Financial System Strategy 2020

FSS 2020 International Conference

Credit Market

Presentation Outline

- Industry/Sector Overview
- Current Position Assessment
  - Industry Structure (Players, Regulators, Products etc)
  - Industry Trends
- Industry Issues, Gaps & Key Success Factors
- Industry Vision and Mission
- Proposed Industry Model
- Strategic Objectives & Initiatives
- Implementation Plan & Timelines

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Sector Overview

Industry/Sector Overview

- The Nigerian credit market can be broadly categorized into the *formal* and *informal sectors*, based on how structured the lending process is.
- The better-organized and formal sector of the credit market is driven largely by the *deposit money banks* (DMBs), which set the tone for much of what is reported in this presentation.
- The DMBs dominated the market, representing between *85%* to *90%* (by loan value) of the credit data captured in this survey.
- Most of the credit granted by deposit money banks was of *short-term nature* (On Call), which accounted for about *46.2%* of the aggregate credit.

Industry/Sector Overview (contd.)

- Short-term loans plus credit of a 6-month maturity represented *63.05%* of the aggregate.
- This reflected the maturity structure of deposit liabilities, wherein demand deposits accounted for *44.46%* of the total.
- This constraint on long-term lending was further worsened by the near total absence of alternative *long-term funds*, especially that most pensions were not funded and insurance funds were limited.

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Industry/Sector Overview (contd.)

- One of the major challenges of this study is the *paucity of data* for the entire market.
- Much of the data available was on the deposit money banks (DMBs), finance companies, micro finance banks (formerly community banks) and discount houses.
  - These represent about 85% to 90% of the Nigerian credit market, putting the estimated size of the market at about *N3.0 trillion* (or *US$20.6 billion*) in 2005.
- There has been a shift of dominance in the credit market in Nigeria from the *Federal Government* to the private sector.
  - This reflects the government's commitment to fiscally prudence since 2003, complemented by better-focused monetary policy.

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Industry/Sector Overview (contd.)

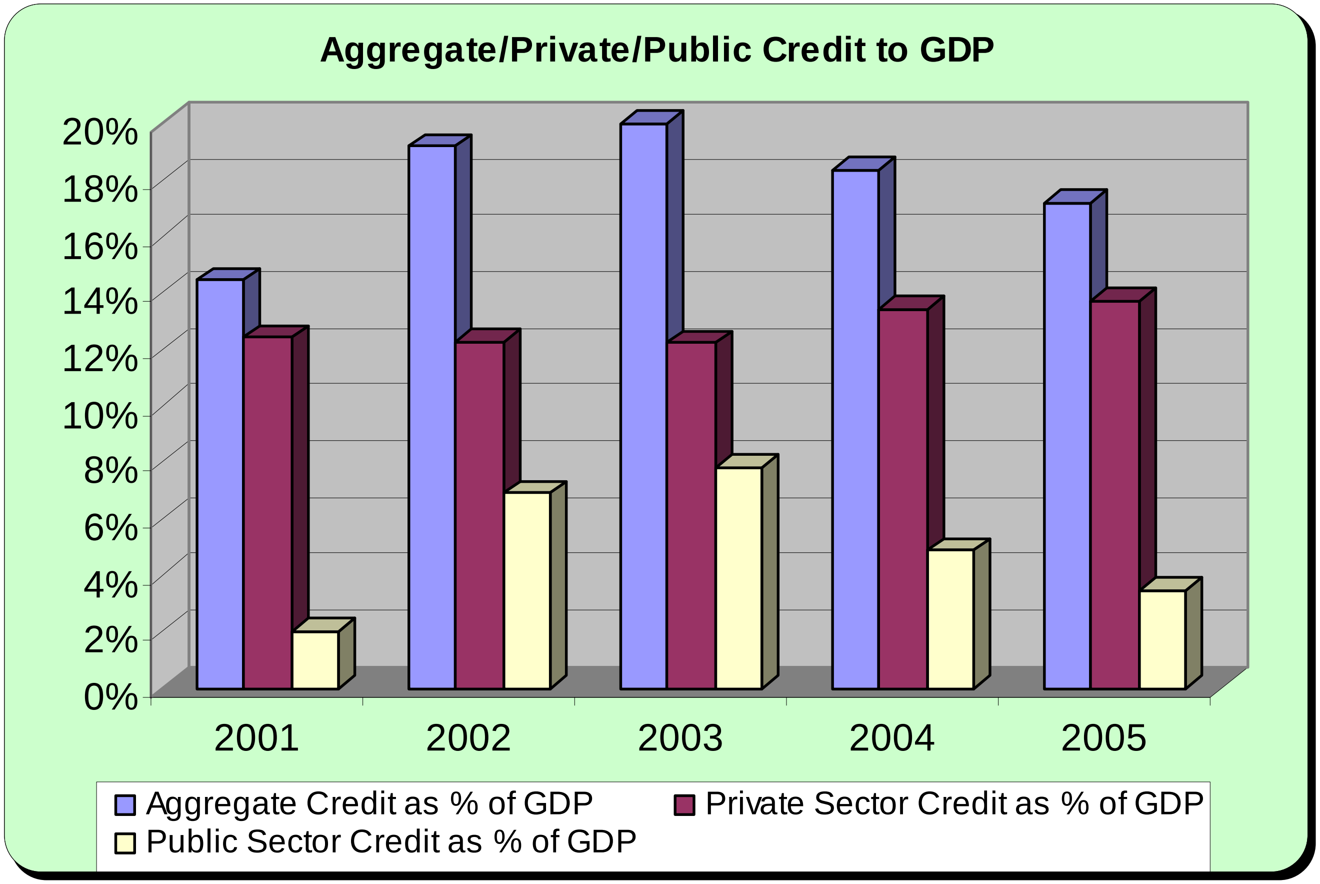
- Pre-consolidation, the three biggest banks in Nigeria dominated the credit market, accounting for about 62% of aggregate credit – just a little lower than the same proportion they had in total deposit liabilities.
  - This was due to a combination of factors, including their age, relative size and cost of funds – they were the cheapest lenders.
- The market was thus oligopolistic in nature.

Industry/Sector Overview (contd.)

- An important metric in measuring the relative size of the credit market is the ratio of aggregate credit to the Gross Domestic Product (GDP), along side the ratio of credit of the private sector to GDP.
- Chart 1 below shows that GDP maintained an average growth rate of 6.35% during 2001 to 2005, when compared to the aggregate domestic credit and the credit received by the private sector.

Industry/Sector Overview (contd.)

- **CHART 1**



Source: Central Bank of Nigeria Annual Reports

Industry/Sector Overview (contd.)

- GDP also grew faster than aggregate credit in the five-year period considered, while credit to the private sector grew at a faster pace than the aggregate.
- This is an important issue in the credit strategy being proposed in this document.

MAJOR LENDERS IN THE NIGERIAN CREDIT MARKET

INSTITUTION	2001	2002	2003	2004	2005
DEPOSIT MONEY BANKS	1,033,636.20	1,302,219.10	1,591,218.70	2,077,779.30	2,588,916.70
FINANCE COMPANIES	6,915.60	4,101.50	14,789.20	11,009.00	16,251.30
MICRO FINANCE BANKS	1,314.00	4,310.90	9,954.80	11,353.80	28,504.80
DISCOUNT HOUSES	1,450.00	-	1,020.80	1,949.10	625.60
LEASING COMPANIES	19,086.07	25,232.88	38,912.80	53,187.07	76,460.08
AGGREGATE (N’ml)	1,063,256.97	1,335,864.38	1,655,896.30	2,155,278.27	2,710,758.48
AGGREGATE (US$)	8,075.78	10,146.32	12,577.06	16,370.03	20,589.08

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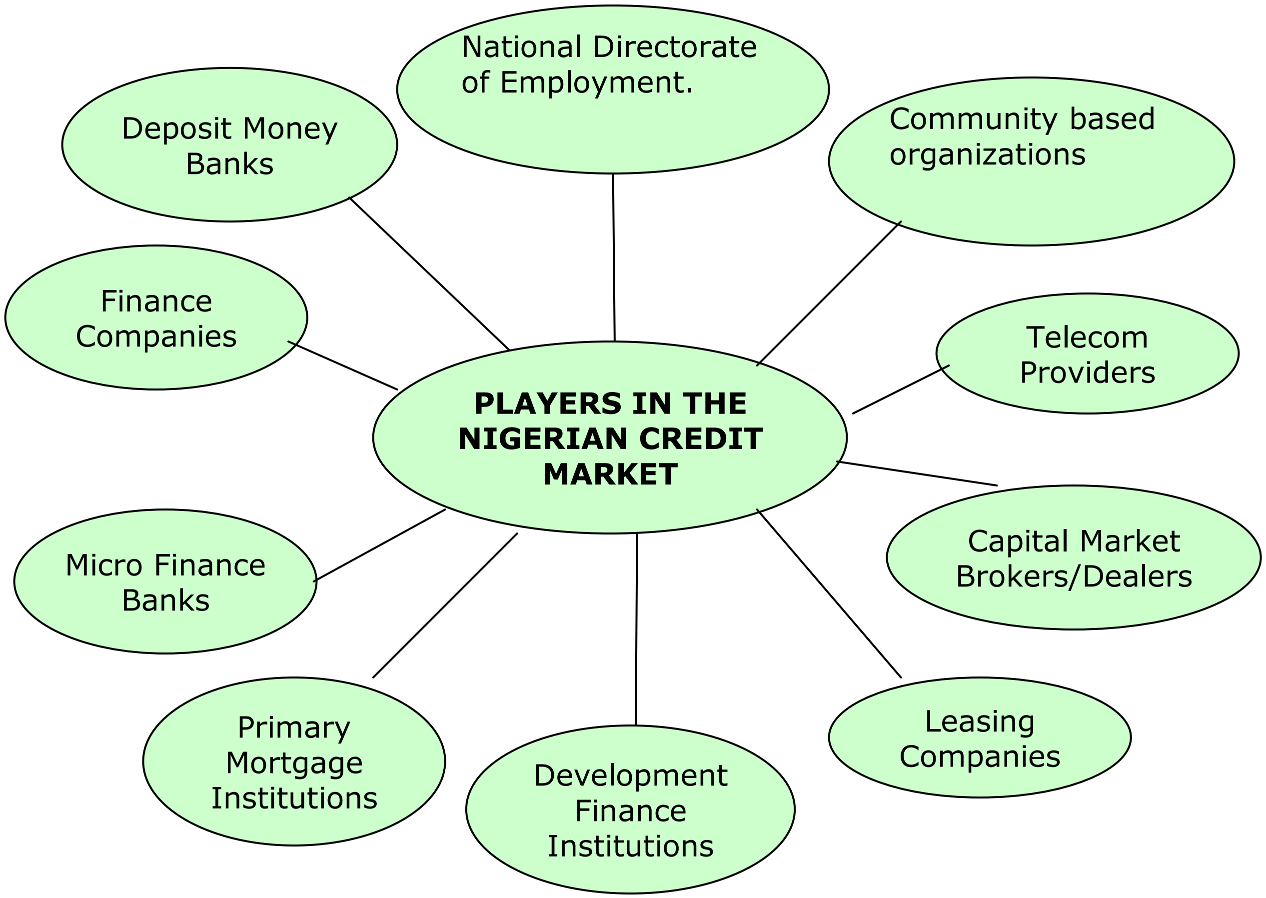
Industry/Sector Structure: Players

- **The players in the credit market are depicted below:**



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NIGERIA:
Current Position Assessment

Industry/Sector Structure: Regulators

- The Nigerian credit market is regulated primarily by the Central Bank of Nigeria (CBN), which is the apex regulatory authority in the banking system and thus has responsibility for the DMBs. There are of course, credit lenders that are outside the regulation or supervision of the CBN.

Industry/Sector Structure: Regulators (contd.)

- These include the Primary Mortgage Institutions, which are responsible to the Federal Mortgage Bank and the leasing companies that operate within the self-regulatory organ of the Equipment Leasing Association of Nigeria (ELAN).
- For the purposes of this study, the CBN is regarded as the credit market regulator, as most of the credit (85% to 90%) was granted by the DMBs. In addition to the CBN, other regulatory authorities and the institutions they regulate are shown in the table below:

Industry/Sector Structure: Regulators (contd.)

Institution **Regulator**

	CBN	FMBN	ELAN	SEC/NSE	NCC	None
Deposit Money Banks	x					
Finance Companies	X					
Micro Finance Banks	X					
Discount Houses	X					
Primary Mortgage Institutions	x					
Development Finance Institutions	X	X				
Leasing Companies						
Capital Market Dealers			X			
Telecom Providers				X		
Community Based Organizations					X	
						X

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Industry/Sector Structure: Products

- Overdrafts
- Short Term Loans (0-12 months)
- Medium Term Loans (2 -5 years)
- Long term loans (5 years and above)
- Advances
- Consumer Loans
- Commercial Bills
- Real Estate & Mortgage Loans
- Agricultural Loans

Industry/Sector Trends

- The beginning of 2006, saw some DMBs accessing credit from the international capital markets for on-lending to their customers.
- Some DMBs also formed partnerships with development agencies to facilitate availability and accessibility of credit to the small and medium-scale enterprises, which have been identified as critical to the growth of the Nigerian economy but have difficulty accessing affordable credit.
- The Nigerian credit market is relatively underdeveloped, considering the estimated size of the market against the size of the credit markets in other benchmarked countries and the variety of products.

Industry/Sector Trends (contd.)

- The major challenges of the market are:
  - Difficulty in accessing credit, especially by the disadvantaged Micro Small and Medium Scale Enterprises (MSMEs) and the active poor;
  - High cost of credit, which historically had gone as high as 72% p.a. in the deposit money banks in the early 1990s and currently ranges between 19% and 25% p.a.
  - Inconvenience that requires direct physical meetings by lenders and borrowers.
- Besides these core issues, there are also the challenges of short term lending and crowding out effect of public sector borrowing. This strategic plan when successfully implemented will address these issues, resulting in a migration of many credit market participants from the informal to the formal sector of the market and trigger faster growth of the economy.

Industry Issues

- Inadequate credit infrastructure
- Ineffective legal framework for lending and loan recovery
- Poor credit culture
- Lack of long term funds
- Credit skill gaps
- Large Informal Sector
- Fiscal and macroeconomic instability

- **Controllable Factors**

1. **The basic credit information on borrowers is not available to lenders. A credit bureau comprising required information on individuals needs to be developed in order to achieve our credit vision. This database will provide lenders with the necessary information required on prospective borrowers.**

2. **Investment in building and maintaining a robust ICT platform for credit needs to be done. This will introduce innovative ways of lending credit by leveraging on various delivery channels (e.g. post office, supermarkets etc). Lenders can commit significant resources to building and maintenance of the ICT platform required.**

Industry Gaps (contd.)

- **Controllable Factors (contd.):**

3. The cost of credit is not internationally competitive. Individual credit lenders can embark on the aggressive mobilization of relatively cheap funds to lower funding cost, and also pursue effective cost management strategies.

4. This credit growth vision will also derail if the requisite credit skills are not developed. Individual credit lenders can embark on deliberate skills development and enhancement for its staff, especially preparing them for international competition.

Industry Gaps (contd.)

Uncontrollable Factors

1. **Absence of a strong legal framework: The legal framework and collection strategy are inefficient, thus encouraging deliberate or inadvertent default by borrowers. Credit lenders can initiate actions through recommendations to responsible governments and their agencies. The key issues here are the enforcement and protection of rights, and the vexatious land tenure system.**
2. **Sustainable macro-economic environment, which largely results from the interplay of the fiscal policy/operations vis-à-vis monetary policy and its implementation. This has major influence on the cost of credit, as a sustainable macro economic environment will result in favourable interest rates thereby boosting the demand for credit.**

Industry Gaps (contd.)

Uncontrollable Factors (contd.):

3. **Macro-level credit information collation and management in the form of a national credit registry. Privately promoted credit bureaus might not serve this purpose well, unless they are networked voluntarily or so mandated.**
4. **The same argument holds for personal identification system, which becomes more effective at the national level than at individual credit grantor, group of lenders or regional level.**
5. **Reorientation towards credit has to be implemented, borrowers have to be informed and taught on the importance of repayment.**
6. **Social and physical infrastructures are deficient. This contributes to the high cost of doing business and impacts the cost of credit. It also constitutes physical impediment in accessing credit.**

Key Success Factors

- Robust credit infrastructure
  - Personal identification system, Credit bureau, Credit rating and National credit registry
- Supportive legal framework
- Contemporary credit skills
- Conducive macroeconomic environment

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Sector Vision and Mission

"By 2020, our credit to GDP ratio will be among the top three of emerging markets, and 70% of the Nigerian population."

"To make Credit Accessible, Convenient and Affordable"

Vivid Description of Vision

By the year 2020, the…

Information communication technology (ICT) will facilitate access to the credit market irrespective of where the prospective borrower lives or operates from. The products will be user friendly and the charges internationally competitive, at single digit lending rates and other moderate charges. The credit market will play a key role in the growth of other sectors of the economy through financial support for economic activities, and drive the entire financial services system. It will motivate job creation and expand consumer expenditure.

Proposed Industry Model

Based on the review of the credit markets in Nigeria and selected countries, the Brazilian market was adopted as a benchmark model due to its socio economic similarities with Nigeria. Similarities such as: Large population, Resource potentials, huge investments in ICT which Nigeria is just starting, Brazil embarking on economic reforms in 1994 and attainment of single digit inflation. These altogether informed the following strategy recommendations that are aimed at making credit in Nigeria:

- ❑ Accessible
- ❑ Convenient
- ❑ Affordable

Strategic Objectives & Initiatives

Strategic Objectives

- Accessible
- Convenient
- Affordable

Strategic Initiatives

Legal Framework

- Review/update of the Legal Framework for Bank Lending
- CBN Act
- BOFIA
  - Enabling law for Consumer Credit focusing on developing the consumer market
  - Enabling law for the National Bureau of Credit Statistics
  - Create Commercial Divisions of High Courts
  - Equip the Commercial Courts with innovative and modern processing equipments

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Strategic Objectives & Initiatives (contd.)

BOFIA (contd.) :

  - Appoint judges and train them on laws of credit and basic principles of lending
  - Transfer all pending commercial lending cases from non commercial courts to commercial courts
  - Set up tracking mechanism for commercial cases

- Reform process for obtaining Governor's consent
- Provide legal framework for issuance and usage of credit cards.

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Strategic Objectives & Initiatives (contd.)

Strategic Initiatives (contd.) :

Infrastructure

- Establish a Personal identification system
- Provide tenored incentives for organizations to fast-track the establishment of credit bureaus
- Provide tenored incentives for organizations to fast-track the establishment of Credit Rating Agencies
- Set up a National Collateral Registry
- Set up a National Bureau of Credit Statistics
- Provide tenored incentives for banks, other financial institutions, retailers and other service providers to issue credit cards.
- Introduce awards for most active issuers and users of credit cards.
- Establish Call and Service Centres of financial institutions severally in urban centres.

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Strategic Objectives & Initiatives (contd.)

Strategic Initiatives (contd.):

Macroeconomic Stability

- Enact into law the Fiscal Responsibility Bill
- Stop CBN financing of fiscal deficit
- Maintain single digit inflation rate, targeting 5%

Credit Institute

- Set up an internationally recognized credit training and certification Institute
- Require certification from Chief Credit Officers of financial institutions, especially DMBs
- Publish internationally recognized and accepted Credit Journal

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Strategic Objectives & Initiatives (contd.)

Strategic Initiatives (contd.):

■Savings Mobilization & Credit

- Introduce awards for the following:
- 20% & above growth in deposit portfolio
- Loan-deposit ratio exceeding 60%
- Longest duration of deposit portfolio
- Lowest effective lending rate
- Most effective new liability product over a two-year band

■Consistency

- Review and update initiatives above as required, but not less than every three years up until year 2020.

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Implementation Plan

FSS 2020 Sector Objectives and Initiative	Responsibility	Deliverables
Legal Framework		
Review/update of the Legal Framework for Bank Lending CBN Act; BOFIA	CBN, NDIC, CIBN, DMBs, National Assembly	Updated Acts in 2008
Enabling law for Consumer Credit focusing on developing the consumer market	CBN, NDIC, CIBN, NAICOM, NACCREC, DMBs, National Assembly	Act in 2008
Enabling law for the National Bureau of Credit Statistics	CBN, NDIC, NAICOM, NACCREC, DMBs, National Assembly	Act in 2008
Create Commercial Divisions of High Courts	State Govts, with support from the Chief Justice and the National Judiciary Council	Number of States with Commercial Courts (Divisions of High Courts). Number of Divisions in each State.
Equip the Commercial Courts with innovative and modern processing equipments	State Govts.	State-of-the-art documentation and processing equipment.
Appoint judges and train them on laws of credit and basic principles of lending	State Govts, CBN, CIBN	Sound knowledge of the basic principles of lending by the Judges and their support staff
Transfer all pending commercial lending cases from non-commercial courts to commercial courts	State Chief Judge	No pending credit case in non-commercial court.
Set up tracking mechanism for commercial cases	CBN, CIBN, Chief Judge	Quarterly progress/status report on cases
Reform process for obtaining Governor's consent	State Govts, Judiciary and Land Registry	Number of Days from application to granting of consent
Provide legal framework for issuance and usage of credit cards.	CBN, National Assembly	Legal framework for credit cards.

Implementation Plan

Infrastructure		
Establish a Personal identification system	Federal Government	Social Security number for every Nigerian
Provide tenored incentives for organizations to fast-track the establishment of credit bureaus	CBN, FIRS	Number of Credit Bureaus by 2010
Provide tenored incentives for organizations to fast-track the establishment of Credit Rating Agencies	CBN, FIRS, SEC	Number of Credit Rating Agencies by 2010
Set up a National Collateral Registry	Fed. Govt, State Govts, CBN, CIBN, DMBs	Functional Registry by July 2010
Set up a National Bureau of Credit Statistics	Fed. Govt, CBN, CIBN, DMBs, ELAN, Credit Card Issuers	Functional Bureau by July 2010
Provide tenored incentives for banks, other financial institutions, retailers and other service providers to issue credit cards. Introduce awards for most active issuers and users of credit cards.	CBN, FIRS	Number of credit cards issued. Value of credit card transactions. Frequency of use of credit cards.
Establish Call and Service Centres of financial institutions severally in urban centres.	CBN, DMBs, Other Financial Institutions	Number of Call/Service Centres of financial institutions. Spread of the Call/Service Centres

Implementation Plan

Macroeconomic Stability		
Enact into law the Fiscal Responsibility Bill	Fed. Govt, State Govts, Local Govts, National Assembly, OPS, CBN	Fiscal Responsibility Act
Stop CBN financing of fiscal deficit	Fed. Govt, CBN	Zero Ways & Means Advances
Maintain single digit inflation rate, targeting 5%	Fed. Govt, CBN	Maximum inflation rate of 5%
Credit Institute		
Set up an internationally recognized credit training and certification Institute	CBN, NDIC, DMBs	Functional Institute
Require certification from Chief Credit Officers of financial institutions, especially DMBs	CBN, DMBs, OFIs	Certified CCOs in all financial institutions
Publish internationally recognized and accepted Credit Journal	Credit Institute	Number and destination of journal circulation

Implementation Plan

Mobilization and Credit		
Introduce awards for the following: 20% & above growth in deposit portfolio Loan-deposit ratio exceeding 60% Longest duration of deposit portfolio Lowest effective lending rate Most effective new liability product over a two-year band	CBN, CIBN	Deposit growth Loan-deposit ratio growth Duration of deposits Internationally competitive lending rate Deposit volume and % of total in new products
Consistency		
Review and update 1.1 to 5.1 as required, but not less than every three years up until year 2020.	CBN, CIBN, DMBs	Growth of aggregate credit to GDP. Growth of private sector credit to GDP. Growth of consumer credit. % of the active poor in the credit market. % of informal sector. Price of credit at internationally competitive levels. % of population having ready access to credit.

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Conclusion

- There is clear evidence that credit is a major economic growth driver.
- Credit has been largely inaccessible to the informal sector, which dominates the Nigerian national economy and also harbours the SME's that constitute the primary growth engine.
- Even for the formal sector that has access to credit, affordability remains a major issue.
- Convenience is the third important plank that brings credit to the doorstep of the active poor through a robust infrastructure that makes credit information readily available and accessible to credit grantors.
- While the 13 years from now to 2020 might seem short to the pessimists, there is strong conviction that Nigeria has the will and the capability to develop a robust credit market that will deliver on the vision and mission stated in this study.