Making Finance Work For The Poor

Being a Convocation Lecture Delivered By

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At the Federal University of Technology, Owerri, Imo State

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Outline

I: Introduction

- The boom in the financial system and economy, and challenges of “leaving no one behind”.
- Poverty becoming Dynastic--- the “poor cannot sleep because they are hungry, and the rich cannot sleep because the poor are awake”---- in everybody’s interest to have an INCLUSIVE society.

II: POVERTY AS A NATIONAL CRISIS: Stylized Facts

- Using the World Bank's estimates (based on 1993 Purchasing Power Parity) about 2.6 billion or 40% of the world's population (2005) live in poverty with over 1 billion people in extreme poverty
- Sub-Saharan Africa has the highest incidence of extreme poverty.
- Sub-Saharan Africa is the most likely region to miss the Millennium Development Goals of reducing poverty in half by year 2015
- Less than 20% of African households own bank accounts or have access to financial services

POVERTY AS A CRISIS…

- According to 2004 surveys, 54% of Nigerians still live in poverty although down from about 70% less than a decade ago in spite of significant growth in GDP over the past five years
- Banking services are available to about 40% of the population. More than 70% of the poor do not have access to formal finance
- Total bank Credit is about 30% of GDP
- Nigeria has a highly unequal income distribution profile: about 8% of those that have access to financial services own about 90% of the available deposits

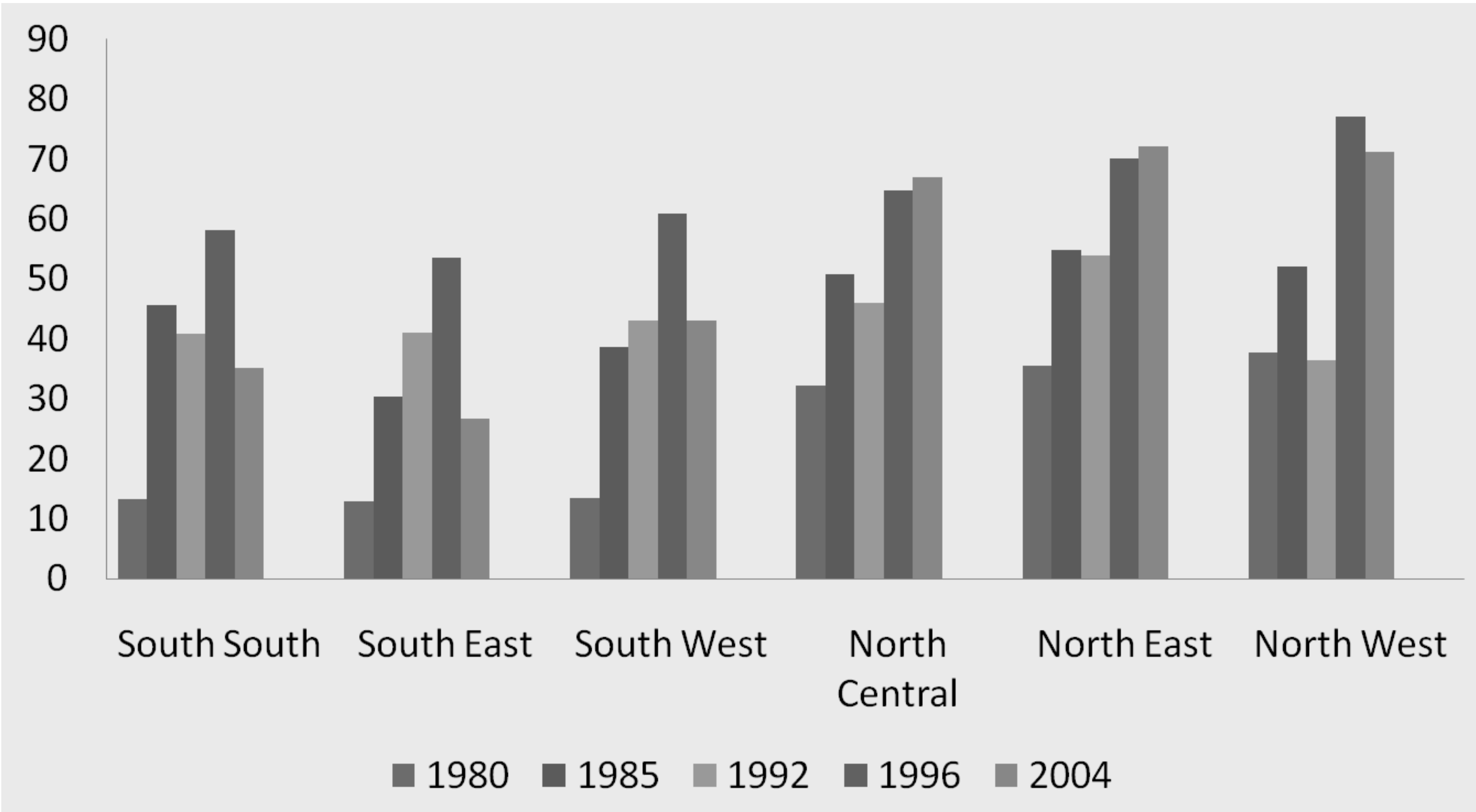
POVERTY AS A CRISIS ....

- ***PER CAPITA INCOME:*** Nigeria's per capita income is barely $1,000; USA about $32,000; South Africa over $5,300. At current population growth rate, and if GDP grows at 13% p.a, it will be in 2033 that Nigeria achieves today's per capita income of SA. At current 6% growth, it will be in 2065.
- ***POVERTY:*** 1 out of 2 Nigerians in poverty
  - Poverty becoming Dynastic– children of the poor likely to become poor due to widening gap in access to quality education and size of family
  - Spatial inequality ---- See following Tables
- ***UNEMPLOYMENT:*** Urbanization rate 5.3% as one of fastest in world, with urban youth unemployment at about 20%---- This is a TIME BOMB waiting to explode!

Poverty as a Crisis: Nigeria's Poverty Levels by Zones 1980-2004 *(latest available surveys)*

Zone	1980	1985	1992	1996	2004
South South	13.2	45.7	40.8	58.2	35.1
South East	12.9	30.4	41.0	53.5	26.7
South West	13.4	38.6	43.1	60.9	43.0
North Central	32.2	50.8	46.0	64.7	67.0
North East	35.5	54.9	54.0	70.1	72.2
North West	37.7	52.1	36.5	77.2	71.2

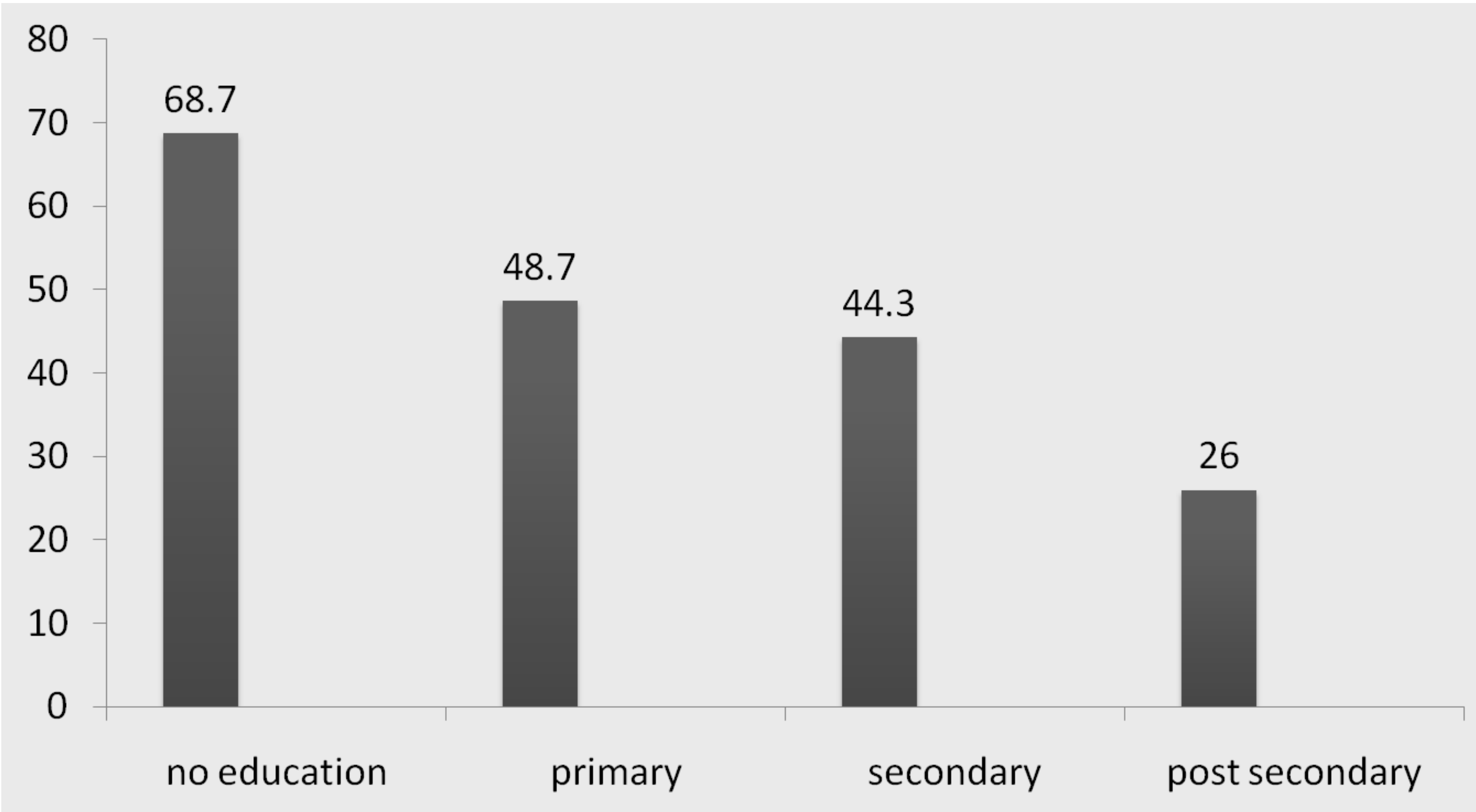
Nigeria's Poverty Levels by Zones (1980-2004)



What Explains Nigeria's Poverty Incidence?

1. Household Size: In 2004, single member households had 12.6% poverty incidence; 2-4 member households 39.3%; 5-9 member households, 57.9%; 10- 20 member households, 73%; and above 20 member households, 90.7%
2. Education: Households headed by those without education had 68.7% poverty; primary education, 48.7%; secondary, 44.3%; post secondary, 26%.
3. Occupation: Dominant in agriculture and forestry, 67%
4. Rural Areas contributed 65% to poverty in 2004
5. Orientation towards private enterprise

Poverty Incidence According to Household Head (%)



Poverty Incidence According to Household Classification (%)

III.HOW DOES FINANCE MATTER?

- Banks play intermediation role—deposit taking/lending
- Resource allocation—from surplus units to deficit units
- The financial system facilitates risk sharing—spreads/reduces risk faced by economic agents
- The financial system generates wealth in the economy
- It facilitates the exchange of goods and services
- FINANCE is the 'poverty trap breaker'--- allowing the poor to access education, health, investment, etc more than current income can allow…..

III.HOW DOES FINANCE MATTER?

- There is a substantial body of literature on the link between finance sector development (FSD), and economic growth and poverty reduction (King and Levine, 1993), (Levine and Zervos, 1998), (Rajan and Zingales, 1998) and (Levine, Loayza and Beck, 1999).

- Calomiris and Mason (2003) estimated an elasticity of real state income growth to bank loan supply growth of 45% where a one standard deviation decrease in loan growth over three years (17.9%) reduces output growth over three years by about 7 percentage points.

- Strong correlation between output and credit.

IV: Banks and the Nigerian Economy: *Recent Evidence*

Nigerian Banking Sector

- Asset Base grew by approx. 277% between 2003 and 2007
- About 11 banks with over $1 billion in Tier 1 capital, by end February, 2008.
- Microfinance Banks – 716 and more to come
- Branch Expansion outside Nigeria – 16 in Africa of which 9 are new branches; 5 outside Africa.
- Share of Banks in NSE most capitalized companies rose substantially – 30% (2003); 65% (2007)

IV: Banks and the Nigerian Economy: *Recent Evidence*

Banking System Indicator (BSI)	
BSI	**Countries**
D	Benin, Bulgaria, China, Columbia, Costa Rica, Croatia, El Salvador, Georgia, Hungary, India, Indonesia, Israel, Kazakhstan, Lebanon, Lithuania, Morocco, **Nigeria,** Panama, Peru, Philippines, Poland, Romania, Taiwan, Thailand, Turkey, Ukraine, Venezuela, Russia
E	Argentina, Armenia, Azerbaijan, Belarus, Bolivia, Dominican Republic, Ecuador, Egypt, Iran, Sri Lanka, Tunisia, Uruguay, Vietnam

Source: Fitch Ratings: Bank Systemic Risk Report, September 2007
BSI measures system quality or strength: D indicates low while E indicates very low.

IV. Banks and the Nigerian Economy: *Recent Evidence*

Macro-Prudential Indicator (MPI)	
MPI	**Countries**
1	Argentina, Austria, Benin, Bermuda, Bolivia, Chile, China, Cyprus, Dominican Republic, Ecuador, Egypt, El Salvador, Germany, Hong Kong, Hungary, Indonesia, Israel, Japan, Lebanon, Malaysia, Mexico, Morocco, **Nigeria,** Oman, Panama, Peru, Philippines, Poland, Singapore, Sri Lanka, Taiwan, Thailand, Tunisia, Uruguay
2	Armenia, Bahrain, Belarus, Belgium, Brazil, Bulgaria, Colombia, Costa Rica, Croatia, Czech Republic, Denmark, Estonia, Finland, France, Georgia, Greece, India, Ireland, Italy, Kazakhstan, Kuwait, Latvia, Lithuania, Luxembourg, Malta, Netherlands, New Zealand, Norway, Portugal, Qatar, Romania, San Marino, Spain, Slovakia, Slovenia, Switzerland, UK, US, Saudi Arabia, Sweden, Turkey, UAE, Ukraine, Venezuela, Vietnam
3	Australia, Azerbaijan, Canada, Iceland, Iran, Korea, Russia, South Africa

Source: Fitch Ratings: Bank Systemic Risk Report, September 2007
MPI measures vulnerability to systemic crises: 1 indicates low risk; 2 indicates moderate risk; 3 indicates high risk.

IV. Banks and the Nigerian Economy: *Recent Evidence*

Bank Credit to Private Sector as % of GDP						
COUNTRY	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**
BENIN	11.4	14.2	14.6	16.3	17.0	16.9
EGYPT	52.1	50.7	50.7	48.3	45.9	42.4
MOROCCO	48.5	49.3	50.3	54.4	59.4	60.7
NIGERIA 1/	18.4	20.5	21.0	21.9	21.5	31.4
TUNISIA	64.2	66.7	65.1	65.0	64.2	63.0
SOUTH AFRICA	62.4	69.1	70.0	75.2	84.2	92.1

1/ CBN data using Non Oil GDP
Source: Fitch Ratings: Bank Systemic Risk Report, September 2007

IV. Banks and the Nigerian Economy: *Recent Evidence*

Other Indicators of Financial Deepening							
Year	M2/GDP Ratio (%)	CIC/M2 Ratio (%)	COB/M2 Ratio (%)	CIC/GDP Ratio (%)	CIC/Non-oil GDP Ratio (%)	COB/GDP Ratio (%)	COB/Non-oil GDP Ratio (%)
2003	20.0	25.3	20.8	5.1	8.7	4.2	7.1
2004	19.8	24.1	20.3	4.8	7.6	4.0	6.4
2005	19.3	22.8	20.0	4.4	7.2	3.9	6.3
2006	19.8	21.2	18.8	4.2	6.7	3.7	6.0
2007	21.0	20.0	15.2	4.2	6.1	3.2	4.6

M2 is broad money stock (end period)

GDP at current basic prices.

CIC is Currency in Circulation (end period)

COB is Currency Outside Banks (end period)

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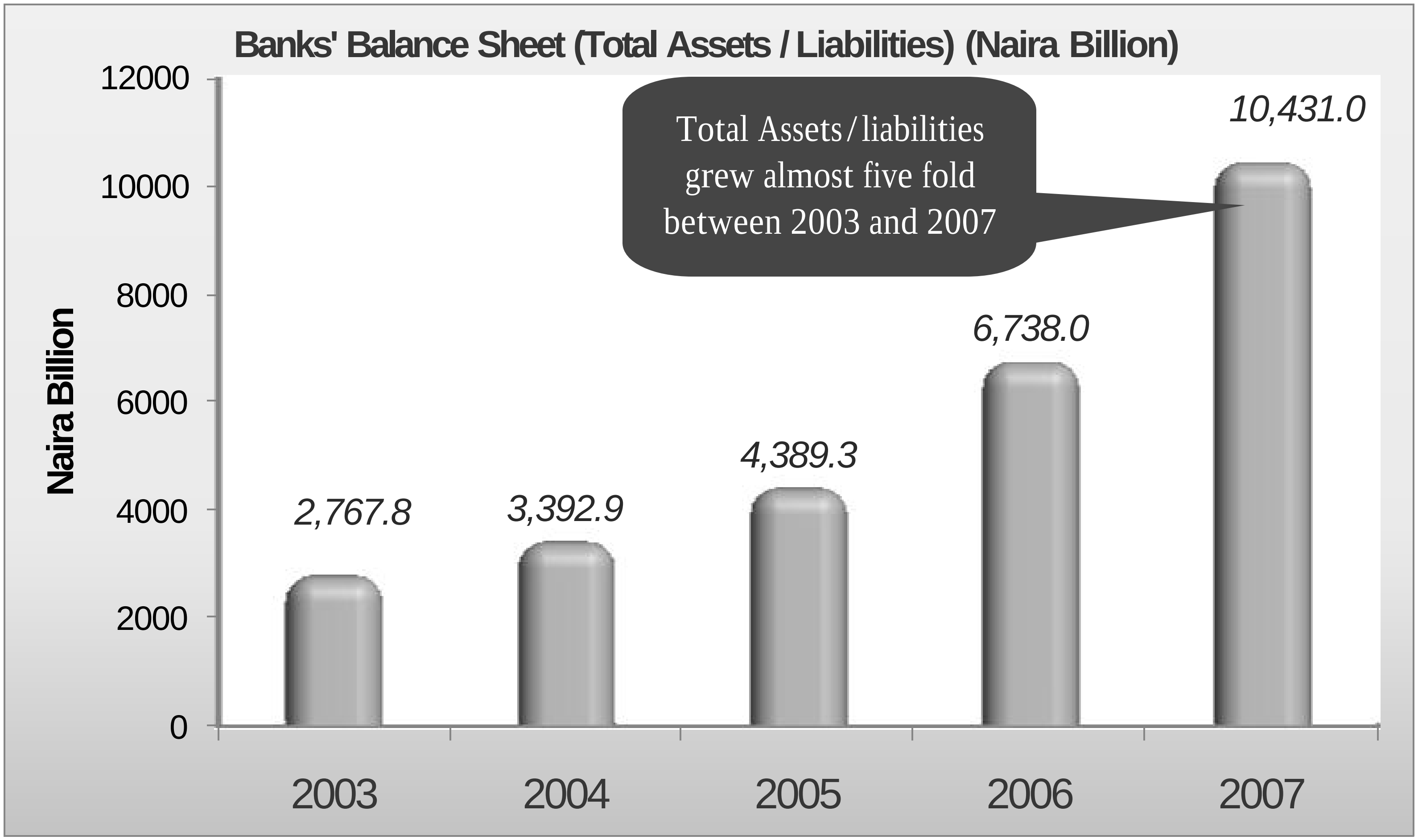

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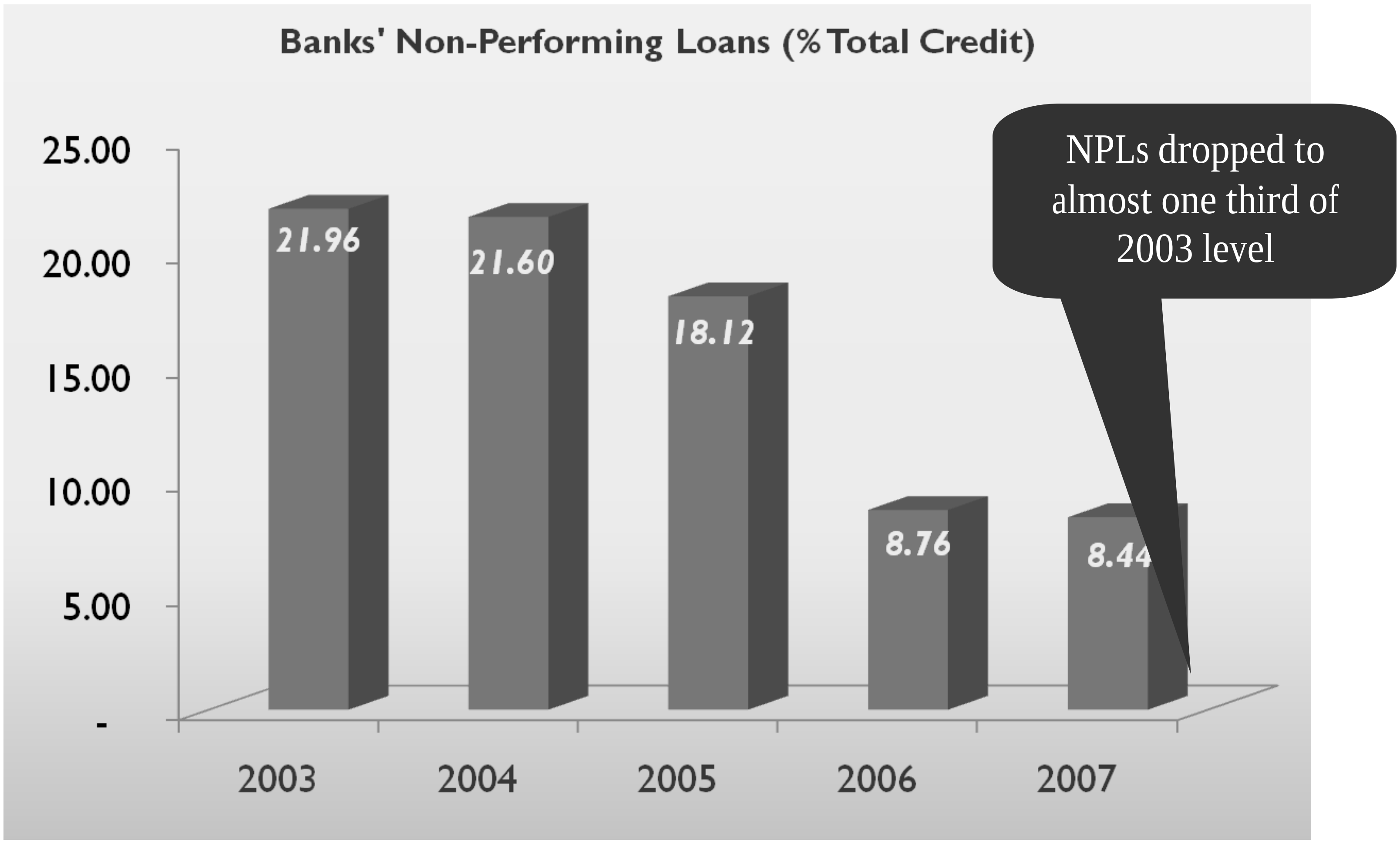

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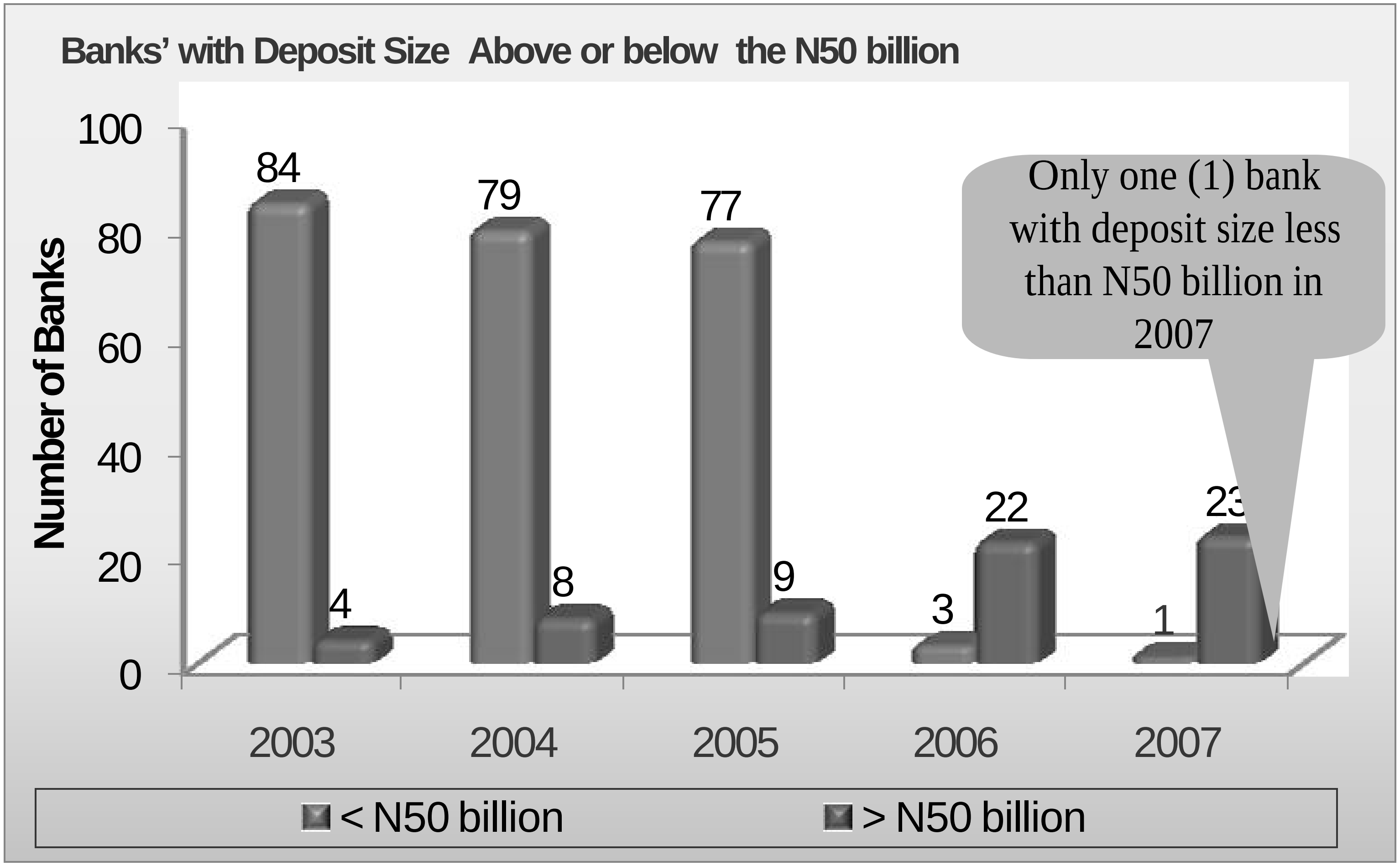

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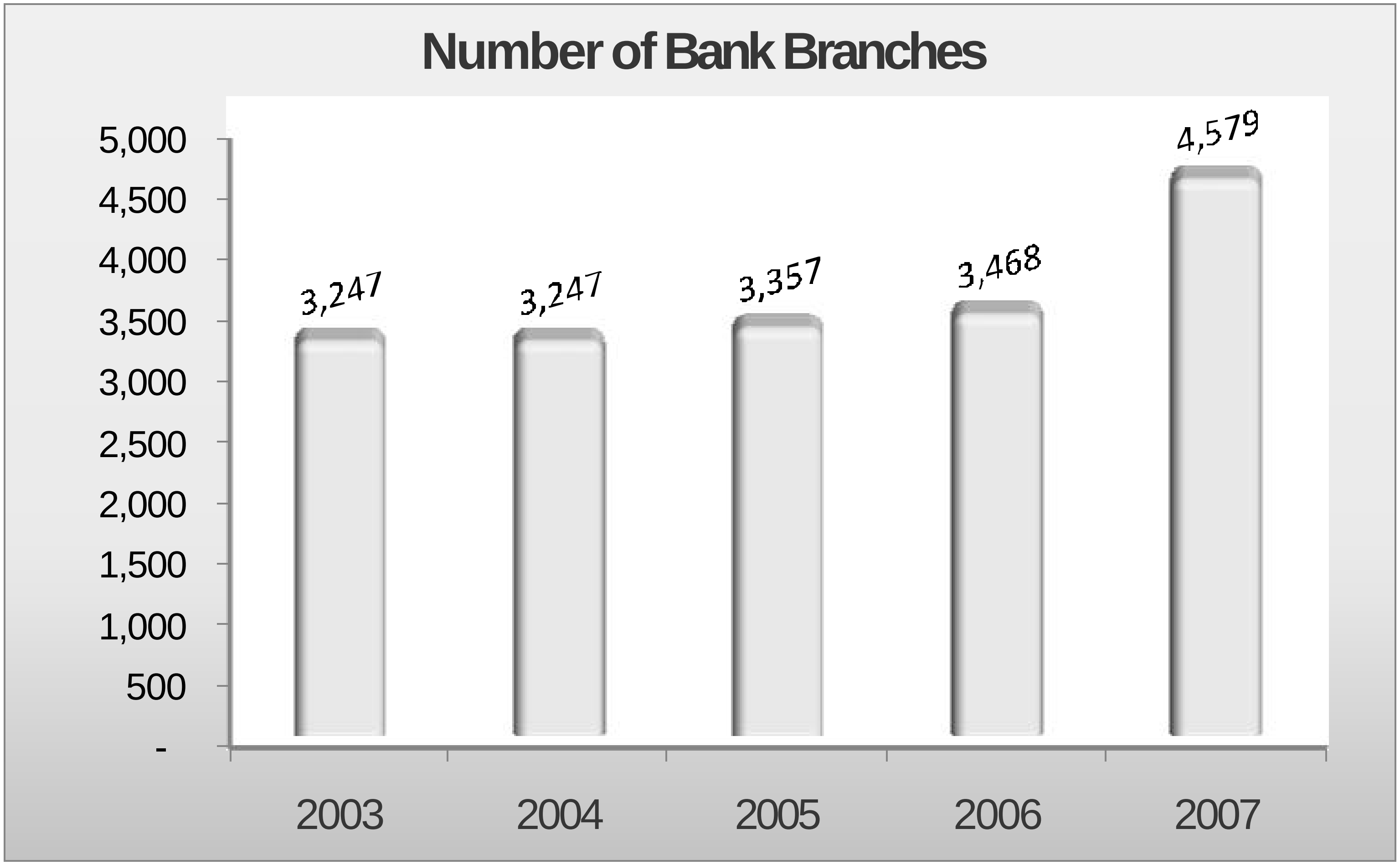

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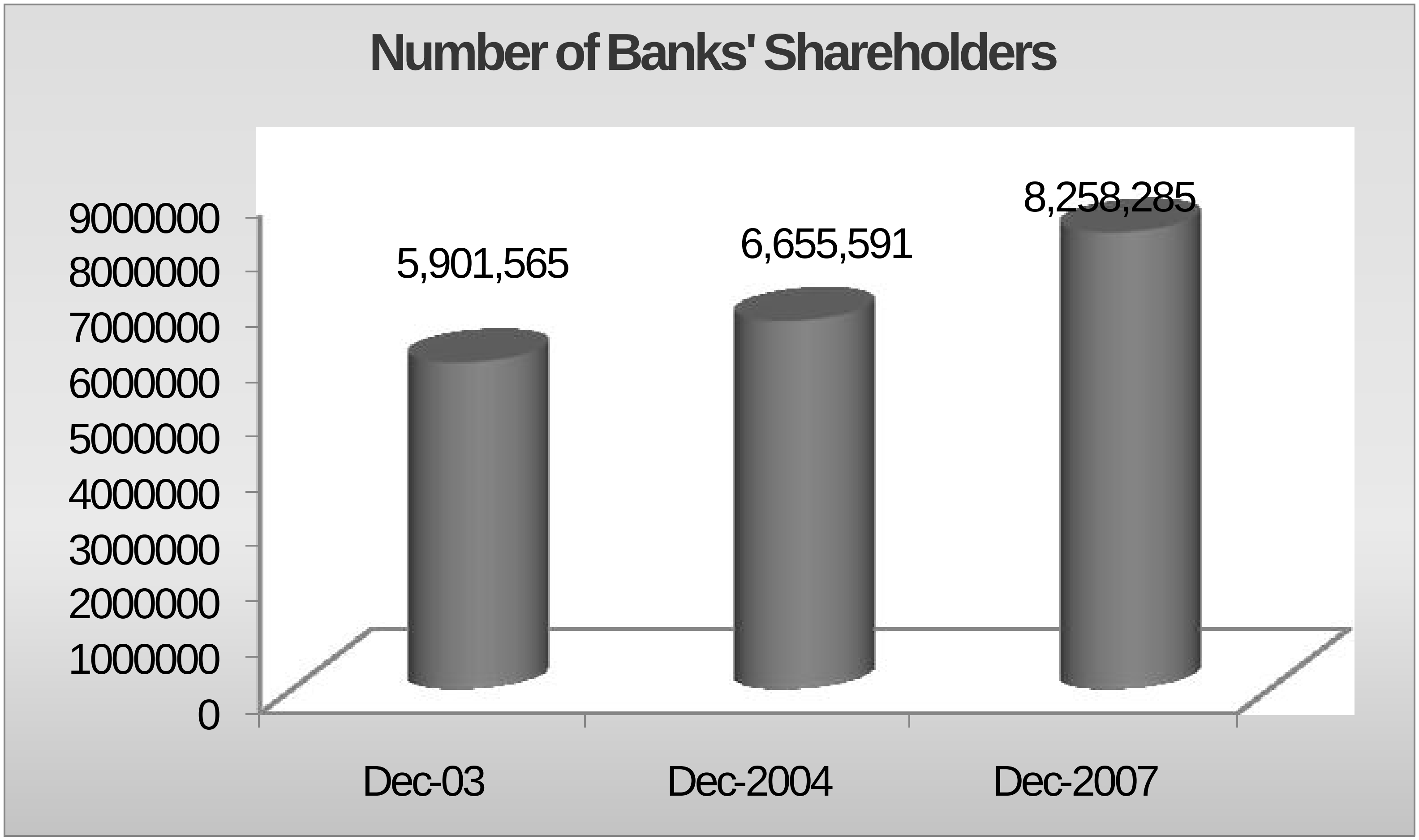

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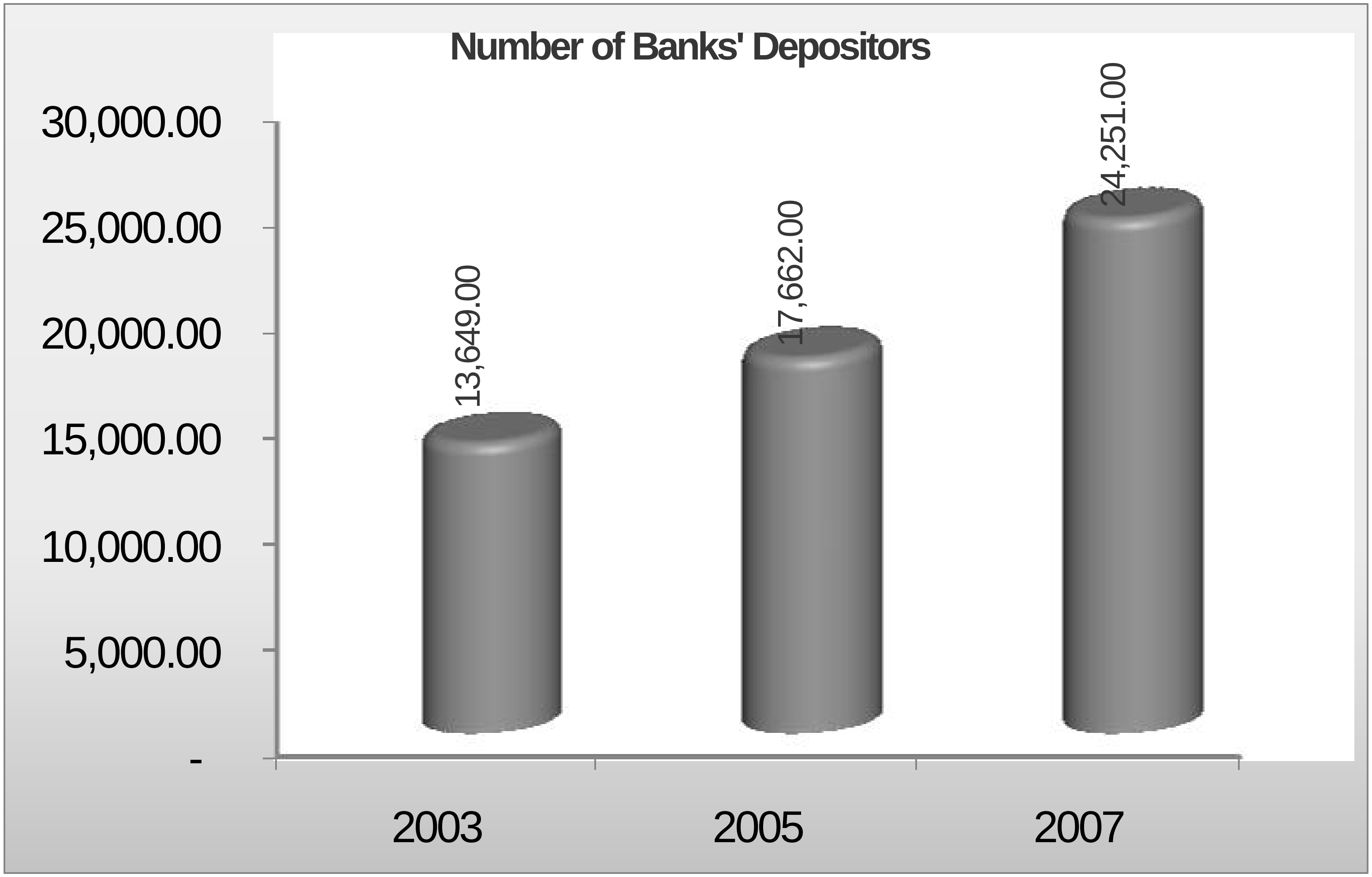

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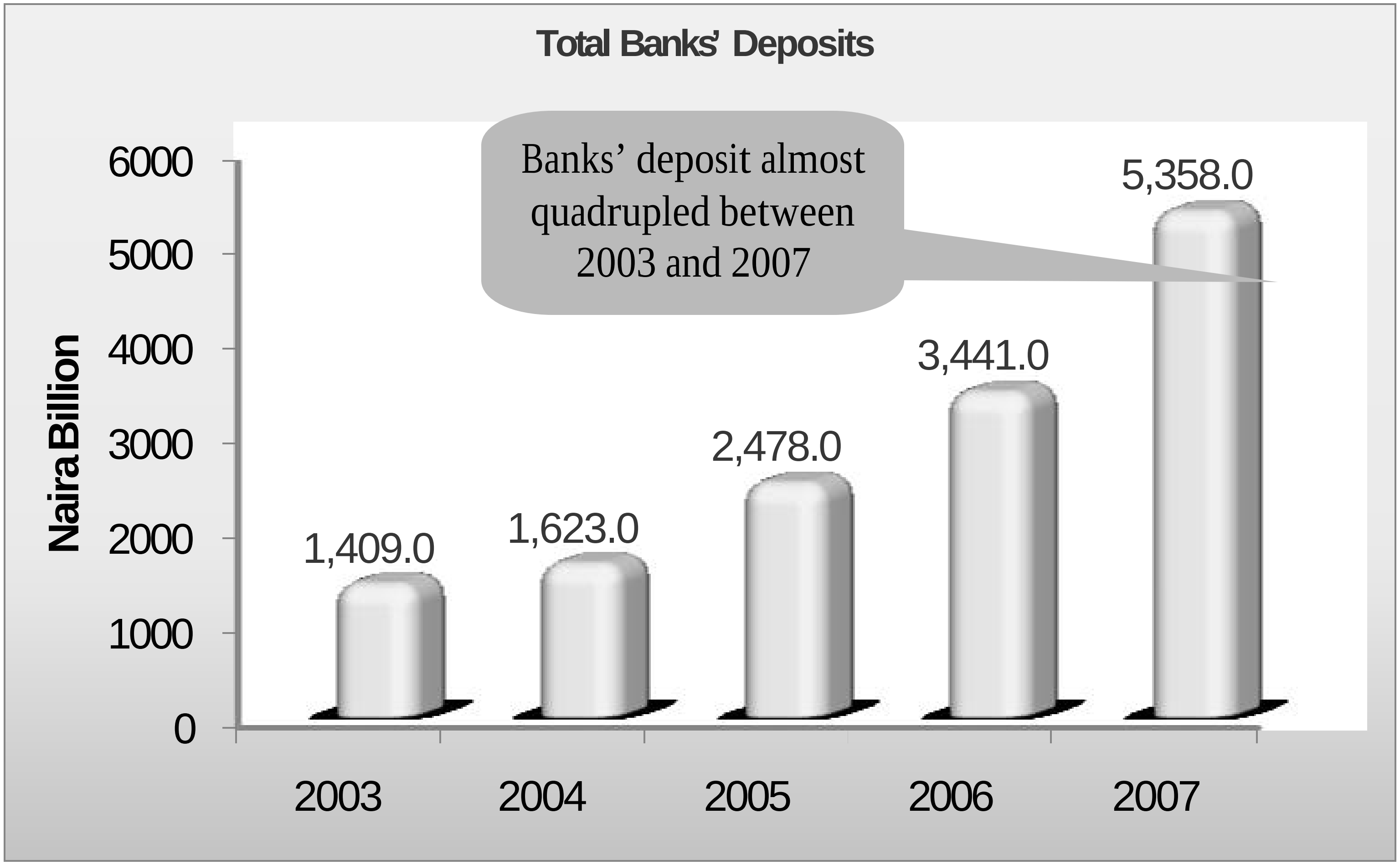

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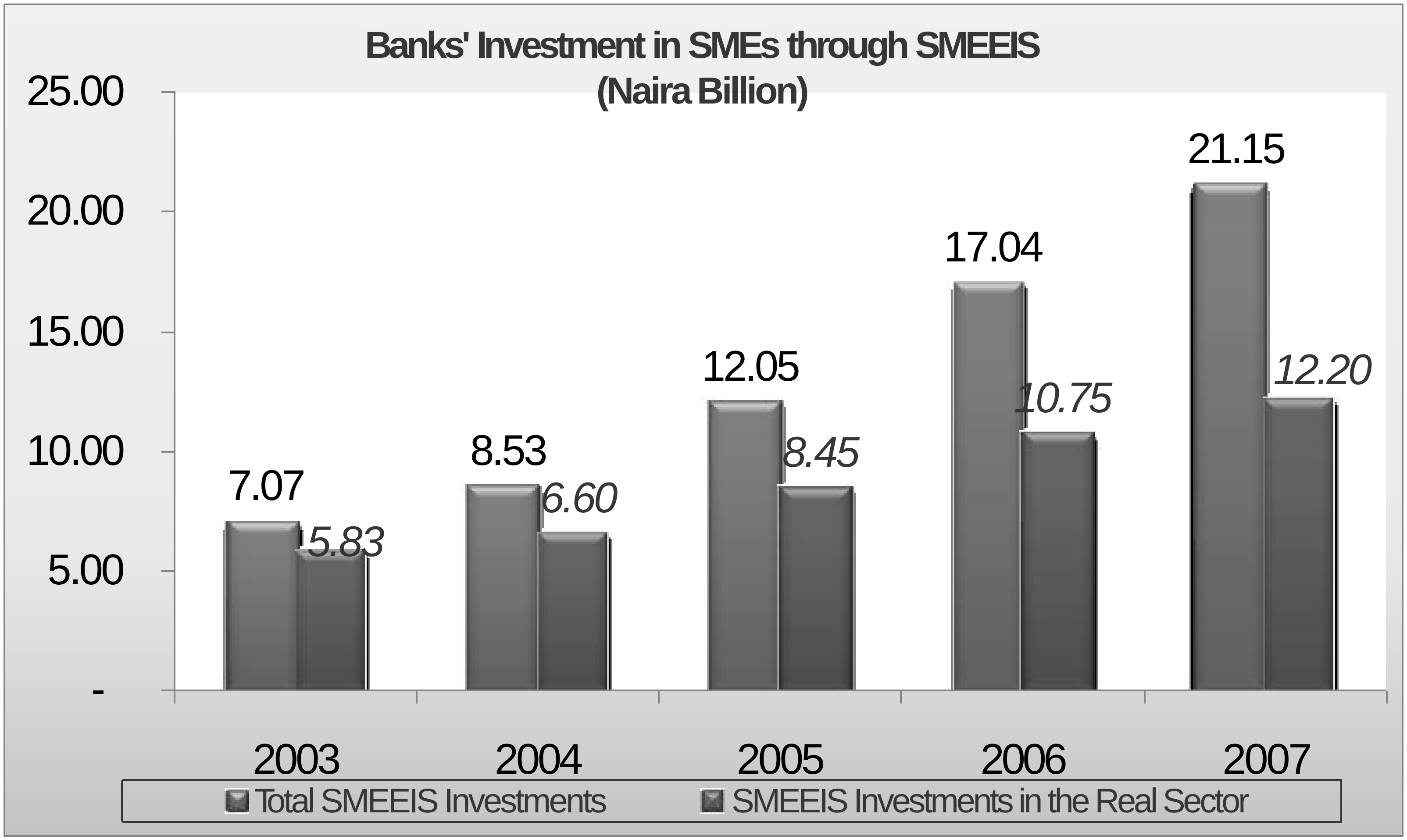

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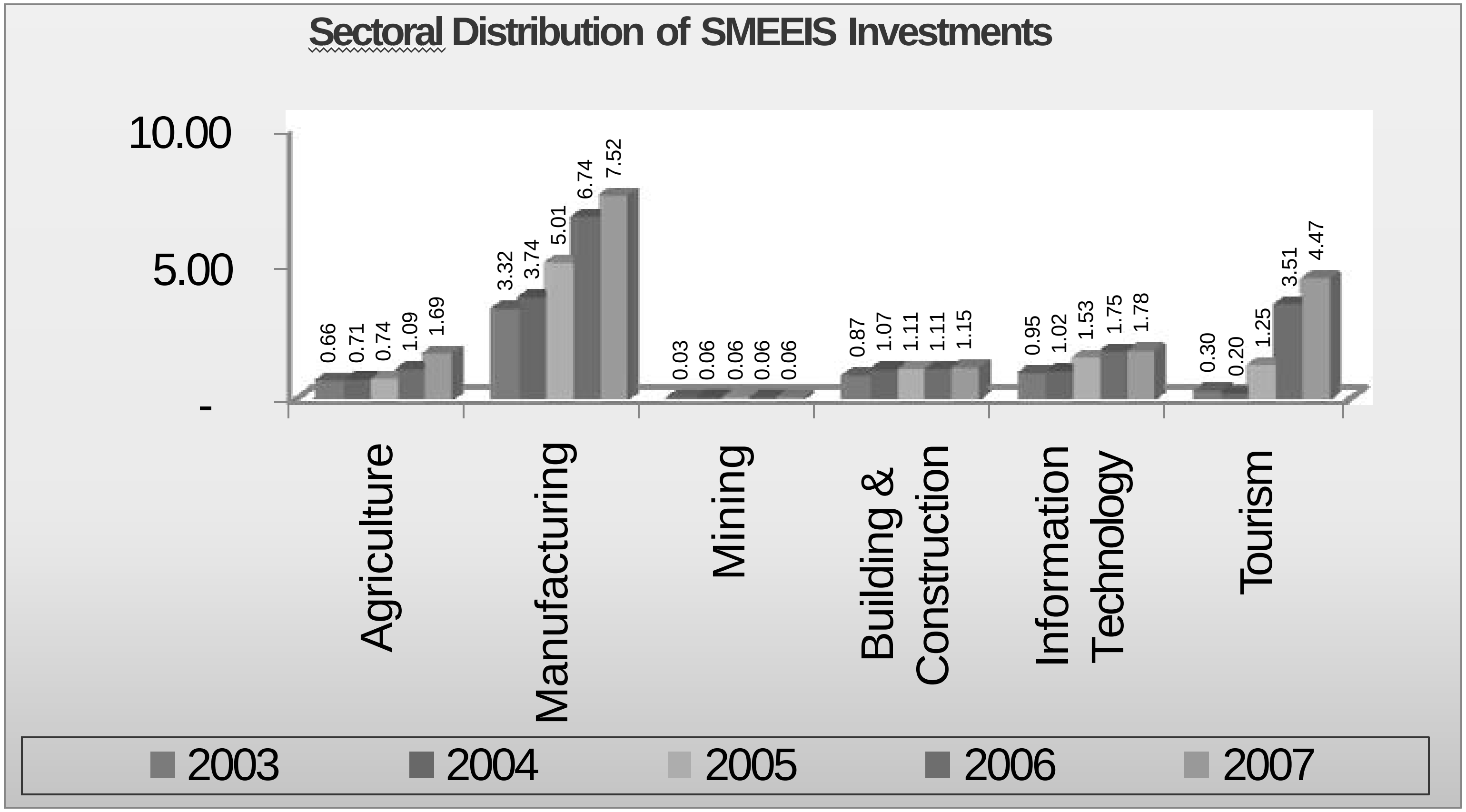

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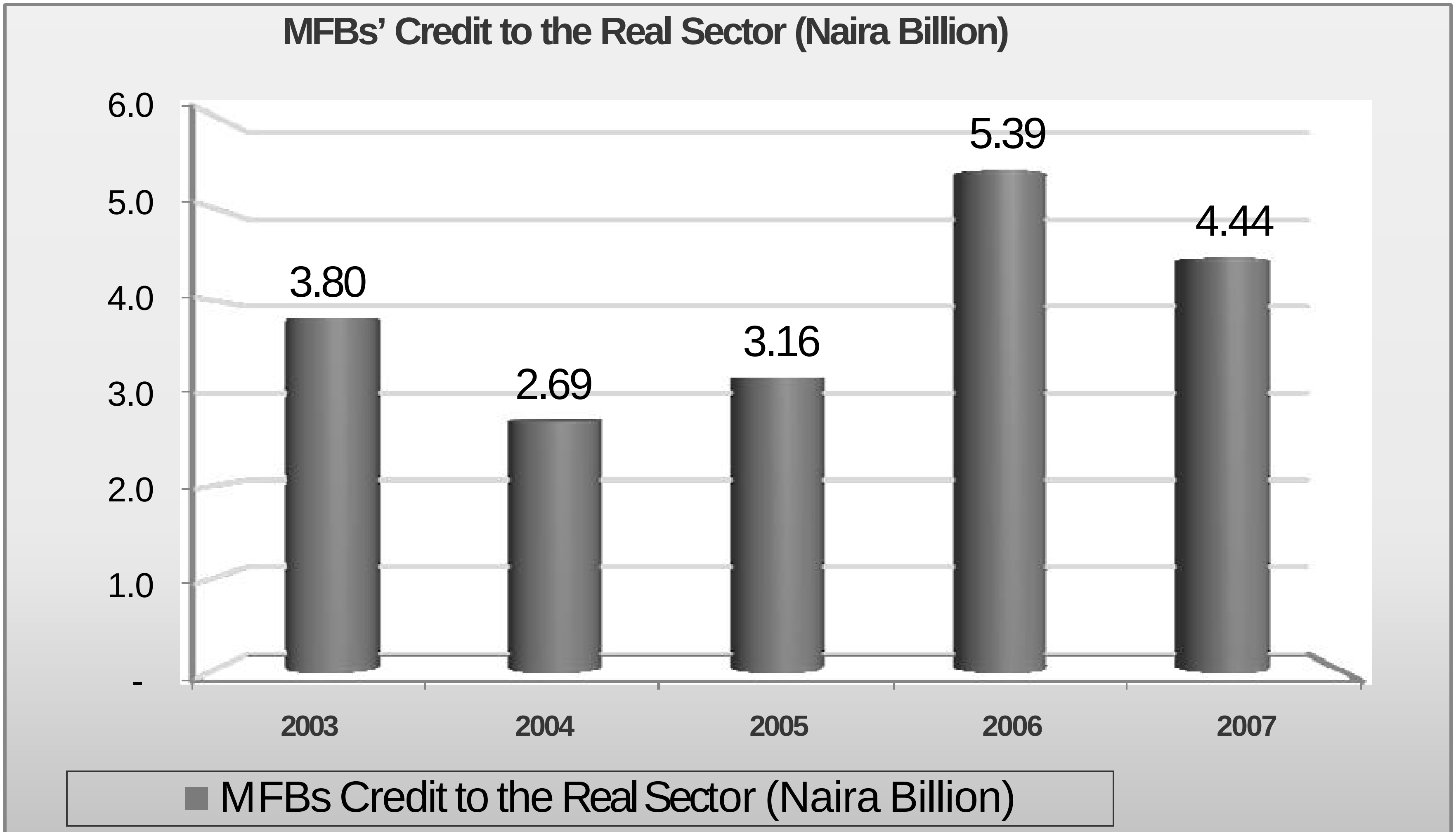

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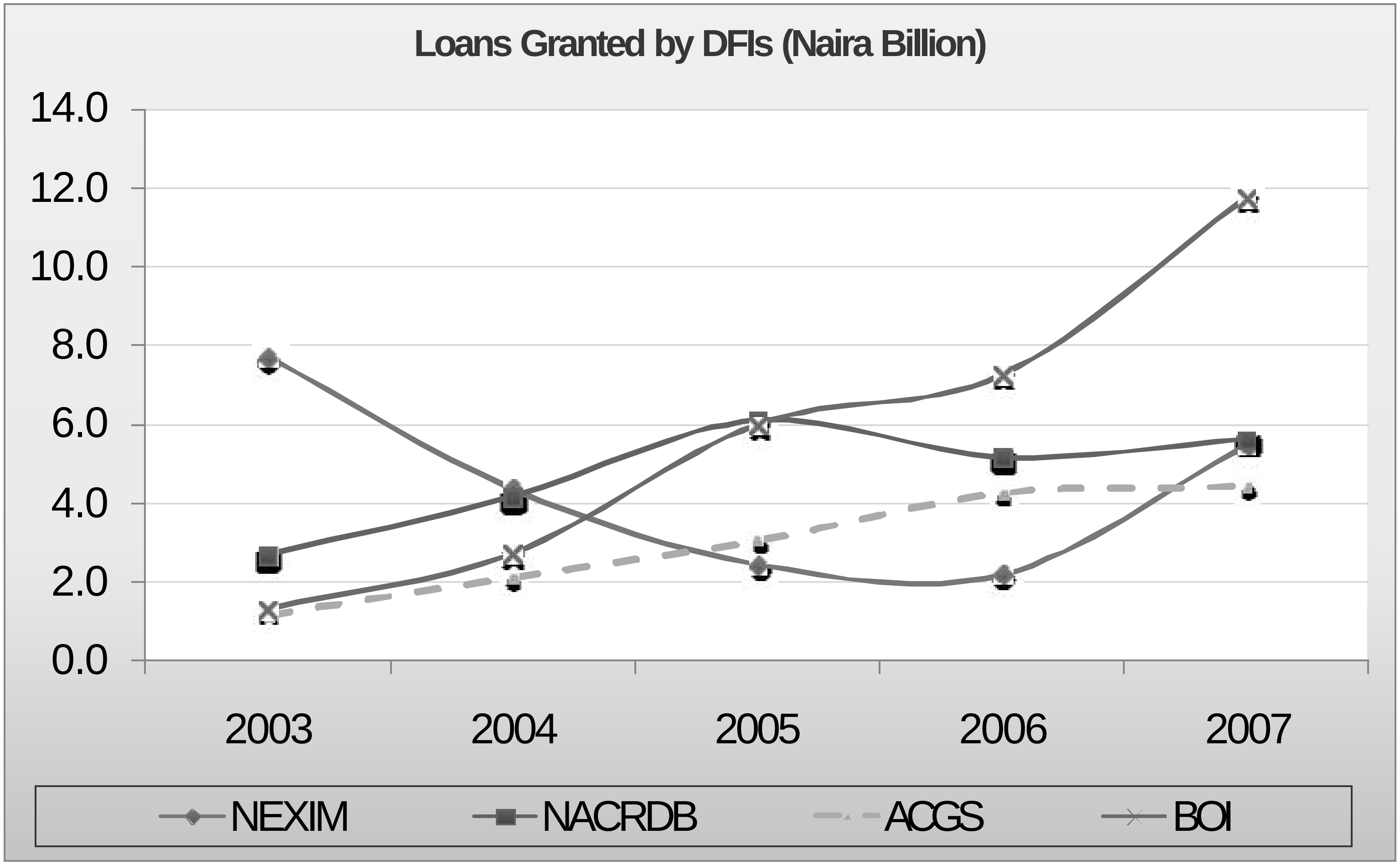
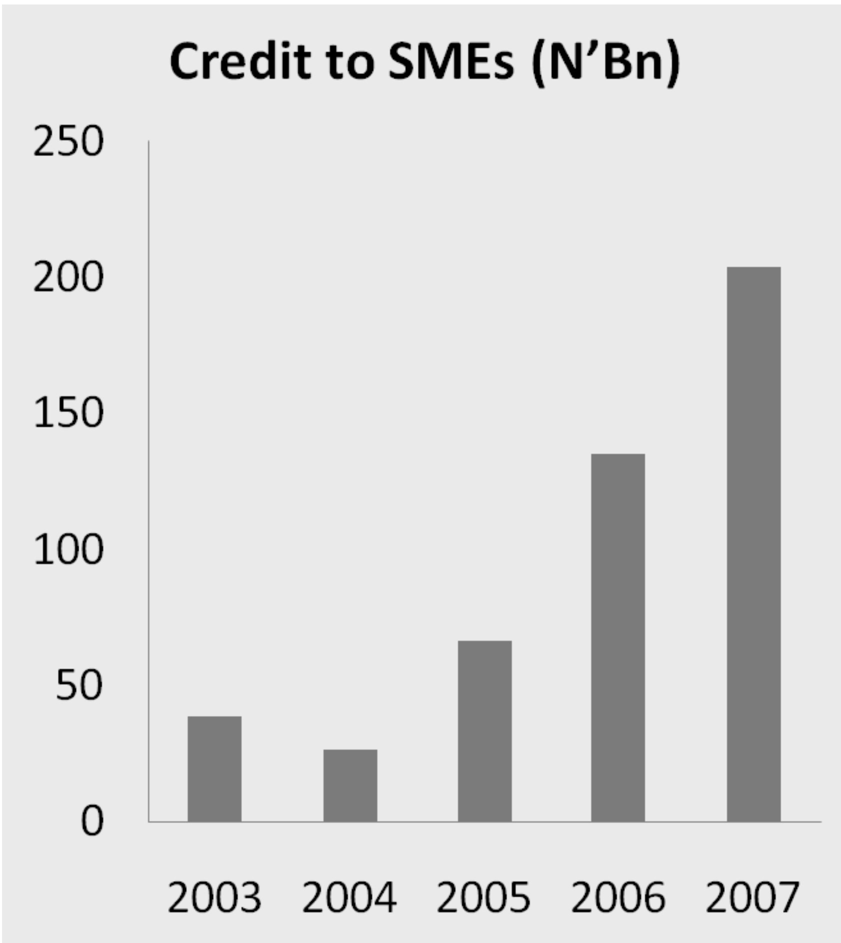
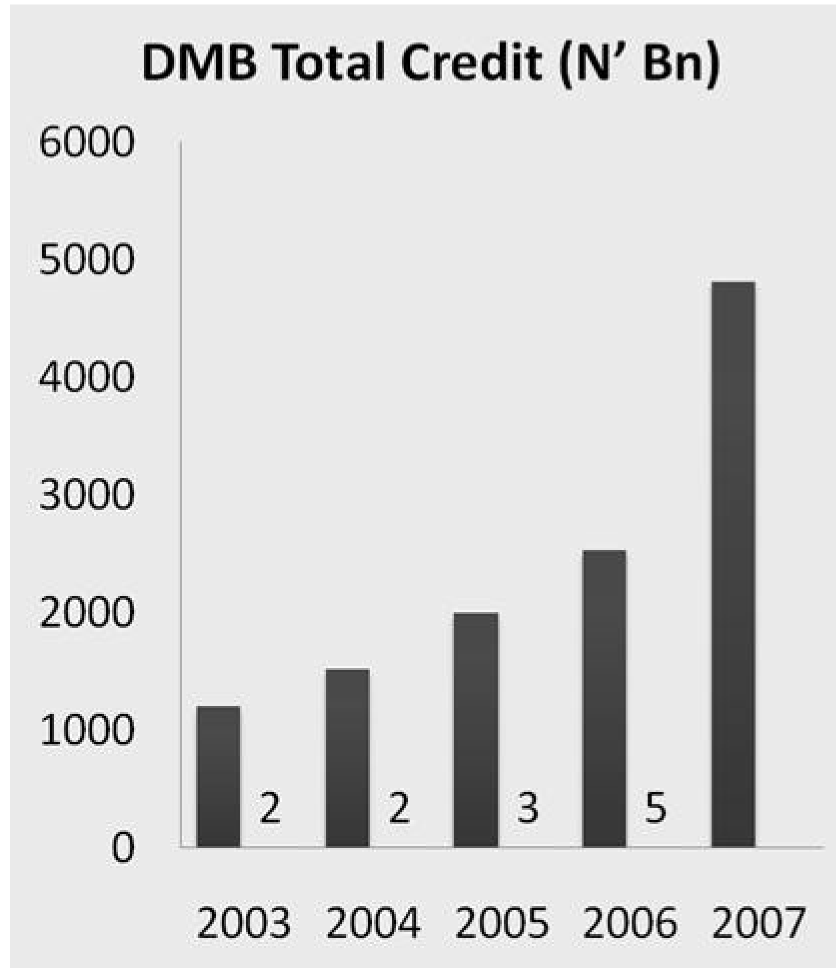


IV. Banks and the Nigerian Economy: *Recent Evidence*

DMBs' Credit to SMEs As Percent of Total Credit			
Year	Credit to SMEs (N'Bn)	DMB Total Credit (N'Bn)	Credit to SMEs as % of DMBs Total Credit (%)
2003	38.51	1,203.20	3.20
2004	26.31	1,519.24	1.73
2005	66.28	1,991.15	3.33
2006	134.68	2,524.30	5.34
2007	203.58	4,813.49	4.23

IV. Credit to SMEs And Total Credit





V: PAST ATTEMPTS AT FINANCE FOR THE POOR….. *SMEEIS*

- Small & Medium Enterprises Equity Investment Scheme (SMEEIS) was a voluntary initiative in 1999 by the Bankers Committee through CBN's moral suasion, to assist in providing finance to the small enterprises
- About N40 billion was raised but as at end 2007, only 60% had been utilised in 523 projects nationwide.
- The location of projects was skewed in favour of urban area (Lagos/Ogun and Cross River [Tinapa] got 70% of projects.
- 12 states had no SMEEIS projects at all
- Even with full deployment, SMEEIS impact is projected at 0.018% of the nation's GDP
- More DMB loans to SME is more than 400% of SMEEIS

V. PAST ATTEMPTS AT FINANCE FOR THE POOR

- ***Rural Banking Scheme:***
  - In the 1980s, banks were mandated to set up branches in the rural areas
  - Objective was to improve access to financial services and to bank the unbanked
  - However it was not market driven and the branches were largely unprofitable
  - The scheme has since been suspended

V. PAST ATTEMPTS AT FINANCE FOR THE POOR

- People’s Bank (Government’s social lending)
- Family Economic Advancement Programme (FEAP)
- Nigerian Agricultural Credit Guarantee Scheme
- NERFUND
- Various poverty alleviation programmes with credit and financial services components

PAST ATTEMPTS: WHY THEY FAILED

Challenges To Providing Finance to the Poor

- ***Supply Side:***
  - Identifying profitable pool of market niches to service in relation to other viable options
  - Managerial capacity to meet the huge small accounts
  - Documentation requirements
  - Availability of financial institutions: most rural areas not served

  Demand Side:
  - Lack of effective national identification system
  - Poor quality collateral
  - Property titles and land/property as dead capital
  - Low savings capacity - sometimes improper savings assets in kind like cattle, crops, land, etc
  - Educational status/skill requirements to manage business
  - Cultural constraints against borrowing, interest payment, etc
  - Psychology – fear of the unknown, past unpleasant experiences

VI.WHERE DO WE GO FROM HERE?...

Microfinance Banks and Micro Credit Fund as a Response

- In place of community banks, the CBN has set up a framework for establishing microfinance banks
- December 31st 2007 was deadline for all community banks to transform into microfinance banks
- About 716 already licensed nationwide

ROAD AHEAD... *Microfinance Banks*

- Rationale for Microfinance banks- The erstwhile community banks were bedevilled with various challenges including:
  - Weak institutional capacity (poor management, weak internal controls, lack of deposit insurance scheme, poor corporate governance regime)
  - Weak capital base (first N250k, then N500k and N5m)
  - Restrictive regulatory/supervisory requirements
  - Relatively poor regulatory oversight
  - Restrictive ownership
  - Absence of clear business model
  - No insurance scheme for deposits

ROAD AHEAD... *Microfinance Banks*

- Improvements under the new microfinance banking regime:
  - Higher capital base (minimum of N20 million)
  - Scope for branch expansion provided they have free funds
  - Clearly defined business model
  - Capacity building programmes
  - More liberal ownership requirements
  - More stringent corporate governance regimes
  - Insurance for deposits

ROAD AHEAD.... *N50 Billion Micro Credit Fund*

- On February 12, 2008, President Musa Yar'Adua launched the N50 billion micro credit scheme– expected to grow to more than N100 billion per annum in a few years time
- It is a Bankers' Committee initiative to pool funds for lending to the micro sector
- Banks will transfer the outstanding SMEEIS to the fund (about N20 billion)
- States are to dedicate at least 1% of their annual budget as matching fund for micro credit
- Borrowing by States from the Banks will be at single digit rates (currently set at 8%)

THE ROAD AHEAD.... *DFIs*

- Development Financial Institutions are being strengthened to help improve access
  - Various government DFIs have been pooled under Bank of Industry to provide developmental (non-commercial) loans
  - Nigeria Agricultural Cooperative And Rural Development Bank Limited (NACRDB)
  - Nigeria Export Import Bank (NEXIM)
  - Agricultural Credit Guarantee Scheme (ACGS)

ROAD AHEAD…

- Entrepreneurship Development Centres (EDCs)
  - CBN's effort to supplement the efforts of SMEDAN and others in skill acquisition and business management
  - Provides centres to teach skills on running businesses--- one per geopolitical zone
  - The EDCs will be supported for a while and ultimately passed to the private sector
  - EDUCATION, EDUCATION: TECHNICAL AND BUSINESS EDUCATION AS COMPULSORY (treated as General Studies)
  - Population control measures--- through public education
  - National identity system:
  - Land reforms
  - Fix the infrastructure– power, transportation, security, etc
  - Fix the commercial court system

VII: CONCLUSION

- Only an INCLUSIVE national development will be SUSTAINABLE
- FINANCE CAN greatly assist in the war against poverty
- BUT FINANCE ALONE is NOT ENOUGH
- OTHER COMPLEMENTARY REFORMS NEEDED
- ALL NIGERIANS MUST WORK TO MAKE THIS HAPPEN

Thank You
For Your Attention