



CENTRAL BANK OF NIGERIA

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LETTER TO BANKS AND DISCOUNT HOUSES

INTERNAL CAPITAL GENERATION AND DIVIDEND PAYOUT RATIO

1.0 Globally, retained earnings have been identified as an important source of growing an institution's capital. Advantages of retained earnings include: being a source of long term finance; being easier and cheaper to raise than external finance; curtailment of financial risk; improving liquidity and profitability.

2.0 However it has been observed that rather than take advantage of this beneficial means of capital generation, some institutions pay out a greater proportion of their profits, irrespective of their risk profile and the need to build resilience through adequate capital buffers.

3.0 Prior to now, dividend payout policy for banks has been as stipulated in Section 16 (1) of BOFIA 2004 (as amended) and Prudential Guidelines for DMBs of 2010, which state that "Every Bank shall maintain a reserve fund and shall, out of its net profits for each year (after due provision made for taxation) and before any dividend is declared, where the amount of the reserve fund is:

- a. Less than the paid-up share capital, transfer to the reserve fund a sum equal to but not less than thirty per cent of net profits; or
- b. Equal to or in excess of the paid-up share capital, transfer to the reserve fund a sum equal to but not less than fifteen per cent of the net profit; provided that no transfer under this subsection shall be made until all identifiable losses have been made good.

3.1 Section 16 (3) also states that; Notwithstanding (a) and (b) of subsection (1), the Bank may, from time to time specify a different proportion of the net profits of each year, being lesser or greater than the proportion specified in paragraph (a) and (b) to be transferred to the reserve fund of a bank for the purpose of ensuring that the amount of the reserve fund of such bank is sufficient for the purpose of its business and adequate in relation to its liabilities.

3.2 Subsequently Section 17 (1) stipulates that no bank shall pay dividend on its shares until-

All its preliminary expenses, organizational expenses, shares, selling commission, brokerage, amount of losses incurred and other capitalized expenses not represented by tangible assets have been completely written off; and adequate provisions have been made to the satisfaction of the bank for actual and contingency losses on the risk assets, liabilities, off balance sheet commitments and such unearned incomes as are derivable therefrom.


3.3 While these regulations are aimed at building statutory reserves for supervised banks, in view of the dynamism, rapid changes and emerging risks on the horizon, there is a need to proactively address these risks.

4.0 In order to facilitate sufficient and adequate capital build up for banks in tandem with their risk appetite, the following directives will now apply:

1. Any Deposit Money Bank (DMB) or Discount House (DH) that does not meet the minimum capital adequacy ratio shall not be allowed to pay dividend.
2. DMBs and DHs that have a Composite Risk Rating (CRR) of "High" or a Non Performing Loan (NPL) of above 10% shall not be allowed to pay dividend.
3. DMBs and DHs that meet the minimum capital adequacy ratio but have a CRR OF "Above Average" or an NPL ratio of more than 5% but less than 10% shall have dividend pay-out ratio of not more than 30%.
4. There shall be no regulatory restriction on dividend pay-out for DMBs and DHs that meet the minimum capital adequacy ratio, have a CRR of "low" or "moderate" and a NPL ratio of not more than 5%. However it is expected that the Board of such institutions will recommend payouts based on effective risk assessment and economic realities.
5. No DMB or DH shall be allowed to pay dividend out of reserves.
6. Banks shall submit their Board approved dividend payout policy to the CBN before the payment of dividend shall be permitted.

All ratios shall be based on financial year averages.

This circular takes immediate effect.



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