CENTRAL BANK OF NIGERIA
REPORT FOR THE FIRST HALF OF 2008

1.0 INTRODUCTION

Monetary targeting remained the framework of monetary policy during the first half of 2008. With a mandate to sustain low and stable inflation rate, consistent with real GDP growth target of 9.80 per cent for 2008, the Bank adopted various restrictive monetary policy measures aimed at containing excessive liquidity. The Bank continued to use the Open Market Operations (OMO) and interest rate via the Monetary Policy Rate (MPR) as the primary instruments for liquidity management, complemented by the issuance of treasury securities in the primary market and Cash Reserve Requirement (CRR). In addition, the Bank intervened in the foreign exchange market to complement domestic money market, while safety net was provided through the standing facility lending window for deposit money banks (DMBs) to square up short positions.

Table 1: Monetary Policy Targets (Growth in % except otherwise stated)

	Key Policy Target	2004	2005	2006	2007	Indicative Benchmark 2008	**Outcome Half Year 2008**
(i)	Broad Money Growth (M2)	15.00	15.04	15-17	10.00	30.00	**37.4**
(ii)	Base Money (under PSI)	-	-	N800 billion*	N860 billion*	₦1124.8 billion*	**₦1,453.9 billion**
(iii)	Aggregate credit to the domestic economy	24.50	22.54	22.50	-29.96	72.84	**51.6**
(iv)	Credit to Government	29.90	14.01	-57.2	-54.94	-5.31	**-13.9**
(v)	Credit to the private sector	30.00	25.24	30.00	30.00	33.95	**33.9**
(vi)	Inflation rate	10.00	10.00	9.00	9.00	10.0	**12.0**
(vii)	GDP	5.00	6.00	7-10	10.00	**6.55****	**6.1**

***Targets for half year**
**** Estimates**

2.0 OPERATIONS OF THE CENTRAL BANK OF NIGERIA

2.1 Liquidity Management

The economy witnessed high system liquidity, particularly towards the end of the first half of 2008. The major drivers of liquidity, included increased fiscal injection arising from the enhanced revenue allocation based on the crude oil benchmark price of

US$59.00 per barrel in contrast to the US$40.00 per barrel benchmark in 2007, Joint Venture (JV) call payments as well as the Paris Club Debt exit refund to states/local governments and the sharing of part of the excess crude proceeds. Consequently, the Bank deployed various liquidity management tools, which included the upward review of the MPR by 50 basis points, from 9.5 per cent to 10.0 per cent in April 2008, and further by 25 basis points to 10.25 per cent in June 2008. The Bank also increased the cash reserve ratio (CRR) by 100 basis points, from 3.0 to 4.0 per cent of reservable deposits with effect from June 2008. Other policy instruments were the intensive use of OMO securities, including the 2-way quotes, repo and reverse repos. The domestic money market instruments were complemented by foreign exchange market intervention at both the Wholesale Dutch Auction System (WDAS) and inter-bank markets. Although the liquidity management efforts of the Bank helped to contain the liquidity surge observed during the period, particularly in June 2008, the reserve money (RM) indicative benchmark for end-June was missed. Provisional data indicated that the RM at N1,453.9 billion, exceeded the indicative benchmark of N1,124.8 billion for end-June, 2008 by N329.1 billion.

2.2 Payments and Clearing System

The reform of the payments system was further boosted in the first half of 2008 as the clearing operations were extended to six new zones in the country. The Bank also approved the harmonisation of the two clearing cycles to three working days (T+2), to positively impact on business processes and reduce float and waiting period for receipt of value for instruments lodged in deposit money banks. The National Payment System Committee received and considered four regulatory documents as deliverables under the Payments System Vision 2020. These included:

- Regulatory framework for Mobile Payments Services to provide regulation for the use of mobile phones for payment services as well as address issues on technology, security, operations and customer protection.
- Nigeria Direct Debt Scheme Rules to regulate the provision and usage of electronic payments for consumer bill payments (e.g. utility bills).
- Transaction Switching Guidelines to standardize the operations of payments switching companies and facilitate interconnectivity of payment switches.

- Nigerian Bankers' Clearing House Rules stipulating additional provisions for automated clearing house (ACH) transactions, in addition to the existing clearing house rules.

2.2.1 Retail Payments System

Activities in the retail payments system comprising electronic payments, ATM transactions, web transactions, point of sale transactions and mobile payments improved significantly in the first half of 2008.

2.2.1.1 Cheque

The aggregate volume and value of cheques cleared rose from 7.1 million instruments and N10,128.9 billion in the first half of 2007 to 17.9 million instruments and N22,611.5 billion at end-June 2008, respectively. The development was attributed to the harmonization of the clearing cycle which effectively reduced up-country clearing cycle to T+2.

In terms of the volumes of cheques cleared, the Ibadan Clearing Zone had the highest as it accounted for 43.1 per cent of the total, followed by Lagos, Abuja and Port Harcourt with 33.7, 4.7 and 3.2 per cent, respectively. In terms of value, the Lagos Zone maintained its lead with 43.0 per cent, while Ibadan, Abuja and Port Harcourt had 22.9, 9.3 and 6.6 per cent, respectively.

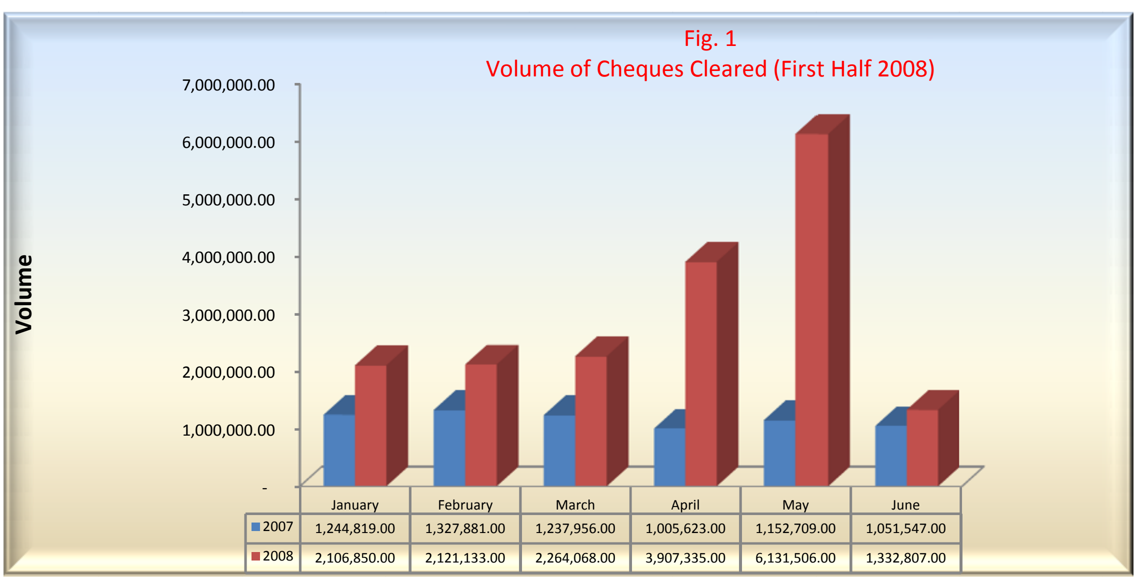
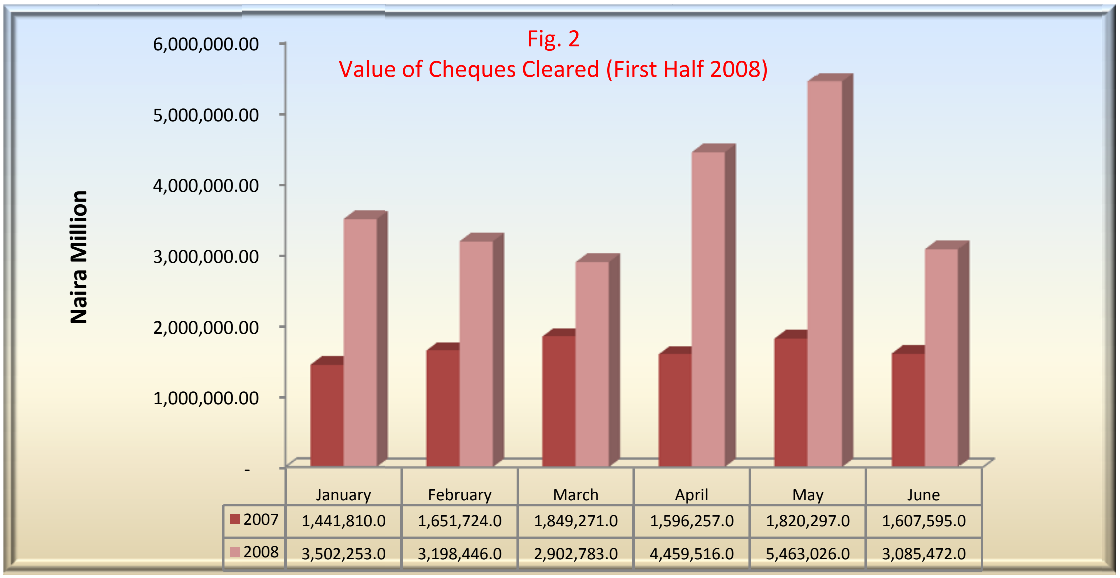


Fig. 1
Volume of Cheques Cleared (First Half 2008)

	January	February	March	April	May	June
2007	1,244,819.00	1,327,881.00	1,237,956.00	1,005,623.00	1,152,709.00	1,051,547.00
2008	2,106,850.00	2,121,133.00	2,264,068.00	3,907,335.00	6,131,506.00	1,332,807.00



2.2.1.2 Electronic Payments

The rise in the use of electronic payments was sustained in the first half of 2008, reflecting the aggressive marketing strategy of the banks and increased public awareness. Available data on various e-payment channels indicated that the Automated Teller Machine (ATM) remained the most patronized, accounting for 87.0 per cent of the total, while Point-of-Sale (POS) terminal was the least with 2.5 per cent.

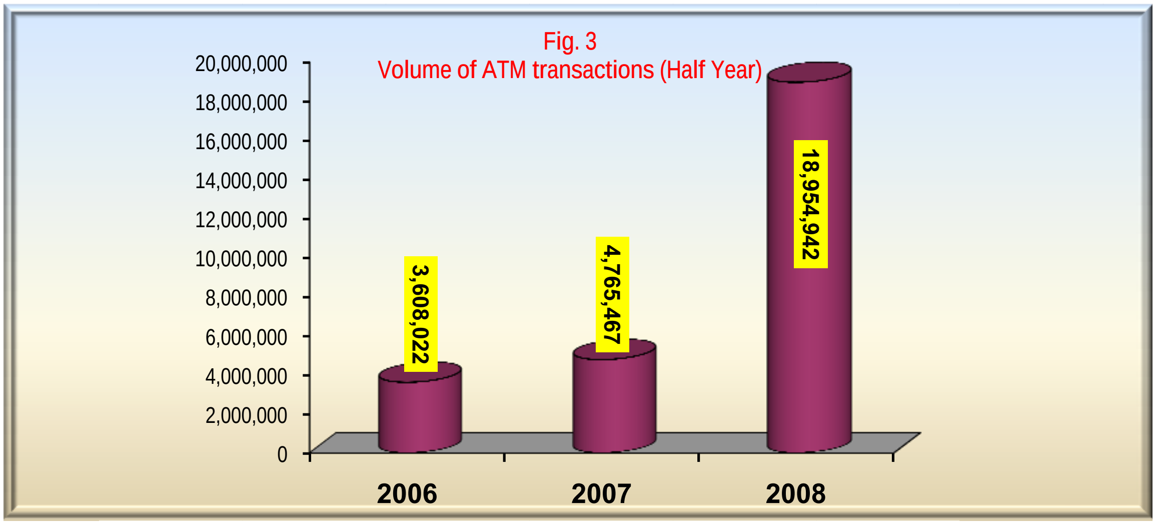
Table 2: Percentage Value and Volume of Electronic Payments

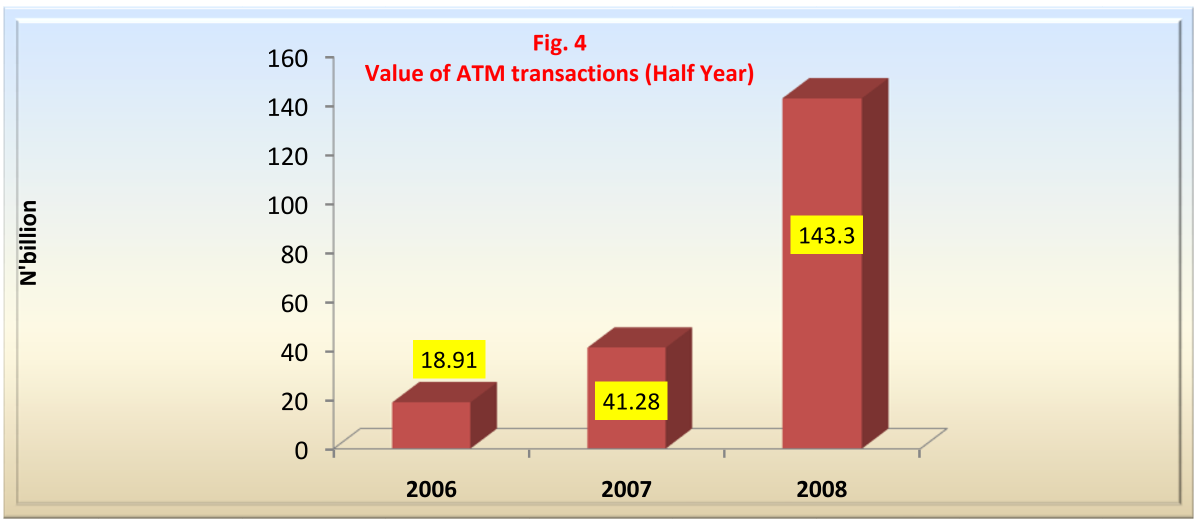
	Channel of Transaction	Per cent
Volume Terms	ATM	87.0
	Mobile	7.3
	Web (Internet)	3.2
	POS	2.5
Value Terms	ATM	90.8
	Web (Internet)	4.8
	POS	4.3
	Mobile	0.1

2.2.1.2.1 ATM Transactions

The increased patronage of ATMs was sustained in the first half of 2008, as the volume and value of transactions rose by 297.8 and 247.1 per cent to 19.0 million and N143.3 billion, respectively, over the levels in the corresponding period of 2007.

The development was attributed to the increased number of ATMs in the country, enhanced public awareness as well as the convenience of the system.



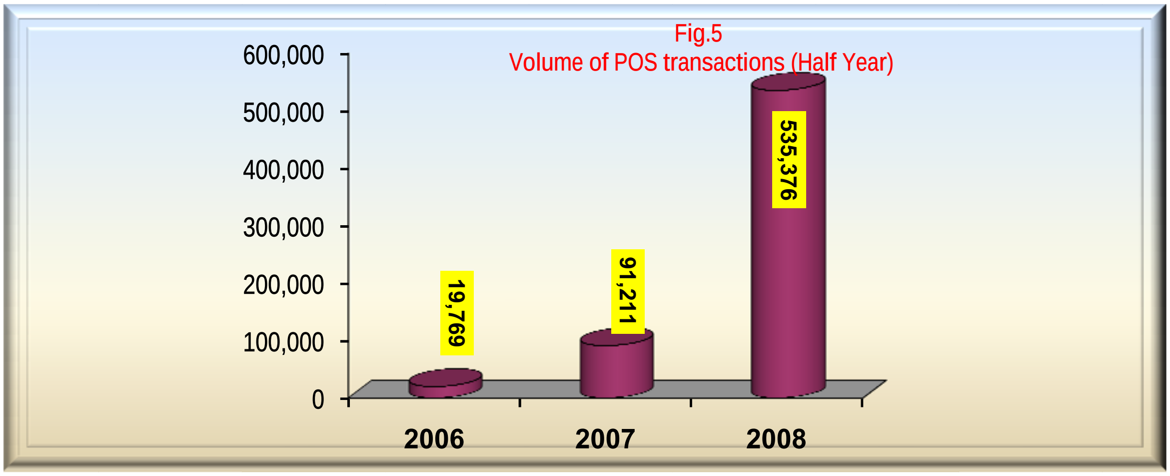


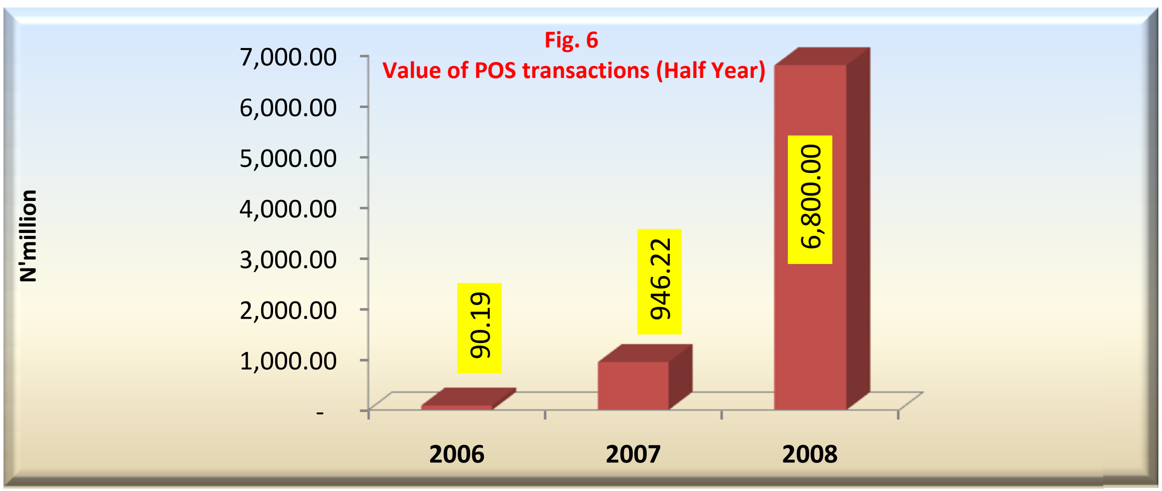
2.2.1.2.2 Web Transactions

The use of internet services for transactions increased. In terms of volume and value, the use of the internet for payments increased by 85.5 and 154.3 per cent to 684,907 and N7.6 billion, respectively, compared with 119.8 and 50.9 per cent at end-June 2007. The development was attributable to the growing number of airlines and merchants that accept payments through their websites.

2.2.1.2.3 Point of Sale (POS) Transactions

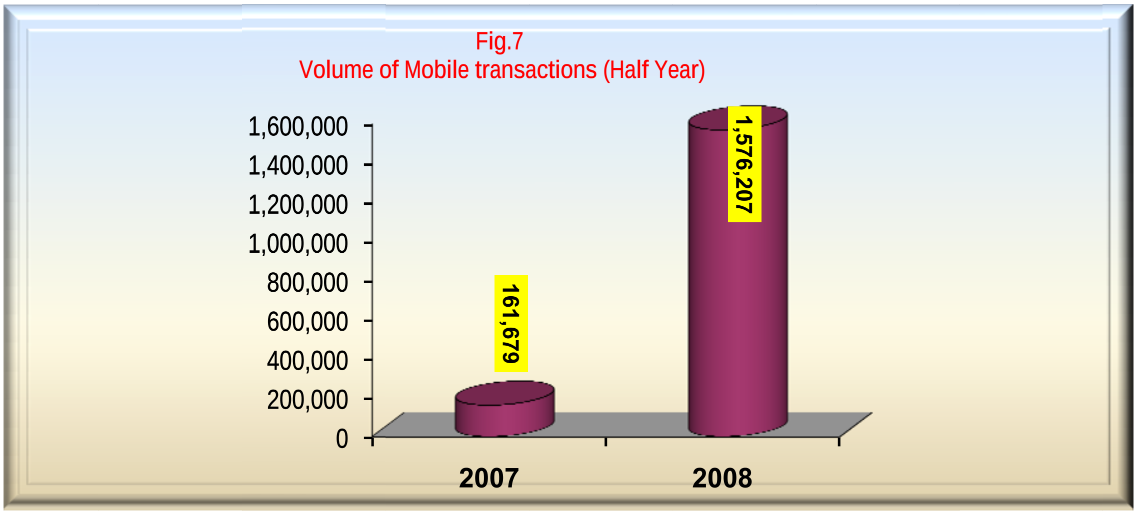
The volume and value of POS transactions increased significantly from 9,211 and ₦946.2 million in June 2007 to 535,376 and ₦6.8 billion, respectively. The development was accounted largely by the widespread use of debit cards.

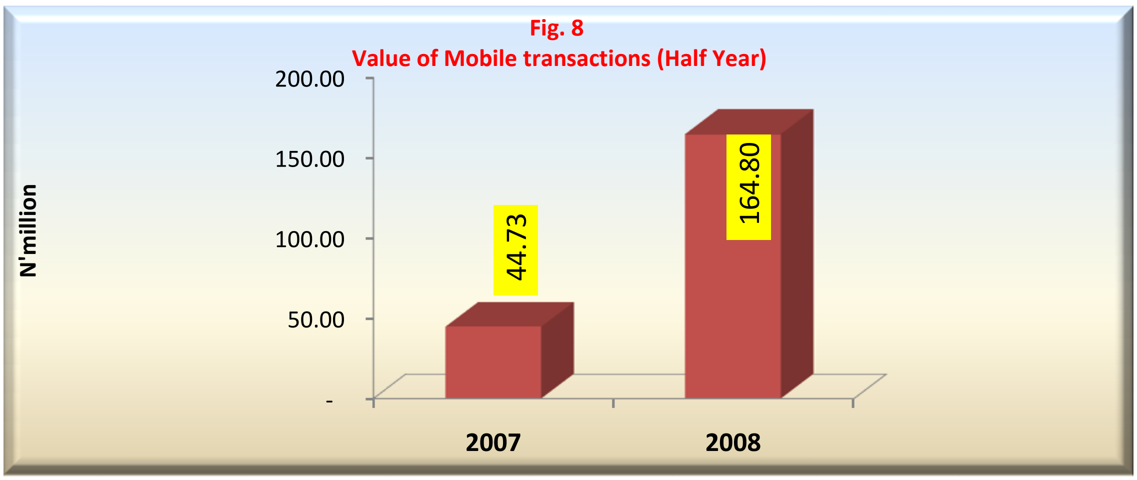




2.2.1.2.4 Mobile Payments

In the first half of 2008, the use of mobile telephones for payments increased significantly. At 1,576,207 and N164.8 million, the volume and value of payments rose by 974.9 and 368.4 per cent over the levels at end-June 2007, respectively.





2.2.2 Wholesale Payments System

The volume and value of transactions through inter-bank transfers rose by 88.4 and 49.4 per cent to 108,761 and ₦43,422.8 billion, respectively, over the levels at end-June 2007. The development was attributable largely to the adoption of the Third Party Transfer mechanism of the CBN Inter-Bank Funds Transfer System (CIFTS) for Bureaux-de-Change deposit for foreign exchange purchases.

2.3 Financial Sector Surveillance

2.3.1 Banking Supervision

The CBN intensified its surveillance activities on the banks during the first half of 2008 with the conduct of on-site verification of the deposit money banks' integration processes, as contained in their strategic business plans. The exercise revealed that out of the nineteen (19) banks that were involved in mergers and acquisitions, fourteen (14) had attained over 80 per cent level of integration, indicating that they have substantially complied with the provisions of CBN circular on integration, four (4) had attained more than 60.0 per cent but less than 80.0 per cent, while one bank achieved less than 60 per cent level of integration.

The Nigeria Deposit Insurance Corporation (NDIC), under its Purchase and Assumption (P & A) method of resolution of the 14 failed banks, invited the healthy banks to assume the private sector deposit liabilities as well as cherry-pick the assets of four (4) additional banks for which it had obtained final court orders for liquidation. Thus far, the private sector liabilities of eleven (11) banks had been assumed by four healthy banks as indicated below:

S/N	Failed Banks	Assumed By
1	Allstates Trust Bank	Ecobank Plc
2	Assurance Bank	Afribank Plc
3	Lead Bank	Afribank Plc
4	Trade Bank	UBA Plc
5	Metropolitan Bank	UBA Plc
6	City Express Bank	UBA Plc
7	Hallmark Bank	Ecobank Plc
8	African Express Bank	UBA Plc
9	Eagle Bank	Zenith Plc
10	Gulf Bank	UBA Plc
11	Liberty Bank	UBA Plc

The CBN issued a number of circulars on the operations of DMBs, which included:

- Public notice on payment of private sector depositors of some of the failed banks that had their licences revoked on January 16, 2006;
- Common accounting year-end for banks and discount houses; and
- Abolition of the policy of restriction in banks' lending rates to a maximum of 400 basis points above the MPR.

The CBN undertook the documentation of the electronic Financial Analysis and Surveillance System (e-FASS) User Requirement Specification (URS). The exercise provided detailed computerisation requirements for the analysis of returns of microfinance banks (MFBs). Strategies were also drawn up to fast track the connectivity of the other financial institutions to the e-FASS facility. In this regard, approval was given for e-FASS training of the other financial institutions (OFIs) in readiness for the commencement of the on-line rendition of returns by September 2008. A total of 315 participants from primary mortgage institutions (PMIs), development finance institutions (DFIs) and Bureaux de Change (BDCs) was expected to be trained during the programme.

2.3.2 Prudential Examination

During the period under review, income audits, verification of capital and special investigations were conducted on some banks to check the authenticity of reports/returns to the CBN. The examination focused on the level of income and profits reported in their audited accounts, liquid assets, as well as the legitimacy of funds used for re-capitalisation.

2.3.3 Banking Sector Soundness

An assessment of the health of the banking sector using Capital Adequacy, Assets Quality, Management Earning, Liquidity and Sensitivity, (CAMELS) ratings indicated that the banks were sound. The average Capital Adequacy Ratio (CAR) of the banks was consistently above the stipulated minimum of 10.0 per cent. The industry-wide liquidity ratio also exceeded the 40.0 per cent minimum requirement. Banks' earnings, in absolute terms, equally improved in the review period, although the ratio of both the returns on assets and equity declined, owing largely to the phenomenal increase in total assets and capital. The ratio of non-performing credit to industry total credit was 6.3 per cent, compared with 7.7 per cent recorded at end-June, 2007. The ratios were below the acceptable contingency threshold of 20.0 per cent for the industry.

2.3.4 Routine Examinations

Hybrid routine examinations comprised of compliance and risk-based approaches, were conducted on some DMBs and discount houses during the period under review. The exercise covered prudential regulations, foreign exchange operations, anti-money laundering controls and know-your-customer (KYC) directives. The examination on foreign exchange operations did not reveal any serious infractions, although poor record keeping, non-compliance with the rules and regulations, among others were observed in some cases and appropriate sanctions were meted out to the errant banks in such instances.

2.3.5 Financial Crime Surveillance

The mutual evaluation of Nigeria's Anti-Money Laundering/Combating Financial Terrorism (AML/CFT) efforts by the Inter-Governmental Action Group Against Money Laundering in West Africa (GIABA), which started in October 2007, progressed with the final report expected within the second half of the year. The Bank and other stakeholders, ensured compliance with the AML/CFT laws and other related measures for Nigeria to remain off the list of the Financial Action Task Force (FATF). It also co-operated with and assisted local and foreign law enforcement agencies in the arrest and prosecution of persons involved in financial crimes.

2.3.6 Compliance with the Code of Corporate Governance for Banks in Nigeria

Verification exercise on compliance with the provisions of the Code of Corporate Governance for banks issued in April 2006 was conducted by the CBN through the appraisal of the banks' monthly reports as well as periodic on-site examinations. The exercise revealed varying levels of compliance. For instance, thirteen (13) banks failed to comply with the code of succession plan, six (6) on board performance appraisal, fourteen (14) on appointment of independent directors, nine (9) on whistle blowing, five (5) on risk management strategy and another five (5) on reporting line of the head of internal audit. All the affected banks had been notified to effect compliance.

2.3.7 Examination of Other Financial Institutions (OFIs)

On-site examinations on the 2,010 OFIs, comprised of 782 microfinance banks (MFBs), 113 finance companies (FCs), 99 primary mortgage institutions (PMIs), 1,012 bureaux de change (BDCs), and 4 development finance institutions (DFIs) were conducted.

Routine examination conducted on the performance of the four (4) DFIs indicated mixed development. The trend of deterioration in asset quality as measured by the ratio of performing assets to non-performing assets was observed to be prevalent in all the institutions, while three (3) recorded improvement in their shareholders' funds. In addition, the code of corporate governance in the DFIs suffered setback following the dissolution of their Boards by the Federal Government.

The number of active FCs declined from seventy-six (76) as at end-December 2007 to fifty-five (55) at end-June 2008. Of the remaining twenty-one (21), seven (7) were undergoing restructuring, while three (3) were not found at their registered addresses.

The CBN in collaboration with the NDIC, drew up an exit strategy for the two hundred and twenty-nine (229) community banks (CBs) that failed to make the re-capitalisation/conversion programme. Of this number, ninety-one (91) submitted their records of assets and liabilities at the instance of the CBN; eighty-nine (89) CBs had no financial records, while forty-nine (49) others had long ceased operation.

Forty-nine (49) fresh applications for BDC licences were approved and one hundred and ninety-five (195) Approvals-In-Principle were granted, while eighty-six (86) others were at various stages of processing.

2.4 Foreign Exchange Management

Forty-nine (49) trading sessions were held under the Wholesale Dutch Auction System (WDAS) in the first half of 2008, as against forty-six (46) sessions in the corresponding period of 2007. Aggregate demand for foreign exchange by authorized dealers at the WDAS window and Bureaux-De-Change (BDC) amounted to US$3.60 billion and US$3.66 billion, compared with the respective amounts of US$6.59 billion and US$2.95 billion in the corresponding period of 2007. The observed decline in demand at the WDAS window was attributed to the increased trading activities at the interbank segment. Consequently, the value of foreign exchange sold by the CBN at the WDAS and BDC windows amounted to US$1.32 billion and US$3.66 billion, respectively, compared with US$5.71 billion and US$2.95 billion in the corresponding period of 2007.

At the inter-bank segment of the foreign exchange market, the CBN interventions resulted in foreign exchange purchases and sales of US$0.75 billion and US$7.87 billion, respectively. Foreign exchange swap transactions by banks amounted to US$0.95 billion, compared with US$0.61 billion in the corresponding period of 2007.

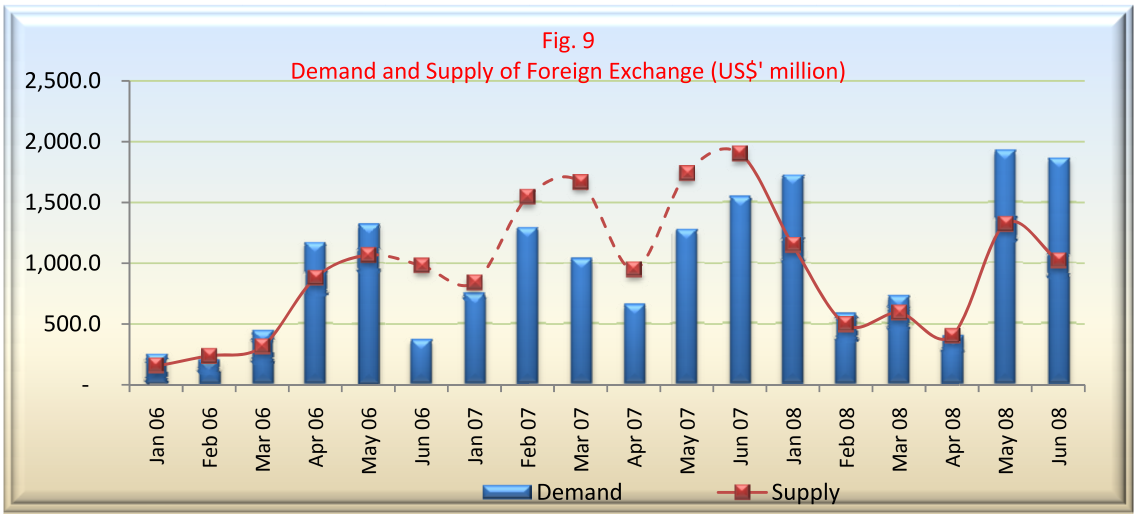
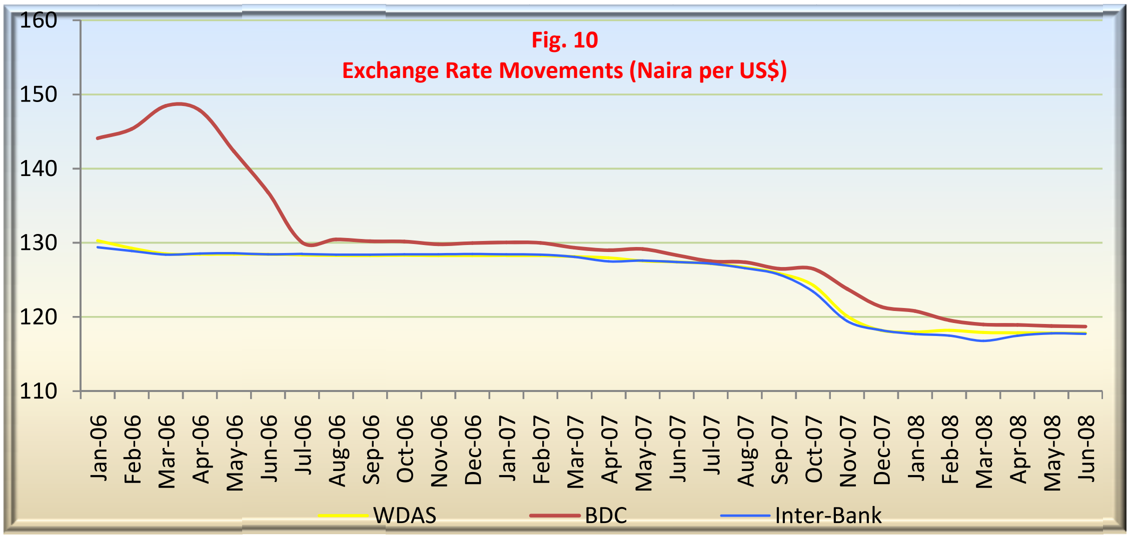
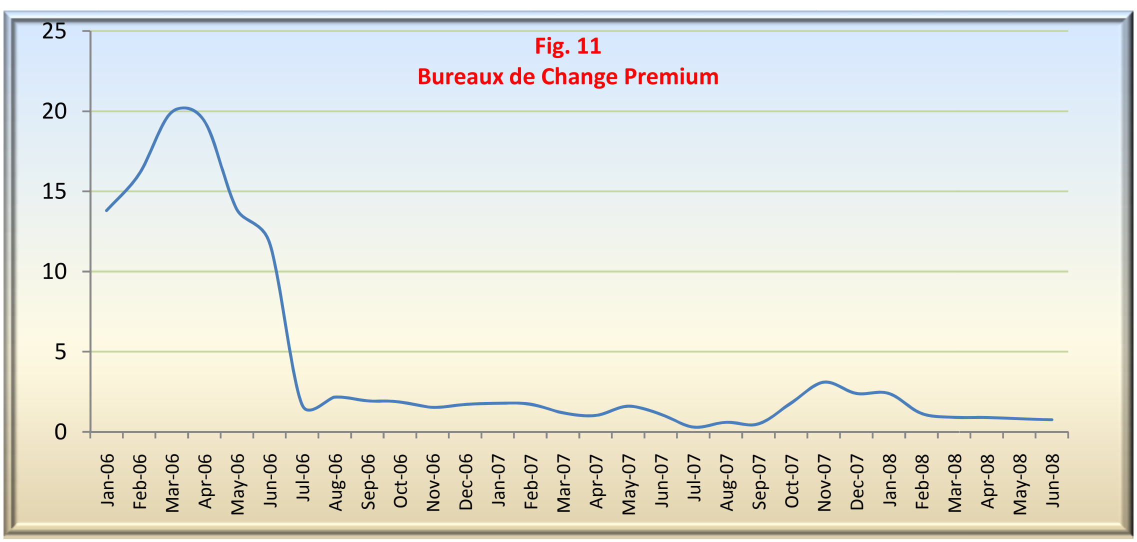


Fig. 9
Demand and Supply of Foreign Exchange (US$' million)

The average exchange rate of the naira stood at N117.94 per US dollar as against N127.94 in the corresponding period of 2007, showing an appreciation of 8.5 per cent. At the inter-bank and BDC segments of the market, the naira traded at an average of N117.50 and N119.30 per US dollar, indicating an appreciation of 8.9 and 8.4 per cent, over the levels in the preceding period of 2007, respectively. Consequently, the premium between the WDAS/BDC rates increased marginally from 1.1 per cent in the corresponding period of 2007 to 1.2 per cent.



The end-period exchange rate at the WDAS segment of the market was N117.80 per dollar, indicating an appreciation of 8.1 per cent over the level in the corresponding period. Similarly, at the inter-bank and BDC segments of the foreign exchange market, the naira exchanged at N117.75 and N119.00 per dollar, showing an appreciation of 8.2 and 7.6 per cent, respectively, over the levels in the corresponding period of 2007.

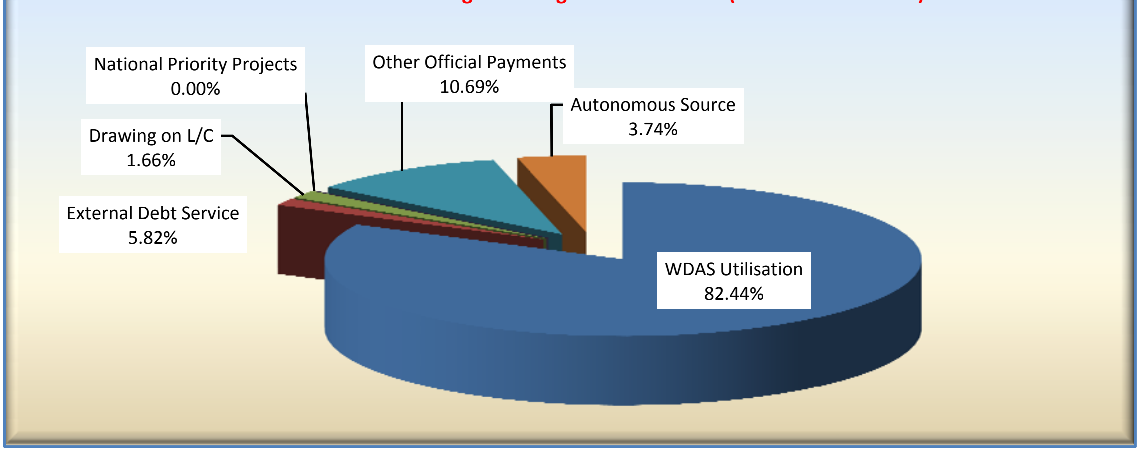


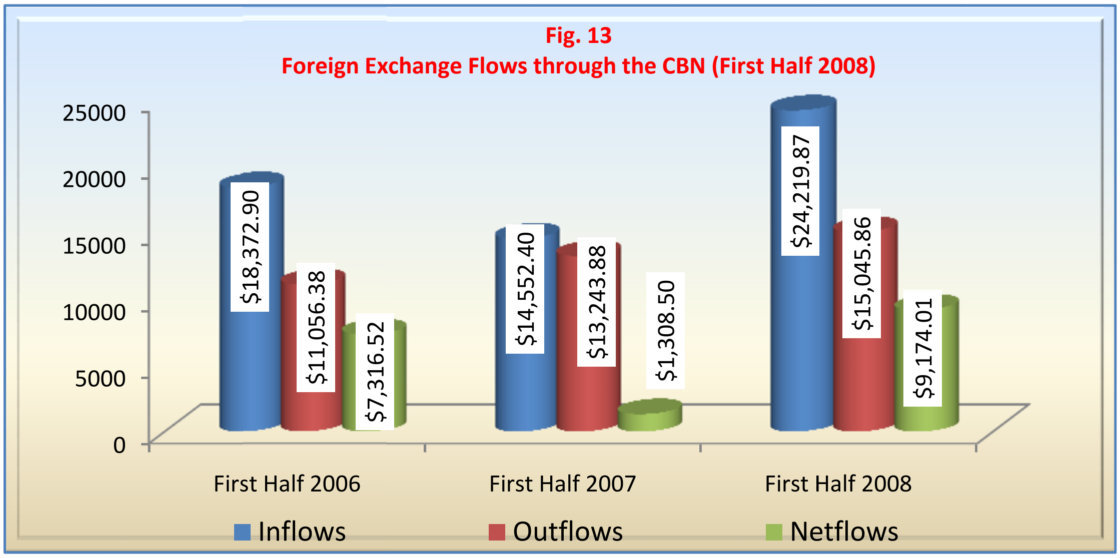
2.4.2 Foreign Exchange Flows

Foreign exchange flows through the economy for the first half of 2008, showed that total inflows increased by 85.0 per cent over the level in the corresponding period of 2007 to US$54.54 billion. Of the total, the inflow through the CBN accounted for 44.0 per cent, while autonomous sources accounted for the balance of 56.0 per cent. The development was due largely to the increased inflow into the domiciliary accounts, purchases from oil companies, capital importation and home remittances. Total foreign exchange outflow amounted to US$15.59 billion, representing an increase of 14.7 per cent over the level in the corresponding period of 2007. Consequently, a net inflow of US$38.96 billion was recorded, compared with US$15.90 billion in the corresponding half of 2007.

Transactions through the CBN showed that inflows increased by 66.4 per cent over the level recorded in the corresponding period of 2007 to US$24.24 billion. The share of oil sector in total inflow was 87.5 per cent, while the non-oil public sector receipts accounted for the balance. The total outflow increased by 13.6 per cent over the level in the corresponding period of 2007 to US$15.05 billion. The increase in outflows was due to the rise in imports as well as CBN intervention at the interbank foreign exchange market for liquidity management purposes. Overall, a net inflow of US$9.19 billion was recorded during the period, compared with US$1.31 billion in the corresponding period of 2007.

Fig. 12
Foreign Exchange Disbursements (First Half Year 2008)





Source: Foreign Operations Department (FOD)

2.4.3 Sectoral Utilization of Foreign Exchange

Aggregate sectoral utilization of foreign exchange through official and autonomous sources amounted to US$20.82 billion, showing an increase of 44.8 per cent over the level recorded in the corresponding period of 2007. Analysis of the foreign exchange utilization showed that the industrial and manufactured goods sectors accounted for 26.0 and 14.4 per cent, respectively, compared with 35.3 and 22.0 per cent in the corresponding period of 2007. The share of oil, food, transport and agriculture were 8.9, 6.6, 3.8 and 0.6 per cent, respectively. Invisible transactions namely financial, communication and education services accounted for 27.9, 3.4 and 2.8 per cent, respectively.