit rate rose to 6.64 per cent, from 6.58 per cent in the first half of 2013. Similarly, rates for other deposits with various maturities rose to a range of 1.71 - 7.92 per cent in the second half of 2013, from a range of 1.34 - 7.72 per cent in the first half of 2013.

However, the average Inter-bank Call and Open-Buy-Back (OBB) rates stood at 11.02 and 11.07 per cent in the second half of 2013, down from 11.69 and 11.27 per cent in the first half of 2013, respectively. The prime and maximum lending rates rose by 0.47 and 0.37 percentage points, respectively, to 17.09 and 24.93 per cent in the review period. Thus, the spread between the maximum lending and the average term deposit rates stood at 18.30 percentage points, a 0.32 percentage point over the level in the first half of 2013. With the inflation rate at 8.0 per cent in December 2013, all deposit rates were negative in real terms, while lending rates were positive in real terms. The negative real rate of return on deposits, which has been a disincentive to savings, remained a major challenge to capital accumulation and the ability of banks to build a sustainable long-term loanable funds base.

As part of efforts to improve the savings culture, the CBN continued to initiate and encourage banks to implement customer-friendly policies. Specifically, the recently revised *Guide to Bank Charges* specifies the minimum interest rate payable on savings accounts at 30 per cent of the ruling MPR.

1.2.4 Fiscal Operations

The Federal Government's retained revenue stood at ₦1,817.49 billion in the second half of 2013, against the proportionate budget estimate of ₦2,452.68 billion, while expenditure was

Figure 1.5: Money Market Interest Rates and MPR

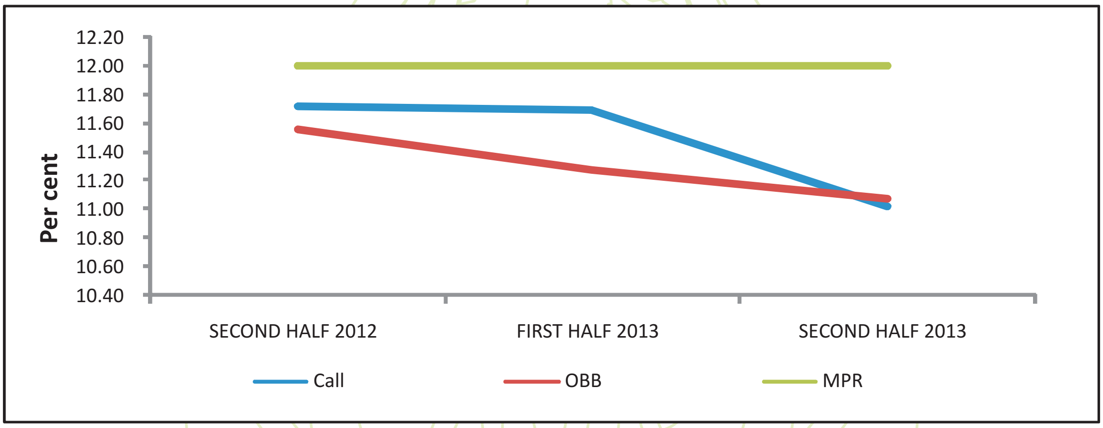
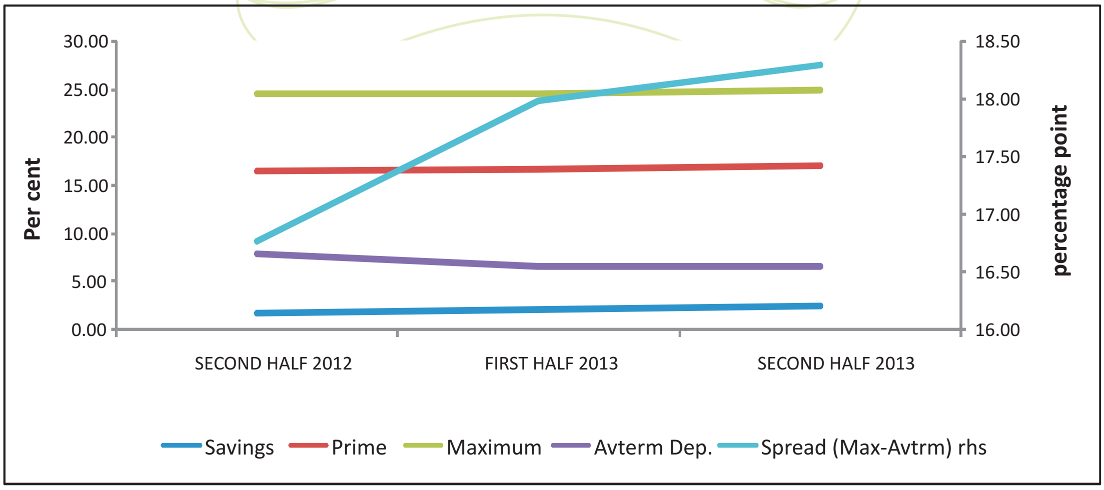
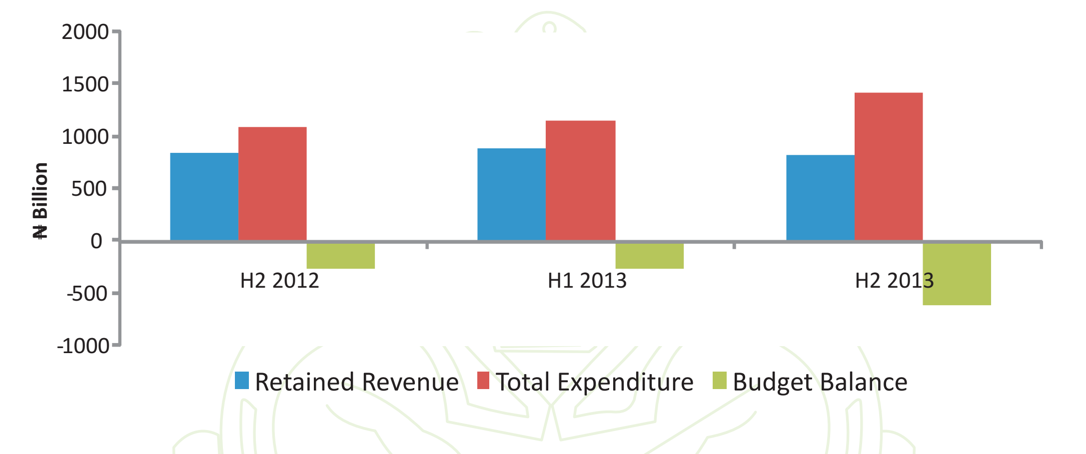


Figure 1.6: Lending and Deposit Rates



estimated at ₦2,561.77 billion, compared with ₦2,896.22 billion budgeted for the second half of 2013. Thus, the fiscal operations of Government resulted in a deficit of ₦744.28 billion or 6.3 per cent of GDP, as against the proportionate budget deficit of ₦443.53 billion for the first half of 2013 and ₦278.55 billion for the corresponding period of 2012. The deficit was financed through domestic borrowings and privatization proceeds.

Figure 1.7: Federal Government Fiscal Operations



2.0 DEVELOPMENTS IN THE FINANCIAL SYSTEM

2.0 DEVELOPMENTS IN THE FINANCIAL SYSTEM

2.1 Money and Credit[5]

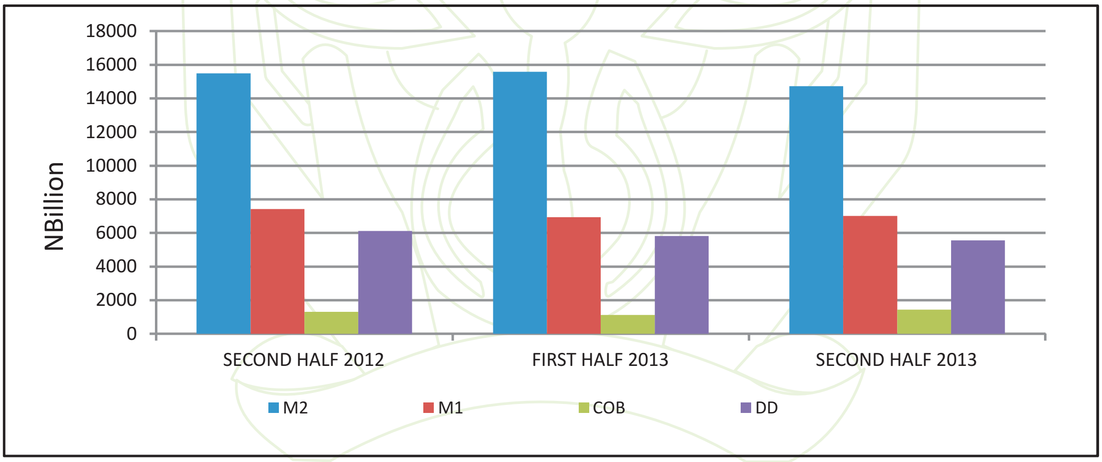
Growth in money supply remained sluggish at the end of the second half of 2013. Relative to the level at end-June 2013, broad money supply (M_2) grew by 0.5 per cent to ₦15,668.95 billion at the end of the second half of 2013. The increase in money supply relative to the position during the preceding half year reflected, largely, the respective 14.4 and 17.3 per cent rise in net domestic credit and other assets (net) which more than offset the 7.1 per cent decline in net foreign assets of the banking system. Over the level at end-December 2012, M_2 rose by1.2 per cent, due largely, to the 18.5 per cent increase in net domestic credit, which more than offset the respective 26.0 and 5.9 per cent decline in other assets (net) and foreign assets (net) of the banking system.

Narrow money supply (M_1) rose by 1.1 per cent at end-December 2013, in contrast to the 6.5 per cent decline at the end of the first half of 2013.The increase relative to the position in the preceding half year was attributed, largely, to the 28.3 per cent rise in currency outside banks (COB). As a ratio of total monetary assets, COB stood at 9.2 per cent, compared with the 7.2 per cent recorded at the end of the preceding half year.

2.1.1 Aggregate Credit to the Economy

Net domestic credit (NDC) to the economy grew by 7.3 per cent to ₦15,040.7 billion at end-December 2013, compared with ₦13,149.4 billion at end-June 2013. This reflected the 42.2, 17.3 and 5.2 per cent growth in claims on the Federal Government, and other assets (net) and claims on the private sector, respectively.

Figure 2 .1: Trend in Monetary Aggregate



[5]The analysis is based on the revised *CBN Monetary Survey.*

Figure 2.2: Credit to the Economy

2.1.1.1 Claims on the Federal Government

Net claims on the Federal Government rose by 42.2 per cent at end-December 2013, compared with the growth of 3.6 per cent at end-June 2013. The development reflected, mainly the increase in the banking system holdings of government securities. This increase in net claims on the Federal Government tended to "crowd out" private sector credit. However, the Federal Government remained a net lender in the system, a situation that mitigated the apparent "crowding out" effect.

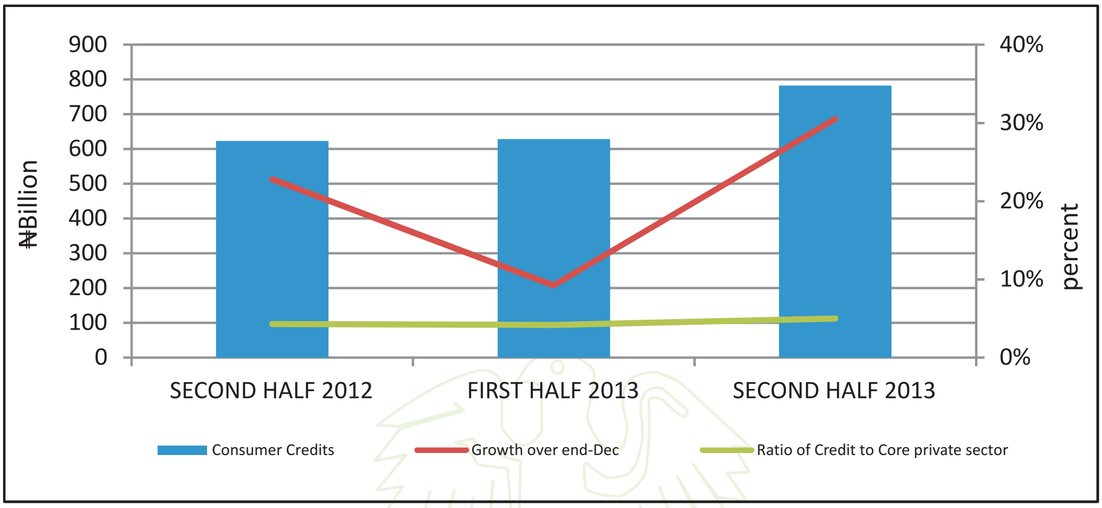
2.1.1.2 Claims on the Private Sector

Credit to the private sector increased by 5.2 per cent at end-December 2013, compared with the growth rate of 3.6 per cent at end-June 2013. The growth in private sector credit reflected, largely, the 4.5 per cent rise in claims on the core private sector. The contribution of the change in claims on the private sector to the total monetary assets stood at 5.2 per cent, compared with the 3.5 per cent recorded at the end of the first half of 2013.

2.1.1.3 Consumer Credit

Consumer credit grew by 24.5 per cent to ₦782.6 billion in the review period, compared with the marginal growth of 0.8 per cent in the first half of 2013. As a ratio of credit to the core private sector, consumer credit constituted 5.0 per cent, compared with 4.2 per cent at end-June 2013.

Figure 2.3: Consumer Credit



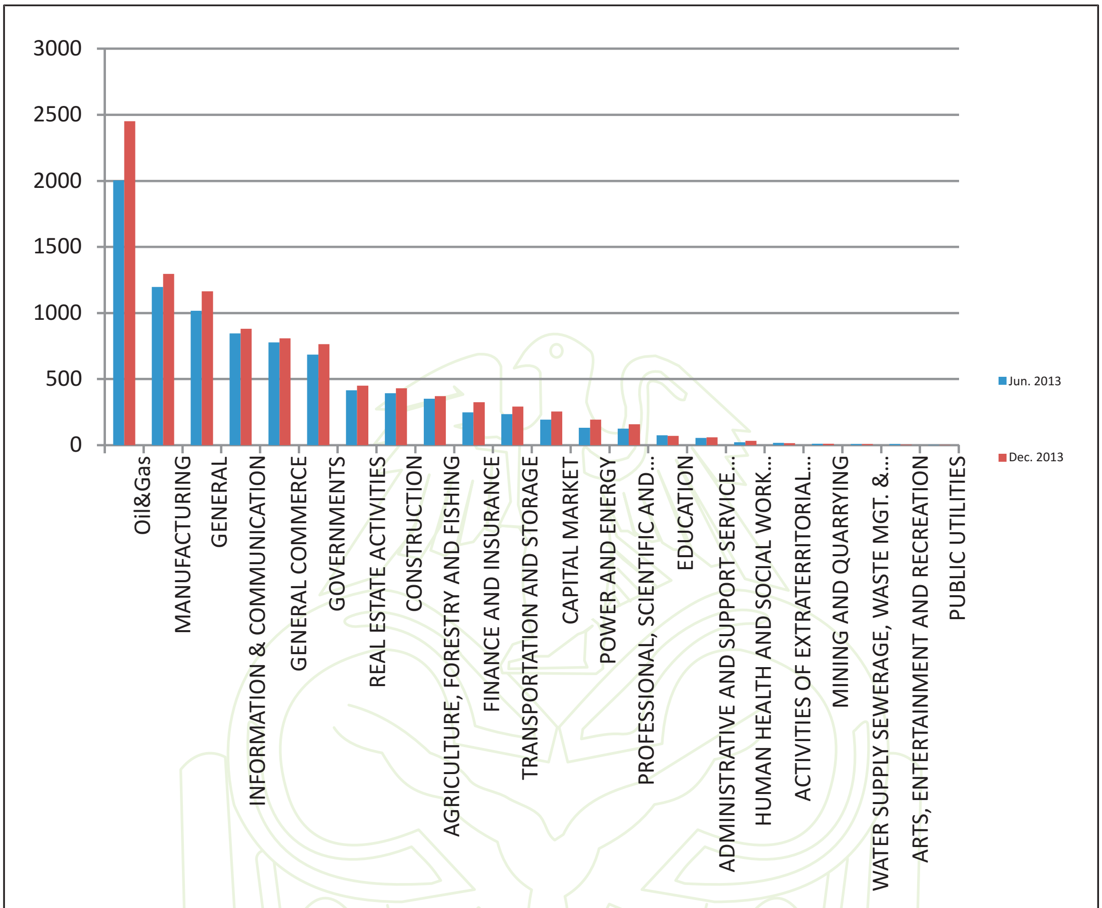
2.1.2 Sectoral Classification of Private Sector Credit

Total bank loans and advances to the various sectors of the economy grew by 13.9 per cent to ₦10,042.71 billion at end-December 2013. The oil and gas sector recorded the highest growth rate, with a share of 24.4 per cent, followed by manufacturing (12.9 per cent) and the general sector (11.6 per cent). The share of the agricultural sector declined to 3.7 per cent, from 4.0 per cent in the first half of 2013 (Table 2.1).

Table 2.1: Consumer Credit by Sector

	Jun. 2013		Dec. 2013	
Sector	₦'Billion	Per cent	₦'Billion	Per cent
Oil and Gas	2,002.26	22.72	2,450.48	24.40
Manufacturing	1,196.64	13.58	1,295.41	12.90
General	1,017.03	11.54	1,164.42	11.59
Information and Communication	845.86	9.60	881.22	8.77
General Commerce	777.45	8.80	807.51	8.04
Governments	684.48	7.77	764.91	7.62
Real Estate Activities	414.44	4.70	450.10	4.48
Construction	394.26	4.47	431.27	4.29
Agriculture, Forestry and Fishing	352.43	4.00	370.63	3.69
Finance and Insurance	247.70	2.80	324.21	3.23
Transportation and Storage	235.09	2.67	291.44	2.90
Capital Market	192.83	2.19	255.79	2.55
Power and Energy	131.11	1.49	193.98	1.93
Professional, Scientific and Technical Activities	125.90	1.43	159.13	1.58
Education	74.16	0.84	70.99	0.71
Administrative and Support Service Activities	54.55	0.62	58.67	0.58
Human Health and Social Work Activities	22.19	0.25	32.38	0.32
Activities of Extraterritorial Organizations and Bodies	18.07	0.21	14.66	0.15
Mining and Quarrying	10.59	0.12	11.35	0.11
Water Supply Sewerage, Waste Management and Remediation Activities	8.38	0.10	8.22	0.08
Arts, Entertainment and Recreation	8.05	0.09	3.98	0.04
Public Utilities	0.88	0.01	1.96	0.02
Total	8,814.36	100.00	10,042.71	100.00

Figure 2.4: Sectoral Allocation of Credit



2.1.3 Reserve Money

Reserve money (RM) increased at the end of the second half of 2013 and was higher than the indicative benchmark for 2013. It rose by 71.8 per cent to ₦5,558.9 billion at end-December 2013, in contrast to the decline of 12.6 per cent recorded at the end of the first half of 2013. This development reflected the 108.9 and 24.6 per cent increases in bank deposit with the Bank and currency-in-circulation, respectively. The corresponding rise in the sources of reserve money, relative to the first half of 2013, was attributed to increases in net domestic credit and other assets (net) of the Bank.

2.1.4 Maturity Structure of Bank Deposits and Credits

Short-term maturities remained dominant in the credit market in the second half of 2013. On the average, credits maturing within one year accounted for 52.6 per cent, compared with 57.1 per cent in the first half of 2013. The medium-term ($\geq$1yr and < 3yrs) and long-term (3yrs and above) maturities stood at 19.1 and 28.3 per cent in the review period, compared with 19.7 and 23.2 per cent, respectively, in the first half of 2013.

Similarly, deposits of below one-year maturity constituted 97.1 per cent of total deposits (out of which 76.7 per cent had maturity of less than 30 days), compared with 96.9 per cent at end-June 2013. The medium and long-term deposits constituted 2.8 and 0.003 per cent in the review period, compared with 3.1 and 0.05 per cent recorded in the first half of

2013, respectively. The continued dominance of short-term deposits constrained the ability of banks to lend long term loans and especially to the real sector which typically has a preference

Figure 2.5: Distribution of Bank Loans and Advances by Maturity

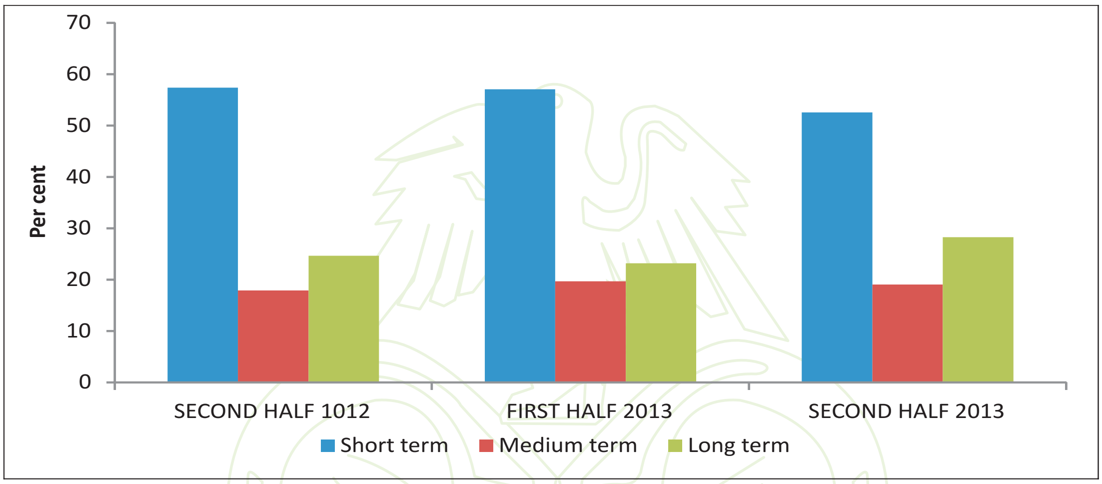
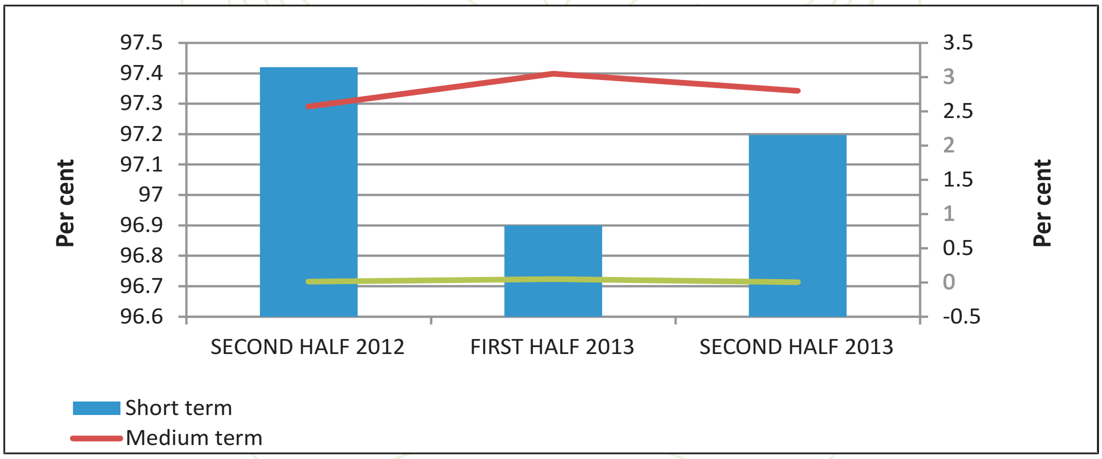


Figure 2.6: Distribution of Banks' Deposit Structure



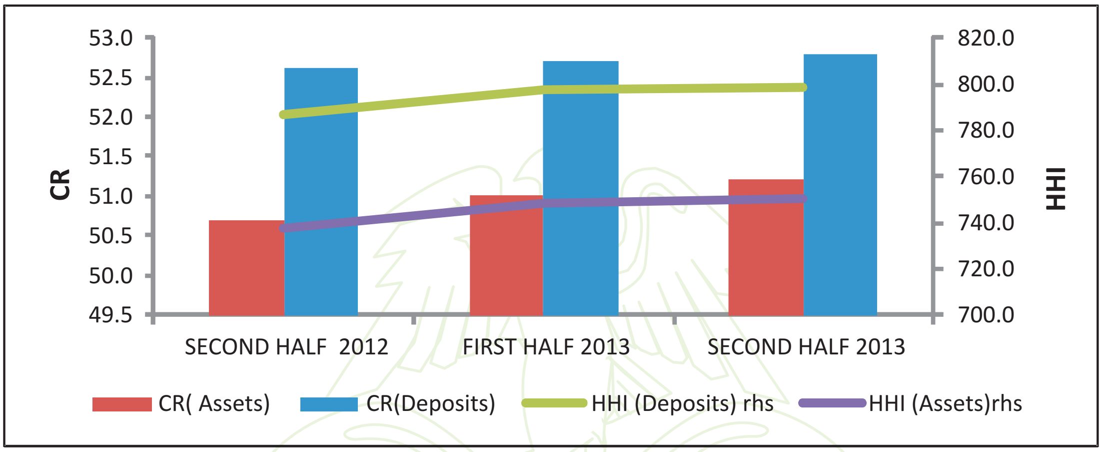
for longer loan maturities. Thus, the observed mismatch portends refinancing and re-pricing risks for the system.

2.1.5 Market Structure of the Banking Industry

The banking industry was dominated by a few banks as the average market share of assets and deposits of the six largest banks (concentration ratio–CR_6) stood at 50.68 and 52.23 per cent, respectively. During the review period, the market share of the largest bank, in terms of assets and deposits, stood at 13.71 and 15.14 per cent, respectively, compared with 13.57 and 15.17 per cent at end-June 2013. However, the banking industry remained competitive in both deposits and assets as revealed by the respective Herfindahl-Hirschman Index (HHI) of 798.08 and 750.16 for total deposits and assets, compared with 797.36 and 748.55, respectively, in the preceding period. (Figure 2.7)

Approval-in-Principle (AIP) was issued to a micro-finance bank (MFB) to establish a state-wide non-interest MFB

Figure 2.7: Market Concentration Ratios of Banks (Assets and Deposits)



2.2 Implementation of the 2010 Banking Model

The deadline for the implementation of the prescribed banking model introduced in October 2010 expired on June 30, 2013. At end-December 2013, most of the banks had complied with the *Regulation on the Scope of Banking Activities and Ancillary Matters* by divesting from their non-banking activities.

2.3 Non-Interest (Islamic) Banking

As part of efforts to promote non-interest banking (NIB) in Nigeria, the CBN intensified collaboration with international agencies, such as the Islamic Financial Services Board (IFSB) and the International Islamic Liquidity Management Corporation (IILM) in the review period.

As evidence of growing interest in NIB products and services in Nigeria, one bank was granted approval to operate a non-interest banking window, while an during the review period.

A new unit was created in the CBN to formulate policies on Islamic finance and serve as a secretariat for the Financial Regulation Advisory Council of Experts (FRACE).The roles and responsibilities of the Unit include the following:

- Develop policies on the Non-Interest Financial Institutions (NIFIs) under the purview of the CBN;
- Process requests for the establishment of NIFIs;
- Develop guidelines for the operations of NIFIs;
- Arrange and co-ordinate the meetings of FRACE;
- Receive requests and queries directed to the Council from NIFIs and other regulatory authorities; and
- Develop parameters for non-interest products and instruments issued by the NIFIs.

2.4 Cross-border Collaboration

Nigerian banks continued to expand their operations outside the country with the opening of seven subsidiaries across the African continent during the review period, bringing the total to 64 at end-December 2013 (Table 2.2). The increase in foreign subsidiaries was as a result of four acquisitions in West Africa and three in East Africa, while one bank divested from a subsidiary in West Africa.

Table 2.2: Distribution of Off-shore Subsidiaries of Nigerian Banks

Region	Subsidiaries		Representative Offices& Branches	
	Jan-Jun 2013	Jul-Dec 2013	Jan-Jun 2013	Jul-Dec 2013
West Africa	32	35	-	-
The Rest of Africa	17	20	4	4
Europe, N/ America & Asia	9	9	5	5
	58	64	9	9

The cross-border expansion of Nigerian banks has continued to be motivated by several factors which include profit maximization, risk diversification, the demand pull from corporate clients, and increasing business opportunities. However, the expansion exposes the Nigerian financial system to regional contagion risk.

The major thrust in managing the contagion risk is the timely exchange of information amongst home and host regulatory authorities. This is facilitated through the execution of MoUs, the activities of the College of Supervisors, and cross-border examination.

2.4.1 Memoranda of Understanding (MoUs)

At end-December 2013, 15 MoUs had been executed between the CBN and the host regulators. The MoUs facilitated information sharing, consolidated supervision and joint examinations across jurisdictions. In the review period, the CBN also initiated the process of signing an MoU with the Bank of Mauritius, while collaborative discussions on the MoUs with the Central Bank of Sudan and the Banque Central du Congo continued.

2.4.2 Colleges of Supervisors

During the review period, agreements were reached on the establishment of a College of Supervisors for the banking subsidiaries of Ecobank Transnational Incorporated (ETI) led by the Central Bank of West African States (BCEAO), and a College of Supervisors for the United Bank of Africa, led by the CBN.

2.4.3 Cross-border Examination

In order to ascertain the health of foreign subsidiaries of Nigerian banks, the CBN examined 14 of them in the review period. Of this number, eight (8) were jointly conducted with host supervisors, while six (6) were solely carried out by the CBN. Six (6) examination reports were issued during the period, which indicated that three (3) of the subsidiaries had a "Moderate" composite risk rating while three (3) other subsidiaries had a risk rating of "Above Average".

2.4.4 Nigerian Sustainable Banking Principles

The CBN and the entire banking industry have adopted the *Nigerian Sustainable Banking Principles*. This is to ensure that financial institutions get committed to economic growth that is environmentally responsible and socially relevant. The *Nigerian Sustainable Banking Principles* consist of the following nine overarching commitments:

- Managing environmental and social risks;
- Managing each bank's own environmental and social footprints;
- Safeguarding human rights;
- Promoting women's economic participation and empowerment;
- Promoting financial inclusion;
- Ensuring good governance, transparency and accountability;
- Supporting capacity building in the sector;
- Promoting collaborative partnership to accelerate sector progress; and
- Reporting to take stock of progress.

During the review period, the Bank issued guidelines on sustainable bank lending to the power, aviation as well as the oil and gas sectors. A reporting template was also developed to standardize reporting by financial institutions.

2.5 Other Financial Institutions (OFIs)

During the review period, significant developments were recorded in each of the five segments into which the sub-sector is divided by institution-type: Development Finance Institutions (DFIs), Primary Mortgage Banks (PMBs), Microfinance Banks (MFBs), Finance Companies (FCs), and Bureaux de Change (BDCs). In terms of total number of OFIs in operation, the figure rose to 3,858 at end-December 2013, representing an increase of 9.95 per cent over the 3,509 recorded at end-June 2013. The number comprised 6 Development Finance Institutions (DFIs), 82 Primary Mortgage Banks (PMBs), 820 Microfinance Banks (MFBs), 61 Finance Companies (FCs) and 2,889 Bureaux de Change (BDCs). The increase was accounted for by approvals to resume operations/licences granted to 456 operators (1 DFI, 4 MFBs and 451 BDCs) and the exit of 107 OFIs (83 MFBs, 4 FCs and 20 BDCs) during the review period. Total assets of the sub-sector similarly increased by 39.00 per cent to ₦1,565.65 billion at end-December 2013, from ₦1,126.40 billion at end-June 2013. Paid-up capital and net loans/advances also increased by 156.10 and 43.75 per cent to ₦532.31 billion and ₦673.95 billion, respectively, at end-December 2013. Total deposit liabilities followed the same pattern, increasing by 10.73 per cent to ₦457.56 billion at end-December 2013, from ₦413.22 billion at end-June 2013.

The specific developments analyzed under each segment/OFI-type were as follows:

2.5.1 Development Finance Institutions (DFIs)

At end-December 31, 2013, the number of DFIs under the supervisory purview of the CBN was six (6), compared with five (5) at end-June 2013. The increase resulted from the re-emergence, in October 2013, of the National Economic Reconstruction Fund (NERFUND).

Following the appointment of a new management team, the process of restructuring and recapitalizing the Fund, as well as the recovery of loans, commenced.

Provisional data showed that the total assets of the 6 DFIs increased by 31.26 per cent to ₦586.66 billion at end-December 2013, from ₦446.94 billion at end-June 2012.The increase in aggregate assets was due to the improved financial performance of the Bank of Industry (BOI), Bank of Agriculture (BOA), and The Infrastructure Bank (TIB), while the data showed that the financial performance of FMBN and NEXIM declined marginally during the review period. The paid-up capital and net loans/advances of the institutions increased by 227.44 and 57.86 per cent to ₦230.94 billion and ₦358.21 billion, respectively, as at December 31, 2013. Also, total deposit liabilities increased by 56.22 per cent to ₦171.81 billion at end-December 2013. A disaggregation of the total assets showed that BOA, FMBN, NEXIM, TIB, BOI and NERFUND accounted for 8.85, 24.03, 9.13, 5.22, 50.49 and 2.28 per cent, respectively, while their respective shares of the total loans and advances were 7.22, 31.59, 8.55, 3.93, 45.57 and 3.13 per cent.

In the area of corporate governance, the review period also witnessed the reconstitution of the Boards of Directors of BOA and NEXIM. Those of FMBN and the privatized TIB were already in place while BOI and NERFUND were still being governed by a Shareholders' and Interim Management Committees, respectively.

2.5.2 Primary Mortgage Banks

At the expiration of the December 31, 2013 deadline for operators of PMBs to increase their capital to the prescribed minimum of ₦2.5 billion (for state licence) and ₦5 billion (for national licence), 40 PMBs met the new capital requirement. Further analysis of the existing 82 PMBs indicated that: seven (7) emerged as National PMBs; 33 as State PMBs; four (4) were subsumed in merger and acquisition arrangements; 13 applied for conversion to OFI-types, with lower capital requirements; and 25 were unable to meet the re-capitalization deadline.

Analysis of PMBs' financial information showed that their total assets increased by 32.77 per cent to ₦484.01 billion at end-December 2013, from ₦364.54 billion at end-June 2013. Paid-up capital and shareholders' funds also increased by 117.97 and 88.33 per cent to ₦150.25 billion and ₦144.58 billion, respectively, at end-December 2013, from ₦68.93 billion and ₦76.77 billion respectively at end-June 2013. The growth was attributed to the effort of PMBs to comply with the new capital requirements under the mortgage/housing finance sector reforms. Similarly, loans/advances and deposits increased by 21.05 and 0.12 per cent to ₦157.40 billion and ₦164.69 billion, respectively, at end-December 2013, from ₦130.03 billion and ₦164.50 billion, respectively, at end-June 2013, respectively.

2.5.2.1 Mortgage Refinancing

The Nigeria Mortgage Re-finance Company Plc (NMRC) was incorporated in the second half of 2013 as a second-tier, mono-line institution to promote the availability and affordability of housing to Nigerians by providing liquidity in the mortgage market through financial institutions. The NMRC is expected to address the mismatch between the short-term tenor of deposit liabilities and the long-term nature of mortgage assets. This would be achieved by raising long-term funds from the capital market and other sources of debt capital to re-finance eligible mortgages originated by the financial institutions. To ensure a smooth take-off of the NMRC, the Federal Government of Nigeria secured a 40-year term loan of US$ 300 million from the World Bank, on International Development Association (IDA) terms. Of the total loan, US$250 million was for the NMRC, US$25 million for financing micro-housing", and US$25 million for a mortgage-guarantee programme to enable low income borrowers to access mortgage loans.

2.5.2.2 Guidelines on Mortgage Brokerage

Following the CBN's "No Objection" approval in 2012 for the registration of mortgage brokers in Nigeria, the Mortgage Banking Association of Nigeria (MBAN), in July 2013, released the guidelines for mortgage brokerage companies/operators in Nigeria. The guidelines created a new class of operators in the system - Licensed Professional Mortgage Brokers - who are authorized to solicit for borrowers; negotiate, find and place mortgages; as well as provide related advisory services - for a fee.

2.5.3 Microfinance Banks

The number of licensed microfinance banks (MFBs) fell to 820 at end-December 2013 from 899 at end-June 2013. The fall was due to the revocation of the licenses of 83 institutions that were confirmed to have either closed shop or ceased to carry on microfinance business, while four new MFBs were licensed. Of the existing 820 MFBs four (4) operated as National, 69 as State, and 753 as Unit MFBs. Available data indicated that the total assets of MFBs decreased by 2.88 per cent to ₦270.90 billion at end-December 2013, from ₦278.93 billion at end-June 2013. The paid-up share capital and net loans/advances also decreased by 2.54 and 8.92 per cent to ₦67.40 billion and ₦129.03 billion, respectively, at end-December 2013, from ₦69.16 billion and ₦141.67 billion, respectively, at end-June 2013. Similarly, aggregate reserves decreased to ₦5.56 billion at end-December 2013, compared with ₦5.76 billion at end-June 2013, reflecting a decline of 3.47 per cent. The decrease was attributed, largely, to the revocation of the licenses of 83 MFBs.

In 2013, the Microfinance Certification Programme (MCP), which was introduced to bridge the observed skills gap in the microfinance industry, concluded its second phase and with it, the withdrawal of the subsidy to it by the CBN and the NDIC. The subsidy, designed to nurture the fledgling programme, had entailed the payment of 60 per cent of the total cost of training. The CBN will, however, continue to co-ordinate the Programme and accredit the Microfinance Training Service Providers (MTSPs). During the first four years of the Programme, a total of 9,352 operators of microfinance banks were trained in the 12 runs organized for the two approved levels of training as against the set target of 6,000, representing a 156 per cent performance rate. Of the 9,352 trained MFB operators, 2,202 have been certified by the Chartered Institute of Bankers of Nigeria and are spread over 632 MFBs. The Programme was also extended to non-executive directors of MFBs and other stakeholders, with a total of 1,406 non-executive directors and 223 regulators having been trained in 2012 and 2013.

2.5.4 Finance Companies

The number of operating finance companies (FCs) fell to 61 at end-

December 2013, from 65 at end-June 2013. This was due to the voluntary liquidation of two (2) FCs and discontinuation of finance company business by two (2) others, while one (1) was sealed up and is being investigated by the Economic and Financial Crimes Commission. One (1) new FC was licensed in the period.

Total assets of FCs increased to ₦103.05 billion at end-December 2013, from ₦82.13 billion at end-June 2013, reflecting a growth of 25.47 per cent. Similarly, paid-up capital increased by 3.23 per cent to ₦14.69 billion at end-December 2013, from ₦14.23 billion at end-June 2013. Aggregate reserves rose to ₦3.59 billion at end-December 2013, from ₦0.07 billion at end-June 2013. Net loans/advances and borrowings also increased by 68.58 and 20.64 per cent to ₦46.68 billion and ₦59.22 billion, respectively, at end-December 2013, from ₦27.69 billion and ₦49.09 billion, respectively, at end-June 2013.

2.6 Financial Inclusion

As part of efforts to implement the national financial inclusion strategy, the geo-spatial mapping of financial services access points was launched in July 2013.The mapping exercise was aimed at providing consumer information by indicating the geographic distribution of financial access points across the country, including banks, other financial institutions, non-governmental organisations, ATMs, and Nigeria Postal Service offices.

The ₦220 billion Micro Small and Medium Enterprises Development Fund (MSMEDF) was launched on August 15, 2013 to provide wholesale funding to MFBs/MFIs, as well as enhance access to financial services by women. Towards this end, 60 per cent of the Fund was dedicated to enterprises promoted by women. The Financial Inclusion Secretariat was also established in the review period to co-ordinate the financial inclusion programmes in the country.

Following the adoption of the tiered-KYC and the need to mitigate the associated risk, CBN's *Anti Money Laundering/Combating the Financing of Terrorism Regulation 77 (1)-(8)* was amended to require financial institutions to:

- Allow third parties with acceptable means of identification, such as clergymen, village/clan heads and headmasters, to identify the financially excluded persons, for account opening purposes;
- Formulate policies on financially disadvantaged customers and prescribe the type of documents to be provided by third-party identifiers;
- Adopt a risk-based approach on the operation of this category of customers; and
- Enhance the monitoring of such accounts, customers and third party identifiers and render monthly returns to the CBN and the NFIU on their operations.

It is expected that full implementation of these measures will improve access to formal financial services.

2.6.1 Financial Literacy

The Bank commenced the implementation of its Financial Literacy Awareness/Enlightenment initiative, in line with its financial inclusion strategy, through public workshops, road shows, a secondary schools programme, and the engagement of the media.

The secondary schools programme was designed by the Bank to teach school children the rudiments of banking and the need to imbibe the culture of savings, budgeting and investment.

In addition, the Bank developed and circulated public enlightenment/educational materials on: *'How to Lodge Complaints'*, *'Consumer Bill of Rights'* and *'101 Ways to Save Money in Nigeria'*.

During the review period, the Financial Literacy Steering Committee (FLSC), comprising all heads of financial sector regulatory institutions, representatives of the Federal Ministries of Education, Finance, Information and Communication Technology, was inaugurated by the CBN Governor. The Committee was established to ensure implementation of the Financial Literacy Framework, through policy formulation and oversight of the implementation arm of the Committee.

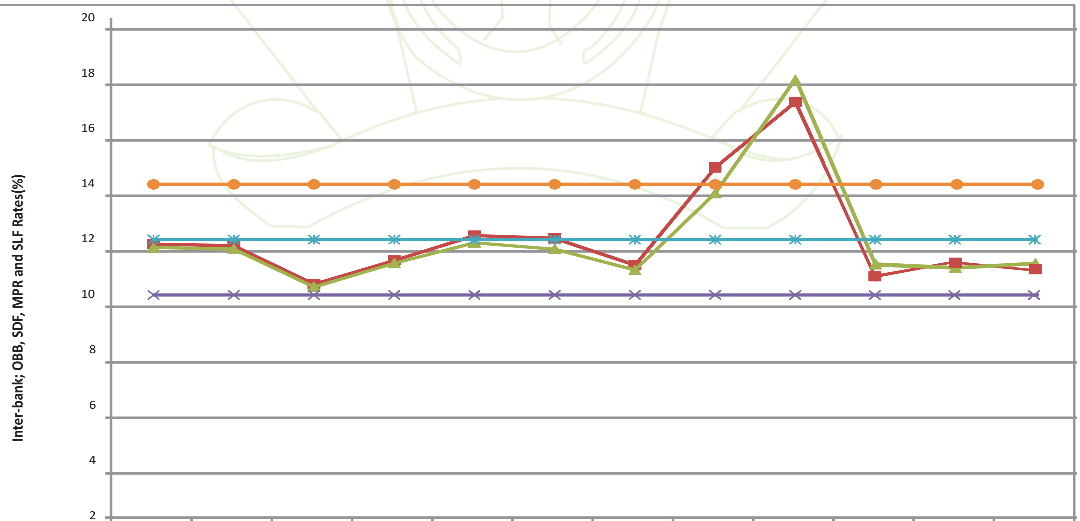
2.7 Financial Markets

2.7.1 The Money Market

The Bank maintained its tight monetary policy stance in 2013. Money market rates were relatively stable during the review period, due to the responsiveness of the Bank to developments in the market through effective liquidity management. Rates at the inter-bank funds market moved upward in August and September 2013, due to tight liquidity in the banking system. The movement followed the implementation of the increase in CRR on public sector deposits, as the DMBs had to borrow at a higher cost to rebalance their portfolio positions and comply with prudential requirements. Rates, however, moderated to their pre-August levels in the last quarter of the year, as overall liquidity in the banking system improved and inter-bank funds intermediation slowed down.

The weighted average monthly OBB and Inter-bank Call rates closed at 11.16 and 10.86 per cent, respectively, at end-December 2013, compared with 11.66

Figure 2.8: Inter-bank Rates Movements



	January	February	March	April	May	June	July	August	September	October	November	December
Inter-bank	11.84	11.78	10.39	11.25	12.15	12.05	11.08	14.61	16.98	10.65	11.22	10.86
OBB	11.72	11.66	10.29	11.15	11.89	11.66	10.90	13.68	17.82	11.12	10.99	11.16
SDF	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00
MPR	12.00	12.00	12.00	12.00	12.00	12.00	12.00	12.00	12.00	12.00	12.00	12.00
SLF	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00	14.00

and 12.05 per cent at end-June 2013.

The Scripless Securities Settlement System (S4) was deployed in December 2013 to provide a straight-through process for securities trading and settlement. The S4 is geared towards facilitating electronic management of securities by easing transfer and settlement of OBB transactions, thereby boosting activities in the segment. It is also aimed at facilitating delivery versus payment (DvP) settlements and reducing settlement risks, thus encouraging trading in Federal Government debt instruments.

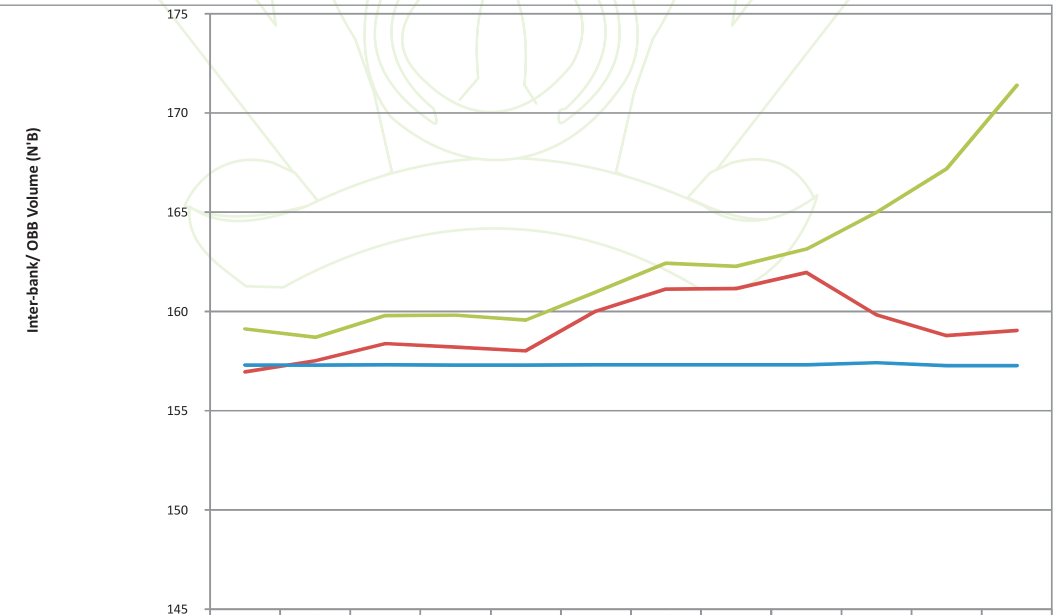
2.7.2 The Foreign Exchange Market

During the review period, the CBN introduced a number of policies to address inherent risks to exchange rate stability and check money laundering. These included: the re-introduction of the Retail Dutch Auction System (RDAS); the pegging of purchases from DMBs to US$250,000 by each BDC per week; restriction on importation of foreign currency, subject to CBN approval; payment of receipts of the proceeds of international money transfers in naira; and an increase in the amount spendable on naira debit and credit cards to US$150,000 from US$40,000 per annum.

The WDAS operated in the third quarter until October 2, 2013 when they were replaced by the RDAS in a bid to check the persistent demand pressures in the foreign exchange markets and curb the huge movement of cash without the required documentation and reporting to the monetary authorities. The re-introduction of the RDAS was aimed at monitoring the utilisation of funds in order to curtail round tripping and ensure exchange rate stability.

The average foreign exchange rate at the RDAS and Inter-bank segments appreciated by 0.02 and 0.60 per cent to ₦157.2742/$ and ₦159.0505/$,

Figure 2.9: WDAS, Inter-bank and BDC Rates, 2013



	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
W/DAS-SPT (incl. 1% comm.)	157.30	157.30	157.31	157.31	157.30	157.31	157.32	157.31	157.32	157.42	157.27	157.27
Inter-Bank	156.96	157.52	158.38	158.20	158.02	160.01	161.12	161.15	161.96	159.83	158.79	159.05
BDC	159.12	158.70	159.80	159.81	159.57	160.98	162.43	162.28	163.14	165.00	167.19	171.40

respectively, while the average rate at the BDC segment depreciated by 6.08 per cent to close at ₦171.4000/$ at end-December 2013.

2.7.3 The Capital Market

Transactions on the Nigerian Stock Exchange (NSE) were bullish during the review period as both the All Share Index (ASI) and Market Capitalization (MC) trended upwards. The development was attributed to improved corporate earnings by blue chip companies and increased portfolio investment. The implementation of the Transformation Agenda of the Federal Government, such as privatization of the power sector and the Subsidy Re-investment and Empowerment Programme (SURE-P) bolstered capital investment. Salient institutional developments were also contributory factors.

2.7.3.1 The Ten-Year Blueprint Committees

The Ten-Year Master Plan Committees, which the Securities and Exchange Commission (SEC) set up to articulate modalities for moving the market forward, presented their interim reports during the 3rd Annual Capital Market Committee Retreat in November 2013. The Committees are:

I. Capital Market Master Plan Committee;
ii. Capital Market Literacy Master Plan Committee; and
iii. Non-interest Capital Market Products Master Plan Committee.

The Committees were expected to submit their final reports by March 2014.

2.7.3.2 Minimum Capital Requirements for Capital Market Operators

In September 2013, the Board of the SEC approved a review of the minimum capital requirements for registered market operators as follows:

I.	Brokers/Dealers	₦300 million
ii.	Trustees	₦300 million
iii.	Brokers	₦200 million
iv.	Issuing Houses	₦200 million
v.	Underwriters	₦200 million
vi.	Registrars	₦150 million
vii.	Rating Agency	₦150 million
viii.	Fund/Portfolio Manager	₦150 million
ix.	Dealer	₦100 million
x.	Corporate Investment Adviser	₦5 million
xi.	Individual Investment Adviser	₦2 million

2.7.3.3 Financial Markets Dealers Quotations Over-the-Counter Plc

The Financial Markets Dealers Quotations Over the Counter (FMDQ-OTC) Plc was inaugurated on November 7, 2013 as a SEC-licensed OTC market securities exchange and self-regulatory organization with a focus on the money market and government securities. The functions of the FMDQ-OTC include market governance, compliance and development, as well as data services to ensure market integrity, liquidity, transparency and reliability. It has also improved quoting on the Nigeria Inter Bank Offered Rate; the Nigeria Inter-Bank Foreign Exchange Fixing; and yields on NTBs, FGN bonds, sub-national and corporate bonds. The FMDQ-OTC publishes these rates on its electronic platform daily.

2.7.3.4 The Bond Market

Total bonds outstanding at end-December 2013 stood at ₦5,038.04 billion, of which FGN, sub-national and corporate bonds constituted ₦4,222.03 billion (83.80%), ₦597.50 billion (11.86%) and ₦218.51 billion (4.34%), respectively. This level reflected an increase over end-June 2013 figures of ₦4,745.90 billion, comprising FGN, sub -national and corporate bonds valued ₦4,032.90 billion (84.98%), ₦498.00 billion (10.49%) and ₦215.00 billion (4.53%), respectively.

FGN Bonds

Demand for FGN Bonds at the secondary market increased as evidenced by the decline in yields, compared with the position at end-June 2013.This was attributed to the high level of liquidity in the banking system and the establishment of the Financial Markets Dealers Quotations Over-the-Counter Plc. (FMDQ-OTC Plc) platform. The FMDQ-OTC Plc platform standardized OTC transactions.

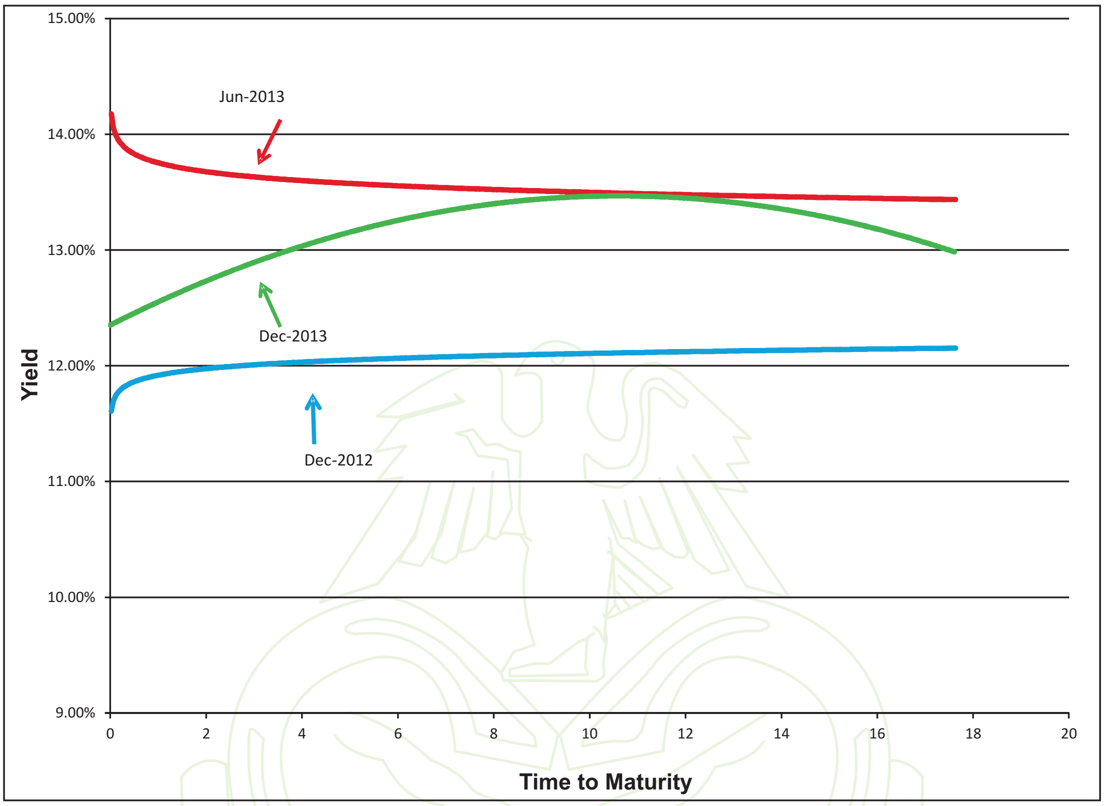
Five (5) bonds matured and were redeemed by the Federal Government during the review period. These were the 3.75%+NTB Rate FGN September 2013, the 12.74% FGN October 2013, the 10.98% FGN November 2013, the 11.99% FGN December 2013 and the 10.50% FGN November 2013 (Table 2.3).

With headline inflation at single digit, FGN bonds remained attractive to investors. The yield curve reflected investors' expectations of future monetary policy tightening. Therefore, they demanded higher compensation on the long-dated assets. Another reason was that investors were swapping long- for short-term assets, thus pushing down long-term asset prices and raising their yield.

Table 2.3: Matured FGN Bonds, July - Dec 2013

NEW NOMENCLATURE	INTEREST. RATE	ISSUE DATE	ISSUE AMOUNT (₦)	REDEMPTION DATE	INTEREST PAY DATES
3.75%+NTB RATE FGN SEP 2013	3.75% + NTB RATE	27-10-2003	599,454,000	30-09-2013	31 MAR & 30 SEP.
12.74% FGN OCT 2013	12.74%	27/10/2006	10,000,000,000	27/10/2013	27 APR & 27 OCT
10.98% FGN NOV 2013	10.98%	24/11/2006	10,000,000,000	24/11/2013	24 MAY & 24 NOV
11.99% FGN DEC 2013	11.99%	22/12/2006	10,000,000,000	22/12/2013	22 JUN & 22 DEC.
10.50% FGN NOV 2013	10.50%	28/11/2008	200,000,000,000	28/11/2013	28 MAY & 28 NOV.

Figure 2.10: Yield Curves for Nigeria



Source: Financial Markets Dealers Quotations

Sub-National Bonds

Two state governments issued bonds valued ₦99.50 billion, compared with three state governments that issued bonds

Table 2.4: New Sub-national Bonds Issued During the Review Period

State Government	Bond Features	Value (₦ Billion)	Issue Date
Niger	14% Fixed Rate 5-Year Amortiz ing Bond (Tranche 1)	12.0	Nov-13
Lagos	13.50% Fixed Rate 7-Year Bullet Payment Bond (Tranche 4)	87.5	Nov-13
Total		**99.5**	

valued ₦130.00 billion in the first half of 2013. Total outstanding bonds held by 14 state governments stood at ₦597.50 billion.

Corporate Bonds

Three corporate bonds were issued, valued ₦10.60 billion, compared with ₦12.94 billion in the first half of 2013.

Table 2.5: New Corporate Bonds Issued in the Second Half of 2013

Company	Description	Value (₦billion)	Issue Date
Lacasera Company Plc	15.75% Fixed Rate 5 -Year Amortising Bond	3.0	Oct-13
FSDH SPV Plc	14.25% Fixed Rate 3 -Year Amortising Bond	5.5	Oct-13
NAHCO	15.25% Fixed Rate 7 -Year Bullet Payment Bond	2.1	Dec-13
Total		**10.6**	

2.7.3.5 The Equities Market

In the review period, several initiatives were taken to enhance the performance of the equities market. Specifically, the NSE:

- Launched the electronic issuers portal, called X-Issuer, to enhance efficiency, compliance and integrity in the market;
- Partnered with Standard & Poor's, Dow Jones, and Morgan Stanley Capital International for the generation of key market data;
- Migrated to a new trading platform (X-Gen); and
- Established an OTC market platform in un-listed equities by the National Association of Securities Dealers to standardize operations and promote liquidity, efficiency and reliability in the market.

These initiatives resulted in increased trading activities on the floor of the NSE and led to a significant rise in market indices, as the ASI and MC attained new heights since May 2008. The NSE ASI closed at 39,858.23 at end-December 2013, from 36,164.31 at end-June 2013.

During the review period, foreign investors invested ₦203.60 billion in the equities market while total sales amounted to ₦255.80 billion, compared with ₦327.66 billion and ₦254.98 billion invested and sold by foreign investors, respectively, in the first half of 2013. The development reflected a decline in foreign portfolio investments in the review period. As a result of risks posed to the stability of the market by the continued decline in foreign portfolio investment, the Bank will continue to monitor movements in portfolio funds to ensure system stability.

2.8 Real Sector Intervention

2.8.1 The Nigerian Incentive-based Risk Sharing System for Agricultural Lending (NIRSAL) Plc.

During the review period, NIRSAL Plc accomplished the following:

- Issued four (4) Credit Risk Guarantees (CRGs) valued ₦3.051 billion to four (4) counterparties, compared with 22 CRGs valued ₦6.653 billion issued in the first half of 2013;
- Paid the sum of ₦67.52 million to 18 customers from eleven (11)

counterparties as interest drawback;

- Guaranteed ₦8.891 billion accessed by 59 agro-dealers and paid ₦7.781 million as interest drawback to two (2) borrowers under the Growth Enhancement Scheme of the Federal Ministry of Agriculture and Rural Development;
- Trained 15,000 cocoa farmers, in collaboration with GIZ/Farmers Business School; and
- Guaranteed ₦164.0 million to West African Cotton Company Ltd's contract farmers.

Table 2.6: Activities of NIRSAL, July - Dec 2013

S/N	Focus Area	Number of Projects	Amount (₦)	(%)
1	Poultry Production	2	1,050,683,592	34.44
2	Oil Palm Processing	1	1,000,000,000	32.78
3	Cotton Production	1	1,000,000,000	32.78
	Total	**4**	**3,050,683,592**	**100**

2.8.2 The Commercial Agriculture Credit Scheme

The Bank continued to finance large projects in the agricultural value chain through the Commercial Agriculture Credit Scheme (CACS) established in 2009. In the review period, ₦9.90 billion was disbursed to sixteen (16) projects through nine (9) banks in the second half of 2013, compared with ₦16.26 billion disbursed to 19 projects in the first half of 2013. This reflected decreases of 15.79 and 39.12 per cent, respectively, in number and value. Analysis of the value of funds disbursed also showed that marketing, storage, production and processing, accounted for 38.0, 24.0, 24.0 and 14.0 per cent, respectively, of the total funds disbursed. The recoveries from the projects for January to June 2013 stood at ₦6.68 billion, while the figure for July – December stood at ₦6.92 billion.

2.8.3 The Agricultural Credit Guarantee Scheme

A total of 33,667 loans ,valued ₦5.84 billion granted by five (5) commercial and 50 microfinance banks were guaranteed in the review period. When compared with 22,610 loans valued ₦3.59 billion guaranteed in the first half of 2013, the performance in the second half of 2013 reflected increases of 48.9 and 62.6 per cent in number and value of loans, respectively.

The increases in the second half of 2013 were attributed to a number of factors, among which are the:

- Intensity of farming activities in the northern part of the country that peaked with the rains in the second half of the year;
- Increase in the number of participating microfinance banks; and
- Prompt processing and payment of interest drawback claims .

2.8.4 The Small and Medium Enterprises Credit Guarantee Scheme

The Scheme, established to fast track the development of the Nigerian economy by guaranteeing bank credits to small and medium enterprises (SMEs), continued to play a critical role in facilitating funding for start-ups. The number of facilities guaranteed increased by 112.5 per cent to 17 ,valued ₦896.78 million ,in the second half of 2013 ,from 8 facilities valued ₦279.22 million that were guaranteed in the first half of 2013.

2.8.5 The Power and Aviation Intervention Fund

The Fund, established to stimulate and sustain investment in the power and aviation sectors of the economy through the provision of long-term credits suitable for infrastructure projects, contributed to enhancing the quality of credits in the banking industry. Other impacts of the Fund included:

- Improvement in the liquidity of banks and the balance sheet positions of the beneficiaries;
- Reduction of the cost of doing business;
- Resuscitation of some non-performing projects; and
- Increase in capacity utilization of benefiting projects.

During the review period, ₦11.628 billion was disbursed to five (5) power projects, compared with ₦39.61 billion disbursed to the same number of projects in the first half of 2013. The power projects financed through the scheme had a combined generating capacity of 847.4MW of power, out of which 440.1MW was utilized by the companies to guarantee stable and reliable power for their manufacturing processes. The power generated increased by 30.85 per cent over the level of 647.6MW generated in 2012.

2.8.6 The SME Restructuring and Refinancing Fund

The Fund was established to fast-track the development of the manufacturing sector of the Nigerian economy by facilitating access to credit by manufacturers, improve the financial position of DMBs, generate employment and increase foreign exchange earnings, among others.

Some of the repayments were ploughed back to finance new SMEs, resulting in the disbursement of ₦28.98 billion to fund thirty two (32) projects. Consequently, direct employment created by the benefiting SMEs increased by 22.3 per cent, and turnover increased by 24.9 per cent during the review period.

2.8.7 Entrepreneurship Development Centres

During the review period, a total of 2,806 participants were trained by the new entrepreneurship development centres located in North-East (Maiduguri), North-Central (Makurdi) and South-South (Calabar). A total of 1,018 start-up businesses were thereby created, while 317 graduates, representing 11.3 per cent of the total trained participants accessed loans valued ₦22.4 million to start or expand their businesses.

The process of transferring ownership of the first phase EDCs located in Kano (North-West), Lagos (South-West) and Onitsha (South-East) to the host states had commenced, in line with the policy establishing the Scheme.

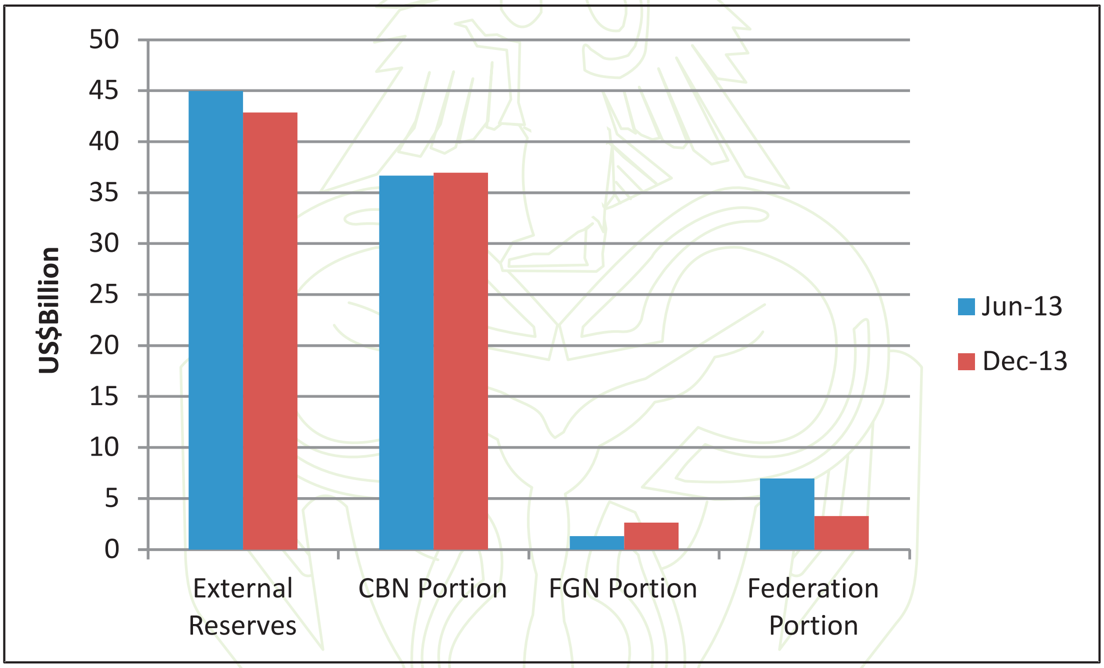
2.9 The External Sector

The level of gross external reserves decreased to US$42.85 billion at end-

December 2013, from US$44.96 billion at end-June 2013, representing a decline of US$2.11 billion or 4.69 per cent. The decrease in reserves, when compared with the level at the end of first half 2013, reflected an increase in demand and sale to authorized dealers.

A breakdown of the external reserves

Figure 2.11: Breakdown of External Reserves



indicated that the CBN, the FGN and the Federation holdings were US$36.94 billion, US$2.62 billion and US$3.29 billion, respectively, at end-December 2013, compared with US$36.68 billion, US$1.30 billion and US$6.98billion, respectively at end-June 2013. Further analysis showed that 83.88 per cent of the reserves was held in US Dollars, 5.90 per cent in Euro, 2.09 per cent in Renminbi, 2.08 per cent in Pound Sterling, and 6.02 per cent in SDR at end-December 2013.

Total foreign exchange inflow during the second half of 2013 was US$21.32 billion, compared with US$19.75 billion recorded in the first half of 2013, reflecting an increase of US$1.57 billion or 7.95 per cent. The increase in gross inflows in the review period reflected, largely, the increase in other government revenues, reinforced by the rise in non-oil export proceeds and interest on reserves and investments. The sum of US$0.24 billion was recorded as unrealized exchange rate gain at end-December 2013.

Similarly, total outflow rose to US$23.46 billion in the review period, from US$18.86 billion in the first half of 2013, reflecting an increase of US$4.60 billion or 24.39 per cent. Foreign exchange flows in the review period resulted in a net outflow of US$2.14 billion.

At end-December 2013, the country's external reserves could finance about10 months of imports. This was lower than the 11.96 months at end-June 2013, but higher than the minimum international benchmark of 3 months.

In order to manage the decreasing trend in reserves, a number of measures were taken, including the following:

- The increase in CRR for public sector deposits in order to reduce banks' capacity to fund speculative activities in the foreign exchange market;
- The re-introduction of RDAS in place of WDAS to reduce speculation; and
- Reconciliation of critical inflows into the reserve accounts to ensure that all receivables are tracked.

In addition, the Federal Government continued to encourage the development of local industries that would reduce over-reliance on imports and thus conserve foreign exchange.

2.10 The Insurance Sector

In order to promote micro-insurance, the National Insurance Commission issued guidelines on micro-insurance operations in Nigeria in December 2013 and inaugurated the Micro-Insurance Steering Committee.

During the period under review, four insurance companies merged to form a single entity. This is expected to enable the consolidated company benefit from economies of scale and thereby engage in big ticket transactions.

In pursuance of the *National Roadmap for the Adoption of IFRS*, 43 of the 50 operating insurance companies published IFRS-compliant accounts.

NAICOM facilitated the settlement of 61 disputes on claims between insurance companies and customers, with the settlement claims valued ₦2.24 billion for 2013.

The *Takaful (Shari'a Insurance) Operational Guidelines* was formally launched in November 2013 at the Takaful Stakeholder Engagement Workshop, held in Lagos.

2.10.1 Airtel Nigeria Life Insurance

In July 2013, FBN Life Assurance, in partnership with Airtel Nigeria, introduced a micro insurance scheme, 'Padi4Life'. The scheme is aimed at providing low-income earners living in remote locations a daily insurance cover for permanent disability or death. For a daily premium of ₦20, the subscriber would be entitled to a ₦500,000 insurance cover.

2.10.2 MTN Nigeria Life Assurance Service

In October 2013, MTN Nigeria introduced airtime-based insurance service, in collaboration with Mansard Insurance Plc. This service would enable subscribers on the platform to have access to affordable life protection plan directly from their mobile phones. For a ₦15 daily premium, the subscriber would receive a ₦350,000 insurance cover.

The first claim on the MTN Yello Cover was made in December 2013. The settlement came barely two months after the launch of the service.

Overall, the introduction of the new products would increase the patronage of insurance by people in the lower segment of the market to purchase life insurance at low cost, via the use of mobile phone technology.

It is envisaged that there would be increased consolidation of activities among the 50 existing insurance companies as the pressure of competition forces them into mergers. Furthermore, the sustained enforcement of compulsory insurances schemes, particularly Group Life and motor, is expected to increase premium income for insurance companies and thereby enhance their viability.

3.0 REGULATORY AND SUPERVISORY ACTIVITIES

3.0 REGULATORY AND SUPERVISORY ACTIVITIES

3.1 Macro-Prudential Supervision

3.1.1 Financial Soundness Indicators

3.1.1.1 Asset and Liquidity-based Indicators

The quality of assets of the banking industry improved slightly in the second half of 2013, compared with the first half. The ratio of non-performing loans (NPLs) to total loans dropped by 0.5 percentage point to 3.2 per cent at end-December 2013, from 3.7 per cent at end-June 2013 (Figure 3.1). The improvement in asset quality was attributed to stricter adherence to credit risk management policies and standards by banks. The ratio of core liquid assets to total assets increased by 1.2 percentage points to 22.2 per cent at end-December 2013, from 21.0 per cent at end-June 2013. Similarly, the ratio of liquid assets to short-term liabilities improved by 0.9 percentage point to 25.2 per cent at end-June 2013 (Figure 3.2).

Figure 3.1: Banking Industry NPLs to Total Gross Loans

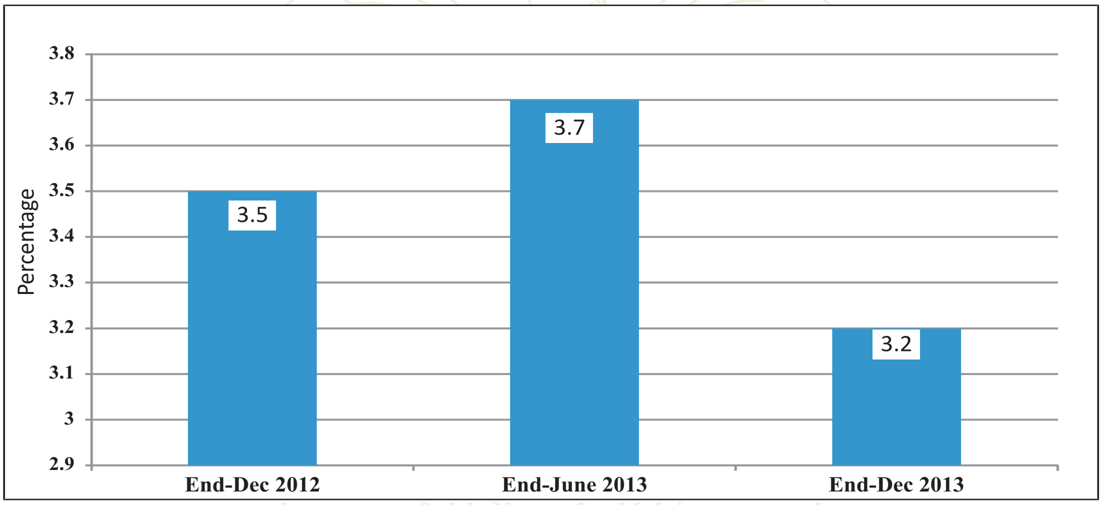
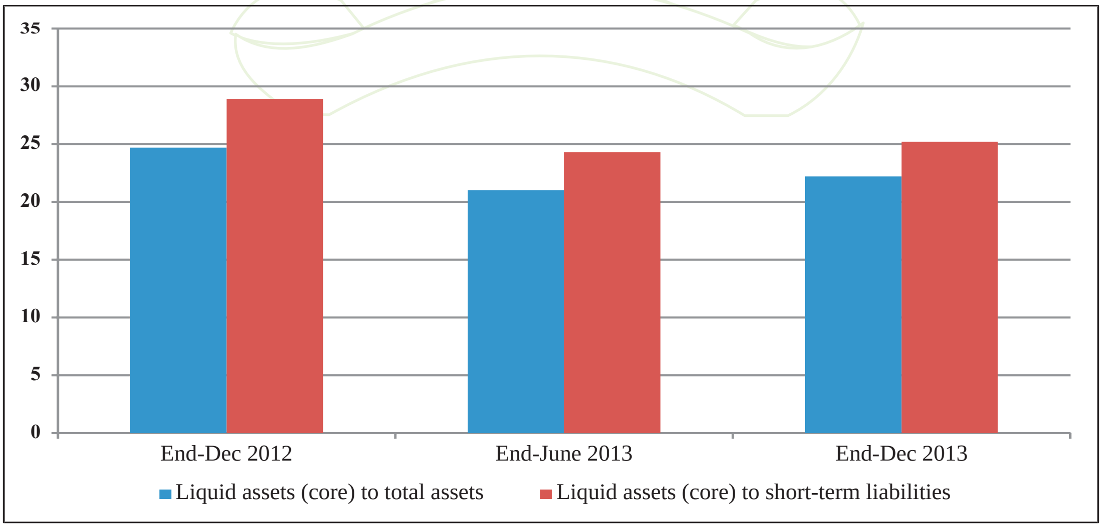


Figure 3.2: Banking Industry Liquidity Indicators



3.1.1.2 Capital-based Indicators

The average ratio of regulatory capital to risk weighted assets stood at 17.2 per cent at end-December 2013, showing a decrease of 1.7 and 1.1 percentage points, respectively, below the levels at end-June 2013 and end-December 2012. Similarly, the ratio of Tier 1 capital to risk weighted assets of 17.1 per cent at end-December 2013 was 1.4 and 0.9 percentage points below the levels at end-June 2013 and end-December 2012, respectively (Figure 3.3).The industry ratio of non-performing loans (net of provisions) to capital remained stable at 7.4 per cent at end-December 2013. On the whole, the above scenario reflected a strong capital base for Nigerian banks (Table 3.1).

3.1.1.3 Income and Expense-based Indicators

The ratio of interest margin to gross income increased to 64.9 per cent in the review period, from 63.9 per cent at end-June 2013. The ratio of non-interest expenses to gross income rose by 5.9 percentage points to 68.9 per cent at end-December 2013. Conversely, the ratio of personnel expenses to non-interest expenses fell by 3.2 percentage points to 36.5 per cent, from 39.7 per cent at end-June 2013 (Table 3.1).

Figure 3.3: Banking Industry Capital Adequacy Indicators

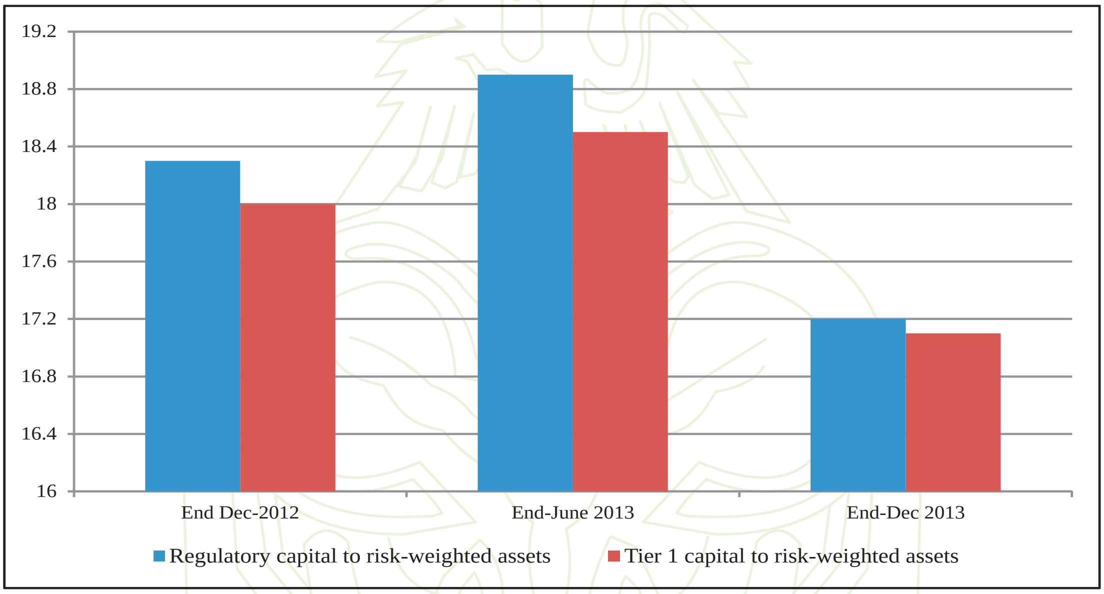


Table 3.1: Selected Financial Soundness Indicators of the Nigerian Banking Industry

	2009		2010		2011		2012		2013	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
	End June	*End Dec*	*End June*	*End Dec*	*End June*	*End Dec*	*End June*	*End Dec*	*End June*	*End Dec*
1. Asset-based Indicators										
NPL to total gross loans	8.5	27.6	28.8	15.7	10.8	5.3	4.3	3.5	3.7	3.2
Liquid assets (core) to total assets	15.6	16.5	17.2	17.2	22.6	25.7	23.5	24.7	21.0	22.2
Liquid assets (core) to short-term liabilities	21.5	22.3	19.4	19.8	25.7	31.3	28.1	28.9	24.3	25.2
Return on Assets (ROA)	1.7	-8.9	1.0	3.9	0.9	0.1	1.5	1.2	1.4	0.8

2. Capital-based Indicators										
Regulatory capital to risk-weighted assets	22.4	4.1	1.5	1.8	4.2	17.9	17.7	18.3	18.9	17.2
Tier 1 capital to risk-weighted assets	21.9	4.9	2.4	2.2	4.5	18.1	17.8	18.0	18.5	17.1
NPLs net of provision to capital	12.5	106.8	289.8	192.7	74.3	10.1	6.8	6.1	7.4	7.4
Return on equity (ROE)	8.9	-222.8	50.2	265.2	29.4	0.5	13.1	11.2	12.4	7.7
3. Income and Expense-based Indicators										
Interest margin to gross income	60.1	57.8	54.0	53.7	50.8	45.2	64.6	64.3	63.9	64.9
Non-interest expenses to gross income	64.5	81.2	80.5	66.9	72.9	75.4	64.8	64.9	63.0	68.9
Personnel expenses to gross income	46.7	47.6	45.5	42.8	44.6	36.1	43.6	43.9	39.7	36.5

3.1.2 Banking Industry Stress Tests

3.1.2.1 Liquidity Stress Test

The liquidity stress test was conducted at end-December 2013 to assess the resilience of the banking industry to liquidity and funding shocks, using the Implied Cash Flow Analysis (ICFA) and Maturity Mismatch/Rollover Risk approaches.

The ICFA test assessed the ability of the banking system to withstand unanticipated substantial withdrawal of deposits, as well as short-term wholesale and long-term funding over 5-day and cumulative 30-day shocks, with specific assumptions on fire sale of assets.

The test assumed a gradual average outflow of 3.8, 5.0 and 1.5 per cent of total deposits, short-term and long-term funding, respectively, over a 5-day (Test 1.1) and a cumulative average outflow of 22.0, 11.0 and 1.5 per cent of total deposits, short-term and long-term funding, respectively, on a 30-day balance (Test 1.2). The test further assumed that a percentage of the assets would remain unencumbered on a fire sale (Table 3.2).

Table 3.2: Assets Un-encumbered

Item No	Assets	% Unencumbered
1	Cash and cash equivalent	100
2	Current account with CBN	100
3	CRR	30
4	Government Bonds & Treasury Bills and other assets with 0% risk weighting exposure	66.5
5	Other Short - term investments	49
6	Certificates of deposits held	66.5

The Maturity Mismatch/Rollover Risk approach assessed funding maturity mismatch and rollover risk for assets and liabilities in the 0-30 and 31-90 day buckets, with the assumption on the availability of funding from CBN and intra-group sources as described below:

i. Test 2a: *Descriptive Maturity Mismatch* assumed that the baseline mismatch remained, but 5 per cent of total deposits would be made available from the CBN and intra-group funding;

ii. Test 2b: *Static Rollover Risk* assumed that 80.0 and 72.0 percent of the funding in the 0-30 and 31-90 day buckets would be rolled over with no possibility to close the funding gap from other buckets. However, it is assumed that 5 per cent of total deposits would be available from the CBN and intra-group funding; and

iii. Test 2c: *Dynamic Rollover Risk*: the assumption was as in 2b above, but with the option of closing the liquidity gap from other buckets.

Analysis of Test Results

The test revealed that, after the 5-day and cumulative 30-day shocks were applied, the industry liquidity ratio (LR) declined to 12.2 and 10.4 per cent, respectively, from 50.53 per cent (Table 3.3). Most banks' LRs were also below the 30.0 per cent threshold after the two scenarios. Furthermore, three (3) banks recorded a negative LR, following a cumulative 30-day shock. Two of these banks were among the categorised "large banks"[6].

Table 3.3: Implied Cash Flow Analysis

Total Number of Banks tested	**Number of Banks with < 30% liquidity ratio**				**Dec 2013**	
23	Dec 2013 (23 DMBs)	Sept 2013 (23 DMBs)	June 2013 (23 DMBs)	Mar 2013 (20 DMBs)	System LR	Liquidity Shortfall to make 30% LR (₦'billion)
Test 1.1: Implied Cash Flow Test (5 Days)						
Day 1	7	12	9	4	34.1%	NIL
Day 2	10	13	11	9	29.4%	168.78
Day 3	14	17	12	11	24.2%	716.94
Day 4	16	17	14	14	18.5%	1,240.33
Day 5	17	17	16	15	12.2%	1,740.82
Test 1.2: Implied Cash Flow Test (30 Days)	17	18	18	17	10.4%	1,873.30

[6] Banks with assets over N1 trillion

Figure 3.4: Industry and Individual Bank Pre-Shock Liquidity Ratio Positions

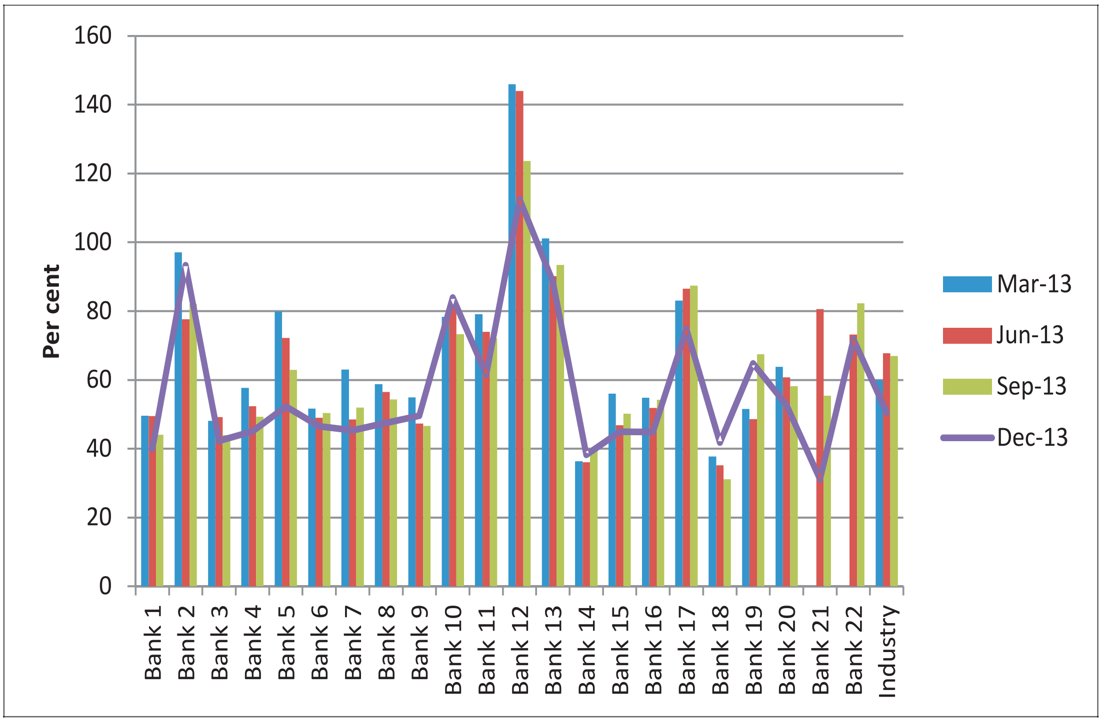


Figure 3.5: Industry Position after 1-5 day and Cumulative 30- day Shocks

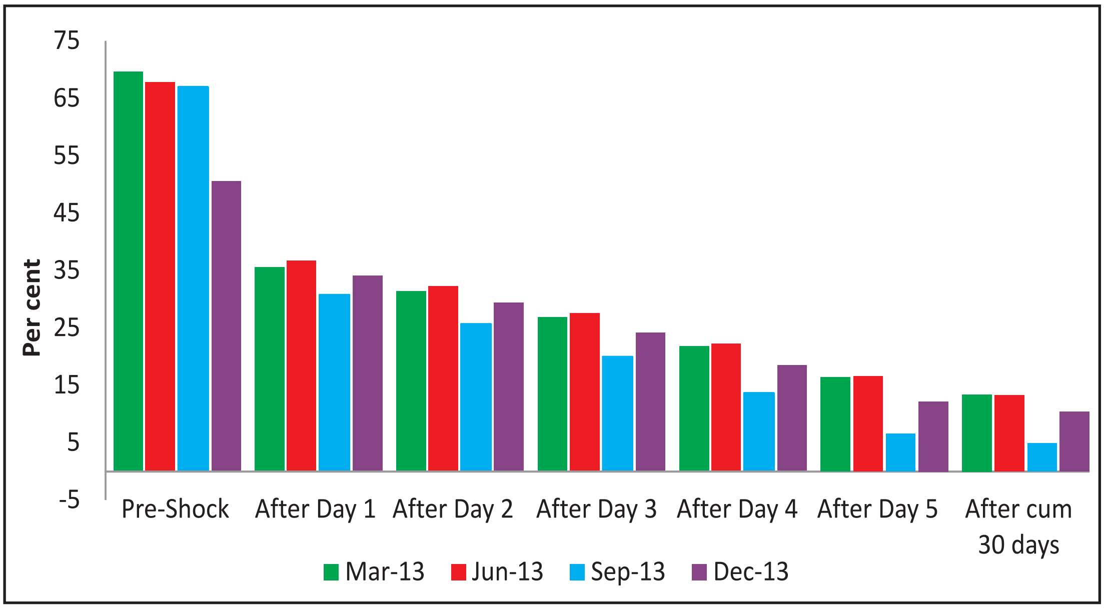
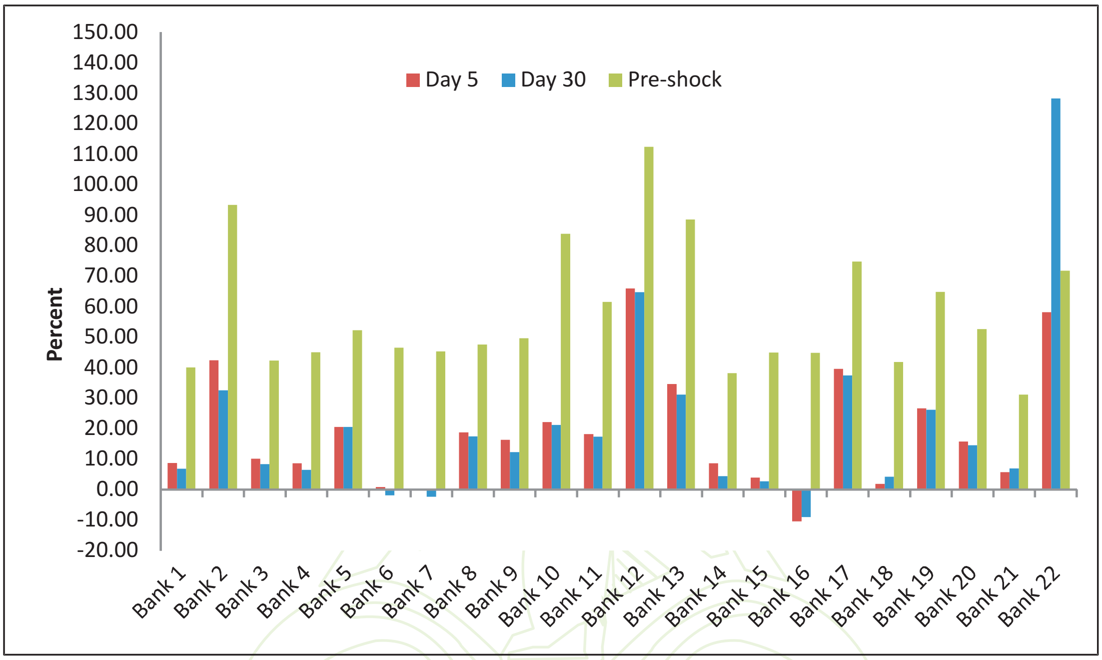


Figure 3.6: Individual Bank Positions after 5-day and Cumulative 30-day Shocks

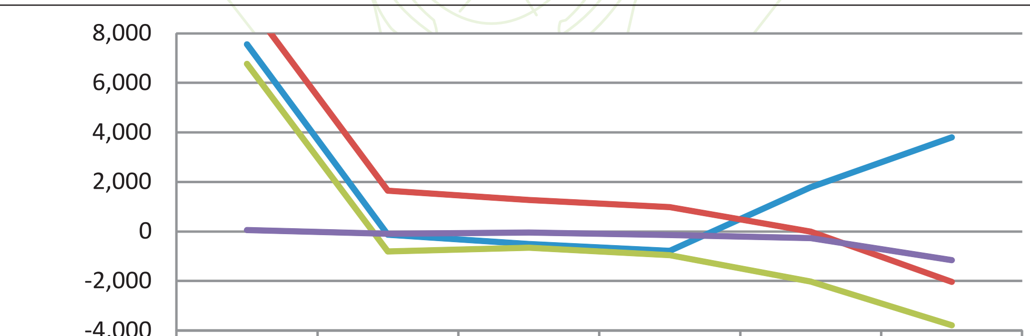


N.B: Bank 23 was excluded from figure 3.6 because of its outlier effect

Under the maturity mismatch/rollover test, assets in the 0-30 day bucket were adequately funded under the three scenarios used for the test. However, there was deterioration in the 31-90 day bucket under the Static Rollover Analysis (Test 2b) and the Dynamic Risk Rollover Tests (Test 2c) (Figure 3.7).

In general, the banking industry was resilient to liquidity stress, although the test results indicated a deterioration in the banks' resilience, compared with the position in the preceding period.

Figure 3.7: Roll-over Risk, Pre- and Post-shock

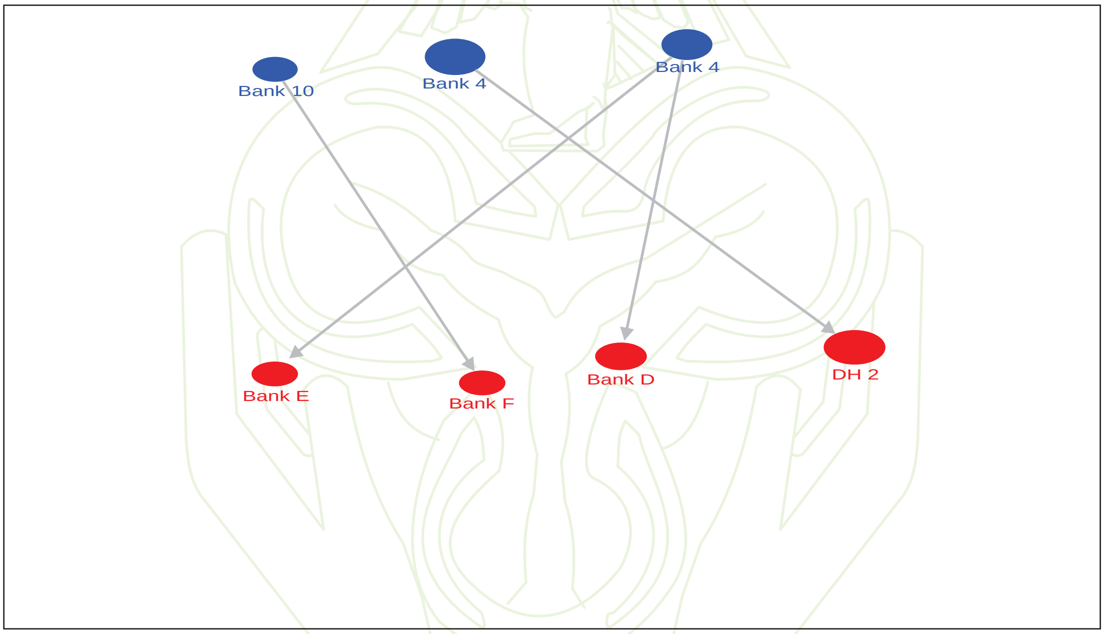


	Less than 30 days (₦'billion)	31-90 days (₦'billion)	90 - 180days (₦'billion)	180 360days (₦'billion)	1-3 years (₦'billion)	above 3 years (₦'billion)
Pre-shock	7,557	-134.61	-507.22	-780.01	1,789	3,803
Test 2a	9281.38	1,653.62	1267.62	989.81	-5.7	-2,026.93
Test 2b	6,768.55	-800.84	-656.57	-957.27	-2,020.21	-3,790.64
Test 2c	56.51	-87.31	-45.87	-137.94	-267.3	-1153.69

3.1.2.2 Contagion Risk Analysis through Inter Bank Exposures

The contagion risk analysis assessed the effect of the financial interconnectedness of institutions in transmitting shocks to individual banks and the banking system as a whole. The test was conducted using a network analysis tool which evaluates sets of bilateral links among different financial institutions. It assessed the impact of a failure or a weakness of multiple financial institutions on the entire banking system arising from exposures across institutions.

Figure 3.8: Total Bilateral Exposure



The analysis revealed that contagion risk through interbank exposures in the banking sector was minimal, as all the placing banks met the minimum CAR. Also, the industry position was above the minimum required CAR.

3.1.2.3 Solvency Stress Test

A solvency stress test was conducted on the banking industry as at December 31, 2013 to assess the stability of the sector under various hypothetically strained macroeconomic conditions.

Baseline Position

The pre-shock CARs for the entire banking industry, large, medium and small banks stood at 17.20, 16.24, 18.05 and 18.33 per cent, respectively. These reflected decreases of 1.49, 2.62, 0.2 and 0.5 percentage points over the end-June 2013 positions. Similarly, the pre-shock liquidity ratios for the banking industry, large and medium banks declined by 18.68, 19.47 and 13.15 percentage points to 51.02, 50.75 and 62.30 per cent, respectively compared with the end-June 2013 positions. However, the pre-shock liquidity ratio for small banks increased by 5.96 percentage points (Table 3.4).

Table 3.4: Baseline CARs and Lrs

Ratio	Banking Industry (%)	Large Banks (%)	Medium Banks (%)	Small Banks (%)
Dec-2013 CAR	17.20	16.05	18.05	17.83
June-2013 CAR	18.69	18.86	18.25	18.33
Dec-2012 CAR	18.36	18.06	20.32	16.93
Dec-2013 Liquidity Ratio (LR)	51.02	50.75	62.30	74.43
June-2013 Liquidity Ratio (LR)	69.7	70.22	75.45	68.47
Dec-2012 Liquidity Ratio (LR)	55.56	50.75	62.30	72.38

Figure 3.9: Banks in Each Bucket of CAR

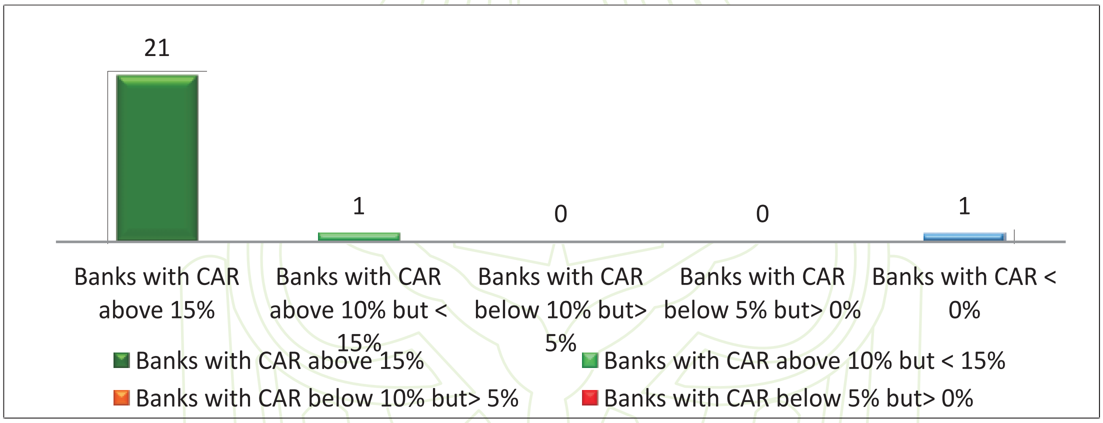


Figure 3.10: Banks in Each Bucket of LR

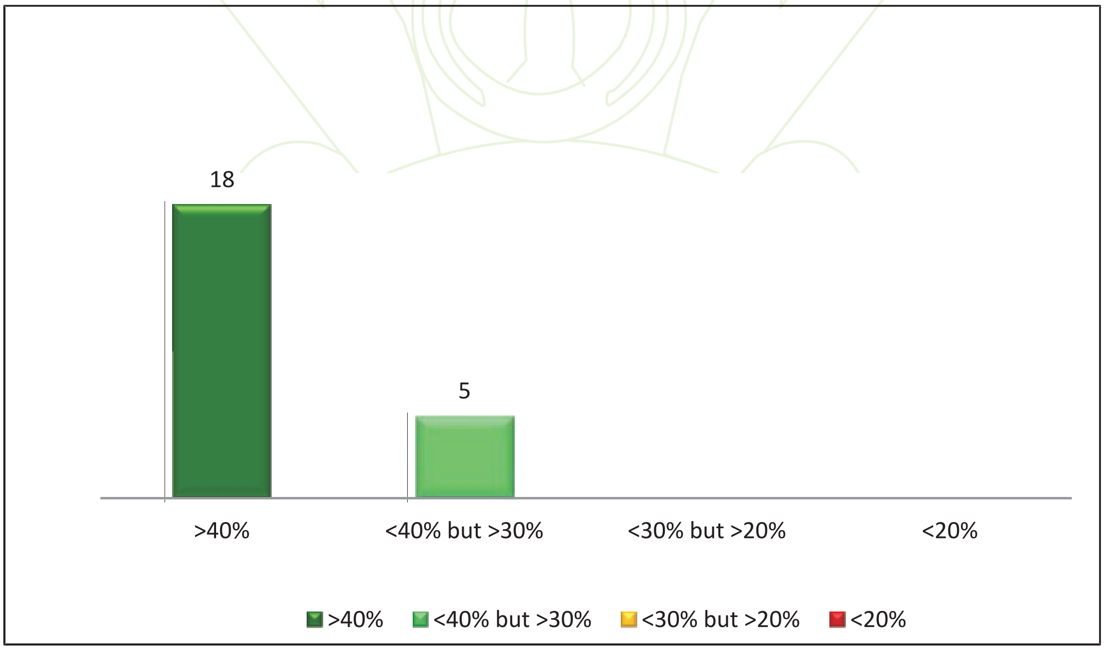
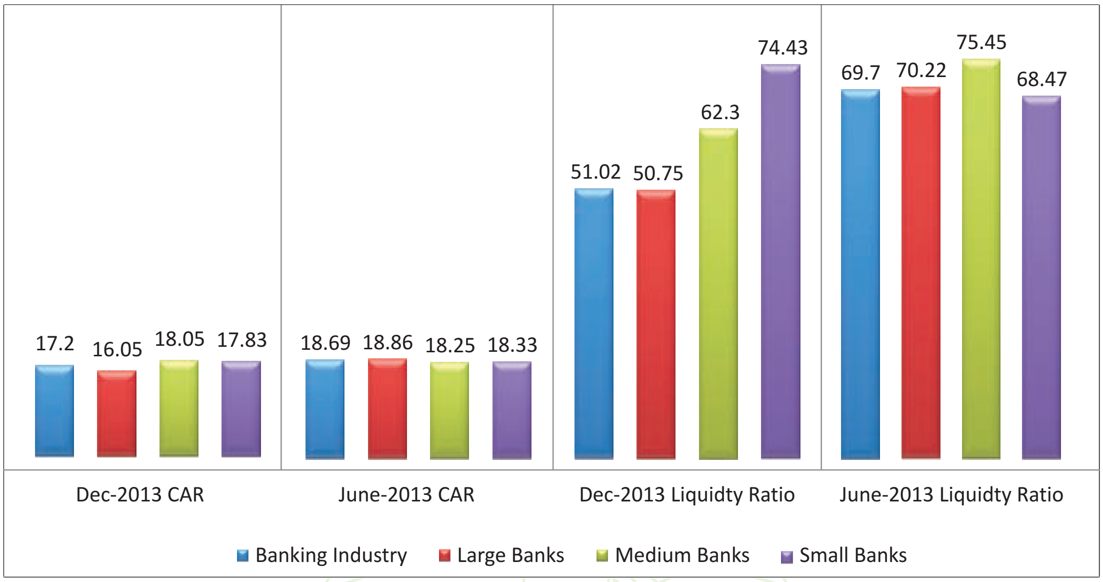
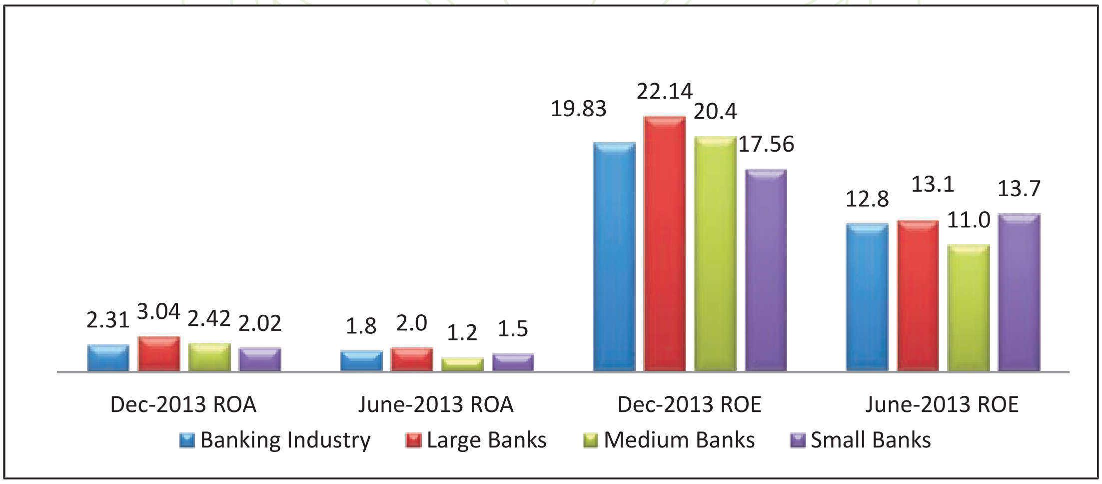


Figure 3.11: Banks in Each Bucket of LR



The pre-shock ROAs for the entire banking industry, large, medium and small banks were 2.31, 3.04, 2.42 and 2.02 per cent, respectively, with large banks being the most profitable, while ROEs stood at 19.83, 22.14, 20.40 and 17.56 per cent, respectively.

Figure 3.12: Baseline ROAs and ROEs (%)



Analysis of Test Results

- ***Credit Risk***

Generally, the banking industry resilience to credit risk sustained an upward trend as the average industry CAR stood at 12.42 per cent under a shock scenario of 200 per cent rise in NPLs. Also, large banks and medium-sized banks were less vulnerable to general credit risks as their average CARs fell from 17.64 per cent to 12.21 per cent and 17.03 to 11.45 per cent, respectively. However, the average CAR for the small banks deteriorated to 5.56 per cent (below the required minimum of 10.0 per cent), from 18.33 per cent. This indicated that about ₦89.15 billion would be required to raise their CAR to 10.0 per

Table 3.5: Stress Test Results – Credit Risk

Scenarios	Number of banks					
	≤0%	>0 but ≤5	>5 but ≤10	>10 but ≤15	>15	Total
Shock 1av-50% NPLs increase	1	2	2	5	13	23
Shock 1avi-100% NPLs increase	2	1	2	10	8	23
Shock 1avii-200% NPLs increase	2	1	5	7	8	23

cent. Under this scenario, 15 banks maintained CARs above 10.0 per cent, 5 banks had CARs between 5.0 and 10.0 per cent and 3 banks had less than 5 per cent CARs (Table 3.5).

The banking industry and peered banks, however, showed significant levels of credit concentration as indicated by the extent of capital depletion under the various shock scenarios. On the assumption that the credit facilities of the five (5) biggest corporate obligors deteriorated from “doubtful” to “lost”, the CARs of the entire banking industry, large, medium and small banks declined from their baseline positions to 9.91, 7.22, 4.19 and 9.02 per cent, respectively. Under this scenario, only five banks would be able to maintain CARs equal to or above 10.0 per cent, while the remaining 18 would record less than 10.0 per cent CAR.

Figure 3.13: Credit Concentration Risk

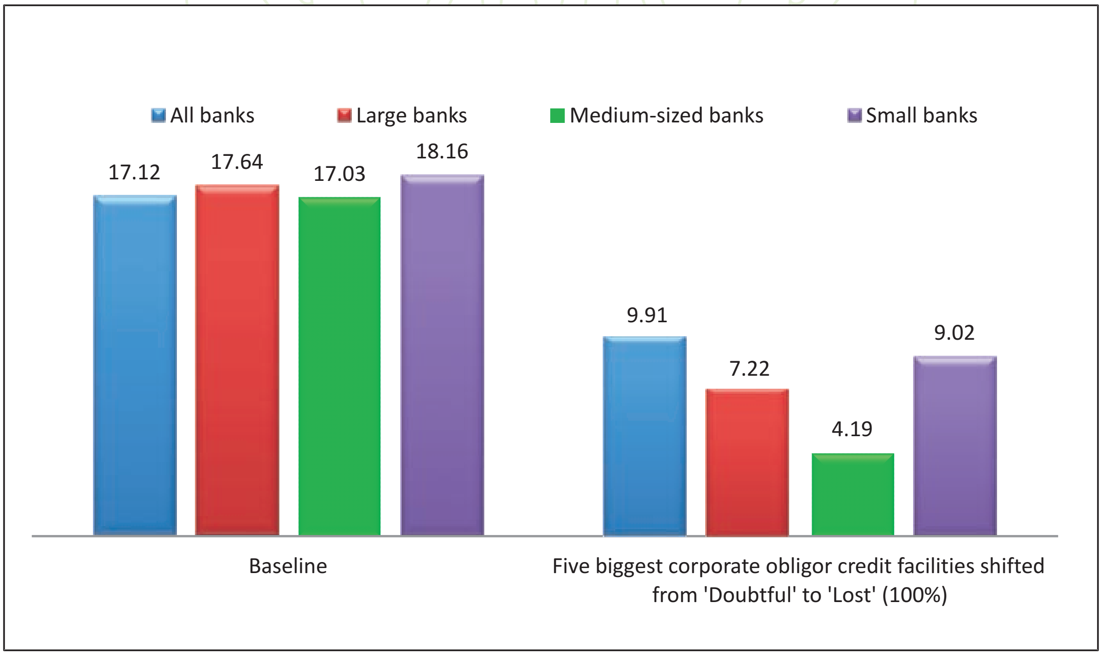


Table 3.6: Credit Concentration Risk

CREDIT CONCENTRATION RISK				
	All Banks	**Large Banks**	**Medium**	**Small**
Baseline	17.20	16.05	18.05	17.83
Single Factor Credit Concentration Shocks	Solvency Ratios after Shocks			
	All Banks	Large Banks	Medium	Small
2bi - Five biggest corporate obligors credit facilities shifted from 'pass-through'to 'sub-standard'(10%)	16.73	16.89	16.22	17.53
2bii- Five biggest corporate obligor credit facilitie s shifted from 'sub-standard' to 'doubtful' (50%)	14.03	11.85	10.27	12.56
2biii - Five biggest corporate obligor credit facilities shifted from 'doubtful' to 'lost' (100%)	9.91	7.22	4.19	9.02

- ***Liquidity Risk***

Liquidity risk was moderate as the impact of a 10 per cent general run on the banking industry resulted in the average liquidity ratio falling to 31.24 per cent (above the threshold of 30 per cent) from 51.02 per cent. Large banks followed the same trajectory as their liquidity ratio deteriorated to 30.07 per cent from 50.75 per cent. The medium and small banks showed more resilience as their liquidity ratios were 36.00 and 42.12 per cent, from 62.30 and 74.43 per cent, respectively. All the peered groups of banks remained above the 30 per cent benchmark. Thus, the banking industry and the three groups of peered banks were resilient to the liquidity shock at the level indicated.

Table 3.7: Stress Test Results - Liquidity Risk

	Banking Industry (%)	**Banks by Category**		
		Large (%)	**Medium (%)**	**Small (%)**
Baseline	51.02	50.75	62.30	74. 43
Shock 6gi (10% General Run)	31.24	30.07	36.00	42.12
Shock 6gii (15% General Run)	27.21	22.17	31.77	41.61
Shock 6giii (20% General Run)	21.10	17.13	22.42	37.35
Shock 6hi (20% Run on 20 largest Deposits)	38.42	36.99	43.45	48.52
Shock 6hii (50% Run on 20 largest Deposits)	33.47	34.52	44.97	47.00
Unsatisfactory	<30			
Border Line	≥30 < 35			
Sound Position	≥35<60			
Very Sound Position	≥60			

- ***Interest Rate Risk***

The results of the test on the net position of interest-sensitive instruments in relation to capital impairment, ROA and ROE, revealed that the banking industry and its peered categories were stable as their positions declined only marginally, even after the most severe shocks were applied (Table 3.8).

Table 3.8: Stress Test Results - Interest Rate Risk

Scenario	Banking Industry (%)	Banks by Category		
		Large (%)	Medium (%)	Small (%)
Baseline CAR	17.20	16.05	18.05	17.83
Baseline ROA	2.31	3.04	2.42	2.02
Baseline ROE	19.83	22.14	20.4	17.56
Interest Rate Volatility (Impact on CAR)				
Shock 5biii (500bps downward parallel shift in yield curve)	16.89	15.13	17.03	16.54
Shock 5biv (1000bps downward parallel shift in yield curve)	16.41	14.85	16.55	15.14
Impact of Parallel Shift in Yield Curve Shocks on ROA				
Interest Rate Volatility				
Shock 5biii (500bps downward parallel shift in yield curve)	1.23	2.89	0.74	1.58
Shock 5biv (1000bps downward parallel shift in yield curve)	1.07	1.50	0.70	1.24
Impact of Parallel Shift in Yield Curve Shocks on ROE				
Interest Rate Volatility				
Shock 5biii (500bps downward parallel shift in yield curve)	15.42	19.52	17.35	16.12
Shock 5biv (1000bps downward parallel shift in yield curve)	13.45	17.83	16.25	15.17

- ***Exchange Rate Risk***

The banks generally showed modest resilience to exchange rate risk as the industry CAR deteriorated only marginally, after a 50 per cent exchange rate appreciation shock was induced, with a 15 per cent hedging cover. After the shock, 4 banks had their CARs below the 10 per cent minimum prudential requirement (Table 3.9).

However, counterparty risk arising from exchange rate depreciation was significant, as the industry, large, medium and small banks CARs deteriorated to 12.23, 11.07, 13.54 and 14.12 per cent, respectively when 30 per cent of the total foreign exchange loan exposure was assumed lost. Assuming a 50 per cent counterparty loss due to exchange rate depreciation, the industry, large, medium and small banks CARs would fall to 7.34, 6.64, 8.12 and 8.47 per cent, respectively (Table 3.9).

Table 3.9: Stress Test Result - Exchange Rate Risk

Exchange Rate Shocks	Banking Industry	Banks by Category		
		Large	Medium	Small
CAR - Pre-shock position	17.20	17.64	17.03	18.16
Shock 4bi (10% appreciation in favour of the Naira)	17.14	17.20	16.93	17.12
Shock 4bii (20% appreciation in favour of the Naira)	15.59	15.53	15.61	15.90
Shock 4biii (50% appreciation in favour of the Naira)	14.13	12.24	14.36	12.91
Shock 4biv (100% appreciation in favour of the Naira)	3.21	2.22	5.08	6.20
Counterparty Risk Due to Exchange Rate Depreciation				
20% of the total foreign exchange loans exposure are categorised as loss	14.23	13.07	15.34	15.79
30% of the total foreign exchange loans exposure are categorised as loss	12.23	11.07	13.54	14.12
50% of the total foreign exchange loans exposure are categorised as loss	7.34	6.64	8.12	8.47

- ***Foreign Exchange Trading Risk***

The results of the test showed that the banking industry was resilient to FX trading risk. The banks' pre-shock ROA and ROE changed marginally after a 100 per cent decline in FX trading income was assumed. This was largely due to the small proportion of FX trading income to gross income.

Table 3.10: Stress Test Result - FX Trading Risk

Number of Banks with ROAs and ROEs in the Respective Buckets	≤0%	>0 ≤5%	>5 ≤10%	>10 ≤15%	>15%	
Impact of FX Trading Shocks on ROA						
FX Trading Income Volatility						Banks
Shock 7ai (10% decline in FX trading Income)	0	0	4	3	16	23
Shock 7aii (20% decline in FX trading Income)	1	0	4	3	15	23
Shock 7aiii (50% decline in FX trading Income)	1	0	6	2	14	23
Shock 7aiv (100% decline in FX trading Income)	3	0	8	2	10	23

Impact of FX Trading Shocks on ROE	<0%	<1%	<2%	<5%	>5%	
Initial ROE						
FX Trading Income Volatility						Banks
Shock 7ai (10% decline in FX trading Income)	1	2	18	2	0	23
Shock 7aii (20% decline in FX trading Income)	1	2	17	3	0	23
Shock 7aiii (50% decline in FX trading Income)	2	3	16	2	0	23
Shock 7aiv (100% decline in FX trading Income)	5	2	15	1	0	23

On the whole, the banking industry was adjudged as being stable and resilient to most of the shocks, even with severe shock scenarios.

3.2 Supervision of Banks and Other Financial Institutions

3.2.1 Banks and Discount Houses

3.2.1.1 Banks

The Bank conducted risk-based examination jointly with NDIC on 21 DMBs in the second half of 2013. The examination covered the assessment of risk assets and tested compliance with prudential requirements and the quality of the risk management control functions. Of the 21 banks examined, two were maiden examinations of the recently licensed merchant banks.

Most banks' composite risk rating had a stable outlook; while one (1) bank had an increasing and two (2) others had a decreasing risk outlook. Four of the banks were examined under the risk-based supervision framework for the first time.

The relatively stable risk profile of banks, coupled with the measures taken by the CBN and AMCON to support the industry, resulted in the general stability experienced by the banking industry as the industry witnessed signs of recovery and profitability.

The key challenges in the banking industry remained weak corporate governance and inadequate risk management practices, while the rating of the control functions generally trended towards 'needs improvement' due to the non-implementation of some previous recommendations. Improvements were, however, noted in the internal audit and financial analysis functions of most banks.

Risk-based examination of some specialized financial institutions, including the Asset Management Corporation of Nigeria (AMCON), the three private credit bureaux, and the non-interest banks (including the non-interest banking windows of conventional banks) was also conducted in the review period.

As part of its monitoring activities in the foreign exchange market, the CBN examined banks to ascertain their compliance with regulations and extant laws on utilisation of foreign exchange. The major infractions observed included failure to issue certificates of capital importation to beneficiaries on time, rendition of inaccurate returns to regulators, and non-compliance with approved net open position limits. The erring banks were appropriately penalised.

3.2.1.2 Discount Houses

The license of one discount house was revoked as a result of its failure to meet maturing obligations, severe under-capitalization and inability of the shareholders to inject additional capital. A liquidator was subsequently appointed.

In September 2013, a special examination conducted on another discount house showed signs of distress. The investigation revealed that the company's capital had been significantly eroded, thus requiring a fresh capital injection for it to continue as a going concern. In the overarching interest of financial system stability, the CBN took over the company's management and AMCON acquired its shares and injected additional funds to recapitalize it.

3.2.2 Other Financial Institutions

3.2.2.1 Microfinance Banks

Of the 821 MFBs in existence as at December 31, 2013, on-site examination was conducted on 797 MFBs in 2013, while 24 MFBs were not examined. The 24 MFBs that were not examined comprised 18 newly licensed MFBs that had not operated for up to 6 six months as at December 31, 2013 and 6 MFBs located in volatile parts of the North-east geo-political zone. Analysis of the on-site examination revealed that 526 MFBs or 66 per cent of the 797 MFBs met the capital adequacy ratio (CAR) of 10 per cent. Furthermore, 568 MFBs or 71.27 per cent satisfied the minimum liquidity ratio requirement of 20 per cent. The asset quality of the MFBs was, however, relatively poor as the average portfolio-at-risk (PAR) ratio for the sub-sector was 45.70 per cent, much higher than the prescribed maximum ratio of five (5) per cent. The CBN will continue to ensure effective supervision of the institutions with a view to enhancing stability in the sub-sector.

To give greater attention to the supervision of MFBs and in consideration of their large number, the bank engaged 116 consultants to carry out post-examination monitoring. The first round of the post-examination monitoring, involving 580 MFBs, took place in December 2013, the outcome of which is expected to inform appropriate supervisory action early in 2014.

The examinations conducted in the second half brought the total number of MFBs examined in 2013 to 810. The CBN will continue to ensure effective supervision of the institutions with a view to enhancing stability in the sub-sector.

The examinations conducted in the second half brought the total number of MFBs examined in 2013 to 810. The CBN will continue to ensure effective supervision of the in institutions with a view to enhancing stability in the sub-sector.

3.2.2.2 Primary Mortgage Banks (PMBs)

On-site examination of the 82 licensed PMBs was undertaken in the period. The examination revealed that the average NPL ratio was 42.0 per cent, with 23 meeting the 30 per cent benchmark. The examination further revealed the lack of focus on core mortgage banking business by most operators as only 26 PMBs met the minimum mortgage assets to loanable funds ratio of 60 per cent, while 3 met the minimum mortgage assets to total assets ratio of 50 per cent. The examination also showed that a considerable proportion of the sub-sector's investible funds were placed with commercial banks.

3.2.2.3 Finance Companies (FCs)

On-site examination was conducted on 55 out of the 61 operating finance companies during the review period. Six of the companies were undergoing restructuring. The examination revealed that 40 per cent of the FCs met the capital adequacy ratio (CAR) of 12.5 per cent. The average CAR for the sub- sector was, however, a negative 442 per cent. Overall, 40 per cent of the FCs had shareholders' fund unimpaired by losses of above ₦20 million. Thirty nine of the FCs were operating with a lower capital than the regulatory minimum of ₦20 million. Poor asset quality remained the bane of the sub-sector, as the NPL ratio stood at 40.7 per cent, well above the prescribed maximum of 20 per cent. As part of the reform measures adopted by the Bank, the minimum capital was raised to ₦100 million, from ₦20 million, during the review period while the final approval of the operating guidelines for the sub- sector was being awaited.

3.2.2.4 Bureaux de Change

Spot checks were carried out on 160 bureaux de change (BDCs) during the review period, compared with the checks on 60 undertaken in the first half of 2013, thus bringing the total number of reviewed BDCs in 2013 to 220. The exercise indicated that certain infractions persisted amongst the institutions, including: non-rendition of returns on the purchase and utilization of foreign exchange (Forex); failure to keep accounting records; and engaging in wholesale foreign exchange trading. Accordingly, 29 BDCs were suspended from the CBN Forex window, 58 were subjected to monetary sanctions, while the licenses of 20 BDCs were revoked. This brought the total number of revoked BDC licenses in 2013 to 222.

3.3 Compliance with International Standards

3.3.1 Anti-Money Laundering/Combating the Financing of Terrorism

In supporting the global fight against terrorism, the CBN regularly circulated the *United Nations Consolidated Lists of Persons/Entities Involved in Terrorism Financing or Terrorist Activities* to financial institutions under its regulatory purview for appropriate action.

In order to strengthen domestic collaboration, the CBN inaugurated the AML/CFT Stakeholders' Consultative Forum for key stakeholders in the fight against money laundering and financing of terrorism. This resulted in an increased level of co-operation through the exchange of information, joint examinations, and training programmes.

Nigeria had been placed on the Financial Action Task Force (FATF) “grey list” of countries which had failed to make significant progress in their AML/CFT regimes in 2009. To address this problem, the CBN and other stakeholders took action based on the reports of the GIABA Mutual Evaluation and International Monetary Fund Technical Assistance Team to improve legislation and enforcement of the regulations on AML/CFT.

The CBN action included the issuance of:

- AML/CFT Regulations in 2013 (amended);
- An AML/CFT Risk-based Supervision (RBS) Framework;
- An AML/CFT Compliance Framework applicable to the Bank's operations;
- A Dud Cheques Policy;
- Standard account opening forms for financial institutions, in

collaboration with the Committee of Chief Compliance Officers of Banks in Nigeria; and
- A Safe Custody Items Policy.

These measures led to the delisting of Nigeria from the "grey list" by the Financial Action Task Force on October 18, 2013.

3.3.2 Implementation of Basel II/III

For effective implementation of the Basel II/III framework in Nigeria, the Bank issued the *Guidance Notes on the Calculation of Regulatory Capital* to the banking industry in the reporting period.

The *Guidance Notes* took cognisance of the peculiarities of Nigeria's local environment and, therefore, required banks to:

- Commence a parallel run of capital adequacy computation, based on the requirements of the new guidelines alongside Basel I requirements, effective January 1, 2014 and migrate fully to Basel II by June 2014;
- Adopt basic approaches for calculating credit, market and operational risks capital requirements for the first two years, in anticipation of the development of an effective rating system in Nigeria. This would also afford banks sufficient time to gather the required data and acquire necessary experience for the adoption of the more advanced approaches;
- Carry out an Internal Capital Adequacy Assessment Process (ICAAP) on an annual basis, as at December 31, and forward copies of the assessment report to the CBN for review, not later than four (4) months after the year end, beginning from 2014; and
- Comply with the Pillar 3 disclosure requirements on a bi-annual basis.

The implementation of Basel II/III in Nigeria is expected to enhance the safety and soundness of financial institutions and promote broad stability of the financial system.

Review of Risk Weights on Certain Industry Exposures

One of the identified risks in the banking system is concentration risk. To mitigate this risk and to provide incentives for diversification, the CBN reviewed the risk weights for the computation of capital adequacy ratio. The review provided that:

- Where the exposure to a particular sector, as defined by the *International Standard Industrial Classification of Economic Sectors* is in excess of 20 per cent of the total credit facilities of a bank, the risk weight of the entire portfolio shall be 150 per cent;
- Bonds that meet the eligibility criteria set out in the *Guidelines for Granting Liquid Asset Status for State Government Bonds* would be risk-weighted at 20 per cent, while others would be weighted at 100 per cent;
- Any breach of the single obligor limit shall be regarded as impairment of capital;
- Lending by a bank to its financial holding company would be regarded as return of capital and shall, accordingly, be deducted from the capital of the bank in the course of computing its capital adequacy ratio; and
- Lending to subsidiaries within the group shall be risk-weighted at 100 per cent, provided they are fully collateralised. Otherwise,

such exposures would be taken as reduction of capital and be deducted from capital during capital adequacy computation.

The above policy measures, approved to take effect from January 1, 2014, would ensure a stricter prudential assessment of the banks' capital adequacy.

3.3.3 International Financial Reporting Standards

Sequel to the publication of the first IFRS-based annual financial statements by banks and discount houses in the first half of 2013, the CBN/NDIC added traction to the implementation by conducting an assessment of the impairment methodology and IT support for IFRS reporting of the entities in the second half of 2013. The impairment methodology assessment reviewed the impairment models of the entities for appropriateness, adequacy of the inputs, and correctness of the output.

The assessment of IT support for IFRS reporting indicated that while some entities used Excel to convert their NGAAP figures to IFRS figures, others were at various stages of implementing IT solutions for IFRS reporting.

During the review period, capacity building programmes continued, especially in the Other Financial Institutions (OFIs) sub-sector. In addition, 19 publicly quoted OFIs issued their first IFRS financial statements as at December 31, 2012. Guidelines were also issued on the mode of adoption expected of the other OFIs, with the unit MFBs and BDCs categorised under SMEGA Levels II and III respectively.

Following the adoption of IFRS in the banking industry, an application, FinA, was deployed by the Bank in November 2013. The new application, which went live in December 2013, is expected to run concurrently with the existing e-FASS application.

3.4 The Assets Management Corporation of Nigeria

The Corporation's bonds held by banks and other private investors, amounting to ₦734.09 billion, became due and were redeemed on 31st December 2013, in line with the terms of the indenture, while bonds of ₦3.51 trillion held by the CBN were restructured into a ₦3.80 trillion Note at 6 per cent, with a 10-year tenor. AMCON is due to redeem the third tranche of its bonds held by private investors in the sum of ₦866.73 billion by October 2014. Thereafter, the CBN would be the only bondholder in AMCON.

The Eligible Bank Assets (EBAs) acquired by AMCON stood at ₦2.37 trillion at end-December 2013, from ₦2.72 trillion at end-June 2013. Restructured loans amounted to ₦374.35 billion as at December 31, 2013 of which 55.75 per cent were performing, while 44.25 per cent were non-performing. Total recoveries at end-December 2013 were ₦164.5 billion, from the ₦109.40 billion achieved at end-June 2013.

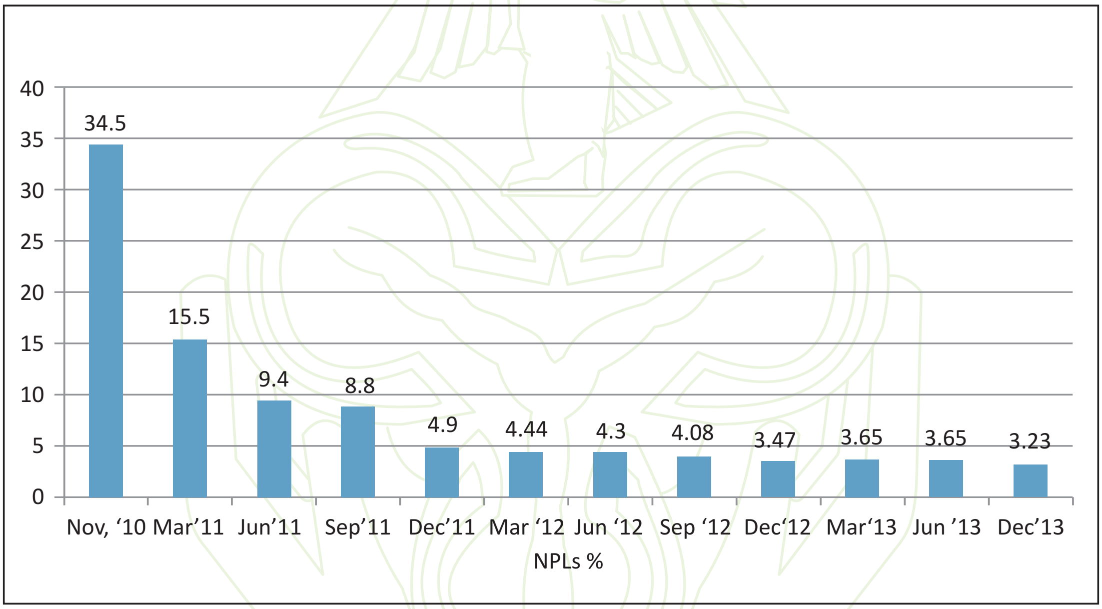
3.5 Key Risks in the Financial System

3.5.1 Credit Risk

The NPL ratio decreased to 3.23 per cent, compared with 3.65 per cent at end-June 2013, reflecting an improvement in the quality of banks' assets. It also remained within the regulatory threshold of 5 per cent. Total NPLs, however, increased by 0.72 per cent to ₦324.13 billion at end-December 2013, from ₦321.80 billion at end-June 2013.

Furthermore, credit concentration remained a concern as the top 50 and 100 borrowers constituted 31.88 and 40.51 per cent, respectively, of gross credit at end-December 2013. This compares with 32.57 and 40.76 per cent, respectively, at

Figure 3.14: Trend of Banking Industry NPLs, 2010 - 2013



end-June 2013, indicating a marginal decrease in credit concentration.

3.5.2 Liquidity Risk

Liquidity risk remained subdued during the review period as all banks exceeded the minimum required ratio of 30 per cent and the industry maintained an average of 50.63 per cent. The downside risk, however, was the cost of liquidity management in order to contain inflationary pressure and to protect the naira exchange rate.

3.5.3 Market Risk

Rates were generally stable in the second half of 2013 except for the fluctuations caused by the short-run effects of the July 2013 MPC decision to raise CRR on public sector deposits to 50 per cent from 12 per cent, and the challenges experienced by some discount houses. Measures taken by the CBN, however, helped in moderating the rates towards the end of the reporting period.

Notwithstanding the stable rates, the continued decline of foreign reserves and decrease in oil receipts due to challenges in the oil sector, coupled with possible foreign portfolio investment reversals following the tapering of the US quantitative easing programme, could elevate market risk.

3.5.4 Operational Risk

With enhanced security features in electronic banking software, identity theft and other cyber crimes have been ameliorated. However, other operational risks, such as fraud and forgeries, persisted.

Reported cases of fraud and forgery increased by 58.07 per cent to 3,917, involving a total sum of ₦31.49 billion in the second half of 2013, from 2,478 cases involving ₦22.41 billion in the first half of 2013. Actual losses, however, declined by 45.55 per cent to ₦2.08 billion in the review period, from ₦3.82 billion in the first half of 2013.

3.5.5 Reputational Risk

The activities of the consumer protection function of the CBN, in mediating between banks and their customers, contributed in enhancing confidence in the banking system. Furthermore, the engagement of the general public through sensitization workshops, road shows, and consumer parliaments improved confidence in the system. This was evidenced by the substantial decline in the number of complaints by bank customers to the CBN.

Also, the delisting of Nigeria from the Financial Action Task Force (FATF) “Grey List” in October 2013 has improved the country's reputation as an investors' destination.

3.6 Credit Bureaux

3.6.1 CBN's Credit Risk Management System

The Credit Risk Management System (CRMS)[7] continued to complement the process of credit risk management in the banking industry. At end-December 2013, the number of borrowers registered by banks in the CRMS database stood at 202,611, while the total value of outstanding credits was ₦16.49 billion.

During the review period, 75 requests/or complaints on customers' credit records in the CRMS were processed as against 86 from January to June 2013.

Periodic spot checks on banks' compliance with the CRMS regulation helped to improve the number of borrowers registered in the database, while the decline in CRMS-related complaints was due to improved compliance with the CRMS *Guidelines*. Also, a workshop on basic CRMS administration and processes was conducted in November 2013 to train desk officers of reporting institutions.

3.6.2 Private Credit Bureaux

The three licensed private credit bureaux (PCBs) continued to complement the efforts of CBN's CRMS in ensuring that financial institutions have adequate information on prospective borrowers while processing their credit requests. The number of credit records in PCBs increased to 21.89 million, from 21.08 million at end-June 2013.

The progress made by the PCBs notwithstanding, they continued to face the challenges of low public awareness, absence of a unique identifier, inadequate skilled human resources, and lack of an efficient information sharing mechanism. The guidelines for the operation and regulation of PCBs were revised, effective November 14, 2013, to address the identified challenges and facilitate sustainable growth of the economy.

3.7 The Financial Services Regulation Coordinating Committee

The Financial Services Regulation Coordinating Committee (FSRCC) continued to provide a forum for interaction and coordination by the

[7]The CRMS is a depository of credit information on borrowers of ₦1 million and above for individuals, and ₦5 million and above for corporate customers.

regulatory authorities in the Nigerian financial system. The framework for the enhancement of supervisory tools, developed by the Bank, was adopted by the Committee for implementation.

Under the framework, the FSRCC would be restructured to have a Support Service Group (SSG) responsible for financial research and macro-prudential analysis. A robust, IT-driven database infrastructure is expected to become an important component part of the restructuring arrangement. Other aspects of the adopted framework include the review of existing legislation and capacity building to transform the FSRCC into the Financial System Stability Committee (FSSC).

The FSRCC also identified the need for regular reports on vulnerabilities and threats to financial system stability and charged its Financial Sector Soundness Sub-Committee (FSSSC) with the task of developing a financial stability monitor/dashboard and report on the dashboard at every meeting of the FSRCC.

3.8 Consumer Protection

3.8.1 Customer Complaints

The Bank received a total of 305 customer petitions against financial institutions during the second half of 2013.The figure showed a decrease of 59.82 per cent, from the 759 petitions received in the first half of 2013. The total refunds by banks to petitioners arising from the complaints amounted to ₦1.48 billion and US$194,000, compared with ₦1.45 billion recorded in the first half of the year.

4.0 THE PAYMENTS SYSTEM

4.0 THE PAYMENTS SYSTEM

In pursuance of the Payments System Vision 2020, the CBN deployed a new real-time gross settlement (RTGS) system in the review period for the settlement of inter-bank fund transfers, customers' transfers and net positions from clearing systems on real-time basis. The new system interfaces with the Scripless Securities Settlement System (S4) to facilitate simultaneous delivery versus payment to mitigate settlement risks.

The Bank extended its cash-less policy, earlier launched in Lagos, to five additional States and the FCT, effective October 1, 2013. This reduced the cost of cash management, increased efficiency of the payments system, and enhanced financial inclusion.

Ten (10) additional Payment Terminal Service Providers (PTSPs) were licensed in the review period to deploy and maintain PoS terminals, bringing the total number of PTSPs to 16. With the additional PTSPs, a wider coverage on the deployment of PoS terminals across the country would be achieved.

The Bank, in collaboration with the Bankers Committee, commenced the development of a biometric solution to address the challenges posed by the absence of a unique identifier in the Nigerian banking industry.

During the review period, the Bank adopted the use of mobile money and issued the *Guidelines for the Operation and Regulation of Agent Banking in Nigeria,* aimed at promoting financial inclusion.

4.1 The Payments System Vision 2020

The Bank sustained the implementation of the Payments System Vision 2020 (PSV 2020) and achieved the following milestones during the review period:

1. Hosted a 2-day maiden International Conference on the Payments System, with over one thousand participants from stakeholders across the globe;

2. Revised and launched the *Payments System Vision 2020 Strategy* document. This would provide the policy direction for the Bank in the payments space in the next five years. The overall objective remains consistent with the original *PSV 2020* document, intended to create an electronic payments infrastructure that is nationally utilised and internationally recognized; and

3. Assessed the Nigerian Payments System Market Infrastructure against the current 24 BIS/IOSCO core Principles for Financial Market Infrastructure (PFMI).

Consequent upon the revision of the strategy document and benchmarking of the Nigerian PFMI against the 24 BIS/IOSCO principles, the CBN shall:

a. Ensure that, henceforth, no national payments system shall invoke the principle of unwind;
b. Remove its implicit role of 'Lender of Last Resort' for the RTGS payment system by December 2016 and Deferred Net Settlement systems by December 2019;

c. Strengthen its scheme governance structure to reflect the significantly greater responsibility of scheme management, covering all aspects of risk, business management and operational resilience;

d. Ensure that each Scheme Management Board carries out an annual self-assessment against the CPSS/IOSCO PFMI. An independent review shall be undertaken every four years, with the objective of making the results publicly available by end-2017;

e. Open formal engagement channels with Continuous Linked Settlement as a first step towards the naira becoming a settlement currency;

f. Mandate the use of the SWIFT Sanctions Checking (or its equivalent) for international payment instructions originating from all banks in Nigeria; and

g. Work jointly with SEC and other key stakeholders to sponsor a formal review of the securities market in Nigeria, which would be completed under the FSS2020 Financial Markets work stream.

4. Furthermore, the CBN identified the following new areas and initiatives to deepen the adoption of e-payment in the next phase of the PSV2020 Project in the following areas:
   i. Agriculture,
   ii. Smart cities,
   iii. Transportation,
   iv. Education,
   v. Hotels & entertainment,
   I. Health,
   ii. Bill Presentment.

5. Issued the following guidelines:
   i. The Revised RTGS Rules and Regulations, and
   ii. The Clearing House sanctions.

4.2 The Real-Time Gross Settlement System

The volume and value of inter-bank transfers through the Nigeria Inter-bank Settlement System (NISS) increased to 200,918 and ₦56,610.69 billion at end-December 2013, from 197,220 and ₦55,005.31 billion at end-June 2013, reflecting increases of 1.88 and 2.92 percent in volume and value, respectively.

4.3 NIBSS Instant Payment

The volume of NIBSS instant payment (NIP) rose to 11,186,930 at end-December 2013, from 5,924,602 at end-June 2013, reflecting an increase of 88.82 per cent, while the value increased by 59.53 percent to ₦6,666.17 billion. The significant rise in volume and value of NIP was attributed to the extension of the cash-less policy to 5 additional states and the FCT.

Figure 4.1: Volume of NIP Transactions, July to December 2013

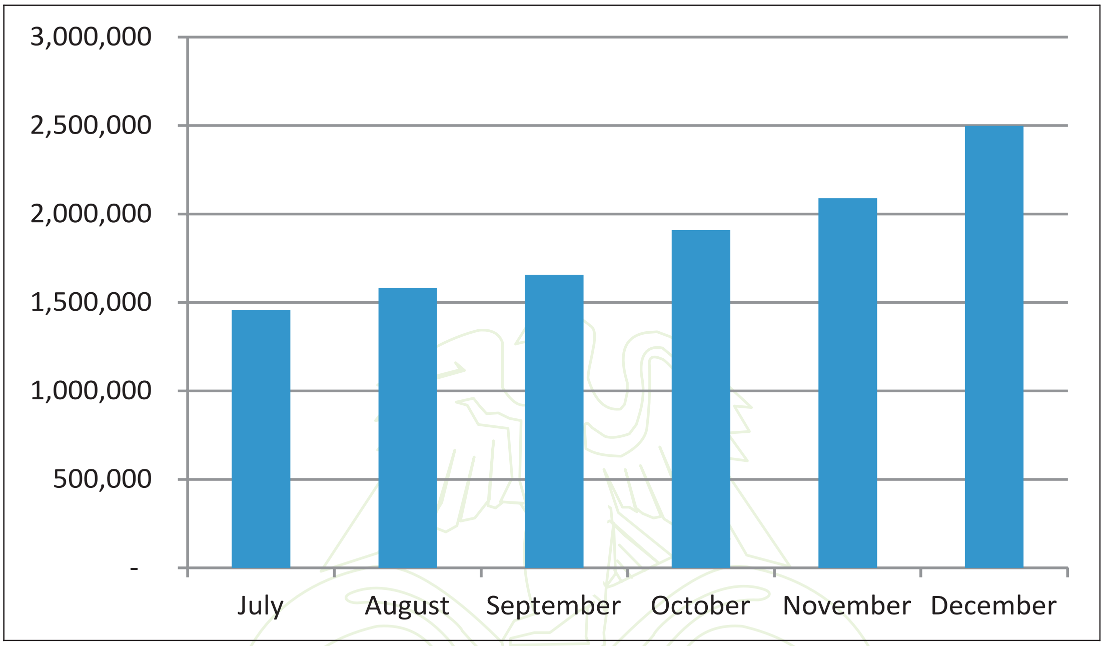
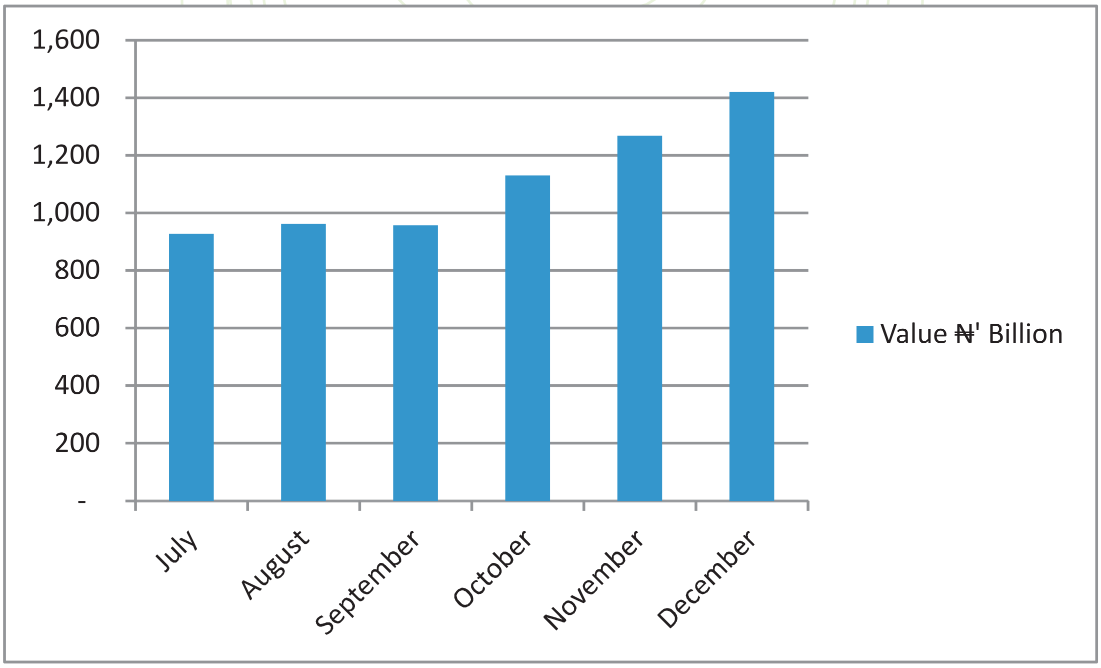


Figure 4.2: Value (₦ Billion) of NIP Transactions, July to December 2013



4.4 NIBSS Electronic Fund Transfer

The volume and value of NIBSS Electronic Funds Transfer (NEFT) increased to 16,115,171 and ₦7,569.17 billion at end-December 2013, from 13,918,838 and ₦6,738.14 billion at end-June 2013, reflecting increases of 15.78 per cent and 12.33 per cent in volume and value, respectively.

Figure 4.3: Volume of NEFT Transactions, July to December 2013

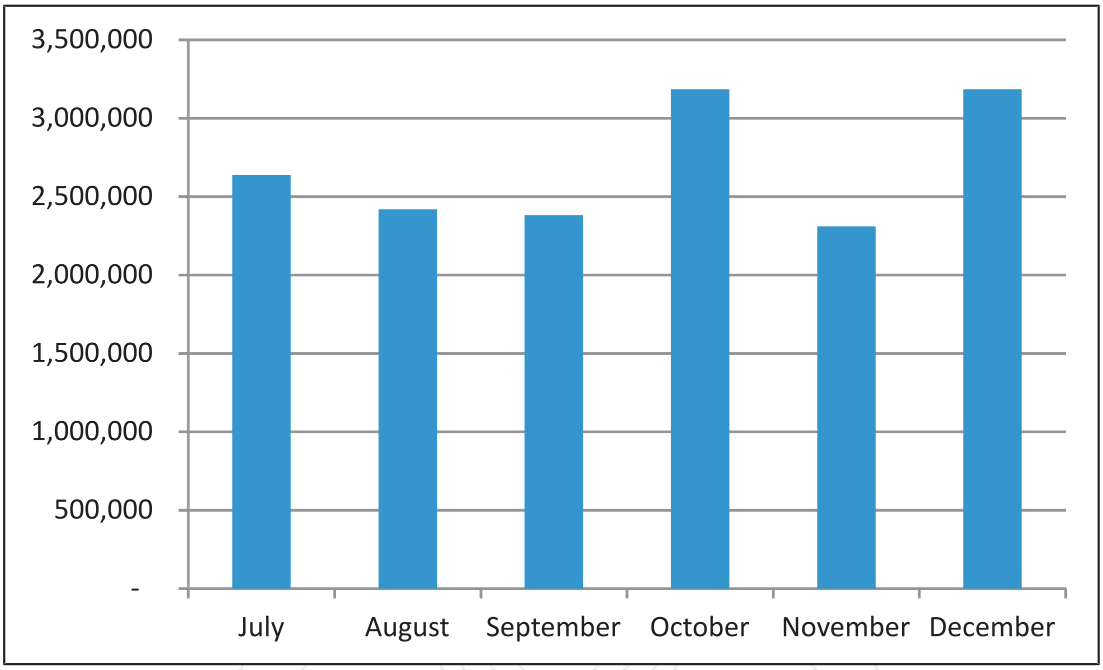
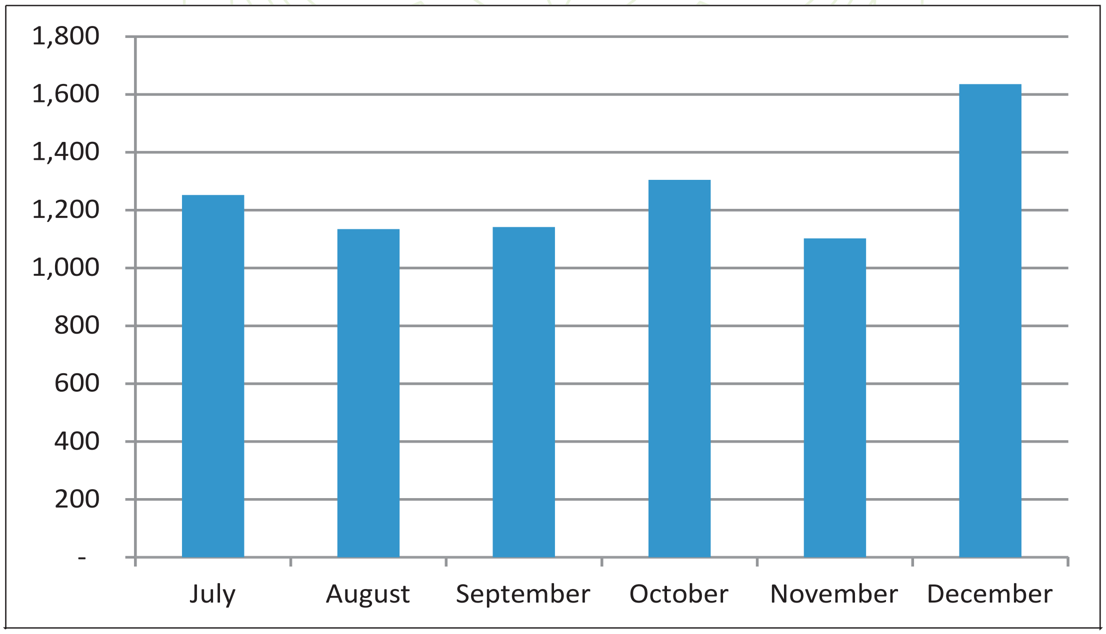


Figure 4.4: Value (₦ Billion) of NEFT Transactions, July to December 2013



4.5 Cheque Clearing

The volume and value of cheques cleared decreased to 8,257,330 and ₦4, 073.15 billion at end-December 2013, from 21,096,075 and ₦11,492.50 billion at end-June 2013, thus reflecting decreases of 40.23 and 13.09 per cent, respectively.

Figure 4.5: Volume of Cheques Cleared, July to December 2013

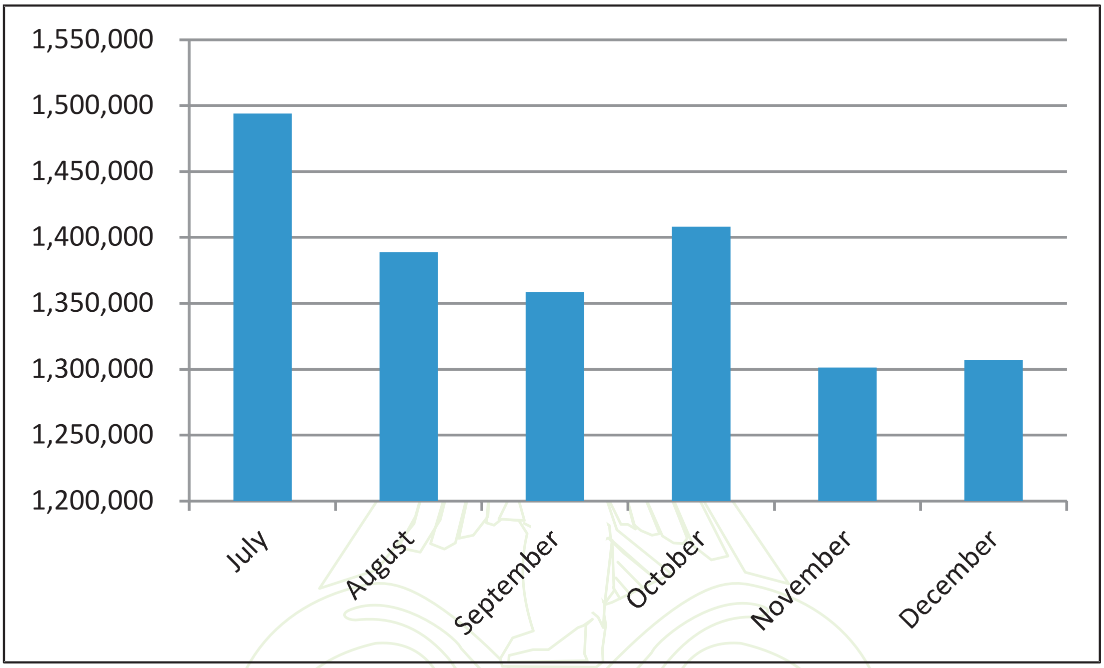
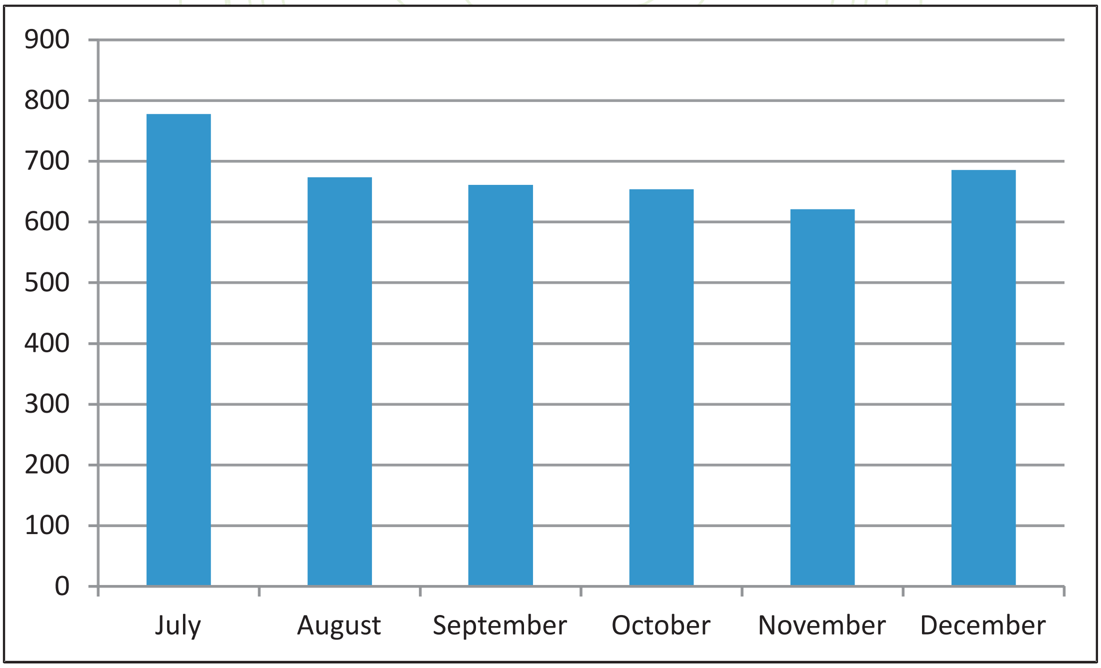


Figure 4.6: Value (₦ Billion) of Cheques Cleared, July to December 2013



4.6 Electronic Cards

Electronic card (e-card) transactions rose to ₦1,764.11 billion in the second half of 2013, from ₦1,416.10 billion in the first half of 2013, reflecting an increase of 20.04 per cent, while the volume increased to 176,413,492 at end-December 2013, from 146,961,511 at end-June 2013.

Automated teller machines (ATMs) remained the dominant channel of electronic payments. ATMs accounted for 89.92 per cent, followed by mobile payments with 5.55 per cent and PoS terminals with 3.51 per cent. The Internet as a payment channel (e-commerce) is yet to be fully embraced by the banking public. Thus, it remained the least patronised and accounted for only 1.02 per cent of the total. In value terms, ATMs accounted for 87.44 per cent; PoS, 5.88 per cent; mobile payments 5.17 per cent; while the Internet accounted for 1.51 per cent.

Figure 4.7: Volume of Electronic Card Transactions, July to December 2013

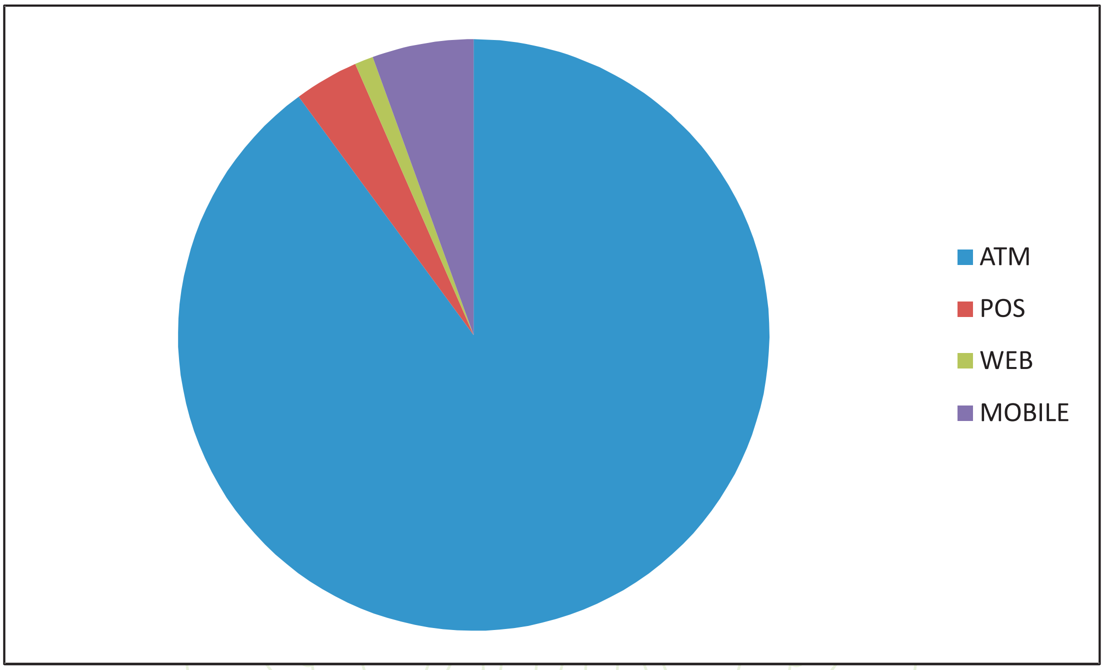
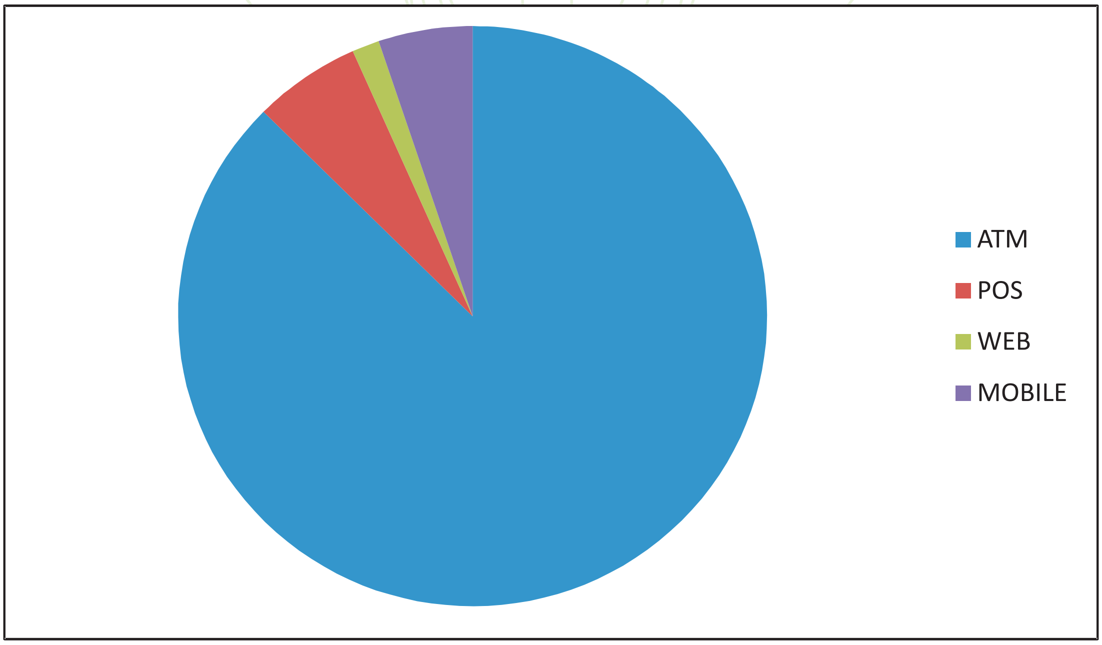


Figure 4.8: Value of Electronic Card Transactions, July to Dec 2013



4.6.1 ATM Transactions

The number of ATMs rose to 12,755 at end-December 2013, from 11,702 at end-June 2013. The volume of ATM transactions increased during the period under review to 158,629,927, from 136,663,013, reflecting an increase of 16.07 per cent, while the value increased to ₦1,542.59 billion from ₦1,286.35 billion at end-June 2013, reflecting an increase of 19.92 per cent.

Figure 4.9: Volume of ATM Transactions, July - Dec 2013

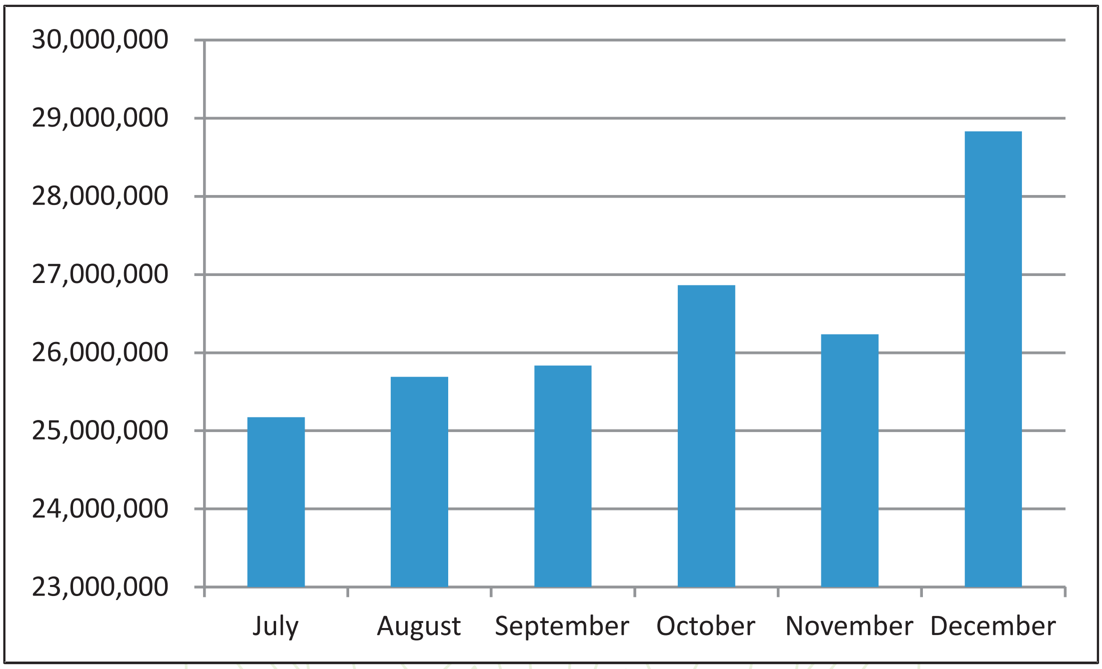
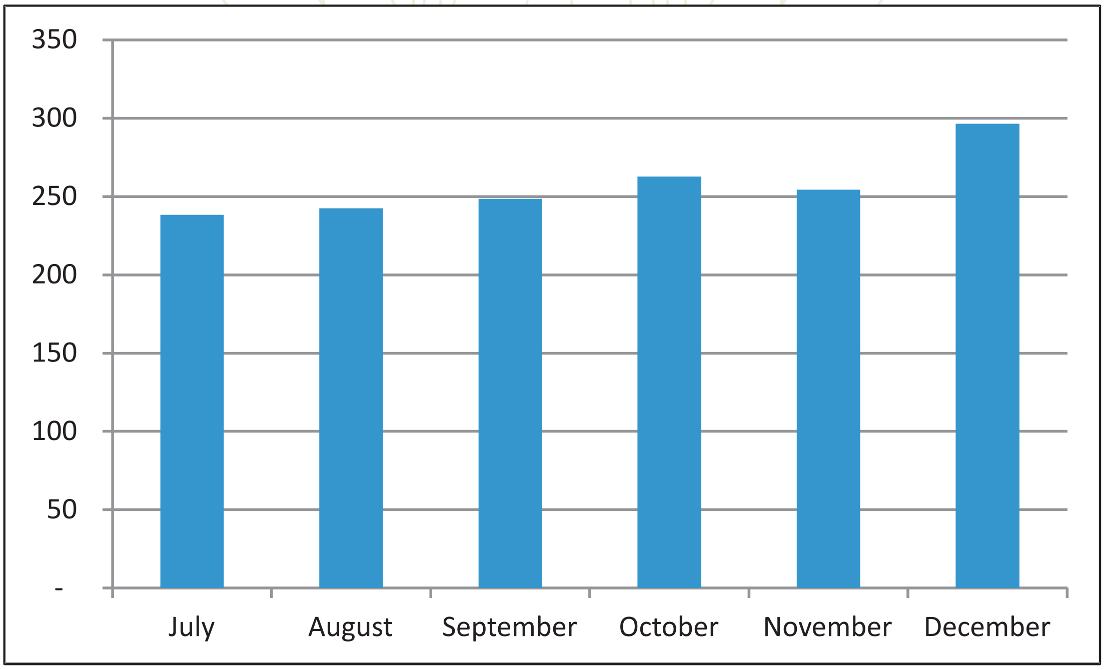


Figure 4.10: Value (₦ Billion) of ATM Transactions, July - Dec 2013



4.6.2 Mobile Payments

The volume and value of mobile payments increased during the review period to 9,797,110 and ₦91.14 billion, from 5,982,225 and ₦51.79 billion, respective, in the first half of 2013, respectively, reflecting increases of 63.77 and 75.96 per cent, respective, in volume and value, respectively.

Figure 4.11: Volume of Mobile Payments, July - Dec 2013

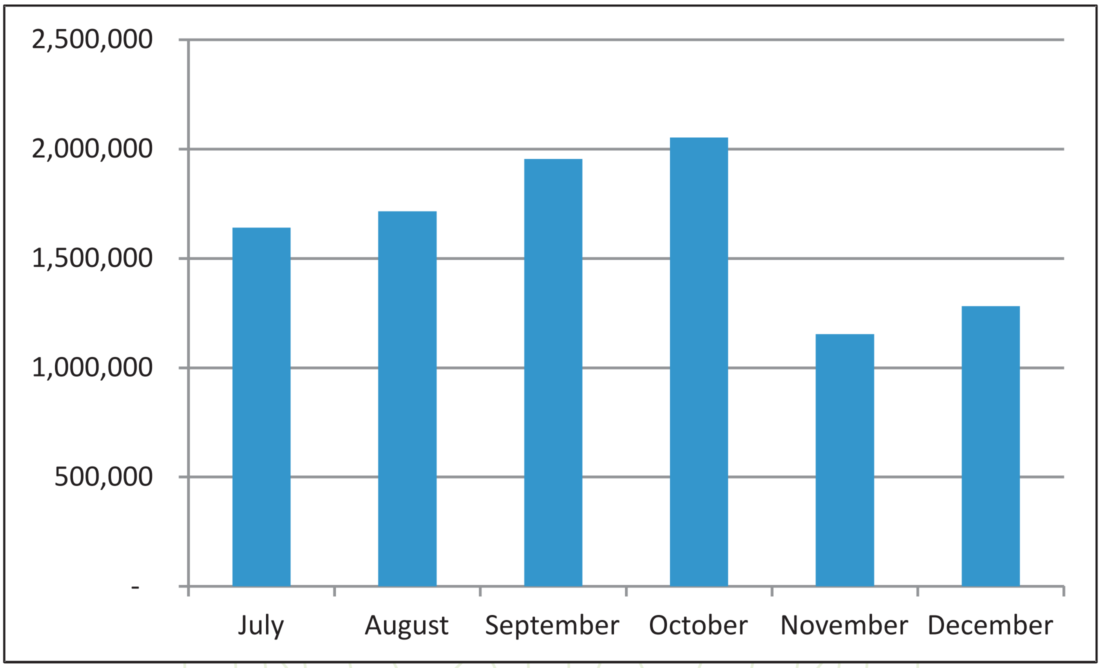
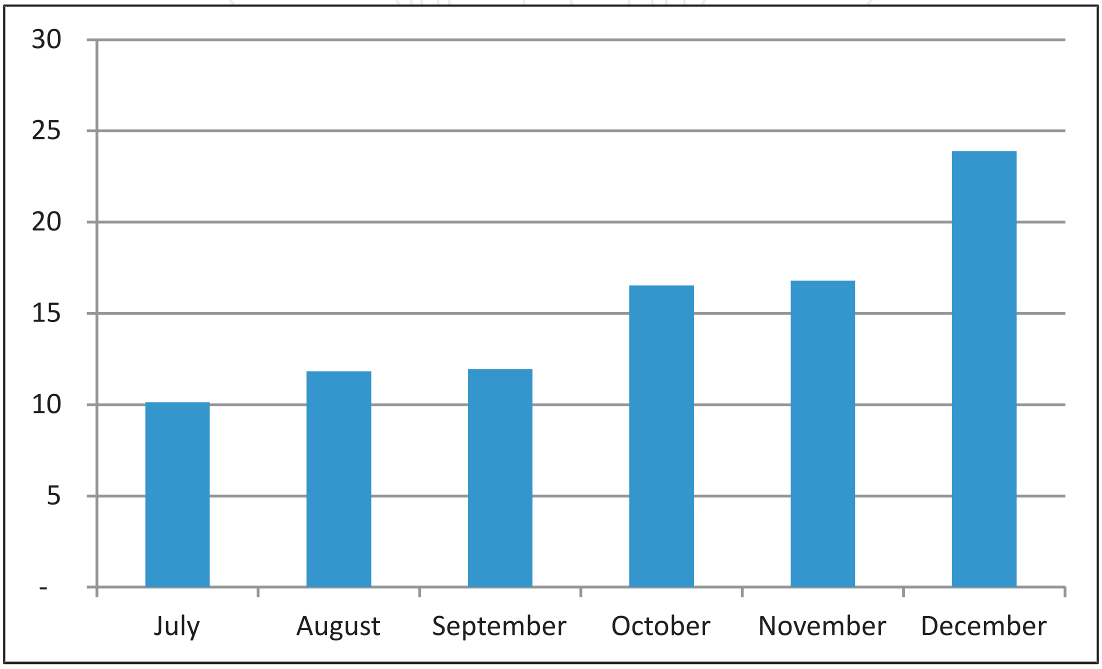


Figure 4.12: Value (₦ Billion) of Mobile Payments, July - Dec 2013



4.6.3 Point of Sale Terminal Transactions

The volume and value of point of sale (PoS) transactions increased during the review period to 6,194,467 and ₦103.79 billion from 3,207,788 and ₦57.23 billion, respectively, in the second half of 2013, reflecting increases of 93.11 and 81.37 per cent in volume and value. The number of PoS terminals rose to 120,191 at end-December 2013 from 119,653 at end June 2013.

Figure 4.13: Volume of PoS Transactions, July - Dec 2013

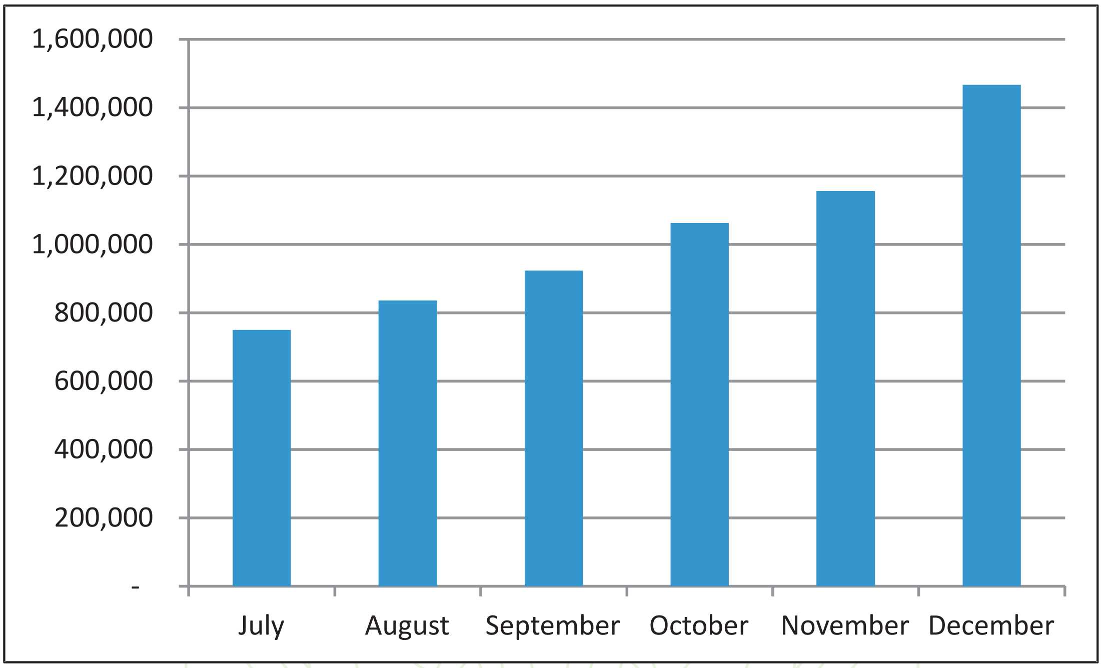
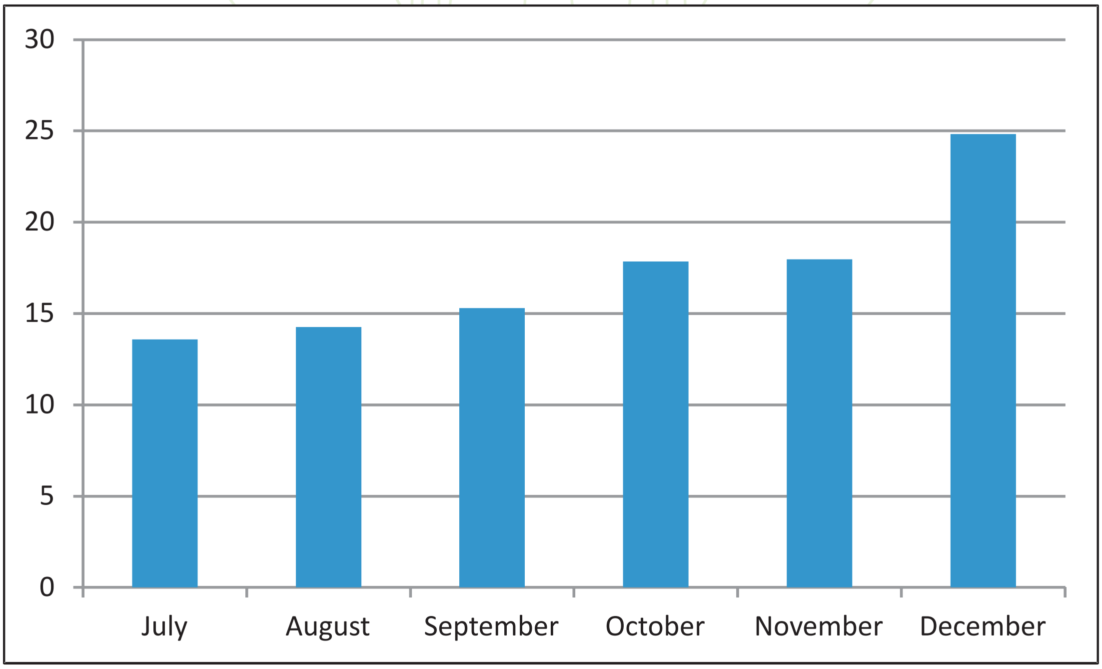


Figure 4.14: Value (₦ Billion) of PoS Transactions, July - Dec 2013



5.0 OUTLOOK

5.0 OUTLOOK

Growth in global output is projected to strengthen at 3.7 per cent in 2014, up from the 3.0 per cent recorded in 2013. Most of the growth is expected to come from the advanced economies, as the drag in fiscal consolidation and uncertainties surrounding the impact of the US Federal Reserve's decision to systematically cut back on its quantitative easing programme on most economies thin out and private sector demand gains firmer ground. Also, it is expected that 2014 would witness an appreciable reduction in fiscal tightening, but accommodative monetary conditions in most economies. Consequently, output growth in the advanced economies is projected at 2.2 per cent or 0.9 per cent higher than the 1.3 per cent recorded in 2013. The stronger recovery in advanced economies will see emerging markets benefiting from higher external demand. Output in Emerging Market and Developing Economies is projected to grow at 5.1 per cent in 2014, compared to 4.7 per cent in 2013, and growth in Sub-Saharan Africa is projected to expand to 6.1 per cent in 2014 from 5.1 per cent in 2013.

The IMF *World Economic Outlook (January 2014 Update),* however, noted that downside risks remained with these forecasts. The risks include low inflation in advanced economies, especially the Euro area. Increases in real debt burdens and “premature real interest rate”, given that monetary policy in the Euro area, is constrained in lowering nominal interest rate. In the emerging market economies, increased financial market and capital flow volatility remains an issue of concern, given the announcement in December 2013 that the U.S. Federal Reserve would start its tapering early 2014. Although responses to the news on tapering were relatively subdued in most economies, the combination of portfolio shifts and domestic weaknesses could result in sharper capital outflows and exchange rate adjustments.

Consequently, the report recommends that efforts to strengthen the global financial system and sever the links between banking and sovereign debt distress in Europe should be embarked upon to ensure that improvements in the global financial outlook translate into better prospects for the real economy.

For the Nigerian economy, real GDP growth is expected to remain strong at 7.3 per cent in 2014, up from the 6.4 per cent recorded in 2013. Similarly, real GDP growth in the non-oil sector is expected to remain strong, driven largely by agriculture, trade and services, while activities in the oil sector are projected to recover in 2014. Inflation is projected to decline to 7.0 per cent by end of 2014, down from the 8.0 per cent recorded at end December 2013. The forecast is based on the assumption that the Bank would sustain its tight monetary policy stance, in view of the forthcoming 2015 elections, and that the trend of declining food prices, arising from higher rice and wheat production, would persist. The downside risks to developments in the domestic economy include a continued decline in oil revenues due to changes in the international oil market, lack of fiscal prudence induced by increasing political activities, unabated security challenges in the northern part of the country, likely capital flow reversals as the Federal Reserve continues implementing its tapering programme, and uncertainties about the pace of recovery in the global economy.

Money market rates are expected to remain stable in the first half of 2014, albeit at a slightly higher level than was recorded in the second half of 2013. Expectations of an increased liquidity surfeit in the system would likely be counter-balanced by tight monetary policy in order to maintain price stability.

The biometric solution to address the challenges associated with a unique identifier in the Nigerian banking industry is expected to be deployed in the first half of 2014. This would enhance the application of the “Know Your Customer” (KYC) principle, with its associated benefits in the reduction of fraud and credit risk.

In the area of regulation, further measures are expected to address issues relating to capacity in the banking system to further enhance the resilience of the financial system. These measures include the development of a competency framework for the banking industry, the issuance of regulations for holding companies, and the automation of the 'fit and proper persons' portal.

It is envisaged that the system will remain resilient and capable of dealing with emerging challenges, despite short-term risks to financial stability.

Box 1: Guidance Note on Regulatory Capital

REGULATORY CAPITAL

1.0 Introduction

This document lays down new supervisory regulations for assessing the capital adequacy levels of banks and banking groups. The regulations[8] have been revised following the changes that were introduced in international regulations to take account of developments in risk management methodologies adopted by banks and the new policies and criteria underpinning supervisory activities.

The rules governing regulatory capital[9], the total capital requirement, the internal capital assessment process and risk concentration shall be applied on solo and consolidated bases.

The following regulation is applicable to all banks licensed by the CBN.

2.0 Composition of Regulatory Capital

This guideline establishes the procedures for calculating regulatory capital, which shall be the sum of

Capital elements:

Tier 1 Capital[10]

(a) Paid-up share capital/common stock

(b) Disclosed reserves[11]

Tier 2 Capital[12]

(a) Revaluation reserves

(b) General provisions/general loan-loss reserves

(c) Hybrid (debt/equity) capital instruments

(d) Subordinated debt

Less any

a) From Tier 1:

(i) Goodwill and increase in equity capital resulting from a securitization;

(ii) Investment in own shares (treasury stock);

(iii) Losses carried forward and losses for the current financial year; and

(iv) Intangible assets .

b) The following items shall be deducted 50% from Tier 1 and 50% from Tier 2 capital:

(i) Investments in unconsolidated banking and financial subsidiary companies;

(ii) Investments in the capital of other banks and financial institutions; and

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[8] More specifically, these are contained in International Convergence of Capital Measurement and Capital Standards, A Revised Framework. Comprehensive Version, published by the Basel Committee on Banking Supervision June 2006 (the "New Basel Capital Accord", or "Basel II")

[9] Regulatory capital shall not be less than the initial capital required for authorization to engage in banking.

[10] Subject to Tier 1 capital prudential filters, if any, as computed by the CBN.

[11] These include share premium, retained profit, general reserves, SMEEIS reserves, regulatory risk reserves and statutory/legal reserves .

[12] Subject to Tier 2 capital prudential filters, if any, as specified by the CBN.

(iii) Significant minority investments in other financial entities.

3.0 Qualifying Criteria for the Assessment of Capital Components

3.1 Tier 1 Capital

This includes only permanent shareholders' equity (issued and fully paid ordinary shares/common stock and perpetual non-cumulative preference shares) and disclosed reserves (created or increased by appropriations of retained earnings or other surpluses).

In the case of consolidated accounts, this also includes minority interests in the equity of subsidiaries which are not wholly owned. This basic definition of capital excludes revaluation reserves and cumulative preference shares.

There is no limit on the inclusion of Tier 1 capital for the purpose of calculating regulatory capital. For this purpose, the equity shares with the following characteristics are included in Tier 1 capital:

- Issued directly by the bank;
- Clearly and separately identified in the balance sheet;
- Have no maturity (are perpetual);
- Fully paid;
- Cannot be refunded beyond the possibility of the liquidation of a bank or a reduction of its share capital;
- Do not give to the holder rights to a minimum remuneration nor are there any clauses that require the compulsory payment of dividends;
- The dividends are paid solely out of distributable profits or retained earnings distributable; and
- Classified as equity instruments in accordance with IFRS.

3.2 Tier 2 Capital[13]

(a) Revaluation Reserve

i) **Fixed Asset Revaluation Reserve:** This relates to revaluation of fixed assets in line with market values reflected on the face of the balance sheet.

Prior approval of the CBN must be obtained by any bank before the recognition of the revaluation surplus on fixed assets in its books, which can only be done taking into consideration the following:

- The valuation must be made by qualified professionals and the basis of the revaluation as well as the identities of the valuers must be stated;
- The difference between the market and historic values of the eligible fixed assets being revalued shall be discounted by 55%;
- The revaluation of fixed assets is applicable to own premises only; and
- The revaluation of fixed assets (own premises only) is permissible within a

[13] The total of Tier 2 capital will be limited to a maximum of 33.3% of the total of Tier 1, while Tier 3 capital, innovative instrument and undisclosed reserve are not allowed for inclusion in regulatory capital.

minimum period of seven years after the date of the purchase of the asset or the last revaluation.

ii) **Other revaluation reserves:** The inclusion of other revaluation reserves created by the adoption of the International Financial Reporting Standards (IFRS) as part of the Tier 2 capital shall be subject to the limitations that will be specified by the CBN from time to time.

(b) General provisions/General loan-loss reserves

For the purpose of the standardized credit risk measurement approach, provisions or loan-loss reserves held against future (presently unidentified) losses are freely available to meet losses which subsequently materialize and therefore qualify for inclusion in Tier 2 capital. Provisions ascribed to specific or identified deterioration of particular assets or known liabilities, whether individual or group (collective), are excluded. Furthermore, general provisions/general loan-loss reserves eligible for inclusion in Tier 2 will be limited to a maximum of 1.25 percentage points of credit risk-weighted assets and subject to the approval of the CBN.

(c) Hybrid (debt/equity) capital instruments

These include financial instruments which combine characteristics of equity and debt capital. Essentially, they should meet the following requirements:

- They are unsecured, subordinated and fully paid-up;
- They are not redeemable at the initiative of the holder or without the prior consent of the CBN;
- They are available to participate in losses without the bank being obliged to cease trading (unlike conventional subordinated debt);
- Although the capital instrument may carry an obligation to pay interest that cannot permanently be reduced or waived (unlike dividends on ordinary shareholders' equity), it should allow service obligations to be deferred (as with cumulative preference shares) where the profitability of the bank would not support payment; and
- Hybrid capital instruments that are redeemable must have a maturity of **at least 10 years**. The contract must clearly specify that repayment is subject to authorization by the Central Bank of Nigeria. Cumulative preference shares, having these characteristics, would be eligible for inclusion in this category.
- The valuation must be made by qualified professionals and the basis of the revaluation as well as the identities of the valuers must be stated;
- The difference between the market and historic values of the eligible fixed assets being revalued shall be discounted by 55%;
- The revaluation of fixed assets is applicable to own premises only; and
- The revaluation of fixed assets (own premises only) is permissible within a minimum period of seven years after the date of the purchase of the asset or the last revaluation.

(d) Subordinated term debts

Subordinated debts issued by banks shall form part of the Tier 2 capital, provided that the contracts governing their issue expressly envisage that:

- In the case of the liquidation of the issuer, the debt shall be repaid only after all other creditors not equally subordinated have been satisfied;
- The debt has an original maturity of at least five years. Where there is no set maturity, repayment shall be subject to at least five years' prior notice;
- Early repayment of the liabilities may take place only at the initiative of the issuer and shall be subject to approval of the CBN;
- The contracts shall not contain clauses whereby, in cases other than those referred to in points (a) and (c), the debt may become redeemable prior to maturity; and
- During the last five years to maturity, a cumulative discount (or amortization) factor of 20% per year will be applied to reflect the diminishing value of these instruments as a continuing source of strength.

Unlike instruments included in hybrid capital above, these instruments are not normally available to participate in the losses of a bank which continues trading. For this reason, these instruments will be limited to a maximum of 50% of Tier 1 Capital.

4.0 Prudential Filters

Owing to the adoption of International Financial Reporting Standards (IFRS) by banks and for the purpose of calculating regulatory capital, the CBN may, from time to time, apply prudential filters.

5.0 Frequency of Reporting and Procedures for Calculating Individual Regulatory Capital

Banks shall continue to report on regulatory capital in accordance with the CBN's extant rules.