FINANCIAL STABILITY REPORT

December 2016

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LIST OF ACRONYMS

AMCON	Asset Management Corporation of Nigeria
AML/CFT	Anti-Money Laundering and Combating the Financing of Terrorism
BDCs	Bureaux de Change
BOI	Bank of Industry
BRICS	Brazil, Russia, India, China, and South Africa
BVN	Bank Verification Number
CACS	Commercial Agriculture Credit Scheme
CAR	Capital Adequacy Ratio
CBN	Central Bank of Nigeria
COB	Currency Outside Banks
CR_5	Concentration Ratio (of the five largest banks)
CRMS	Credit Risk Management System
DAX	Deutscher Aktienindex (German stock index of 30 major German companies)
DFIs	Development Finance Institutions
DMBs	Deposit Money Banks
EBAs	Eligible Bank Assets
ECB	European Central Bank
EDC	Entrepreneurship Development Centre
EGX CASE 30	Egypt Stock Exchange (Cairo and Alexandria Stock Exchange) 30 Stock Index
FAO	Food and Agriculture Organisation
FATF	Financial Action Task Force
FCs	Finance Companies
FGN	Federal Government of Nigeria
FMBN	Federal Mortgage Bank of Nigeria
FRACE	Financial Regulation Advisory Council of Experts
FSIs	Financial Soundness Indicators
FSR	Financial Stability Report
FSRCC	Financial Services Regulation Co-ordinating Committee
GDP	Gross Domestic Product
GIZ	Deutsche Gesellschaft fur Internationale Zusammenarbeit (German Society for International Cooperation)
GSE	Ghanaian Stock Exchange
HHI	Herfindahl-Hirschman Index
ICE	Intercontinental Exchange
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
KYC	Know Your Customer
M_1	Narrow Money Supply
M_2	Broad Money Supply
MENA	Middle East and North African Countries
MFBs	Microfinance Banks
MICEX	Moscow Interbank Currency Exchange
MoUs	Memoranda of Understanding
MPR	Monetary Policy Rate
NBS	National Bureau of Statistics
NDC	Net Domestic Credit
NDIC	Nigeria Deposit Insurance Corporation

NIBSS	Nigerian Inter-bank Settlement System
NMRC	Nigeria Mortgage Re-finance Company Plc
NPLs	Non-Performing Loans
NSE ASI	Nigerian Stock Exchange All Share Index
NSE 20	Nairobi Stock Exchange 20-Share Index
NYMEX	New York Mercantile Exchange
OBB	Open Buy Back
OFIs	Other Financial Institutions
OPEC	Organisation of Petroleum Exporting Countries
ORB	OPEC Reference Basket
PAIF	Power and Aviation Infrastructure Fund
PENCOM	National Pension Commission of Nigeria
PFAs	Pension Fund Administrators
PFCs	Pension Fund Custodians
PMBs	Primary Mortgage Banks
PoS	Point of Sale
PSV 2020	Payments System Vision 2020
ROA	Return on Assets
ROE	Return on Equity
RTGS	Real-Time Gross Settlement System
S&P/TSX	Standards and Poor's Composite Index of the Toronto Stock Exchange
SEC	Securities and Exchange Commission
SMEs	Small and Medium Enterprises
WAMZ	West African Monetary Zone
WEO	World Economic Outlook
WTI	West Texas Intermediate

GOVERNOR'S STATEMENT

This issue of the *Financial Stability Report* highlights developments in the financial system in the second half of 2016. Global expectations from the fall-out of the Brexit vote, the recent US elections and the expected significant policy shifts dominate global economic outlook. The trend in global output growth was attributable to the moderated headwinds from the Brexit vote and the earlier expected monetary policy normalization in the US. However, investment activities were low, especially in countries that were affected by the Euro Area debt crisis. According to the IMF, global output growth is projected at 3.4 per cent in 2017 and 3.6 per cent in 2018, while the Euro Area is projected to grow at 1.6 per cent in 2017 and 2018, respectively.

Developments in emerging markets indicated a positive growth trajectory. The forecasts for 2017 and 2018 remain optimistic at 4.5 and 4.8 per cent, respectively. Economies in Sub-Saharan Africa (SSA) continued to be affected by headwinds and low commodity prices. Inflation in the region rose sharply, reflecting the structural supply constraints and volatility in foreign exchange. However, SSA is projected to grow by 2.8 per cent in 2017 and 3.7 per cent in 2018 (IMF WEO).

In Nigeria, output performance remained benign at negative 1.5 per cent in 2016, although the economy is expected to grow by 0.8 and 2.3 per cent in 2017 and 2018, respectively. Generally, credit to the private sector grew during the review period but household credit reduced marginally reflecting dwindling income and high domestic prices. The CBN will continue to encourage lending to the critical sectors of the economy and provide incentives for lending to SMEs and households.

The continued demand pressure on the naira and persistent supply constraints remained a key challenge in the foreign exchange market. Inflationary pressures compounded market conditions necessary to attract foreign capital required for the sustenance of exchange rate stability.

The banking sector witnessed major challenges from the negative domestic output growth, deteriorating macroeconomic indicators and global uncertainties. However, the banking sector remained safe and resilient despite these challenges.

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FOREWORD

The projected pick-up in the global output growth may be dampened by the Brexit vote, policy uncertainties in the US and volatility in international financial markets. Consequently, this may have negative impact on the growth trajectory of developing and emerging economies.

In Nigeria, the adverse macroeconomic conditions remained the major challenge to sustaining economic growth and financial system stability. Specifically, the supply constraints and demand pressure in the foreign exchange market, rising inflation and the declining output growth have threatened the sustenance of price stability and attraction of foreign capital. However, the strengthening of regulatory and supervisory measures has significantly moderated the negative consequences of the prevailing economic conditions on the banking sector and the financial system. The continued resilience of the banks was buttressed by the results of the shocks scenario of the banking sector stress tests.

To address the challenges in the industry, countercyclical measures were adopted to ensure that the banks remain resilient. Specifically, efforts were focused on ensuring that systemic risks are curtailed and that banks continue to contribute to real sector growth. As Government continues to address the adverse macroeconomic conditions, it is the goal of the CBN to ensure that banks provide support for fiscal initiatives.

Microprudential and macroprudential supervisory tools will continue to be used in surveillance and oversight of the banking sector. As appropriate structures are entrenched for the implementation of Basel II and III and IFRS 9, it is expected that the overall capacity of the banks to manage the risks in their business environment will be enhanced. It will also help ensure that Nigerian banks have systems in place for prevention of money laundering and financing of terrorism.

This edition of the Financial Stability Report is divided into five sections. Section One reviews the global and domestic economic and financial developments. Section Two discusses developments in the financial system, while Section Three covers regulatory and supervisory activities and highlights key stability issues. Key developments in the payments system are highlighted in Section Four and Section Five provides the outlook for financial stability.

We welcome financial analysts and other stakeholders to read this Report and look forward to useful feedback and suggestions.

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Deputy Governor, Financial System Stability

EXECUTIVE SUMMARY

Output growth in the global economy remained slow in 2016 due to uncertainties in some advanced economies, several emerging markets and developing economies. Consequently, global output growth remained at 3.1 per cent in both 2016 and 2015, but lower than the 3.4 and 3.6 per cent projected for 2017 and 2018, respectively.

Inflation remained a challenge for emerging market and developing economies due mainly to domestic demand pressures and supply shocks. However inflation in most advanced economies was moderate, though it experienced an upward movement in many of the countries, except for Japan where there was a slight dip in the inflation rate. Crude oil prices showed a moderate recovery in the review period to a level above $50pb at end-December 2016. Similarly, food prices rose, with most components of the FAO Food Price Index showing increases.

International stock markets showed a mixed performance across the different regions of the globe. While market indices in Europe and America showed increases, many African stock markets experienced a decline in the second half of 2016. In Asia, economic conditions in China were among the factors that impacted the performance of many Asian stock markets in the review period.

Monetary policy rates of most central banks were fairly stable. In the foreign exchange markets, most currencies depreciated against the US dollar with the exception of the Russian ruble and the South African Rand which appreciated in the second half of 2016.

In Nigeria, there was poor output performance as the growth rate remained negative. This was largely attributed to low oil prices, the impact of the insecurity in some parts of the country and foreign exchange shortages. Inflationary pressures persisted as headline inflation year-on-year remained double digit.

The economy recorded a net foreign exchange inflow, representing a 12.21 per cent rise above the level in the first half of 2016. Similarly, the total foreign exchange transactions through the Bank resulted in a net inflow. However, the external reserves declined marginally in the second half of 2016.

Money supply expanded during the review period as the growth in broad money supply, M_2, was mainly driven by the significant growth in narrow money components such as demand deposits with banks and currency outside banks. Aggregate credit to the economy also increased in the review period.

The Bank maintained its contractionary monetary policy stance in the second half of 2016 in order to stimulate capital inflow, reduce demand pressures in the foreign exchange market and tackle rising inflation. Activities in the money market reflected largely the tight liquidity in the banking system.

Activities in the equities market remained subdued as the key indices decreased compared with the preceding period. This arose mainly from the uncertainties in the macro-economy, poor corporate performance due to tougher operating environment and rising operating costs, as well as depressed household demand. However yields in the fixed income market increased, and hence attracted investors to that market.

The Bank continued to operate its risk mitigation and insurance schemes as well as the credit support schemes with the main aim of providing support to the real sector.

Key financial soundness indicators showed a decline in asset quality as the ratio of non-performing loans (NPLs) to gross loans deteriorated in the second half of 2016 by 2.3 percentage points, compared with the levels at end-June 2016. Capital adequacy indicators declined marginally, but remained above the regulatory thresholds.

A solvency stress test of the banking industry at end-December 2016 showed that the resilience of banks to moderate and severe shocks deteriorated marginally during the review period. Although the sector is more exposed to credit concentration and default risks, there were no significant systemic threats.

The result of examinations conducted in the review period confirmed the resilience and soundness of banks in the face of daunting challenges. Other regulatory activities of the Bank included the issuance of a guideline on Recovery and Resolution Plans for domestic systemically important banks and the guidance notes on the implementation of IFRS 9.

The Bank continued the implementation of the PSV 2020, registering a majority of account holders in the banking system under the BVN scheme, which has proved to be effective in fraud prevention and investigation.

The outlook is positive, despite current challenges. It is expected that with the implementation of the Government's Economic Recovery Plan, the country will return to the path of growth in 2017.

1.0 MACROECONOMIC DEVELOPMENTS AND FINANCIAL SYSTEM STABILITY

1.1 Global Economic and Financial Developments

1.1.1 Output

Global economic recovery was weak in 2016 following uncertainties in some advanced economies, particularly the United States and the United Kingdom, as well as several emerging market and developing economies. Although global output growth remained unchanged in 2016, several commodity exporting economies experienced persistent negative growth (recession), while political uncertainties in the US and UK further slowed the global economic recovery. At end-December 2016, global output remained at 3.1 per cent same as at end-December 2015, lower than 3.4 and 3.6 per cent projected for 2017 and 2018 respectively (IMF's World Economic Outlook, January 2017 Update). The marginal growth experienced by a few countries at end-December 2016 when compared with end-December 2015, was due largely to some recovery in manufacturing output, while others that witnessed unexpected slowdown during the year were mostly influenced by idiosyncratic factors. There are doubts surrounding these projections, given the uncertainties of the economic policy stance of the incoming US government and its consequences on the rest of the world.

In advanced economies, output growth was 1.6 per cent at end-December 2016, lower than 1.8 and 1.9 per cent at end-June 2016 and end-December 2015, respectively. The growth in advanced economies was projected at 1.9 per cent for 2017 and 2.0 per cent for 2018. The decline in growth in advanced economies at end-December 2016 was accounted for by the drop in output in the US and Canada.

In the United States, growth was 1.6 per cent at end-December 2016, lower than 2.2 and 2.4 per cent achieved at end-June 2016 and end-December 2015, respectively. The US growth is projected at 2.3 and 2.5 per cent for 2017 and 2018, higher than the 1.6 per cent at end-December 2016. In the UK, output growth increased from 1.7 per cent at end-June 2016 to 2.0 per cent at end-December 2016 despite the uncertainties of the Brexit in 2016. Output growth in the UK is projected at 1.5 and 1.4 per cent for 2017 and 2018, respectively. Output growth in Japan was 0.9 per cent at end-December 2016, compared with 0.3 and 0.5 per cent at end-June 2016 and end-December 2015, respectively, but projected at 0.8 per cent in 2017 and 0.5 per cent in 2018.

Output growth in the Euro area was 1.7 per cent at end-December 2016, same as at end-December 2015, but higher than 1.6 per cent recorded at end-June 2016. The slight increase over the June 2016 level was attributed to the moderated headwinds from the Brexit referendum and earlier expected monetary policy normalization in the US. However, investment activities were low, especially in countries that were affected by the Euro Area debt crisis. In the Euro Area, output growth was projected at 1.6 per cent in 2017 and 2018.

Growth in emerging market and developing economies at end-December 2016 was 4.1 per cent, the same as at end-June 2016. This was slightly higher than 4.0 per cent at end-

December 2015, and was projected at 4.5 per cent in 2017 and 4.8 per cent in 2018. In China, output growth was 6.7 per cent at end-December 2016, higher than the 6.6 per cent recorded at end-June 2016, but expected to reduce to 6.5 and 6.0 per cent in 2017 and 2018, respectively.

In the Middle East and North Africa (MENA) region, output growth was 3.8 per cent at the end of the second half of 2016, as against 3.4 per cent at the end of the first half of 2016, but projected at 3.1 per cent in 2017 and 3.5 per cent in 2018.

Output growth in Sub-Saharan Africa (SSA) was projected to increase significantly to 2.8 per cent in 2017 and 3.7 per cent in 2018, from 1.6 per cent at end-December 2016. The growth rate in the first and second halves of 2016 remained unchanged. In Nigeria, output growth improved from negative 1.8 per cent recorded at end-June 2016 to negative 1.5 per cent at end-December 2016. The Nigerian economy remained in recession in 2016, due to low oil receipts and inadequate power supply, among others. However, the IMF projected Nigeria's output growth to increase to 0.8 and 2.3 per cent in 2017 and 2018, respectively (Table 1.1).

Table 1. 1: Global Economic Outlook

Region/Country	**Year-on-Year**					
	Dec. 2014	**Dec. 2015**	**Jun. 2016**	**Dec. 2016**	**2017***	**2018***
World	3.4	3.1	3.1	3.1	3.4	3.6
Advanced Economies	1.8	1.9	1.8	1.6	1.9	2.0
United States	2.4	2.4	2.2	1.6	2.3	2.5
Euro Area	0.9	1.7	1.6	1.7	1.6	1.6
Japan	0.0	0.5	0.3	0.9	0.8	0.5
United Kingdom	2.9	2.2	1.7	2.0	1.5	1.4
Canada	2.5	1.1	1.4	1.3	1.9	2.0
Emerging Market and Developing Economies	4.6	4.0	4.1	4.1	4.5	4.8
China	7.3	6.9	6.6	6.7	6.5	6.0
MENA Region	2.8	2.3	3.4	3.8	3.1	3.5
Sub-Saharan Africa	5.0	3.3	1.6	1.6	2.8	3.7
Nigeria	6.3	2.7	-1.8	-1.5	0.8	2.3

** Projections*
Source: *World Economic Outlook, January 2017 Update*

1.1.2 Inflation

Globally, inflationary pressures were witnessed in most economies for 2016 due largely to domestic demand pressures and supply shocks. In the advanced economies, headline inflation rose significantly to 1.7 per cent in 2016 from 0.3 per cent in 2015, as oil prices showed signs of recovery. In the US, inflation rate increased to 2.1 per cent in 2016 from 0.1 per cent in 2015 and projected to 2.2 per cent in 2017. Inflation rate in Euro Area was 1.1 per cent in 2016, compared to 0.2 per cent in 2015 and projected to 1.4 per cent in 2017. In Japan, inflation declined from 0.7 per cent in 2015 to 0.5 per cent in 2016, but projected to 0.7 per cent in 2017. In the UK, the rate increased from 0.1 per cent in 2015 to 1.6 per cent in 2016 and projected to 2.2 per cent in 2017. The increase in the UK was associated with the depreciation of the Pound Sterling during the period.

Inflation rate in Emerging Market and Developing Economies was 5.6 per cent at end-December 2015, declined to 4.5 per cent at end-December 2016, but projected to 5.4 per cent in 2017. MENA Region had 5.1 per cent inflation rate in 2016, declining from 6.5 per cent in 2015 and projected to decline further to 4.0 per cent in 2017. In Sub-Saharan Africa, the rate significantly increased from 6.9 per cent at end-December 2015 to 11.3 per cent at end-December 2016, but projected to decline to 9.0 per cent in 2017. In Nigeria, the rate jumped from 9.1 per cent in 2015 to 18.6 per cent in 2016, due largely to exchange rate depreciation, rising energy prices and declining output. However, inflation in Nigeria was projected to moderate to 12.1 per cent in 2017 (Table 1.2).

Table 1. 2: Global Consumer Prices/Inflation (Per cent)

Region/Country	2012	2013	2014	2015	2016	2017*
Advanced Economies	2.0	1.4	1.4	0.3	1.7	1.9
United States	2.1	1.5	1.6	0.1	2.1	2.2
Euro Area	2.5	1.3	0.4	0.2	1.1	1.4
Japan	0.0	0.4	2.7	0.7	0.5	0.7
United Kingdom	2.8	2.6	1.5	0.1	1.6	2.2
Emerging and Developing Economies	6.1	5.9	5.1	5.6	4.5	5.4
MENA Region	9.7	9.0	6.5	6.5	5.1	4.0
Sub-Saharan Africa	9.3	6.6	6.4	6.9	11.3	9.0
Nigeria	12.2	8.5	8.1	9.1	18.6	12.1

Source: *Bloomberg*

** Projections*

1.1.3 Commodity Prices

1.1.3.1 Oil Prices

For the first time in 18 months, crude oil prices closed above $50/b at the end of 2016, compared with below $40/b at the end of 2015. The moderate uptick in crude oil prices was traced to increased global demand, the supply-cut agreement by OPEC, supply disruptions caused by the Canadian wildfires, crises in some MENA countries and the Niger Delta region of Nigeria.

The OPEC Reference Basket (ORB) price increased by 15.19 per cent to $53.30/b at end-December 2016, from $46.27/b at end-June 2016 and was higher than the end-December 2015 price of $31.27/b.

The price of Brent Crude oil increased by 15.07 per cent to $54.66/b at end-December 2016 from $47.50/b at end-June 2016, which was higher than the $37.59/b recorded at end-December 2015.

West Texas Intermediate (WTI) rose to $54.75/b at end-December 2016 from $45.30/b at end-June 2016, which was 20.86 per cent higher than the $36.77/b recorded at end-December 2015. The significant increase in the price of oil at end-December 2016 was as a result of, among other things, the unusual oil stock built-up activities by major oil suppliers at the end of 2016.

OPEC Oil supply fell by 0.221mb/d, while non-OPEC oil supply contracted by 0.71 mb/d in 2016. The decline in supply was largely due to higher-than-expected domestic consumption in Russia and Norway, as well as reduction in production levels of shale oil in the US. The non-OPEC supply is projected to rise by 0.12 mb/d in 2017, while OPEC supply is expected to rise by 0.15 mb/d in 2017.

The growth in global crude oil demand in 2016 was 1.25mb/d above the 93.95 mb/d in 2015, mostly reflecting the better economic performance in OECD, Asia Pacific and Europe regions. Global oil demand is expected to rise by 1.16 mb/d in 2017. Demand for OPEC crude oil was 31.2 mb/d, higher than its level in 2015 by 1.8 mb/d and projected at 32.1 mb/d in 2017.

Table 1. 3: World Oil Price as at December 2016

	Dec. 2015	Jun. 2016	Dec. 2016
OPEC Ref. Basket	31.27	46.27	53.30
Brent	37.59	47.50	54.66
WTI	36.77	45.30	54.75

Source: *Reuters*

1.1.3.2 Food Prices[1]

The Food and Agriculture Organisation (FAO) Food Price Index averaged 171.8 points in December 2016, compared to 163.4 points in June 2016 and 153.4 points in December 2015, reflecting an increase of 5.1 and 12.0 per cent from the June 2016 and December 2015 positions, respectively. In 2016, the index averaged 161.6 points, down by 1.5 per cent from 2015. Despite the significant increase in the prices of sugar and vegetable oils in 2016, the decline in prices of cereal, meat and dairy products kept the index below its 2015 average (Table 1.4).

The Meat Price Index averaged 161.5 points in December 2016, higher than the 159.9 points recorded in June 2016 by 1.6 points (1.0 per cent). The value was higher than the 150.0 points recorded in December 2015. Total average for 2016 was 156.6 points, lower than 168.1 points for 2015 by 7.0 per cent, influenced by a significant decline recorded for bovine and poultry meats.

The Dairy Price Index averaged 192.6 points in December 2016, higher than the level of 137.9 points in June 2016. The index was also higher than the 149.5 points recorded in December 2015 by 43.1 points, or 28.8 per cent. The increase in the second half of the year was as a result of moderate rise in the prices of butter, cheese and Whole Milk Powder (WMP), while prices for Skimmed Milk Powder (SMP) remained stable. Reduction in the production of milk in the EU and Oceania, and increase in demand continued to influence the market. The Index average for 2016 was 153.8 points marginally lower than 160.3 points for the preceding year by 4.1 per cent.

The Cereal Price Index averaged 142.1 points in December 2016, reflecting a slight reduction of 9.4 per cent from the 156.9 points in June 2016. This was 6.3 per cent lower than the 151.6 points at end-December 2015. The decline in the Cereal Price Index was attributed to the larger-than-expected wheat harvests in Australia and the Russian Federation, good crop prospects in Argentina and upward adjustments in maize production in South America. In 2016, the annual Cereal Price Index averaged 146.9 points, 9.5 per cent lower than the 162.4 points recorded in 2015.

The Vegetable Oil Price Index averaged 183.0 points in December 2016, higher than 161.9 points in June 2016 and 141.5 points in December 2015. The increase was driven primarily by palm and soy oils. The low palm oil global inventory levels and low supply continued to bolster prices, while soy oil was affected by adverse weather in Argentina and the prospect of rising uptake by the bio-diesel sector in the United States, Brazil and Argentina. Overall, the index averaged 163.8 points in 2016, compared with 147.0 in 2015, representing an increase of 11.4 per cent.

Sugar Price Index averaged 262.6 points in December 2016, lower than 276.0 points in June 2016 by 13.4 points (4.9 per cent), but higher than the 207.8 points recorded in December 2015. The fall in world sugar prices in December 2016 was majorly triggered by a continuous weakening of the Brazilian real against the US dollar and increasing sugar exports from

[1] The analysis was based on the FAO index.

Brazil (the world's largest sugar producer and exporter) in the second half of the year. Despite the fall in the price at the end of the second half of the year, the price in 2016 averaged 256.0 points, higher than 190.7 in 2015 by 34.2 per cent. The increase in the annual average price was mainly attributed to tighter supplies in Thailand and India (Table 1.4).

Table 1. 4: World Food Price Index as at December 2016

	Dec 2015	Av. 2015	June 2016	Dec 2016	Av. 2016
Food Price Index	153.4	164.0	163.4	171.8	161.6
Meat	150.0	168.1	159.9	161.5	156.6
Dairy	149.5	160.3	137.9	192.6	153.8
Cereals	151.6	162.4	156.9	142.1	146.9
Vegetable Oils	141.5	147.0	161.9	183.0	163.8
Sugar	207.8	190.7	276.0	262.6	256.0

Sources: *WEO January 2017.*

1.1.4 International Financial Markets

1.1.4.1 Stock Markets

The international stock markets recorded mixed performance in 2016. In North America, the Canadian S&P/TSX Composite, Mexican Bolsa and United States S&P 500 indices increased by 17.5, 6.2 and 9.5 per cent, respectively, between end-December 2015 and end-December 2016. In South America, the Argentine Merval, Brazilian Bovespa and Colombian IGBC General indices increased by 44.9, 38.9 and 17.2 per cent, respectively. The improved performance of the markets was due to strong domestic demand and rebound in investments during the year. In Europe, the FTSE 100, DAX, CAC 40 and MICEX indices increased by 14.4, 6.9, 4.9 and 26.8 per cent, respectively.

In Asia, the weakening economic conditions in China remained a feature in the Asian markets. As at end-December 2016, China's Shanghai Stock Exchange-A index decreased by 12.3 per cent, while India's BSE Sensex and Japan's Nikkei 225 indices increased by 1.9 and 0.4 per cent, respectively.

Stock market indices in Africa, notably, the Nigerian NSE, South African JSE All-Share, Ghanaian GSE ASI and Kenyan Nairobi NSE 20 all decreased by 6.2, 0.1, 15.3 and 21.1 per cent, respectively. The weak economic conditions in most African economies, the appreciation of the US dollar, and the continued normalization in the US, accounted for the decline in the markets. However, the Egyptian EGX CASE 30 index increased by 75.4 per cent following major economic and financial market reforms (Table 1.5).

Table 1. 5: Indices of Selected International Stock Markets: December 2015 and December 2016

Country	Index	31-Dec-15	30-Jun-16	31-Dec-16	% Change (Dec 15 – Dec 16)	% Change (Jun 16 – Dec 16)
AFRICA						
Nigeria	NSE All-Share Index	28,642.25	29,597.79	26,874.62	-6.2	-9.2
South Africa	JSE All-Share Index	50,693.76	52,217.72	50,653.54	-0.1	-3.0
Kenya	Nairobi NSE 20 Share Index	4,040.75	3,640.61	3,186.21	-21.1	-12.5
Egypt	EGX CASE 30	7,006.01	6,942.52	12,290.61	75.4	77.0
Ghana	GSE All-Share Index	1,994.91	1,787.50	1,689.18	-15.3	-5.5
NORTH AMERICA						
US	S&P 500	2,043.94	2,098.86	2,238.83	9.5	6.7
Canada	S&P/TSX Composite	13,009.95	14,064.54	15,287.59	17.5	8.7
Mexico	Bolsa	42,977.50	45,966.49	45,642.90	6.2	-0.7
SOUTH AMERICA						
Brazil	Bovespa Stock	43,349.96	51,526.93	60,227.29	38.9	16.9
Argentina	Merval	11,675.18	14,683.49	16,917.86	44.9	15.2
Columbia	COLCAP	1,153.71	1,313.18	1,351.68	17.2	2.9
EUROPE						
UK	FTSE 100	6,242.32	6,504.33	7,142.83	14.4	9.8
France	CAC 40	4,637.06	4,237.48	4,862.31	4.9	14.7
Germany	DAX	10,743.01	9,680.09	11,481.06	6.9	18.6
Russia	MICEX	1,761.36	1,891.09	2,232.72	26.8	18.1
ASIA						
Japan	NIKKEI 225	19,033.71	15,575.92	19,114.37	0.4	22.7
China	Shanghai SE A	3,704.29	3,066.50	3,249.59	-12.3	6.0
India	BSE Sensex	26,117.54	26,999.72	26,626.46	1.9	-1.4

Source: *Bloomberg*

1.1.5 Foreign Exchange Markets

During the second half of 2016, most of the currencies under review experienced mixed movements against the U.S. dollar. In Africa, the South African rand appreciated against the U.S. dollar by 5.97 per cent, while the Nigerian naira, Kenyan shilling, Egyptian pound and Ghanaian cedi depreciated against the U.S. dollar by 7.21, 1.38, 50.99 and 6.84 per cent, respectively.

Foreign exchange rate movement in North America indicated that the Canadian dollar and Mexican Peso depreciated against the U.S. dollar by 2.99 and 10.90 per cent, respectively. In South America, the Brazilian real, Argentine peso and Colombian peso depreciated against the U.S. dollar by 1.53, 5.23 and 2.72 per cent, respectively. In Europe, the British pound and euro depreciated against the U.S. dollar by 7.41 and 5.26 per cent, respectively, while the Russian ruble appreciated against the U.S. dollar by 3.90 per cent.

In the Asian region, the Japanese yen, Chinese yuan and Indian rupee depreciated against the U.S. dollar by 11.77, 4.32 and 0.57 per cent, respectively. The low global commodity prices and weak economic conditions accounted for the general depreciation of most currencies against the dollar (Table 1.6).

Table 1. 6: Exchange Rate of Selected Countries (Value in currency units to US$): Dec.2015 and Dec. 2016

	Currency	31-Dec-15	30-Jun-16	31-Dec-16	June 16 - Dec. 2016 % App/Dep.	Y-on-Y App/Dep.
AFRICA						
Nigeria	Naira	197.00	283.00	305.00	-7.21	-35.41
South Africa	Rand	15.48	14.56	13.74	5.97	12.66
Kenya	Shilling	102.30	101.10	102.51	-1.38	-0.20
Egypt	Pound	7.83	8.89	18.14	-50.99	-56.84
Ghana	Cedi	3.81	3.95	4.24	-6.84	-10.14
NORTH AMERICA						
Canada	Dollar	1.38	1.30	1.34	-2.99	2.99
Mexico	Peso	17.23	18.47	20.73	-10.90	-16.88
SOUTH AMERICA						
Brazil	Real	3.96	3.21	3.26	-1.53	21.47
Argentina	Peso	12.93	15.05	15.88	-5.23	-18.58
Colombia	Peso	3174.50	2920.35	3002.00	-2.72	5.75
EUROPE						
UK	Pound	0.68	0.75	0.81	-7.41	-16.05
Euro Area	Euro	0.92	0.90	0.95	-5.26	-3.16
Russia	Ruble	72.85	63.94	61.54	3.90	18.38
ASIA						
Japan	Yen	120.20	103.19	116.96	-11.77	2.77
China	Yuan	6.49	6.65	6.95	-4.32	-6.62
India	Rupee	66.15	67.53	67.92	-0.57	-2.61

***Source**: Bloomberg*

1.1.6 Monetary Policy Rates

Monetary policy rates of most central banks were fairly stable during the second half of 2016. The rates remained within the zero bound in advanced economies in a bid to catalyze growth. The US Federal Reserve kept its rate within the bound of 0.25-0.50 per cent for eleven months of 2016, but shifted to 0.50 - 0.75 per cent bound in December 2016.

The Bank of Japan, Bank of Canada and Bank Negara Malaysia, as well as the central banks of Chile and Colombia held their rates constant. However, Bank of England, European Central Bank, Bank of Korea, Reserve Bank of Australia, Bank of Indonesia, Central Bank of Russia, Peoples Bank of China (PBOC), and Reserve Bank of New Zealand lowered their rates during the review period. South Korea maintained 1.50 per cent since July 2015, but reduced to 1.25 per cent in June 2016. New Zealand maintained 2.75 per cent from September 2015, but reduced to 2.25 per cent in March 2016 and further to 1.75 in November 2016. The Bank of Indonesia which maintained its rate at 7.50 per cent since July 2015 reduced it to 6.5 per cent in June 2016 and further to 4.75 per cent in November 2016. The central bank of Mexico increased its rate from 3.75 to 4.25 per cent in May 2016 with an increase it to 4.75 per cent in October 2016 and then to 5.25 per cent in December 2016.

In the BRICS economies, Brazil maintained 14.25 per cent in the first ten months of 2016 and reduced to 13.75 per cent in December 2016. Russia reduced from 11.00 per cent to 10.50 per cent in June 2016 and further to 10.00 per cent in September 2016. India reduced the rate to 6.50 per cent from 6.75 per cent in April 2016 and further to 6.25 per cent in October, while China's rate remained at 4.35 per cent from July 2016. South Africa also maintained 7.00 per cent.

Policy rates in African economies changed slightly, except in Nigeria where 14.00 per cent was maintained during the review period. Egypt was 11.75 per cent in June 2016, but moved up to 14.75 per cent in November 2016. Ghana's rate increased from 25.00 per cent to 26.00 per cent in June 2016 and reduced to 25.5 per cent in November 2016 (Table 1.7).

Table 1.7: Policy Rates Across Selected Countries (January – December 2016)

	2016					2016						
Country	**Jan-16**	**Feb-16**	**Mar-16**	**Apr-16**	**May-16**	**Jun-16**	**Jul-16**	**Aug-16**	**Sep-16**	**Oct-16**	**Nov-16**	**Dec-16**
Developed Economies												
Japan	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Europe	0.05	0.05	0.00	0.00	0.00	0.00	0.05	0.05	0.05	0.05	0.05	0.05
UK	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.25	0.25	0.25	0.25	0.25
US	0.25-0.50	0.25-0.50	0.25-0.50	0.25-0.50	0.25-0.50	0.25-0.50	0.25-0.50	0.25-0.50	0.25-0.50	0.25-0.50	0.25-0.50	0.50-0.75
Canada	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
South Korea	1.50	1.50	1.50	1.50	1.50	1.25	1.25	1.25	1.25	1.25	1.25	1.25
New Zealand	2.75	2.75	2.25	2.25	2.25	2.25	3.50	3.50	2.75	2.75	1.75	1.75
Australia	2.00	2.00	2.00	2.00	1.75	1.75	2.00	1.5	1.5	1.5	1.5	1.50
ASEAN												
Indonesia	7.25	7.00	6.75	6.75	6.75	6.50	5.25	5.25	5.25	5.25	4.75	4.75

Malaysia	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.00	3.00	3.00	3.00	3.00
BRICS												
Brazil	14.25	14.25	14.25	14.25	14.25	14.25	14.25	14.25	14.25	14.25	14.00	13.75
Russia	11.00	11.00	11.00	11.00	11.00	10.50	10.50	10.50	10.00	10.00	10.00	10.00
India	6.75	6.75	6.75	6.50	6.50	6.50	6.50	6.50	6.50	6.25	6.25	6.25
China	5.60	5.35	5.35	5.35	5.10	4.81	4.35	4.35	4.35	4.35	4.35	4.35
South Africa	6.75	6.75	7.00	7.00	7.00	7.00	7.00	7.00	7.00	7.00	7.00	7.00
Other Emerging Economies & South America												
Mexico	3.25	3.75	3.75	3.75	3.75	4.25	4.25	4.25	4.25	4.75	4.75	5.25
Chile	3.50	3.50	3.50	3.50	3.50	3.50	3.00	3.50	3.50	3.50	3.50	3.50
Colombia	6.00	6.25	6.50	7.00	7.25	7.50	7.50	7.75	7.75	7.75	7.75	7.75
Africa												
Egypt	10.25	10.25	11.75	11.75	11.75	12.75	11.75	11.75	11.75	11.75	14.75	14.75
Ghana	25.00	25.00	25.00	25.00	25.00	25.00	26.00	26.00	26.00	26.00	25.50	25.50
Nigeria	11.00	11.00	12.00	12.00	12.00	12.00	14.00	14.00	14.00	14.00	14.00	14.00

Source: *Bloomberg*

1.2 Domestic Developments

1.2.1 Output

The negative output performance witnessed in the first half of 2016 moderated in the second half of the year. This was largely attributed to low oil price and the impact of the insecurity in some parts of the country. Furthermore, the foreign currency shortages contributed significantly to naira depreciation in the foreign exchange market, and the pass-through effect on domestic prices and cost of production. Consequently, data from the National Bureau of Statistics (NBS) indicated that the contraction in the Gross Domestic Product (GDP) at 2010 constant basic prices continued, to negative 1.76 per cent in the second half of 2016, compared with the negative 1.22 per cent in the first half of 2016.

Figure 1. 1: Real GDP Growth rate (%)

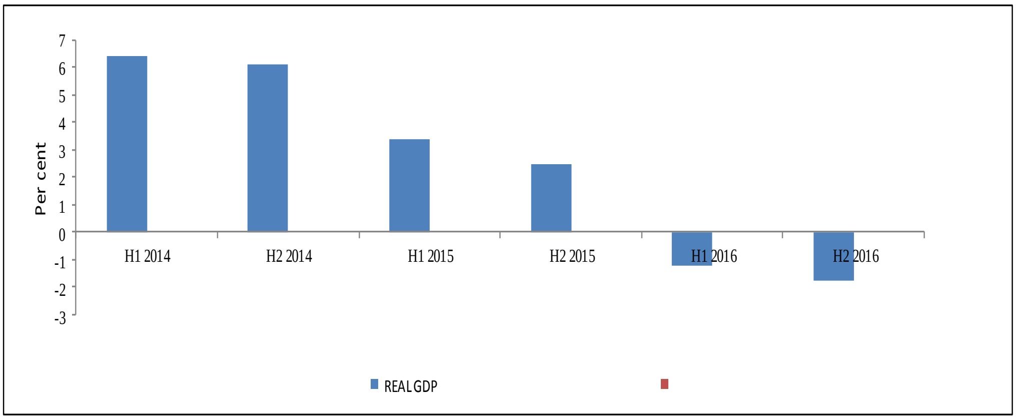
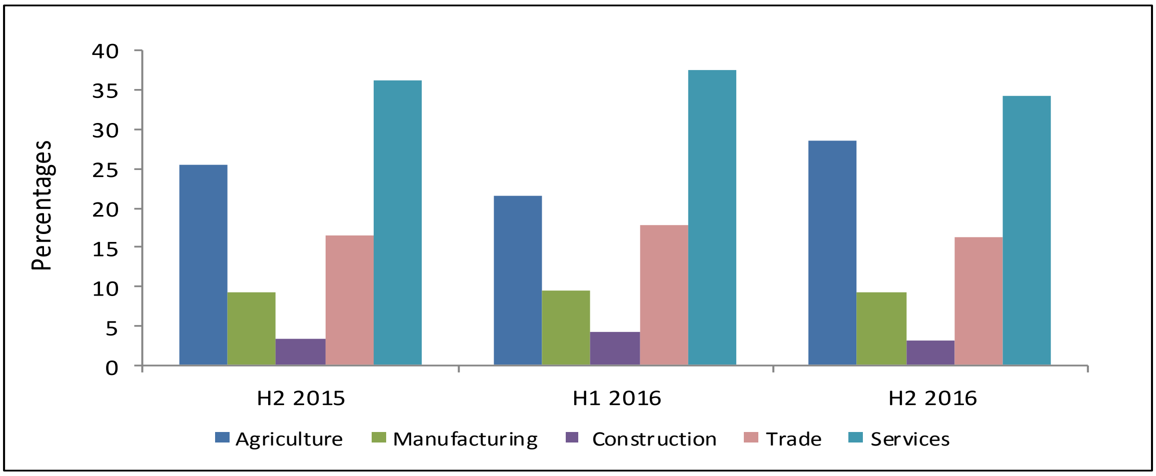


Figure 1. 2: Gross Domestic Product by Sectors (%)



The non-oil GDP fell to 0.16 per cent in the second half of 2016, compared with the decline of 0.29 per cent in the first half of the year. The significant decline in oil prices led to the increase in the contribution of the non-oil sector GDP by 1.61 and 1.48 percentage points above the 90.73 and 90.86 per cent recorded in the preceding half year and the corresponding period of 2015, respectively. With respect to sectoral contribution in real terms, the services sector accounted for the largest share (36.28%), followed by the agricultural sector (27.04%), industry (16.91%), trade (16.52%) and construction (3.25%) (Figure 1.2).

During the second half of 2016 the average daily production of crude oil fell to 1.60 million barrels per day (mb/d) in the second half from 1.68 mb/d in the first half of 2016. Consequently, the contribution of the oil sector to the real GDP decreased to 7.66 per cent from 9.27 and 9.14 per cent recorded in the preceding half year and the corresponding period of 2015, indicating a decline of 1.61 and 1.43 percentage points, respectively.

Figure 1. 3: Share of Oil and Non-oil Sectors in Real GDP (%)

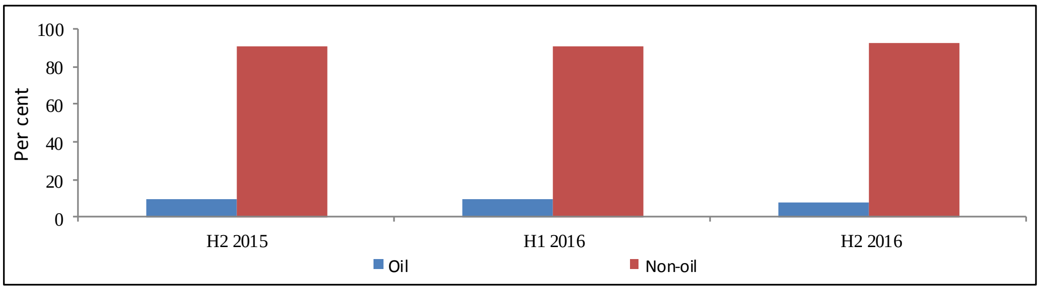


Table 1. 8: Changes (per cent) in Real GDP by Sector over Corresponding Half Year

Sector	H2 2015	H1 2016	H2 2016
Manufacturing	-0.70	-5.22	-3.46
Construction	-0.24	-5.83	-6.07
Services	3.50	-1.04	-1.34
Trade	4.55	0.99	-1.41
Industry	-1.96	-7.62	-10.42
Agriculture	3.47	3.84	4.29
Crude Petroleum, Natural Resources and Solid Minerals	-3.34	-9.53	-17.71

1.2.2 Inflation

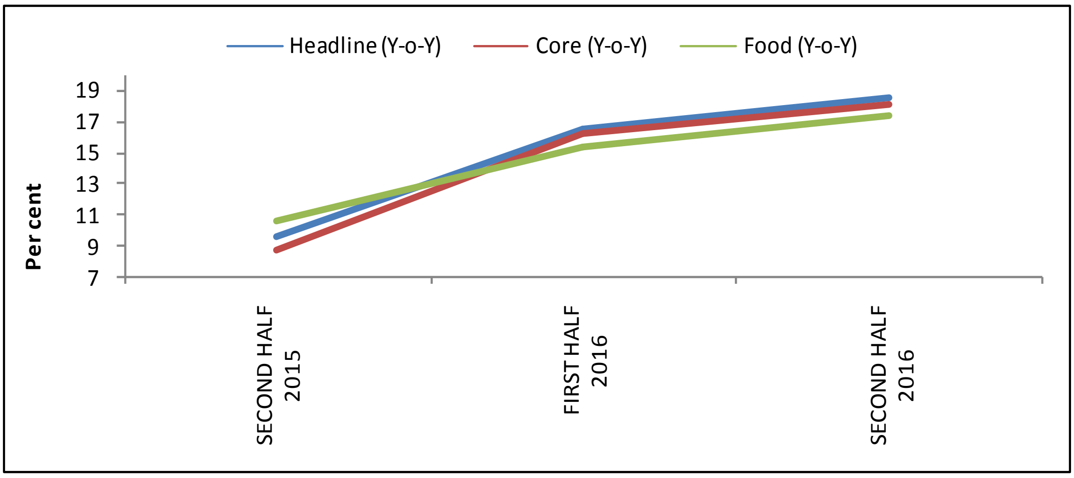
The composite Consumer Price Index (CPI) at November 2009 constant prices was 213.55 in December 2016, compared with 201.7 and 180.1 at end-June 2016 and the corresponding period of 2015, respectively. Consequently, year-on-year headline inflation stood at 18.55 per cent in December 2016, compared with the level of 16.48 per cent in June 2016, representing an increase of 2.07 percentage points. The inflationary pressure, during the period, was largely driven by the continued impact of the removal of subsidies in the energy sector and the depreciation of the naira, which increased domestic cost of production and services.

Food inflation, which comprises farm produce and processed food stood at 17.39 per cent year-on-year at end-December 2016, from 15.30 and 10.59 per cent at end-June 2016 and end-December 2015, respectively. This represents increases of 2.09 and 6.80 percentage points over the preceding and corresponding periods.

The imported food inflation (year-on-year) at end-December 2016, rose by 1.06 percentage points to 21.09 per cent from its level at end-June 2016, contributing 5.25 percentage points of the food inflation at end-December 2016 compared to 4.96 percentage points at end-June 2016. Rice accounted for the highest contribution of 11.67 per cent to imported food inflation, followed by frozen fish with 9.56 per cent.

Similarly, core inflation, which excludes the prices of volatile agricultural produce, rose to 18.1 per cent at end-December 2016, from 16.22 and 8.73 per cent at end-June 2016 and end-December 2015, respectively (Figure 1.4).

Figure 1. 4: Inflationary Trend (Year-on-Year)



1.2.3 External Sector

1.2.3.1 Foreign Exchange Flows

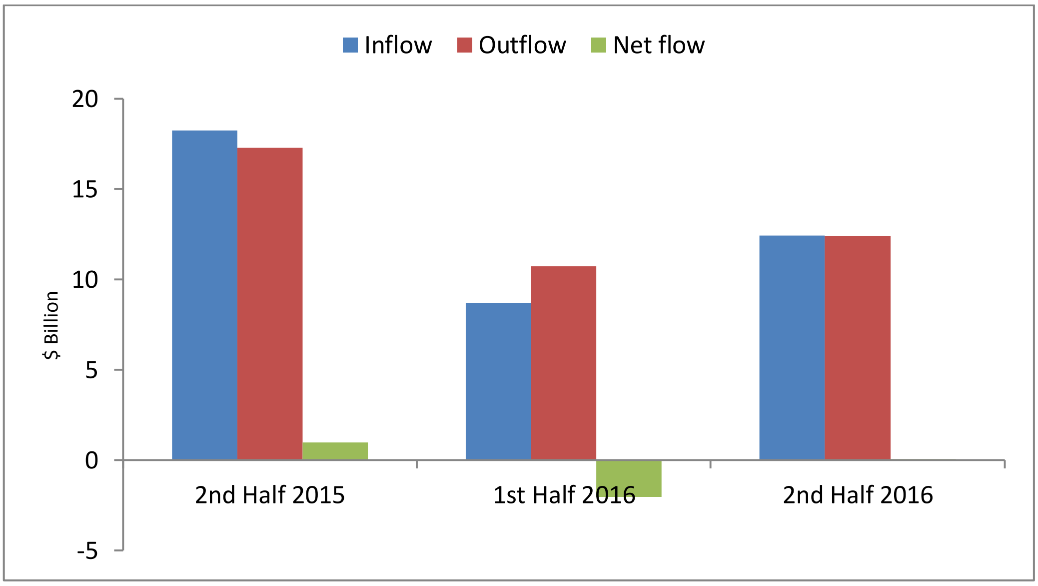
The provisional cumulative inflow of foreign exchange into the economy, at US$33.02 billion, was 13.3 per cent above the level in the first half of 2016. Of this amount, inflow through autonomous sources accounted for 62.3 per cent, while inflow through the CBN accounted for 37.7 per cent. Total foreign exchange outflow from the economy rose by 14.8 per cent to US$13.64 billion from the level in the first half of 2016. The rise in outflow was mainly attributed to the increase in the interbank forwards settled in the second half of 2016. The economy recorded a net foreign exchange inflow of US$19.38 billion, representing 12.21 per cent rise above the level in the first half of 2016.

The total autonomous inflow rose by 0.7 per cent to US$20.58 billion, compared to the level in the first half of 2016 due mainly to rise in invisibles by 2.5 per cent, of which 62.3 per cent was accounted for by ordinary domiciliary accounts. Foreign exchange inflow through the CBN rose by 42.9 per cent above the level in the first half of 2016 to US$12.45 billion, due to increases in crude oil and non-oil export earnings. Receipts from crude oil sales rose by 22.7 per cent to US$5.66 billion, in the first half of 2016. This is attributable to the gradual increase in domestic production and international crude oil prices. The non-oil receipts rose by 65.5 per cent to US$6.79 billion in the second half of 2016, due mainly to increase in other official receipts.

Foreign exchange outflow through the CBN rose by 15.5 per cent to US$12.39 billion, above the level in the first half of 2016. Of this amount, interbank utilization accounted for US$7.99 billion, of which inter-bank forwards, inter-bank sales and others stood at US$4.17 billion (52.14%), US$0.72 billion (8.92%) and US$3.11 billion (38.9%), respectively.

Overall, the total foreign exchange transactions through the Bank resulted in a net inflow of US$0.58 billion in the second half of 2016, compared with a net inflow of US$0.96 billion in the corresponding half of 2015. This is, however, in contrast to a net outflow of US$2.03 billion in the first half of 2016.

Figure 1. 5: Foreign Exchange Transactions through the CBN (Second Half 2016, US$' Billion)



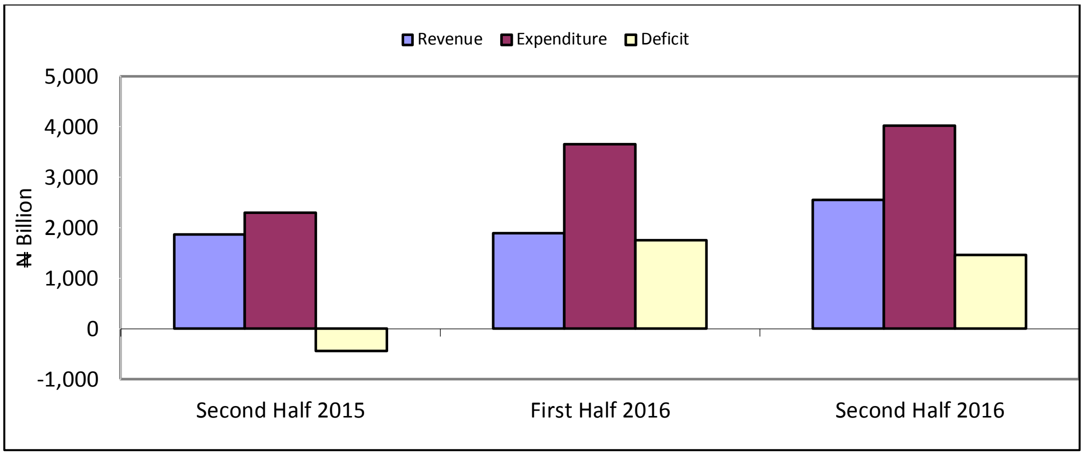
1.2.4 Fiscal Operations

Federal Government Retained revenue for the second half of 2016 increased to ₦2,558.0 billion, above the levels of ₦1,898.21 billion recorded in the first half of 2016 and the half-year budget estimate of ₦2,024.90 billion for 2016. The increase in the retained revenue relative to the first half was mainly attributed to increase in non-oil receipts. The breakdown of the retained revenue showed that the Federal Government's share of the Federation Account was ₦1,262.4 billion (49.4%); the VAT Pool Account, ₦90.7 billion (3.5%); the Federal Government Independent Revenue, ₦267.8 billion (10.5%); share of excess crude Account, ₦141.4 billion (5.5%); Exchange Gain, ₦316.4 billion (12.4%) while others (including NNPC Refund) accounted for the balance of ₦479.3 billion (18.7%).

The fiscal stance of increased spending to address the challenges of the negative growth (recession) led to higher government expenditure in the second half of 2016. Consequently, Federal Government expenditure grew by 10.3 per cent to ₦4,024.8 billion, above ₦3,650.33 billion in the first half of 2016. It was, also higher than the budgeted expenditure of ₦3,127.27 billion for the second half of 2016. Recurrent expenditure component of the total expenditure accounted for ₦3,496.5 billion (86.9%) while capital and statutory transfers components accounted for ₦264.9 billion (6.6%) and ₦263.4 billion (6.5%), respectively.

The fiscal operations of the Federal Government in the second half of 2016 resulted in an overall deficit of ₦1,466.8 billion, compared with the ₦1,752.11 billion recorded in the first half of 2016 and the budgeted deficit of ₦1,102.37 billion for the second half of 2016. The deficit was financed through domestic sources including issuance of government securities.

Figure 1. 6: Federal Government Fiscal Operations (₦ Billion)



The consolidated domestic debt stock of the Federal Government at end-December 2016 was ₦11,738.62 billion. This represented an increase of 10.8 per cent over ₦10,606.33 billion at end-June 2016.

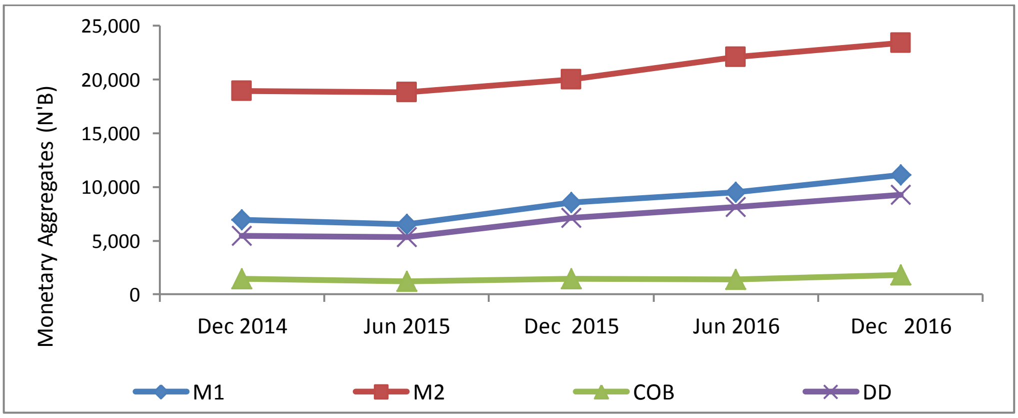
2.0 DEVELOPMENTS IN THE FINANCIAL SYSTEM

2.1 Monetary and Credit Developments[2]

Monetary policy management in the second half of 2016 remained a challenge due to slow recovery of crude oil prices in the international market, shortage of foreign exchange, inflationary pressures and weak economic conditions. Money supply expanded during the review period compared to the first half of 2016 and the corresponding period of 2015. Relative to the level at end-December 2015 broad money supply, M_2, rose by 16.93 per cent to ₦23,421.82 billion at end-December 2016, compared with the growth of 10.23 per cent at end-June 2016.

The growth in broad money at end-December 2016 was also higher than the 5.90 per cent growth recorded at end-December 2015. The growth in M_2 at end-December 2016 was largely due to the 57.27 and 25.64 per cent expansion in net foreign assets and domestic credit (net) of the banking system. The increases more than offset the effect of the 74.45 per cent decline in other assets (net) of the banking system. Correspondingly, the growth in total monetary liabilities, M_2, was driven by the significant increase in narrow money (M_1). Provisional data indicated that narrow money (M_1) grew by 29.51 per cent to ₦11,101.59 billion at end-December 2016, compared with the growth of 11.05 per cent at end-June 2016. The growth in M_1 at end-December 2016 was due to the 30.43 per cent and 25.02 per cent growth in demand deposits (DD) with banks and currency outside banks (COB), respectively.

Figure 2. 1: Trend in Monetary Aggregates



There was a slight weakening in intermediation efficiency of the banking industry at end-December 2016. The ratio of intermediation efficiency measured by the proportion of currency outside banks (COB) to total monetary liabilities, stood at 7.8 per cent, representing an increase of 1.6 and 0.5 percentage points above the level at end-June 2016 and the corresponding period of 2015, respectively. Negative real rates of interest on deposits and higher cost of living contributed to the relatively high level of currency outside the banks during the review period.

Aggregate savings at end-December 2016 declined with the ratio of quasi-money to total

[2] The analysis is based on the provisional December 2016 CBN Monetary Survey.

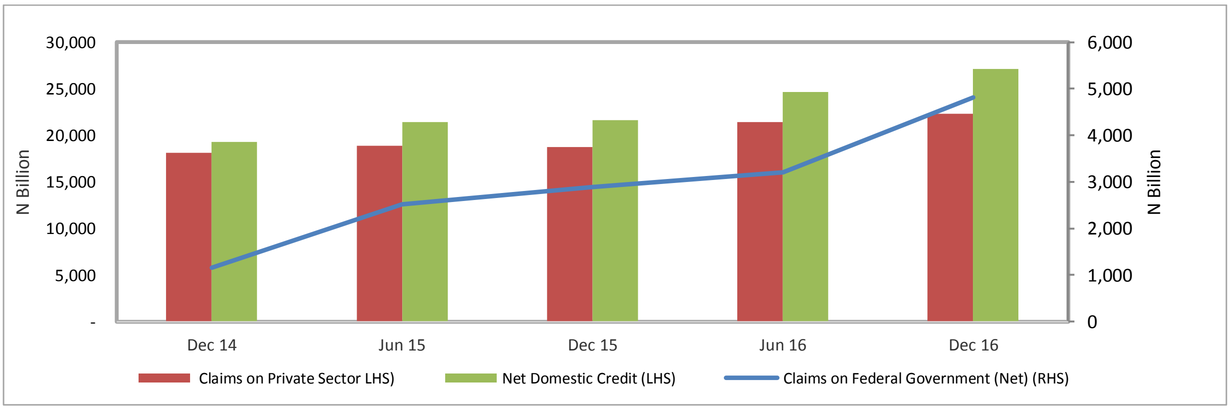
monetary assets at 52.6 per cent from 56.9 per cent at end-June 2016. The outcome was driven, largely, by the decline in savings and time deposits of commercial and merchant banks, which proportion of M_2 fell by 4.3 percentage points below the level at end-June 2016.

2.1.1 Aggregate Credit to the Economy

Despite the continuing contractionary monetary policy stance of the Bank, net aggregate credit to the domestic economy rose from ₦24,623.63 billion at end-June 2016 to ₦27, 153.87 billion at end-December 2016 representing a 10.3 per cent rise. The development reflected increases in claims on the private sector and net claims on the Federal Government.

In terms of contribution to the growth in M_2, the net domestic credit of the banking system contributed 27.3 percentage points compared with 13.6 percentage points at end-June 2016. The contribution of credit to the core private sector to the growth in M_2 rose from 11.6 percentage points at end-June 2016 to 17.3 percentage points, during the review period.

Figure 2. 2: Credit to the Economy



2.1.1.1 Claims on the Federal Government

Net claims on the Federal Government increased to ₦4,808.04 billion at end-December 2016 compared with ₦2,893.19 billion at end-June 2016, representing an increase of 10.6 per cent. The development reflected significant growth in holding of government securities, especially Treasury bills and FGN bonds, which grew by 28.9 per cent and 42.7 per cent, respectively.

Net claims on the Federal Government contributed 9.6 percentage points to the growth rate of total monetary assets, compared with 1.5 percentage points at end-June 2016.

2.1.1.2 Aggregate Claims on the Private Sector

Banking system's credit to the private sector grew by 19.37 per cent to ₦22,345.84 billion, at end-December 2016 compared with the growth of 14.44 and 3.29 per cent recorded at end-June 2016 and the corresponding period of 2015, respectively. The development reflected, largely, the 19.14 per cent increase in claims on the core private sector[3], which continues to reflect the impact of various policies of the CBN that enhanced the lending capacity of banks.

[3]Excludes the states and local governments.

In terms of contribution to the growth rate of total monetary assets, claims on the private sector stood at 17.3 percentage points, compared with 11.61 percentage points at end-June 2016.

Table 2. 1: Growth in Monetary Aggregates

% Change (Over preceding December)	Jun 14 revised	Dec 14 revised	Jun 15 revised	Dec 15	Jun 16 revised	Dec 16
Domestic Credit (Net)	14.82	32.6	11.08	12.13	13.93	25.64
Claims on Federal Government (Net)	85.75	169.44	118.45	151.56	0.00003	58.84
Claims on Private Sector	4.53	11.93	4.27	3.29	14.44	19.37
Foreign Assets (Net)	(11.38)	(19.68)	(14.42)	(18.71)	25.69	57.27
Other Assets (Net)	(9.58)	2.53	(16.88)	1.08	(33.38)	(74.45)
Total Monetary Assets (M2)	12.03	20.55	(0.54)	5.90	10.23	16.93
Quasi-Money	21.07	38.73	2.17	(4.58)	9.61	7.52
Money Supply (M1)	0.90	-1.82	(5.25)	24.14	11.05	29.51
Currency Outside Banks	(16.25)	(0.64)	(17.63)	1.30	(5.29)	25.02
Demand Deposits	5.35	(2.13)	(1.99)	30.15	14.40	30.43
Total Monetary Assets (M2)	12.03	20.55	(0.54)	5.90	10.23	16.93

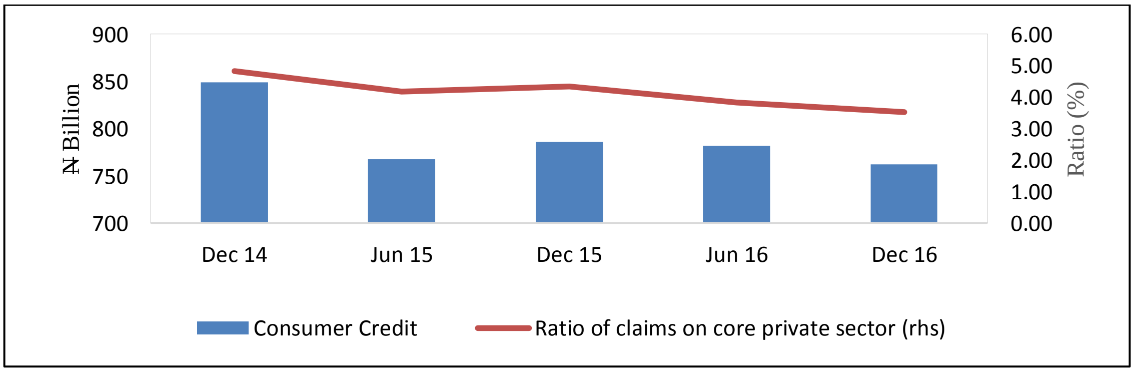
2.1.1.3 Foreign Assets (net) of the Banking System

Net foreign assets of the banking system rose by 57.27 per cent to ₦8,891.06 billion at end-December 2016, compared with the 25.7 per cent growth at end-June 2016, in contrast to a decline of 18.7 per cent at the end of the corresponding period of 2015. The development reflected significant growth in foreign assets of the CBN which grew by 53.9 per cent relative to its level at end December 2015.

2.1.1.4 Consumer Credit

The volume of consumer credit during the second half of 2016 reduced marginally by 2.51 per cent to ₦762.07 billion relative to its level at end-June 2016, due largely to build up of uncertainties and higher cost of funds in the economy. Consumer credit, which constituted 3.53 per cent of the total credit to the core private sector, was 0.3 percentage point lower than the proportion in the first half of 2016 (Figure 2.3).

Figure 2. 3: Consumer Credit



2.1.2 Sectoral Classification of Private Sector Credit

As at end-December 2016, bank credit to the various sectors showed an upward trend. Sectoral credit to the private sector rose by 3.9 per cent to ₦16,293.48 billion at end-December 2016 from ₦15,677.71 billion at end-June 2016. The oil and gas sector accounted for the highest share of total credit with 30.02 per cent, compared with 28.78 per cent in the first half of 2016. Manufacturing and power & energy sub-sectors accounted for 13.6 per cent and 4.5 per cent, compared with 12.9 per cent and 4.4 per cent, respectively, in the preceding half year. Agriculture, forestry, and fishery sub-sector accounted for 3.3 per cent, indicating a 0.2 percentage point increase above the 3.1 per cent in the preceding half year. The contribution of the construction sector remained the same at 3.89 per cent as in the preceding half year (Figure 2.4 and Table 2.2).

Figure 2. 4: Sectoral Distribution of Credit

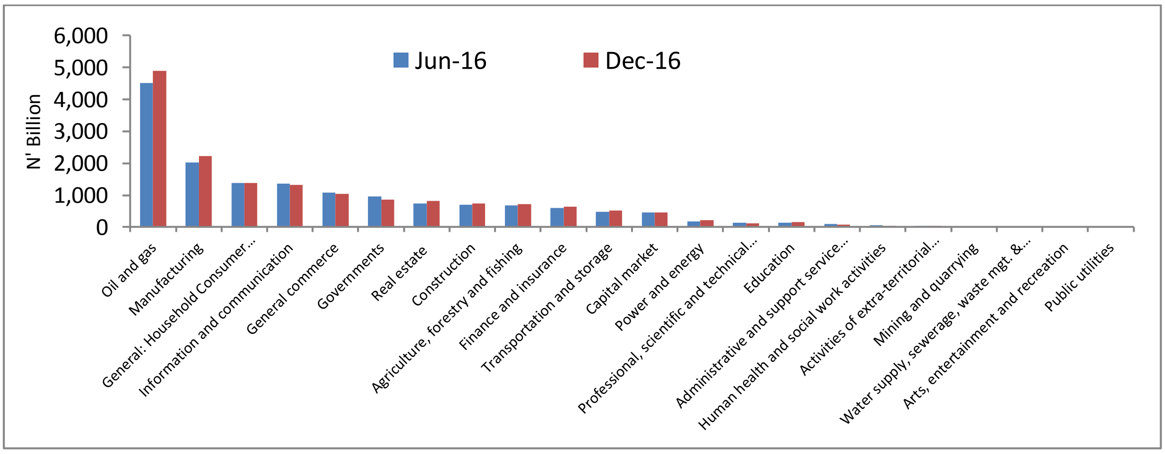


Table 2. 2: Sectoral Distribution of Credit

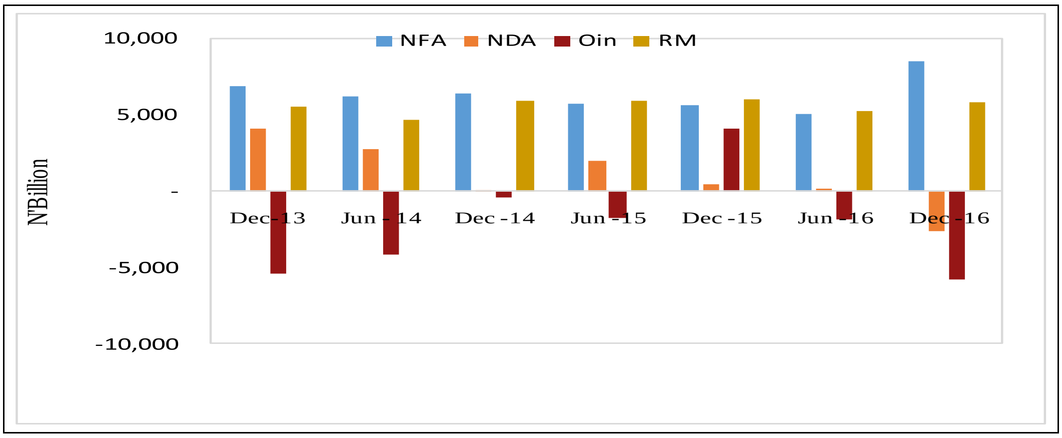
Sector	June 2016		December 2016	
	₦' Billion	Share of Total (%)	₦ 'Billion	Share of Total (%)
Oil and gas	4,511.34	28.78	4,890.91	30.02
Manufacturing	2,030.67	12.95	2,214.98	13.59
Governments	1,386.61	8.84	1,376.89	8.45
General	1,363.54	8.70	1,324.10	8.13
General commerce	1,071.57	6.83	1,038.92	6.38
Information and communication	960.85	6.13	859.16	5.27
Real estate activities	737.96	4.71	820.32	5.03
Finance and insurance	692.94	4.42	737.65	4.53
Power and energy	685.23	4.37	726.29	4.46
Construction	609.68	3.89	633.62	3.89
Agriculture, forestry and fishing	482.71	3.08	529.06	3.25
Transportation and storage	458.85	2.93	452.19	2.78

Capital market	178.02	1.14	212.28	1.30
Public utilities	133.67	0.85	111.96	0.69
Professional, scientific and technical activities	130.23	0.83	151.23	0.93
Education	88.94	0.57	88.4	0.54
Administrative and support service activities	66.42	0.42	30.61	0.19
Human health and social work activities	42.59	0.27	42.16	0.26
Mining and quarrying	16.35	0.10	21.28	0.13
Water supply sewerage, waste management and remediation activities	15.74	0.10	17.03	0.10
Arts, entertainment and recreation	13.65	0.09	14.44	0.09
Activities of extraterritorial organization and bodies	0.12	0.00	0.01	0.00
Total	**15,677.71**	100.00	**16,293.48**	100.00

2.1.3 Reserve Money (RM)

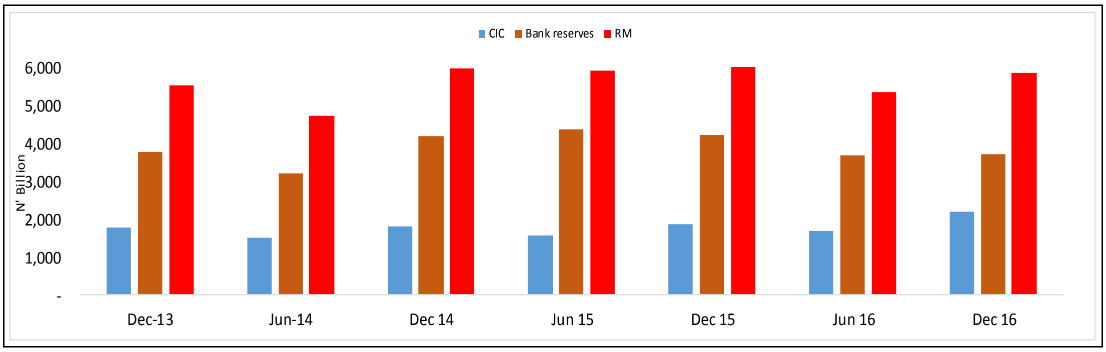
Reserve money (RM) at end-December 2016 rose by 9.61 per cent to ₦5,888.20 billion from ₦5,372.01 billion at end-June 2016. This was, however, lower than its level by 3.01 and 10.52 per cent for the corresponding period of 2015 and the fourth quarter of 2016 indicative benchmark of ₦6,580.39 billion, respectively. The upward movement in reserve money relative to the level at end-June 2016 reflected the 56.94 per cent increase in the net foreign assets of the CBN, which more than offset the decline in net domestic assets and other assets net.

Figure 2. 5 Reserve Money and its Components - Sources



The corresponding increase in the uses of reserve money was due to the 29.35 and 0.59 per cent rise in currency-in-circulation and bank reserves, respectively.

Figure 2. 6: Reserve Money and its Components – Uses



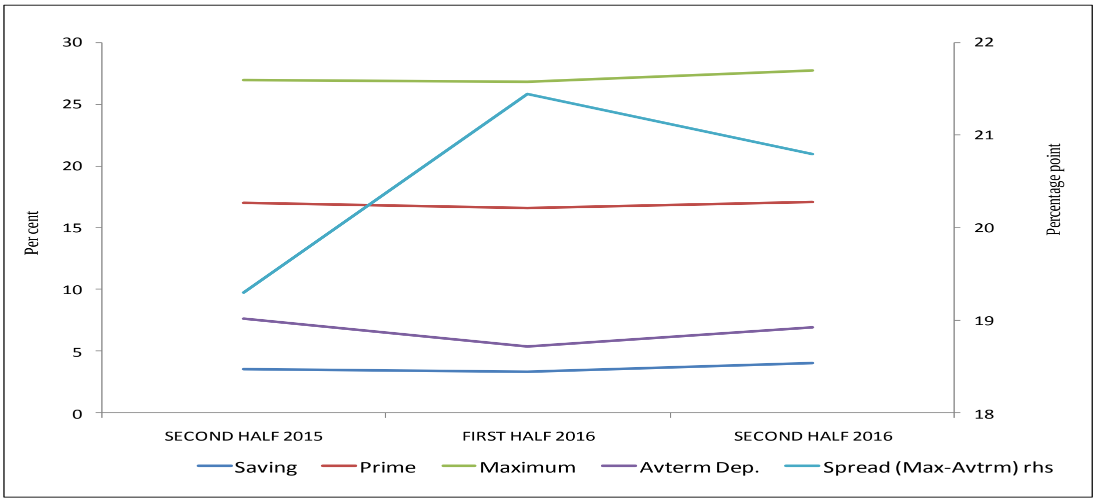
2.1.4 Interest Rate

The Monetary Policy Committee (MPC) at its July 2016 meeting increased the Monetary Policy Rate (MPR) from 12.00 to 14.00 per cent. This was to complement the adoption of the flexible foreign exchange policy framework in a bid to moderate inflation and provide for positive real returns on investment to attract investors. The tight monetary policy stance of the Bank brought about a reduction in the banking system liquidity, which impacted on money market rates. In a bid to stem inflationary pressure and curtail liquidity arising from maturing CBN bills as well as fiscal injections, the CBN intensified its liquidity management activities through the Open Market Operation (OMO) auctions.

On the average, all the rates in the second half of 2016 were higher than their levels in the first half. Savings deposit rate rose slightly by 0.70 percentage point from 3.4 per cent in the first half, to 4.1 per cent in the second half of 2016. Similarly, average deposit rates for 7-day, 3-month and 1-year tenors rose from 2.83, 6.84 and 5.25 per cent in the first half of 2016 to 3.65, 8.13 and 7.20 per cent, respectively in the second half of 2016.

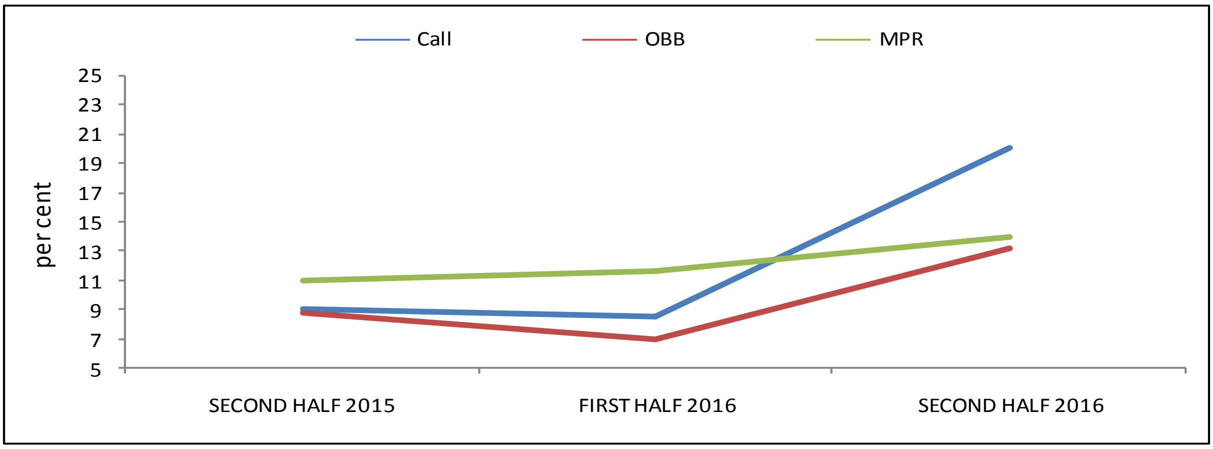
The 6-month average prime and maximum lending rates rose in the second half of 2016 by 0.48 percentage point to 17.11 per cent and by 0.93 percentage point to 27.75 per cent, compared with their levels in the first half of 2016. Relative to the first half of 2016, the average term deposit rate rose by 1.58 percentage points to 6.96 per cent in the second half of 2016. Consequently, the spread between the average term deposit and the average maximum lending rates narrowed by 0.65 percentage point to 20.80 per cent at the end of the second half of 2016. Real deposit and prime lending rates were negative, while real maximum lending rate recorded positive trend given the prevailing headline inflation rate of 18.55 per cent at end-December 2016.

Figure 2. 7: Lending and Deposit Rates



The 6-month average open-buy-back (OBB) rate in the second half of 2016 stood at 13.15 per cent while inter-bank call rate averaged 20.13 per cent, representing 6.14 and 11.63 percentage points increase above their levels in the first half of 2016. The NIBOR averaged 19.24 and 17.36 per cent for the call and 30-day segments in the second half of 2016 compared with 6.73 and 6.75 per cent in the first half of 2016. The corridor around the MPR for standing lending and deposit facilities was retained at +200 and -500 basis points, respectively, in the second half of 2016. Similarly, the cash reserve ratio (CRR) and liquidity ratio (LR) were also retained at 22.50 per cent and 30 per cent, respectively, during the second half of 2016.

Figure 2. 8: Money Market Interest Rates and MPR

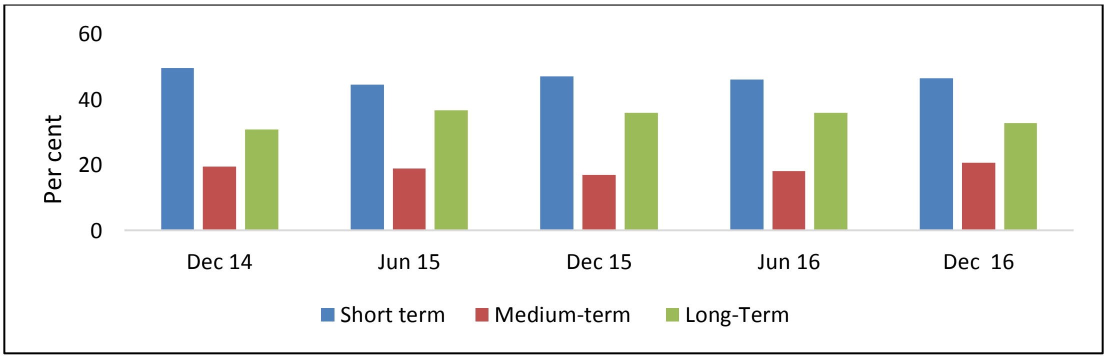


2.1.5 Maturity Structure of Bank Deposits and Credit

The total DMB's deposit which was ₦16,673.7 billion in June 2016 rose moderately by 0.75 per cent to ₦16,798.4 billion in December 2016. The structure of DMBs' credit in the second half of 2016 indicated that short-term maturities remained dominant in the market. Loans and advances maturing in one year and below accounted for 46.4 per cent of the total at end-

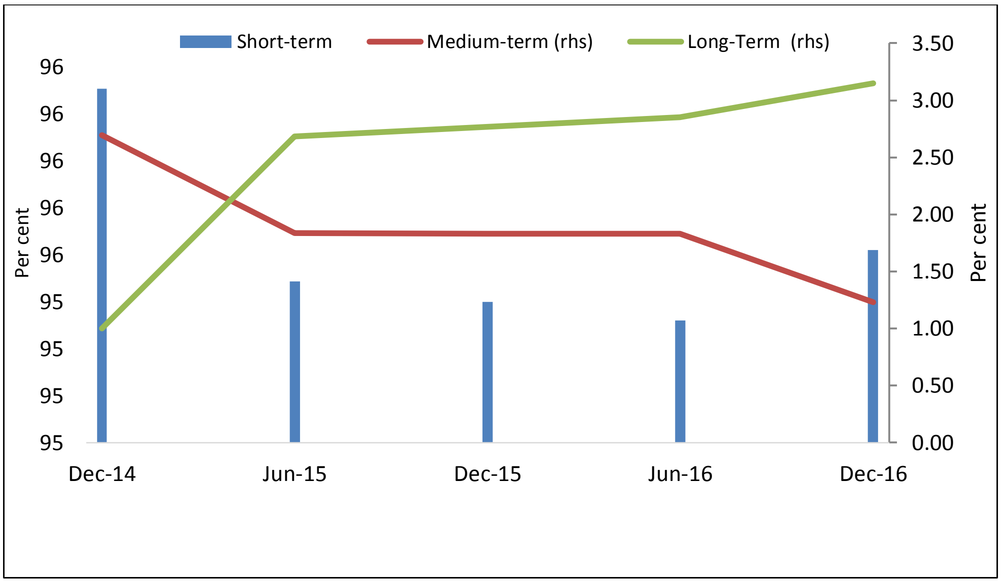
December 2016, compared with 46.0 per cent at end-June 2016. The medium-term[4] maturities rose by 2.6 percentage points to 20.7 per cent, from its level at end-June 2016, while the long-term[5] maturities rose to 32.9 per cent, compared with 35.9 per cent at end-June 2016 (Figure 2.9).

Figure 2. 9: Distribution of Bank Loans and Advances by Maturity



DMBs' deposit liabilities showed an increasing trend with short-term deposits of less than 1-year tenor constituting 95.6 per cent of the total, of which 75.9 per cent had a maturity of less than 30 days. Deposits of more than 1-year but less than 3-year tenor, constituted 1.2 per cent of total deposits, while deposits of more than 3-year tenor, constituted 3.2 per cent of total deposits at end-December 2016 compared with 2.9 and 2.8 per cent at end-June 2016 and the corresponding period of 2015, respectively (Figure 2.10).

Figure 2. 10: Maturity Structure of Bank Deposits



The maturity mismatch in the banking system remained a challenge to the growth of long-tenured assets, thereby limiting lending to the real sector. However, increasing fiscal

[4]Medium term implies maturities ≥1yr and < 3yrs.
[5] Long term implies maturities of 3yrs and above.

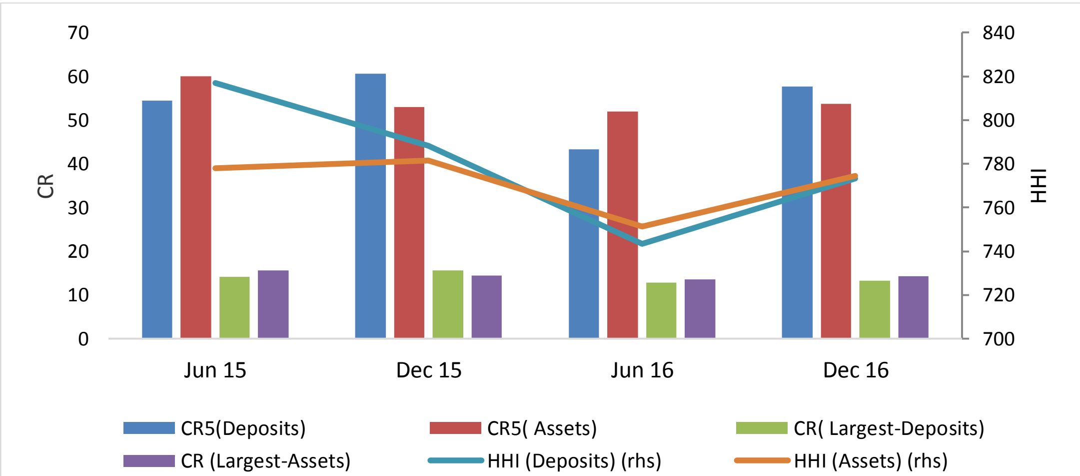
interventions complemented by enhanced developmental activities of the CBN will help in attracting long term funds for real sector development and growth.

2.1.6 Market Structure of the Banking Industry

In the second half of 2016, five banks dominated activities in the banking industry. The average concentration ratio of the five largest banks (CR_5) with respect to deposits and assets stood at 53.70 and 53.68 per cent, respectively, at end-December 2016, compared with 43.3 and 51.9 per cent at end-June 2016. The market shares of the largest bank with respect to deposits and assets stood at 13.20 and 14.23 per cent, respectively. Nineteen other banks had market shares ranging from 0.02 per cent to 6.19 per cent, in deposits, and 0.06 per cent to 6.23 per cent in assets.

The concentration ratio of the banking industry was supported by the Herfindahl-Hirschman Index (HHI)[6] for the industry at 773.21 and 774.50 for deposits and assets, at end-December 2016, compared with 764.13 and 757.00 at end-June 2016, respectively (Figure 2.11). This showed a weakening of the competitiveness of the industry compared to the first half of 2016.

Figure 2. 11: Concentration Ratios of the Banking Industry Assets and Deposits



2.2 New Institutions Licensed

The following category of banks and other financial institutions (OFIs) were granted the authorizations indicated against their classes during the period under review:

Table 2. 3: Institutions Licensed in the Second Half of 2016

S/N	Type of Institution	Number of Institutions Jan 1 – June 30, 2016	Number of Institutions July 1 – December 31, 2016	Total Number of Institutions as at December 31, 2016
1	Microfinance Bank	18	13	978
2	Bureau De Change	34 (New)	24(New)	3,147

[6]HHI is based on a scale of 100 to 10,000.

		113 (Old)	121(Old)	
3	Finance Company	1	4	70
4	Commercial Banks	1	-	22
5	Development Finance Institution (DFI)	-	-	6
6	Merchant Banks	-	-	4
7	Primary Mortgage Banks	-	-	34
8	Nigeria Mortgage Refinance Company	-	-	1

Other developments in the period under review included the licensing of 24 BDCs bringing the total to 3,147. Also a unit Non-Interest Microfinance Bank was licensed, while 11 unit MFBs merged into a State MFB bringing the total number of MFBs to 978. Four Finance Companies were also licensed. A categorization of the authorization of commercial banks at end-December 2016 showed 10 international, nine national and two regional licenses.

2.3 Other Financial Institutions

Total assets of the sub-sector decreased by 7.18 per cent to ₦1,812.93 billion at end-December 2016, from ₦1,953.20 billion at end-June 2016. Total net loans/advances also decreased by 17.36 per cent to ₦951.98 billion at end-December 2016, from ₦1,151.97 billion at end-June 2016. Similarly, the total paid-up capital decreased by 11.71 per cent to ₦413.06 billion at end-December 2016 from ₦467.85 billion at end-June 2016. Total deposits also decreased by 15.26 per cent to ₦535.57 billion at end-December 2016, from ₦632.02 billion at end-June 2016.

2.3.1 Development Finance Institutions

The total assets of the five (5) DFIs decreased by 2.63 per cent to ₦964.24 billion at end-December 2016, compared with ₦990.24 billion at end-June 2016. Of this amount, Bank of Industry (BOI), Federal Mortgage Bank of Nigeria (FMBN), Nigerian Export-Import Bank (NEXIM), Bank of Agriculture (BOA) and The Infrastructure Bank (TIB) accounted for 69.26, 20.24, 6.57, 3.15, and 0.78 per cent, respectively.

The net loans and advances decreased by 19.49 per cent to ₦571.85 billion at end-December 2016, from ₦710.27 billion at end-June 2016 due mainly to increased loan loss provisioning arising from higher rates of default. Of the net loans and advances of ₦571.85 billion, BOI accounted for 4.87 per cent, FMBN 19.85 per cent, NEXIM 4.62 per cent, BOA 0.16 per cent and TIB 0.50 per cent.

2.3.2 Microfinance Banks

The total assets of microfinance banks (MFBs) decreased to ₦341.68 billion at end-December 2016, from ₦455.96 billion at end-June 2016, reflecting a decrease of 25.06 per cent. The shareholders' funds also decreased by 42.91 per cent from ₦135.09 billion to ₦77.12 billion at end-December 2016. The decrease in shareholders' funds was largely attributed to losses by the microfinance banks resulting from increased provisioning for non-performing loans.

Total deposit liabilities and net loans/advances also decreased by 13.05 and 20.96 per cent to ₦166.29 billion and ₦183.96 billion at end-December 2016, compared with ₦191.25 billion and ₦232.73 billion at end-June 2016, respectively. Reserves also decreased by 24.39 per cent to ₦16.80 billion at end-December 2016, from ₦22.22 billion at end-June 2016. The decrease in reserves was as a result of operational losses.

2.3.2.1 Microfinance Certification Programme

The Microfinance Certification Programme (MCP) continued in the review period. The number of certified candidates (Level II) increased by 309 to 3,899 in the second half of 2016 from 3,590 at end-June 2016.

2.3.3 Primary Mortgage Banks

The number of licensed primary mortgage banks (PMBs) remained 34 at end-December 2016, comprising 10 National PMBs and 24 State PMBs. Total assets of PMBs increased marginally to ₦383.67 billion at end-December 2016 from ₦382.36 billion at end-June 2016, representing an increase of 0.34 per cent. Similarly, balances with banks and paid up capital increased by 78.86 per cent and 0.05 per cent to ₦24.79 billion and ₦103.35 billion respectively, at end-December 2016 from ₦13.86 billion and ₦103.29 billion at end-June 2016.

However, loans and advances, deposit liabilities and other liabilities decreased by 6.85 per cent, 5.25 per cent and 5.89 per cent to ₦154.46 billion, ₦115.77 billion and ₦68.06 billion, respectively, at end-December 2016 from ₦165.83 billion, ₦122.18 billion and ₦72.32 billion at end-June 2016.

Table 2. 4: Financial Highlights of PMBs as at December 31, 2016

	December 2016 (₦' billion)	**June 2016 (₦' billion)**	**% Change**
Total Assets	383.67	382.36	0.34
Loans and Advances	154.46	165.83	(6.85)
Balances with Banks	24.79	13.86	78.86
Deposit Liabilities	115.77	122.18	(5.25)
Other Liabilities	68.06	72.32	(5.89)
Paid up Capital	103.35	103.29	0.05

2.3.3.1 National Housing Finance Programme

The implementation of the National Housing Finance Programme achieved new milestones in the review period as reported below:

Nigeria Mortgage Refinance Company

At end-December 2016 the Nigeria Mortgage Refinance Company (NMRC) had refinanced mortgages amounting to ₦8 billion representing an increase of 200.75 per cent compared with ₦2.66 billion at end-June 2016. Having exhausted the first ₦8.0 billion bonds raised from the market, the company is in the process of raising additional ₦2.4 billion to refinance eligible mortgages of its member Participating Lending Institutions (PLIs).

In line with its condition for credit recourse, the NMRC exchanged refinanced non-performing mortgages of ₦172.46 million with 3 Primary Lending Institutions for performing mortgages of ₦208.96 million within the review period.

The NMRC successfully hosted the African Union Conference for Housing in Abuja in September 2016. The Conference created awareness on opportunities in the housing finance sector and proffered solutions to common challenges.

Housing Microfinance

Further to the expression of interest (EOI), and completion of the evaluation process, two firms were selected to work with the eight MFBs that had been prequalified to participate in the pilot Housing Microfinance (HMF) Scheme with a budget of USD15 million aimed at catering for the housing needs of low income earners.

2.3.4 Finance Companies

Following the return of operating licenses by five (5) FCs, the number of finance companies (FCs) stood at 70 inclusive of four (4) newly licensed institutions that were yet to commence operations.

Following the implementation of the new capital requirement of ₦100 million, paid-up capital increased to ₦19.19 billion at end-December 2016 from ₦15.35 billion at end-June 2016. Consequently, total assets of the subsector increased by 12.71 per cent to ₦123.34 billion at end-December 2016 compared with ₦109.43 billion at end-June 2016. Also, loans and advances, investments, and fixed assets increased by 4.51 per cent, 2.69 per cent and 21.15 per cent to ₦41.71 billion, ₦14.09 billion and ₦13.69 billion from ₦39.91 billion, ₦13.72 billion and ₦11.30 billion at end-December 2016 and at end-June 2016, respectively. Shareholders' funds also increased by ₦2.49 billion to ₦23.03 billion at end-December 2016, from ₦20.54 billion at end-June 2016. Similarly, borrowings increased by 9.98 per cent to ₦74.67 billion at end-December 2016, from ₦67.89 billion at end-June 2016. However, reserves decreased by 28.01 per cent to ₦3.83 billion at end-December 2016 from ₦5.32 billion at end-June 2016 due mainly to operational losses.

Table 2. 5: Key Finance Companies' Financial Highlights at end-December 2016

	December 2016 (₦' billion)	**June 2016 (₦' billion)**	**% Change**
Total Assets	123.34	109.43	12.71
Cash in Vault	0.50	1.19	(57.98)
Balances with Banks	3.52	3.33	5.7
Loans and Advances	41.71	39.91	4.51
Investments	14.09	13.72	2.69
Fixed Assets	13.69	11.30	21.15

Borrowings	74.67	67.89	9.98
Paid up capital	19.19	15.35	25.01
Reserves	3.83	5.32	(28.01)
Shareholders Fund	23.03	20.54	12.12

2.3.5 Bureaux de Change

The number of licensed BDCs stood at 3,147 at end-December 2016. During the period under review, the CBN directed Authorised Foreign Exchange Dealers to commence the sale of dollars to BDCs from the proceeds of international money transfers with effect from July 22, 2016.

2.4 Financial Markets

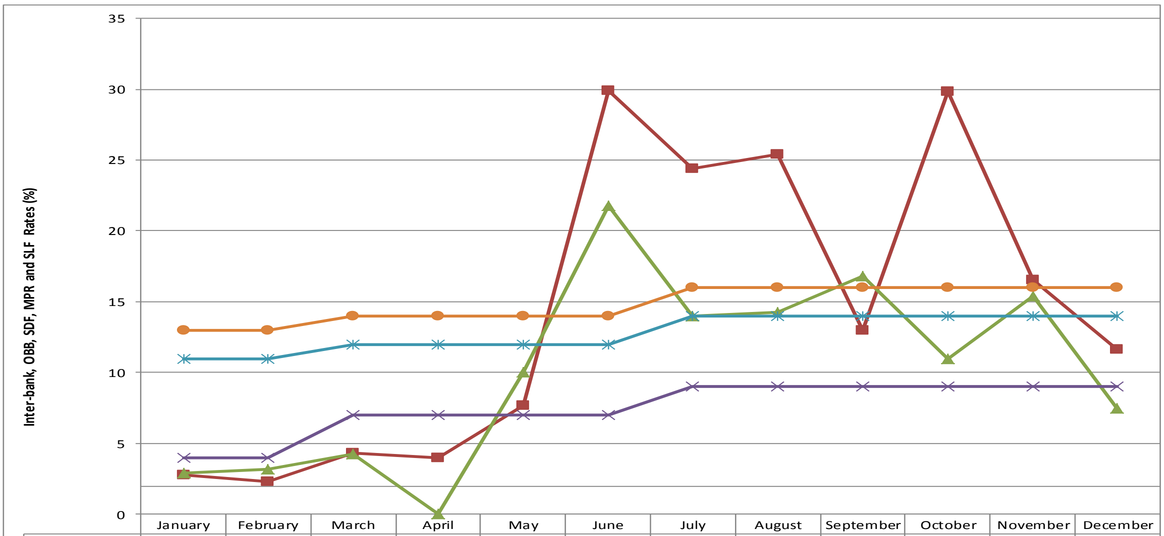
2.4.1 The Money Market

The CBN maintained its contractionary monetary policy stance in the second half of 2016 in order to stimulate capital inflow, reduce demand pressures in the foreign exchange market and tackle rising inflation. At the Monetary Policy Committee meeting held in July 2016, the Bank adjusted the Monetary Policy Rate (MPR) upward by 200bps to 14.00 per cent from 12.00 per cent but retained the asymmetric corridor around the MPR at +200/-500 basis points, while the Cash Reserve Requirement (CRR) on deposits was also retained at 22.50 per cent.

Activities in the money market in the second half of 2016 reflected largely the tight liquidity in the banking system occasioned by dwindling statutory revenue and extensive open market operations (OMO) auctions. The provisioning of funds for special foreign exchange interventions also exerted pressure on available liquidity and money markets rates moved in tandem with the level of banking system liquidity. Consequently, money market rates opened high and trended largely above the MPR for most of the review period. Overnight call rate opened on July 8, 2016 at 15.00 per cent, while open buy back (OBB) rate opened on July 20, 2016 at 14.00 per cent. Rates spiked at 160 per cent on October 18, 2016 for inter-bank call, and at 25.40 per cent on November 15, 2016 for OBB.

However, towards the end of 2016, there was respite in the market as inflows from maturing CBN bills and the refund of ₦349.59 billion to state governments from the Paris Club, buoyed liquidity and neutralised the effect of the various withdrawals through OMO. Consequently, monthly weighted average OBB and inter-bank call rates closed lower at 7.45 and 11.62 per cent in December 2016, compared with 21.75 and 29.91 per cent recorded in June 2016, respectively. The monthly average OBB rate ranged from 7.45 to 16.79 per cent, while the inter-bank call rate ranged from 11.62 to 29.81 per cent.

Figure 2. 12: Money Market Rates Movements, January – December 2016



	January	February	March	April	May	June	July	August	September	October	November	December
Inter-bank	2.75	2.33	4.32	4.00	7.68	29.91	24.38	25.40	13.00	29.81	16.55	11.62
OBB	2.90	3.18	4.25	0.00	10.00	21.75	14.00	14.25	16.79	11.00	15.41	7.45
SDF	4.00	4.00	7.00	7.00	7.00	7.00	9.00	9.00	9.00	9.00	9.00	9.00
MPR	11.00	11.00	12.00	12.00	12.00	12.00	14.00	14.00	14.00	14.00	14.00	14.00
SLF	13.00	13.00	14.00	14.00	14.00	14.00	16.00	16.00	16.00	16.00	16.00	16.00

2.4.1.1 Nigerian Treasury Bills

Nigerian Treasury Bills (NTBs) of 91-, 182- and 364-day tenors totalling ₦2,098.23 billion were issued and allotted during the second half of 2016. This represented a decrease of 14.61 per cent, when compared with ₦2,457.28 billion recorded as at end-June 2016. Similarly, total subscription was lower at ₦3,620.30 billion, depicting a decrease of 28.41 per cent, when compared with ₦5,057.30 billion recorded in the first half of 2016. The decrease in NTBs issued, allotted and subscribed was attributed to the tight liquidity in the banking system precipitated by the sustained mop-up by the CBN, provisioning of funds by banks for the special foreign exchange interventions for Forwards transactions at the foreign exchange market.

The holding structure of investments in NTBs in the review period indicated that banks took-up ₦887.14 billion, representing 42.28 per cent of the total NTBs issued, as against ₦1,745.90 billion, representing 71.05 per cent of NTBs issued in the preceding period. Mandate and internal customers, and CBN take-up accounted for ₦1,075.50 billion and ₦135.59 billion, respectively compared with ₦683.38 billion, and ₦28.00 billion in the first half of 2016. The reduced up-take by banks was attributed to tight liquidity in the banking system and higher yield in CBN bills, leading to the significant increase in mandate and internal customers' participation as well as increase in CBN take-up.

The total stock of NTBs outstanding as at end-December 2016 showed that banks accounted for 38.61 per cent; the non-bank, and mandate and internal customers accounted for 61.33 per cent, while CBN held the balance of 0.06 per cent. The range of average marginal rates for the period were 9.9800 - 15.4400 per cent for the 91-day; 12.2400 - 18.0589 per cent for the 182-day; and 14.9900 - 18.7000 per cent for the 364-day tenors.

2.4.2 The Foreign Exchange Market

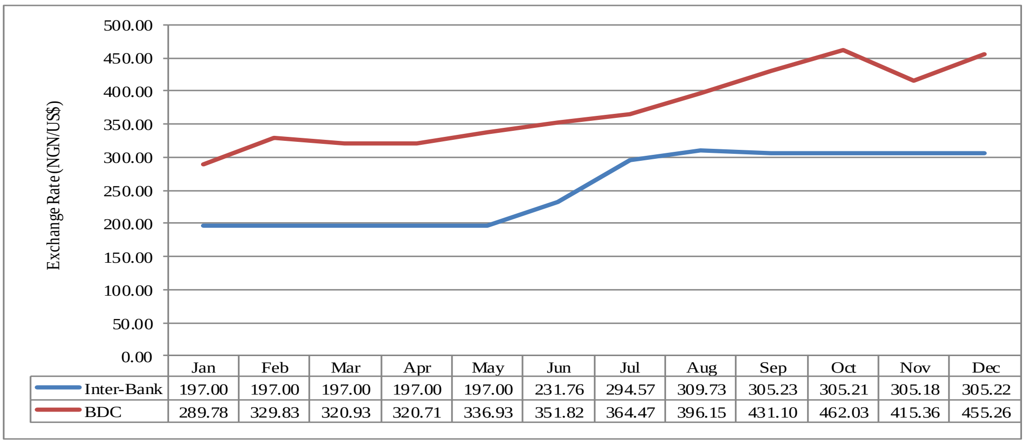
The Bank's effort at maintaining a stable exchange rate was sustained with the full implementation of the flexible foreign exchange rate regime. However, low accretion to the foreign reserves due to low oil price, declining oil production attributable to the restiveness in the Niger Delta region, foreign portfolio investment reversals and high import bills, continued to exert pressures on the exchange rate. Consequently, the naira depreciated at both the inter-bank and BDC segments. The Bank, however, continued to intervene directly in the inter-bank market in an attempt to stabilise the exchange rate.

2.4.2.1 Foreign Exchange Market Rates

The exchange rate of the naira at the inter-bank segment, opened at ₦282.25/US$ on July 1, 2016 and closed at ₦305.00/US$ on December 30, 2016. Similarly, at the BDC segment of the foreign exchange market, the selling rate opened and closed at ₦348.00/US$ and ₦490.00/US$, respectively. This represented depreciation of 7.46 per cent at the inter-bank and 28.98 per cent at the BDC segments of the market.

On monthly average basis, the exchange rates at the interbank and BDC segments depreciated by 24.07 and 22.72 per cent from ₦231.76/US$ and ₦351.82/US$ in June 2016, to close at ₦305.22/US$ and ₦455.26/US$ in December 2016, respectively (Figure 2.7). The depreciation of the naira at the interbank and the BDC segments was due to the scarcity of foreign exchange and sustained demand pressures.

Figure 2. 13: Inter-bank and BDC Rates, January - December 2016



	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Inter-Bank	197.00	197.00	197.00	197.00	197.00	231.76	294.57	309.73	305.23	305.21	305.18	305.22
BDC	289.78	329.83	320.93	320.71	336.93	351.82	364.47	396.15	431.10	462.03	415.36	455.26

2.4.2.2 Foreign Exchange Spot, Forwards and OTC FX Futures Transactions

In the review period, total CBN foreign exchange sales was $2,940.05 million. Of this, inter-bank spot sales amounted to $575.50 million, while forwards through special market intervention sales (SMIS) was $2,364.55 million. The SMIS were directed to critical purposes including raw materials and machinery, petroleum products, airlines, and agriculture.

OTC FX Futures contracts amounted to $5,184.10 million (notional value). The sum of $1,528.94 million matured, while $3,655.16 million remained open as at December 30, 2016.

2.4.2.3 Potential Risks/Challenges in the Foreign Exchange Markets

The implementation of the flexible exchange rate regime faced some challenges including:

- Market illiquidity arising from low inflow from autonomous sources;
- Perceived devaluation risk from market participants;
- Persistent foreign exchange demand pressures;
- Arbitrage opportunities following the widening spread between the interbank and BDC rates; and
- Uncertainty in the macroeconomic environment.

2.4.3 The Capital Market

Activities in the Nigerian Stock Exchange (NSE) remained depressed during the review period as the All Share Index (ASI) and Market Capitalisation (MC) decreased compared with the preceding period. This was due to the bearish trend in the stock market, arising from uncertainties in the macroeconomic environment, poor corporate performance due to tougher operating environment, depressed household demand and rising costs which impacted on stock performance. In addition, the increasing yield in the fixed income market also distracted investors from the stock market and contributed towards driving prices down.

During the second half of 2016, eleven (11) new issues comprising two (2) State Government bonds, three (3) FGN Bonds, two (2) corporate bonds, two (2) corporate equities and two (2) exchange traded funds (ETF), were listed, while nine (9) companies were delisted from the exchange for either ceasing to exist or non-compliance with post-listing requirements. Four (4) supplementary listings were also recorded on account of additional public offers and special placements.

2.4.3.1 The Bond Market

Total bonds outstanding at end-December 2016 stood at ₦7,552.32 billion, of which FGN, agency, sub-national and corporate bonds amounted to ₦6,663.36 billion (88.23%), ₦0.30 billion (0.004%), ₦417.72 billion (5.53%) and ₦470.94 billion (6.24%), respectively. The total bonds outstanding at end-December 2016 reflected a 9.28 per cent increase over the ₦7,542.17 billion end-June 2016 figure, comprising FGN, agency, sub-national and corporate bonds valued at ₦6,571.96 billion (87.14%), ₦0.90 billion (0.01%), ₦433.24 billion (5.74%) and ₦536.07 billion (7.11%), respectively.

Table 2. 6: Outstanding Bonds

	June 2016 (N 'billion)	December 2016 (N 'billion)	% Change	Proportion of Total
FGN	6,571.96	6,663.36	1.39	88.229
Agency	0.90	0.30	-66.67	0.004
Sub-National	433.24	417.72	-3.58	5.531
Corporate	536.07	470.94	-12.15	6.236
Total	7,542.17	7,552.32	0.13	100.00

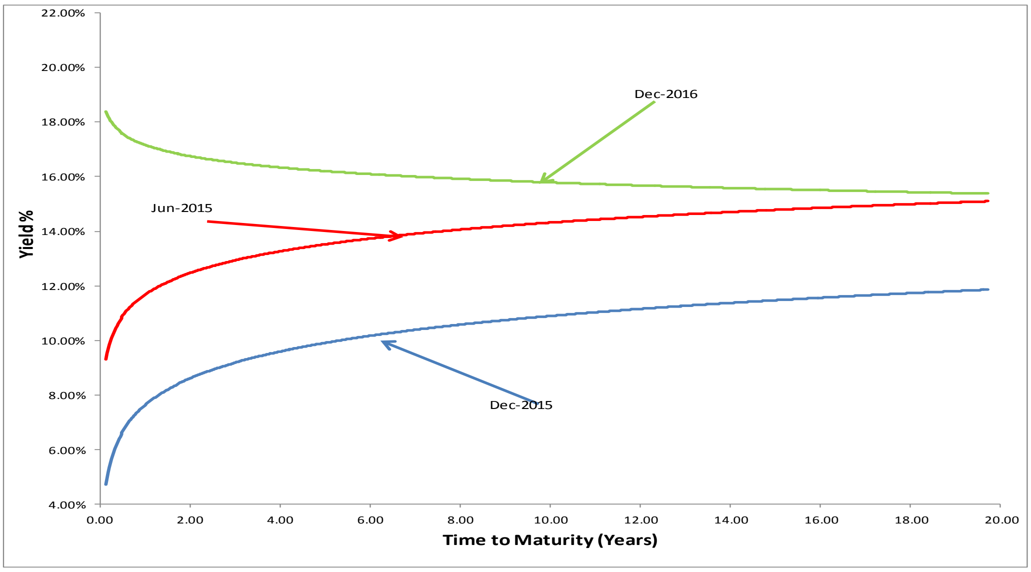
Source: *FMDQ OTC PlC*

FGN Bonds

In the review period, FGN Bonds offered for sale (new issues and re-openings) was ₦645.00 billion, representing an increase of 9.32 per cent above the ₦590.00 billion offered in the first half of 2016. Public subscription and sales decreased to ₦941.90 billion and ₦499.20 billion, at end-December 2016, from ₦1,183.83 billion and ₦529.50 billion, at end-June 2016, respectively. The decrease in subscription and sales were attributed to the liquidity constraints in the banking system which led to reduced patronage of FGN bonds by banks despite the strong appeal of fixed income assets and the impressive yield on FGN bonds.

The price of FGN Bonds at the secondary market declined as a result of reduced transactions and demand, as well as increased banking system liquidity constraints and other macroeconomic uncertainties. Consequently, yields on FGN Bonds at end-December 2016 increased considerably at both the long and short ends of the curve when compared with FGN bond yields in the preceding period (Figure 2.8). The upward review of the MPR by 200 basis points in the second half of 2016, and the sustained open market operations activities by the Bank which further reduced market liquidity, contributed to increased yield on FGN bonds in the secondary market.

Figure 2. 14: Yield Curves for Nigeria



Source: *FMDQ-OTC Plc.*

Agency Bonds

During the review period, no agency bond was issued. Federal Mortgage Bank of Nigeria (FMBN) bonds valued ₦0.60 billion were redeemed, the same as the amount redeemed in the first half of 2016. Consequently, total outstanding Agency Bonds as at end-December 2016, stood at ₦0.30 billion.

Sub-National Bonds

There was no new issue of sub-national bonds in the second half of 2016, the same as in the preceding period. A total amount of ₦15.52 billion was amortised by eleven (11) states as against ₦19.87 billion amortised by twenty (20) states in the first half of 2016. The total outstanding bonds held by sixteen (16) state governments stood at ₦47.72 billion.

Corporate Bonds

Three (3) corporate bonds valued ₦67.97 billion were issued by two companies in the review period compared with two (2) bonds worth ₦30.63 billion issued by two (2) companies in the preceding period. Bonds valued ₦2.66 billion were amortised by eight (8) companies, while bonds worth ₦132.75 billion were redeemed by three (3) companies. The outstanding corporate bonds which were held by fourteen (14) companies at end-December 2016, stood at ₦470.94 billion.

Table 2. 7: Corporate Bonds issued in the second half of 2016

Company	**Description**	**Value (N' Billion)**
Lafarge Africa Plc	14.25 Lafarge 15-June-2019	26.39
Lafarge Africa Plc	14.75 Lafarge	33.61
Sterling Inv. Mgt. Plc	16.50 Sterling Inv. 3-Aug-2023	7.97
Total		67.97
Source: *FMDQ OTC PLC*		

2.4.3.2 The Equities Market

At end-December 2016, the NSE ASI closed at 26,874.62, reflecting a decrease of 9.20 per cent below the 29,597.79 recorded at end-June 2016. Market capitalization also closed lower at ₦9,246.92 billion, reflecting a decrease of 9.03 per cent below the ₦10,165.34 billion recorded at the end of the preceding period. The breakdown of trading by foreign portfolio investors (FPI) showed that inflows were valued at ₦135.23 billion, while divestments (outflows) stood at ₦113.11 billion, reflecting a net inflow of ₦22.12 billion at end-December 2016, in contrast to a net outflow of ₦26.63 billion recorded at end-June 2016. Total FPI transactions (inflow and outflow) accounted for 47.12 per cent of total equity transaction in the period, compared with 43.12 per cent recorded at end-June 2016.

The decrease in the market indicators (NSE ASI and Market capitalization) was attributable to general contraction in economic activities, reduced corporate activities and increased investors' skepticism, coupled with other macroeconomic uncertainties. However the increase in net FPI inflows was attributable to greater exchange rate liberalisation in the second half of 2016.

Table 2. 8: Domestic and Foreign Portfolio Participation in Equity Trading in the second Half of 2016

Period	**Total Volume (N' Billion)**	**Foreign (N' Billion)**	**% Foreign**	**Domestic (N' Billion)**	**% Domestic**	**Foreign Inflow (N' Billion)**	**Foreign Outflow (N' Billion**	**NSE ASI**	**Market Capitalization (N' Billion)**
Nov-16	431.09	204.32	47.4	226.77	52.6	115.74	88.58	26,874.62	9,246.92
Jun-16	624.41	269.22	43.12	355.19	56.88	121.29	147.92	29,597.79	10,165.34
Period % Change	-30.9604	-24.10668		-36.1553		-4.57581	-40.11628	-9.2	-9.03

2.5 Financial Inclusion

Towards achieving the goals of the National Financial Inclusion Strategy (NFIS), the following activities were undertaken in the review period.

2.5.1 Access to Financial Services Survey 2016

The report of the 2016 Access to Financial Services (A2F) Survey, which was conducted to provide data on the status of the 80 per cent inclusion target by 2020 as enunciated in the NFIS, was being compiled for publication.

2.5.2 NFIS Governing Committee Meetings

During the review period, the NFIS Governing Committee met and took the following decisions:

- Approved the 2015 annual report of the National Financial Inclusion Strategy for publication;
- Directed NAIC to implement the capacity building plan for agricultural insurance as from 2017;
- Requested NIPOST to devise ways that will ensure that the approved stamp duty would not hinder financial inclusion goals;
- Charged the Securities and Exchange Commission (SEC) to expedite action on finalizing the Capital Market Financial Inclusion Strategy as well as to finalize the draft guidelines on the expansion of distribution channels for capital market products;
- Directed the CBN and the National Insurance Commission (NAICOM) to jointly review and harmonize the Bancassurance Guidelines; and
- Set up a Committee to review the NFIS.

2.6 Real Sector Intervention Programmes

2.6.1 Risk Mitigation and Insurance Schemes

2.6.1.1 The Agricultural Credit Guarantee Scheme Fund

A total of 34,774 loans valued at ₦4.47 billion were guaranteed in the second half of 2016 for three commercial and 37 microfinance banks as against 23,774 loans valued at ₦3.63 billion for three commercial and 72 microfinance banks in the first half of 2016. This trend indicated an increase of 46.27 and 23.14 per cent in the number and value of loans guaranteed, respectively. The sum of ₦5.55 billion involving 34,083 projects was repaid during the same period compared with ₦4.03 billion for 29,519 projects in the corresponding period of 2016. This performance reflected an increase of 37.72 and 15.46 per cent in the value and number of loans guaranteed, respectively. Cumulatively, 1.060 million loans valued at ₦104.01billion had been guaranteed from inception to December, 2016.

2.6.1.2 National Collateral Registry

The National Collateral Registry (NCR) carried out the following activities during the review period:

i. Registry Operations

A total of 72 Financial Institutions registered on the NCR comprising 21 Deposit Money Banks, three Development Finance Institutions, three Merchant Banks, one Non-interest Bank and 44 Microfinance Banks.

ii. Registration of Financing Statements

During the review period, 1,462 financing statements detailing priority interest in movable assets valued at ₦24.136 billion, were registered by five financial institutions.

2.6.2 Credit Support Schemes

2.6.2.1 The Commercial Agriculture Credit Scheme

During the period under review, the sum of ₦40.97 billion was disbursed to 14 banks for 31 projects compared with ₦35.99 billion disbursed to 13 banks for 39 projects at end-June 2016. This outcome reflected an increase of ₦4.98 billion (13.83%) and a decrease of eight projects (20.51%). The total repayments during the second half of 2016 stood at ₦26.28 billion by 18 banks for 214 projects, bringing the cumulative repayments to ₦225.01 billion at end-December 2016.

The cumulative amount disbursed under the scheme from inception to end-December 2016 stood at ₦407.63 billion to 487 projects, 80 of which were state government projects.

2.6.2.2 SME Restructuring and Refinancing Facility

The repayment proceeds under the Facility in the review period stood at ₦6.57 billion. The cumulative disbursements to the participating banks at end-December 2016 remained the same at ₦381.99 billion for 604 projects, while the total repayment from BOI from inception to December 2016 was ₦159.53 billion.

2.6.2.3 Real Sector Support Facility

During the period under review, the sum of ₦2.25 billion was released to two (2) projects under the Real Sector Support Facility (RSSF), bringing the number of projects to four (4) valued at ₦6.85 billion from inception in 2014.

2.6.2.4 Textile Sector Intervention Fund

The CBN earmarked the sum of ₦50 billion for restructuring of existing loans and provision of new facilities under the Textiles Industry Intervention Fund. The sum of ₦7.36 billion was disbursed to eight participating banks for nine projects in the review period. Total amount disbursed from inception on October 6, 2015 to end-December 2016 was ₦14.92 billion to 14 participating banks for 20 projects.

2.6.2.5 Micro, Small and Medium Enterprises Development Fund

During the review period, activities carried out by the CBN under the Micro, Small and Medium Enterprises Development Fund (MSMEDF) included:

- **MSMEDF Disbursements to SME and Micro Credit**

During the review period, the sum of ₦16.74 billion was disbursed as against ₦30.24 billion disbursed in the first half of 2016. The cumulative disbursement from inception to date stood at ₦97.84 billion. Specifically, 97,519 female and 63,302 male micro-enterprise owners as well as 408 SMEs benefited from the Fund since inception.

- **Anchor Borrowers' Programme (ABP)**

The Bank approved the funding of Anchor Borrowers' Programme (ABP) from the ₦220 billion MSMEDF at a single-digit interest rate of 9 per cent. From July to December, 2016, the sum of ₦12.09 billion had been disbursed to 49,658 farmers in Adamawa, Anambra, Benue, Cross River, Enugu, Edo, Kwara, Kaduna, Kogi, Oyo, Kano, Nasarawa, Taraba, Sokoto, Niger, and Zamfara States. This figure represents 49.48 per cent of the total net disbursement from inception to end-December 2016.

2.6.2.6 Power and Aviation Intervention Fund

During the review period, the sum of ₦11.41 billion was disbursed to three (3) power projects. Cumulative disbursement from inception stood at ₦272.61 billion for 59 projects, comprising 43 power and 16 airline projects at end-December 2016. The sum of ₦17.57 billion was repaid by 27 obligors during the review period. The total repayment (cumulative) stood at ₦93.12 billion at end-December 2016.

Table 2. 9: PAIF Performance as at December 31, 2016

S/N	Type	No. of Obligors	No. of projects	Amount (₦' Billion)	%	Repayments (₦' Billion)
1	Airline	10	16	120.76	46.2	50.54
2	Power	29	43	151.85	53.8	42.58
	Total	**39**	**59**	**272.61**	**100.0**	**93.12**

A total of 1,758 MW of electricity generation and the construction of 120-kilometre natural gas pipeline were financed under the scheme at end-December 2016.

2.6.2.7 Nigeria Electricity Market Stabilization Facility

During the review period, the sum of ₦8.11 billion was released to 6 Generating Companies (Gencos). Total disbursement of funds from inception stood at ₦114.74 billion to 29 eligible electricity market participants. The sum of ₦4.11 billion was repaid by 8 Distribution Companies (Discos) bringing the cumulative total repayments to ₦6.26 billion.

Table 2. 10: NEMSF Disbursements at end-December 2016

S/N	Market Participants	Disbursements (January – June 2016)	Disbursements (July – December, 2016)		Cumulative as at December 31, 2016	
		Value (N' Billion)	No.	Value (N' Billion)	No.	Value (N' Billion)
1	Discos	49.62	-	-	7	49.62
2	Gencos	32.67	6	8.11	15	49.06
3	Gascos	23.89	-	-	6	15.60
4	Service Providers	0.46	-	-	1	0.46
	Total	**106.64**	**6**	**8.11**	29	**114.74**

Table 2. 11: NESMF Repayments as at December 31, 2016

Name of Obligor under NEMSF	Repayment Obligation (₦' Billion)	Repayment to Date (₦' Billion)	Amount Outstanding (₦' Billion)
Benin Disco	17.31	0.70	16.61
Eko Disco	5.85	0.39	5.47
Enugu Disco	26.64	1.56	25.08
Ibadan Disco	21.32	1.29	20.02
Ikeja Disco	5.99	0.24	5.75
Jos Disco	11.69	0.49	11.20
Kano Disco	9.67	0.62	9.05
Port Harcourt Disco	16.27	0.96	15.31
Total	114.75	6.26	108.49

Note: *Only Discos are required to make repayments for the legacy debts settled under NEMSF*

The Bank’s intervention has facilitated the following:

- Recovery of 1,193MW of generating capacity through the overhaul of 10 turbines;
- Acquisition of 414,000 meters and 70,310 number of 500KVA transformers by the Discos;
- Rehabilitation of 332km of 11KV lines and 130km of 0.45KV lines;
- Procurement and construction of 34 new distribution substations; and
- Acquisition of one (1) mobile injection sub-station.

In addition, capacity recovery programmes were carried out in three hydro power stations while 10 gas turbines at major thermal power plants including Geregu, Transcorp Ughelli, and Ibom Power Plants were rehabilitated.

2.6.2.8 Entrepreneurship Development Centres

The number of participants trained by the Entrepreneurship Development Centres (EDCs) during the review period was 7,553, surpassing the target of 6,600. A total of 3,196 (42.31%) of the participants were female and 4,357 (57.69%) were male. Cumulatively, the sum of ₦2.31 billion has been accessed through banks and other financial institutions by the graduates since inception, while a total of 66,854 participants have been trained.

2.6.2.9 Youth Entrepreneurship Development Programme

The second stream of the training of young entrepreneurs under the YEDP was flagged off on 20th October, 2016. Heritage Bank Ltd forwarded 548 business plans for funding, out of which, the Bank approved 310 amounting to ₦776,773,885.87. As at December 30, 2016, the sum of ₦179,717,629.82 has been disbursed to 67 successful applicants.

2.6.2.10 CBN Non-Oil Export Stimulation Fund and Rediscounting & Refinancing Facility

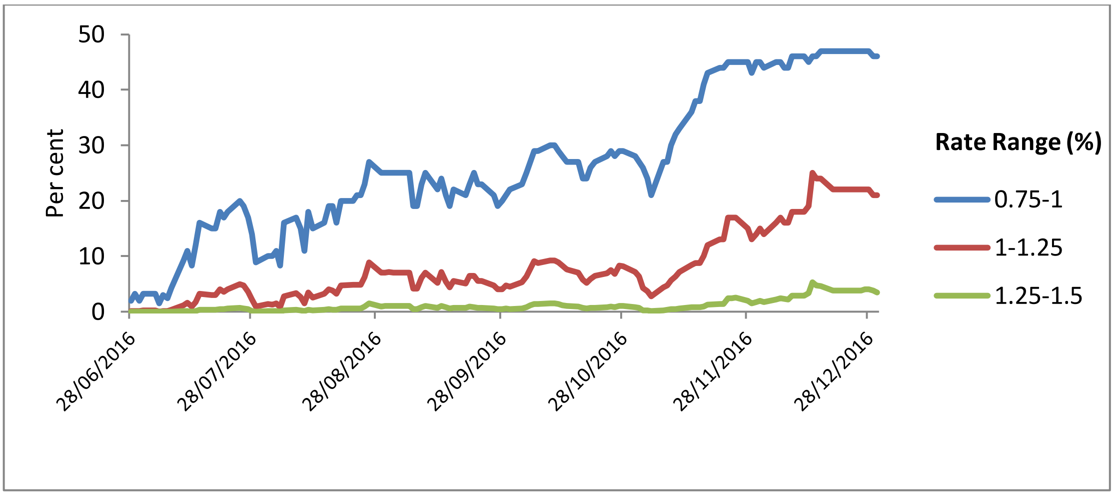
During the review period, 13 applications were received under the Export Stimulation Fund (ESF) valued at ₦25.48 billion while two (2) applications valued at ₦3.59 billion were received for Rediscounting and Refinancing Facility (RRF).

2.7 External Reserve Management

External reserves decreased by $235.96 million to $26.99 billion at end-December 2016 from $27.22 billion at end-June 2016, comprising $2.67 billion for the Federation, $8.84 billion for the Federal Government and $15.53 billion for the CBN. A breakdown of the reserves indicated that 84.35 per cent was held in US Dollars, 7.45 per cent in IMF SDRs, 6.87 per cent in Renminbi and 1.33 per cent in other currencies.

Key issues that dominated external reserve management in the review period were the expectations and eventual rate hike by the Federal Reserve in December 2016. This led to decline in the value of US dollar-denominated assets and strengthening of the US dollar against other currencies. There are still strong expectations of further increase in the Federal Reserve rate in the near term.

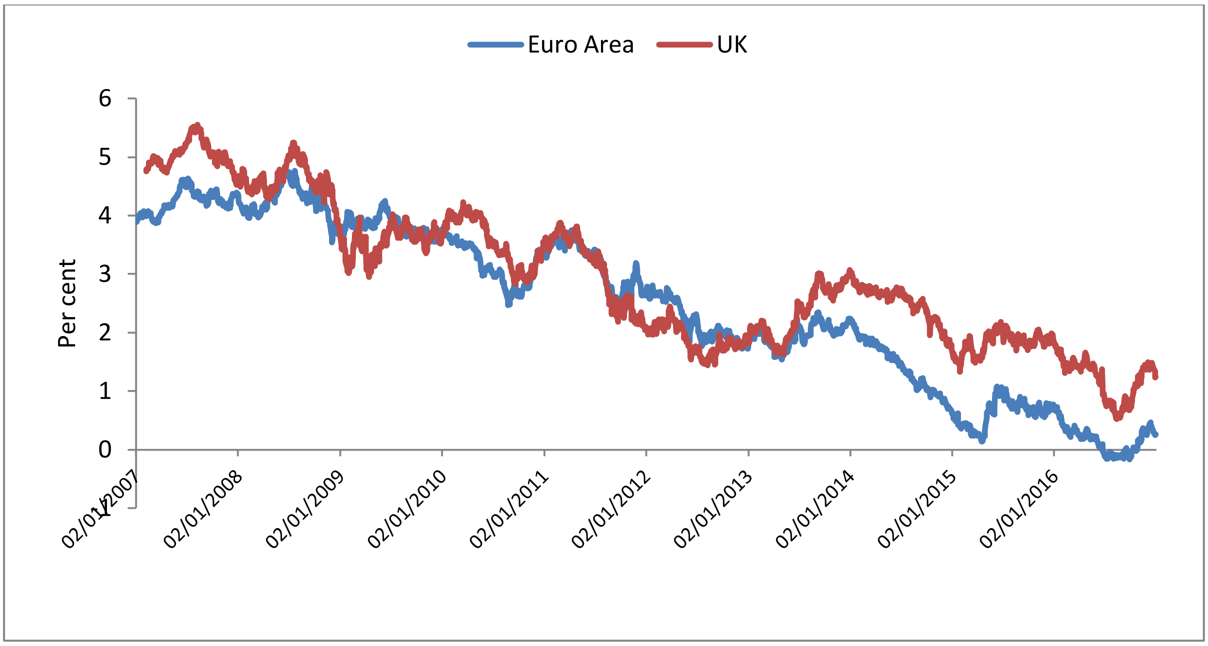
Figure 2. 15: Probability of Federal Reserve Hike in June 2017



Source: *Bloomberg*

The policies of the Bank of England (BOE) and European Central Bank (ECB) were expansionary. During the review period, the BOE policies which included reduction in the Bank Rate to 0.25 per cent, introduction of Corporate Bond Purchases and Term Funding Schemes decreased yields on GBP-denominated assets. Similarly, the ECB Targeted Long Term Refinancing Operations (TLTRO) scheme in the same period contributed to the decrease in sovereign yields.

Figure 2. 16: Yield on 10-year Government Bonds



Source: *Bloomberg*

3.0 REGULATORY AND SUPERVISORY ACTIVITIES

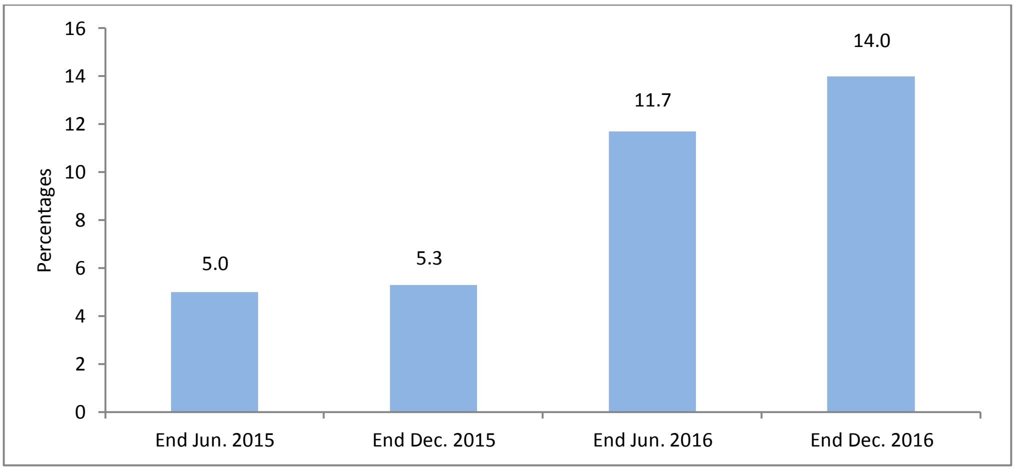
3.1 Financial Soundness Indicators

The financial soundness indicators used to appraise and monitor the stability of the financial system included assets, capital, and income/expense-based indicators.

3.1.1 Assets-Based Indicators

Commercial banks in Nigeria experienced deterioration in assets quality at end-December 2016. The ratio of non-performing loans (NPLs) to gross loans deteriorated in the second half of 2016 by 2.3 and 8.7 percentage points to 14.0 per cent at end-December 2016 compared with the levels at end-June 2016 and end-December 2015, respectively. The deterioration in asset quality was largely attributed to the rising inflationary trend, negative GDP growth, and the depreciation of the naira.

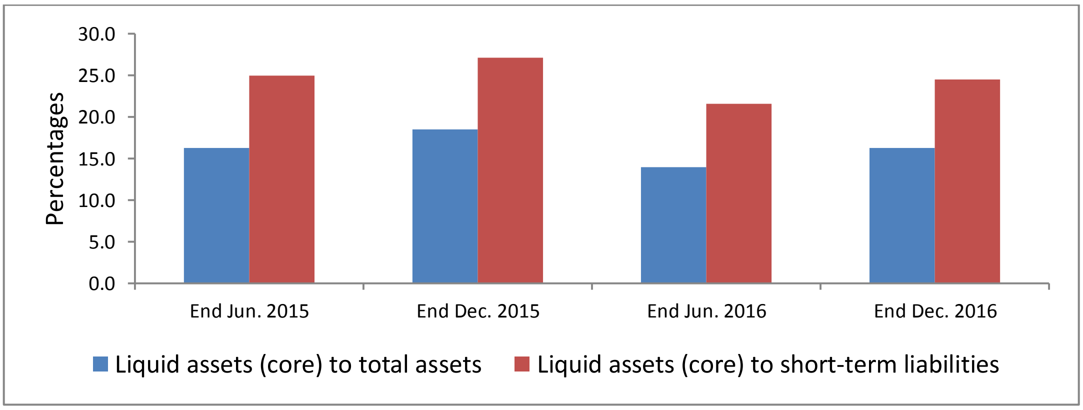
Figure 3. 1: Banking Industry NPLs to Gross Loans at end-December 2016



3.1.1.1 Core Liquid Assets to Total Assets

The ratio of core liquid assets to total assets increased by 2.3 percentage points to 16.3 per cent at end-December 2016 from 14.0 per cent recorded at end-June 2016. Also, the ratio of core liquid assets to short-term liabilities increased by 2.9 percentage points to 24.5 per cent at end-December 2016, compared with 21.6 per cent at end-June 2016. The increase in the ratio of core liquid assets to both total assets and short-term liabilities reflects improved buffers to absorb short term obligations.

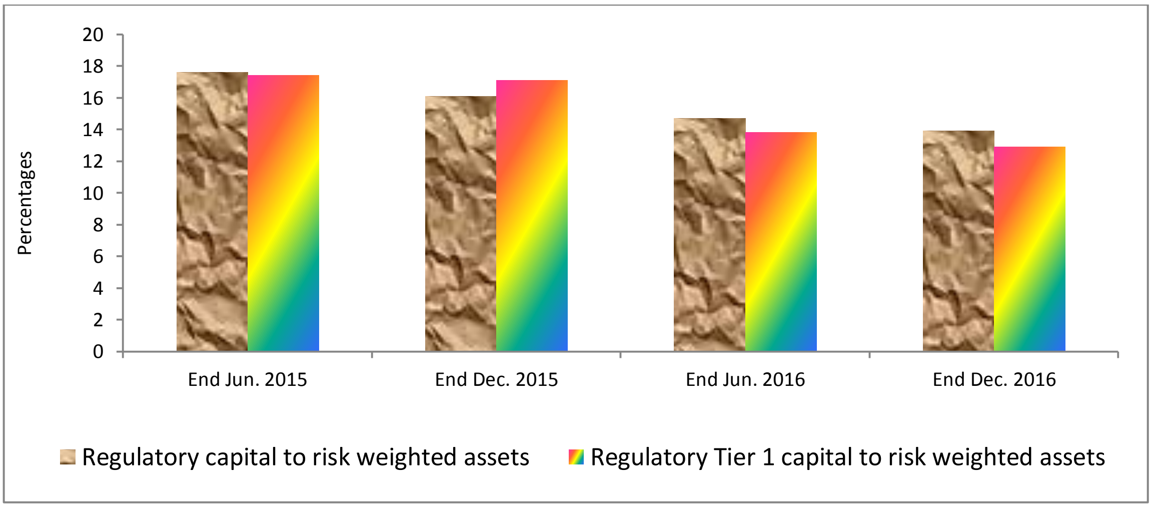
Figure 3. 2: Banking Industry Liquidity Indicators at end-December 2016



3.1.2 Capital-Based Indicators

The ratio of regulatory capital to risk weighted assets decreased by 0.8 percentage point to 13.9 per cent at end-December 2016, compared to 14.7 per cent at end-June 2016. Similarly, the ratio of Tier 1 capital to risk weighted assets declined by 0.9 percentage point to 12.9 per cent at end-December 2016 from 13.8 per cent at end-June 2016. Despite the marginal decrease, the ratios remained above the Basel minimum threshold.

Figure 3. 3: Banking Industry Capital Adequacy Indicators



The ratio of non-performing loans net of provision to capital for the industry increased to 38.4 per cent at end-December 2016 from 28.4 per cent at end-June 2016.

3.1.3 Income and Expense Based Indicators

The return on assets (ROA) declined by 1.0 percentage point to 1.3 per cent at end-December 2016 from 2.3 per cent recorded at end-June 2016, while the ratio of non-interest expenses to gross income increased to 63.8 per cent at end-December 2016 from 54.6 per cent recorded in the preceding half. The ratio of interest margin to gross income deteriorated to 50.0 per cent during the review period from 61.4 per cent at end-June 2016, while the ratio of personnel expenses to non-interest expenses declined to 30.5 per cent at end-December 2016 from 41.2 per cent recorded at end-June 2016.

Table 3. 1: Selected Financial Soundness Indicators of the Nigerian Banking Industry

Indicators	2012		2013		2014		2015**		2016***	
	End-Jun	End-Dec	End-Jun	End-Dec	End-Jun	End-Dec	End-Jun	End-Dec	End-Jun	End-Dec
1. Asset-Based Indicators										
Non-performing loans to gross loans*	4.5	3.7	3.9	3.4	3.5	2.9	5.0	5.3	11.7	14.0
Liquid assets (core) to total assets*	14.3	16.2	13.7	16.8	11.7	11.4	16.3	18.5	14.0	16.3
Liquid assets (core) to short term liabilities	19.4	22.1	19.0	23.1	16.6	16.7	25.0	27.1	21.6	24.5
2. Capital-Based Indicators										
Regulatory capital to risk-weighted assets*	17.7	18.3	18.9	17.1	16.4	17.2	17.6	16.1	14.7	13.9
Regulatory Tier 1 Capital to risk-weighted assets*	17.8	18.0	18.5	17.1	16.4	15.5	17.4	17.1	13.8	12.9
Non-performing loans net of provisions to capital*	4.3	3.8	5.9	5.8	5.6	4.1	7.4	5.9	28.4	38.4
3.Income and Expense Based Indicators										
Return on assets*	2.9	2.4	2.9	2.3	2.5	2.5	2.8	2.5	2.3	1.3
Interest margin to gross income*	67.7	62.0	65.2	63.9	62.7	51.2	53.9	63.8	61.4	50.0
Noninterest expenses to gross	59.2	64.8	62.7	68.1	65.5	56.9	69.0	64.2	54.6	63.8
Personnel expenses to noninterest expenses	39.3	42.5	39.5	36.9	38.5	36.6	31.4	36.0	41.2	30.5

Note: **FSIs are computed based on IMF guidelines.*

***The indicators for the period End June 2012 to End December 2015 are revised*

**** Provisional*

3.2 The Banking Industry Stress Test

The banking industry stress test was carried out at end-December 2016, covering 23 commercial and merchant banks, to evaluate the resilience of the banks to credit, liquidity, interest rate and contagion risks. The banking industry is categorised into large (assets ≥₦1 trillion), medium (assets >₦500 billion but<₦1 trillion) and small banks (assets ≤₦500 billion).

Baseline Position

The baseline CAR for the banking industry, large, medium, and small banks stood at 14.78, 15.47, 12.75 and 3.14 per cent, respectively. These represented a 0.04, -0.18, 0.76 and -0.02

percentage points change from June 2016 for the banking industry, large, medium and small banks, respectively.

Table 3. 2: Baseline Position

Baseline CAR	All Banks	Large Banks	Medium Banks	Small Banks
December 2016	14.78	15.47	12.75	3.14
June 2016	14.74	15.65	11.99	3.16
% Change	0.04	-0.18	0.76	-0.02

Figure 3. 4: Baseline (Pre-Shock) CAR (%)

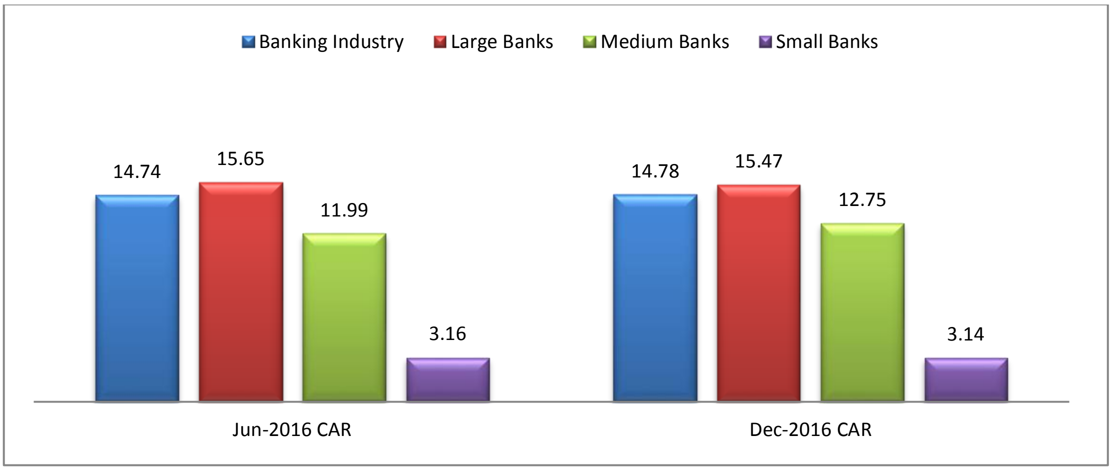
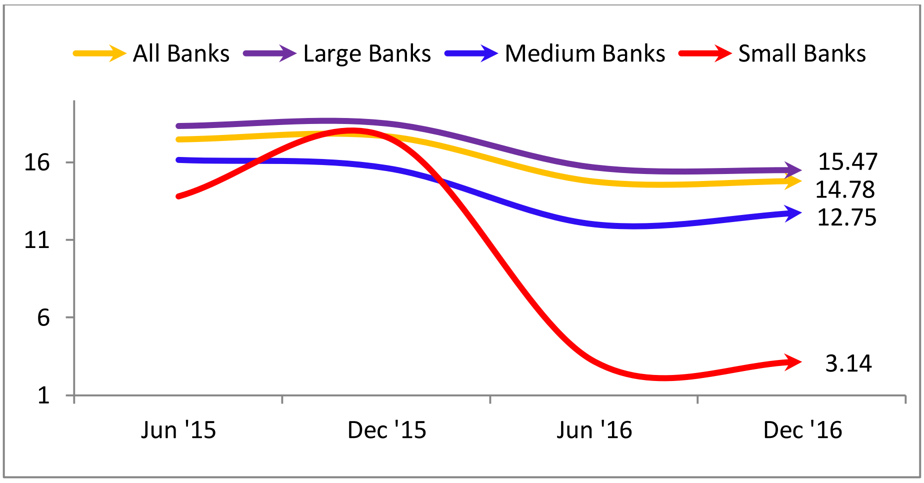


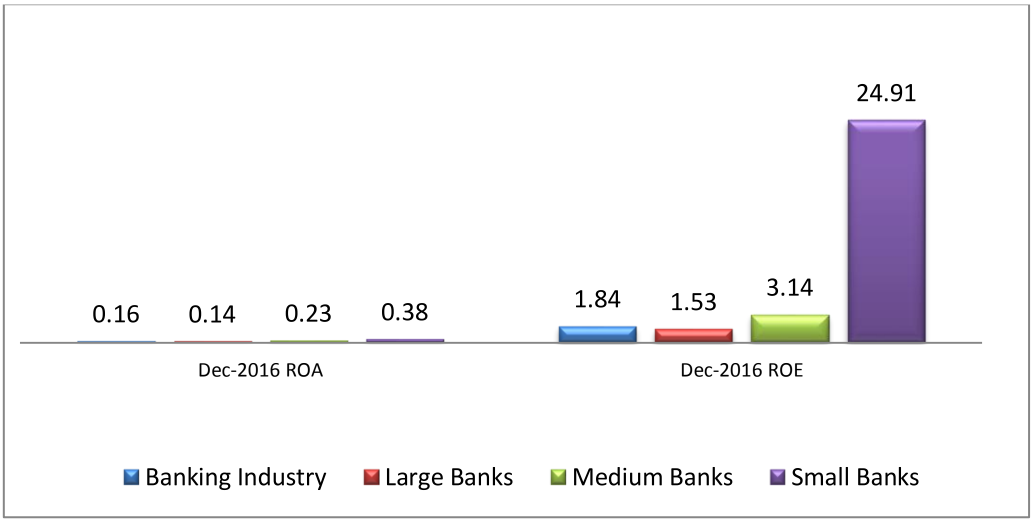
Figure 3. 5: CAR Trajectory: June 2015 - December 2016



The economic headwinds have adversely impacted bank borrowers, resulting in rising NPLs which required additional provisioning by banks, thereby reducing the banks' CAR. The decline of the CAR of small and medium banks did not weigh significantly on the industry CAR because large banks hold a significant proportion (88.02%) of total banking industry loans.

The pre-shock ROA of the banking industry, large, medium and small banks were 0.16, 0.14, 0.23 and 0.38 per cent, while the ROE of the banking industry, large, medium and small banks were 1.84, 1.53, 3.14 and 24.91 per cent in December 2016, respectively.

Figure 3. 6: Baseline (Pre-shock) ROA and ROE (%)



3.2.1 Solvency Stress Test

Credit Risk

The post-shock stress test results showed that a 100 per cent increase in NPLs will lead to a CAR of 10.55, 12.01, 10.34 and -27.03 per cent for the banking industry, large, medium and small banks, respectively. The results revealed that all the groups except small banks can withstand a 100 per cent increase in NPLs. However, none of the groups could sustain the impact of the most severe shock of a 200 per cent increase in NPLs as their post-shock CARs fell below the 10 per cent minimum prudential requirement. The impact of the severe shock scenario will result in a decline of CAR to 5.87, 8.25, 7.80 and -84.50 per cent for the banking industry, large, medium and small banks, respectively.

Table 3. 3: General Credit Shocks

Single Factor Shocks	**Solvency Ratio After Shocks**			
	All Banks	Large Banks	Medium	Small
Base line CAR	14.78	15.47	12.75	3.14
50% NPLs increase	12.72	13.78	11.56	-9.91
100% NPLs increase	10.55	12.01	10.34	-27.03
200% NPLs increase	5.87	8.25	7.80	-84.50

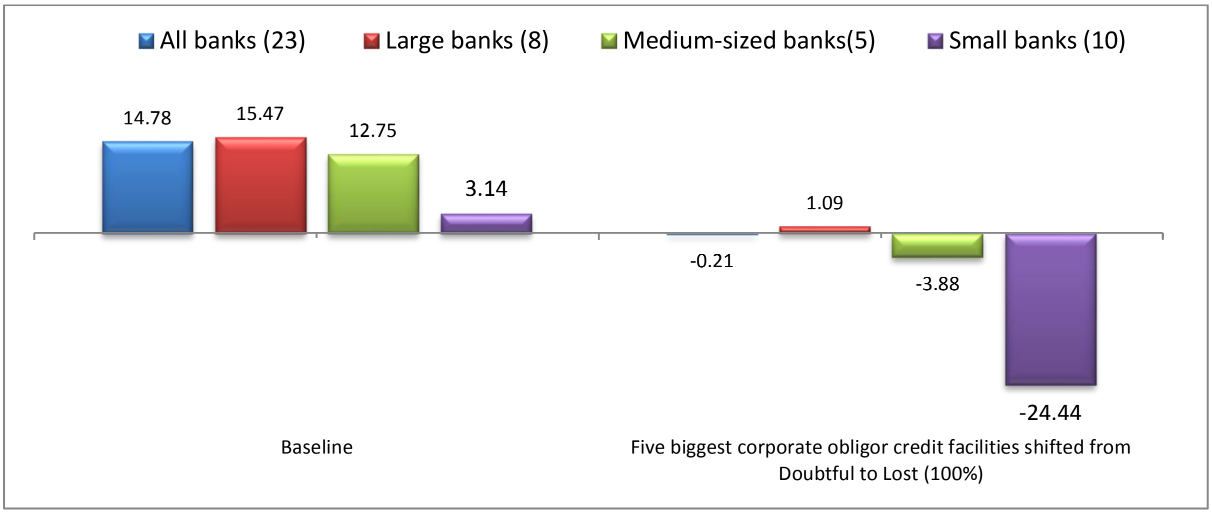
Credit Concentration

The banking industry and the peered-groups showed a high level of credit concentration risk as their respective CARs fell below 10 per cent under the shocks of deterioration in the quality of the risk assets. If the five biggest corporate obligor credit facilities shifts from Sub-standard to Doubtful, the CARs fell to 7.89, 8.84, 5.16 and -8.93 per cent for banking industry, large, medium and small banks, while if the five biggest corporate obligor credit facilities shifts from Doubtful to Lost, the CARs fell to -0.21, 1.09, -3.88 and -24.44 per cent, for the corresponding categories, respectively.

Table 3. 4: Credit Concentration Risk

	All Banks	Large Banks	Medium	Small
Baseline CAR	14.78	15.47	12.75	3.14
Single Factor Credit Concentration Shocks	**Solvency Ratio After Shocks**			
	All Banks	Large Banks	Medium	Small
Five biggest corporate obligors credit facilities shifted from pass-through to sub-standard (20%)	12.15	12.94	9.87	-1.35
Five biggest corporate obligor credit facilities shifted from sub-standard to Doubtful (50%)	7.89	8.84	5.16	-8.93
Five biggest corporate obligor credit facilities shifted from Doubtful to Lost (100%)	-0.21	1.09	-3.88	-24.44

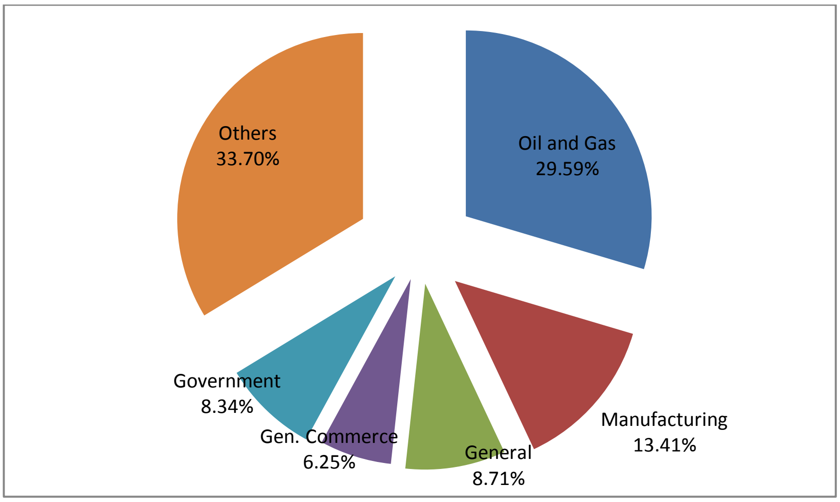
Figure 3. 7: Credit Concentration Shock (100% Loss)



Sectoral Credit Concentration Risk

Analysis of banking industry total credit by sector showed that, Oil & Gas sector constituted 29.59 per cent of total banking industry credit, while Manufacturing, General, General Commerce, Government and Others, constituted 13.41, 8.71, 6.25, 8.34 and 33.70 per cent, respectively, at end-December 2016.

Figure 3. 8: Sectoral concentration of Credit



The stress test result of a 20 per cent default in oil and gas exposures will lead to CARs of 13.98, 14.67, 11.87 and 2.63 per cent for the banking industry, large, medium and small banks, respectively. However, with a more severe shock of 50 per cent default in exposure to the sector, only the large banks will have CAR of 10.17 per cent which is above the regulatory threshold. This showed that medium and small banks have more oil and gas credit concentration risk than the large banks, despite their smaller proportion of exposure to the sector.

Table 3. 5: Impact of Credit Shocks on Oil & Gas Exposures

	All banks (24)	**Large (13)**	**Medium-sized Banks (3)**	**Small Banks (8)**
Baseline CARs	14.78	15.47	12.75	14.78
20% Default on total exposure to **Oil & Gas**	13.98	14.67	11.87	2.63
50% Default on total exposure to Oil and Gas	9.53	10.17	6.96	-0.14

Interest Rate Risk

The results of the stress tests on interest rate risk showed that the banking industry as well as peered-groups (except small banks) maintained a stable solvency position to interest rate shock as their post-shock positions (in terms of CAR) deteriorated marginally. However, the interest rate shocks have significant adverse impact on the ROA and ROE of both the industry position and the peered groups of banks due to their low baseline positions.

Figure 3. 9: Interest Rate Risk

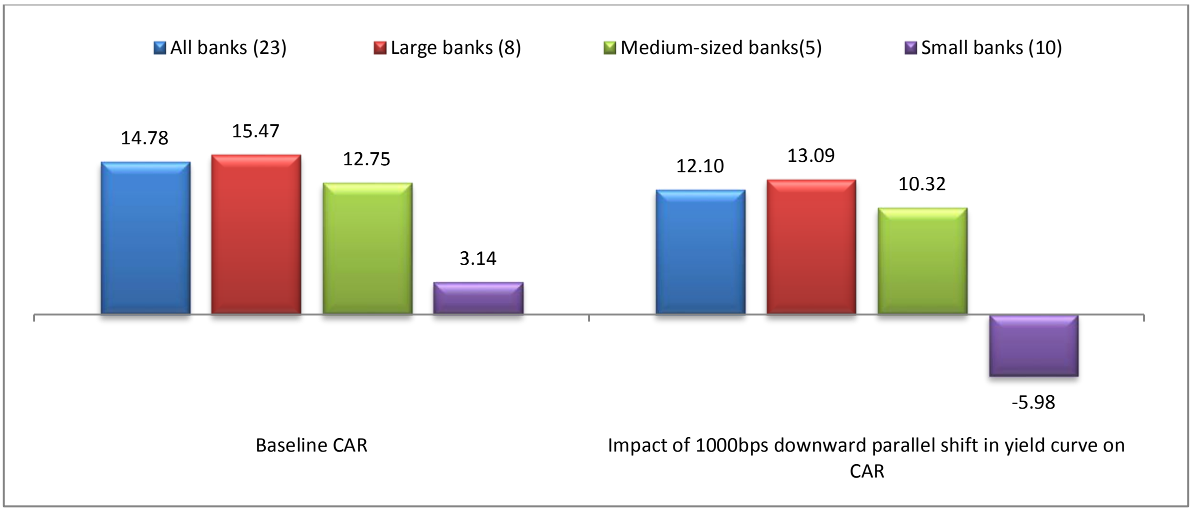


Figure 3. 10: Impact on Interest Rate Risk ROA and ROE

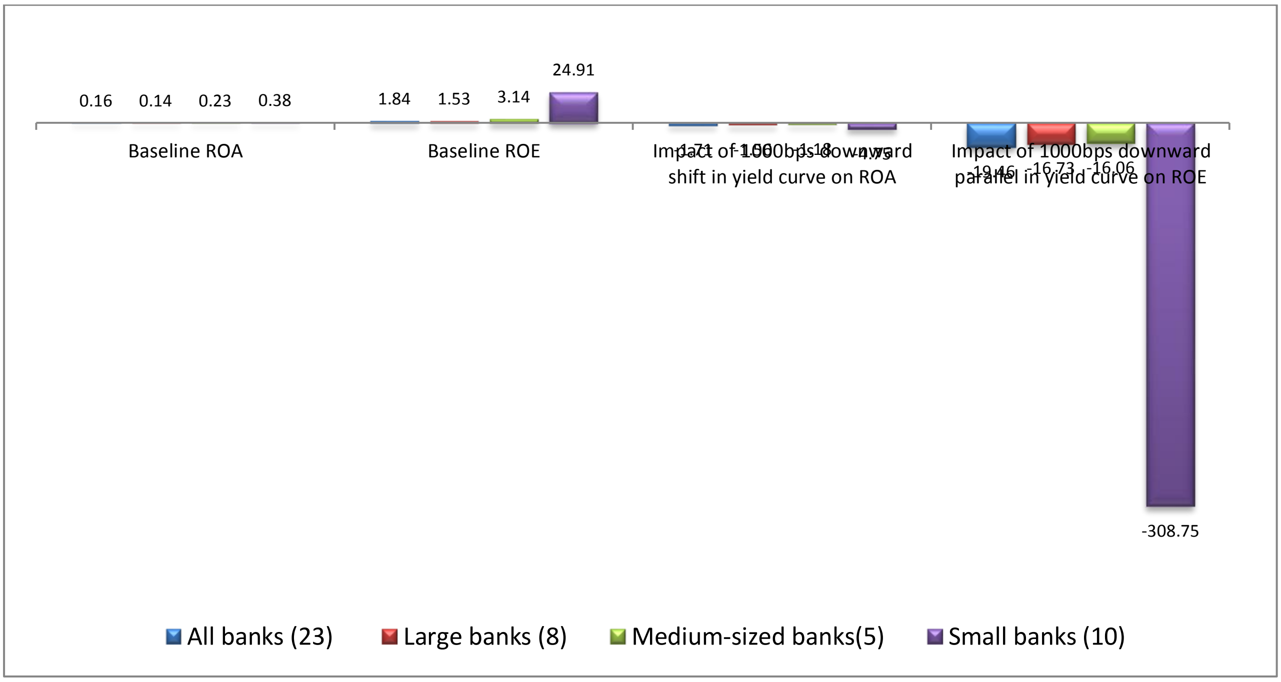


Table 3. 6: Impact of Selected Shocks on CAR, ROA and ROE (500bps to 1000bps)

Most Severe Shocks (500bps to 1000bps)	Banking Industry	Large Banks	Medium Banks	Small Banks
Baseline ROA	0.16	0.14	0.23	0.38
Baseline ROE	1.84	1.53	3.14	24.91
Interest Rate Volatility (Impact on CAR)				
500bps downward parallel shift in yield curve	13.44	14.28	11.54	-1.42
1000bps downward parallel shift in yield curve	12.10	13.09	10.32	-5.98
Impact of Parallel Shift in Yield Curve Shocks on ROA				
Interest Rate Volatility				
500bps downward parallel shift in yield curve	-0.77	-0.71	-0.47	-2.18

1000bps downward parallel shift in yield curve	-1.71	-1.56	-1.18	-4.75
Impact of Parallel Shift in Yield Curve Shocks on ROE				
Interest Rate Volatility				
500bps downward parallel shift in yield curve	-8.81	-7.60	-6.46	-141.92
1000bps downward parallel shift in yield curve	-19.46	-16.73	-16.06	-308.75

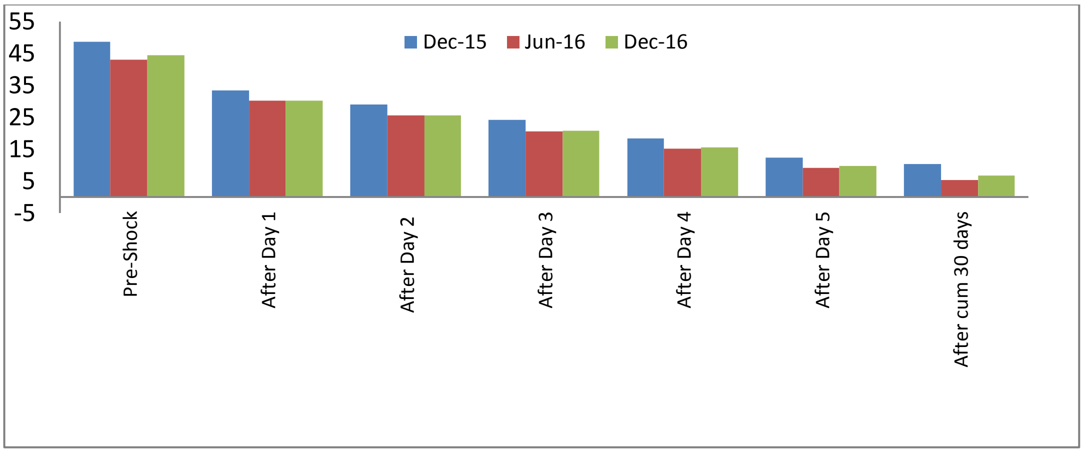
The banking industry solvency stress tests indicated that the resilience of banks to moderate and severe shocks deteriorated marginally during the review period. Although the sector is more exposed to credit concentration and default risks, there were no significant systemic threats.

3.2.2 Liquidity Stress Test

Liquidity stress tests were conducted using the Implied Cash Flow Analysis (ICFA) and Maturity Mismatch/Rollover Risk methods, to assess the resilience of individual banks and the banking industry to both liquidity and funding shocks.

The tests revealed that after a one-day run, the liquidity ratio for the industry would decline to 30.2 per cent from the 44.4 per cent pre-shock position and, to 9.73 per cent and 6.76 per cent after a five-day and cumulative 30-day run, respectively. Similarly, a 5-day and cumulative 30-day run on the banking industry would result in liquidity shortfalls of ₦2.1 trillion and ₦2.3 trillion, respectively.

Figure 3. 11: Banking Sector Liquidity Ratio after Period 1-5 and cumulative 30-day shocks



Box. 1: Implied Cash Flow Analysis (ICFA) Assumptions

The ICFA assesses the capacity of the banking system to withstand unanticipated substantial withdrawals of deposits, short-term wholesale and long-term funding over 5 days and cumulative 30 days, with specific assumptions on fire sale of assets. In this particular instance, the test assumed gradual average outflows of 3.8, 5.0 and 1.5 per cent of total deposits, short-term funding and long-term funding, respectively, over a 5-day period (Test 1.1) and a cumulative average outflow of 22.0, 11.0 and 1.5 per cent of total deposits, short-term funding and long-term funding, respectively, on a 30-day balance (Test 1.2). It also assumed that the assets in the following table would remain unencumbered after a fire sale.

Percentage of Assets Unencumbered after Fire Sales

Item No	***Assets***	***% Unencumbered***
1.	*Cash and cash equivalent*	*100*
2.	*Current account with CBN*	*100*
3.	*Government bonds, treasury bills and other assets with 0% risk-weighting*	*66.5*
4.	*Certificates of deposit held*	*66.5*
5.	*Other short-term investments*	*49*
6.	*Collateralized placement and money at call*	*49*
7.	*CRR*	*100*

Table 3. 7: Liquidity Stress Test Results

Scenarios	**Number of Banks with < 30% liquidity ratios**		**December 2016**	
	June 2016 (23 DMBs)	**December 2016 (24 DMBs)**	**System LR (%)**	**Liquidity Shortfall to 30% LR (₦' billion)**
Test 1.1: Implied Cash Flow Test				
Day 1	11	12	30.15	20.5
Day 2	13	16	25.66	568.04
Day 3	17	16	20.82	1,088.73
Day 4	18	17	15.51	1,592.92
Day 5	19	19	9.73	2,072.55
Test 1.2: Implied Cash Flow Test (30 Days)	19	18	6.76	2,308.03

3.2.3 Maturity Mismatch

At end-December 2016, the industry baseline position revealed that, on the average, the shorter end of the market (≤30 day and 31-90 day buckets) were adequately funded. However, on individual analysis, four (4) banks were not adequately funded in the ≤30 day bucket, while ten (10) banks had funding gaps in the 31-90 day bucket.

The cumulative position for the industry showed an excess of ₦5.5 trillion assets over liabilities.

Table 3. 8: Maturity Profile of Assets and Liabilities at end-December 2016

	Liabilities	Assets	Mismatch	Cumulative
	₦ Billion			
≤30 days	14,294.84	8,837.33	5,457.51	5,457.51
31-90 days	2,394.96	1,560.05	834.92	6,292.42
91-180 days	991.47	1,923.07	(931.60)	5,360.82
181-365 days	773.20	2,424.95	(1,651.75)	3,709.07
1-3 years	628.80	3,789.38	(3,160.58)	548.49
Above 3 years	822.54	6,885.98	(6,063.44)	(5,514.95)
Total	**19,905.81**	**25,420.76**	**(5,514.95)**	

The Test 2A was cumulatively adequately funded, but Test 2B and 2C had a mismatch of ₦7.1 trillion and ₦7.5 trillion respectively (Table 3.11).

Box. 2: The Maturity Mismatch/Rollover Risk Assumptions

This approach assessed funding maturity mismatch and rollover risk for assets and liabilities in the 0-30 and 31-90 day buckets, with assumptions on the availability of funding from CBN and intra-group as described below:

*i. **Test 2a: Descriptive Maturity Mismatch** assumed that the baseline mismatch remained but that 5 per cent of total deposits would be made available from the CBN and the intra-group;*

*ii. **Test 2b: Static Rollover Risk** assumed that 80.0 and 72.0 per cent of the funding in the 0-30 and 31-90 day buckets would be rolled over, with no possibility to close the funding gap from other buckets. However, 5 per cent of the total deposits would still be available from the CBN and the intra-group; and*

*iii. **Test 2c: Dynamic Rollover Risk** made the same assumption as in 2b above, but with the option of closing the liquidity gap from other buckets.*

Table 3. 9: Test Results for System-wide Maturity Mismatch

	Test 2A Descriptive Maturity Mismatch (no consideration of rollover)		**Test 2B Static Rollover risk Analysis. (No possibility to close liquidity gaps in other buckets)**		**Test 2C Dynamic Rollover risk test. (No possibility to close liquidity gaps in other buckets and free assets is used to close liquidity gaps in other buckets)**	
	₦' billion	**No of banks with mismatch**	**₦' billion**	**No of banks with mismatch**	**₦' billion**	**No of banks with mismatch**
≤30 days	7,917.67	1	5,061.12	3	61.72	3
31-90 days	3,257.61	2	155.52	13	(31.92)	4
91-180days	1,522.34	4	(1,112.07)	17	(81.15)	5
181-365days	827.52	10	(1,842.07)	20	(394.51)	8
1-3 years	(712.14)	17	(3,340.51)	21	(2,052.14)	13
Above 3 years	(3,629.03)	20	(6,068.76)	21	(5,094.86)	18
Total	**9,183.98**		**(7,146.75)**		**(7,592.85)**	

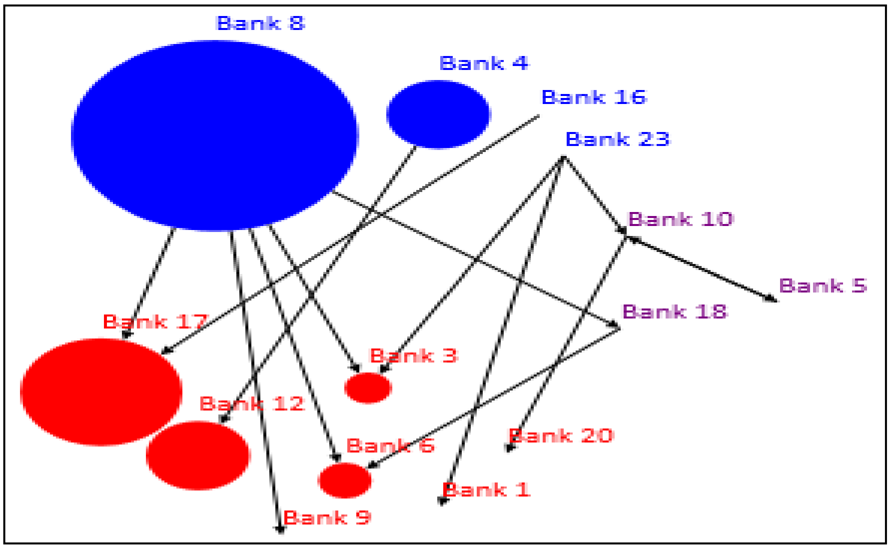
3.2.4 Contagion Risk Analysis through Interbank Exposures

The analysis of banks based on unsecured interbank exposures revealed that one (1) bank was central in the network, as it was exposed to more than two counterparties in the system, while a review of secured transactions showed that five (5) banks were central in the network as they had three or more bilateral exposures. Overall, the result indicated the potential for high contagion risk through unsecured interbank exposure as three banks (including two Systemically Important Banks) failed CAR after a 100 per cent default shock (Table 3.12).

Table 3. 10: Result of Net Interbank Unsecured Exposures on Capital Adequacy Ratio.

Lending Banks	**Bank 4**	**Bank 5**	**Bank 8**	**Bank 10**	**Bank 16**	**Bank 18**	**Bank 23**	**Industry**
Pre-Test CAR (%)	15.08	16.59	16.60	22.76	18.26	11.80	12.13	14.78
Post-Test CAR (%)	13.52	16.31	14.91	15.15	17.43	11.09	9.62	14.35
Net Placement (₦' Billion)	20.45	4.73	48.22	5.92	5.00	4.66	4.86	93.84

Figure 3. 12: Tiered Structure of Unsecured Placements at end-December 2016



Note: Node colour representation (Blue= Lenders; Red= Borrowers; Purple= Borrowers and Lenders); the sizes of the nodes represent the quantum of transactions.

3.3 Supervision of Banks

3.3.1 Routine/Target Examinations

The CBN in conjunction with the NDIC conducted the routine examination of 10 banks in the “Low” and “Medium” Composite Risk Rating (CRR) categories during the second half of 2016. The examination of banks in the “High” and “Above Average” categories were earlier conducted in the first half of the year. The non-interest bank and the two non-interest windows were examined during the second half of the year. The CBN also monitored compliance of banks to the recommendations of the Money Laundering, and Foreign Exchange examination reports of 2015.

The outcome of the examinations revealed, among others, a decline in capital adequacy ratios (CAR) and asset quality which was attributable to weak domestic macroeconomic conditions and the slow recovery of the global economy. The decline in CAR was due to a slight decline in total qualifying capital from increased provisions for loan losses and a corresponding increase in risk weighted assets. The decline in the asset quality was driven by a decline in oil prices which impacted on the obligors in the oil and gas sector and by extension the banking industry in view of its large exposures to the sector. The monitoring exercise revealed an acceptable level of compliance to the recommendations.

The routine examination of the Asset Management Corporation of Nigeria (AMCON) was conducted during the second half of 2016. The examination focused on the management of the acquired and restructured Eligible Bank Assets (EBAs), the recoveries made, assets disposed and strategies for redemption of liabilities.

As at the examination review date of September 30, 2016, the corporation had made total recovery of ₦78.76 billion for 2016, which was made up of cash recoveries, asset forfeiture and securities forfeiture. This represented a 90.2 per cent increase in the recoveries of ₦41.42 billion recorded in the corresponding period to September 30, 2015.

From its inception to September 30, 2015, the corporation has made total recoveries of ₦681.541 billion, representing 38.95 per cent of the corporation's total Eligible Bank Asset purchase price of ₦1.75 trillion.

During the period under review, the corporation maintained its strategy of increased recovery momentum, complemented with the balances accrued in the Banking Sector Resolution Trust Funds to enable it redeem its obligations.

3.3.1.1 Foreign Exchange Examinations

The CBN conducted routine and special examinations of foreign exchange activities of banks during the review period. The examinations revealed a number of infractions which included: breaches in Net Open Position (NOP) and Foreign Currency Trading Position (FCTP) limits, failure to repatriate export proceeds timeously and inappropriate involvement of banks in international money transfer. Other breaches observed were non-compliance with forward trading rules, late/non-submission of foreign exchange transaction documents by importers, and non-compliance of Authorised Dealers (ADs) with CBN directives on the specified sectoral disbursements. Appropriate regulatory measures including sanctions were taken.

Furthermore, the Bank conducted spot checks on International Money Transfer Operators (IMTO) activities, which revealed several cases of irregularities in IMTO transactions by unregistered firms.

3.3.1.2 Anti- Money Laundering/Combating the Financing of Terrorism

The Bank, in compliance with Financial Action Task Force (FATF) and Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) requirements, directed banks to appoint Executive Compliance Officers, not below the rank of Executive Director, who will be responsible for compliance with regulations. This is in addition to the existing Chief Compliance Officers. Other activities include the following:

- As part of the process towards developing an AML/CFT Strategy Document, the Bank participated in the maiden Money Laundering/Financing of Terrorism National Risk Assessment (NRA) exercise which was coordinated by the Nigerian Financial Intelligence Unit.
- The Bank also participated in the AML/CFT Expert Review Forum for the implementation of the recommendations of the United Nation Convention Against Corruption (UNCAC).
- The CBN coordinated the preparedness exercise of banks for the forthcoming Mutual Evaluation while it continued to work with GIABA to address issues identified in its previous Mutual Evaluation Report.

- The Bank reviewed the daily deposit limits of the Tier I and II accounts in the Tiered KYC Policy to ₦50,000 and ₦100,000, respectively. Cumulative balances were also revised to ₦300,000 and ₦500,000 for Tier I and II accounts, respectively.
- The Bank commissioned a study on Virtual Currency to appraise its implications for the Nigerian Payments System. Following an interim report of the study, a cautionary notice was issued drawing the attention of the public to the inherent risks in virtual currencies pending the conclusion of the study.

Nigeria is no longer subject to FATF's monitoring process under its on-going global AML/CFT compliance process. It has also applied for membership of the FATF with a high level mission of the FATF scheduled to visit Nigeria in the first quarter of 2017.

Box. 3: The Implementation of the Nigeria Sustainable Banking Principles

The Bank conducted an onsite assessment of 18 banks on the adoption and implementation of the Nigerian Sustainable Banking Principles. The highlights of the assessment, which involved the review of internal records and engagement with relevant desk officers, were:

Principle 1: E&S Management System for Business Activities
All 18 banks assessed had in place environmental and social (E&S) policies approved by their Boards of Directors. The policy documents indicated that E&S considerations had been integrated into the enterprise risk management systems and corporate governance structures of the banks. However, some banks were yet to develop E&S procedure manuals while others had manuals that were not comprehensive.

Principle 2: Footprint Management for Business Operations
Most of the banks had documented E&S footprint management procedures in place.

Principle 3: Human rights
All the banks had human right policies, recorded either in their E&S or human resource policy documents. Although staff unions were non-existent in some of the banks, the banks indicated that staff had freedom of association.

Principle 4: Women Economic Empowerment
Several banks had developed and launched women-friendly products and services, most of which were tied to the CBN ₦200 billion Micro Small and Medium Enterprises Development Fund scheme. On the average, female staff constituted 42 per cent of the total staff and 26 per cent of both top management and the Board.

Principle 5: Financial Inclusion
All the banks had implemented the tiered KYC initiative, leading to an increase in the number of previously unbanked individuals drawn to the banking sector. It was also observed that 11 banks designed innovative financial products and services for underprivileged groups.

Principle 6: E&S Governance
All the banks had E&S risk management governance structures in place. Common to all banks were the following features -

(a) The Board was responsible for all social, ethical and environmental policies and also had oversight responsibility on the implementation.
(b) Management was responsible for the development and implementation of E&S risk management strategies, policies and procedures to facilitate the integration of sustainability into the business decision models as well as report periodically to the Boards on implementation of the E&S risk

management policies and procedures.

Principle 7: Capacity Building
While many banks adopted various platforms for capacity building on sustainability, it was observed that the trainings were inadequate to embed strong sustainability culture in business activities.

Principle 8: Collaborative Partnership
All the banks provided evidence of regular attendance of NSBP champion meetings. Some banks had obtained membership of international bodies such as Global Reporting Initiative (GRI) and United Nations Environmental Programme – Financial Sector Initiative (UNEP-FI) to assist in their sustainability initiatives.

Principle 9: Reporting
All the banks had been submitting their E&S reports as and when due.

3.3.1.3 National Road Map on Sustainable Finance

Following the approval of the FSRCC for the implementation of the roadmap for the Nigerian Sustainable Finance Principle (NSFP), each member agency was required to set up a steering committee to coordinate the development of sector-specific Sustainability Principles and Guidelines. The steering committees would interface with the Harmonisation and Coordination Sub-Committee (HCSC) of the FSRCC to ensure that each sector regulators meet the agreed 30-month implementation period.

The FSRCC also agreed to collaborate with the International Finance Corporation (IFC) to build capacity in sustainability and green finance in the review period.

3.3.2 Enhanced Supervision of Domestic Systemically Important Banks

In line with the Framework for the Regulation and Supervision of Domestic Systemically Important Banks (D-SIBs), eight (8) banks earlier designated as D-SIBs retained their status during the period under review. These banks were required to meet more stringent prudential regulations to reflect their systemic importance.

At end-December 2016, the D-SIBs accounted for ₦20.87 trillion (69.06%) of industry total assets of ₦30.22 trillion. Similarly, the D-SIBs accounted for ₦13.04 trillion (70.25%) of total industry deposits of ₦18.56 trillion and ₦11.76 trillion (72.2%) of the aggregate industry loans of ₦16.29 trillion.

During the review period, the banking sector witnessed a rise in non-performing loans due to weakening economic conditions with four (4) D-SIBs recording NPL ratios above the regulatory limit of 5.0 per cent. The CBN directed the D-SIBs to take appropriate actions to address the breach.

3.3.2.1 Recovery and Resolution Plan

During the review period, the Bank, in collaboration with the NDIC, issued a guideline on the *Minimum Content for Recovery Plans and Requirements for Resolution Planning* to all D-SIBs. The Guideline covers the minimum contents for recovery planning and the documentary requirements for resolution planning to aid D-SIBs in the preparation of their submissions.

The Guideline was to assist D-SIBs in:

- Identifying critical functions and services rendered;
- Designing stress scenarios for evaluating their capacity to provide identified critical services and assess the impact of these scenarios on capital, liquidity, profitability, and asset quality;
- Preparing comprehensive range of actionable recovery options to be taken to remedy financial weaknesses and maintain market confidence;
- Providing documentary evidence that the responsibility for review and approval of the plan is vested in the Board of Directors and/or other appropriate senior management; and
- Preparing resolution pack with detailed information to assist the resolution authorities in designing relevant resolution strategy for the bank in the event of failure.

The second submissions of RRPs are scheduled to be reviewed in the first half of 2017.

3.3.3 Cross Border Supervision

3.3.3.1 Cross Border Institutions

The total number of cross border institutions decreased from 70 at end-June 2016 to 68 at end-December 2016 following the closure of two representative offices in South Africa. The 68 entities comprised 59 subsidiaries, one affiliate, one branch and seven representative offices located in 28 countries.

3.3.3.2 Onsite examination of offshore subsidiaries of Nigerian banks

During the second half of 2016, the CBN participated in the onsite examination of nine (9) offshore subsidiaries of five Nigerian banks. Seven of the examinations were jointly carried out with host supervisors in the West African zone, while two were solo.

The report of the joint examinations revealed that five (5) subsidiaries maintained their “Moderate” risk profile while two (2) subsidiaries whose visits were maiden had risk profile of “Above Average”. The solo examinations revealed a “High” risk profile for one bank. The “Above Average” and “High” risk subsidiaries are being subjected to intensive surveillance in line with the cross border supervisory framework.

In line with FATF recommendations, two (2) joint AML/CFT examinations were carried out in collaboration with host supervisors in the second half of 2016. The examinations revealed that the subsidiaries were exposed to significant AML/CFT risk regarding inadequate customer due diligence. The parent banks have been directed to remediate the observed lapses.

3.3.4 Offsite Analysis and Supervision

The CBN continued to analyze prudential and other returns from the offshore banking subsidiaries received through the parent banks during the period. The analysis highlighted areas requiring improvement in risk management and corporate governance in some subsidiaries. The parent banks were directed to submit actionable plans to improve the non-performing loans ratio, reduce operating costs and address lapses in risk management in the affected subsidiaries.

3.3.5 College of Supervisors

3.3.5.1 College of Supervisors of the West African Monetary Zone

The 23rd meeting of the College of Supervisors of the West African Monetary Zone (CSWAMZ) was held in Ghana from October 24th to 28th, 2016. The meeting deliberated on the macroeconomic and financial sector developments in the zone and their impact on the safety and soundness of individual banks and the financial system. The meeting was held alongside a high level seminar for college members on Financial Instruments (IFRS 9) and Micro Prudential Analysis. The seminar was part of the college activities to build examiners' capacity in key areas of supervision, particularly Basel Core Principles, Risk Based Supervision, AML/CFT and contemporary supervision matters.

3.3.5.2 United Bank for Africa College of Supervisors

The Bank hosted the third forum of United Bank for Africa (UBA) College of Supervisors in the second half of 2016. The forum, which had in attendance supervisors from 11 African countries, concluded that the overall risk profile of UBA was satisfactory.

3.3.5.3 Eco Transnational Incorporated College of Supervisors

The Bank participated in the second Meeting of Eco Transnational Incorporated (ETI) Supervisory College in Lome, Togo during the second half of 2016. The Meeting was to assess the risk profile of ETI and its capacity to support Ecobank Nigeria Ltd.

3.3.5.4 Other Supervisory Collaborations

The CBN hosted the annual general meeting of the Association of African Central Banks (AACB) in August 2016. During the meeting, the CBN signed two Memoranda of Understanding (MoUs) with the Bank of Central African States and the Banking Commission of Central African States. The MoUs were executed to facilitate supervisory cooperation and information sharing.

The Bank also participated in the 17th meeting of the Legal and Institutional Issues Committee of the West African Monetary Zone in Accra, Ghana, from October 11 - 14, 2016 to consider a Model Banking Act for countries in the zone. The Committee discussed the draft and agreed on enhancements in the areas of consolidated supervision, large exposures, corporate governance, risk management and related parties transactions.

3.3.6 Mandatory Registration of Commercial Paper Issued by Commercial Banks in Nigeria

Nigerian banks were hitherto allowed to participate in any commercial paper (CP) issuance (including unquoted CP). In line with global reforms which requires more stringent regulation of OTC markets, the CBN directed banks to deal in only CP that are registered on Authorized Securities Exchanges with effect from July 11, 2016.

The registration and quotation of CP is expected to bring significant benefits, which include:

1. Providing CBN with price/volume data that would aid oversight and valuation of CP;
2. Offering comfort to other financial market regulators such as the National Pension Commission and the National Insurance Commission (NAICOM) to permit their regulated entities to invest in CP, thus providing additional funding for the real sector;
3. Reducing the CBN's need for interventions, thereby, freeing up resources which could be devoted to other activities of the Bank; and
4. Enhancing transparency in the market to support sound investment decisions.

3.3.7 Watch-list

An exposure draft of the *Framework on Watch-list for the Nigerian Banking System* was issued in the second half of 2016. The Framework is a collaborative effort of CBN and Nigeria Inter-Bank Settlement System (NIBSS) to address the increasing incidence of fraud, forgeries and other unethical practices in the financial system.

3.4 Supervision of Other Financial Institutions

3.4.1 Routine Examination of Development Finance Institutions

At end-December 2016, the number of DFIs reduced to five (5) in comparison with the six (6) institutions in operation at end-June 2016, as liquidation of the Nigerian Economic Recovery Fund (NERFUND) commenced in the period under review. The remaining five institutions as at December 31, 2015, had composite risk ratings as follows: one, "High"; three, "Above Average", and one, "Moderate" compared with June 2016 position of: two, "High"; three, "Above Average"; and one, "Moderate".

The capital ratings for the other five DFIs were "Strong" for two and "Weak" for the other three in comparison with the capital ratings for the six DFIs which were "Strong" for two and "Weak" for the other four. The prudential and soundness analysis of the DFIs further revealed that three of the institutions met the minimum capital adequacy ratio (CAR) requirement of 10 per cent, while the other two had negative CAR. All the DFIs maintained non-performing loan (NPL) ratios above the stipulated regulatory maximum of 5 per cent.

3.4.2 Examination of Microfinance Banks

A total of 743 MFBs were examined during the period under review. This comprised 585 risk-based and 158 special examinations. Reports of the RBS examinations were being finalized, while regulatory letters have been issued to various institutions on which the special examinations were conducted, specifying regulatory actions and defined time lines for injection of additional capital and recovery of non-performing loan facilities.

3.4.3 Examination of Finance Companies

The examination of nine (9) FCs granted 90-day extension for recapitalization was carried out in December 2016. The reports of the examination were being compiled.

The Bank approved 40 Finance companies that fully met the new capital requirement of ₦100 million, while the licenses of 13 finance companies that did not meet the new capital requirement were approved for revocation. Also, the licenses of eight other FCs were approved for revocation for voluntary surrendering of licenses, insolvency and discontinuation of finance company business.

The appointment of liquidators to wind up the activities and the publication of the names of all the institutions approved for revocation in the Federal Gazette in line with Section 60 of BOFIA was also approved by the Bank.

3.4.4 Examination of Primary Mortgage Banks

The 34 primary mortgage banks in operation were examined in the review period. Routine examination was conducted on 24 PMBs using the risk based methodology, while target examination was conducted on the others.

The Nigeria Mortgage Refinance Company (NMRC) was also examined in the last quarter of 2016 and retained its “Moderate” composite risk rating (CRR).

3.5 Non-Interest (Islamic) Banking

During the review period, one (1) Micro-Finance (Islamic) bank was granted a license, bringing to two (2) the number of non-interest microfinance banks.

The Governing Board of the International Islamic Liquidity Management Corporation (IILM), Malaysia, at its meeting on December 16, 2016 in Jakarta Indonesia appointed the Governor of the CBN as Chairman, effective January 1 to December 31, 2017.

The Bank also participated in the Council meeting of the IFSB, Governing Board of the IILM and the Working Group Meetings of the two (2) multilateral institutions.

3.6 Developments in Basel II/III and IFRS 9 Implementation

3.6.1 Developments in the Implementation of Basel II/III

During the review period, the CBN issued Guidance Notes for the Implementation of IFRS 9 (Financial Instruments) which would become effective on January 1, 2018. The Guidance Notes communicate supervisory expectations for the implementation of the new Expected Credit Loss (ECL) model, especially in areas where banks are expected to exercise considerable judgment and/or elect to use simplifications and other practical expedients permitted under the Standards.

The Guidance Notes further require banks to:

1. Commence parallel run of the new ECL model alongside the current Incurred Loss Model as from July 1, 2017;

2. Obtain External Auditors'/Independent Consultants' certification of their IFRS 9 accounting policies and impairment models by the third quarter of 2017;

3. Submit information to the CBN on their Project Governance Structures, IFRS 9 Gap Analysis and Impact Assessment Reports, and existing or proposed models for ECL calculation, not later than April 30, 2017; and

4. Submit periodic status reports to the CBN starting from May 2017.

3.6.2 Implementation of Basel II/III

During the second half of 2016, the CBN engaged banks as part of the Supervisory Review and Evaluation Process of Basel II requirements. The engagement involved an initial review of banks' Internal Capital Adequacy Assessment Process (ICAAP) reports submitted in 2016, onsite validations and supervisory dialogue.

Improvements were observed in the quality and presentation of the 2016 ICAAP reports, being the third sets of submissions since the adoption of Basel II requirements in 2014. Most of the banks adopted specified regulatory approaches for economic capital estimation for credit (standardized approach), market (standardized approach) and operational risks (basic indicator approach) and other approaches for other material risks. Other banks used internal models to estimate the required capital charges for all the material risks identified. The engagement provided a platform for supervisors to understand banks' risk and capital management systems.

3.7 The Asset Management Corporation of Nigeria

The net carrying value of AMCON's outstanding liabilities remained unchanged at ₦4.5 trillion at end-December 2016. However, the carrying value of its assets net of impairment was ₦624 billion[7] at end-December 2016, down from ₦846.41 billion at end-June 2016 following recoveries realized and additional impairments booked by the Corporation.

The gap between AMCON's assets and its liabilities would potentially be covered through the Banking Sector Resolution Cost Trust Fund (BSRCTF) as well as credit recoveries and assets sales by AMCON.

The BSRCTF realized total collections of ₦175.97 billion during the 2016 financial year while AMCON realized total recoveries of ₦139.04 billion during the year.

[7] This figure reflects IFRS reporting as opposed to NGAAP reporting in prior periods.

3.8 Key Risks to the Financial System

3.8.1 Credit Risk

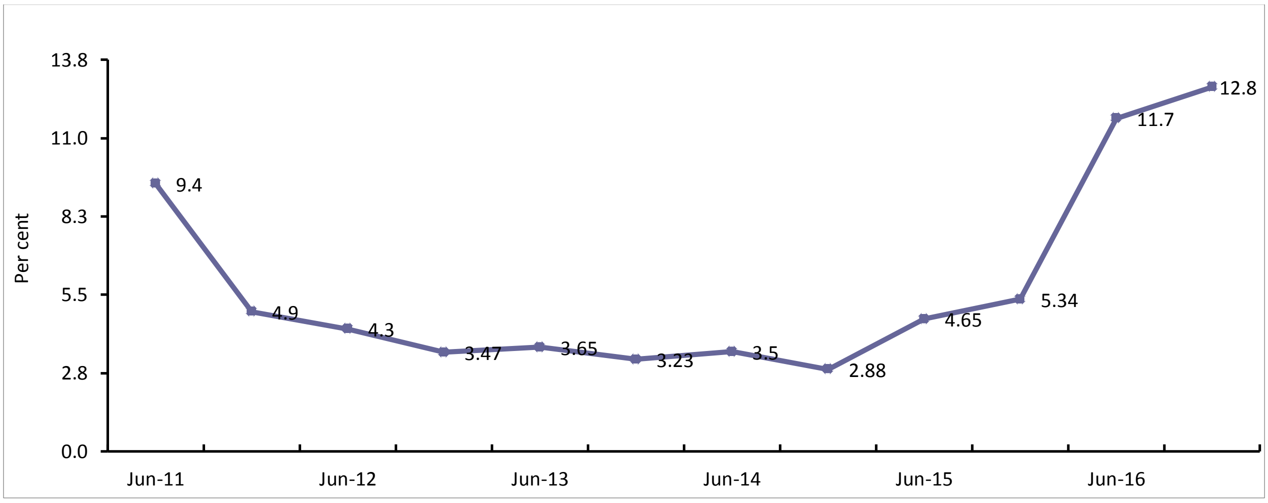
Risk Rating (High Risk, Trending Up)	

During the period under review, credit risk trended higher as the industry wide NPL ratio moved from 11.7 per cent to 12.8 per cent at the end of 2016 and non-performing loans grew to ₦2,084.92 billion at end-December 2016 from ₦1,678.59 billion at end-June 2016. Total exposure of the top 50 obligors stood at ₦5.59 trillion (34%) of total industry credit exposure of ₦16.29 trillion.

At end-December 2016, loans to the oil and gas sector constituted 30.02 per cent of the gross loan portfolio of the banking system as credit to that sector grew from ₦4,511.34 billion, to ₦4,890.91 billion. Loans to State Governments declined marginally to ₦1,376.89 billion from ₦1,386.61 billion at end-June 2016. The period witnessed increased funding to the states via a Federal Government refund totalling ₦522 billion in excess debt service deductions (Paris Club Debt Refund). In addition, ₦90 billion bail-out facility at 9.0 per cent interest rate, was provided to enable States reduce backlog of salaries.

Overall, credit risk remains tangible in 2017 as obligors remain constrained in servicing both Naira and FCY denominated loans owing to the low level of economic activities, low international oil prices and the depreciation of the naira.

Figure 3. 13: Non-Performing Loans Ratio



3.8.2 Liquidity Risk

Risk Rating (Medium Risk, Stable)	

The liquidity ratio for the banking industry increased by 1.35 percentage points to 43.96 per cent at end-December 2016 from 42.61 per cent at end-June 2016, above the prudential minimum limit of 30 per cent by 13.96 percentage points. Market liquidity decreased to ₦159.29 billion at the end of 2016 from ₦175.15 billion at end-June 2016, owing largely to the increase in Monetary Policy Rates from 12.00 to 14.00 per cent.

3.8.3 Market Risk

Risk Rating (Medium Risk, Trending Up)	

Savings rate rose marginally by 0.57 percentage point from 3.61 per cent at end-June 2016 to 4.18 per cent at end-December 2016, while the maximum lending rate grew by 1.62 per cent to 28.55 per cent in the same period. The movement in rates reflected the contractionary monetary stance of the Bank.

The 91-day NTB rates closed at 13.96 per cent at end-December, 2016 from 8.32 per cent as at June 2016. The increased rate is expected to attract higher capital inflows to the market. Interbank and Open Buy Back rates declined significantly to 10.39 and 7.35 at end-December 2016, from 35.26 and 21.75 per cent as at end-June 2016. The downward trending rates reflected the normalization of the market following the newly introduced flexible foreign exchange policy.

During the period, management of exchange rates remained constrained as foreign exchange scarcity prevailed. The scarcity was mainly as a result of reduced capital inflows, slow recovery in oil prices and general macroeconomic uncertainties. The divergence between the supply and demand sides brought about disparity in exchange rates as reflected by the steep depreciation of the naira. However, the newly introduced regime provided respite in accessing foreign currency as FX forward contracts assisted in reducing overdue trade finance obligations.

In 2017, based on forecasts of improved performance in the global oil market, foreign currency liquidity is expected to increase while the further downgrade of Nigeria by S&P from B+ to B in 2016 is anticipated to increase borrowing costs as Nigerian bonds had been classified speculative.

3.8.4 Operational Risk

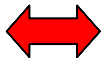
Risk Rating (High risk, trending up)	

Operational risk events reported during the period included the incidence of frauds and forgeries, increased cybercrime attempts and rising insecurity in some parts of the country. Cases of fraud and forgeries increased to 9,929 at end-December 2016 from 9,164 reported at end-June 2016. The total amount involved in the cases, however, reduced from ₦4.36 billion at end-June 2016 to ₦4.12 billion at end-December 2016. Similarly, actual losses reduced to ₦1.003 billion at end-December 2016 from ₦1.38 billion at end-June 2016. Returns from banks showed that majority of frauds and forgeries were perpetrated by outsiders. The frauds were committed mainly through suppression and conversion of customers' deposits, illegal fund transfers, pilfering and ATM withdrawals.

Cybercrime was identified as a key operational risk due to increased reliance on technology by banks, ease of access to the internet and other electronic platforms by customers. In order to mitigate this class of operational risk, bank customers were continually sensitized on safe banking practices.

Operational costs increased significantly due to increments in electricity tariffs as well as increased petroleum product prices occasioned by the deregulation of the downstream sector. Consequently, rising costs would translate to further layoffs in the banking industry.

3.8.5 Macroeconomic Risk

Risk Rating (High Risk, Stable)	

During the review period, macroeconomic risks heightened, largely due to the slow pace of global economic recovery, dwindling oil prices which impacted adversely on Government revenue, depreciation of the naira, rising inflation and negative growth. However, current efforts by the Government to stimulate domestic demand through investment in infrastructure, the Conditional Cash Transfer Programme and implementation of the National Recovery Strategy are expected to improve overall economic conditions.

3.9 CBN Credit Risk Management System

At end-December 2016, the number of borrowers registered in the CRMS database stood at 221,822, indicating an increase of 13.66 per cent over 195,159 recorded at end-June 2016. Similarly, the number of registered borrowers with outstanding facilities rose by 11.76 per cent to 104,126 at end-December 2016 from 93,168 at end-June 2016 and the number of running credit facilities in the database also increased by 5.16 per cent to 181,987 at end-December 2016 from 173,050 at end-June 2016, due to increased compliance by banks.

Table 3. 11: Borrowers from the Banking Sector

Description	June 2016	December 2016	Absolute Change	% Change
Total No. of Borrowers on the CRMS	195,159	221,822	22,663	13.66
No. of Borrowers with outstanding credit	93,168	104,126	10,958	11.76
No. of Credit/facilities	173,050	181,987	8,937	5.16

Note: *These figures are based on submission by Commercial and Merchant Banks only and for amount of ₦1m and above.*

The redesigned CBN Credit Risk Management System (CRMS) which is currently on a pilot-run is scheduled for roll out in the first quarter of 2017.

3.10 The Financial Services Regulation Coordinating Committee

3.10.1 Consolidated Examination of Financial Holding Companies

The FSRCC conducted the consolidated examinations of FBN and FCMB Holdings in the review period. The Reports of the examinations were distributed in December 2016 to the HoldCos and participating agencies.

3.10.2 Illegal Fund Managers

The FSRCC had disbursed all monies escrowed in the CBN in respect of the Illegal Funds Managers (IFMs)/'Wonder Banks' to the court-appointed liquidators, except for the two with subsisting court cases. During the review period, the FSRCC in conjunction with the Nigeria Police closed a "wonder bank", named "AMF Bank Limited".

The FSRCC Secretariat also inaugurated an ad-hoc committee on the activities of a suspected fraudulent financial service outfit Mavrodi Mondial Moneybox (MMM). The committee is charged with the responsibility of recommending ways to curb the spread of MMM in Nigeria. The MMM and other ponzi schemes operate over the internet with no physical location. The FSRCC and law enforcement agencies are ensuring the deactivation of the websites and prosecution of the promoters.

Stakeholders have intensified campaigns and sensitization against the patronage of IFMs.

3.10.3 Capacity Building

During the review period, the FSRCC conducted training for staff of member agencies on the new Auditor's Reporting Standard issued by the International Auditing and Assurance Standards Board (IAASB) and IFRS 9 (Financial Instruments Recognition and Measurement).

3.11 Consumer Protection

3.11.1 Complaints Management and Resolution

The Bank received 1,183 complaints from consumers during the review period, a decrease of 19.69 per cent compared with 1,473 received in the first half of the year. The number of complaints against commercial and merchant banks was 1,145 or 96.79 per cent, while those against other financial institutions (OFIs) and miscellaneous complaints totaled 38 or 3.21 per cent. The complaints were on ATM and e-payment-related issues, excess charges, dishonoured guarantees, dishonoured cheques, fraudulent withdrawals and deposit irregularities.

A total of 928 complaints were resolved in the period under review compared with 1,157 resolved in the first half of the year, this represented a decrease of 229 or 19.79 per cent. The total refunds to customers in the second half of 2016 was ₦16.64 billion and $3.35 million compared with ₦4.63 billion, $80,415.46 and €19,263.62 refunded at end-June 2016.

3.11.2 Compliance Examination

The Bank conducted compliance examination of banks and other financial institutions during the review period to ascertain their level of compliance with policies, guidelines and directives. The examination revealed substantial compliance with regulations. However, some observations were made and had been communicated to the affected banks for corrective actions.

3.11.3 Consumer Protection Framework

The Bank in collaboration with Consumer Protection Council, NDIC, the SEC and relevant stakeholders has developed and issued the *Consumer Protection Framework (CPF)* to the industry. The objective of the Framework is to provide context and direction for financial consumer protection in Nigeria.

3.11.4 Financial Literacy Activities

Highlights of the activities carried out within the review period are:

a) Curriculum Development Project

The CBN in collaboration with the Nigerian Educational Research and Development Council (NERDC) and some development partners carried out the following activities in line with the implementation priorities of the National Financial Literacy Framework:

i. Developed a stand-alone curriculum for Basic Education and Senior Secondary Schools;
ii. Conducted a Workshop for the infusion of the stand-alone Financial Education Curriculum for Basic Education and Senior Secondary Schools in Nigeria into existing career subjects;
iii. Conducted the Critique and Editorial Workshops for the infused Financial Education curriculum into the Basic and Senior Secondary Schools Curricula.

b) Reach-out and Mentoring Programme

The Bank, in collaboration with the Bankers Committee and other stakeholders celebrated the World Savings Day on October 31, 2016. In the review period, 26,294 students from 235 secondary schools across the six geopolitical zones of the country were involved in the Financial Education Programme organised by the CBN, banks and NGOs.

c) Financial Literacy and Consumer Protection Sensitization and Mass Awareness Programme

The Bank carried out a sensitization campaign on financial literacy, tagged CBN Fair, in 8 state capitals namely, Birnin-Kebbi, Sokoto, Uyo, Enugu, Yenagoa, Benin City, Makurdi and Lafia.

d) Targeted Financial Education Programme for MSMEs and Farmers

Under its Financial Education Programme, the Bank in collaboration with GIZ[8] conducted a train-the-trainers programme for MSMEs and farmers. The modules covered in the training

[8] Deutsche Gesellschaft fur Internationale Zusammenarbeit (German Society for International Cooperation)

included: Needs and Wants; Record keeping and Cash flow management; Savings & Savings group formation; and Borrowing (Loans).

4.0 PAYMENTS SYSTEM

4.1 Developments in the Payments System

In order to ensure a safer and more efficient payments system in Nigeria, the Bank recorded significant improvements in the following areas:

4.1.1 Update on the Bank Verification Number (BVN) Scheme

At end-December 2016, 27,689,678 individuals had been registered in the BVN database and 39,312,797 accounts linked with BVN out of 60,878,449 active customer bank accounts.

The Bank undertook the following during the review period:

i. BVN enrolment for Nigerian bank customers in diaspora and security personnel on special assignment was extended till end-December 2016. This was to enable them participate in the registration exercise bearing in mind the peculiar nature of their challenges.

ii. Savings Account Customers with BVN were allowed to deposit cheques not more than ₦2 million in value into their accounts, per customer, per day.

iii. The Bank exposed a draft Framework to stakeholders for watch-listing any fraudulent customer in the banking industry using the BVN database.

The implementation of BVN has impacted positively in ensuring the safety of the Nigerian Payments System. Law Enforcement Agencies continued to leverage on BVN to fast-track investigation of financial and other related crimes while other stakeholders used it as credible means of customer identification and authentication.

4.1.2 Nigeria electronic Fraud Forum

The Nigeria electronic Fraud Forum (NeFF) developed a framework for the operation of a dedicated e-Payment and Card Crime Unit of the Nigerian Police. The Forum collaborated with the Nigeria Communications Commission to address cases of call diversion due to SIM swap, fraudulent SMS alert and SIM registration loopholes to minimise electronic fraud.

4.1.3 Migration from Merchant Service Charge to Interchange Fee Regime

To enhance card issuance and utilization, through increased investment in network infrastructure, a guideline to migrate the payment card operators from Merchant Service Charge to Interchange Fee Pricing regime, effective May 2017, was issued in December 2016. Under the new arrangement, merchants and acquirers will henceforth negotiate the merchant service charge, while the CBN will control the interchange fees paid by the acquirer to the card issuer and other regulated service providers.

4.1.4 Nigeria Automated Clearing System

In its effort to increase the efficiency of cheque clearing, the Bank in collaboration with NIBSS and other stakeholders upgraded the Nigeria Automated Clearing System (NACS) to support near real-time online processing of clearing instruments and enhance central image archiving. The upgrade would facilitate reduction in cheque clearing cycle from the current T+1 to T+0, and express clearing.

4.1.5 Licensing of Payment System Participants

Two (2) Payment Terminal Service Providers (PTSP), one (1) mobile money operator and two (2) Payment Solution Service Providers (PSSP) were licensed, bringing the total of PTSPs, mobile money operators and PSSPs to 18, 22 and six (6), respectively. As at end-December 2016, there were also three (3) Card Schemes, seven (7) transaction switching companies and three (3) third party processors in operation.

Table 4. 1: Licensed Payment System Participants

License -Type	Number	
	June 2016	Dec 2016
Card Schemes	3	3
Mobile Money Operators	21	22
Payment Solution Service Providers	4	6
Payment Terminal Service Providers	16	18
Transaction Switching Companies	7	7
Third Party Processors	3	3
Total	**54**	**59**

4.2 Payments System Vision 2020

Under this initiative, the CBN, in collaboration with the SEC, issued Guidelines on Securities Settlement in Nigeria. The main aim of the guidelines was to ensure competitive, efficient, safe and sound post trading arrangements which will lead to greater confidence in securities market and enhance investor protection.

4.3 Large Value Payments

The volume and value of inter-bank fund transfers through the CBN RTGS System increased to 612,843 and ₦188,273 billion at end-December 2016 from 546,283 and ₦183,365 billion at end-June 2016, representing an increase of 12.18 and 2.68 per cent, respectively. The increase was largely attributable to bulk upload of government payments through the System.

4.4 Retail Payments

4.4.1 Electronic Transactions

The volume of electronic transactions rose to 538,080,841 at end-December 2016 from 403,648,266 at end-June 2016, while the value increased **to ₦40,457.79 billion** at end-December 2016 from ₦30,618.06 billion at end-June 2016. The increase of 33.30 per cent and 32.14 per cent in volume and value, respectively, reflected the growing public confidence in the system as a result of the convenience of electronic transactions and CBN sensitization.

Table 4. 2: Electronic Transactions

Payment Channel	Number of Terminals		Number of Transactions		% Change (Volume)	Value ₦' Billion		% Change (Value)
	June 2016	Dec 2016	Jun-16	Dec-16		Jun-16	Dec-16	
ATMs	17,083	17,398	261,180,873	329,058,061	25.99	2,204.49	2,783.65	26.27
POS	121,388	112,847	25,337,605	38,377,598	51.46	308.47	450.52	46.05
Mobile	-	-	22,735,523	24,317,729	6.96	303.53	453.37	49.37
Internet (Web)	-	-	5,386,431	8,701,816	61.55	57.97	74.39	28.32
NEFT			13,009,783	16,744,399	28.71	5,799.40	8,785.41	51.49
NIP			56,318,341	97,298,109	72.76	16,365.26	21,743.80	32.87
e-Bills Pay			508,169	518,717	2.08	149.04	190.37	27.73
REMITA			18,175,450	20,074,436	10.45	5,328.84	5,323.65	- 0.10
NAPS			996,091	2,989,976	200.17	101.06	652.63	545.78
Total			**403,648,266**	**538,080,841**	**33.30**	**30,618.06**	**40,457.79**	**32.14**

4.4.1.1 Instant Payments

The growth of instant payments continued during the review period as volume and value increased to 97,298,109 and ₦21,743.80 billion in the second half of 2016 from 56,318,341 and ₦16,365.26 billion, in the first half of 2016, respectively. The increase was due to customers' preference for instant settlement.

4.4.1.2 Point of Sale Transactions

During the review period, the volume and value of Point of Sale (PoS) transactions increased to 38,377,598 and ₦450.52 billion at end-December 2016 from 25,337,605 and ₦308.47 billion at end-June 2016, representing an increase of 51.46 and 46.05 per cent, respectively. The increase was attributed to the growing number of merchants that accept POS payments, incentives programmes and better network availability.

4.4.1.3 Mobile Payments

The volume and value of mobile payments increased from 22,735,523 and ₦303.53 billion at end-June 2016 to 24,317,729 and ₦453.37 billion at end-December 2016, representing an increase of 6.96 and 49.37 per cent, respectively. The improvement was due to the growing public awareness of the system.

4.4.2 Cheque Clearing

The volume and value of cheques increased to 5,988,042 and ₦2,934.76 billion at end-December 2016 from 5,731,805 and ₦2,894.79 billion at end-June 2016, reflecting an increase of 4.47 per cent and 1.38 per cent, respectively.

5.0 OUTLOOK

Global economic recovery is expected to be moderate in the near to medium term as the impact of risks associated with declining commodity prices, uncertainties concerning the policies of the incoming US administration, the Brexit vote, negative interest rates in the Euro Area and Japan and the rebalancing in China tapers off. World output growth is expected to pick up in 2017 at 3.4 per cent and to 3.6 per cent in 2018. Financial markets may however, continue to be sensitive to disruptions in prices.

In Nigeria, notwithstanding the US rate hikes which might lead to outflow of some investments and further depreciation of the naira with pass-through to domestic prices, the projected gradual recovery in global oil prices, increased crude oil production, passage of the 2017 budget as well as the implementation of the National Economic Reconstruction and Growth Plan, are expected to spur economic activities and reverse the current recession in the domestic economy. Consequently, Nigeria's economy is expected to move out of recession to an output growth[9] of 0.8 per cent in 2017 and 2.3 per cent in 2018.

The resilience of the financial system is expected to be enhanced with the continued application of sound macro and micro prudential policies. Specifically, the Bank will strengthen macroprudential stress testing and supervisory colleges to enhance the regulation and supervision of cross-border banking entities. The revised D-SIBs Guidelines will further improve the surveillance and prudential regulation of systemic institutions. Also, the Watch-List Framework for fraudulent customers, review of the Cybercrime Prohibition Act 2015 and the collateral management framework are expected to reduce settlement risk and improve the efficiency of the payments system.

In general, proactive monetary and financial policies that will ensure macroeconomic stability will constitute the Bank's main focus.

[9] World Economic Outlook, October 2016

ACKNOWLEDGEMENTS

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