

DRAFT
BANKING
SUPERVISION
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REPORT

2008

TABLE OF CONTENTS

CHAPTER ONE: DEVELOPMENTS IN THE FINANCIAL SERVICES INDUSTRY

- 1.01 Update on the Cooperation Among the Regulatory and Supervisory Agencies in West and Central Africa
- 1.02 Update on e-FASS
- 1.03 Developments in the Other Financial Institutions Sub-Sector
- 1.04 Update on Banking Sector Reforms
- 1.05 Implementing the CBN Code of Corporate Governance
- 1.06 Developments in Anti-Money Laundering Efforts

CHAPTER TWO: SUPERVISORY ACTIVITIES

- 2.01 Off-site Supervision of Banks and Discount Houses
- 2.02 On-site Supervision of Banks
- 2.03 Supervision of Other Financial Institutions
- 2.04 Highlights of the Activities of the Bankers' Committee

CHAPTER THREE: ISSUES IN SUPERVISION

- 3.01 Efforts of the CBN at Averting Credit Crunch in Nigeria
- 3.02 Resident Examiner: Concept and Regulation
- 3.03 Microfinance Certification Programme
- 3.04 Curbing the Activities of Illegal Fund Managers/Wonder Banks
- 3.05 Efforts Towards Implementing Basel II

CHAPTER FOUR: FRAMEWORK FOR SUPERVISION

- 4.01 Evolution of Banking Supervision in the Central Bank of Nigeria
- 4.02 Regulatory Framework for Credit Bureaux in Nigeria
- 4.03 Efforts Towards Introducing Non-Interest Banking in Nigeria

CHAPTER FIVE: PERFORMANCE TRENDS IN THE BANKING SYSTEM

- 5.01 Balance Sheet Structure and Growth Rates
- 5.02 Deposits and Liquidity in Banks

- 5.03 Loans and Other Assets Quality in Banks
- 5.04 Banks' Capital Adequacy
- 5.05 Banks' Profitability
- 5.06 Market Share of the Ten Largest Banks
- 5.07 Efficiency of Operations in Banks
- 5.08 Other Financial Institutions

CHAPTER SIX: CAPACITY BUILDING FOR SUPERVISION

- 6.01 Training and Development
- 6.02 Interim Capacity Building for MFB Operators and Directors
- 6.03 BSD Conference and Retreat
- 6.04 OFID Retreat

APPENDICES

- 1. Circulars to All Banks and Other Financial Institutions in 2008
- 2. Major Financial Indicators of Individual Banks
- 3. Glossary

FOREWORD

The relative stability of the Nigerian banking system, in the midst of the global financial crisis, is not unconnected with the banking system reforms, particularly the consolidation programme, which greatly strengthened the banks. Another bolstering factor for the resilience of the banking industry had been the proactive regulation of the system, which is complemented with stringent supervision.

In the sustained efforts of the Central Bank of Nigeria (CBN) to entrench a strong banking system, various improvements to the supervisory process are being explored. In this regard, risk-based and consolidated supervision are being vigorously implemented to complement existing regulatory measures such as the contingency planning framework for systemic distress and the CBN Code of Corporate Governance for Banks in Nigeria. Also, the deployment of the electronic Financial Analysis and Surveillance System has significantly improved the quality of financial reporting by banks.

To further strengthen banking supervision in Nigeria, plans had been concluded to deploy Resident Examiners to banks to monitor their activities on a daily basis.

The CBN also took some monetary policy measures intended to avert credit crunch in the banking system. To this end, the discount window was expanded to include eligible instruments such as commercial paper and bankers acceptances, in addition to treasury bills. The Monetary Policy Rate was reduced from 10.25 percent to 9.75 percent; Cash Reserve Requirement from four to two percent; and Liquidity Ratio from 40 to 30 percent.

The quest by the CBN for the safety and soundness of the financial system is not limited to the deposit money banks but also to other financial institutions under its purview. Thus, the CBN took steps to build the capacity of operators in the nascent microfinance banking sub-sector to ensure that the institutions are professionally run to achieve the underlying economic policy objective of poverty reduction and sustain overall public confidence in the Nigerian financial system.

The effort to strengthen the Nigerian banking system is consistent with the Financial System Strategy FSS 2020 programme aimed at fostering a strong and robust domestic

financial system that would serve as a catalyst for the emergence of Nigeria as one of the top 20 economies in the world by the year 2020.

With the benefit of hindsight, and experience of 50 years of banking regulation in Nigeria, the CBN is adequately positioned to keep a close watch on the Nigerian banking system and would continue to take necessary steps to keep the system sound and stable.

Tunde Lemo
Deputy Governor
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PREFACE

This 12th edition of the Banking Supervision Annual Report highlights the activities of the supervisory departments of the CBN as well as major developments in the Nigerian financial system in 2008.

The report is divided into six chapters. Chapter one details developments in the banking industry, which include updates on the banking sector reform, electronic Financial Analysis and Surveillance System, banks' compliance with the CBN Code of Corporate Governance as well as cooperation among the various regulatory and supervisory agencies. Developments in the fight against money laundering and combating the financing of terrorism are also covered in this chapter.

Chapter two highlights the on-site and off-site supervision of banks and other financial institutions as well as the activities of the Bankers' Committee during the year.

Topical issues that dominated financial discourse in 2008 are covered in chapter three. Efforts of the CBN at averting the effect of the credit crunch, which has affected the global financial system, are also documented in this chapter. Other issues highlighted in the chapter are the resident examiner programme, efforts of the CBN towards implementing Basel II, curtailing the activities of illegal fund managers and the microfinance certification programme.

Chapter four reviews the development of private credit bureaux and the efforts towards introducing non-interest banking in Nigeria.

The performance of the banking industry and the other financial institutions sub-sector is reported in chapter five. This chapter also provides a detailed analysis of the trend of assets and liabilities, earnings and profitability, and efficiency of operations, among others.

The CBN sustained its efforts to build capacity through staff training and development during the year. This stems from its resolve to enhance, on a continuous basis, the skills of its supervisors, thus, assuring their ability to cope with the dynamics of supervision. The activities of the CBN in this area are captured in chapter six. This chapter also

highlights the conferences/retreats organized by both the Banking Supervision and Other Financial Institutions Departments in 2008.

We are deeply grateful to the Management of the CBN and all the contributors to this edition of the report for their support. Our heartfelt appreciation also goes to the members of the Banking Supervision Annual Report Committee, whose tireless efforts ensured the early publication of the report. The comments from readers have challenged us to continuously seek improvement in the standard of our report. We, therefore, welcome such comments and suggestions.

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CHAPTER ONE: DEVELOPMENTS IN THE FINANCIAL SERVICES INDUSTRY

1.01 UPDATE ON COOPERATION AMONG THE REGULATORY AND SUPERVISORY AGENCIES

The various regulatory and supervisory agencies sustained their cooperation during the year. Highlights of their activities are presented below:

CBN/NDIC COMMITTEE ON SUPERVISION

The CBN/NDIC Committee on Supervision held a sensitization workshop on consolidated supervision for management staff of the CBN, NDIC and banks in August 2008. It also commenced the review of the Framework for Contingency Planning for Banking Systemic Distress and Crisis.

Furthermore, some of the work hitherto done by the CBN/NDIC Technical Committee on Supervision, particularly the review of the Framework for Risk- Based Supervision and Consolidated Supervision, was assigned to the Supervisory Methodology Unit created by the CBN to develop, implement and support a risk-based supervision regime.

COMMITTEE OF BANKING SUPERVISORS OF WEST AND CENTRAL AFRICA

The Central Bank of The Gambia hosted the 14th Annual General Meeting of the Committee of Banking Supervisors of West and Central Africa, in October 2008. The three-day meeting was attended by 40 participants from the banking supervision departments of the central banks of the Democratic Republic of Congo, Ghana, Guinea, Liberia, Nigeria, Sierra Leone, Sudan and The Gambia as well as two banking commissions (Central African Banking Commission and the WAMU Banking Commission). Representatives of the Nigeria Deposit Insurance Corporation attended the meeting as observers. Resource persons from Societe Generale Bank (France) and Valtech (India) presented papers on Anti-Money Laundering and Terrorism Financing, and Supervisory Challenges of Outsourcing in Banks, respectively.

The opening ceremony was presided over by Mr. Basiru Njai, First Deputy Governor of the Central Bank of The Gambia, who stressed the need to improve the laws of finance

and increase cooperation and coordination among supervisors within the sub-region in the face of the current global financial/economic crisis.

Earlier on, the outgoing Chairman of the Committee, Mr. L. N. Elongo of the Central Bank of the Democratic Republic of Congo, restated the objectives and reviewed the activities of the Committee in the areas of cooperation, harmonization of supervisory practices, experience-sharing and training. He recalled that the meeting provided an opportunity to undertake an in-depth analysis of the challenges confronting member countries. He observed that the Committee had made significant strides towards achieving its mandate in its 14 years of existence, through:

- Regular meetings of the committee and participation in the activities of the Basel Committee for Banking Supervision;
- Harmonization of prudential regulations within the sub-region;
- Improved information-sharing among members; and
- Organization of seminars on topical supervisory issues, in collaboration with the Financial Stability Institute (FSI) of the Basel Committee, Switzerland.

Mr. Ousman A. Sowe, Director of Banking Supervision of Central Bank of The Gambia, was elected the new Chairman of the Committee. During his tenure, he would be expected to:

- Coordinate the process leading to the adoption and signing of the Committee's Charter by members;
- Ensure a fully operational secretariat for the Committee;
- Adopt/implement the harmonization of supervisory processes as recommended by the Sub-committee on the Harmonization of Prudential Regulation within the sub-region;
- Organize training programmes for bank supervisors in addition to the annual training programme held in collaboration with the FSI;

- Develop a uniform reporting format for supervisory processes that would ensure comparison across member states;
- Encourage the signing of memoranda of understanding (MOU) among members to foster cooperation on consolidated supervision; and
- Contact inactive members with a view to activating their participation.

The next Annual General Meeting of the Committee would be hosted by Guinea, in 2009.

1.02 UPDATE ON eFASS

Highlights of the implementation efforts on eFASS during the year are indicated below:

Requirements for Risk-based Supervision and Consolidated Supervision

The eFASS Implementation Committee set up a sub-committee to identify other enhancements needed in the software to meet the requirements of risk-based supervision and consolidated supervision.

Automation of Processing of Annual Accounts

The CBN approved the development of a platform for the electronic submission and processing of annual accounts of banks and discount houses. Consequently, a Sub-committee of the eFASS Implementation Committee was set up to articulate the Software Requirements Specification (SRS) for onward delivery to the developer.

Set-up of Replicating Server in the NDIC

The installation of the eFASS replicating server in the NDIC began during the year.

eFASS Software Marketing Agreement

The eFASS Software Marketing Agreement was signed by all the parties concerned after incorporating the amendments proposed. More central banks have shown interest in the software and marketing discussions are at various stages. Similarly, discussions were ongoing with the developer with a view to incorporating the latest technology in the software to make it more robust.

Connectivity of Other Financial Institutions (OFIs) to eFASS

The eFASS could not be fully deployed to the reporting institutions (RIs) in the OFI sub-sector due to some challenges relating to capacity building. For instance, the PMIs and the FCs could not conclude writing the conversion programmes of their applications to XML templates. In order to address the challenges, further training on the eFASS XML return template was conducted for the staff of the RIs in July 2008.

As at end 2008, only 19 of the 99 PMIs were registered in the eFASS database, while the FCs were yet to complete the writing of conversion programmes of their applications to the XML template. The parallel rendition of returns is expected to commence by January 2009.

Training on eFASS Query Builder

The planned training programme on the eFASS query builder, which was meant to enhance the capacity of the users to generate dynamic reports from the eFASS database, could not take place during the year due to congestion in programmes/activities. It is expected that the training would take place in 2009.

1.03 DEVELOPMENTS IN THE OTHER FINANCIAL INSTITUTIONS (OFI) SUB-SECTOR

The reforms in the OFI sub-sector of the Nigerian financial system continued in 2008, with significant developments, as highlighted below:

Microfinance Banks (MFBs)

Three hundred and eight of the 607 erstwhile community banks that successfully converted to MFBs obtained final licences. The final licencing of the remaining 299 MFBs with provisional approval had not been concluded. This was largely due to delays in registering increases in capital, change of name, replacement of directors and the reluctance of the institutions to pay penal charges for non-submission of statutory returns at the Corporate Affairs Commission (CAC).

One hundred and twenty-seven applications for MFB licences were received in 2008, bringing the total number, since the MFB policy was launched, to 249. One hundred and thirty-eight of the applications received final licences, 95 were granted approvals-in-principle (AIPs), while 16 were being processed.

Three Deposit Money Banks (DMBs) received approval to establish microfinance bank subsidiaries/associated companies. The total number of DMBs involved in microfinance through either the establishment of subsidiaries or in-house units was 10 at end 2008 (see Table 1). Two of the applications received during the year involved foreign investors, bringing the total number of MFBs with significant foreign ownership/participation to three (see Table 2). The number of approved MFBs as at end 2008 was 840.

The CBN inaugurated the Committee of Microfinance Banks in Nigeria (COMBIN) as a platform for interaction between regulators and the operators in the microfinance sub-sector. The Committee comprised the Managing Directors/Chief Executive Officers of all MFBs and officials of the regulatory agencies.

The certification programme for the training of supervisors, directors and operators of the MFBs was approved in December 2008. The programme is scheduled to commence in 2009.

The CBN, in collaboration with the NDIC, drew up an Exit Strategy for the 229 CBs that failed to convert as at December 31, 2007. Special examinations of the failed CBs to ascertain the extent of insolvency and the veracity of claims, was undertaken in September 2008, setting the stage for the implementation of the Exit Strategy.

Bureaux De Change (BDCs)

In addition to 64 outstanding applications for BDC licences as at end 2007, 589 others were received in 2008. Three hundred and forty-five were granted final licences, 216 received AIPs, while 92 were being processed. The total number of approved BDCs at end 2008 was 1,264 as against 703 at end 2007.

Finance Companies (FCs)

Two finance companies were granted final licences, bringing the total number of finance companies to 113.

The activities of the illegal fund managers/'wonder banks' attracted the attention of regulatory authorities during the year. To address the menace posed by the illegal fund managers/ 'wonder banks', an inter-agency committee comprising the CBN, Securities and Exchange Commission, Nigeria Deposit Insurance Corporation, (CAC), Economic and Financial Crimes Commission and the Nigeria Police, was inaugurated in February 2008.

As part of the on-going reforms in the financial system, a draft paper to reposition the FCs is being articulated by the CBN.

Primary Mortgage Institutions (PMIs)

Approval was granted for the establishment of four new PMIs including a subsidiary of a DMB. The approvals brought the total number of PMIs to 99, while 14 others were being restructured. The number of DMBs with PMI subsidiaries was 12 as at year end (see Table 3).

Efforts continued in the drive to restructure and reposition the mortgage/housing finance sub-sector, through a comprehensive reform package, designed to redress the perennial under-performance of the licensed PMIs. The reforms are expected to facilitate the implementation of the various initiatives arising from the work of both the Presidential Committee on Affordable/Social Housing and the FSS 2020 Mortgage Sector Committee.

Development Finance Institutions (DFIs)

The regulation of DFIs received a boost with the issuance of the “Prudential Standards and Guidelines for African Development Banks and Finance Institutions” and the selection of Nigeria’s Bank of Industry Ltd as one of the African DFIs for the pilot scheme on the rating of DFIs. The document, which was drawn up under the aegis of the Association of African Development Finance Institutions (AADFI), was expected to serve as the basis for regulating these institutions for enhanced operational sustainability and greater effectiveness in fulfilling their institutional mandates.

TABLE 1

DEPOSIT MONEY BANKS INVOLVED IN MICROFINANCE BANKING

S/N.	DEPOSIT MONEY BANK	SUBSIDIARY/ VEHICLE	PERCENTAGE HOLDING
1.	United Bank for Africa Plc	UBA MFB Ltd	100
2.	First Bank of Nigeria Plc	FBN MFB Ltd	100
3.	Intercontinental Bank	Blue	35

	Plc	Intercontinental MFB Ltd	
4.	Ecobank Plc	Accion MFB Ltd	18.47
5.	Zenith Bank Plc	Accion MFB Ltd	10
6.	Citibank Ltd	Accion MFB Ltd	19.9
7.	Afribank Nigeria Plc	Afribank MFB Ltd	100
8.	Oceanic Bank Int'l. Plc	Microfinance Unit/Dept	Not Applicable
9.	Diamond Bank Plc	Microfinance Unit/ Dept	Not Applicable
10.	Union Bank of Nigeria Plc	Microfinance Unit/ Dept	Not Applicable

TABLE 2
MICROFINANCE BANKS WITH SIGNIFICANT FOREIGN
OWNERSHIP/PARTICIPATION

S/N.	NAME	FOREIGN SHAREHOLDERS	PERCENTAGE SHAREHOLDING
1.	Accion MFB Ltd.	Accion Investments Inc., USA	24.03%
		International Finance Corporation (IFC), USA	12.06%
2.	Blue Intercontinental MFB Ltd.	Blue Employee Benefits Pty Ltd., South Africa	65%
3.	AB MFB (Nig.) Ltd.	Access Microfinance Holding AG, Germany	50.1%
		African Development Bank (AfDB)	12.45%
		Impulse Microfinance Fund, Belgium	15%
		International Finance Corporation (IFC), USA	10%
		KfW Development Bank, Germany	12.45%

**TABLE 3
DEPOSIT MONEY**

BANKS WITH PRIMARY MORTGAGE INSTITUTION (PMI) SUBSIDIARIES

S/N.	DEPOSIT MONEY BANK	PRIMARY MORTGAGE INSTITUTION
1.	Diamond Bank Plc.	Diamond Mortgages Limited (formerly Dominium Building Society Limited)
2.	First Bank of Nigeria Plc.	FBN Mortgages Limited
3.	Guaranty Trust Bank Plc.	GT Homes Limited (formerly New Patriot Building Society Limited)
4.	Intercontinental Bank Plc.	Partnership Savings and Loans Limited
5.	Oceanic Bank International Plc.	Oceanic Homes Savings and Loans Limited (formerly Fine Homes Limited)
6.	Platinum Habib Bank Plc.	PHB Mortgages Limited (formerly Finacorp Building Society Limited)
7.	Skye Bank Plc.	EIB Building Society Limited
8.	Spring Bank Plc.	Spring Mortgages Limited (Guardian Mortgages Limited)
9.	Sterling Bank Plc.	Safe Trust Savings and Loans Limited
10.	Union Bank of Nigeria Plc.	Union Homes Savings and Loans Limited
11.	Wema Bank Plc.	Wema Savings and Loans Limited
12.	Access Bank Plc.	Access Homes & Mortgages Limited

1.04 UPDATE ON THE BANKING SECTOR REFORMS

Introduction

The CBN continued to consolidate on the gains of the banking sector reform programmes, introduced in 2004, to strengthen local banks and enhance their international competitiveness. Specifically, the following milestones were attained in 2008:

Purchase and Assumption

The CBN and the NDIC sustained the Purchase and Assumption (P & A) arrangement for the resolution of insolvent banks that had their licences revoked on January 16, 2006, following their inability to scale through the banking sector consolidation programme.

In accordance with the terms of the P & A arrangement, the CBN, as at December 31, 2008, had issued Promissory Notes (P-Notes) totaling N40.45 billion to the acquiring banks to cover the shortfall between the assumed deposit liabilities and the cherry-picked assets of the 11 failed banks for which final court orders had been obtained for their liquidation.

Resolution of Private-Sector Deposits

S/N	Acquiring Bank	Assumed Bank	Assumed Private Sector Deposits	Value Of Fixed Assets Cherry Picked	NDIC Premium Released	Promissory Notes Released By CBN	Total Deposits Equivalent Accessed

			(1) =N=	(2) =N=	(3) =N=	(4) =N=	(2)+(3)+(4) =N=
1.	Ecobank	Allstates	22,660,655,731	2,699,165,274	1,761,394,788	12,431,350,911	16,891,910,973
2.	UBA	Trade	7,372,134,218	1,644,434,000	414,500,446	3,954,818,776	6,013,753,222
3.	Afribank	Lead	7,336,028,000	1,016,501,000	40,000,000	5,993,022,465	7,049,523,465
4.	Afribank	Assurance	5,091,120,000	1,754,135,588	600,000,000	2,909,488,947	5,263,624,535
5.	UBA	Metropolit an	2,553,846,496	250,391,690	101,185,000	1,667,272,699	2,018,849,389
6.	UBA	City Express	10,886,597,255	680,032,000	222,000,000	8,015,389,574	8,917,421,574
7.	Ecobank	Hallmark	12,045,315,966	10,758,715,956	300,000,000	107,000,000	11,165,715,956
8.	UBA	African Express	1,354,373,636	150,000,000	40,000,000	873,965,656	1,063,965,656
9.	Zenith	Eagle	890,807,327	1,110,291,179	-	Not applicable	1,110,291,179
10.	UBA	Gulf	8,523,645,617	450,000,000	100,000,000	4,159,019,913	4,709,019,913
11.	UBA	Liberty	1,906,525,025	1,036,120,000	50,000,000	338,371,358	1,424,491,358
	TOTAL		80,621,049,271	21,549,786,687	3,629,080,234	40,449,700,299	65,628,567,220

Also during the year, Ecobank Nigeria Plc acquired African International Bank Limited and commenced the verification of the bank's deposits. In that regard, the CBN was committed to issuing P-Notes totaling N10.9 billion, out of which it had issued N2.72 billion as at December 31, 2008.

The Federal High Court, in February 2008, ruled that the CBN should restore the operating licence of Societe Generale Bank Nigeria Ltd (SGBN) and give the bank time to recapitalize. As a result of this, the number of banks that had their licenses revoked dropped from 14 to 13.

As at end 2008, final court orders for the liquidation of two failed banks (Fortune International Bank Plc and Triumph Bank Plc) had not been obtained. Consequently, the banks could not be offered for resolution under the P & A arrangement.

Resident Examiner Programme

In order to strengthen the effectiveness of supervision, the CBN, in July 2008 approved the introduction of the Resident Examiner Programme with effect from January 2009. The programme was designed to enhance supervisors' knowledge of the banks, their risk profiles and to provide timely and continuous evaluation of their operations.

The CBN would continue to introduce appropriate regulations to ensure that the gains of the reform are sustained.

1.05 IMPLEMENTING THE CBN CODE OF CORPORATE GOVERNANCE

Introduction

The implementation of the CBN Code of Corporate Governance for banks in Nigeria has contributed immensely towards the improvement of governance practices in the industry. A survey conducted by the International Finance Corporation (IFC) in late 2007 indicated that the industry had witnessed greater commitment to corporate governance principles,

as all Nigerian banks had embarked on one or more corporate governance initiatives.

The survey found that:

- proper structure and formality in board processes existed in most banks;
- over 90 percent of board members possessed relevant qualifications;
- board committees had been created;
- formal board performance evaluation process was in place;
- transparency and information disclosure had improved; and
- audit functions and risk management procedures had improved.

Furthermore, family dominance and government influence in banks as well as industry ratio of non-performing director-related loans had substantially reduced.

Concerns and Challenges

Notwithstanding these achievements, the implementation of the Code posed some challenges, prominent among which were:

- ambiguities regarding the appointment and shareholding status of independent directors;
- government equity ownership;
- qualifications of the Head of Internal Audit; and
- signatories to statutory returns.

To address these challenges, the CBN employed both on-site and off-site supervisory procedures. Banks were requested to submit monthly compliance status reports while examiners undertook quarterly on-site verification exercise.

On-site verification reports of some institutions indicated non-compliance with some provisions of the code such as:

- succession plan;
- whistle blowing procedure;
- independent directors;
- reporting and business relationships of internal and external auditors; and
- remuneration for Executive and non-Executive Directors.

Other provisions of the Code presented genuine difficulties on which the banks expressed concerns. These included provisions on the board audit committee,

certification of returns , external auditors' report on risk management, tenure of directors and auditors, and board appraisal.

These concerns and challenges are being articulated with a view to effecting necessary amendments to the Code.

1.06 REGULATORY EFFORTS IN THE FIGHT AGAINST MONEY LAUNDERING AND THE FINANCING OF TERRORISM

Stakeholders in the fight against money laundering and the financing of terrorism continued to collaborate at ensuring that the delisting of Nigeria from the list of non-cooperative and compliant territories (NCCTs) under the Financial Action Task Force (FATF) recommendations is sustained. To this end, the inauguration in July 2008, of the National Inter-Ministerial Committee on Anti- Money Laundering and the Combating the Financing of Terrorism (AML/CFT) provided a platform for enhanced cooperation among

the stakeholders. The Committee had met thrice and the synergy from its efforts had up-scaled AML/CFT activities.

Furthermore, year 2008 saw the effective implementation of relevant laws enacted in 2007 to enhance accountability and transparency in government business with a view to strengthening anti-corruption efforts in Nigeria. Such laws include:

- Nigeria Extractive Industry Transparency Initiative (NEITI) Act;
- Public Procurement Act;
- Federal Inland Revenue Services (FIRS) Act;
- The Four Tax Reforms Acts;
- CBN Act;
- Statistics Act; and
- The Fiscal Responsibility Act.

These laws have reinforced the efforts of the CBN at ensuring that money laundering activities through the banking system is minimized. Other efforts undertaken during the year include the following:

STATUTORY RETURNS ON AML/CFT

Financial Institutions and Designated Non-Financial Institutions continued to submit Currency Transaction Reports (CTRs), Suspicious Transactions Reports (STRs) and other related investigation reports to Economic and Financial Crime Commission/Nigeria Financial Intelligence Unit (EFCC/NFIU). The NFIU maintains a comprehensive database on all renditions from reporting entities.

INTERNATIONAL COOPERATION

Nigeria being a signatory to all relevant UN Conventions on Money Laundering and Terrorism and Terrorist Financing, and Convention against Corruption (UNCAC), had been taking steps to freeze assets of suspected terrorists. The CBN, on its part, had been cooperating with international agencies in the fight against ML/CFT. It had also been circulating names of individuals and corporate bodies suspected of involvement with terrorism as received from the United Nations from time to time.

i. Memorandum of Understanding (MoU)

As part of international cooperation, the NFIU had been signing Memorandum of Understanding (MoU) with other countries on behalf of Nigeria. In 2008, the NFIU signed

a total of eight MoUs with the underlisted countries while that with Australia was yet to be finalised:

- The Bahamas
- Netherland Antilles
- Romania
- Senegal
- South Africa
- The Russian Federation
- Ukraine
- Zimbabwe

ii. FATF Compliance Status

The mutual evaluation exercise of the AML/CFT regime in Nigeria was undertaken by The Inter-Governmental Action Group Against Money Laundering and Terrorism Financing (GIABA) between September 24 and October 5, 2007. The report of the exercise issued in May 2008, showed that out of the 40+9 FATF Special Recommendations, Nigeria was rated Non-Compliant (NC) in 20, Partially Compliant in another 20 and Largely Compliant in seven, while two were considered not applicable.

CRIMINALISATION OF TERRORISM

Notwithstanding the powers of the CBN to freeze bank accounts of entities suspected to be involved with terrorism and/or terrorist financing, and the joint investigation responsibility with the NFIU, EFCC, Department of State Services, Nigeria Intelligence Agency, Nigeria Police and NDLEA, terrorism and terrorist financing have not been adequately criminalized under the Nigerian legal framework. Nigeria ratified the UN Convention for the Suppression of the Financing of Terrorism on April 28, 2003, and had subsequently ratified seven out of the 13 UN Terrorism Conventions. However, Section 15 of the EFCC (Establishment) Act, 2004, was the only attempt by Nigeria to criminalize the financing of terrorism.

To strengthen the capacity of the EFCC, a draft anti-terrorism bill incorporating the requirements of the UN Security Council Resolutions 1267 and 1373, including specific provisions regarding freezing, confiscation and repatriation of terrorist related funds/assets, had been submitted to the National Assembly for enactment into law.

SANCTIONS

The CBN continued to enforce and monitor compliance with AML/CFT laws, while enforcing sanctions and penalties for breaches. As a result, financial institutions in Nigeria have realized the importance of adhering to AML/CFT laws and regulations and the enormous consequences of any breach.

CAPACITY BUILDING

The CBN continued to build the capacity of its staff on AML/CFT issues. It also encouraged financial institutions to expose their staff to all AML/CFT laws, legislations and related obligations so as to ensure compliance at all times.

CONCLUSION

The image of the country is improving as a result of concerted efforts to reform the relevant bodies responsible for AML/CFT, and check the activities of drug traffickers, advance fee fraud perpetrators and money launderers. The efforts are bearing fruit as public confidence in the financial institutions and law enforcement agencies is rebounding.

CHAPTER TWO: SUPERVISORY ACTIVITIES

2.01 OFF-SITE SUPERVISION OF BANKS AND DISCOUNT HOUSES

The CBN applied appropriate measures in the supervision of banks and discount houses during the year. The off-site supervisory activities focused on the following major areas:

(i) Statutory Returns

The periodic rendition of statutory returns of banks and discount houses was done electronically through the electronic Financial Analysis and Surveillance System (eFASS). The returns were analysed to ascertain the financial condition and performance of banks and discount houses, using financial indicators such as asset quality, liquidity, capital adequacy, earnings and loans to deposits ratios. Appropriate regulatory actions were taken to address areas of concern.

(ii) Board and Management

The CBN approved the appointment of 42 persons into the boards and top management positions of some banks and discount houses. It turned down the appointment of a few others on grounds of insufficient experience and unfavourable references from other regulatory and security agencies, among other reasons. Nineteen resignations from boards and top management positions of some banks were also recorded.

An Interim Management Committee that was put in place by the CBN in one of the banks in 2007 gave way to a substantive board of directors, following the successful acquisition of the bank.

(iii) Financial Statements

A total of 18 audited financial statements of banks and discount houses were approved for publication in line with the provisions of BOFIA.

(iv) Banks' Branch Network

Approvals were granted by the CBN for the opening of branches and cash centres during the period. The total number of branches and cash centres in operation as at December 31, 2008, was 5,134 as against 4,579 in the preceding year. Branch expansion was closely monitored to ensure that banks did not utilise depositors' funds for such investments.

(v) Credit Risk Management System (CRMS)

As at end 2008, the web-enabled CRMS database had an outstanding balance of N3.11 trillion, involving 60,273 borrowers, as against N2.13 trillion with a total customer base of 51,696 in the preceding year. The Naira value and number of borrowers recorded significant growths, reflecting increasing acceptability of the scheme and the growing confidence of the public in the banking system.

The guidelines for the establishment and supervision of private credit bureaux were issued by the CBN in October 2008. Three applications for licence had been received and were being processed as at year end.

(vi) Contraventions

In line with the provisions of BOFIA, the CBN continued to impose sanctions and enforce the payment of appropriate penalties on erring banks and discount houses.

(vii) Public Complaints against Banks

Several bank/customer-related complaints were received and referred to the Ethics and Professionalism Sub-committee of the Bankers' Committee for adjudication. Some complaints were resolved amicably among the parties.

(viii) Discount Houses

The performance of the five discount houses was monitored through the analysis of statutory returns using the eFASS platform. The guidelines on the operation of discount houses were revised during the year. The financial outlook of the discount houses as at year end remained strong.

(ix) Fraud and Forgeries

As at December 31, 2008, 1,974 cases of fraud and forgeries, amounting to N24.49 billion and various other sums in foreign currencies were reported by banks. Seven hundred and forty-six of the cases, amounting to over N6.37 billion were reported to have been successful. Arising therefrom, 316 staff of deposit money banks were dismissed and 220 others had their appointments terminated.

(x) Enforcing Statutory Requirements

(a) Liquidity Ratio

The minimum liquidity ratio for banks was reduced from 40 to 30 percent during the year. Compliance with the prescribed minimum liquidity ratio of 30 and 60 percent by banks and discount houses respectively, was closely monitored on daily and monthly basis. Two banks failed to meet the minimum prescribed liquidity ratio of 30 percent in the month of December 2008.

(b) Capital Adequacy Ratio

Compliance with the capital adequacy ratio requirement of banks and discount houses was also monitored throughout the year. In the month of December 2008 two banks failed to meet the minimum prescribed capital adequacy ratio of 10 percent.

(c) **Cash Reserve Requirement (CRR)**

Towards the achievement of monetary stability, the CBN continued to utilise cash reserve requirement (CRR) as a tool for monetary control, to complement the Open Market Operations. The CRR which was calculated fortnightly varied between three and four percent from January – August 2008, but was reduced to two percent with effect from September 2008. Overall, the banking system exhibited good fundamentals, remained strong and continued to perform its intermediation function.

2.02 ON-SITE SUPERVISION OF BANKS AND DISCOUNT HOUSES

The CBN and the NDIC continued to collaborate on the on-site examination of banks and discount houses. The CBN conducted target examination on 14 banks and five discount houses while the NDIC examined 10 banks in 2008.

The major findings of the target examination were:

i) **RISK ASSESSMENT**

Significant progress had been made by most banks in the establishment of enterprise-wide risk management frameworks. An appraisal of some of the frameworks showed that they were adequate in depth and coverage; where there were exceptions, the banks were advised to correct them.

ii) **CAPITAL ADEQUACY**

The banks had adequate capital to support their level of operations.

iii) **RISK ASSET QUALITY**

Significant growth in lending activities was observed in all the banks examined. Loan to deposit ratio was higher than the prudential requirement of 80 percent.

Credit administration was also poor in some banks. Facilities were allowed to exceed limits; while draw-down on facilities without full execution of loan agreements was still observed. Adequate review of facilities to ensure performance and/or provision was lacking while some delinquent facilities were not classified.

iv) **BOARD AND MANAGEMENT**

In many of the banks, Board and Management oversight needed improvement as evidenced by lapses in risk asset quality, corporate governance and abuse of insider-related facilities.

v) **EARNINGS**

Most of the banks reported increased earnings and profitability due to increased lending and business diversification.

vi) **LIQUIDITY MANAGEMENT**

The crisis in the capital market threatened the liquidity in the banking system due to banks' exposure to margin loans. The CBN took some actions, such as the stoppage of liquidity mop-up and reduction of liquidity ratio from 40 percent to 30 percent, to assist banks in their liquidity management.

vii) **FOREIGN EXCHANGE OPERATIONS**

Some of the banks had their foreign lines reviewed downward by their foreign correspondent banks, which reduced supply of foreign exchange in the market and exerted pressure on the exchange rate.

viii) **REPORT WRITING FORMAT**

The format of examination report witnessed a significant change during the period under review. The new format was redesigned to suit the risk-based supervisory approach, reduce its volume without sacrificing the facts of the examination and bring out vividly ranking and assessment parameters.

2.03 SUPERVISION OF THE OTHER FINANCIAL INSTITUTIONS SUB-SECTOR

In the pursuit of its mandate for the sustained safety, soundness and orderly development of the financial system, the CBN undertook both regulatory and supervisory activities on the Other Financial Institutions (OFIs) sub-sector. The scope of the supervisory work covered all 2,321 OFIs, comprising 840 Microfinance Banks (MFBs), 113 Finance Companies (FCs), 99 Primary Mortgage Institutions (PMIs), 1,264 Bureaux de Change (BDCs) and 5 Development Finance Institutions (DFIs). The total number represented an increase of 59.63 percent over 2007 position of 1,454.

Highlights of the on-site examination carried out during the year are as follows:

Microfinance Banks

Maiden/post conversion examinations were conducted on 430 MFBs to ascertain compliance with their business plans and the extant rules and regulations. The exercise showed that the institutions, on the average, were well capitalized and liquid. However, average portfolio-at-risk (PAR) of 33.4 percent far exceeded the prescribed maximum of 2.5 percent, indicating poor asset quality. The high level of PAR was largely accounted for by the non-performing credit facilities carried over from the community banking era by the erstwhile community banks that converted to microfinance banks. Also, corporate governance was generally weak in the MFBs. The reports indicated the need for greater focus on capacity building in order to assure the long-term sustainability of the MFB initiative.

Primary Mortgage Institutions

A total of 67 PMIs were examined in 2008 compared to 39 in 2007. The examinations, which were carried out under a collaborative arrangement with the NDIC, revealed a preponderance of commercial assets over mortgage assets, an indication that the operational focus of these institutions was still not on their core mandate to promote housing finance/mortgage banking. Regular prudential returns were received from 80 PMIs compared to 72 in 2007. Fifteen PMIs were penalized for late and non-rendition of returns and late submission of audited accounts for approval during the year.

Finance Companies

On site examinations on 77 out of the 113 licensed FCs revealed that 55 of the institutions were actively involved in finance company business, 22 had either ceased operations, were undergoing restructuring or mainly engaged in capital market activities.

Issues of regulatory concern included under-capitalization, poor corporate governance and skill gaps on the part of operators. In addition, pre-licensing inspections were carried out on three FCs that were operating with Approvals-in- Principle.

Bureaux de Change

Spot checks on 182 BDCs revealed that a number of the institutions were in breach of the set guidelines, especially in the area of the mark-up margins and the utilization of foreign exchange allocations.

Development Finance Institutions

The trend of deteriorating asset quality persisted in the four reporting DFIs that were examined during the year. The boards of the DFIs, which were dissolved by the Federal Government, were yet to be reconstituted as at end 2008.

The fifth DFI, following its privatization in 2006, was still undergoing restructuring as at year end.

2.04 HIGHLIGHTS OF THE ACTIVITIES OF THE BANKERS' COMMITTEE

The activities of the Bankers' Committee were geared towards strengthening the banking system. Highlights of the activities are stated below:

Bank Security

The Bankers' Committee handed over 26 Armoured Personnel Carriers to the Nigeria Police in furtherance of its commitment to complement efforts at securing and protecting the banks.

Common Accounting Year-end

The Bankers' Committee meeting of January 2008 adopted December 31st as the common financial year-end to take effect from December 2008.

Following developments in the economy, especially the misplaced perception that the interest rate trends were linked to the requirement of a common year-end, the CBN cancelled the policy vide a circular BSD/DIR/CIR/Gen/Vol.2/08 of August 25, 2008. Banks

and discount houses were thus, permitted to adopt year-ends as they deemed appropriate and inform the CBN accordingly.

Micro Credit Fund (MCF)

The Micro Credit Fund (MCF), an initiative of the Bankers' Committee, was launched by the President, Alhaji Umaru Musa Yar'adua, GCFR, on February 12, 2008, to ensure increased access to financial services by micro, small and medium enterprises. The MCF

was initiated to address some of the challenges experienced under the Small and Medium Enterprises Equity Investment Scheme (SMEEIS).

As at September 15, 2008, 12 state governments had set aside the sum of N9.48 billion for micro finance activities in their states while a number of them had made disbursements through selected MFBs and the Nigerian Agricultural Cooperative and Rural Development Bank.

Seminar for Judges

The 8th Annual National Seminar on Banking and Allied Matters for Judges was held in December 2008. The seminar with the theme: "Rule Of Law And Banking Practice In Nigeria" drew participants from the banks, CIBN, Judiciary, NDLEA, EFCC, the Nigeria Police, CBN and NDIC.

A total of six papers were presented at the seminar, namely:

- The Rule of Law And Economic Performance
- Corporate Governance and Ethics – Post Merger Challenges in Banks
- Banker-Customer Relationship
- Achieving Quicker Dispensation of Banking Cases in the Law Courts
- Private Banking Practices in Nigeria – Issues, Challenges and Prospects
- Enforcement of Fundamental Human Rights – Implication for Credit Administration and Management in Banks

Relevant issues affecting all the stakeholders were adequately addressed.

Self Regulation

One hundred and five disputes were resolved by the Ethics and Professionalism sub-committee, six cases were at various stages of resolution while four were taken to court.

Banks were encouraged by the Committee to adhere to Know-Your-Customer principles in addition to the provision of caution notices in the clearing of cheques. They were also advised to install strong controls over ATM operations.

The Bankers' Committee continues to provide a forum for bank Chief Executives to share information and experience.

CHAPTER THREE: ISSUES IN SUPERVISION

3.01 EFFORTS OF THE CBN AT AVERTING THE CREDIT CRUNCH IN NIGERIA

Credit crunch is a sudden reduction in the general availability of credit or a sudden increase in the cost of obtaining credits from financial institutions. It is caused by a combination of factors such as:

- Anticipated decline in the value of collaterals used to support credits;
- Increased perception of risk regarding the solvency of another bank within a banking system; and/or
- Changes in monetary conditions.

Credit crunch is usually preceded by a period of careless and inappropriate lending, which results in losses to investors in debt instruments and lending institutions as a result of the facilities going bad with the full extent of the delinquent facilities becoming unknown.

A major consequence of credit crunch is that it triggers liquidity crisis within an economy such that otherwise sound businesses are temporarily incapable of accessing required working capital financing or implementing cash flow projections.

The current credit crunch, which has affected the world financial system, arose as a result of the subprime mortgage crisis in the USA. This, however, turned into a worldwide economic downturn with devastating effects in the developed and developing worlds, thereby requiring immediate intervention of governments and financial system regulators in order to avert economic depression.

Incidentally, no Nigerian bank including the three foreign owned banks, as at end 2008, reported any subprime related exposures. It was on this basis that the regulatory

authorities in Nigeria affirmed that the country's banking system was not directly exposed to the subprime mortgage crisis.

However, stock prices tumbled significantly in Nigeria. The market capitalization of the Nigerian Stock Exchange crashed from over N13 trillion as at end 2007 to about N6 trillion as at end 2008. Furthermore, capital inflow into Nigeria understandably declined as some foreign banks recalled funds placed for on-lending in Nigeria to shore up their liquidity at home.

Regulatory Efforts by the CBN at Averting the Crisis

The CBN, in recognition of the growing financial and real linkages of the Nigerian banking system with the rest of the world, held a special Monetary Policy Committee meeting on September 18, 2008. The meeting reviewed the stance of monetary policy in the light of evolving economic and financial developments in the domestic and international economies.

The Committee noted that, in spite of the decline in the international price of crude oil, the economic fundamentals in Nigeria as at end August 2008, were strong, with foreign exchange reserves of US\$63 billion; growth in broad money (M2); growth in credit to the private sector at an annualized rate of 70.6 percent; and growth in non-oil GDP at over eight percent.

The CBN, however, acknowledged the increase in interest rate in August 2008, which was due to pressure of liquidity in the financial and inter-bank markets. To this end, it decided on a menu of actions to ensure that the financial system remained liquid.

Accordingly, the CBN decided to:

- Reduce the Monetary Policy Rate (MPR) from 10.25 percent to 9.75 percent;
- Reduce the Cash Reserve Requirement (CRR) from four percent to two percent;
- Reduce the Liquidity Ratio from 40 percent to 30 percent;
- Allow Repurchase (Repo) transactions against eligible securities for 90 days, 180 days and 360 days; and
- Buy and sell securities through the two-way quotes.

The CBN also affirmed its readiness to take appropriate actions to ensure the smooth functioning of the financial markets and the economy in general. In that regard, the CBN

suspended liquidity mop-up with effect from September 2008 and expanded the discount window to cover eligible securities other than Treasury Bills and Bonds for tenor up to 360 days.

The current global crisis, which started as a financial crisis in the USA has turned into a global economic crisis. Governments and regulatory authorities all over the world are concerned. There is unanimity that all jurisdictions should put in place necessary policies to avert a great depression akin to that of the 1930s.

The CBN, in response to possible threat enunciated a number of policy measures to contain the threat of credit crunch in the Nigerian banking system while the Securities and Exchange Commission (SEC) had earlier put in place a number of capital market safeguards to arrest the deteriorating stock values in the market.

3.02 DEPLOYMENT OF RESIDENT EXAMINERS TO BANKS

As part of the efforts to reposition the Nigerian banking system, the CBN had, at different fora, sensitized the industry of its intention to deploy Resident Examiners (REs) to deposit money banks. Accordingly, the CBN, on December 31, 2008, issued a circular to all deposit money banks, on the deployment of REs. REs are bank supervisors deployed by regulators to work at the operators' premises in order to monitor the observance of safe and sound banking practices and compliance with banking laws, regulations, guidelines and circulars issued by the regulatory authorities.

Objective of Resident Examination

The primary objective of deploying REs to banks is to provide real-time and continuous evaluation of the risks posed by the banks' operations. The programme places emphasis on the evaluation of a bank's risk management system and controls as opposed to performing transaction testing and asset valuation (e.g. loan reviews) that take place during conventional examinations. The REs would continually monitor and assess a bank's financial condition and risk management system through the review of management reports and meetings with bank officials.

This continuous access to Management and the risk management system allows REs to respond more quickly to emerging problems than would be possible with an annual examination approach. As a result of the REs' continuous interaction with the bank, the

regulatory authorities generally observe shifts in risk profile or strategic directions well in advance.

The duties of the Resident Examiner are to, among others:

- Continually monitor the bank's financial condition and risk management system through the review of management reports and meetings with bank officials;
- Determine the condition of a bank, using CAMELS parameters, and identify areas requiring corrective action;
- Evaluate the overall integrity and effectiveness of the bank's risk management system, using periodic validation through transaction testing;
- Obtain bank management's commitment to correct significant deficiencies and verify that corrective actions are taken in a timely and successful manner;
- Ensure that current and prospective issues that affect the bank's risk profile or overall condition are identified and appropriate supervisory strategies developed;
- Constantly communicate with the CBN and bank management on areas of concern. Communication with the bank includes formal and informal discussion and meetings, examination reports, and other documents;
- Maintain frequent contact with the business and risk managers of the bank to enable close monitoring of market conditions, investment and funding activities;
- Review the bank's risk selection and management processes with a view to taking action whenever necessary to correct weaknesses;
- Provide inputs on various regulatory issues that require broader responses with a view to strengthening the supervisory process;
- Monitor prompt implementation of previous examination exceptions;
- Ensure compliance with prudential/regulatory requirements such as liquidity ratio, capital adequacy, lending limits, CRMS etc; and
- Submit reports to the CBN on meetings attended with board and management.

Advantages of Deploying REs to Banks

The advantages of deploying resident examiners to banks include:

- Ensuring supervisory policies and processes that would tailor supervision to the unique characteristics of each bank. This would result in a customized supervisory

approach that reflects the banks' underlying risks in line with risk based supervision;

- Allowing the supervisor to respond appropriately to emerging risks and issues in individual institutions within business segments or across the banking industry as a whole;
- Enabling supervisors to monitor the observance of safe and sound banking practices and compliance with banking laws, regulations, guidelines and circulars issued by the regulatory authorities;
- Granting the supervisors timely and easy access to "whistle blower(s)" on critical happenings in the banks;
- Giving the supervisors better oversight on activities that cannot be effectively supervised by a combination of regular examinations and periodic rendition of returns;
- Quick resolution of the problems that may arise in intervening periods between examination and rendition of returns during which banks may undertake actions that could jeopardize supervisory effectiveness thereby causing problems in the system; and
- Prompt monitoring of corrective actions.

Exceptional Powers of the REs

In addition to the powers of regular Examiners, the Resident Examiner shall have power to:

- i. Attend Board meetings, Board Committees and Management meetings as an observer without hindrance, whenever deemed necessary; and
- ii. Call meetings of the bank's top management to discuss exception reports, and unsound and unsafe banking practices.

Challenges to the Deployment of REs

Expectedly, there are a number of challenges to the implementation of the RE programme. They include the possible perception as to whether the programme constitute a regulatory over-kill; the moral hazard of the supervisors being involved in the day-to-day management of the banks; the willingness of the banks to accept the programme; and the tendency of REs to be absorbed by the banks.

The CBN, mindful of the challenges, has put in place appropriate measures, including the limitation of the tenor of the REs to a maximum of two years and the prohibition of their employment by the bank during the period of the residency and two years thereafter.

The policy would become effective on January 5, 2009, when REs would be deployed to all the twenty four deposit money banks.

3.03 MICROFINANCE CERTIFICATION PROGRAMME

Introduction

The principal objective of the National Microfinance Policy, Regulatory and Supervisory Framework is to widen and deepen access to financial services for the large productive segment of the population that had been under-served or excluded from the services provided by the formal financial system.

To achieve this objective, the framework recognized the need to address the weaknesses that militated against the successful operations of the erstwhile community banks. Notable among these weaknesses were unsound corporate governance practices and skill gaps.

It was against this background that section 11.6 of the policy stipulates that a microfinance bank (MFB) management certification programme be put in place as a core element of the implementation strategy. This is to enhance the acquisition of appropriate operational skills by the operators and regulators of MFBs.

Objectives of the Certification Programme

The objectives of the certification programme are to:

- provide appropriate standards for the microfinance sub-sector, in line with international best practice;
- build the capacity of the microfinance practitioners;
- offer all microfinance practitioners the opportunity to be certified;
- create a strong professional and self sustaining microfinance certification process;
- build capacity for the regulators to enable them effectively supervise the microfinance banks; and
- ensure that microfinance banking is effectively carried out to meet the policy target of poverty reduction.

Types of Training

The certification programme would involve two types of training, namely:

- train-the-trainer programme, by international experts; and
- training of supervisors and operators of MFBs by WAIFEM, FITC and other training service providers.

The training programme, which would be partly funded by the CBN/NDIC, comprises a one-year pilot phase, followed by another phase of two years duration. The third phase entails the attainment of operational self sufficiency as the CBN/NDIC withdraw their subsidies and the programme becomes self-sustaining. There would be modular training programmes for trainers, regulators, supervisors, operators and directors under the certification scheme.

The trainers' module is directed towards expanding knowledge of best practice in microfinance. It is aimed at training and accrediting trainers of the microfinance operators and regulators. This module is to enhance the capacity of local instructors who, after certification, would be able to conduct training programmes for the certification of operators and regulators.

The training module for regulators and supervisors has been created to capture the skills and competencies critical to the effective examination and supervision of MFBs. It is

broken into four modules. The first two modules constitute the foundation level, while the last two shall make up the final level.

The training module for operators is structured to make them understand the basic factors that shape the environment of micro-entrepreneurs and the type of services they require to advance their socio-economic growth. The syllabus focuses on understanding basic credit and saving instruments, business skills, production technologies, marketing and corporate governance.

There would be two levels of six weeks each. Each level of the curriculum shall be examined twice a year during the months of April and October.

The training programme for non-executive directors shall be in streams of five working days and would focus on the microfinance concept as well as issues on good corporate governance.

The CIBN would be responsible for the examination and certification of the operators during the programme, while the training would be handled by accredited training service providers through a competitive bidding process and after undergoing the train-the trainer programme.

The CBN, in collaboration with development partners, would appoint a technical advisor to strengthen and bring appropriate skills to bear on the programme. The programme would be supervised by the National Microfinance Consultative Committee (NMFCC) under the Chairmanship of the Deputy Governor, Financial Sector Surveillance and would be coordinated by the Other Financial Institutions Department of the CBN.

3.04 EFFORTS BY THE CBN TO CURB THE ACTIVITIES OF ILLEGAL FUND MANAGERS/'WONDER BANKS'

Following the upsurge in the number of companies operating as illegal fund managers in the country, the CBN launched investigations into the activities of some identified companies. The investigations revealed that a number of the companies were involved in

the illegal business. As a preliminary measure, the balances in their bank accounts were determined, the accounts frozen; and the cases transferred to the EFCC for necessary action.

To enlighten the members of the public on the dangers of continued patronage of illegal fund managers, a list of the finance companies licensed by the CBN was published repeatedly in newspapers nationwide, and members of the public advised to transact business with licensed financial institutions only.

In order to adopt a holistic approach to deal with the menace, which had become an issue of national concern, an Inter-agency Committee on Illegal Fund Managers/'Wonder Banks' comprising the CBN, NDIC, SEC, CAC, EFCC and the Nigeria Police was established at the instance of the CBN, in February 2008, to enhance collaboration among the relevant agencies of government. The broad objectives of the Committee were to:

- put in place an appropriate mechanism for inter-agency collaboration to stop the activities of wonder banks and prevent a resurgence in the future;
- map out modalities for pursuing cases against offending companies at the Investments and Securities Tribunal; and
- establish procedures for returning the trapped funds to the depositors/investors of the illegal fund managers.

An implementation sub-committee was set up by the main committee to ascertain the liabilities of each of the companies and propose procedures for repaying the trapped funds. Following a newspaper publication, members of the public who had invested/deposited funds with the illegal fund managers/'wonder banks' submitted claims against 417 companies.

The resolution of the claims remained a huge challenge to the Committee as a result of the large number of companies involved, the quantum of claims, the complex verification procedures and the determination of the tangible assets of the illegal fund managers. Also, series of litigations had been instituted by the illegal fund managers and/or investors/depositors against the CBN, some banks and other regulatory bodies. Some of these litigations had led to the payment of claims on the order of the courts, thereby frustrating the efforts of the Committee.

However, measures had been put in place to surmount these challenges with a view to resolving the claims. Also, plans are underway to embark upon a massive nationwide media campaign in 2009, to discourage members of the public from patronising illegal finance companies.

The CBN would continue to intensify efforts to curb the activities of illegal fund managers/‘wonder banks’ in the country.

3.05 EFFORTS TOWARDS THE IMPLEMENTATION OF BASEL II

The CBN/NDIC, in 2008, continued with activities aimed at implementing Basel II in Nigeria. A memorandum to that effect was presented to the Bankers’ Committee to get its buy-in.

The Committee on Basel II identified some key success factors necessary for the implementation of the Accord. These included:

- Constitution of Basel II implementation organs, namely, Basel II Steering Committee, Basel II Project Team and Basel II Work Groups (with membership from regulators, external auditors and operators);
- Implementation of robust risk management systems in banks;
- Establishment of functional rating agencies;
- Conduct of gap and impact analysis;
- Collation of data on loss events;
- Capacity building for both regulators and operators;
- Strategy retreats to review progress and chart the way forward, at intervals;
- Awareness campaign; and
- Setting up of functional credit bureaux.

The Project Implementation Team is to:

- Implement the decisions of the Steering Committee;
- Carry out the day-to-day work for the implementation of Basel II;
- Serve as a clearing house for, and coordinate the activities of the work groups; and
- Liaise with the Steering Committee, the Work Groups and other stakeholders.

The preparatory work for implementation has reached an advanced stage with the planned constitution of the Steering Committee, the Project Team, the Work Groups and the engagement of consultants to facilitate the implementation of the Accord.

The seven work groups, which would work on a full-time basis, would cover such critical areas as credit risk, operational risk, market risk, asset securitization, supervisory review and regulatory framework, disclosure and accounting standards as well as law and rating agencies.

The Basel Committee on Banking Supervision (BCBS) and the Reserve Bank of India were contacted with a view to getting their support and gaining insight into the practical aspects of the implementation of Basel II. Also, it is expected that these institutions would provide necessary guidance and assistance in the areas of training, experience sharing and attendance of seminars and conferences organized by BCBS /FSI.

The implementation of the Basel II in Nigeria would be in line with the recommendation of the Basel Committee, that each national supervisor should consider carefully the benefits of the Basel Framework in the context of its own domestic banking system in developing a timetable and approach to implementation.

The Accord is expected to build on the solid foundation of prudent capital regulation, supervision and market discipline, and further enhance risk management and financial stability in the country.

CHAPTER FOUR: FRAMEWORK FOR SUPERVISION

4.01 EVOLUTION OF BANKING SUPERVISION IN THE CENTRAL BANK OF NIGERIA OVER THE PAST 50 YEARS (1959 – 2008)

The CBN commenced operations in July 1959 with a "Scrutiny Section" whose primary responsibility was the off-site supervision of banks, while on-site examination functions resided in the Banking Examination Department (BED) of the Federal Ministry of Finance [FMF]. This arrangement subsisted until December 1965.

In January 1966, the CBN fully took over the function of bank supervision, with the BED transferred to the CBN and merged with the Scrutiny Section. Subsequently, an autonomous Bank Examination Department (BED) was created in 1967. The BED operated with two offices, Bank Examination and Scrutiny Offices, from 1967 to 1976.

The search for an appropriate nomenclature and structure for the functions and responsibilities of the department led to the adoption of Banking Supervision Department (BSD) and the creation of three divisions; Central Supervision, Field Examination, and Financial Sector Development Divisions, in 1977. A fourth division, the Foreign Exchange Inspectorate Division, was created in 1984, to supervise the activities of authorised dealers, sequel to some developments in the foreign exchange market.

The liberalization of the banking sector, as a result of the Structural Adjustment Programme introduced in 1986, led to an upsurge in the number of banks and other financial institutions in the system with a consequent challenge on the capacity and effectiveness of supervision. Thus, the BSD was split into two departments, BED and BSD, and assigned On-site and Off-site supervisory responsibilities, respectively.

The new BSD had four divisions comprising the Banking Development Division with Surveillance, Policy and Staff Development offices; the Central Regulation Division with Information and Applications, and Bankers' Committee Offices; the Other Financial Institutions Division with Analysis, and Statistics and Information Offices; and the Prudential Analysis Division made up of Scrutiny I and Scrutiny II Offices, Credit Risk Management Bureau, and Administrative Unit. During this period, the BED had four divisions, viz; Commercial Banking Division (CBD); Merchant Banking and Other Financial Institution Division (MBOFID); Foreign Exchange Inspectorate Division (FEID); Monitoring, Enforcement & Administration Division (MEAD)

Emerging developments in the banking system continued to compel the CBN to restructure its supervisory roles so as to remain relevant in the efficient and effective supervision of the system. The Banks and Other Financial Institutions Act (BOFIA) was enacted in 1991 to strengthen the functions of supervision while the BSD was further restructured in 1992 with the creation of a new division, realignment of functions and change in the names of some divisions. Central Regulation Division had Finance Companies, Information and Application, Bureau de Change, Advert and New Products offices; Surveillance Division had Policy Evaluation, Problem Banks, Inter-agency Relations, and Bank Rating Offices; Prudential Analysis Division had Statistics, Financial

Analysis and Branch Expansion Offices; and a new division called the Credit Risk Division with EDP and Credit Risk Offices was created.

Prior to the enactment of the BOFIA in 1991, the regulation and supervision of the financial system by the CBN was limited to the banking industry. Other financial institutions (OFIs) were not supervised at all. The BOFIA, therefore, incorporated OFIs under the regulatory purview of the CBN.

Subsequently, a new department, the Other Financial Institutions Department [OFID] was created in 1993 to take over the off-site and on-site supervision of other financial institutions from BSD and BED, respectively. However, some OFIs like the erstwhile community banks, the Development Finance Institutions, and primary mortgage institutions had other supervisors other than the CBN. To facilitate coordinated and through supervision of the whole OFIs sub-sector, the Federal Government in 1997 transferred the regulation and supervision of the entire OFIs sector to the CBN while the 1999 amendment to the BOFIA gave the CBN the statutory powers for the licencing, regulation and supervision of the OFIs.

Further, the CBN in August 1999 embarked on a comprehensive restructuring exercise called the Project EAGLES, (acronyms for **E**fficiency, **A**ccountability, **G**oal Orientation, **L**eadership, **E**ffectiveness and **S**taff Motivation). The exercise resulted in a reduction in the number of departments in the bank to ensure effective and proper alignment of functions. OFID was retained as a Department while the BED and BSD were fused to form a Banking Supervision Department with on-site and off-site responsibilities. The new BSD adopted a team based structure for supervision in August 2000, in line with the recommendations of the International Monetary Fund (IMF) and World Bank. This was to ensure a holistic approach to supervision through a structure that will proactively and effectively achieve the objectives of supervision. Subsequently, the OFID finally assumed its supervisory role in April 2001.

Composition of Other Financial Institutions

The OFIs under the regulatory purview of the CBN has supervisory and regulatory responsibilities for the following institutions:

Development Finance Institutions (DFIs), presently made up of:

- i. The Bank of Industry Limited (BOI)
- ii. The Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB)

- iii. The Nigerian Export Import Bank (NEXIM).
- iv. The Federal Mortgage Bank of Nigeria (FMBN).
- v. The Urban Development Bank of Nigeria (UDBN)- privatized in 2007 and currently undergoing restructuring.
- vi. The Education Bank of Nigeria (also under restructuring currently).
- b) Finance Companies (FCs):
- c) Bureaux de Change (BDCs):
- d) Primary Mortgage Institutions (PMIs):
- e) Microfinance Banks (MFBs): and

With the coming into effect of OFID, the activities of the OFI sub-sector had been fundamentally structured and coordinated, while deserving institutions had been licenced and minimum capital requirements put in place for the various segments of the sector. The reform and restructuring of the sector is on-going. The reform of the community banks (CBs) had been concluded with the conversion of the CBs that met the criteria to microfinance banks. The operations of the Primary Mortgage Institutions (PMIs), and Bureaux de change had been streamlined. Capacity building workshops for operators and managers of the OFIs are continually being carried out to build competencies and upscale skills in the industry.

STRATEGIES AND TOOLS DEPLOYED FOR EFFECTIVE SUPERVISION

In dealing with its supervisory responsibilities, the CBN adopts best practice in addition to proactively developing some innovative approaches to meet its needs. Some of these strategies and tools include the following:

- ▣ The establishment of the Other Financial Institutions Department (OFID) April 2001 to deal with the challenge of effective supervision of the OFIs.
- ▣ Deployment of e-FASS in the supervision of banks and OFIs.
- ▣ Implantation of the banking sector reform/consolidation programme.
- ▣ Issuance of Code of Corporate Governance.
- ▣ The adoption of a risk-based approach to supervision of banks and the OFI sub-sector.
- ▣ Enactment of BOFIA 1991 and subsequent amendments to strengthen the regulatory powers of the CBN.
- ▣ Establishment of the NDIC in 1988 to insure deposits.
- ▣ Introduction of new capital adequacy requirements, based on risk-weighted assets, consistent with the Basel Capital Accord.

- ▣ Issuance of prudential guidelines to compel banks and OFIs to adopt a uniform standard for risk asset classification, loan loss and off-balance sheet commitments provisioning and recognition of interest income.

CHALLENGES TO SUPERVISION

In carrying out its regulatory and supervisory roles, the CBN is faced with the following challenges, among others:

- ▣ Low capital base of the OFIs, which inhibit their ability to play the desired economic and developmental roles especially in the area of access to finance to Micro, Small and Medium Enterprises (MSMEs);
- ▣ A large number of institutions, which require huge financial and personnel supervisory resources, especially in the OFI sub-sector;
- ▣ Inadequate supervisory capacity (skills, equipment etc) to cope with the large number of supervised institutions spread across the country,
- ▣ Pervasive unethical practices and poor corporate governance by operators,

Notwithstanding these drawbacks, a strong banking supervision in the CBN has evolved over the past 50 years and has contributed significantly to the promotion of stability in the financial system. The CBN would continue to restructure and reform its supervisory process to meet with the increasing challenge of supervision.

4.02 TOWARDS THE IMPLEMENTATION OF PRIVATE CREDIT BUREAUX IN NIGERIA

In line with the practice in some jurisdictions and to address the challenges facing the CBN CRMS, namely, its limitation to only banks and the non-coverage of some sectors of the economy, the decision to allow private ownership of credit bureaux was implemented during the year. This decision was aimed at complementing the CBN CRMS in monitoring credits in the financial system and ensuring easy access to credits. To facilitate the process, the CBN relied on Section 57 of the CBN Act, 2007 which empowers it to licence and regulate private credit bureaux operators in Nigeria.

Consequently, a committee was set up to prepare the guidelines on the licensing, operational and regulatory requirements for private sector-run credit bureaux in Nigeria. In preparing the guidelines, the Committee took cognizance of global best practice in credit bureaux operations as well as the environmental peculiarities of the country. Also, inputs and contributions were received from various stakeholders including the World Bank MSME project, the IFC, individuals and corporate organizations that indicated interest in credit bureaux operations in Nigeria.

The guidelines were issued and posted on the CBN website, in October 2008, the major highlights were as follows:

1. **Licensing Requirement:** Investors wishing to operate credit bureaux shall satisfy the following conditions:

- a) Submit a formal application and detailed feasibility report with a non-refundable application fee of N250,000.
- b) A minimum capital requirement of N500 million to be deposited in an escrow account with the CBN; 50 percent of which will be returned on grant of Approval-in-Principle, while the balance of 50 percent with accrued interest will be returned on grant of final licence.

2. **Operational Procedures of Credit Bureaux**

- a) **Permissible Purpose:** Access to credit information from credit bureaux should be for a permissible purpose such as court order or arbitration, terms of any form of credit/acceptance of guarantees, credit scoring, written consent from the client, legislation, public interest and government or its agencies.
- b) **Data Collection:** A licensed credit bureau shall collect information on the background and credit history relating to the commitments of persons, enterprises and other organizations, in order to determine their overall debt exposure and capacity/ability to repay. Such data can be collected from banks and other financial institutions operating in Nigeria, CBN CRMS, mortgage finance companies, financial/operating leasing companies, insurance companies, institutions that offer credit to medium, small and micro enterprises, asset management companies, suppliers of goods and providers of services on a post-paid or instalment payment basis e.g. telecommunication, water, health, energy etc., other credit bureaux licensed by the CBN, other entities that have data and information that serve the purposes of the credit bureaux.
- c) **Information Dissemination:** A credit bureau shall provide credit information services to authorised users and any other body as may be determined by the CBN from time to time. Every bank must have data exchange agreement with at least two credit bureaux.

- d) **Responsibilities of Credit Bureaux:** A credit bureau shall be responsible for the implementation of strict quality control procedures in order to ensure the quality, accuracy of information and reliability of its database.
- e) **Data Retention period:** A credit bureau shall maintain a historical data covering a 5-year period for the purpose of providing detailed credit information, and shall keep the database for a period of not less than 10 years after which it shall be archived. It shall also implement procedures and systems that ensure that the information registered in its database is updated on an on-going basis and in standardized formats.
- f) **Fees and Charges:** A credit bureau shall charge fees for its services.
- g) **Unique Identifier:** A credit bureau shall make use of a unique identifier to replace the name of the holder/data subject, as a means of protecting his/her identity and also ease data collection, collation, processing and dissemination of information.
- h) **Submission of Returns/Audited Accounts and Supervision:** A credit bureau shall submit to the CBN on a monthly basis, details of its activities as specified by the CBN, 10 working days into the following month. The credit bureau shall also submit its audited accounts not later than three months after its year-end for approval by CBN for publication. It shall be subjected to annual examination of its activities by the CBN. The CBN, shall have unrestricted access to all the information managed by the bureaux for the purpose of supervision and utilize the information collected solely for the purposes set out in the guidelines.
- i) **Compliance with Guidelines:** A credit bureau shall comply strictly with the provisions of the guidelines. Contraventions or non-compliance shall attract appropriate sanctions.
- j) **Dissolution, Liquidation and Revocation of Licence:** Where a credit bureau is to be dissolved, it shall notify the CBN in writing. The CBN shall conduct an investigation of the credit bureau and the credit bureau shall deliver its/any database containing information to the CBN. A credit bureau shall not transfer, directly or indirectly, any database containing information to any person other than the CBN or its nominated recipient.

- 3. The Role of CBN Credit Risk Management System (CRMS):** The CBN CRMS shall continue to serve its regulatory functions, operate as a public credit registry and would, therefore, share its information with the licensed credit bureau. Banks and other financial institutions shall continue to render the mandatory returns and comply with the provision of all relevant circulars and guidelines.

Addendum: The CBN shall not be liable or joined in any dispute(s) arising from wrong information given in respect of a credit report by a bank or a credit bureau.

Following the release of the guidelines, applications from corporate bodies for the establishment of credit bureaux had been received and were being processed pursuant to the issuance of operating licenses. There is no doubt that the smooth take off and supervision of private credit bureaux would pose some challenges to the regulatory authorities and stakeholders. Principal among the challenges are the absence of an acceptable unique identifier in Nigeria, lack of public awareness of the relevance and operational modalities of credit bureaux, absence of reliable and accurate data collection and dissemination methods, and absence of consumer rights and protection laws. These challenges are, however, surmountable.

Going by the plan of the CBN, private credit bureaux are expected to commence operations in Nigeria in the second quarter of 2009.

4.03 EFFORTS TOWARDS INTRODUCING NON-INTEREST BANKING IN NIGERIA

Non-interest banking involves the provision of financial products and services that comply with the principles and rules of Islamic commercial jurisprudence. It prohibits usury, the payment of fees for the renting of money, as well as investing in businesses that provide goods or services considered contrary to its principles. Transactions and contracts under this type of banking are non-permissible if they involve:

- interest;
- uncertainty or ambiguity relating to the subject matter, terms or conditions;
- gambling;
- unjust enrichment; and/or
- exploitation/unfair trade practices.

Given the increasing number of banks and other financial institutions desiring to offer sharia-compliant products in Nigeria, the CBN has taken the following steps to provide an enabling environment for the development of the new banking practice:

- capacity building in Islamic banking;
- participation in the annual Islamic Finance Conference of the Durham University, United Kingdom to gain insight into global developments on the concept;
- applied for membership of the Islamic Financial Services Board; and
- indicated interest in joining the Islamic Finance Information Services.

Furthermore, an eight-member Committee was constituted by the CBN to develop a regulatory and supervisory framework on the subject. Following the Committee's preliminary review of the practices in other jurisdictions, the need to build capacity, through training and exposure, was identified. Consequently, the Committee undertook a study tour to Kuala Lumpur, Malaysia from July 14 – 26, 2008.

The choice of Malaysia for the study visit was informed by its current position as a leading Islamic financial centre in the world, with a robust regulatory and institutional infrastructure and home to global standard-setting and learning institutions on Islamic finance.

The visit commenced with a conference in the first week during which notable scholars, experts, regulators and bank operators made presentations and shared their experiences and perspectives with the CBN delegation. The conference covered a broad spectrum of issues in Islamic finance and banking, ranging from the overview of Islamic finance, regulatory issues to developments and practices of Islamic finance and banking across the globe.

In the second week, the Committee visited key regulatory and banking institutions, such as the Bank Negara Malaysia, the Islamic Financial Services Board, CIMB Islamic Bank and Standard Chartered Bank (Islamic Operations).

The study tour was significant as it afforded the Committee an opportunity to validate and seek clarifications on some of the issues arising from the conference, and experience first-hand the regulatory and operating environment in Malaysia. The Committee also used the visit to network and establish strategic links with key institutions in Malaysia.

The knowledge gained assisted the Committee in its effort at preparing a draft framework. It is expected that the regulatory/supervisory framework as well as the accompanying guidelines would be issued in the first quarter of 2009. Also, an international conference on non-interest banking is being planned to create awareness in the new field.

Developing the non-interest banking sector in Nigeria would not only increase the sophistication and product offering in the industry, but would also create a veritable tool for financing economic development in the country.

CHAPTER FIVE: PERFORMANCE TRENDS IN THE BANKING SYSTEM

PERFORMANCE TRENDS IN THE BANKING SYSTEM

The total assets of the banking sector increased, by 46.56 percent or N4.87 trillion, from N10.47 trillion in 2007 to N15.34 trillion

5.01 BALANCE SHEET STRUCTURE AND GROWTH RATES IN BANKS

in 2008. Cash and Due from Banks accounted for 18.84 percent in 2008 compared to 17.21 percent in 2007. Advances/leases, which constituted the largest component of total assets, grew from N3.80 trillion or 36.32 percent in 2007 to N6.17 trillion or 40.21 percent of total assets in 2008.

The major components of liabilities also witnessed increases. Total deposits, other liabilities and paid-up capital and reserves rose by 62.28 percent, 2.05 percent and 63 percent, respectively.

The aggregate balance sheet of the banking industry from 2004 to 2008 and the individual components are presented in Table 1below:

Aggregate Balance Sheet Structure of the Banking system

ASSETS	31-Dec-08		31-Dec-07		31-Dec-06		30-Sep-05		31-Dec-04	
	N'b	%	N'b	%	N'b	%	N'b	%	N'b	%
Cash & Due from Banks	2,891	18.84	1,802	17.21	2,066	30.66	1,034	23.56	935	27.56
Call & Placements	1,224	7.98	438	4.18	135	2.00	230	5.24	102	3.01
Government Securities	792	5.16	1,584	15.13	1,048	15.55	665	15.15	573	16.89
Short Term Funds	929	6.05	491	4.69	263	3.90	238	5.42	104	3.07
Advances & Leases (Net)	6,170	40.21	3,802	36.32	2,081	30.88	1,477	33.65	1,133	33.39
Investments	1,356	8.84	892	8.52	430	6.38	194	4.42	105	3.09
Other Assets	1,411	9.20	1,006	9.61	450	6.68	368	8.38	281	8.28
Fixed Assets	570	3.72	454	4.34	265	3.93	183	4.17	160	4.72
TOTAL (Net)	15,343	100.00	10,469	100.00	6,738	100.00	4,389	100.00	3,393	100.00
LIABILITIES	31-Dec-08		31-Dec-07		31-Dec-06		30-Sep-05		31-Dec-04	
	N'b	%	N'b	%	N'b	%	N'b	%	N'b	%
Total Deposits	8,703	56.72	5,363	51.23	3,442	51.08	2,546	58.01	1,797	52.96
Money at Call and Takings	567	3.70	254	2.43	57	0.85	70	1.59	54	1.59
Due to Other Banks	226	1.47	198	1.89	689	10.23	57	1.30	47	1.39
Other Borrowed Funds	1	0.01	1	0.01	67	0.99	67	1.53	61	1.80
Other Liabilities	2,740	17.86	2,685	25.65	1,441	21.39	1,091	24.86	1,080	31.85
Long Term Loans	317	2.07	257	2.45	1	0.01	4	0.09	3	0.09
Paid-Up Capital	211	1.38	153	1.46	170	2.52	171	3.90	141	4.16
Reserves	2,578	16.80	1,558	14.88	871	12.93	383	8.73	210	6.19
TOTAL	15,343	100.00	10,469	100.00	6,738	100.00	4,389	100.00	3,393	100.00
OFF BALANCE SHEET ITEMS	3,918	25.54	2,581	24.65	1,380	20.48	859	19.57	664	19.57
NUMBER OF BANKS	24		24		25		86		87	

Figure 1
Aggregate Balance Sheet: 2004 b- 2008

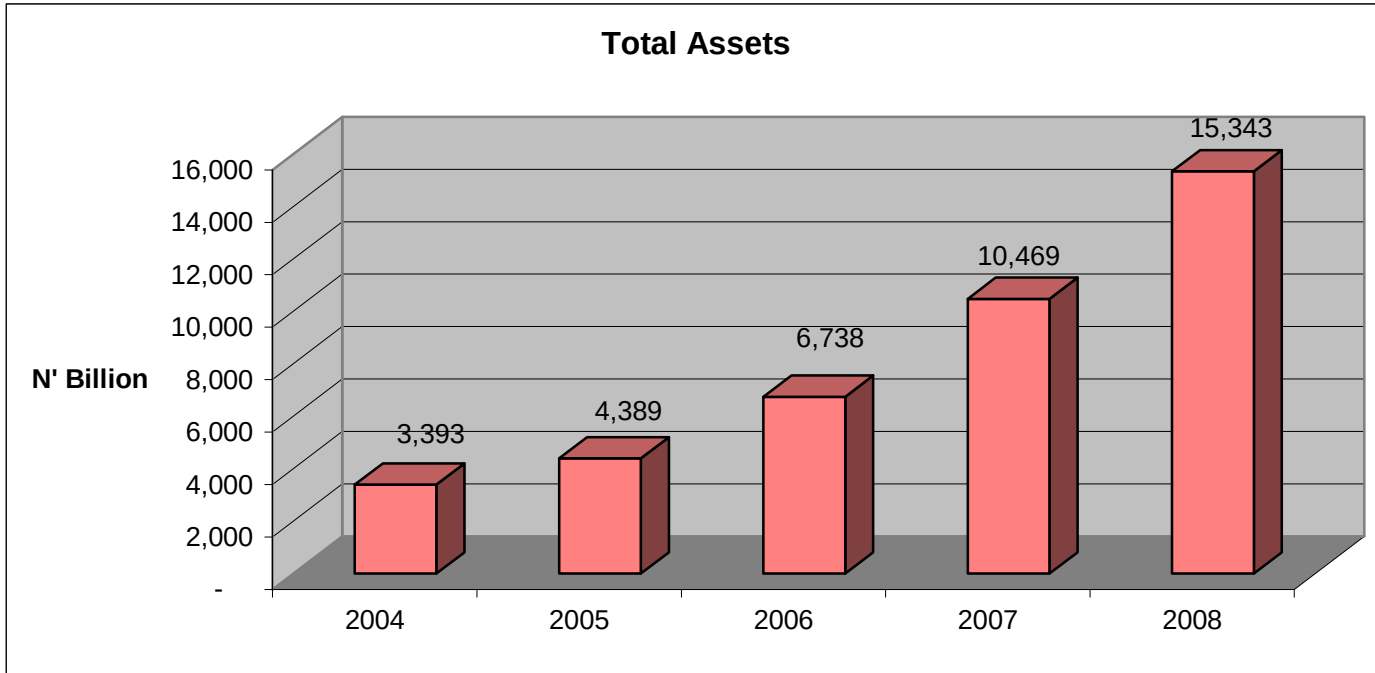


Figure 2
Composition of Assets in 2004

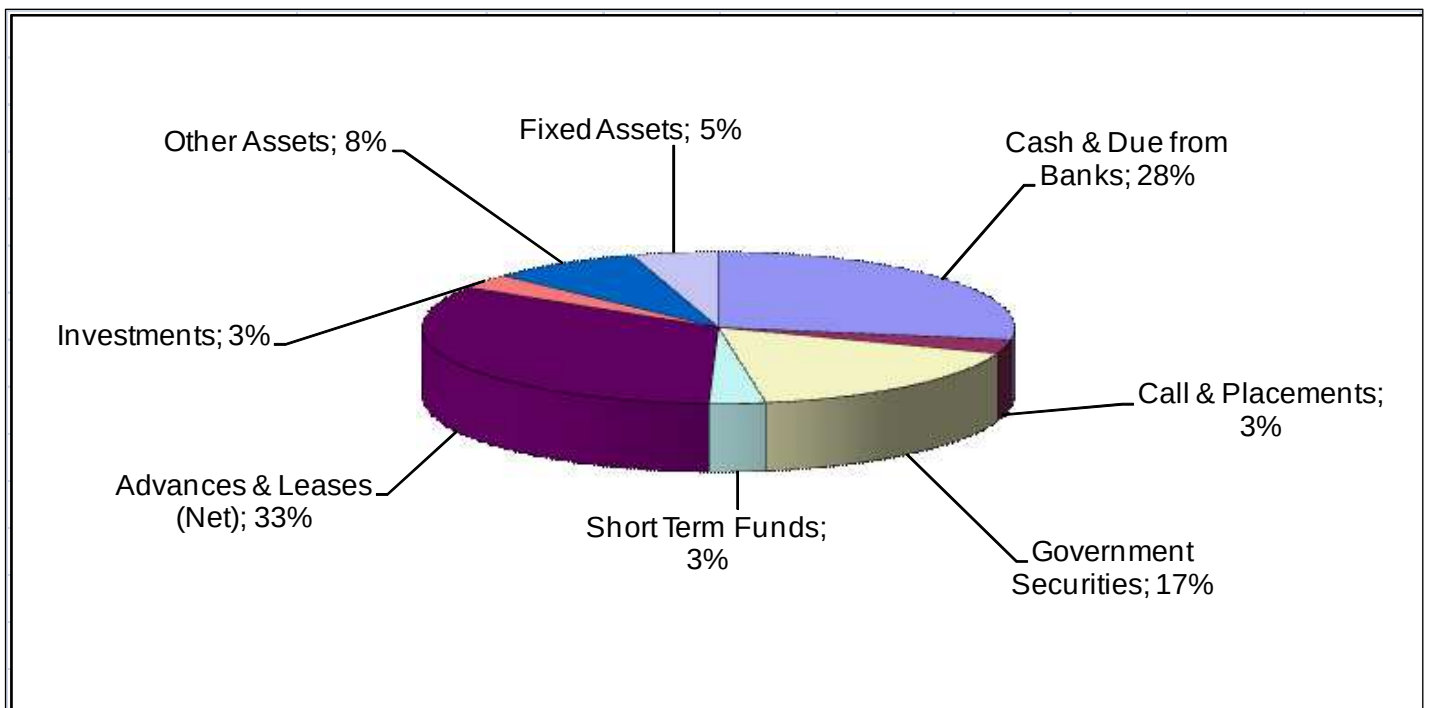


Figure 3
Composition of Assets in 2005

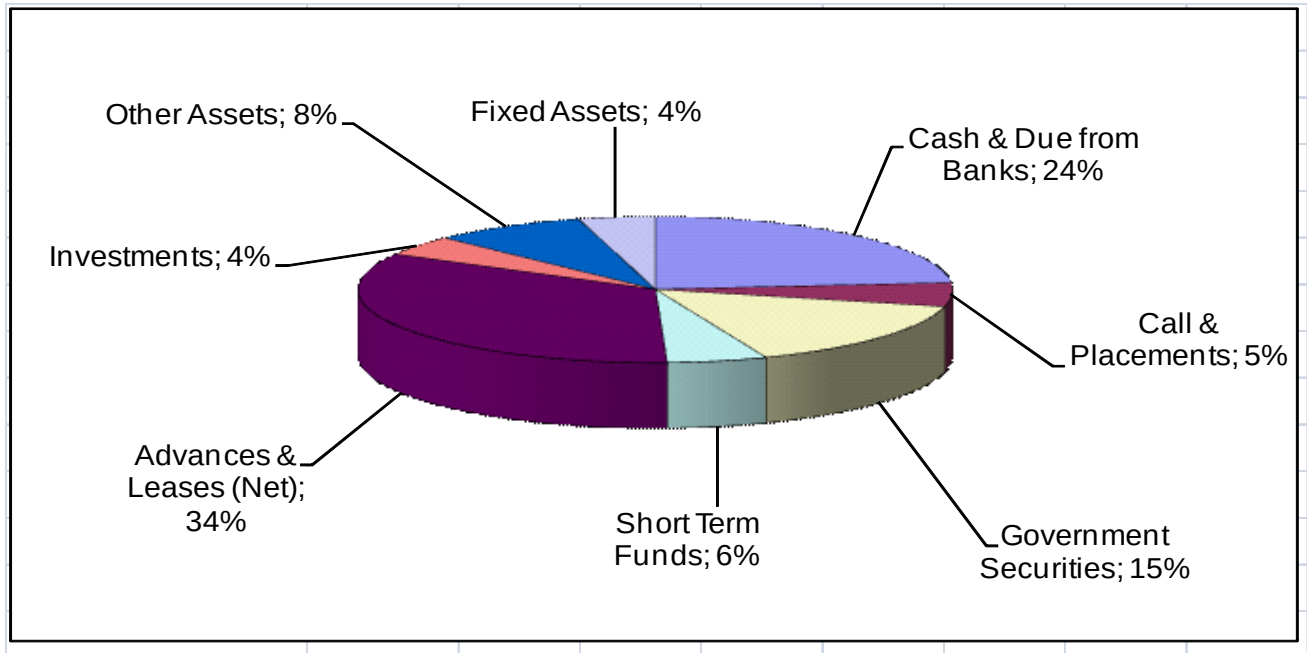


Figure 4
Composition of Assets in 2006

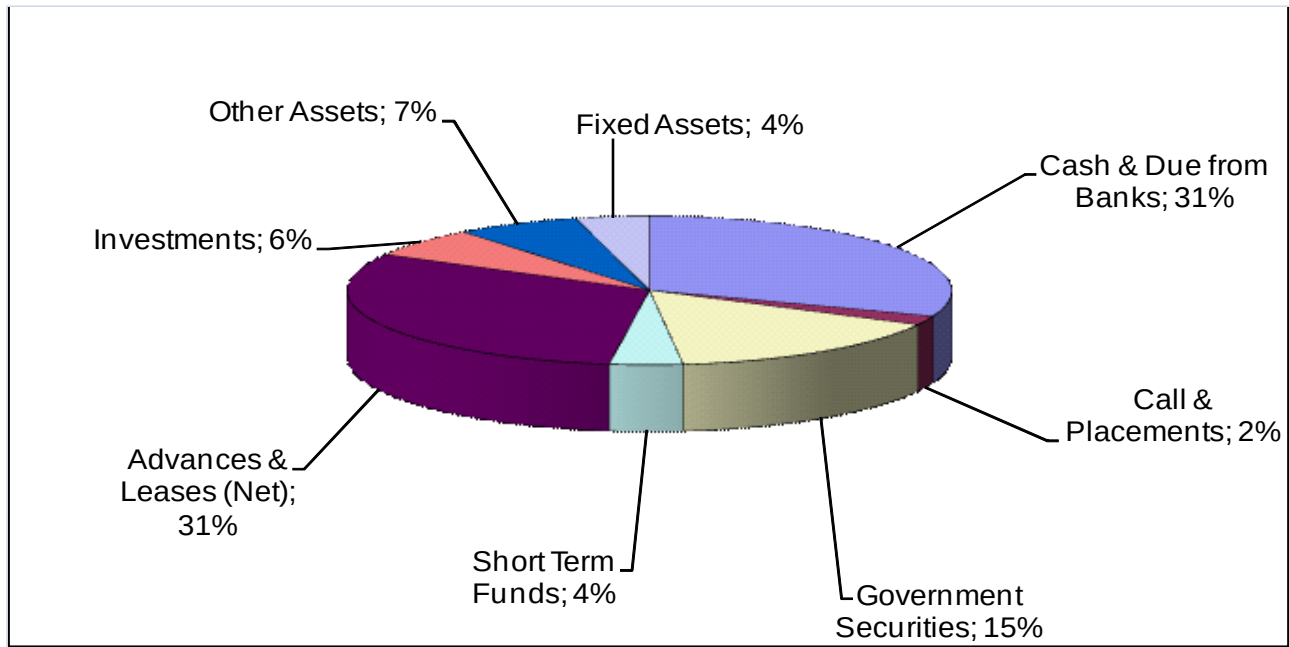


Figure 5
Composition of Assets in 2007

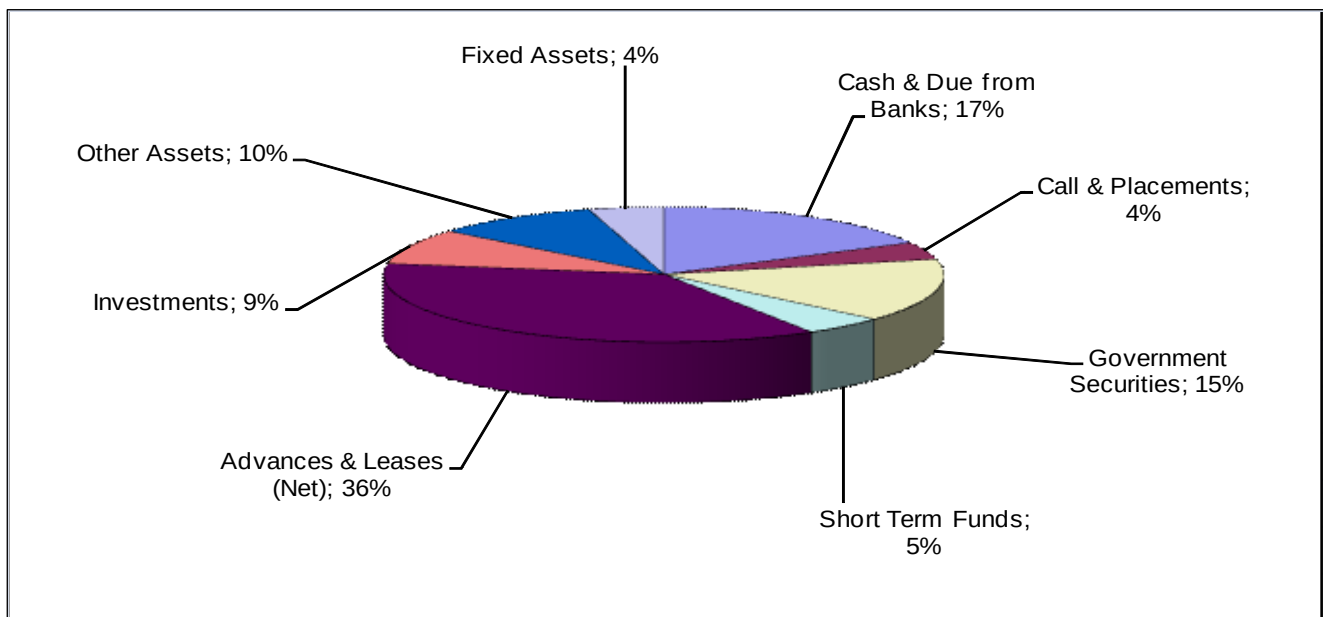


Figure 6
Composition of Assets in 2008

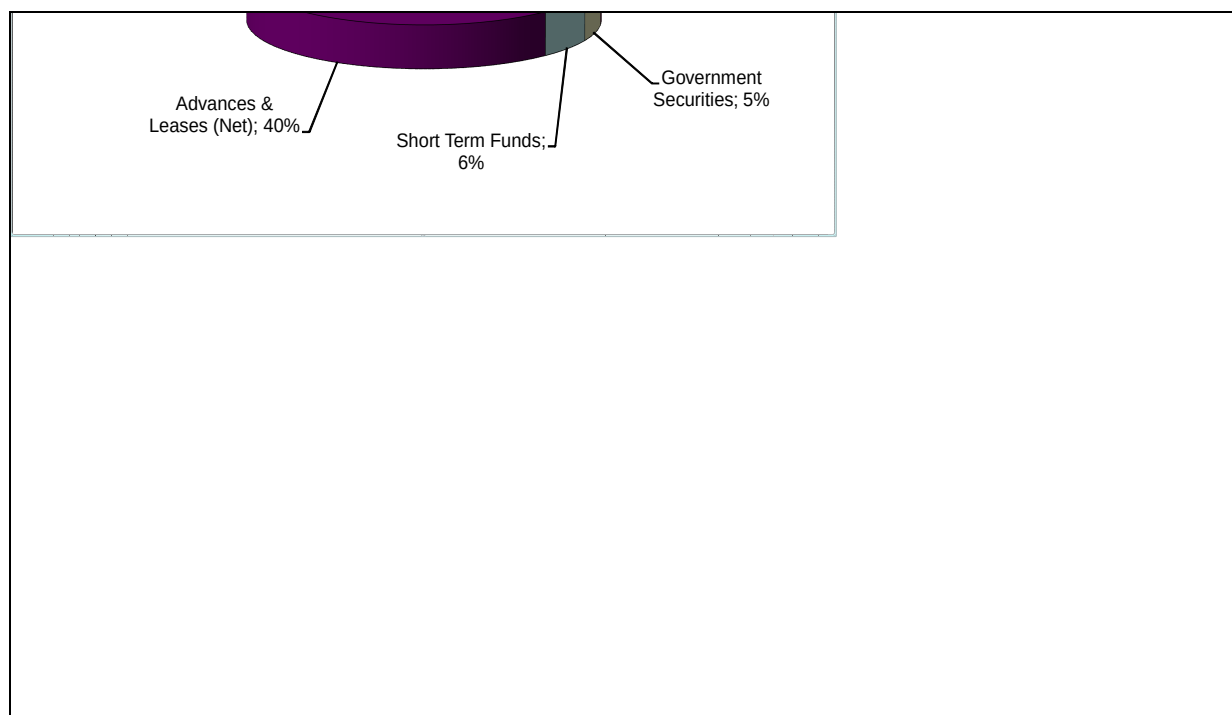


Figure 7

Composition of Liabilities in 2004

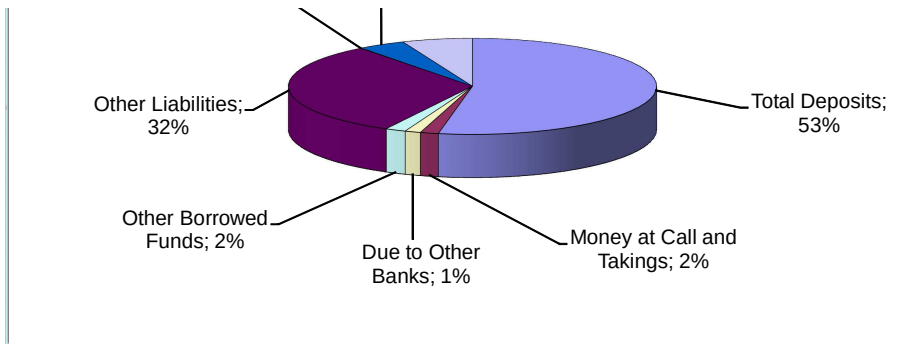


Figure 8
Composition of Liabilities in 2005

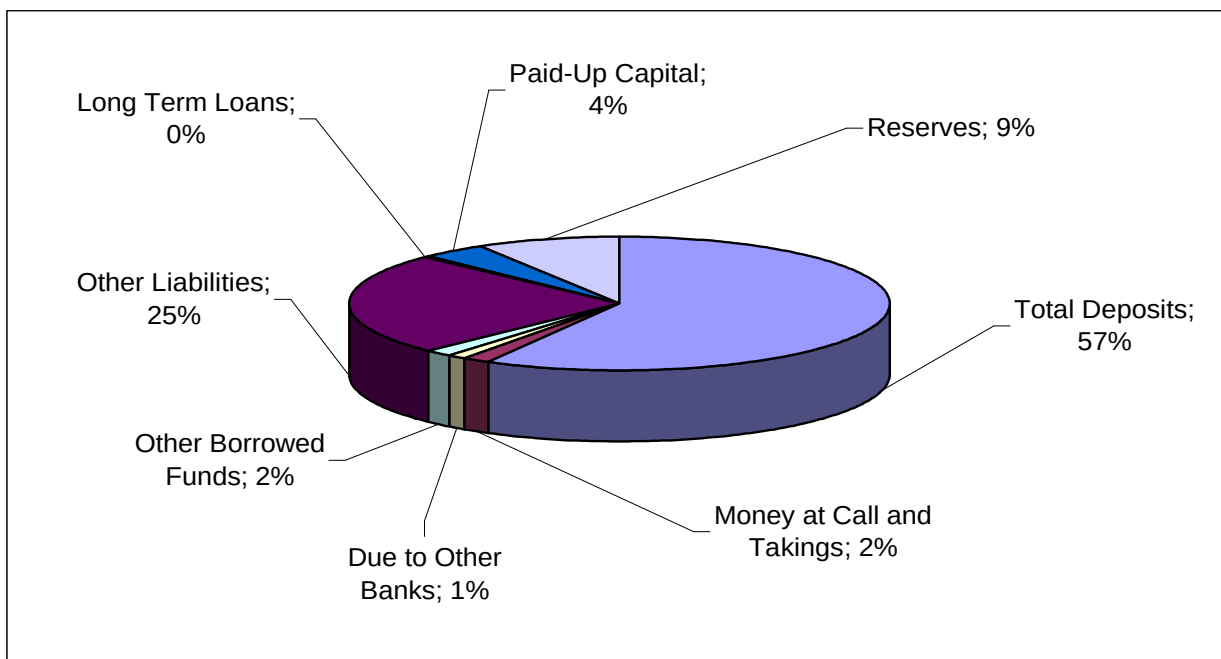


Figure 9
Composition of Liabilities in 2006

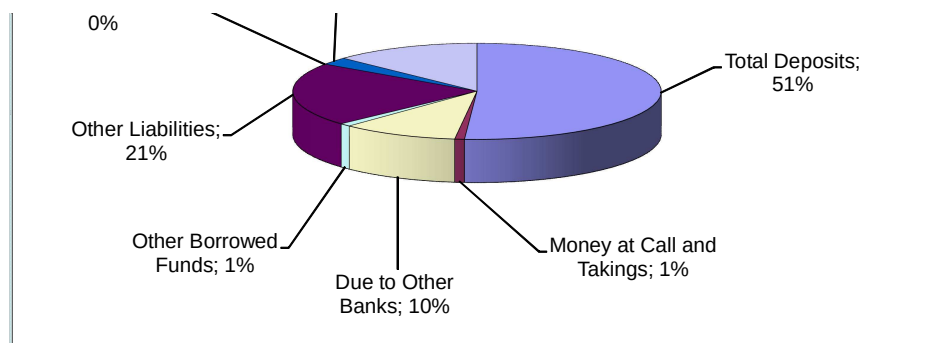


Figure 10
Composition of Liabilities in 2007

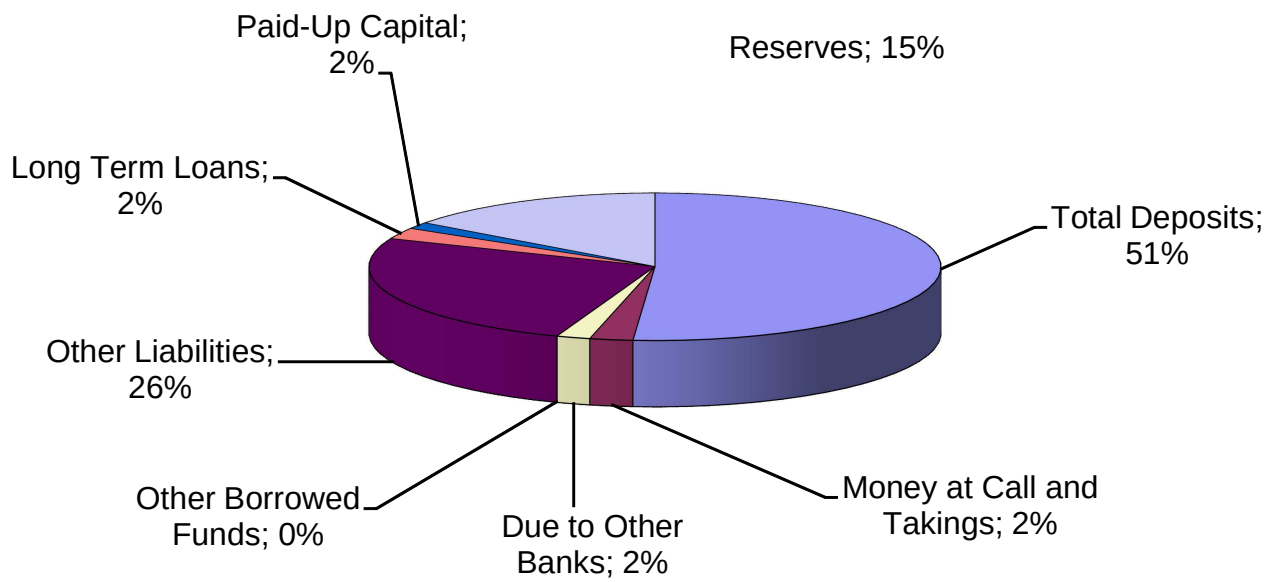
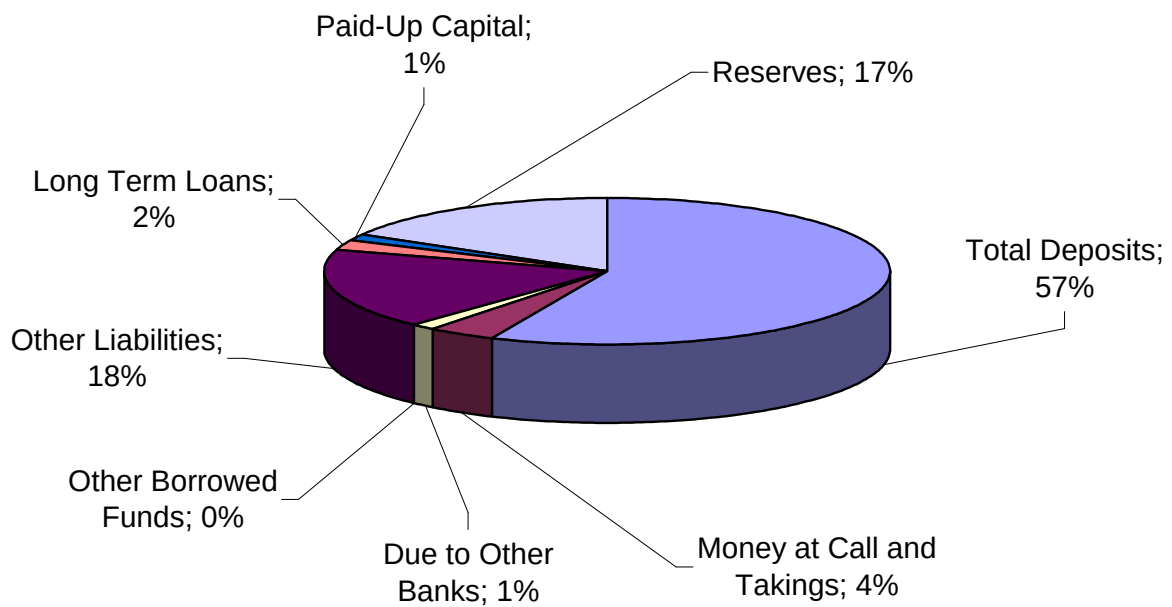


Figure 11
Composition of Liabilities in 2008

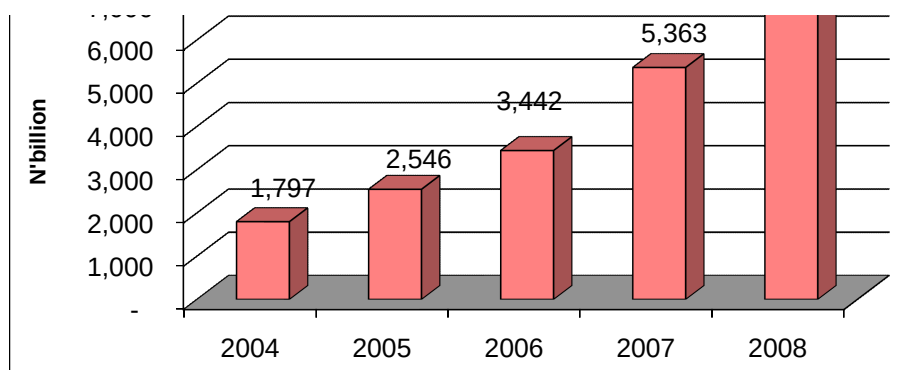


5.02 DEPOSIT LIABILITIES AND LIQUIDITY IN BANKS

In 2008, the aggregate deposits in the banking sector sustained its growth trend. It grew from N1.8 trillion in 2004 to N2.5 trillion in 2005, N3.4 trillion in 2006, N5.4 trillion in 2007 and N8.7 trillion in 2008. The observed trend reflected a growth rate of 27.54 percent in 2004, 41.68 percent in 2005, 35.19 percent in 2006, 55.81 percent in 2007 and 62.28 percent in 2008.

,Figure 12

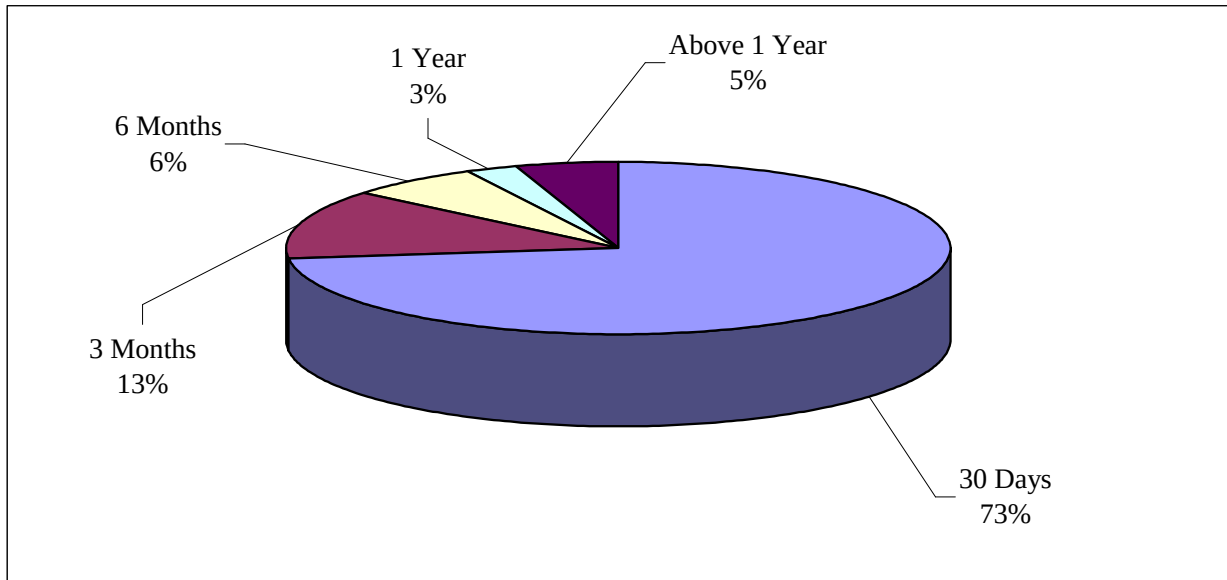
Aggregate Deposits: 2004 - 2008



About 73 percent of the deposits of the banking sector were to mature within 30 days, an indication that there was paucity of long-term deposits in the banking system.

Figure 13

Maturity profile of Deposits in 2008



Demand deposit remained the major type of deposit available to banks. It accounted for N3.9 trillion or 44.8 percent of the total deposit liabilities as against N2.5 trillion or 46.9 percent in 2007, N1.6 trillion or 46.4 percent in 2006, N1.2 trillion or 46.8 percent in 2005 and N0.8 trillion or 44.5 percent in 2004.

Figure 14
Composition of Deposits in 2004

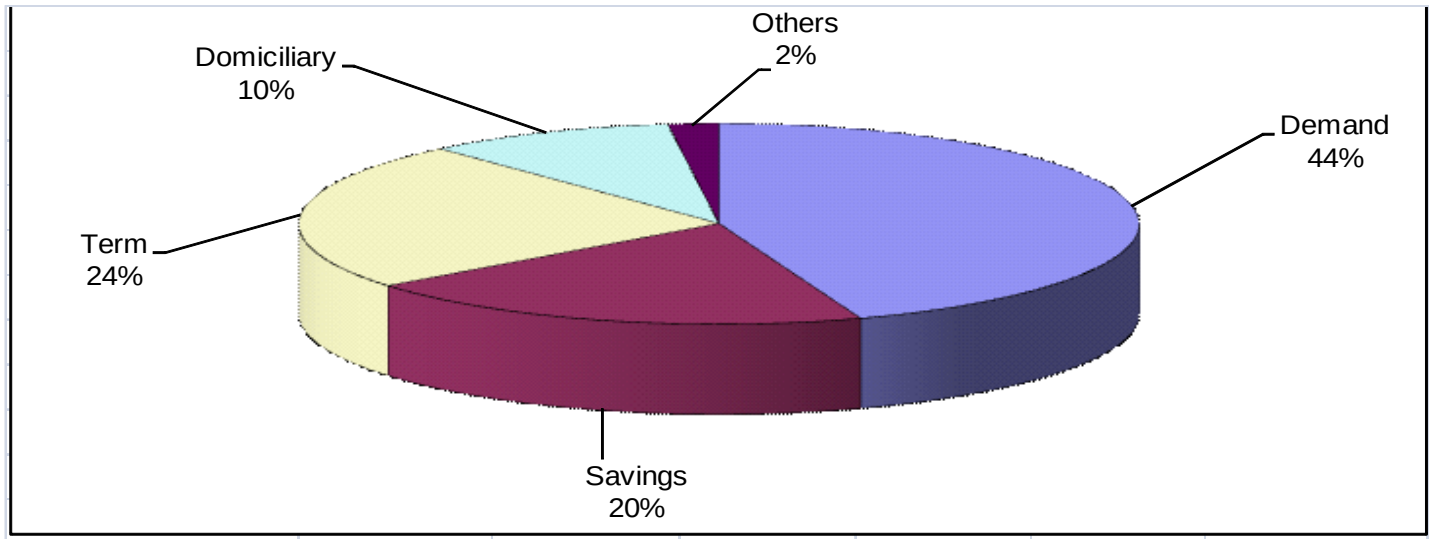


Figure 15
Composition of Deposits in 2005

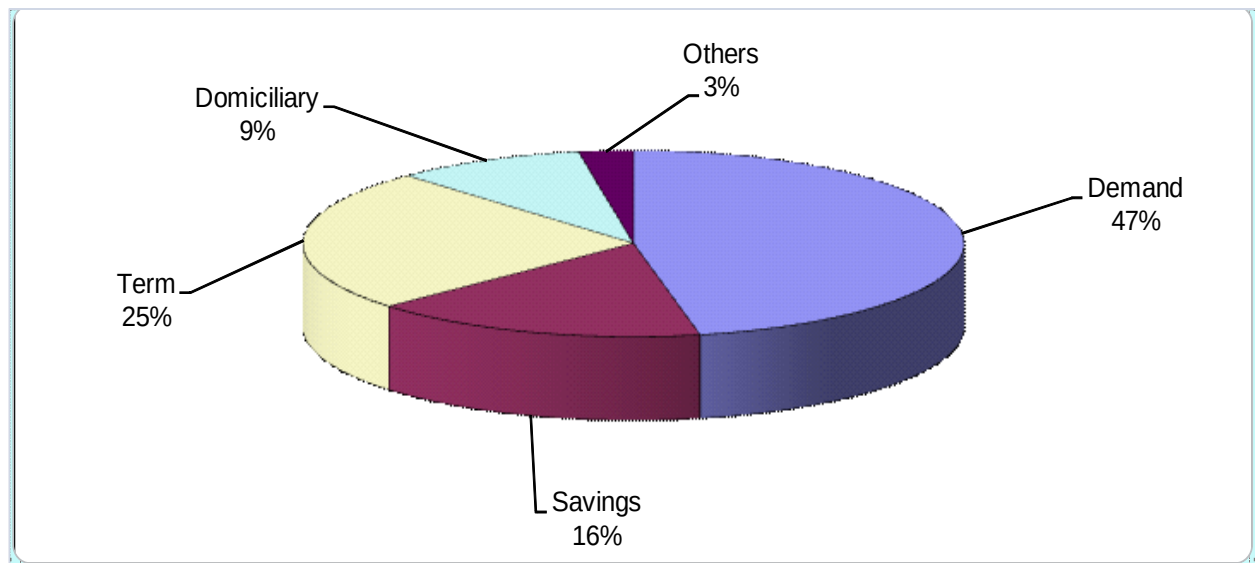


Figure 16
Composition of Deposits in 2006

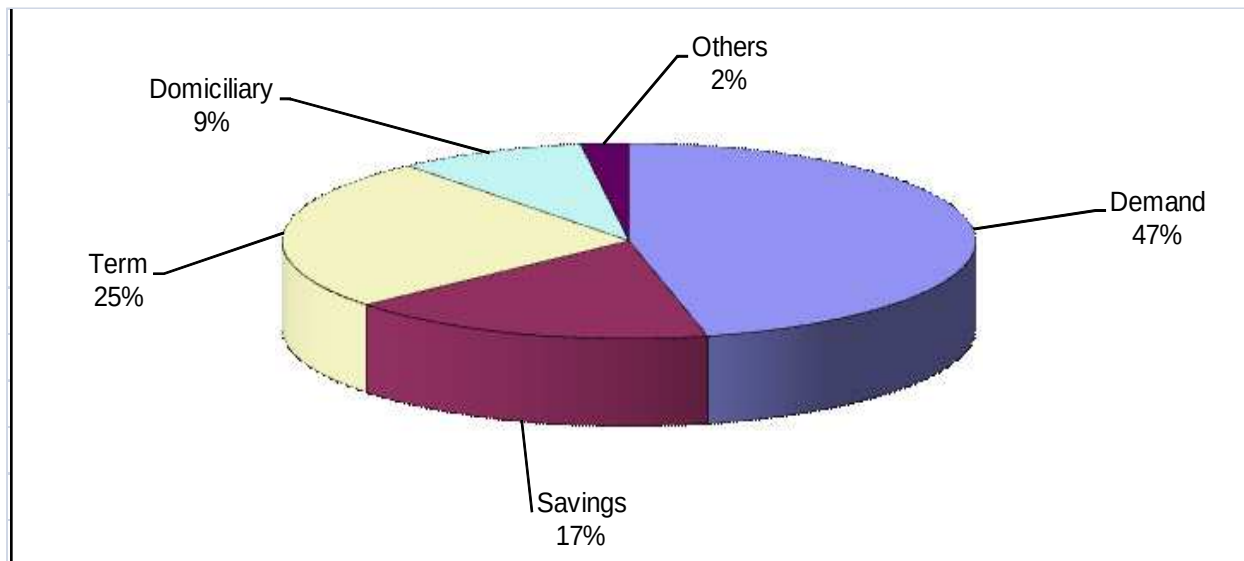


Figure 17
Composition of Deposits in 2007

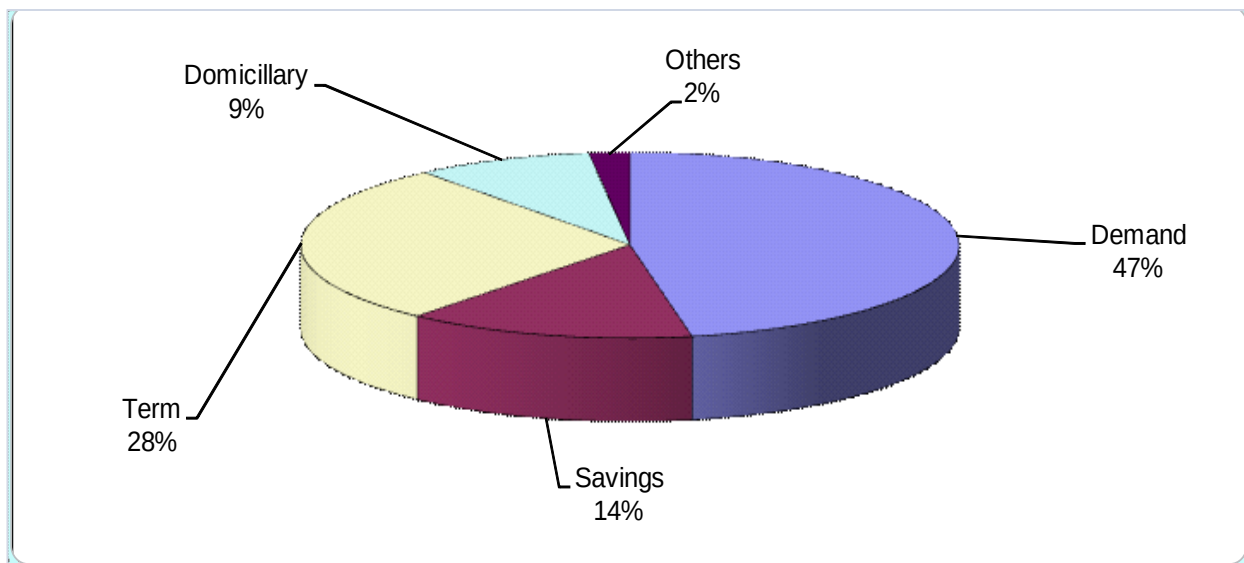
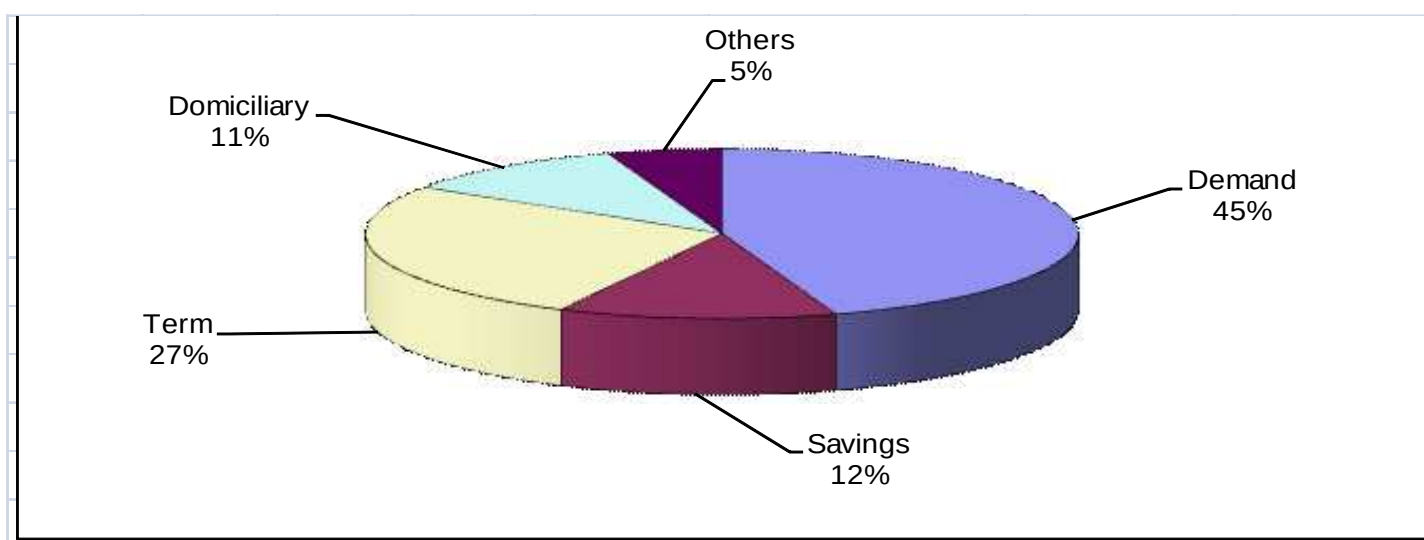
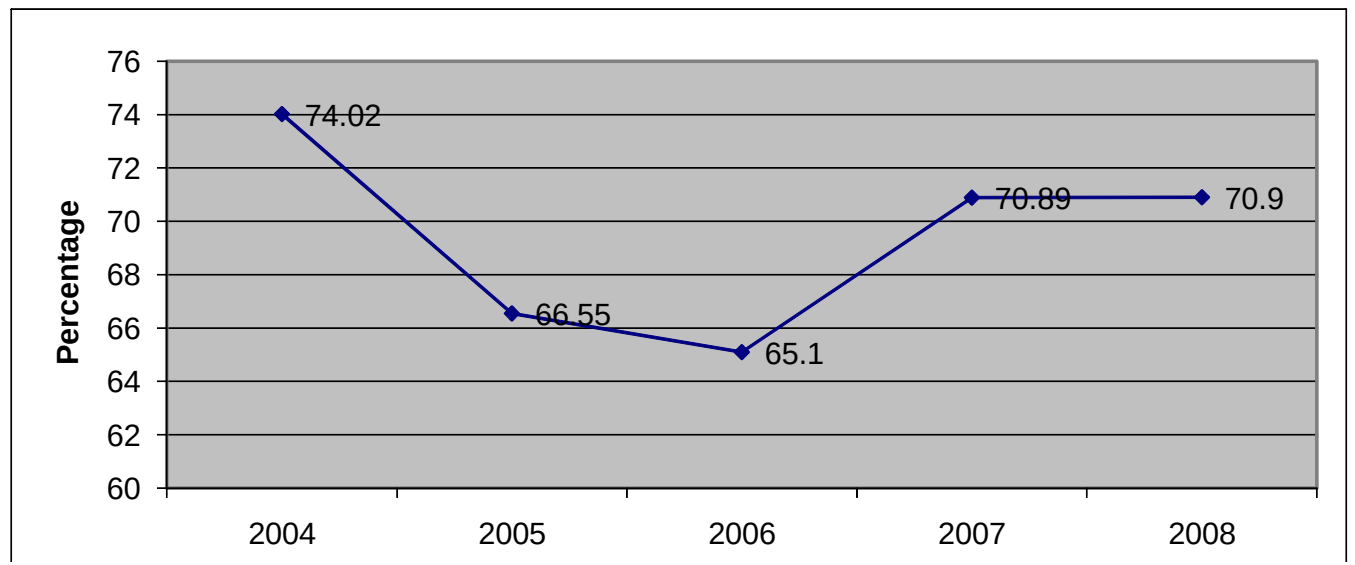


Figure 18
Composition of Deposits in 2008



During the year, the minimum liquidity ratio requirement for banks was reduced from 40 percent to 30 percent, while the specified liquid assets, for the purpose of liquidity ratio computation for banks, remained mainly cash and due from banks, short-term government instruments, placements with discount houses and inter-bank placements. The average liquidity ratio of the industry was 46.49 percent as at December 31, 2008.

Figure 19
Aggregate Credit to Deposits Ratio: 2004 - 2008

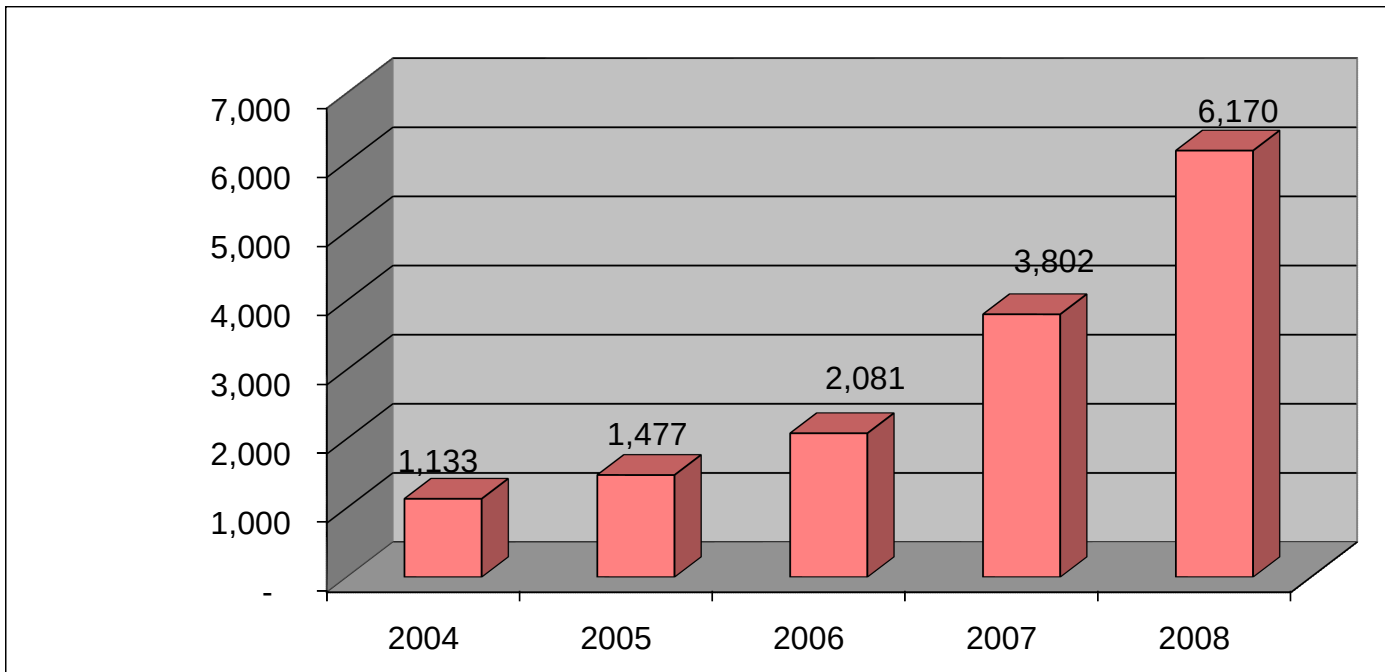


The ratio of aggregate credit to aggregate deposits was flat at about 71 percent over the last two years. The level was below the maximum recommended ratio of 80 percent. Generally, a ratio above the maximum is indicative of over-trading.

5.03 ASSET QUALITY IN BANKS

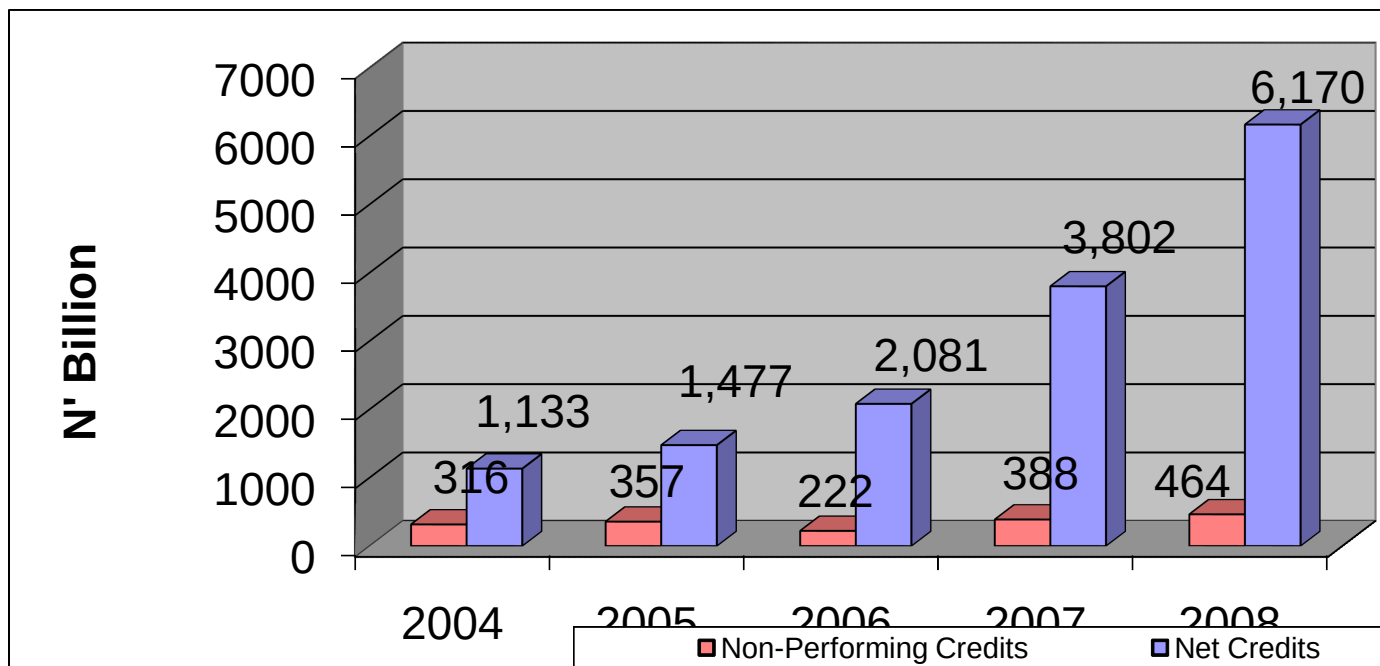
The asset quality of the banking sector improved in 2008. As in the previous years, loans and advances, which stood at N6.17 trillion as at December 2008, and constituted 40.21 percent of the banking sector aggregate assets of N15.34 trillion, were the largest earning assets during the period. Total credit recorded a growth rate of 23.83 percent in 2004, 30.36 percent in 2005, 40.89 percent in 2006, 82.7 percent in 2007 and 62.28 percent in 2008.

Figure 20
Loans and Advances: 2004 - 2008



Non-performing credits increased from N0.4 trillion in 2007 to N0.5 trillion in 2008. The ratio of non-performing credits to total credits of 6.26 percent during the review period was far below the trigger level of 35 percent for setting up a Crisis Management Unit as stipulated in the Contingency Planning Framework for Systemic Distress. The ratio was lower than 21.6 percent, 18.12 percent, 8.77 percent and 8.44 percent recorded in 2004, 2005, 2006 and 2007, respectively.

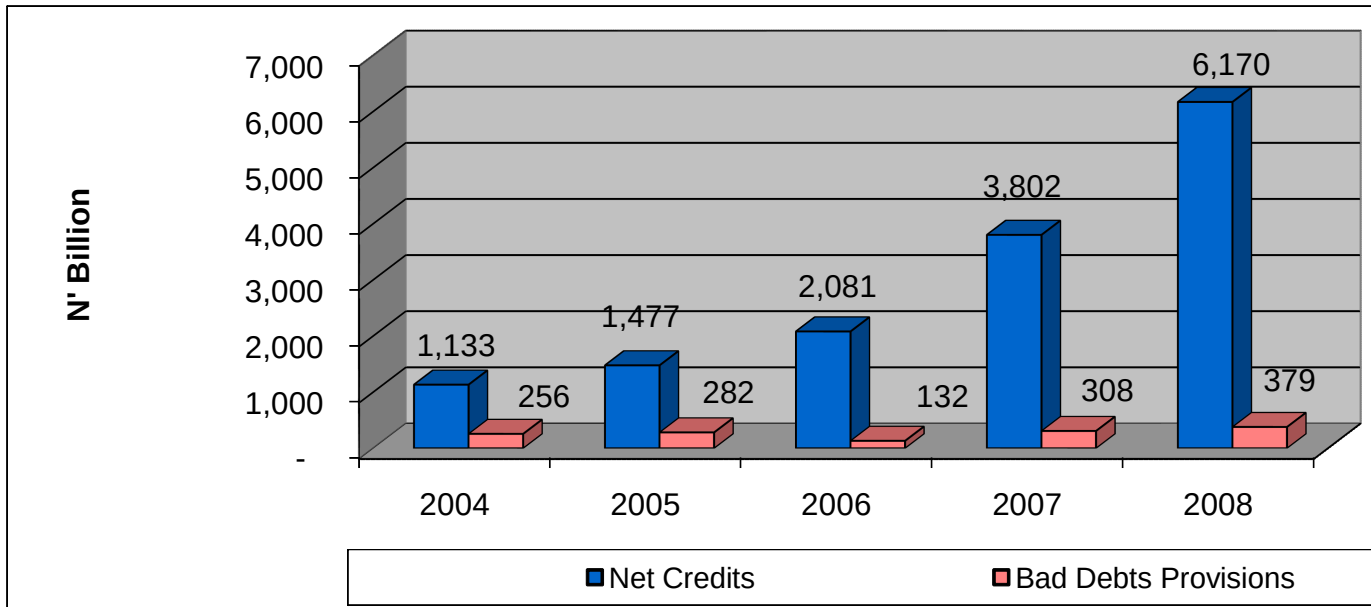
Figure 21
Non-Performing Credits to Total Net Credits: 2004 - 2008



Provision for bad and doubtful debts grew from N0.2 trillion in 2004 to N0.4 trillion in 2008. The ratio of bad debt provision to total credits was 22.6 percent in 2004, 19.1 percent in 2005, 6.3 percent in 2006, 8.1 percent in 2007 and 6.1 percent in 2008.

Figure 22

Bad Debt Provision to Total Net Credits: 2004 - 2008



5.04 CAPITAL ADEQUACY OF BANKS

At the end of December 2008, all the 24 banks, except one, met the required minimum shareholders' funds of N25 billion. Against the risk-weighted assets level of N12.8 trillion, the total qualifying capital of N2.8 trillion, represented an average capital adequacy ratio (CAR) of 21.91 percent. This position was satisfactory when compared with the required minimum CAR of 10 percent.

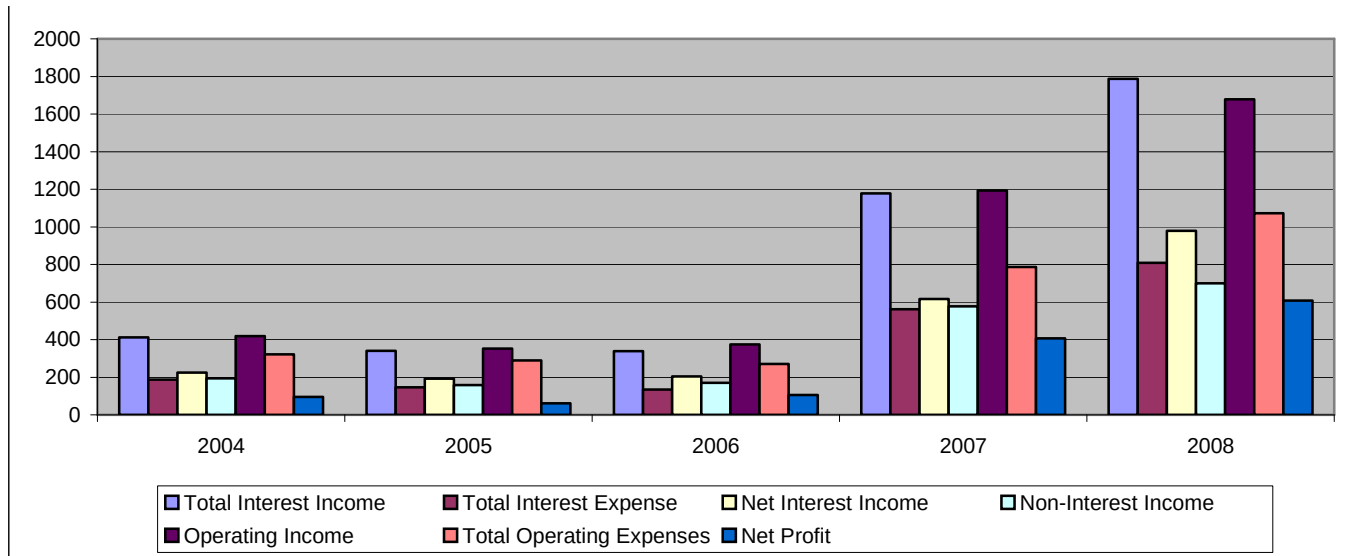
5.05 EARNINGS AND PROFITABILITY OF BANKS: 2004 - 2008

All the earnings and profitability indices showed that the total earnings of the banking industry increased in 2008 relative to 2007. The improved earning was reflected in the increase in net interest income, non-interest income and profit before tax.

Table 2
Earnings and Profitability of Banks

	2004	2005	2006	2007	2008	Percentage Growth				
	Amount N'b	Amount N'b	Amount N'b	Amount N'b	Amount N'b	2004	2005	2006	2007	2008
Interest Income	412	340	339	1,178	1,787	18.05	(17.48)	(0.29)	247.49	51.70
Interest Expense	188	147	135	562	808	22.08	(21.81)	(8.16)	316.30	43.77
Net Interest Income	224	193	204	616	979	14.87	(13.84)	5.70	201.96	58.93
Non-Interest Income	194	159	171	577	700	14.29	(18.04)	7.55	237.43	21.32
Operating Income	418	352	375	1,193	1,679	17.42	(15.79)	6.53	218.13	40.74
Operating Expenses	322	290	270	786	1,072	14.18	(9.94)	(6.90)	191.11	36.39
Profit Before Tax	96	62	105	407	607	29.73	(35.42)	69.35	287.62	49.14

Figure 23
Earnings and Profitability of Banks: 2004 - 2008



5.06 MARKET SHARE OF THE TEN LARGEST BANKS

In 2008, the 10 largest banks held 71.8 percent of the total assets of the banking system and 72.3 percent of the industry deposit liabilities as against 71.4 percent and 70.6 percent of assets and deposits, respectively, in 2007. However, their share of total credits decreased from 74.2 percent in 2007 to 72.9 percent in 2008. In terms of capitalization, the 10 banks controlled 71.8 percent in 2008 as against 76.6 percent in 2007.

5.07 EFFICIENCY OF OPERATIONS

The efficiency of operations in the banking industry improved in 2008. The industry recorded return on assets of 3.95 percent in 2008 as against 3.89 percent in 2007. The cost efficiency ratio was 31.77 percent 2008 as against 65.9 percent in 2007. However, in terms of return on equity, the industry recorded a ratio of 22.01 percent in 2008 as against 23.84 percent in 2007. The reduction in the ratio was due to the increase in the capital of banks in 2008 which did not generate correspondent profit after tax. The table below highlights some ratios used to measure the operating efficiency of the banks.

Table 3
Efficiency of Operations of Nigerian Banks from 2004 to 2008
(Percent)

	2004	2005	2006	2007	2008
Interest Margin	55.87	54.37	60.15	52.25	54.80
Return on Assets	3.12	1.85	1.61	3.89	3.95
Return on Equity	27.35	12.97	10.60	23.84	22.01
Operating Cost Efficiency Ratio	77.03	39.97	71.43	65.90	31.77

Figure 24
Trend of Net Interest Margin of Banks: 2004 - 2008

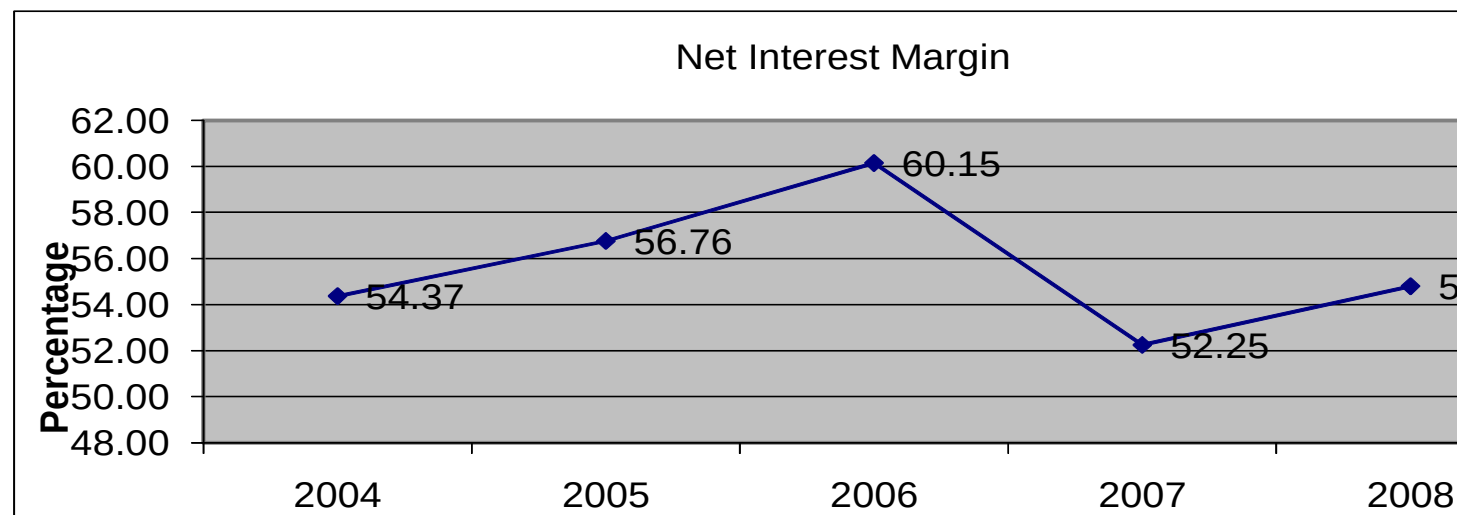


Figure 25
Return on Capital Employed: 2004 - 2008

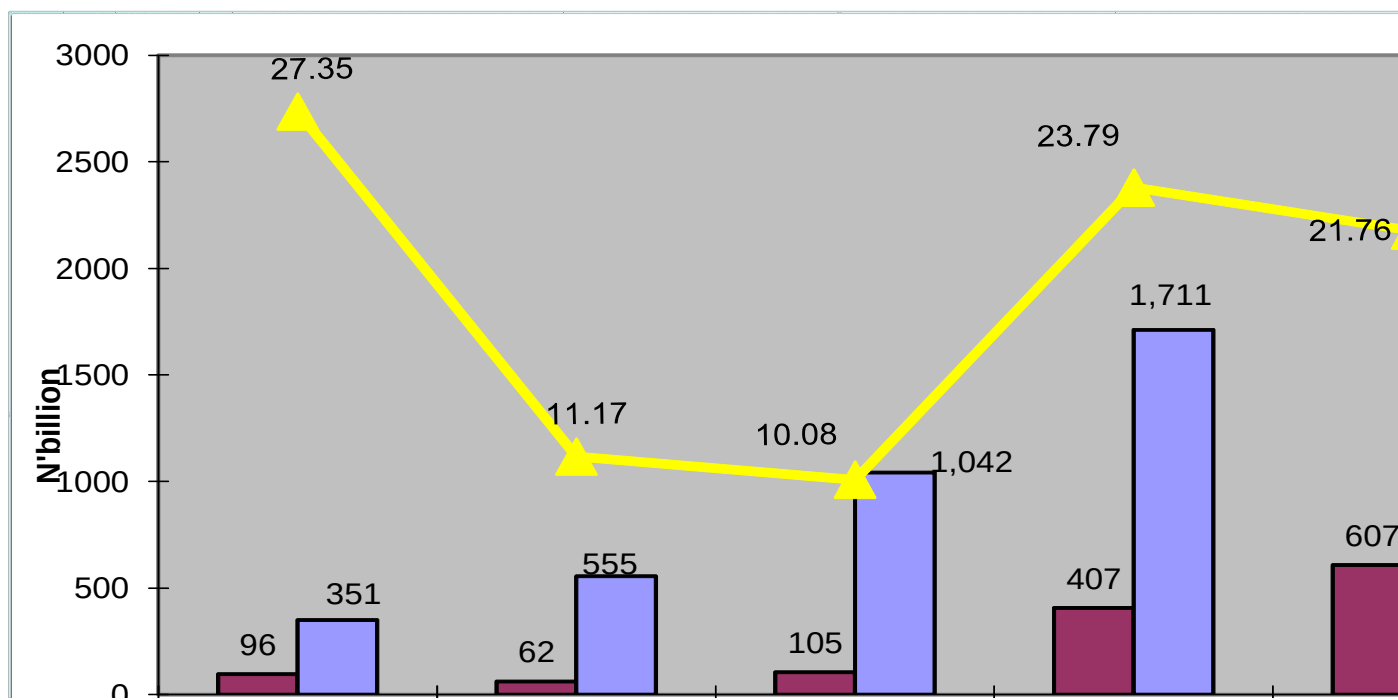
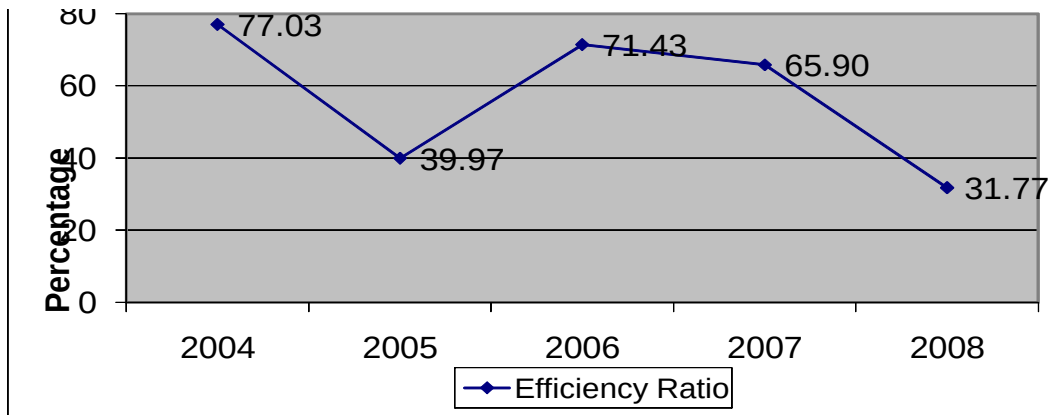


Figure 26
Efficiency Ratio of the Banking System: 2004 - 2008



5.08 OTHER FINANCIAL INSTITUTIONS SUB-SECTOR

The key financial indicators of all the institutions in the sub-sector recorded appreciable growth during the year under review.

Microfinance Banks (MFBs)

The total assets of MFBs increased from N75.5 billion in 2007 to N122.7 billion in 2008, representing an increase of 62.5 percent.

The major components of the total assets were loans and advances N42.75 billion, placements N26.25 billion and balances with banks N17.46 billion, representing for 34.8 percent, 21.4 percent and 14.2 percent, respectively. The assets of the MFBs were largely funded by deposit liabilities of N61.17 billion and shareholders' funds of N37.02 billion.

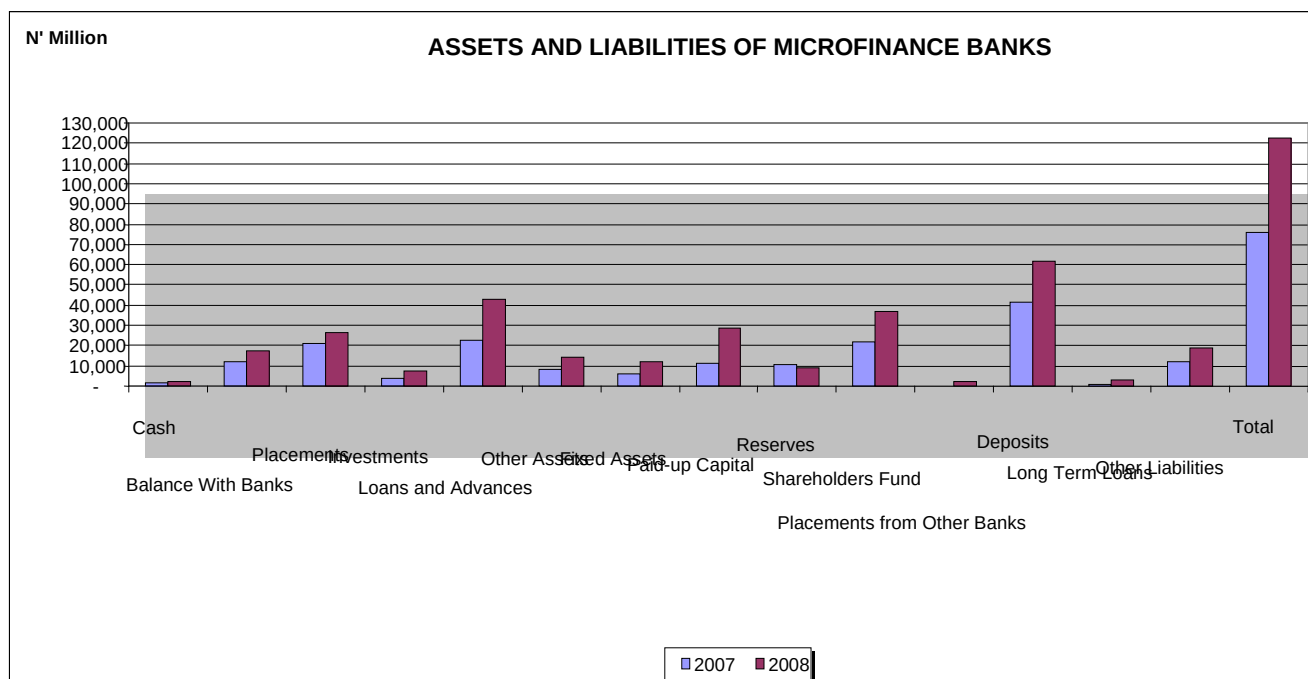
Details of MFBs' financial statistics are shown in table 4.

Table 4
ASSETS AND LIABILITIES OF MFBs (END-DECEMBER)

	2007	%	2008	%	VARIANCE	PERCENT
ASSETS	N'000		N'000		N'000	CHANGE
Cash	1,410,122	1.9	2,292,586	1.9	882,464	62.6
Balances with Banks	11,801,327	15.6	17,458,886	14.2	5,657,559	47.9
Placements	21,381,543	28.3	26,246,792	21.4	4,865,249	22.8
Investments	3,715,676	4.9	7,295,318	5.9	3,579,642	96.3
Loans and Advances	22,850,226	30.2	42,752,990	34.8	19,902,764	87.1
Other Assets	8,141,945	10.8	14,469,789	11.8	6,327,844	77.7
Fixed Assets	<u>6,249,078</u>	8.3	<u>12,237,353</u>	10.0	5,988,275	95.8
TOTAL ASSETS	<u>75,549,917</u>	100.0	<u>122,753,714</u>	100.0	47,203,797	62.5
FINANCED BY:						
Paid-up Capital	11,203,112	14.8	28,340,254	23.1	17,137,142	153.0
Reserves	<u>10,607,658</u>	14.0	<u>8,681,521</u>	7.1	(1,926,137)	(18.2)
Shareholders Fund	21,810,770	28.9	37,021,775	30.2	15,211,005	69.7
Placements from Other Banks	290,500	0.4	2,081,648	1.7	1,791,148	616.6
Deposits	41,217,713	54.6	61,568,100	50.2	20,350,387	49.4
Long Term Loans	497,881	0.7	3,033,965	2.5	2,536,084	509.4
Other Liabilities	<u>11,733,053</u>	15.5	<u>19,048,226</u>	15.5	7,315,173	62.3
TOTAL LIABILITIES	<u>75,549,917</u>	100.0	<u>122,753,714</u>	100.0	47,203,797	62.5

Figure 27

ASSETS AND LIABILITIES OF MFBs (END-DECEMBER)



a) Primary Mortgage Institution

The asset base of PMIs stood at N329.83 billion in 2008 compared to N202.79 billion in 2007, indicating a growth of N127.04 billion or 62.6 percent.

The analysis of the balance sheet of the PMIs showed that loans and advances of N108.53 billion constituted 32.9 percent of the total assets. Other major asset components were Balances with banks of N102.82 billion and investments of N69.83 billion, representing 31.2 percent and 21.2 percent, respectively, of the total assets as at end 2008. The assets were mainly funded by deposit liabilities of N166.23 billion (50.4 percent) and shareholders' funds of N70.35 billion (21.3 percent).

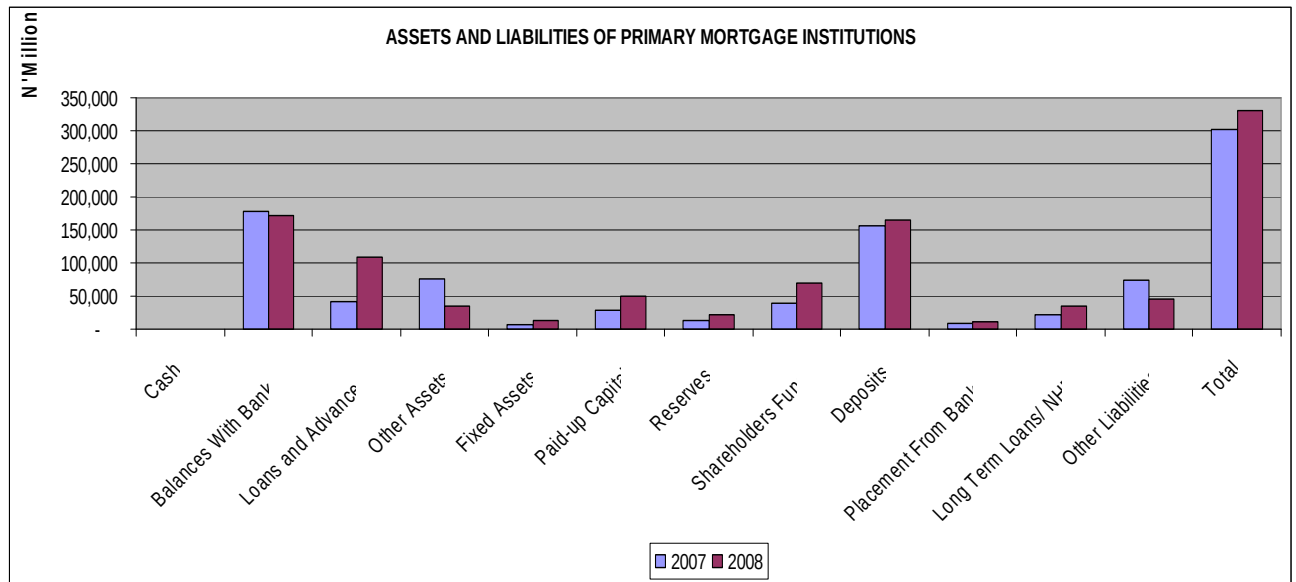
Table 5 and Figure 28 show the comparative financial statistics of the PMI sub-sector for 2007 and 2008.

TABLE 5**ASSETS AND LIABILITIES OF PMIs
(END DECEMBER)**

ASSETS	2008		2007		VARIANCE	%
	=N='000	%	=N='000	%	=N='000	CHANGE
Cash	779,044	0.2	1,263,565	0.6	(484,521)	(38.3)
Balances with Banks	102,817,759	31.2	64,576,370	31.8	38,241,389	59.2
Investments	69,829,210	21.2	28,483,588	14.0	41,345,622	145.2
Loans and Advances	108,531,488	32.9	39,430,612	19.4	69,100,876	175.2
Other Assets	35,005,045	10.6	61,637,071	30.4	(26,632,026)	(43.2)
Fixed Assets	12,865,413	3.9	7,396,818	3.6	5,468,595	73.9
TOTAL	329,827,959	100.0	202,788,024	100.0	127,039,935	62.6
FINANCED BY:						
Paid-up Capital	49,183,956	14.9	22,676,181	11.2	26,507,775	116.9
Reserves	21,161,184	6.4	10,399,387	5.1	10,761,797	103.5
Shareholders' Fund	70,345,140	21.3	33,075,568	16.2	37,269,572	112.7
Deposits	166,234,932	50.4	124,122,936	61.2	42,111,996	33.9
Placements from Banks	11,729,080	3.6	9,136,001	4.5	2,593,079	28.4
Long Term Loans/NHF	35,038,451	10.6	12,168,494	6.0	22,869,957	187.9
Other Liabilities	46,480,356	14.1	24,285,025	12.0	22,195,331	91.4
TOTAL	329,827,959	100.0	202,788,024	100.0	127,039,935	62.6

Figure 28

ASSETS AND LIABILITIES OF PMIs: 2007 - 2008



b) Finance Companies (FCs)

The total assets of FCs increased from N65.8 billion in 2007 to N134.19 billion in 2008, representing a growth of 103.92 percent. Analysis of the balance sheet of the FCs showed that loans and advances of N50.39 billion constituted 37.6 percent of the total assets. Other major asset components were investment of N34.44 billion and placement of N21.79 billion, representing 25.7 percent and 16.2 percent, respectively, of the total assets as at end 2008. The assets were mainly funded by total borrowings of N83.13 billion (62.0 percent) and shareholders' funds of N25.21 billion (18.8 percent).

Table 6 and figure 29 show the comparative financial statistics of the FCs for 2007 and 2008.

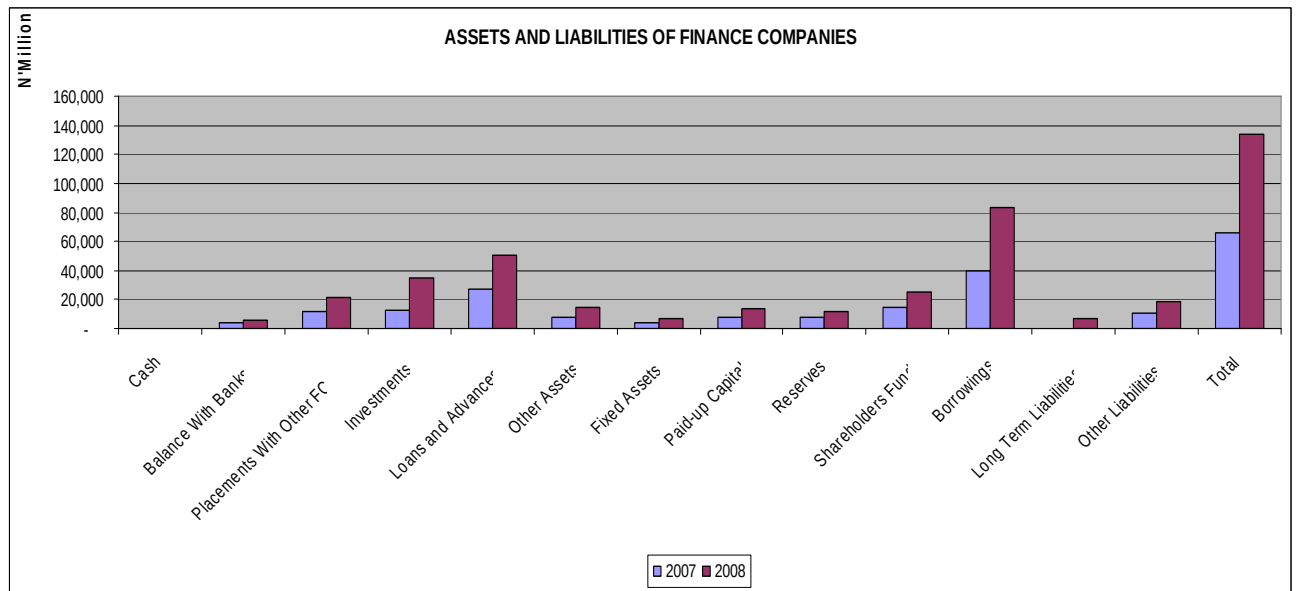
TABLE 6

ASSETS AND LIABILITIES OF FINANCE COMPANIES
(END DECEMBER)

ASSETS	2008	%	2007	%	VARIANCE	% CHANGE
	=N='000		=N='000		=N='000	
Cash	92,966	0.1	98,218	0.1	(5,252)	(5.35)
Balances with Banks	5,877,350	4.4	3,721,876	5.7	2,155,474	57.91
Placements	21,791,915	16.2	11,458,926	17.4	10,332,989	90.17
Investments	34,442,271	25.7	12,755,959	19.4	21,686,312	170.01
Net Loans and Advances	50,388,474	37.6	26,779,136	40.7	23,609,338	88.16
Other Assets	14,711,470	11.0	7,302,922	11.1	7,408,548	101.45
Fixed Assets	6,882,558	5.1	3,687,610	5.6	3,194,948	86.64
TOTAL	134,187,004	100.0	65,804,647	100.0	68,382,356	103.92
FINANCED BY:						
Paid-up Capital	13,253,600	9.9	7,435,750	11.3	5,817,850	78.24
Reserves	11,952,237	8.9	7,421,038	11.3	4,531,199	61.06
Shareholders' Fund	25,205,837	18.8	14,856,788	22.6	10,349,049	69.66
Long Term Liabilities	7,108,852	5.3	156,741	0.2	6,952,111	4,435.41
Total Borrowings	83,132,942	62.0	39,948,464	60.7	43,184,478	108.10
Other Liabilities	18,739,373	14.0	10,842,654	16.5	7,896,719	72.83
TOTAL	134,187,004	100.0	65,804,647	100.0	68,382,356	103.92

Figure 29

ASSETS AND LIABILITIES OF FCs: 2007 - 2008



c) Development Finance Institutions (DFIs)

The total assets and shareholders' funds of the four reporting DFIs, namely BOI, NEXIM, FMBN and NACRDB, stood at N158.9 billion and N39.0 billion, respectively, as at end 2008.

The breakdown of the assets and shareholders' funds was as follows:

	Total Assets	Shareholders' funds
	N' billion	N' billion
BOI	47.95	19.6
NEXIM	20.96	10.8
FMBN	49.78	(2.2)
NACRDB	40.22	6.4
TOTAL	158.90	37.0

CHAPTER SIX: CAPACITY BUILDING FOR SUPERVISION

6.01 TRAINING AND DEVELOPMENT

The CBN implemented several local and foreign training programmes in order to equip supervisors with the requisite knowledge and skills to deliver on its mandate of ensuring a safe and sound banking system.

Local Training

A total of 821 local training slots covering Basel II, Consolidated Supervision, Risk-based Supervision, Financial Markets/Products, Anti-money Laundering, Microfinance Banking, Corporate Governance and Bank Examiners' courses were utilized during the year.

Corporate Governance

Given the importance of corporate governance to the health of the banking system, a stakeholders' workshop on "Compliance Monitoring of Code of Best Practices in Bank Corporate Governance" took place at the Gateway Hotel, Abeokuta from April 7 – 18, 2008. A total of 220 participants, drawn from the CBN, NDIC, SEC and the deposit money banks, were in attendance.

Consolidated Supervision

A training programme on consolidated supervision of banks/financial institutions was held at the CBN Abeokuta branch from May 5 to August 29, 2008. The programme was designed to explore the nature, importance and the techniques for the implementation of consolidated and risk-based supervision. A total of 320 bank supervisors participated in the training.

Financial Products

An in-plant course on financial derivatives for 128 bank supervisors was organized from February 25 to March 21, 2008. The programme covered current developments in forwards, futures, options and swaps.

Basel II

The Office of the Superintendent of Financial Institutions, Canada, organized training programmes during the year on Basel II, RBS Soft Skills and Insurance Supervision. In addition to the CBN, participants were drawn from the NDIC and NAICOM.

Foreign Training

A total of 116 bank supervisors participated in various foreign capacity building programmes. Technical assistance was received from the Federal Deposit Insurance Corporation, the Federal Reserve Bank and the World Bank, all in the U.S.A. The courses included Examination Management, Loan Analysis, Introduction to Examination, Financial Institutions Analysis and Bank Management. In the same vein, the CBN provided training/technical assistance for some regulatory agencies in Nigeria as well as some African countries.

During the year, a team of bank supervisors undertook a study visit to Malaysia as part of efforts to develop non-interest banking in Nigeria.

In line with its core values, the CBN would continue to place emphasis on capacity building to ensure that bank supervisors are empowered to effectively regulate the Nigerian banking industry.

6.02 INTERIM CAPACITY BUILDING FOR MFB OPERATORS AND DIRECTORS

Following the introduction of the Microfinance Policy, Regulatory and Supervisory Framework for Nigeria and the licensing of microfinance banks, there was the need for the development of a critical mass of sustainable microfinance institutions, with strong organizational structures and management resources.

Towards this end, the development of skilled and knowledgeable human resource to manage the nascent microfinance banking sub-sector on a sustainable basis became imperative. Indeed, on-site examination reports revealed that most of the institutions, especially those that converted from community banks to MFBs, were far from embracing the new concept of microfinance banking, owing largely to knowledge and skill gaps. There was therefore, the need to develop institutional capacity to ensure that microfinance banks avoid the pitfalls which characterized the operations of the erstwhile community banks.

Specifically, the skill-gaps and challenges faced by operators, which the regulatory authorities perceived as capable of impacting adversely on the operations of the banks, included the following:

- Poor understanding of the microfinance concept;
- Inadequate knowledge and lack of skills in microfinance models;
- Inappropriate product design and pricing;
- Inability to identify target markets/clients;
- High operational cost;
- Poor risk management systems;
- Weak internal control systems;
- Poor corporate governance; and
- Poor understanding of the Regulatory Guidelines for Microfinance Banks.

To address these challenges, a capacity building workshop for the operators was designed as an interim measure, pending the take-off of the planned microfinance certification programme.

Objective of the Workshop

The objective of the workshop was to address the observed mission drift and re-orientate the operators to adopt basic microfinance service delivery models and best practice. The workshop was, therefore, aimed at refocusing the microfinance banks on their core business and preventing them from derailing even before the advent of the formal certification programme.

The workshop was organized in two phases in September and November, 2008. The first phase was organized for the management staff, while the second was for the non-executive directors of the microfinance banks.

The first phase of the workshop, held in eight centres nationwide from September 1 - 12, 2008, was attended by 2,718 participants from 723 microfinance banks. Similarly, the second phase held in four centres from November 10 - 15, 2008, was attended by 1,150 participants from 612 microfinance banks.

The broad topics covered at the workshop were:

- Concept and Principles of Microfinance;
- Credit and Marketing in Microfinance;
- Organizational, Operational and Staffing Structure for Microfinance Banks;
- Corporate Governance Issues in Microfinance Banks;
- Accounting for Microfinance Institutions;

- Management Information Systems in Microfinance Banks;
- Risk Management Systems in Microfinance Banks;
- Business Planning in Commercial Microfinance;
- Fraud Detection Techniques in Microfinance Banks; and
- Regulatory Guidelines/Challenges of Rendering Monthly Returns.

Experienced foreign and local microfinance experts and practitioners constituted the faculty for the workshop.

Learning Points

The following major learning points were brought to the fore from the workshop.

- The programme exposed poor understanding of the concept of microfinance banking among operators in terms of the target market, product design and client outreach optimization.
- Some microfinance banks, especially the newly established ones, were operating as mini-universal banks, as evidenced by their product offerings and service delivery methodology.
- The need to establish the microfinance certification programme, as obtainable in other jurisdictions, to ensure sustainable capacity building in the sub-sector, was further reinforced.
- The need to review the Regulatory and Supervisory Guidelines for Microfinance Banks in Nigeria to address genuine concerns of operators in the area of permissible and prohibited activities, penalties etc.

Impact of the Workshop

From the reaction of the participants, the impact of the capacity building programme included:

- the re-orientation of operators to proper understanding of the microfinance concept, methodology and best practice; and
- a better understanding of the provisions of the Regulatory and Supervisory Guidelines for Microfinance Banks in Nigeria.

The inauguration of microfinance banking in Nigeria threw up the challenge of inadequate human capacity, capable of derailing the objectives of the microfinance policy. The interim capacity building workshop was one in a series of programmes that would be sustained by the CBN to ensure adequate capacity for the microfinance banking sub-sector.

6.03 THE BANK EXAMINERS' CONFERENCE AND RETREAT

The Bank Examiners' Conference and Retreat were held at the Gateway Hotel, Abeokuta, from June 19 to 21, 2008, with the theme: "From Compliance Examination to Risk-based Supervision".

The Director, Banking Supervision Department, delivered the welcome address while the keynote address and the goodwill message were delivered by the representatives of the Deputy Governor (Financial Sector Surveillance), CBN and the Managing Director, Nigeria Deposit Insurance Corporation, respectively.

The conference was facilitated by Saike Green Resources International in conjunction with the Risk Reward Limited, UK and Pulse Professionals. Participants were drawn from CBN, SEC, NAICOM and deposit money banks.

Four papers were presented at the conference, namely:

- RBS as an Effective Tool of Banking Supervision;
- Regulatory Challenges in the Implementation of RBS;
- Consolidated Supervision in an Emerging Market; and
- Corporate Governance Practices in the Nigerian Banking System and the Challenges to Regulators.

During the sessions, experiences in other jurisdictions were reviewed and supervisors advised to develop appropriate risk-based supervisory techniques for the Nigerian environment. Also, the following issues, which were hitherto not prominent in the existing risk management framework, were raised.

- The need for financial institutions to maintain risk registers.
- Provision of information on banks' internal operational loss and credit loss data on a consolidated basis, which is consistent, scaled and relevant.

- Determination of the financial institutions risk appetite and the communication of such to the CBN.
- Risk-based internal audit functions in the financial institutions.
- Scenario modeling, stress testing and sensitivity analysis.
- Banks with cross-border branches deserving more regulatory attention.
- Preparing appropriate regulations for the emergence of securitization and financial derivatives in the Nigerian financial market.

Participants were grouped into four to brainstorm along the lines of the papers that were presented and the recommendations of the groups were discussed at the plenary session.

The plenary session identified the following as the main challenges to the implementation of risk-based supervision.

- Integrity of data submitted by financial institutions.
- Obtaining internal operational loss and credit loss data on a consolidated basis.
- Skill and knowledge gap among the operators and the regulators.
- Risk management and corporate governance practices among banks, which may not conform with international best practice.
- Development of risk management models that may capture the peculiar situations in the Nigerian economy.
- Provision of tools for bank examiners to monitor and capture early warning signals.
- Understanding the various products and markets in which the financial institutions operate.
- Macroeconomic policies and their effects on the financial institutions.
- Risk management of subsidiaries of Nigerian banks, especially offshore.

At the end of the conference/retreat, the following recommendations were made.

- Financial institutions should maintain risk registers as part of the institutions' implementation of the risk management system.
- Internal audit functions should be risk-based.
- Scenario modeling and stress-testing should form an integral part of the risk management system.
- There should be improved cross-border and cross-sector collaboration by regulators.
- Directors of financial institutions should be trained on best corporate governance practices.
- The current banking regulations should be reviewed to grant the CBN powers to conduct consolidated supervision.
- Guidelines for securitization and derivatives should be prepared.
- There should be continuous capacity building for examiners, especially in risk-based and consolidated supervision.

The conference provided an insight into the RBS methodology which will assist in developing a home-grown RBS model. It also afforded participants an opportunity to review recent happenings in the global financial system, further consolidate on the gains of the banking sector reforms and chart an appropriate supervisory direction to the challenges thrown up by the implementation of risk-based and consolidated supervision as well as the CBN code of corporate governance.

6.04 OTHER FINANCIAL INSTITUTIONS DEPARTMENT RETREAT

The Retreat of the Other Financial Institutions Department (OFID) was held at Gateway Hotel, Abeokuta, Ogun State, from November 6 - 9, 2008. The theme of the retreat was "Other Financial Institutions and the Attainment of FSS 20:20: Challenges to Supervisors".

The Acting Director, OFID, in his welcome address, observed that the retreat provided the department an opportunity to review its processes, achievements and shortcomings and explore means of mitigating its major challenges.

In his keynote address, the Deputy Governor, Financial Sector Surveillance, stressed that the proposed reforms in the other financial institutions sub-sector were geared towards repositioning it for greater efficiency and the attainment of the FSS 20:20 objectives.

The theme paper of the retreat was delivered by the Managing Director, BAA Consult. He stated that the growth envisaged in the FSS 20:20 could only come from micro, small and medium scale enterprises. He also reviewed some of the challenges facing operators and supervisors in the implementation of the strategy.

Five other papers that had strategic relevance to the theme of the retreat were also delivered by eminent resource persons. These were:

- Capacity Building for Supervisors: An Imperative for Meeting Future Challenges;
- Risk-based and Consolidated Supervision;

- Corporate Governance and Risk Management Practices in MFBs and PMIs;
- The Role of Microfinance Banks and Specialized Institutions in Promoting and Sustaining the Growth of the SMEs; and
- The Proposed Reform of the PMI Sub-sector and its Implication on Affordable Housing Policy in Nigeria.

The paper on Capacity Building for Supervisors: An Imperative for Meeting Future Challenges noted that capacity building was a long-term continuing process, which gives flexibility and functionality to an organization in adapting to changing needs. Accordingly, recognizing the dynamics and fast pace of changes in the contemporary world, requires individuals and corporate entities to continuously enhance and renew their capabilities. The paper, therefore, urged that appropriate steps should be taken through capacity building to make OFID better suited to deliver on its mandates.

The Special Adviser to the Governor, (Banking Supervision), who delivered the paper on Risk-based and Consolidated Supervision, highlighted the features of the Supervisory Framework for Banks and Other Financial Institutions in Nigeria.

In the paper on Corporate Governance and Risk Management Practices in MFBs and PMIs, the Managing Director, NPF Microfinance Bank, noted that many MFBs and PMIs did not have the capacity and/or the will to put in place a robust risk management framework, nor were they able to adhere to sound corporate governance practices and principles. He urged the regulatory authorities to prepare a code of corporate governance

specifically for OFIs and ensure that the institutions put in place effective risk management frameworks.

In her paper, *The Role of Microfinance Banks and Specialised Institutions in Promoting and Sustaining the Growth of SMEs*, Managing Director, H. Pierson Associates Ltd., noted the huge untapped potentials for financial intermediation by MFBs and specialized institutions. The paper advised that MFBs and specialized institutions should provide micro loans to SMEs in an efficient and financially sustainable manner, and create linkages between the commercial banks and local groups so as to give SMEs the required leverage to conduct their activities profitably.

The Executive Secretary, Mortgage Banking Association of Nigeria (MBAN), presented a paper on *The Proposed Reform of the PMI Sub-sector and its Implication on Affordable Housing Policy in Nigeria*. He opined that, an effective housing finance system would develop automatically if the required structures were put in place. He stated that the MBAN had made a number of far-reaching recommendations for the reform of the housing sector covering land reform, capital requirement for PMIs, institutional reforms, deepening of mortgage finance, legal reform, etc.

At the end of the retreat, a communiqué with key action plans was issued, covering:

- implementation of the proposed reforms of the PMI and the FC sub-sectors;
- adoption of the Prudential and Operational Standards for DFIs;
- bridging the skill gaps in OFIs and improving competencies;

- ensuring that all OFIs adhere to regulations and the fundamentals of corporate governance;
- adoption of risk-based and consolidated supervision;
- Increasing the manning level of OFID;
- strengthening the relationship between OFID and the OFIs;
- implementation of eFASS and the creation of a robust data base in the department; and
- bridging the skill gaps of supervisors through training and the deployment of appropriate technology.

The retreat provided the participants an opportunity to learn, exchange ideas and to interact with one another in an informal atmosphere.

UPDATE ON CONSOLIDATED SUPERVISION OF BANKS IN NIGERIA

Brief on Consolidated Supervision

Consolidated Supervision is a comprehensive approach to banking supervision which seeks to evaluate the strength of an entire group to which a bank belongs, taking into account all the risks which may affect the bank, regardless of whether such risks are carried in the books of the bank or the related entities. The basic objective of consolidated supervision of banks is the promotion of the overall evaluation, both quantitatively and qualitatively, of the strength of a group to which a bank belongs, in order to assess the potential impact of other companies in the group on the operations of the bank.

Consolidated Supervision allows financial sector supervisors to understand the relationship among the legal entities and to assess and monitor how effectively the group identifies, measures, monitors and controls risks, and to recognize insipient problems.

The consolidation of the Nigerian banking sector, had led to the emergence of 25 well capitalized banks in 2006 and in the subsequent market induced merger, further reduced the number of banks in Nigeria to 24 in 2007. Most of the banks have since embarked on cross-sector and cross-border operations. Financial conglomerates had thus emerged covering insurance, securities trading etc. In the absence of consolidated supervision, the risks in these conglomerate banking structures could escape supervisory attention. Therefore, concerned that such group structures would complicate risk assessment and render it difficult for banks to identify the distribution of risks in the constituents of their groups and in line with global best practice, the CBN commenced the move towards addressing such supervisory concerns

with the planned adoption and implementation of consolidated supervision of banks in Nigeria.

Identified Targeted Achievements

1. Development of a supervisory framework for consolidated supervision
2. Development of the required capacity for the effective implementation of Consolidated Supervision through staff training and other initiatives
3. Consultation with relevant stakeholders
4. Full implementation of Consolidated Supervision

Achievements/Milestones

Some key achievements which have been recorded so far include the following:

- ★ A “Draft Framework for Consolidated Supervision of Banks in Nigeria” was jointly developed by the CBN and NDIC in 2007 and issued as exposure draft.
- ★ As a further demonstration of its commitment to implement Consolidated Supervision, the CBN in conjunction with the Office of the Superintendent of Financial Institutions (OSFI), Canada, organized various capacity building seminars in 2007 and 2008 in Abuja and Lagos, which drew participants from the CBN, NDIC and other regulatory agencies in Nigeria as well as The Gambia and Sierra-Leone.

- ★ The BSD in 2007 began the process of harmonizing the accounting year end of entities within banking groups. A census of banks' subsidiaries and their accounting year ends was taken during the year, thus marking a major preparatory ground work towards the consolidated supervision of banks in Nigeria. A co-terminus accounting year end of banks and their subsidiaries is expected to facilitate the assessment, analysis and comparison of the results of operations of a banking group.

- ★ In January 2008, the IMF in partnership with the DFID under its Technical Assistance Programme (TAC), engaged a Technical Advisor for the CBN to provide the much needed technical advice and hands-on guidance to aid the full implementation of Consolidated Supervision.

- ★ The CBN has signed MoU on information sharing and supervisory cooperation with other foreign regulatory agencies, such as Bank of China, Reserve Bank of South Africa, Bank of Sierra Leone, etc

- ★ The CBN in 2008 issued guidelines on banks' domestic and cross-border expansion. The guidelines for instance made the establishment of Memorandum of Understanding (MoU) with the host country supervisor a condition before a Nigerian bank would be allowed to branch into the country. The MoU will guide Home-Host supervisors' information sharing and supervisory cooperation, among others. This is a key necessity for consolidated supervision of banking institutions with cross-border locations.

- ★ The RBS framework has been revised by the Supervisory Methodology Group of the BSD to incorporate key consolidated

supervision requirements to guide the implementation of risk based and consolidated supervision of banks and other financial institutions in Nigeria.

- ★ As part of the on-going amendment of BOFIA, the BSD in concert with the Legal Services Unit had proposed draft provisions which will empower the CBN to effectively supervise banks on a consolidated basis.
- ★ As part of the fall-out of the recent meeting of the Bankers Committee, all banks agreed to adopt a common accounting year end. This will further facilitate the effective implementation of consolidated supervision in Nigeria.

Next Steps

1. Final phase of consultation with key stakeholders
2. Commencement of implementation of Consolidated Supervision
3. Continuous capacity building

APPENDICES

1. Circulars to All Banks and Other Financial Institutions
2. Major Financial Indicators of Individual Banks
3. Glossary