Zenith Economic Quarterly

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SOVEREIGN WEALTH FUND:

A Development Imperative For Nigeria?

INSIDE

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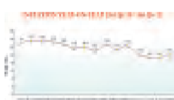
Nigeria: From Excess Cash To 'Cashless' Economy

Contents



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Set for the Rainy Day

Savings and investments have been considered as two critical macro-economic variables for achieving price stability and promoting employment opportunities thereby contributing to sustainable economic growth of nations. But the challenge of achieving substantial savings to drive investment has remained a consistent policy dilemma to governments whether in developed or developing economies.

Over the years, various regimes in diverse jurisdictions have attempted addressing this fundamental developmental conundrum in creative ways, including the creation of what is now popularly known as sovereign wealth fund. A sovereign wealth fund (SWF) is a state-owned investment fund (composed of financial assets) that could be invested globally, and the resultant proceeds applied to drive economic development. Many developing economies with huge natural endowment have since taken this route, piling up 'windfalls' from the sales of their natural resources into their SWFs. Nigeria has been one of the few exceptions in this practice, especially among members of the Organization of Petroleum Exporting Countries (OPEC).

Indeed, the absence of an institutional framework to manage the proceeds of crude oil earnings from highly volatile income stream has since left Nigeria to the mercy of cycles of 'booms and busts'. Thus, in our article: "Sovereign Wealth Fund: Development Imperative for Nigeria?" the author says the SWF is an all encompassing fund that seeks to serve as a stabilizer, a guarantee fund for future generations, and a ready fund for infrastructural development.

Still on the Nigerian economy, the impending transformation in the payments system is analyzed under the rubric: "Nigeria: From Surplus Cash to 'Cashless' Economy". In it, the writer posits that the road ahead could be a long one with twists and turns, and calls for a lot of awareness creation for all stakeholders. In the final analysis and in keeping with global trends, going 'cashless' is the direction the economy must take, the author sums up. And in the unending concern for housing challenge in the land, we have a piece on "An Appraisal of Mortgage as Security for Bank Lending in Nigeria". The authors hold that the utmost desirability of mortgage transactions to banks cannot be denied as they yield a huge proportion of bank profits through interest rates, warning however that this attractiveness is watered down by the problems identified in their study.

Indeed, the absence of an institutional framework to manage the proceeds of crude oil earnings from highly volatile income stream has since left Nigeria to the mercy of cycles of 'booms and busts'.

On the global scene, the snowballing of the sovereign debt imbroglio of Greece into a potent threat to the very existence of the European Union and its currency, the Euro, is becoming real by the day. Thus, in one article: "European Debt Crisis: Beyond the Concerns for Greece", the author states that confronted with the current realities, financial institutions and governments with huge exposures to Greece are compelled to make provisions for the worst possible outcomes. Yet in another discourse titled "Greece is the World…", the writer says "the end is inevitable for Greece; it is just a question of how long the life support mechanism of continuous cash injection from the European Central Bank can continue."

Other articles that make up this edition include those on quality and internal control in banks, the take-off of the economic management team in Nigeria, microfinance framework in Nigeria, and figures and charts on the economy.

Indeed, you have another full package for the discerning mind!

Marcel Okeke

from our mailbox

I wish to personally acknowledge with thanks, your letter of 30 September 2011, with which you sent a copy of the July Edition of the Zenith Economic Quarterly (ZEQ), which focuses on the "options for improving the people's wellbeing". The informative magazine is a useful journal in advancing the frontiers of governance, as it provides invaluable, well researched and thought out perspectives and insights on topical economic and socio-political issues, policies and trends.
Best Regards.
Amb. S.S Yusuf
High Commissioner
High Commission of the Federal Republic of Nigeria, Pretoria South Africa

I wish to acknowledge the receipt of various editions of your publications, the Zenith Economic Quarterly (ZEQ) which are as follows:

1. Vol. 2/11 July 2007
2. Vol. July 2008
3. Vol. 3/4 Oct 2008
4. Vol. 4/1 Jan 2009
5. Vol. July 2009
6. Vol. Oct 2009
7. Vol. 5/4 Oct 2010

These journals have gone a long way towards enriching our library collection with the wealth of information they contain, particularly in the area of the Nigerian and global economies. We would appreciate if the NIPSS library could be placed permanently on your distribution list.

Your donation of these publications are highly appreciated.
Florence Adejumo (Mrs.)
Head, Acquisitions section
National institute (for Policy and Strategic Studies) Kuru, Plateau State

I write to acknowledge with thanks the receipt of the above document via your letter dated 30th September, 2011. The ZEQ have been well written and the layout of the journal is excellent. It will indeed contribute to knowledge and serve as a good reference and research material for the University Library and our Departments of Economics, Accounting and Finance. Once again, we thank you for your interest in the University. With warm regards and best wishes.
Yours sincerely,
Professor Isaac A. Adeyemi
Vice-Chancellor, Bells University of Technology, Ota, Ogun State

Your letter dated 30th September, 2011 refers. I am directed to acknowledge receipt of a copy of the July, 2011 edition of the Zenith Economic Quarterly (ZEQ).

We appreciate the classic expertise treatment given on the topic "Option for improving the people's wellbeing". They are very interesting and educative. More grease to your elbow. We hope to continue to receive more of such quarterly from you.
Thanks.
L.N. Nzenweokwu (Mrs.)
For: Director/Chief Executive, Electronics Development Institute (ELDI) Anambra State.

I am directed to acknowledge the receipt of your letter (with a copy of ZEQ), dated September 30, 2011 with thanks. The Zenith Economic Quarterly Magazine was found to be very educative and interesting, especially the reports on Nigeria Economic Growth Indicators; "Guidelines on points of sale (POS); Nigeria Economy: options for improving the people's wellbeing, and towards energy sufficiency in Nigeria."

These articles keep Nigerians in the diaspora and the Mission's staff abreast with Nigerian economic development. Coupled with other monetary and financial policies matters featured in the magazine, readers were fed with relevant information to make projections on the Nigerian economic terrain. The Mission and Australian businessmen and students will find the magazine a good reference source on the Nigerian Economy.

Thanks for including the Nigeria High Commission, Canberra among beneficiaries of this educative and handy reference source.
Warmest regards,
S.K. Bada
Minister Political & Information, High Commission of the Federal Republic of Nigeria, Canberra, Australia

We hereby acknowledge receipt of a copy of the July, 2011 edition of the Zenith Economic Quarterly (ZEQ) with thanks.

It is rich, topical and highly informative.

Please accept our compliments.
Yours faithfully,
For: National Engineering & Technical Co. Ltd.
Engr. L. O. Binitie-Cassidy
Managing Director
National Engineering & Technical Co. Ltd, Lagos

We acknowledge with thanks the receipt of a copy of the July 2011 edition off the Zenith Economic Quarterly (ZEQ).

It is an invaluable addition to our journal collection. Please continue to put us in your mailing list.

Once more, thank you very much.
Yours faithfully
Mrs. M. J. Igben CLN
Serials Librarian
For: University Librarian
Office of the University Librarian
Rivers State University of Science and Technology, Port Harcourt

I wish to acknowledge with thanks the receipt of a copy of the July, 2011 edition of the Zenith Economic Quarterly (ZEQ).

The President and entire members of Nigerian

Medical Association (NMA) commend your efforts on this publication, which focuses on the Nigerian and global economy for strategic decisions. The contents are vey interesting and educative.
Accept our due regards.
Dr. B.M. Audu
Secretary-General
Nigerian Medical Association, Abuja

With reference to your letter dated September, 30th 2011 on the above underlined subject matter. I have been directed to write and acknowledge the receipt of your quarterly journal.

The Journal is very relevant and educating; we appreciated your gesture and hope to continue.
Thanks for your usual cooperation, Please.
Manga Modi Aliyu
For: Hon. Commissioner
Government of Bauchi State
Ministry of Commerce and Industry, Bauchi

I am directed to acknowledge with thanks, receipt of your letter dated 30th September, 2011, forwarding a copy of the July, 2011 edition of the Zenith Economic Quarterly (ZEQ). The High Commissioner finds the journal quite informative and is highly appreciative of your gesture.

Please accept the assurances of the Acting High Commissioner's highest regards.
P.N. Enebeli-Ndukuba
Admin Attaché
For: Acting High Commissioner, Nigeria High Commission, Singapore

I am directed to acknowledge with thanks, receipt of the July, 2011 edition of the Zenith Economic Quarterly (ZEQ), which focuses on the "options for improving the people' wellbeing.
Warmest regards.
Beatrice Ikeku-Thomas (Mrs.)
For: Ambassador/ Permanent Representative

I wish to acknowledge, with gratitude, the receipt of the above mentioned document forwarded under the cover of your letter dated 30th September 2011. Once again, may I congratulate you for putting together such a historic document of tremendous value...

Please accept the assurances of my highest consideration and esteem.
Yours sincerely,
Ambassador (Chief) V.N. Chibundu, IOM, FCIS, FNIM Founder/Chairman, Hon. DG (IBC), Nigeria-China Friendship Association, Lagos

I acknowledge with thanks, receipt of complementary copy of your Zenith Economic Quarterly (ZEQ) for the month of July, 2011 Edition sent to the Economic Adviser/Vice Chairman, State Planning Commission, Calabar.

I am impressed with the economic analysis and critical information provided for national and global policy decisions in your magazine. It is a good reference material. Well done!
Thank you.
Ndem Ayara
State Planning Commission
Government of Cross River State

NIGERIA: Economic Team Takes Off, SUSTAINS STABILITY

*By Marcel Okeke

Composing the economic management team (EMT) of the Federal Government of Nigeria with the erstwhile Managing Director of the World Bank Dr. Ngozi Okonjo-Iweala who is also the Minister of Finance as its head was a major feature of the third quarter 2011. The high-level committee which draws membership from top industrialists, bankers, technocrats, bureaucrats and the academia is saddled with driving the transformation of the Nigerian economy. The quarter under review was also marked by tortuous negotiations between the Federal Government and the state governors regarding the structure and take-off of the Sovereign Wealth Fund (SWF); debates over full deregulation of the downstream oil sector (petroleum subsidy removal); upward review of electricity tariffs as well as the fallout of minimum wage implementation for civil servants in most states of the country.

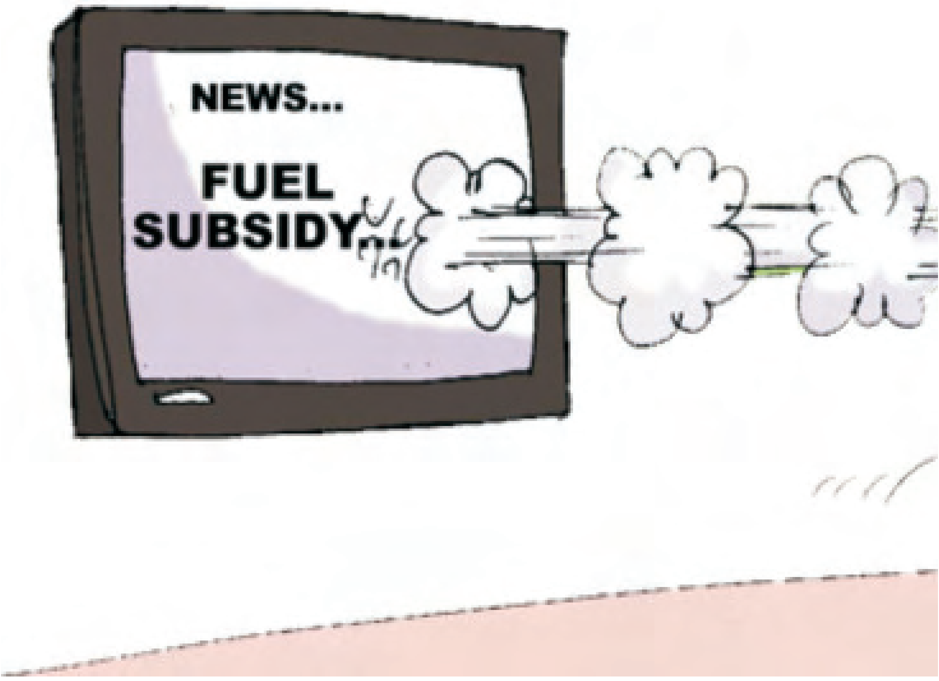
Efforts at the privatization of the Power Holding Company of Nigeria (PHCN); reforms in the agric, banking and oil sectors, among others, also continued to be key features of the economy during the period under review. There was also the volatility in oil prices in the international market, even as Nigeria's oil production continued to improve during the period due, mainly, to the relative peace in the Niger Delta region of the country. Ironically, the quarter closed with a decline in Nigeria's crude oil export, from 2.231 million barrels per day (mbpd) in August to 2.069 mbpd in September—both levels staying yet below the 2011 budget benchmark oil price of 2.30 mbpd. It should also be noted that a substantial part of oil production (about 40 per cent) has been taking place in the deep offshore wells; and based on subsisting terms agreed in the 1990s, royalty from oil wells deeper than 1,000 metres is zero per cent. And by extant practice, Nigeria is paid only 20 per cent of the profit made by oil companies after deducting their expenses. As a result of all these, the country has had limited benefits from high oil prices and rising output, with most of the gains going to multinational oil companies under the existing fiscal arrangement.

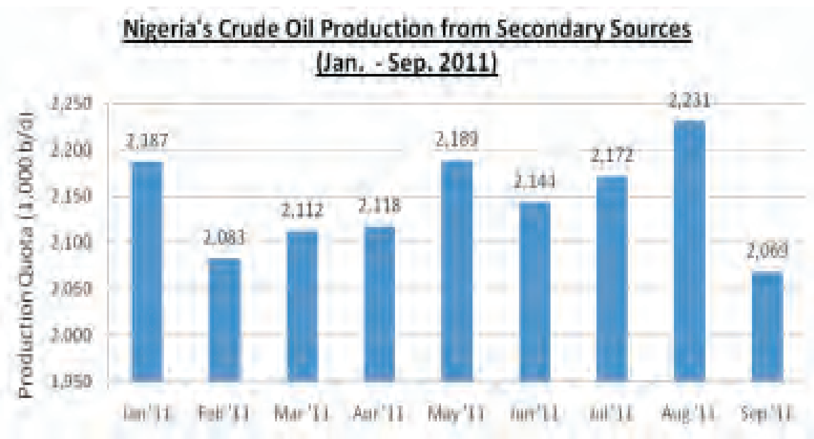
All these yielded mixed results in quantitative terms, with available data from the National Bureau of Statistics (NBS) showing that the Nigerian economy, measured by Real Gross Domestic Product (GDP), grew by 7.4 per cent in the third quarter 2011, as against 7.72 per cent growth in the previous quarter. This growth trend, according to the NBS, was largely driven by activities in agriculture, wholesale/retail trade, telecommunications, manufacturing and finance/insurance sectors. On the other hand, oil sector output recorded negative growth during the period, due to decline in oil production consequent upon some operational constraints faced by oil producing companies.

In a similar trend, the Composite Consumer Price Index (CPI) which measures inflation, stood at 10.3 per cent year-on-year at end-September 2011, up from the 9.3 per cent it attained the previous month. This inflationary trend had been consistently recognized by the Monetary Policy Committee of the Central Bank of Nigeria (CBN), which blamed it mainly on the public sector fiscal profile, particularly the high levels of recurrent expenditure as well as the structural bottlenecks in the Nigerian economy that perpetuate import dependence and make import demand highly inelastic.

This scenario of high import-dependence also played out so much in the importation and consumption of petroleum products, especially the motor premium spirit (PMS) on which the MPC has projected about US$6 billion subsidy in 2011 alone. This has translated into fast drawdown on the nation's external reserves. In fact, the MPC at its October 10, 2011 meeting expressed concerns about the genuineness of demand for petroleum imports. This year alone, according to the committee, oil importers have bought over US$7.0 billion from Wholesale Dutch Auctions (wDAS) of the foreign exchange market, thereby depleting the nation's external reserves. This demand, in the Committee's view, might have been fuelled by rent-seeking and subsidies.

The upshot of this has been pressure on the Naira exchange rate against the US dollar and other major currencies. In deed, the third quarter 2011 witnessed a significant depreciation in the value of the local currency in all segments of the foreign exchange market: official, inter-bank and the parallel markets. Again the MPC alluded to this scenario, when it said in its communiqué that the naira has come under increasing pressure, and has recently traded outside the band of N150 +/- 3.0 per cent. In the Committee's view, the increasing pressure on the

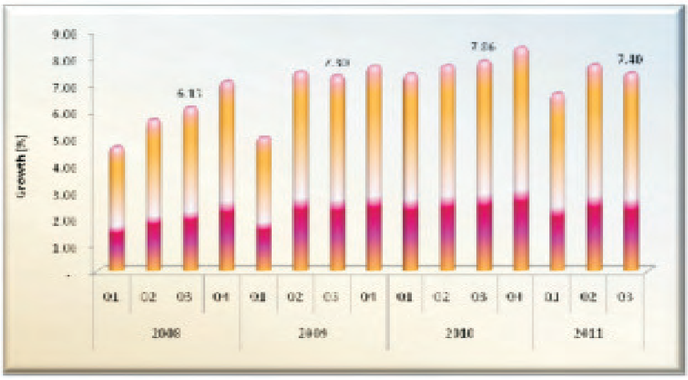




Source: OPEC

This scenario of high import-dependence also played out so much in the importation and consumption of petroleum products, especially the motor premium spirit (PMS) on which the MPC has projected about US$6 billion subsidy in 2011 alone.

Real GDP Growth Rate (Q1 2008 Q3 2011)



Source: **National Bureau of Statistics**

domestic currency has been emanating from a number of sources not all of which can be addressed by purely monetary interventions.

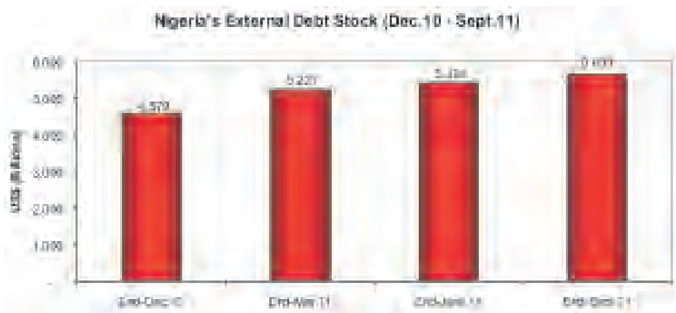
Available data show that the CBN in the bi-weekly WDAS, offered about US$9 billion and sold about US$9.2 billion, against the US$11.6 billion demanded during the period. Disturbed by the fate of the weakening Naira, the CBN moved to check speculative bids in the market by lifting restrictions it earlier placed on dollar purchase by Bureaux de Change (BDCs) and sold some US$10 million to all the banks operating BDCs. This notwithstanding, the nation's currency reached its lowest level in more than two years when it hit N159.42/US$ at the inter-bank market. In the parallel market, the Naira dropped to as low as N165/US$ at a point in July and remained in the region of N160/US$ all through the quarter.

The seemingly unbridled demand and utilization of the dollar impacted the external reserve such that, although it made some accretion of about US$4 billion in early August to hit US$35.90 billion at the close of the month, it still depleted to about US$31.70 billion by the close of the third quarter. Aside the huge cost of importation of petroleum products, Joint Venture Cash Calls (JVCs) and importation of other motley items also contributed to the decline in the reserves. But while the stock of external reserves was depleting, Nigeria's external debt has been inching up—standing at US$5.6 billion as at end-September 2011, according to the Debt Management Office (DMO). In deed, the local debt followed the same pattern, hitting N5.3 trillion, and bringing the nation's total public debt to US$39.72 billion at the end of the third quarter.

The DMO data indicate that the nation's external debt stock at end-September represents about three per cent of the GDP while the domestic component translates to 18 per cent of the GDP. However, the DMO figures show that large portions of Nigeria's external debt are soft loans in the form of World Bank's International Development Association (IDA) facilities (about 85 per cent of multilateral borrowings). For the CBN however, the Federal Government's burgeoning debt posses a challenge, because the FGN's domestic borrowing tends to crowed out the private sector. Thus, of the N5.3 trillion total domestic debt about N3.3 trillion is GFN bond (63 per cent), N1.6 trillion is Treasury Bills (30 per cent) and N353 million is Treasury Bonds (seven per cent).

In tune with the Federal Government's renewed interest in agriculture, support to the sector was significant during the period under review. Specifically, credit guarantee under the Agricultural Credit Guarantee Scheme of the CBN jumped up by a whopping 190.5 per cent over the level in the preceding quarter, to stand at

N3.553 billion covering 20,830 farmers at end-September 2011. Available data indicate that, with the exception of Bayelsa and Taraba states, all the other 34 states (plus the FCT) benefited from the scheme during the quarter. Report on the CBN's N200 billion commercial agricultural credit scheme also show that the apex bank had released the sum of N136.746 billion for disbursement to 173 beneficiaries as at the close of the third quarter. This is made up of 146 individuals/private promoters and 26 state governments that accessed N1.0 billion each. These state governments took the loans for on-lending to farmers' unions, co-operatives and financing of other areas of agricultural initiatives in their jurisdictions. Overall, 26 state governments are so far participating in the scheme which commenced in 2009.



Source: **DMO**

Also during the quarter under review, the Economic Management Team (EMT), rolled out an Agricultural Transformation Action Plan (ATAP) in pursuit of two goals namely employment generation and food sufficiency. The plan seeks to generate over 3.5 million jobs, and inject N410 billion into the economy, and enrich farmers with over N300 billion in the next four years. Further details of the plan show its key components as the development of areas of comparative advantage, value chain and cluster farming settlements in agricultural research and development, production, processing and marketing across the country. Crops to be given priority attention in their production in line with Nigeria's comparative advantage include rice, cassava, sorghum, cocoa and cotton among others.

Within the plan period, the policy is expected to increase rice production which currently stands at 3.4 million metric tons to 7.4 million metric tons; cassava production is to rise from 34 million metric tons to 51 million metric tons; sorghum from 9.3 to 11.3 million metric tons. Cocoa beans production is expected to rise from 250,000 to 500,000 metric tons; cotton lint from 20,000 to 140,000 metric tons while fertilizer supply is to be increased from 550,000 to 20 million metric tons. Prior to the roll out of ATAP, the CBN had introduced the Nigeria Incentive-based Risk Management System for Agricultural Lending (NIRSAL)—which is meant to deal with agric value chain financing challenges. Further to this, a framework has also been put in place to make banks finance the providers of seeds and fertilizers and agro-dealers under an 'interest draw back' arrangement.

THE CAPITAL MARKET

The dismal trend in the capital market since this year remained all through the third quarter 2011, with all market indices making heavy losses. The All-share Index (ASI) and market Capitalization finished the quarter at 20,373 and N6.49 trillion respectively, down from 24,980.20 and N7.98 trillion in the previous quarter. The creation of 'bridge banks' from the former Bank PHB, Spring Bank and Afribank and their prompt de-listing from the official list of the Nigerian Stock Exchange (NSE), partly aided in dragging the indicators downhill. Overall, the volume and value of traded securities fell by 21.5 and 15.5 per cent to 19.11 billion shares and N134.44 billion respectively, in 326,515 deals. This is compared with

Also during the quarter under review, the Economic Management Team (EMT), rolled out an Agricultural Transformation Action Plan (ATAP) in pursuit of two goals namely employment generation and food sufficiency.

http://womensmeetingplace.files.wordpress.com/2010/02/going-to-the-market1.jpg

24.35 billion shares valued at N159.1 billion, in 326,515 deals in the previous quarter.

Further breakdown of available data show that even with the delisting of some banks during the period under review, the banking sub-sector remained the most active on the NSE with a traded volume of 10.0 billion shares, valued at N74.3 billion, in 178,981 deals. This was followed by the conglomerates sub-sector with a traded volume of 54.7 million, valued at N2.14 billion in 13,830 deals. Apparently due to the prevailing investor sentiment about the market, no new issues were recorded during the period, but about seven supplementary issues were reported. Some of them include those of Unity Bank Plc, Smart Products Nigeria Plc, Great Nigeria Insurance Plc and Oando Plc. Others made bonus issues; they include Guarantee Trust Bank, Royal Exchange Assurance, Niger Insurance, PZ Cussons, Prestige Assurance, Union Ventures and Trans-Nationwide Express. The N50 billion Delta State 14 per cent series bond of seven years tenor was also issued and listed in the market during the quarter.

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On the other hand, the NSE took some disciplinary measures on a number of market players for alleged infraction of some market rules. Some of the stocks were placed on partial or full suspension for failure to submit their financial statements as at when due. And at a court-ordered meeting, shareholders of the Nigerian Bottling Company Plc approved the de-listing of the company from the NSE.

In the face of the generally poor performance of the market, the management of the Securities and Exchange Commission (SEC) and the Nigerian Stock Exchange (NSE) have been tinkering with a number of initiatives to buoy public confidence and improve patronage of the market. Specifically, during the third quarter 2011, the authorities came up with the 'market segmentation initiative' which will see the market move from three to two segments—equities and the bond markets. This will also involve shifting from 33 to 12 industry sectors in the equities market, and the reclassifying of listed companies within the 12 industry sectors. In pursuit of the demutualization of the NSE, the SEC set up technical committee to come with the modalities for achieving the objective. Demutualization entails some sort of 'liberalization' of the ownership/control of the stock exchange.

BANKING AND FINANCE

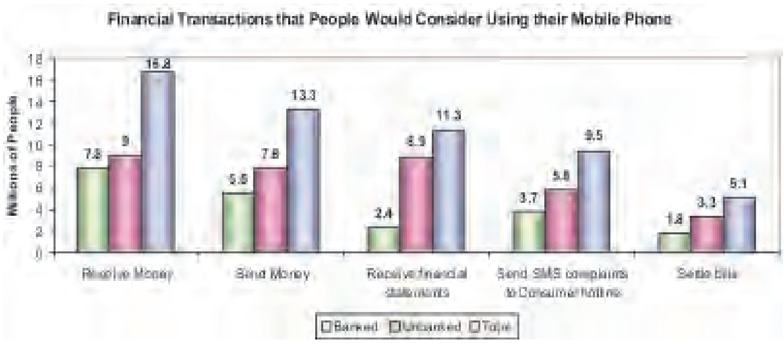
The third quarter 2011 saw a number of landmark developments in the banking sector of the Nigerian economy including the nationalization of three banks in August when it became apparent to the authorities that they would not be able to meet the recapitalization requirements by the stated September 30 deadline. Spring Bank, Afribank, and Bank PHB all had their licenses revoked, their names changed, and management replaced by the Asset Management Corporation of Nigeria (AMCON). These new 'bridge banks' are now known as Enterprise Bank, Mainstreet Bank, and Keystone Bank respectively.

About the same time as these policy initiatives, a flurry of re-licensing, mergers and acquisition deals also took place: Intercontinental Bank merging with Access Bank, Oceanic Bank merging with Econbank, Equitorial Trust Bank merging with Sterling Bank, and Finbank merging with First City Monument Bank. Wema Bank had to scale down its operations to become a regional bank, with lower capital requirement in line with the newly introduced banking model in the country. Union Bank on its part was granted recapitalization approval as its shareholders endorsed the injection of US$750 million by a group of private equity investors including African Capital Alliance. Other major deposit money banks in line with their growth strategies also acquired a few banks in some African countries and commenced operation in several other regions.

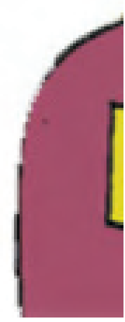
While all these were going on, the CBN on its part embarked on measures and initiatives to keep improving the effectiveness and efficiency of the banking system. In this regard it pursued the 'financial inclusion' strategy by licensing eleven mobile payment companies. They include Fortis Money, UBA/Afripay, GTBank Mobile Money, Pagatech, eTransact, Monetise, Eartholeum, Paycom, FET, Ecobank and Kudi. More organizations have also been licensed, including Zenith Bank Plc –which has come up with 'EASY MONEY' mobile product. And in jumpstarting the mobile payment initiative, a pilot implementation code-named 'Cashless Lagos' is to take off on January 1, 2012. In pursuit of this project, about 40, 000 Point of Sale (PoS) devices are being deployed within Lagos State to cater for settlement of transactions, according to the apex bank. This figure is expected to hit 150, 000 by end-December 2012, and further rise to 375, 000 by 2015. Six Payment Terminal Service Providers (PTSPs) have already been licensed by the CBN to deploy, maintain and support PoSs on behalf of the acquirers. The licensed PTSPs are: ValueCard, ETOP, ITEX, PayMaster, CitiServe and EasyFuel.

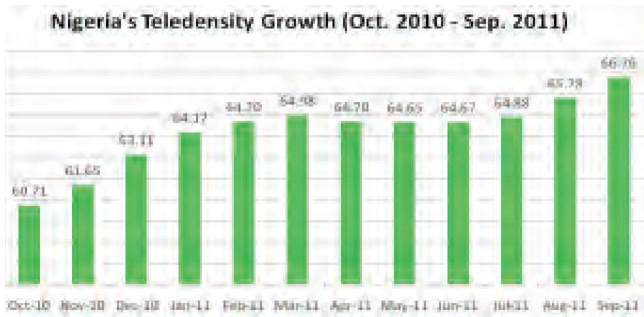
Alongside the mobile payment project, is the encouragement of the deployment of Automated Teller Machines (ATMs) to drive more cashless transactions—not necessarily for their traditional role of cash dispensing. The ATMs are now equipped to facilitate electronic payments of bills and account to account transfers. In pursuit

Alongside the mobile payment project, is the encouragement of the deployment of Automated Teller Machines (ATMs) to drive more cashless transactions—not necessarily for their traditional role of cash dispensing.



Source: EFInA





rce: Nigeria Communications Commission

of all these, especially the mobile payment, the CBN has also forged partnership with telecoms companies with the cooperation of the Nigerian Communication Commission (NCC).

Also in pursuit of the overall development of the industry, the CBN and the Bankers' Committee have embarked on what they termed the 'Industry Infrastructure Transformation Programme' otherwise known as the Shard Services Project in the banking sector. The project seeks to identify areas of collaboration within the banking industry towards achieving improved efficiency that will entail up to 30 per cent industry cost reduction. Under the project, five key areas have been identified for cost savings, namely cash management, payments system transformation, shared IT infrastructure and services, IT standards and industrialization and shared back office operations.

Further to all these, the apex bank in collaboration with the MICR Technical Implementation Committee also approved the accreditation and re-accreditation of 23 cheque printers under the Nigeria Printers Accreditation Scheme (NICPAS) for 2011. Some of the major printers chosen are Nigeria Security Printing and Minting Plc, Kalamozoo Secure Solutions Ltd (England), Security Print Solution (Durham), Smith & Ouzman Ltd (England), Camelot Ghana Ltd (Accra), Superflux International Ltd (Ikeja). Others are De-la Rue (South Africa), Shave and Gibson Group (South Africa), DLRS Group (Ireland), among others.

In further encouraging a 'cashless' environment and electronic payment solutions, the CBN also registered two organizations: Bankers Warehouse Limited and Integrated Cash Management Systems Limited to provide cash-in-transit and currency sorting services to the banking industry. And to encourage the banks to patronize these cash management services providers, the CBN ordered that deposits made with them for sorting will be given off-balance sheet treatment. In other words, the banks will be given value for the approved period of processing on a same-day basis as if the cash has been deposited in any CBN branch. Furthermore, the CBN will bear the cost of transportation of 'unfit' cash generated from processing as well as the volume of 'fit' notes the deposit money banks are willing to deposit with them.

Telecommunications

The third quarter 2011 was dominated by the feverish pitch of the registration of Subscriber Identity Module (SIM) cards which commenced in March throughout the country. Although the deadline was September 28, 2011, the Nigerian Communications Commission (NCC) eventually made it open-ended, as it extended the registration 'indefinitely' to give room for the collation and processing of the registration data. The SIM registration is

Despite this strong growth record in the mobile market, poor quality of service (QoS) as reflected in network coverage continued to hamper customer growth and service usage during the period under review.

http://www.management234.com/Telecom02.jpg

aimed at assisting security agencies in resolving crimes and by extension to enhance the security of the state. It is also intended to facilitate the collation of data by the Commission about phone usage in Nigeria as well as enable operators to have a predictable profile about the users in their networks. NCC could also use the data to effectively implement other value added services like Number Portability among others

As the registration progressed, most of the telecom companies keyed into it to boost their marketing and sales—almost all the networks embarked on incentive providing promos—offering huge rewards to prospective SIM card registrants. While some provided winners of the reward scheme the opportunity to migrate to 'new value propositions', others offered huge sums of money to the winners, plus adjusted tariff opportunity, offering airtime as low as 15 kobo per second. Yet others in addition to cash rewards, offered 'bonus credit' allowing their subscribers to call any network in the country and/or make free trips to major cities in various parts of the globe. All these incentive packages boosted the tempo of the SIM registration, by sustaining awareness and drawing existing and prospective SIM card owners to register.

All these were part of the growth momentum of the telecom sector during the quarter under review when total active telephone lines hit 93,461,436, up by 3.23 per cent from 90,533,178 as at the end of the second quarter. Also, teledensity rose to 66.76 in September 2011 from 64.67 as at end-June 2011, according to NCC figures. With this trend, telephony penetration in the country is fast nearing the 70 per cent mark, and the mobile GSM segment continues to dominate the entire telecom sector. As at the end of the third quarter, total number of active subscribers on the GSM segment was 87,417,508, accounting for 93 of the market, while the Code Multiple Division Access (CDMA) segment had 5,215,131 active subscribers, representing six per cent market share. This was also a drop from the 5,558,612 CDMA lines in June 2011. The fixed wired/wireless segment accounted for one per cent of the market with 828,797 in September, down from 881,393 as at end-June 2011.

Despite this strong growth record in the mobile market, poor quality of service (QoS) as reflected in network coverage continued to hamper customer growth and service usage during the period under review. Subscribers continue to be faced with the problems of none delivery of their short message service (SMS), drop calls, outright inability of subscribers to make calls, among others. It is believed however that much of these issues would be taken care of by mobile number portability—which will allow mobile users to change their service provider more easily.

(* Marcel Okeke is the Editor, Zenith Economic Quarterly)

CENTRAL BANK OF NIGERIA
MICROFINANCE POLICY FRAMEWORK FOR NIGERIA
APRIL 29, 2011

1.0 INTRODUCTION

1.1 In December 2005, the Central Bank of Nigeria (CBN) introduced a Microfinance Policy Framework to enhance the access of micro- entrepreneurs and low income households to financial services required to expand and modernize their operations in order to contribute to rapid economic growth. The rationale was that no inclusive growth can be achieved without improving access of this segment of the economic strata to factors of production, especially financial services.

1.2 The basis of this bold initiative in 2005 is still valid. With the benefit of experience spanning over five years of operating the Microfinance Policy, the CBN believes that a review of the Policy to reflect lessons from experience, global economic trends and the envisioned future for small business development in Nigeria has become auspicious.

1.3 Microfinance services refer to loans, deposits, insurance, fund transfer and other ancillary non-financial products targeted at low-income clients. Three features distinguish microfinance from other formal financial products: (i) smallness of loans and savings, (ii) absence or reduced emphasis on collateral, and (iii) simplicity of operations.

1.4 Before the emergence of Microfinance Banks (MFBs) under the Microfinance Policy, the people that were unserved or under-served by formal financial institutions usually found succour in non-governmental organization-microfinance institutions (NGO-MFIs), moneylenders, friends, relatives, credit unions, etc. These informal sources of funds have helped to partially fill a critical void, in spite of the fact that their activities were neither regulated nor supervised by the CBN. This revised policy framework continues to take cognisance of this category of institutions, which have now become key players in the Nigerian microfinance landscape. However, more emphasis would be placed on MFBs because they are under the regulatory and supervisory purview of the CBN.

1.5 The envisioned microfinance sub-sector under the policy regime recognises the existence of informal institutions and provides for their mainstreaming into the national financial system. The policy also seeks to harmonize operating standards and provide a strategic platform for the evolution of microfinance institutions particularly MFBs. Existing non-deposit taking service providers, which continue to operate outside the purview of regulation and supervision of the CBN, would be encouraged to make periodic returns on their operations for statistical purposes to the CBN.

1.6 This document therefore, presents a revised National Microfinance Policy Framework for Nigeria that would enhance the provision of diversified microfinance services on a sustainable basis for the economically active poor and low income households. It also provides appropriate machinery for tracking the activities of development partners and other non-bank service providers in the microfinance sub-sector of the Nigerian economy.

1.7 This revised policy is prepared in exercise of the powers conferred on the CBN by the provisions of Section 33 (1) (b) of the *CBN Act No. 7 of 2007* and in pursuance of the provisions of Sections 56-60 (a) of the *Banks and Other Financial Institutions Act [BOFIA] No. 25 of 1991* [as amended]. It should be read in conjunction with the MFB Operating Template and the revised Regulatory and Supervisory Guidelines for Microfinance Banks (MFBs) in Nigeria.

2.0 OVERVIEW OF MICROFINANCE ACTIVITIES (2006 – 2010)

2.1 The microfinance industry in Nigeria had been confronted by numerous challenges since the launch of the Microfinance Policy Framework in December, 2005. Coming on the heels of the banking sector consolidation, many of those adversely affected found their way into microfinance. Thus, a significant number of the newly licensed MFBs were established or operated like “mini-commercial banks”. Also, the erstwhile community banks (CBs) that converted to MFBs did not fare any better.

2.2 An assessment of the microfinance sub-sector, following the launching of the policy however revealed some improvements. These include increased awareness among stakeholders such as governments, regulatory authorities, investors, development partners, financial institutions and technical assistance providers on microfinance. Specifically, a total of 866 microfinance banks have been licensed, Microfinance Certification Programme (MCP) for operators of microfinance banks put in place and the promotional machinery beefed up. Accordingly, entrepreneurs are taking advantage of the opportunities offered by increasingly demanding for financial services such as credit, savings, payment services, financial advice and non financial services.

2.3 Despite the above development, a large percentage of Nigerians are still excluded from financial services. A study carried out by Enhancing Financial Innovation and Access (EFInA) in August, 2010 revealed that 39.2 million representing 46.3 per cent of the adults in

Nigeria, were excluded from financial services. Out of the 53.7 per cent that had access, 36.3 per cent derive their financial services from the formal financial institutions, while 17.4 per cent exclusively patronized the informal sector. Also, the results of the survey revealed that Nigeria was lagging behind South Africa, Botswana and Kenya with 26 per cent, 33 per cent and 32.7 per cent in financial exclusion rate, respectively.

2.4 Several factors have accounted for the persisting gap in access to financial services. For instance, the distribution of microfinance banks in Nigeria is not even, as many of the banks are concentrated in a particular section of the country, which investors perceived to possess high business volume and profitability. Also, many of the banks carried over the inefficiencies and challenges faced during the community banking era. In addition, the dearth of knowledge and skills in microfinancing affected the performance of the MFBs. Furthermore, there are still inadequate funds for intermediation owing to lack of aggressive savings mobilization, inability to attract commercial capital, and the non establishment of the Microfinance Development Fund.

2.5 In order to redress this unintended development, the Bank commenced a programme of capacity building, sensitization and awareness on the appropriate model for microfinance banking in December 2007. Maiden, Routine and Target Examinations, as well as nurturing and mentoring of the MFBs were also embarked upon during the same period to inculcate the microfinance concept and assist them to stabilize.

2.6 The impact of the global financial crisis of 2007/2008 on MFBs was more severe than anticipated. Credit lines dried up, competition became more intense and credit risk increased to the extent that many clients of MFBs were unable to pay back their loans owing to the hostile economic environment.

2.7 The banking sector reform of 2009 did not leave the MFBs unscathed as many of them experienced panic withdrawals by clients who were under the notion that if the Deposit Money Banks (DMBs) could have challenges, the MFBs would not fare better. The run on some of the MFBs was so severe that they had to close shop.

2.8 The combination of these factors significantly weakened the microfinance sub-sector and its ability to achieve its objectives. It is against this background that the 2005 Microfinance Policy was reviewed.

3.0 JUSTIFICATION FOR MICROFINANCE POLICY

The justifications for the introduction of the Microfinance Policy are as follows:

3.1 Weak Institutional Capacity

The prolonged sub-optimal performance of many erstwhile community banks, microfinance and development finance institutions is due to incompetent management, weak internal controls and lack of deposit insurance schemes. Other factors are poor corporate governance, lack of well defined operations, restrictive regulatory and supervisory requirements, among others.

3.2 Absence of Technological Platform

The absence of appropriate network platform for information communication technology (ICT) to drive down cost and achieve economies of scale is a major impediment to profitable operations.

3.3 Weak Capital Base

The weak capital base of existing microfinance institutions could not adequately provide cushion for the risk of lending to micro clients.

3.4 The Existence of a Huge Un-Served Market

The size of the un-served market by the existing financial institutions is large. EFInA, in its Access to Finance Survey in Nigeria in 2008, alluded to the fact that 79 per cent of the total population in Nigeria is unbanked out of which 86 per cent are rural dwellers. Also in 2005, the aggregate microcredit facilities in Nigeria accounted for about 0.2 per cent of Gross Domestic Product (GDP) and less than one per cent of total credit to the economy. This revealed the existence of a huge gap in the provision of financial services to a large number of the economically active poor and low income households. The effect of not addressing this situation appropriately would further accentuate poverty and slow down growth and development.

3.5 Poor Banking Culture and Low level of Financial Literacy

The primary aim of the microfinance initiative includes promoting inclusive financial system which entails creating sustained financial awareness. Therefore, the target clients for change are those people that equate microfinance with micro-credit and see banks and other fund providers not as partners in business, but mere sources of loans and advances.

3.6 Economic Empowerment of the Poor

Globally, micro, small and medium enterprises (MSMEs) are known to contribute to poverty alleviation through their employment generating potentials. In Nigeria, however, the employment generation potentials of small businesses have been seriously constrained by lack of access to finance, either to start, expand or modernise their present scope of economic activities. Delivering on employment generation and poverty alleviation by MSMEs, would require multiple channels of financial services, which an improved Microfinance framework should provide.

3.7 The Need for Increased Savings Opportunity

Poor people can and do save, contrary to generally held notions. However, owing to the inadequacy of appropriate savings opportunities and products, savings have continued to grow at a very low rate, particularly in the rural areas of Nigeria. The microfinance policy provides the window of opportunity and promotes the development of appropriate (safe, less costly and easily accessible) savings products that would be attractive to rural clients and improve the savings level in the economy.

3.8 The Increasing Interest of Local and International Investors in Microfinance

Many local and international investors have expressed interest in investing in the country's microfinance sub-sector. Thus, the establishment of a Microfinance Policy Framework for Nigeria provides an opportunity for them to participate in financing the economic activities of low income households and the economically active poor.

3.9 Urban Bias in Banking Services
Most of the existing banks are located in urban centres, and several attempts in the past at encouraging them to open branches in the rural areas did not produce the desired results. With a high proportion of the Nigerian population still living in the rural areas, it has become imperative to develop an institutional framework to reach the hitherto unserved population with banking services.

4.0 THE MICROFINANCE POLICY

4.1 Policy Objectives

The Microfinance policy provides a platform to achieve the following specific objectives:

i. Provision of timely, diversified, affordable and dependable financial services to the economically active poor;
ii. Creation of employment opportunities and increase the productivity and household income of the active poor in the country, thereby enhancing their standard of living;
iii. Promotion of synergy and mainstreaming of the informal Microfinance sub-sector into the formal financial system;
iv. Enhancement of service delivery to micro, small and medium enterprises (MSMEs);
v. Mobilisation of savings for intermediation and rural transformation;
vi. Promotion of linkage programmes between microfinance institutions (MFIs), Deposit Money Banks (DMBs), Development Finance Institutions (DFIs) and specialized funding institutions;
vii. Provision of dependable avenues for the administration of the microcredit programmes of government and high net worth individuals on a non-recourse basis; and
viii. Promotion of a platform for microfinance service providers to network and exchange views and share experiences.

4.2 Policy Targets

Based on the objectives listed above, the targets of the microfinance policy are as follows:

i. To increase access to financial services of the economically active poor by 10 per cent annually;
ii. To increase the share of microcredit as percentage of total credit to the economy from 0.9 per cent in 2005 to at least 20 per cent in 2020; and the share of microcredit as percentage of GDP from 0.2 per cent in 2005 to at least 5 per cent in 2020;
iii. To ensure the participation of all States and the FCT as well as at least two-thirds of all the Local Government Areas (LGAs) in microfinance activities by 2015; and
iv. To eliminate gender disparity by ensuring that womens access to financial services increase by 15 per cent annually, that is 5 per cent above the stipulated minimum of 10 per cent across the board.

4.3 Policy Strategies

A number of strategies were derived from the stated objectives and targets. They include:

4.3.1 **Licensing and Supervision**
The Bank shall license, regulate and supervise the activities of promoters and microfinance service providers that wish to become MFBs. In the light of experiences from the system thus far, the Bank shall ensure that all such licensed MFBs are adequately capitalised and operated in a safe and sound manner.

4.3.2 **Continuous Professional Development**
Professionalism, transparency and good governance shall be the bedrock of the microfinance sub-sector. Therefore, efforts shall be made to strengthen the skills of regulators, operators and directors of microfinance institutions. The establishment of institutions that support the development and growth of microfinance service providers and clients would be encouraged.

4.3.3 **Savings Mobilisation**
Attention will be paid to the promotion of savings and banking culture among low-income households, through Financial Literacy and Consumer Protection Programmes.

4.3.4 **Government Participation**
The participation of Federal, State and Local Governments in the system shall be promoted. This is by encouraging the three-tier of government to devote at least one (1) per cent of their annual budgets to microcredit initiatives, through a combination of moral suasion, advocacy and enlightenment, to be administered largely through MFBs.

4.3.5 **NGO-based Microfinance Institutions**
Non-deposit taking microfinance institutions shall continue their support to micro-enterprises and will be encouraged to render regular returns on their operations to the Bank primarily for statistical purposes. Those that attain the minimum regulatory capital requirements and clientele shall be encouraged and incentivised to transform to licensed MFBs.

4.3.6 **Collaboration with Development Partners**
There shall be collaboration and close monitoring of donors' assistance in the area of microfinance, in line with the provisions of this policy.

4.3.7 **Definition of Stakeholders' Role**
The roles of stakeholders in the development of the microfinance sub-sector are clearly defined in Section 8 of the Policy and efforts towards proper harmonization of these roles would be ensured.

4.3.8 **Submission of Disaggregated Data**
MFBs will be required to include disaggregated data in their periodic returns on the level of patronage of their products and services.

4.3.9 **Institutional Linkages**
The linkages among DMBs, DFIs, NGO-MFIs and MFBs as well as other micro-enterprise finance institutions would be institutionalized and strengthened to increase the flow of funds to clients.

4.4 Microfinance Policy Measures

As stated in Section 4.3.9, this Policy document recognises that there are various players in the microfinance sub-sector of the Nigerian economy. However, for deposit-taking institutions, there are strict prudential and regulatory requirements that must be complied with in order to be granted banking licence to operate as MFB.
These requirements are as follows:

4.4.1 **Microfinance Bank Categorization**
Microfinance Banks shall be required to be adequately capitalized, technically sound, and oriented towards lending based on cash flow and the character of clients. There shall be three categories of Microfinance Banks (MFBs).

4.4.1.1 **Category 1: Unit Microfinance Bank**
A Unit Microfinance Bank is authorized to operate in one location. It shall be required to have a minimum paid up capital of N20 million (twenty million Naira) and is prohibited from having branches and cash centres.

4.4.1.2 **Category 2: State Microfinance Bank**
A State Microfinance Bank is authorized to operate in one State or the Federal Capital Territory (FCT). It shall be required to have a minimum paid up capital of N100 million (one hundred million Naira) and is allowed to open branches within the same State or the FCT, subject to prior written approval by the CBN for each new branch.

4.4.1.3 **Category 3: National Microfinance Bank**
A National Microfinance Bank is authorized to operate in more than one State including the FCT. It shall be required to have a minimum paid up capital of N2 billion (two billion Naira), and is allowed to open branches in all States of the Federation and the FCT, subject to prior written approval by the CBN.

4.4.1.4 **Transformation Path**
i. A Unit MFB that intends to transform to a State MFB shall be required to surrender its licence and obtain a State MFB licence, subject to fulfilling stipulated requirements.
ii. A State MFB that intends to transform to a National MFB must have at least 5 branches which are spread across the Local Government Areas in the State. This is to ensure that the MFB has gained experience necessary to manage a National MFB. It shall also be required to surrender its license and fulfill other stipulated requirements.

The prescribed minimum capital requirement for each Category of MFB may be reviewed from time to time by the Central Bank of Nigeria.

4.4.2 **Ownership of Microfinance Banks**
i. Microfinance Banks can be established by individuals, groups of individuals, community development associations, private corporate entities, NGO-MFIs, or foreign investors.
ii. No individual, group of individuals, their proxies or corporate entities, and/or their subsidiaries, shall own controlling interest in more than one MFB, except as approved by the Central Bank of Nigeria.

5.0 PARTICIPATION OF EXISTING FINANCIAL INSTITUTIONS IN MICROFINANCE ACTIVITIES

5.1 Deposit Money Banks:
Deposit Money Bank (DMB) wishing to engage in microfinance services can continue to do so through a designated Department/Unit and/or offer microfinance as a financial product. Nothing prevents the Holding Company having a DMB as a subsidiary from investing in or owning an MFB.

5.2 Non-Governmental Organization-Micro Finance Institutions (NGO-MFIs):
This policy recognizes the existence of credit-only, membership-based microfinance institutions, which are not required to come under the regulatory and supervisory purview of the CBN. They are however supervised by the appropriate Ministry. Such institutions shall engage in the provision of microcredit to their targeted population but shall not mobilize deposits from the general public.
The registered NGO-MFIs shall be required to forward periodic returns on their activities to the CBN primarily for statistical purposes. NGO-MFIs wishing to obtain operating licences as Microfinance Banks shall be required to meet the stipulated provisions in the Regulatory and Supervisory Guidelines for MFBs in Nigeria.

5.3 Apex Associations of Microfinance Banks and Institutions
The CBN shall support apex associations of microfinance banks and institutions to promote self-regulation, uniform standards, transparency and good corporate practices. The associations shall also serve as platform for capacity building, product development and marketing, as well as resource sharing.

Transformation of the Existing NGO-MFIs and Financial Cooperatives:
An existing NGO-MFI or Financial Cooperative which intend to operate as MFB can either incorporate a subsidiary MFB while still carrying out its NGO operations or transform to a MFB. Such institutions must obtain operating licence and shall be required to meet the stipulated provisions in the revised Regulatory and Supervisory Guidelines for MFBs.

6.0 FRAMEWORK FOR THE SUPERVISION OF MICROFINANCE SUB-SECTOR

6.1 Licensing and Supervision of Microfinance Banks
The licensing of Microfinance Banks shall be the responsibility of the Central Bank of Nigeria. A licensed institution shall be required to add "Microfinance Bank" after its name. All such names shall be registered with the Corporate Affairs Commission (CAC), in compliance with the *Companies and Allied Matters Act (CAMA) 1990*. The licence issued by the CBN will indicate whether it is a Unit, State or National MFB.

6.2 Revised Regulatory and Supervisory Guidelines for Microfinance Banks
The Bank has produced a revised Regulatory and Supervisory Guidelines for the operations of Microfinance Banks in Nigeria. All operators and practitioners are expected to familiarize themselves with this document and comply with its provisions accordingly.

6.3 Minimum Operational Standards/Template for Microfinance Banks
The CBN has prepared a Template to guide the operators of the MFBs. This document provides guidance on corporate governance, business planning, products, services and risk management.

6.4 Establishment of the National Microfinance Policy Consultative Committee
The National Microfinance Policy Consultative Committee (NMFPCC) has been constituted by the CBN to give direction for

the implementation and monitoring of this policy. Membership of the Committee shall be determined from time to time by the CBN. The Development Finance Department of the CBN shall serve as the Secretariat to the Committee.

6.5 Credit Reference Bureau
In view of the peculiarities of microfinance practice, operators shall be required to provide and obtain credit information from Credit Reference Bureau(x) to aid decision making and minimise credit risk.

6.6 Rating Agency
The CBN shall encourage the establishment of private rating agencies to rate microfinance institutions.

6.7 Deposit Insurance Scheme
As a means of protecting depositors funds and reinforcing public confidence, MFBs shall qualify for the deposit insurance scheme of the Nigeria Deposit Insurance Corporation (NDIC).

6.8 Capacity Building Programmes
6.8.1 Microfinance Certification Programme
In order to bridge the technical skills gap, especially among operators and the directors of MFBs, the policy recognizes the need to set up an appropriate capacity building programme. In this regard, the CBN has put in place the Microfinance Certification Programme (MCP) to ensure the acquisition of appropriate microfinance operational skills by staff and management of MFIs in general and MFBs in particular.

In addition, provisions shall be made for Mandatory Continuing Professional Education (MCPE) to update relevant skills of the staff of each MFB in microfinance banking.

6.8.2 Staff Development Programme
Each MFB shall be required to make annual budgetary provision for staff development and capacity building.

6.8.3 Microfinance Development Fund and Capacity Building
The Microfinance Development Fund, when established, shall provide funds to support capacity building for the sub-sector on an ongoing basis.

6.8.4 Apex Associations and Capacity Building
Efforts shall be made to promote capacity building through the apex associations of the microfinance banks and institutions in collaboration with development partners.

6.9 Linkage Programme
The policy recognizes the importance of wholesale funds to microfinance institutions to enable them expand their outreach. Pursuant to this, the CBN shall work out the modalities for fostering linkages between DMBs, DFIs, specialized finance institutions, Donor Agencies and the MFIs in general and MFBs in particular, to enable the MFBs and MFIs source for wholesale funds and refinancing facilities for on-lending to their clients. Furthermore, MFBs and MFIs are charged, under this policy, to foster close linkages with Entrepreneurship Development Centres (EDCs) and micro-enterprises that operate as Self-Help Groups (SHGs).

6.10 Establishment of Microfinance Development Fund (MDF)
In order to promote the development of the sub-sector and provide for the wholesale funding requirements of MFBs and MFIs, a Microfinance Development Fund (MDF) shall be set up by the CBN.

The Fund, which shall be professionally managed to guarantee its sustainability, will provide necessary support for the development of the sub-sector in terms of refinancing/guarantee facility, capacity building, financial education, and other promotional activities. The Fund shall be established with a seed fund to be provided by the Federal Government and the CBN and operating fund through soft facilities from international development financing institutions, as well as multilateral and bilateral institutions.

6.11 Prudential Requirements
The CBN recognizes the peculiarities of microfinance practice and shall accordingly implement appropriate regulatory and prudential regime to

guide the operations and activities of the MFBs. Some of the prudential requirements are, compulsory investment in treasury bills, liquidity ratio, capital adequacy ratio, fixed assets/long-term investments, branch expansion, maintenance of capital funds, limit of lending to a single borrower and related party, maximum equity investment holding ratio, provision for classified assets, and unsecured lending limits, amongst others. The details are contained in the revised Regulatory and Supervisory Guidelines for MFBs in Nigeria.

6.12 Disclosure of Sources of Funds
MFBs shall disclose their sources of funds in compliance with the Money Laundering Prohibition Act 2004.

6.13 Corporate Governance for Microfinance Institutions
All MFIs shall adhere to basic corporate governance principles. The Board of Directors of MFBs shall be primarily responsible for the corporate governance of the bank by establishing strategic objectives, policies and procedures that would guide and direct the activities and the means to attain same, as well as the mechanism for monitoring Management s compliance.

6.14 Apex Associations of Microfinance Banks and Institutions
The CBN shall support apex associations of microfinance banks and institutions to promote self-regulation, uniform standards, transparency and good corporate practices. The associations shall also serve as platform for capacity building, product development and marketing, as well as resource sharing.

7.0 INCENTIVES FOR MFBs
The new window of opportunity to bring financial services to the under-served and un-banked in the rural areas shall require the support of government and the regulatory authorities.

7.1 Microfinance Development Fund will be established by the Government, CBN and other stakeholders to support the MFBs in rendering financial services to their clients on a sustainable basis. The Fund shall comprise two windows - Commercial and Social.

7.2 Subsidized training/capacity building programmes would be made available to staff of the MFBs.

7.3 The Interest Drawback Programme (IDP) of the CBN would be extended to the MFBs clients in agriculture and allied businesses.

7.4 The CBN in collaboration with relevant Ministries, Departments and Agencies (MDAs) as well as other stakeholders would provide enabling environment for MFBs/MFIs to operate.

8.0 THE ROLES AND RESPONSIBILITIES OF STAKEHOLDERS

The roles and responsibilities of respective stakeholders shall include, but not limited to, the following:

8.1 Government

Government shall be responsible for:

i. Ensuring a stable macro-economic environment, providing basic infrastructure (electricity, water, roads, telecommunications, etc), political and social stability;
ii. Creating an efficient land administration system to facilitate ease of transfer of land titles and other property rights to serve the collateral needs of borrowers and financial institutions;
iii. Promoting policy in support of consumer protection and financial literacy for microfinance clients;
iv. Setting aside an amount not less than one (1) per cent of its annual budgets at Federal, State and Local Governments levels for microcredit initiatives.

8.2 Central Bank of Nigeria (CBN)

The CBN shall:

i. Continue to oversees the operations of the National Microfinance Policy Consultative Committee;
ii. Ensure the implementation of the Microfinance Policy Framework to achieve the stated objectives, targets and strategies;
iii. Ensure the emergence of a sustainable microfinance sub-sector through appropriate institutional and regulatory and supervisory framework;
iv. Establish the Microfinance Development to provide wholesale funding for on-lending activities of Microfinance Institutions;
v. Develop and support appropriate capacity building programmes for regulators, directors, operators and practitioners in the sub-sector, in collaboration with other stakeholders;
vi. Promote financial literacy and consumer protection in partnership with relevant public and private sector development institutions as well as Civil Society Organisations (CSOs); and
vii. Undertake periodic reviews of the Microfinance Policy and the Regulatory Guidelines to address emerging issues.

8.3 Apex Associations of Microfinance Banks and Institutions

The Apex Associations of MFBs and MFIs shall:

i. Promote self-regulation;
ii. Ensure uniform standards, transparency and good corporate governance practices among their members;
iii. Provide platform for peer review, capacity building, generic product development and marketing, as well as resource sharing;
iv. Ensure that members render returns on their operations to the CBN; and
v. Work with other stakeholders for the promotion of financial literacy and consumer protection.

8.4 Public Sector Poverty Alleviation Agencies

This Microfinance policy framework recognises the roles of public sector MFIs and poverty alleviation agencies such as the National Poverty Eradication Programme (NAPEP), Small and Medium Enterprises Development Agency of Nigeria (SMEDAN), National Directorate of Employment (NDE) etc. in the development of the sub-sector. They shall be encouraged to play the following roles:

i. Provide non-commercial (social security) resources targeted at difficult-to-reach clients and the vulnerable group;
ii. Support capacity building for stakeholders;
iii. Nurture new MFIs to sustainable levels; and
iv. Collaborate or partner with other relevant stakeholders to achieve the objectives of this policy.

8.5 Donor Agencies and Development Partners

Donor Agencies and Development Partners that provide capital and support for the development of the microfinance industry in Nigeria shall be required to operate within the relevant provisions of this policy.

9.0 CONCLUSION

9.1 There exists a huge untapped potential for financial services at the micro level of the Nigerian economy. Attempts by Government in the past to fill this gap did not achieve the desired result.

9.2 The Microfinance Policy was therefore developed in 2005 to further address the observed gaps. The policy provides for the establishment of a private sector driven microfinance banks.

9.3 Achievements recorded in the microfinance sub-sector since 2005 have been mixed. While outreach by formal financial institutions increased from 35.0 per cent to 36.3 per cent, occasioned by the coming on stream of MFBs, the institutions have been confronted with numerous challenges, including, poor corporate governance and asset quality, weak internal control and risk management, amongst others. It is against this background, that the revision of the 2005 microfinance policy was undertaken.

9.4 The revised microfinance policy framework provides that MFBs shall be required to be adequately capitalized, better managed, run on low cost structure and be operated in a safe and sound manner.

9.5 The CBN shall continue to monitor and ensure a conducive policy environment for the conduct of microfinance activities and businesses in Nigeria.

29th April, 2011

European Debt Crisis: Beyond the Concerns for GREECE

By EUNICE SAMPSON

Two years on, the Greek debt crisis remains perhaps the most topical issue in the global economy, more so for the concern about a contagion in the eurozone which today seems more real than ever before.

The debt crisis in Greece has caused havoc in financial markets since news about it first broke in 2009. As 2011 sets to exit, market sentiments remain fragile, even though Greece' creditors are now better placed to make a fair estimate of the degree of loss they face should the debt default happen. Confronted with current stark realities, financial institutions and governments with huge exposures to Greece are compelled to make provisions for the worse possible outcomes.

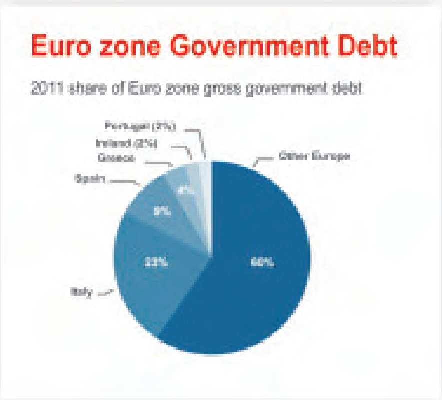
But the dangerous dimension to the crisis is the contagion in other economies, notably Italy and Spain. The eurozone economy may be able to withstand a bad Greek debt; especially since this constitutes just 4% of total sovereign debt in the region. But the prospect of a spill over to Italy and Spain which together control 32% of the eurozone government debt is an entirely different issue.

With more investors expressing their pessimism that an Italian and Spanish bailout is inevitable, global economic growth prospects hang in the balance. The situation in the United States which still struggles with record unemployment, indebtedness and fiscal deficits further complicates an already precarious situation. Beyond the problems in Greece, these are the new global fears as 2011 draws to a close.

The Greek debacle: still unresolved

Despite bailout efforts from eurozone leaders and the International Monetary Fund (IMF) since May 2010, the ghost of the Greek crisis is yet to rest. Markets around the world still quiver at any breaking

Confronted with current stark realities, financial institutions and governments with huge exposures to Greece are compelled to make provisions for the worse possible outcomes.



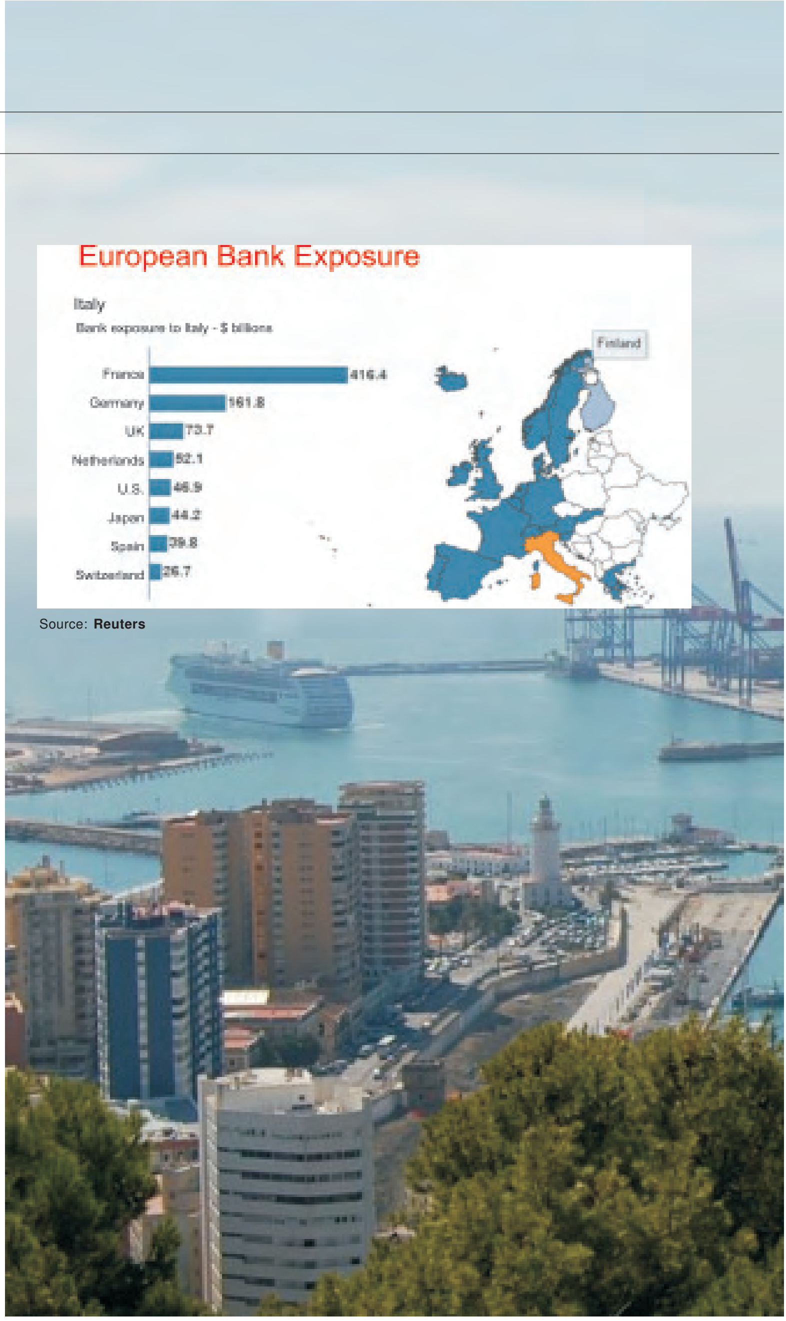
Source: **Reuters**

news on Athens. The latest being a major tumble on Tuesday November 1, after a Greek call for a referendum on the rescue package agreed by the 17 member eurozone leaders five days earlier.

Eurozone leaders meeting in Brussels on October 27 agreed a package of measures designed not just to tackle the Greek crisis but to avert an escalating debt burden in the monetary zone. In the terms of the deal, Greece would receive a new €130 billion rescue loan. In addition, 50% of the country's debt owed private creditors will be written off. The eurozone bailout fund will be increased to about €1 trillion (around $1.4 trillion); while European banks will be required to recapitalize by up to 9% to cushion the effect of the crisis in the zone.

In an unexpected twist, Greece Prime Minister George Papandreou on October 31 announced that the Greek people will be allowed to approve or reject the deal in a referendum expected to hold around January 2012. The move is seen as an attempt by the embattled Prime Minister to calm strained political nerves and appease a Greek people already nervous about the additional austerity burdens that are preconditions for the new deal. But it turned out to be a wrongly calculated move.

Despite all the noise about it, not many believe in the efficacy of the Greek bailout plan. For one thing, the severe austerity package that comes with it is throwing Athens deeper into recession. Short of helping to ward off default, the bailouts have not in any way improved the economic condition in Greece. While the EU leaders strive to ensure that Greece keeps servicing its loans, the country's low economic productivity and capacity, coupled with stringent fiscal tightening, all work against achieving any quick recovery.



Source: **Reuters**

http://www.worldcitypics.com/spain-malaga-castillo-gibralfaro/

From all indications, it could take another decade or more before Greece is able to completely shake off the debt hangover, even with massive international and regional support.

Greece' total debt burden is now put at around $500 billion, with over half held by private creditors, including banks, (especially German and French banks), insurers, mutual funds, pension funds, etc.

Who's next?

While the crisis in Greece remains unresolved, the prospects of similar predicaments in the bigger economies of Italy and Spain, not to mention threats also coming from Ireland and Portugal, are proving to be a handful for eurozone leaders. One troubling sign is the borrowing costs for Italy and Spain which have hit new highs, a signal that investors remain apprehensive about the countries' ability to pay. Analysts put the combined debt of Italy and Spain at over $3 trillions, at least five times more than what Greece owes.

Perhaps the major cause for worry currently is Italy. As market fears mount over its dwindling financial situation, Italian bond yields have hit the roofs, with the 10-year bond now attracting over 7%. The high cost of insuring the country's debt has further eroded market confidence. As cost of credit rises, so does the probability that the economy may default, since this constrains it from borrowing more to service existing debts.

With growth at a near standstill; September unemployment figure at 8.3%; and series of austerity measures being introduced to build market confidence and address huge deficits, there is really not much to cheer about in Rome right now.

As shown in the graph above, several European banks have enormous exposure to Italy, and a full blown financial crisis here would come with major consequences for financial services players. According to reports by Reuters, French banks are exposed to Italy up to $416.4 billion; Germany, $161.8 billion; UK, $74 billion; Netherlands, $52.1 billion; USA, $46.9 billion; Japan, $44.2 billion; Spain, $39.8 billion; Switzerland, $26.7 billion.

There are also growing fears of a credit crunch in Italy as banks struggle to meet higher capital ratios set by EU leaders following credit rating downgrades and higher interest rates. These have intensified pressure on Rome to act fast to address a deteriorating situation. In October, Italian leaders agreed to allow the IMF to monitor its policies and progress in this regard.

Spain also remains under close observation in the global financial market. With a 15-year high unemployment rate of 22% as at third quarter 2011, the highest among major economies; and with overall queue of the unemployed nearing the 5 million mark out of a 46 million population, Madrid is generating as much global concerns as Rome.

Considering the interdependence of the global financial system, the possibility of the feared contagion spreading beyond the common currency zone cannot also be ruled out. The United Kingdom, despite a decade of shunning the euro currency is also vulnerable. Data from the July 2011 stress test on European banks put total exposure of UK's three biggest banks to the troubled eurozone economies (Greece, Ireland, Italy, Portugal and Spain) at about €204 billion, a whopping 19 per cent of UK's GDP. The Royal Bank of Scotland alone is owed a total of €103.3 billion by these economies; Barclays's total exposure is €87.1 billion; and HSBC is exposed up to €14 billion. Should the financial crisis get out of hand, UK banks and the larger economy could be in serious danger. It is pertinent to note that the total exposure of these three banks far exceeds their total Tier 1 capital of €192 billion.

Source: **Reuters**

Spain Malaga
Castillo Gibralfaro

The pilling casualties

In the political front, two major casualties have emerged from the eurozone debt crisis – Prime Minister George Papandreou of Greece and President Sylvio Berlusconi of Italy.

On November 8, 2011, Greek Prime Minister Papandreou was forced to resign over his alleged unsatisfactory handling of the recent bailout plans. While most Greeks would vote any day against the harsh austerity measures that are preconditions for the bailouts, majority are unwilling for their country to exit the eurozone. The vote of no confidence passed on Prime Minister Papandreou on November 4 was the result of a perception that his call for a referendum was a threat to Greece's eurozone membership. Prime Minister Papandreou's announcement that he would bring the bailout decision up for a referendum ruffled feathers not just among Greek politicians and policy makers but also among EU leaders who 4 days before had reached what they believed was a winning deal for Athens. A new Prime Minister, Lucas Papademos, a former European Central Bank Vice President, has been appointed to replace him.

In Italy, President Sylvio Berlusconi resigned on November 12 after new austerity measures designed to cut public debt and government deficit were passed by Italian MPs. Berlusconi had been under pressure to resign first for his series of personal scandals and for an alleged mismanagement of the economy. A replacement for him, Mario Monti, a former EU Commissioner has assumed office.

In the financial services sector, Dexia bank of Belgium on October 10, 2011 became the first bank to go under as a result of the Greek debt crisis. With assets in excess of $700 billion, far bigger than the GDP of its home country, it is the biggest financial services failure since the 2008-2009 multiple banks' collapse. Dexia caved in under the weight of huge exposures to European sovereign debt, notably Greek bonds.

The failure and eventual bailout of Dexia bank by French and Belgian governments have raised questions about the credibility of the July stress test in Europe which gave the bank a clean bill of health and rated it the 12th healthiest bank in the EU.

Two days earlier, Denmark's Max Bank was nationalized after it claimed insolvency owing to huge exposures to the region's sovereign debt.

There are also growing concerns about the fate of regional banking titans including France's BNP Paribas with $2.7 trillion in assets, Credit Agricole with $2.1 trillion, Societe Generale with $1.5 trillion; and Italy's UniCredit with assets in excess of €929 billion; and several others. Though these banks had passed the stress test barely three months earlier, they are already showing signs of impending trouble owing to massive toxic assets from the prolonged eurozone crisis.

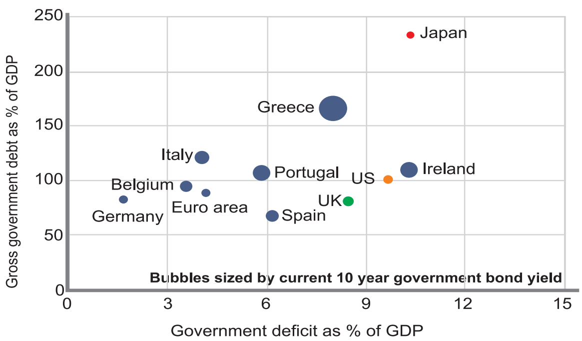
With five of its banks failing the stress test in July, if this counts for anything, Spain's financial services industry is also highly vulnerable. Spanish banks still struggling with the mortgage crisis and another possible round of credit crunch would be lucky to escape major failures during this crisis.

Outside the eurozone, on October 31, United States' MF Global Inc filed for bankruptcy citing over $6.3 billion of eurozone sovereign debt exposure. MF Global, a major financial derivatives broker had earlier shocked investors by reporting a $186 million loss for second quarter 2011. Fitch and Moody's quickly downgraded the

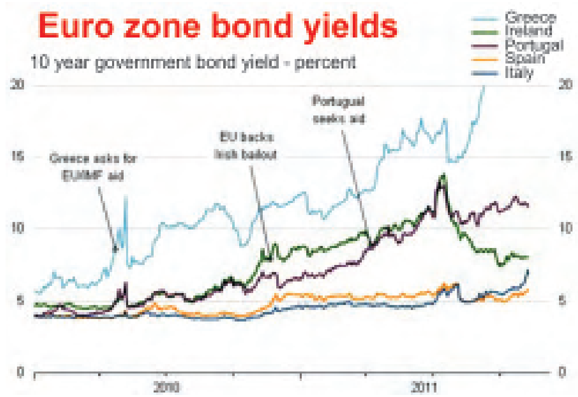
http://upload.wikimedia.org/wikipedia/en/4/4f/Berlaymont_building_european_commission.jpg

Picture of Berlaymont building, headquarters of the European commission

Government debt, deficits and bond yields



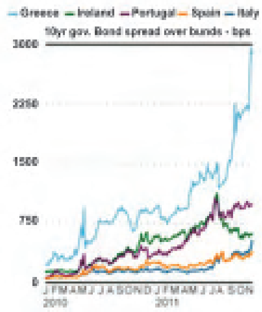
Source: **Reuters**



Source: **Reuters**

Euro zone credit ratings

Country	S&P	Moody's	Fitch	5yr CDS
Greece	CC	Ca	CCC	4,754
Ireland	BBB+	Ba1	BBB+	687
Portugal	BBB-	Ba2	BBB-	1,061
Spain	AA-	A1	AA-	310
Italy	A	A2	A+	427
Belgium	AA+	Aa1	AA+	238
Germany	AAA	Aaa	AAA	88



Source: **Reuters**

company's debt to "junk" status.

The bankruptcy filed by MF Global adds another twist to the whole eurozone saga, which now threatens to engulf other non - European financial institutions. MF Global is a leading broker of commodities and listed derivatives and one of 22 primary dealers authorized to trade U.S. government securities with the Federal Reserve Bank of New York. Its collapse signals the first serious US victim of the eurozone debt crisis, with implications for arms of the company around the world. The London office of MF global sent home about 700 employees of the firm following the announcement of the insolvency.

The failure of MF Global also has far-reaching implications for other financial services institutions in the US and Europe. The list of MF Global's 50 biggest creditors published along with the bankruptcy notice reveals United States' JPMorgan Chase Bank as its largest creditor, owed over $1.2 billion. Germany's Deutsche Bank also made the list, owed a total of $1.015 billion.

The eurozone debt crisis that started in Greece is not only claiming wider European casualties but victims outside the European continent.

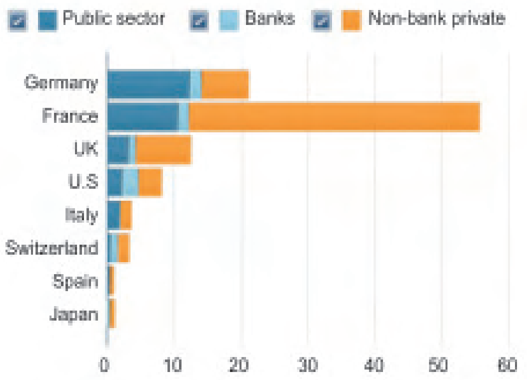
Eurozone: Outlook for 2012

With the monetary zone's unemployment figures reaching 10.2% in September, the highest level since the introduction of the common currency, the outlook for 2012 seems bleak. There are fears that the zone might be heading for a recession or at best an anemic growth this year and next.

The Organization for Economic Cooperation and Development (OECD) recently slashed its 2012 growth forecast for the eurozone, with a warning that the debt crisis means many members of the currency union

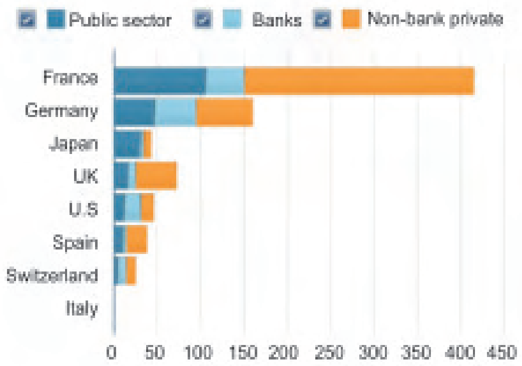
Bank exposure to Greece by type of debt

$ billions



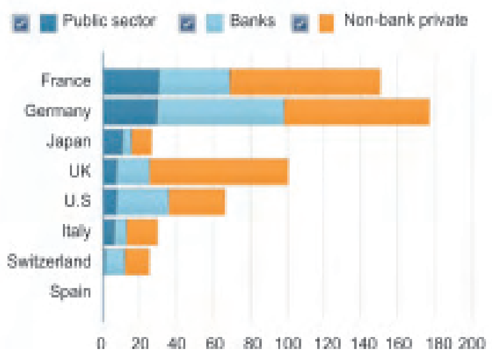
Bank exposure to Italy by type of debt

$ billions



Bank exposure to Spain by type of debt

$ billions



Source: **Reuters**

will shrink this year and next. The OECD now expects the zone to grow by a meager 0.3% in 2012, down from the 2% earlier forecast in May.

The OECD has proposed that the European Central Bank cut rates and increase lending and liquidity in the zone to halt a contagion in Spain and Italy.

With the outcome of the October 27 meeting in Brussels, it is clear that EU leaders are determined to keep Greece in the euro and prevent a contagion. But the darkening economic clouds in Italy and Spain threaten to put a clog in the wheel of this plan. Even if a contagion is averted in the short to mid term, several economies in the zone would be faced with a difficult 2012.

The World Bank and IMF have warned that not just Europe but the major developed and developing economies face the risk of a slower growth in 2012 owing to this crisis.

Implications for the global economy

Market developments since the eurozone crisis have once again reiterated the strong interconnectedness of the modern day global economy. Many investors believe that Italy, and perhaps Spain, would eventually require a bailout just as Greece, Ireland and Portugal. If this happens, global economic growth will suffer a downward risk. And experts have warned that no country is immune, no matter how developed or otherwise.

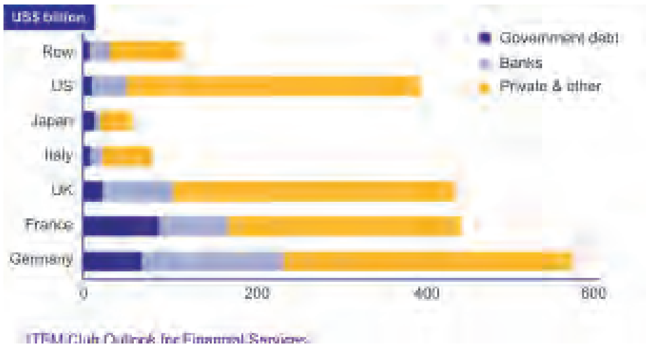
Even with the dreaded contagion yet to be full blown, the eurozone debt crisis is already taking its toll on economies around the world. Massive governments and financial institutions' exposure means that several heads could spin should the crisis deteriorate.

Germany, the economic powerhouse and about the most stable economy in the eurozone, is not immune. In fact Berlin stands the risk of becoming the biggest casualty of the crisis considering its high level of exposure to the debtor countries. Its financial services institutions are also threatened with bad debts arising from the crisis. As the biggest exporter in the zone, a widespread contagion would have devastating effect on the economy; and an outright recession could be looming.

In far away Asia, Chinese and Japanese economies owing to their export dependency will suffer should the crisis spread to major export destinations. The eurozone and the United States are the biggest markets for Asian products.

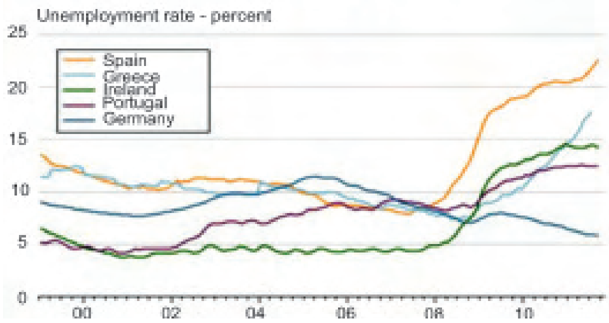
Japan is already struggling with its own share of the crisis. Market traders running away from other troubled currencies (Euro, British pound sterling and the US Dollar) have settled for the Japanese yen as a safe investment haven. This has pushed up the value of the yen against other major currencies, reducing the competitiveness of Japanese exports. Japan's central bank on October 31 waded into the currency markets, selling yen and buying US dollars as the yen reached record high levels against the dollar. The intervention brought down the value of the yen by about 5%, from a record 75.35 yen to the dollar to 79.51. To avert a situation where local manufacturing firms relocate their operations to more export friendly destinations, Japanese policy makers may be forced to keep repeating this exercise for as long as the eurozone crisis lingers.

China's export data also show an uncharacteristic downturn as its new orders index fell to 50.5 in October from 51.3 the month



Source: **independent.co.UK**

Euro zone unemployment



Source: **Reuters**

before. Since the world is banking on China and other fast growing developing economies to drive global growth in the near term, any major slowdown in these countries would have negative implications. The IMF has advised china to change its policy of over dependence on export by boosting local demand and allowing its Yuan to appreciate in value.

The United States has even more reasons to be worried about the eurozone crisis. According to reports from Reuters, Fitch Ratings has warned that should the crisis persist, it may reduce its "stable" rating outlook for U.S. banks with large capital market dealings and exposures to European markets. The OECD also recently slashed its growth forecast for the US to 1.8% next year, down from 3.1% earlier.

In a recent address delivered before a Congress Subcommittee ('The Eurozone Debt Crisis and Implications for the United States'), the U.S. Assistant Secretary for International Finance Charles Collyns reiterated that it was in the best interest of the US for the European crisis to be resolved swiftly: "The United States has no bigger, no more important economic relationship than it does with Europe". According to him, Europe accounts for over 20 percent of U.S goods exports and over 35 percent of U.S. service exports. The total stock of European FDI in the US, put at $1.6 trillion, accounts for 70 percent of all FDI in the United States.

If the example of the recent failure of MF Global is anything to go by, American banks are also highly susceptible, with their exposure to Portugal, Ireland, Italy, Greece and Spain put at nearly five percent of total US banking assets. If the eurozone fails, the US financial services industry would be at risk.

Even for the developing economies, especially the commodity-dependent ones, a crisis in Europe, a major commodity consumer, could spell doom for their export earnings.

The IMF has warned that the overall global economy is at risk of another downturn owing to the eurozone debt crisis. Among other threats, global demand and export could weaken as investors and consumer confidence are dampened by uncertainties around them.

Should the eurozone call it quits?

Some analysts have speculated that the current debt crisis marks the beginning of the end of the common currency zone and that some major economies would be compelled to revert to their original national currencies.

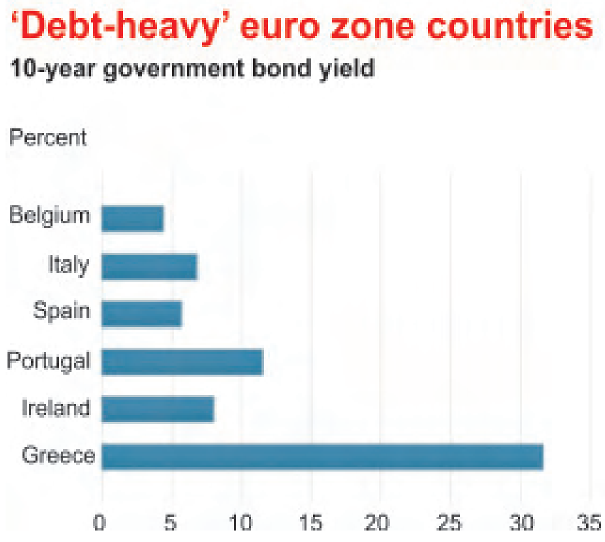
Speculations are also rife that Germany may already be working on a contingency plan just in case the Greek debt bailout fails, a contagion erupts in the zone and the euro currency crumbles. Other reports suggest that Germany is planning to readopt its former currency; the Deutschemarks; and that Berlin is currently building a reserve of it for a possible rainy day. Germany is by far the biggest economy in the zone and the force that holds the currency together. Without it, the end of the euro is near inevitable.

The sovereign debt crisis, especially that of Greece has also raised debates about the 'economic' sense in sandwiching into a single currency zone, economies that are as diverse in size, productivity, technological advancement and industrial base as Germany and Greece, for instance. Analysts have argued that Germany had no business going into a common currency union with small economies like Greece in the first place. They opine that such level of monetary unity perhaps works with equal partners; but not with partners as wide apart in size and capacity, yet working under common rules.

But the prospect of a disintegration of the eurozone or a possible German exit from the union, whether harmonious or otherwise would come with its own setbacks. In July 2010, Dimitri B. Papadimitriou, President of the Jerome Levy Economics Institute opined that an amicable, coordinated divorce in the eurozone is a possibility. He however identified the challenges with this to include higher transaction costs and tariffs and limitations to the current mobility of labor and capital within the zone. This would result in an inefficient, fractured system that necessitated the creation of the eurozone in the first instance. It would also reinforce the preeminence of the US dollar in global commerce and affairs, leaving China as the only credible rival to American economic power.

While stakeholders express their diverse opinions on the likely disintegration or otherwise of the common currency concept, realities on ground so far, as evidenced in the policy decisions and actions of eurozone and other global leaders, do not reflect any immediate plan to dissolve the union. Since the Greek debt crisis broke out, European leaders have displayed sufficient political and financial will, even though most often tainted with individual national interests, to ensure that the future of the euro is preserved. Whether their efforts yield the desired results at the end of the day is an issue for another discussion.

Source: **Reuters**



Source: **Reuters**

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What way forward?

As was the case during the recent global financial crisis, experts around the world have come to the table with diverse opinions on the way out of the European debt crisis.

The US Assistant Secretary for International Finance Charles Collyns has advised eurozone leaders on a four-pronged comprehensive strategy to address the crisis. First, to address the contagion concerns, a convincing firewall needs to be established to ensure that governments can borrow at sustainable interest rates, as they implement policies to bring down debt and strengthen the foundations for growth. Second, steps must be taken to ensure that European banks have sufficient funding and build capital cushions to maintain the full confidence of depositors and the availability of credit, and to ensure that banks have access to a capital backstop when needed. Third, a sustainable program will be needed for Greece as it implements its fiscal and structural reforms. Fourth, ongoing work to strengthen governance in the monetary union should be sustained so as to address the root causes of the crisis, which in the case of Greece was a case of flagrant imprudence and fiscal irresponsibility.

http://upload.wikimedia.org/wikipedia/commons/4/41/China_Hong_Kong_City.jpg

Dimitri B. Papadimitriou's views are not any different from that of Collyns. In July 2010, Papadimitriou suggested that short of calling it quits, the only other option open to eurozone leaders is to strive to achieve a more perfect union. According to him, this will entail the European Central Bank providing sufficient financial succor to the eurozone economies by distributing as much as €1 trillion across all nations on a per capita basis. Each nation would be allowed to use this emergency relief as it deems fit, with highly indebted economies like Greece, for example, choosing to use their own lifeline to purchase their outstanding public debts; and with others using theirs as fiscal stimulus. This could be followed by the setting up of a more centrally controlled fiscal monitoring system within the zone; and a more permanent vehicle through which the central eurozone authorities could distribute funds to member states. This should be overseen by the equivalent of a national treasury responsible to an elected body of representatives, perhaps the European Parliament. In the opinion of Papadimitriou, "this arrangement would relieve pressures to adopt austerity measures, and limit the necessity of borrowing from financial markets in order to finance deficits."

These recommendations summarize the general opinion of experts on the way out of the debt mess; except of course for those that have suggested an outright pulling down of the common currency structure to give troubled member countries more control over their monetary policies.

The Breton Woods institutions have also advised export dependent Asian and other economies including China, Japan, Germany, etc, to strengthen domestic demands and reduce their exposure to demand fluctuations in economies directly affected by the ongoing crisis. The World Bank and IMF are also calling on China to adopt a more flexible currency regime to help other export economies that are currently struggling with financial crisis.

The United States and European leaders are lobbying the BRIC economies (Brazil, Russia, India and China), especially China, to, through the IMF, throw some financial lifeline to the cash-trapped Eurozone. This, it is hoped would help ameliorate liquidity challenges and current account imbalances that have made economies like China to swim in surplus while some of the biggest economies in the world wallow in massive deficits.

(* Eunice Sampson is the Deputy Editor, Zenith Economic Quarterly)

NIGERIA: From Surplus Cash to 'Cashless' Economy

* By 'Bisola Olu-Akindeinde

A cashless society is one in which physical cash as a transaction medium is reduced to the barest minimum. Substituted in the place of cash would be an electronic payment system, in one form or another.

With the recent Central Bank of Nigeria's (CBN) policy and guidelines on Nigeria's transition from a cash-based economy to a 'cashless' society, the stage is set for a new phase of banking in the country. Specifically, on April 20, 2011, CBN issued a memo to all banks, Cash-in-Transit (CIT) operating firms, and payments system service providers, limiting daily cash withdrawals to N150,000 for individuals and N1 million for corporate entities effective June 1, 2012. The memo signed by the Director, Currency Operations Department of the apex bank also warned that any transaction above the threshold would attract a fine of five times the amount that the bank waives as a first offender, while the bank shall, subsequently, pay 10 times the charges waived.

The apex bank had sequel to a meeting with the Bankers' Committee, resolved that where a bank allowed a third party cheque encashment in violation of the stipulated regulation, such a bank would be made to pay higher than the sanctions between 10 per cent of the face value of the cheque and N100,000 fine. It advised customers to engage the services of the cash-in-transit (CIT) companies already licensed to assist with cash transfer to and from their banks at mutually agreed terms and conditions, stating that con-

For Nigeria the push for a 'cashless' economy, according to the CBN, has become imperative owing to the continued dominance of cash with its implication for cost of cash management to the banking industry, security, money laundering, among others.

travention of the policy would attract a fine of N1 million per movement.

In pursuit of the new policy, the apex bank has also come up with what it termed "cashless Lagos", meaning that Lagos State will serve as the pilot for the new innovation—beginning from June 2012. Other locations, including the Federal Capital Territory (FCT) Abuja, Rivers State, Kano State and Abia State will come on subsequently. Extension to other parts of the country will be carried out at a time to be determined by the Bankers' Committee, according to the CBN.

The Case for a cashless society

A cashless society is one in which physical cash as a transaction medium is reduced to the barest minimum. Substituted in the place of cash would be an electronic payment system, in one form or another. Many economies of the world today are either 'cashless' or are in the process of doing so. For Nigeria the push for a 'cashless' economy, according to the CBN, has become imperative owing to the continued dominance of cash with its implication for cost of cash management to the banking industry, security, money laundering, among others. This assertion is underpinned by a World Bank study which showed that the cash transactions that move between Cotonou, Ghana and Nigeria is in the region of $10 billion. These transactions have no records in any of Nigeria's systems and the government can't even plan with these figures in mind and this allows for tax evasion, the study further revealed. Also, by its own record, the CBN spends about N150 billion annually to produce, store, transport and destroy naira notes and this is expected to increase to the tune of N192 billion by 2012.

Recently, Visa also published a report on the cost of cash to the society, as it affects the European region. The report by Visa cited various papers by governments and individual consultants to make a compelling case for a regime of 'cashless' economy. The report by Visa stated that "the European Commission has calculated that the total cost to society of all payments methods, including cash, cheques and payment cards, equates to two to three per cent of Gross Domestic Product

(GDP)." It continued: "to put this figure in context, it should be remembered that the entire European Union's (EU) agricultural sector equates to 2.1per cent of GDP, which means we spend more on payment than we do on food." Visa also argues that because cards are less risky and encourages spending, they are more efficient and offer more value.

A similar report was published by the Dutch central bank in which it was estimated that the annual cost of cash to each family was €300 per annum. It is expected that the cost of card transaction will drop with some countries in Europe already issuing free debit card services to retailers.

Mobile Payment in Nigeria

According to the CBN, mobile payments have very exciting potentials within Nigeria given the low infrastructure requirements and rapidly increasing mobile phone penetration. The apex bank issued approval-in-principles to about 16 mobile payments schemes last year. This is to enable them to commence pilot run in preparation for the mass roll out of their live run in 2012.

To bring this home, CBN has listed the achievements it seeks to make from this exercise. CBN is seeking to balance the objective of meeting genuine customer transaction needs and combating speculative market behaviors that may have negative effects on the economy. The apex bank also believes the new cash withdrawal policy (which will encourage e-payment) will ensure that a large proportion of currency in circulation will be captured within the banking system and as a result develop the efficacy of monetary policy operations and economic stabilization measures. This drive towards a cashless society will also assist the CBN and the Bankers' Committee to keep in line with global trends.

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Attention to the possibility of a cashless society has increased and intensified over the past several years. Proponents and enthusiasts of the prospect of eliminating cash as a transaction medium believe that the immediate benefits would be profound and fundamental. These benefits go to the three main stakeholders: the government, the banks & merchants and the customers.

To the banks and merchants the benefits are larger customer coverage, a reduction in operational costs, availability of international products and services promotion and branding; increased customer satisfaction and personalised relationship with customers, and easier documentation and transaction tracking.

To the customers, the benefits are that it improves convenience, as it is available 24 hours a day and seven days of the week. It also helps reduce transfer costs and processing fees. It reduces processing and transaction time, supports multiple payment options (such as remote payment for goods and services) and also facilitates immediate notification of all transactions on customer's account. With reduced use of cash, there is a heightened sense of safety as the sale of illegal drugs and related violent crime levels would reduce.

For the government the benefits are that there is reduced money laundering because electronic money leaves an audit trail all the time. It aids adequate budgeting and taxation and improves regulatory services. It also improves administrative processes, and reduces cost of currency administration and management. All these benefits may result in the national debt being reduced.

There is however the other side of the coin; the disadvantages of a cashless society must not be ignored. One key disadvantage is that a cashless society gradually robs people of their privacy. There is also the added cost of transaction, which then results in an increase in the cost of goods and services. There is the risk of identity fraud once fraudsters can find a way to override a bank's security system. Having to spend electronic money reduces the control and it can leave one spiralling into debt. The irony of it all is that, in spite of all these drawbacks, the banks still stand to gain from the society going cashless.

Steps to carrying out an e-transaction

Carrying out an electronic transaction is very straightforward and is valid unless the cardholder disputes the transaction at a later date. The steps are highlighted below:

Making a purchase: in doing this, the customer's card is inserted in the Point Of Sale (POS) terminal or his card details are keyed in, if making an online order. The salesperson keys in the transaction sum or the website displays the total cost to be paid by the cardholder if making online order. In the case of Nigerian issued cards, the customer usually has to enter a PIN (personal identification number) to verify the purchase and that he is entering into the transaction. This is a crucial step in preventing fraud, as the cardholder cannot claim that he did not make PIN-verified transactions.

Checking for card validity: in a number of cases, the POS terminal sends details of the transaction to acquirer-bank which checks with the issuing customer's bank to ensure that funds are available to complete the transaction and that the card has not been reported as lost or stolen. If the card is approved, then the transaction is authorised.

Authorizing Transaction: once a transaction is authorised the POS terminal prints out two copies of the receipt; the first copy is for the customer and the second copy is for the business for safekeeping. It is vital that the business owner keeps a copy of the receipt in case the customer refutes the payment. The only evidence that the transaction was genuine and successful would depend on the business owner's ability to provide his copy of the receipt.

There is however the other side of the coin; the disadvantages of a cashless society must not be ignored. One key disadvantage is that a cashless society gradually robs people of their privacy. There is also the added cost of transaction, which then results in an increase in the cost of goods and services. There is the risk of identity fraud once fraudsters can find a way to override a bank's security system.

One must however bear in mind that authorisation does not guarantee that a transaction is not fraudulent or that it will not be charged back at a later date.

According to International Finance Corporation (IFC), approximately 3.5 billion people worldwide currently lack access to financial services. The major reason for this is that financial institutions face high transaction costs and complex logistics to reach the remote areas, due to the cumbersome nature of securely transporting and distributing cash. Providers of other goods and services that require distribution infrastructure and payment mechanisms to transact in remote locations equally face these challenges. However, electronic transaction platforms are beginning to address these challenges, creating opportunities to serve low-income customers and move them toward a cashless society. Cashless transactions bring these customers benefits spanning convenience, efficiency, security, access, and integration into the formal financial system.

Given all these, the IFC is investing in a number of companies with diverse technology skills to help create a complex infrastructure for the cashless society to function effectively. For example, there is YellowPepper—a value added mobile services company in Latin America that offers mobile phone-based "electronic wallets" for unbanked customers to pay for goods and services. In India, Suvidhaa enables customers to purchase virtual goods like train tickets and airtime across over 40,000 retail points. FiNO, also India based has a variety of offerings, which include biometric smart card-based electronic wallets for 23 million customers to receive and spend social benefits distributed by the government of India.

E-payment platforms, Challenges and Solutions

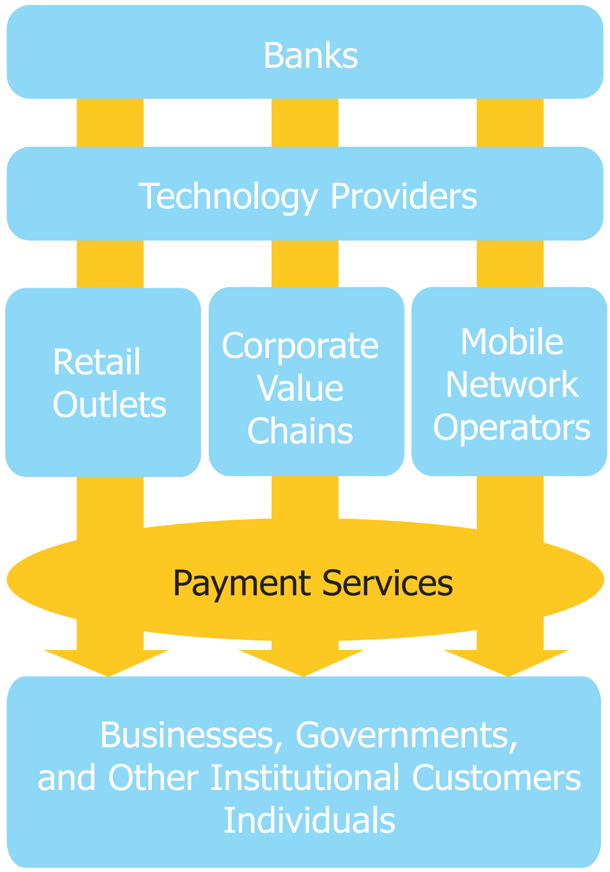


Figure: Representation of a cashless society

The E-Transaction Model

The e-Transaction Platforms model uses technology to provide unbanked and under-banked customers with the means to use money in electronic form, a convenient, low-cost, secure, and transparent alternative to cash. Electronic (or e-money) technology includes front-end devices like mobile phones, smartcards, and point-of-sale terminals used to access stores of e-money, as well as back-end switching and processing infrastructure that moves e-money and keeps records. With electronic transactions, individual customers save time (previously spent travelling great distances or waiting in long lines) and money (in the form of travel costs and forgone income). They are also less vulnerable to robbery and corruption.

For institutional customers like banks and businesses, e-transaction platforms reduce the cost of serving low-income customers because shared technology platforms, distribution channels, and even brands offer economies of scale. This, will in turn, expand consumer choice, offering access to products and services that can now be distributed virtually but were previously unavailable or difficult to obtain. These include loans, remittances, savings products, insurance, mobile airtime and transportation tickets.

For institutional customers like banks and businesses, e-transaction platforms reduce the cost of serving low-income customers because shared technology platforms, distribution channels, and even brands offer economies of scale.

Expanding reach: The e-Transaction Platforms model is high-volume, low-margin and requires a critical mass of customers. As a result, the model involves a number of solutions for getting to critical mass quickly and cost-effectively. One such solution is leveraging established retail networks to develop large footprints of agents—people or businesses contracted to sign up customers and facilitate their transactions. YellowPepper, for example, leverages existing networks of mobile phone airtime distributors. IFC client Suvidhaa, an e-transactions provider in India, leverages e-government centres. Where established networks do not exist or do not provide enough reach, companies also leverage existing independent retail outlets rather than building their own store fronts.

Another solution for reaching critical mass quickly is to target large institutions with signicant constituent networks of customers, employees, or citizens. YellowPepper, for example, targets corporations like Coca-Cola and SABMiller with large numbers of small businesses and customers in their value chains. IFC client FiNO, is working with the Indian government to transfer health insurance and rural employment benefits to millions of low-income beneficiaries.

Capacity-building: During the shift from cash to e-money, agent capacity-building is essential since they are the face of the e-transaction service to the customer, playing the vital roles of customer education, enrolment, transaction support, and exchange between cash and e-money. A customer's interaction with an agent creates the trust that is critical to adoption and use of e-transactions. The model therefore relies on training in the actual service being offered, in customer acquisition, and in general business and finance—which is critical to maintaining the liquidity necessary to help customers exchange cash for electronic value and vice versa, whenever they need to. Several companies using this model—such as Suvidhaa and FiNO—also provide one-on-one coaching to help agents manage their operations.

During the shift from cash to e-money, agent capacity-building is essential since they are the face of the e-transaction service to the customer, playing the vital roles of customer education, enrolment, transaction support, and exchange between cash and e-money.

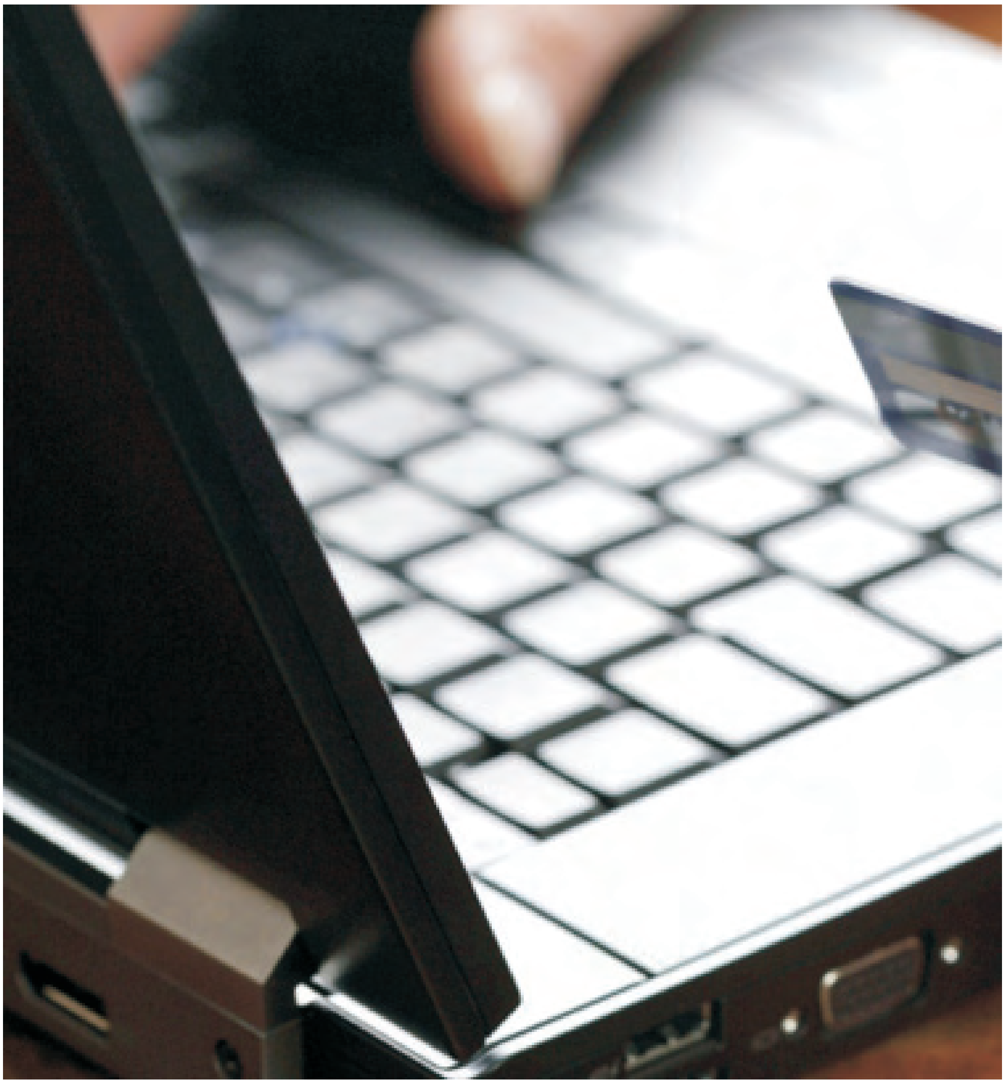
Communicating value: Successful e-Transaction Platforms businesses depend on a key message that expresses the value proposition in a way customers can easily identify with. YellowPepper's ad campaign offers customers "more time for yourself." E-transaction providers also use incentives to encourage customers try out the new service. YellowPepper encourages customer buy-in by preloading an amount of airtime equivalent to the registration fee. However, customers who have no experience with formal financial services need to be engaged by more than advertising and incentives.

Raising customer awareness is key. Agents play a critical role in teaching customers the benefits of shifting from cash to e-

E-Payment Challenges and Solutions

Value Chain	Procurement	Product/Service Development	Distribution	Sales and Marketing	Customer Service
Challenges		Developing a high-value, low-cost offer	Ensuring product accessibility while minimizing distribution costs	Ensuring willingness and ability to pay	Strengthening the value proposition, retaining customers, and fuelling positive word of mouth
Solutions		1 Adding value and reducing cost • Technology	2 Expanding reach • Leveraging established retail networks • Leveraging existing retail outlets • Leveraging existing constituent networks 3 Capacity-building • Training • One-on-one coaching	4 Communicating value • Key message • Incentives • Customer awareness-raising	5 After-sales support • Continuous access to cash

Figure: Challenges and Solutions' Matrix



money, and sometimes broader and more intensive customer education is required. FiNO, for example, holds financial literacy workshops in villages to teach customers about the banking system and financial services in general—and e-banking in particular.

After-sales support: Over time, e-money will become universal. In the short-term, while cash and e-money co-exist, companies in this space need to ensure that customers have continuous access to cash. Otherwise, the system loses utility and customers lose trust. When FiNO first started, new customers would deposit 100 rupees and withdraw 99 five minutes later to see if they could get their money back. A successful customer experience in this regard ensures customer retention and positive word of mouth, helping to get the next generation of users on board.

E-payment External Success Factors

Government Regulation: Regulatory frameworks determine whether non-financial institutions like mobile network operators and technology companies may provide e-transactions and financial services. In most cases, they require such companies to partner with banks. Proportional regulations enable financial inclusion by permitting e-transactions providers to acquire BOPcustomers at lower cost. For example, "know your customer" requirements can be relaxed. On one hand, it is costly or impossible to meet them for BOP customers who may lack formal identification cards with proof of address. At the same time, such customers maintain small stores of e-money and make mall transactions, posing little risk to the financial system.

Willing Partners: Corporations and governments must be willing to adopt e-transactions within their networks for providers to achieve a critical mass of users quickly. Such partners provide access to large numbers of retailers, customers, employees, and other citizens. Also, and especially when required by law, e-transactions providers need to find partner banks that not only want to target BOP customers, but are open to using non-traditional distribution channels to do so.

High penetration of mobile phones: Most e-transactions providers use mobile phones as front-end, user access devices. Mobile phones will continue to be popular: by 2012, an estimated 1.7 billion people in developing countries will have mobile phones, but no access to financial services.

Corporations and governments must be willing to adopt e-transactions within their networks for providers to achieve a critical mass of users quickly.

Critical Considerations for Nigeria

Power: Power must be improved dramatically to accommodate smooth operations of financial activities. Due to the nature of power supply in Nigeria, there must be efficient and reliable back up system as power outages can wreak unimaginable havoc to a cashless economy's infrastructure.

Infrastructure: At present, the financial infrastructure in Nigeria may not be adequate to carry the load of a cashless society. ATM's, Point of Sales system, mobile banking

The road ahead is a long one with various twists and turns. Keeping with global trends by going cashless is the direction the economy must go. To be adequately equipped for this as a nation, there needs to be a lot of awareness creation.

and other mediums have to dramatically expand to touch at least 40 per cent of the whole economy before any meaningful effect can be achieved. There must also be robust business continuity and disaster recovery plans in place.

As part of the robust business continuity and disaster recovery plan the authorised must ensure that there is a minimum of 99.999% (five nines) availability. The Meantime Time Between Failures (MTBF) should be at the barest minimum. Transaction data should be stored real time with mirrored back up carried out at a remote location.

Availability of real data: Proper and accurate identification of account holders must be maintained and shared when necessary by all financial institutions; Know Your Customer (KYC) and Anti Money laundering (AML) policies must be put in place. The CBN must collaborate with all other government and private agencies responsible for collection of identification of individuals in Nigeria for reconciliation of any data.

Investments: The CBN must be ready to invest heavily to make this transition possible. Technology is not cheap and keeps changing at a very fast pace. Investments in billions of dollars have to be made in infrastructure, training, marketing, security, and maintaining IT networks. This will be the case on a yearly basis for years to come and should be a collaboration of efforts by all concerned parties.

Security: As it relates to laws that are needed to enforce new methods of transactions and a changing culture, the CBN must partner and work with the National Assembly to ensure the right legislation is being formulated. The CBN and all other executive arms that are empowered such as the Economic and Financial Crimes Commission (EFCC) would carry out the enforcement of new legislation to the letter. They must commit to the training of personnel and the judiciary must be prudent and up to the task.

The CBN must also work in conjunction with the office of the National Security Agency (NSA) to proactively combat cybercrimes.

Time: Another major concern would be the risk involved, because if the process is rushed and the economy losses confidence in the system due to high level of fraudulent activities, the effects will be devastating and possibly irredeemable to the national economy.

Global Standards: Financial institutions must comply with the Payment Card Industry Data Security Standards (PCI DSS). An addendum to this is that financial institutions while complying with these standards, must take into cognizance the nuances of our economy and as such adopt and adapt some of these standards to suit the local clime.

The road ahead is a long one with various twists and turns. Keeping with global trends by going cashless is the direction the economy must go. To be adequately equipped for this as a nation, there needs to be a lot of awareness creation. The caveat however is that all precautionary measures must be put in place so that Nigeria gets it right in the first instance.

(Bisola Olu-Akindeinde is a private consultant with Peniel Advisory Services limited, Lagos. She has also worked with Royal Bank of Scotland, Deutsche Bank and Santander Bank respectively.)

Quality and Internal Control In Banks: Control Charter and Due Process

*** By Chuks Nwaze**

In the last edition of this serial, we correctly predicted the imminent loss of investment by shareholders through the nationalization of those banks earlier rescued by the regulatory authorities who were not showing visible signs of recovery, recapitalization or acquisition by other strong institutions. Although the deadline of September 30th 2011 previously announced in that regard had not expired, which created the impression that the CBN was subverting its own due process, nonetheless, it was clear enough that based on the intelligence reports at the disposal of the regulators, something needed to be done to pre-empt further slide in the fortunes of the endangered institutions.

THE IMPORTANCE OF CONTROL CHARTER AND DUE PROCESS

At the micro level of the individual banks, the importance of due process and the need to build strong internal control regimes to check operational and managerial abuses constitute the crux of this edition. There is no doubt whatsoever, that the absence of internal control charter and the palpable disregard for due process are responsible for the obvious lapses in the governance process of many financial institutions. Needless to add that even the regulatory authorities themselves can also benefit from these internationally approved benchmarks on internal control and due process in order not to open their flanks to criticisms bordering on undue haste, victimization or hidden agenda as were being insinuated in some quarters on the heels of their intervention few months ago.

THE INTERNAL CONTROL CHARTER

The following is a suggested summary of general and specific standards for the professional practice of internal control, otherwise called internal auditing:

• **Independence:-** Internal auditing should be independent of the activities they audit.

• **Organisational Status:-** The organization status of the internal auditing department should be sufficient to permit the accomplishment of its audit responsibilities

• **Objectivity:-** Internal auditors should be objective in performing audits.
• **Professional Proficiency:-** internal audit be performed with proficiency and due professional care.

The Internal Control Department
• **Staffing:-** The internal auditing department should provide assurance that the technical proficiency and educational background of internal auditors are appropriate for the audits to be performed.
• **Knowledge, Skill and Disciplines:-** The internal auditing department should posses or should obtain the knowledge, skill and disciplines needed to carry out its audit responsibilities
• **Supervision:-** The internal auditing department should provide assurance that internal audits are properly supervised

The Internal Control Officer (or Auditor)
• **Compliance with Standards of Conduct:**- Internal auditors should comply with professional standards of conduct.
• **Knowledge, Skill and Disciplines:-** Internal auditors should posses the knowledge, skill and disciplines essential to the performance of internal audits.
• **Human Relations and Communications:-** Internal auditors should be skilled in dealing with people and in communicating effectively.
• **Continuing Education:-** Internal auditors should maintain their technical competence through continuing education.
• **Due Professional Care-:-** Internal auditors should exercise due professional care in performing internal auditing.
• **Scope of Work:**- The scope of the internal audit should encompass the examination and evaluation of the adequacy and effectiveness of the organisation's systems of internal control and the quality of performance in carrying out assigned responsibilities.
• **Reliability and Integrity of Information:-** Internal auditors should review the reliability and integrity of financial and operating information and the means used to identify, measure, classify, and report such information.
• **Compliance with Policies, Plans, Procedures, Laws and Regulations:-** Internal auditors should review the systems established to ensure compliance with those policies, plans, procedures, laws and regulations which could have a significant impact on operations and reports and should determine whether the organization is in compliance
• **Safeguarding of Assets:-** Internal auditors should review the means of safeguarding assets and, as appropriate, verify the existence of such assets.
• **Economical and Efficient Use of Resources:--** Internal auditors should appraise the economy and efficiency with which resources are employed.
• **Accomplishment of Established Objectives and Goals for Operations or Programmes:-** Internal auditors should review operations or programmes to ascertain whether results are consistent with established objectives and goals and whether the operations or programmes are being carried out as planned.
• **Performance of Audit work:-** Audit work should include planning the audit, examining and evaluating information, communicating results, and following up.
• **Planning the Audit:-** Internal auditors should plan each audit
• **Examining and Evaluating Information:-** Internal auditors should collect, analyse, interpret and document information to support audit results.
• **Communicating Results**:- Internal auditors should report the results of their audit work
• **Following Up:-** Internal auditors should follow up to ascertain that appropriate action is taken on reported audit findings.
• **Management of the Internal Auditing Department:-** The chief internal auditor should properly manage

the internal auditing department.

• **Purpose, Authority and Responsibility**:- The chief internal auditor should have a statement of purpose, authority and responsibility for the internal auditing department.

• **Planning:-** The chief internal auditor should establish plans to carry out the responsibilities of the internal auditing department.

• **Policies and Procedures**:- The chief internal auditor should provide written policies and procedures to guide the audit staff.

• **Personnel Management and Development:-** The chief internal auditor should establish a programme for selecting and developing the staff of the internal auditing department.

• **External Auditors:-** The chief internal auditor should ensure that internal and external audit efforts are properly co-ordinated.

• **Quality Assurance:-** The chief internal auditor should establish and maintain a quality assurance programme to evaluate the operations of the internal auditing department.

DUE PROCESS CHARTER IN RELATION TO DISCIPLINARY RULES AND PROCEDURES IN A BANKING ENVIRONMENT

Since human resources constitute the most important asset in an organisation, It is generally agreed that discipline is essential to all organizations so as to enable them accomplish their goals. Financial institutions and their regulators should, therefore, maintain a positive posture to discipline and avoid arbitrariness by adopting the following suggested approach viz:

- To correct improper conduct and rehabilitate offenders
- To promote fairness and order in the treatment of individuals.

1. RULES

The following basic rules are therefore suggested for the employees of banks while others (such as high degree of integrity and honesty) are implicit for all employees in a banking industry. All branch managers/sectional heads must ensure that employees know the rules and standards expected of them. Generally, therefore, all employees of banks are required to conform to certain minimum standards. Specifically, employees are forbidden from the following:

(i) Issuing post-dated cheques or over drawing their accounts without making prior written arrangement to this effect.

(ii) Maintaining an account in any branch other than where they are posted

(iii) Standing as a guarantor (whatsoever) either individually or severally/jointly

(iv) Accepting any office or gainful employment while still in service without Management's consent.

(v) Accepting gratuities or commission for performing their duties. Moreover, gambling, betting, lending, or borrowing are prohibited.

(vi) Performing any act prejudicial to the general business of the bank and the interest of its customer's security.

(vii) Additionally, employees shall not be interested whether directly or not, in any advance, loan or credit facility and if interested, he must declare the nature of interest to the bank.

(viii) Grant any unauthorized loan or credit facility. He should also not benefit from such facility.

(ix) Disclose anything about the bank's business or that of the bank's customers either during or after employment

(x) Use abusive or insulting language on any person of authority over them or their colleagues.

(xi) Disobey reasonable instructions of their immediate supervisors, sectional heads and other members of management of the bank.

(xii) Enter into any form of contract or carry out any transaction on behalf of the bank without receiving express authority.

2. PROCEDURE

Stage I

(i) All complaints against an employee for any breach of rules shall in the first instance, be investigated by the sectional head.

(ii) The employee shall be given a query to explain the circumstances that led to the breach of rules

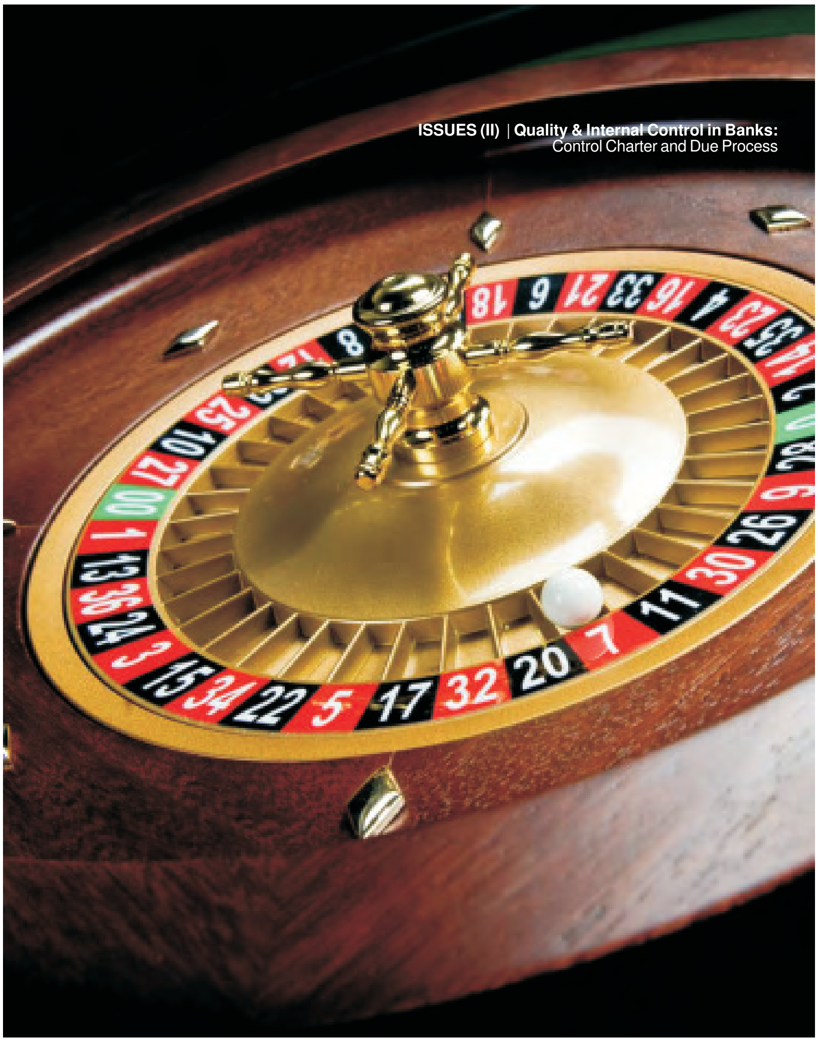
(iii) For minor offences like lateness to work etc, the sectional head

Since human resources constitute the most important asset in an organisation, It is generally agreed that discipline is essential to all organizations so as to enable them accomplish their goals.

may, with the approval of the branch manager/head of department issue verbal or written caution. A copy of this caution letter shall be placed in the employee's file.

Stage II
If the sectional head is not satisfied with the employee's explanation and/or for serious offences, the case will be referred through the branch manager/head of department to the head office human resources department for further investigation and decision. Both the sectional head and branch manager/head of department are required to add their comments to such explanations before forwarding it to head office.

Stage III
Head office human resources department shall forward the reports and comments to the head of audit department for further investigation, if considered to be with fraudulent intent. The recommendations of the audit department will be returned to human resources department.



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Stage IV
Human resources department shall take necessary disciplinary action relating to non-fraudulent cases involving junior employee.

Stage V
Head office human reources department shall send case reports/recommendations involving supervisors and above to the staff committee and executive management committee as applicable. For this category of staff (i.e. senior staff) breaches of bank's rules and regulations and other cases of indiscipline shall be dealt with as follows:

Accepting gratuities or commission for performing their duties. Moreover, gambling, betting, lending, or borrowing are prohibited.

A. CAUTION
Minor offences shall without limitation include lateness to work without adequate cause, unsatisfactory attendance or any other improper behaviour of a minor nature. These offences will attract a verbal or written caution which is just a reminder to the employee that he is stepping out of line or that his behaviour is unsatisfactory to the bank.

B. WARNING
For serious offences involving proven unsatisfactory behaviour, the employee will be given letter of warning; without limitation, such major offences will include the following:

(i) Absenting himself at any time from the place proper and appointed for the performance of his work without leave or other legitimate cause.

(ii) Unfitting himself for the proper performance of his work during working hours, for example by becoming intoxicated

(iii) Neglecting to perform any work which it was his duty to have performed, or carelessly or improperly performing any work which from its nature was his duty to perform carefully and properly.

(iv) Using any abusive or insulting language or becoming guilty of insulting behaviour to any person placed in authority over him;

(v) Refusing to obey any proper instruction of any person placed in authority over him whose instruction it was his duty to obey; and

(vi) Any other offences as set out by management. Generally, before a warning is issued, the employee shall first be given a written query and opportunity of stating his case in writing. All warnings issued to an employee shall be kept in his personal file for record purposes and such employee shall not be entitled to an annual increment for that year.

C. SUSPENSION

(i) If an employee is suspected of dishonesty or any other serious misconduct, he will be suspended from duty for a period not exceeding six months during which investigations shall be concluded.

However, if the investigations are not concluded within six months, the employee shall remain suspended until such a time that the investigations are concluded. During the period of such suspension, the employee shall be paid half of his basic salary and full transport and housing allowances. If after such investigations he is exonerated, he shall be recalled and the balance of his basic salary shall be made good to him from the date of suspension. If however, the employee is found guilty he will be dealt with in accordance with the appropriate section of the disciplinary procedure.

(ii) If an employee is suspected of a criminal offence by the police, he may be suspended and paid half of his basic salary from the date of suspension for a maximum period of eighteen (18) months. If he is exonerated within that eighteen (18) months, he shall be recalled and the balance of his basic salary and any other entitlements due to him will be made good to him from the date of his suspension. If however the case has not been disposed of, his appointment shall be reviewed provided that the matter is not in a court of law.

However, if the investigations are not concluded within six months, the employee shall remain suspended until such a time that the investigations are concluded. During the period of such suspension, the employee shall be paid half of his basic salary and full transport and housing allowances.

(iii) An employee on suspension may, where practicable, be required to report each working day (morning or afternoon) for two hours to an office designated by the employer.

D. TERMINATION

(i) An employee's service may be terminated if, within any period of 12 (twelve) months, he had

been guilty on two occasions of committing any offence for which warning letters have been issued. Termination may only be effected on the second occasion provided warning has been given to the employee in respect of the previous offence within the preceding 12 (twelve) months. Persistent offenders, however, will be treated in accordance with their previous records even though they may have become ineffective after 12 (twelve) months from the date of warning.

(ii) An employee whose services have been terminated under the provisions of this paragraph shall nevertheless be entitled to one month's notice in the case of the probation or salary in lieu.

E. SUMMARY DISMISSAL

An employee may be summarily dismissed for certain offences covered by the broad heading of gross misconduct; such offences include proven cases of:

(i) Theft, fraud, dishonesty, defalcation and irregular practice in respect of cash, vouchers, records returns or customer's account and foreign exchange transactions:

(ii) Willful disobedience of a lawful order or serious negligence:

(iii) Drunkenness or taking drugs other than for medical reasons rendering the employee unfit to carry out his or her duties;

(iv) Intentionally divulging confidential information in breach of any "Declaration of Secrecy"

(v) Conviction for a criminal offence;

(vi) Prolonged and/or frequent absence from work without leave or reasonable cause;

(vii) Fighting and assault or engaging in disorderly behaviour during working hours on the office premises or within its immediate surroundings:

(viii) Deriving any benefit in the course of his official duties which places him in such a position that his personal interest and his duty to the employer or to any customer of the employer are in conflict;

(ix) Failure to report promptly any irregularity on the part of any other employee after having knowledge of such irregularity

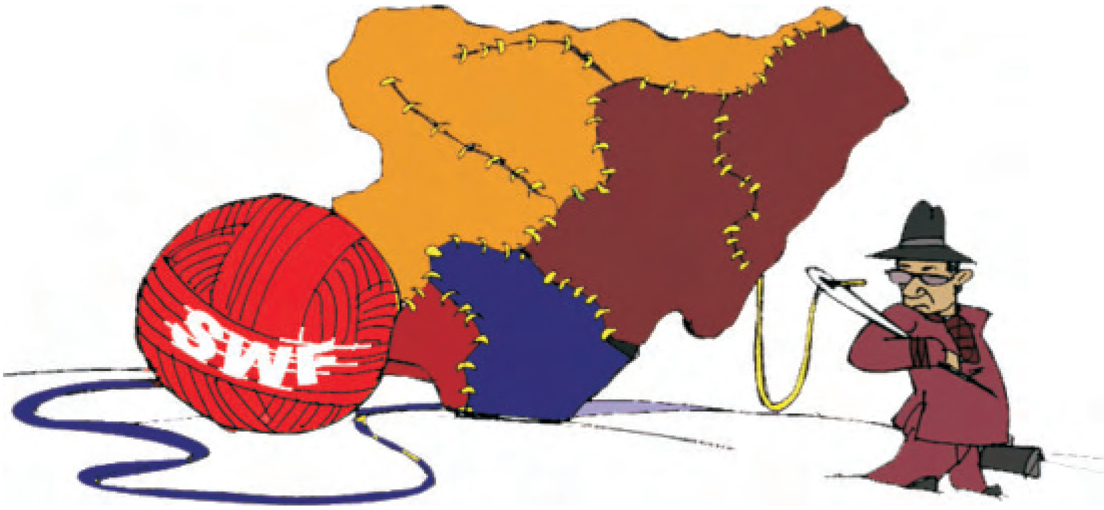
(x) Abusive or insulting language or behaviour to any client which is prejudicial to the business interest of the employer;
and
(xi) Any other offences which may be set out by management of the bank.

F. GENERAL

Where an offence has been committed which merits summary dismissal but where the bank does not exercise its prerogative of dismissal through mitigation, a "first and last" or a "second and last" warning letter may be issued and the fact that the warning is a final one will be made clear in the letter

Before either summary dismissal or warning letter is effected the employee shall be given a written query and afforded the opportunity of defending himself in writing except where the employee has absconded.

(* Chuks Nwaze is the MD/CEO, Control & Surveillance Associates Ltd.)



Sovereign Wealth Fund
Development Imperative for Nigeria?

*By **Sunday Enebeli-Uzor**

After several years of boom-bust cycles due to near total dependence on a highly volatile income stream – oil revenue, the establishment of a Sovereign Wealth Fund (SWF) is perhaps one of the most profound economic decisions the Nigerian government has made in recent times. From all indications, the sovereign wealth fund appears to be one of the major instruments for achieving the transformation agenda of the present administration, hence, it has somewhat occupied a prime position in recent economic and political discourses within and outside the country. Expectedly, since the President assented to the Nigerian Sovereign Investment Authority (NSIA) Act in May 2011, there has been heightened debate about its desirability and legality within the context of the nation's constitution, considering the federal system of government; and whether SWF is the magic wand that will kick start Nigeria's development.

Interest in sovereign wealth fund was rekindled in the wake of the economic crisis that engulfed the global economy from 2007 when SWFs somewhat became "lenders of last resort". As many financial institutions sought new money to shore up their capital bases, sovereign wealth funds provided cash to firms that were on the brink of insolvency. For instance, the Chinese SWF – China Investment Corporation injected $5 billion into Morgan Stanley. The United Arab Emirates' SWF – Abu Dhabi Investment Authority acquired 4.9 percent equity share in Citibank, while Merrill Lynch received $5 billion from Singapore's Temasek Holdings. In all, sovereign wealth funds injected well over $50 billion into financial institutions that were in dire need of liquidity in the United States and Europe. SWFs were pivotal actors in the provision of liquidity to minimise the solvency dilemma across the global banking system. They were handy veritable instruments for economic stabilisation that helped mitigate to a large extent the full impact of the crisis. These high-profile investments in developed countries' financial institutions made SWFs the cynosure of all eyes and have also heightened their scrutiny.

With well over $4.7 trillion in assets, sovereign wealth funds have revolutionised the global financial services industry, with influences on international capital flows. SWFs are now at the heart of international political economy, wielding enormous political influence internationally – at the intersection of financial and political diplomacy. Their growth has been tremendous in the recent past, and they are expected to grow further in the near future (some estimates have it that SWFs assets will hit $12 trillion in 2015). Their increasing importance for global financial markets has fuelled a debate on their nature and has sometimes elicited criticisms. There is currently a shift of financial power from multi-national organisations such as the World Bank, International Finance Corporation (IFC) and others to sovereign wealth funds. Africa is expected to become home to one of the largest pools of sovereign wealth funds in the world in the not too distant future. With enormous natural resources in the continent and the current trend where natural resource rich countries are enamored with SWFs, the continent could well be on track to become home to one of the largest pools of sovereign wealth funds.

What is a Sovereign Wealth Fund (SWF)?

Sovereign Wealth Funds (SWFs) are essentially separated pools of financial assets (primarily but not exclusively internationally invested) owned by governments to achieve economic, financial, and other strategic objectives. SWFs are usually distinct from a country's foreign exchange reserves. Whilst there are well-established norms for investing foreign exchange reserves, same is not so for sovereign wealth funds. They are also separated from government financial and non-financial corporations, purely domestic assets, and assets owned and controlled by sub-national governments. SWFs are usually composed of financial assets such as stocks, bonds, real estate, or other financial instruments funded by foreign exchange assets. They can be structured as a fund or as a reserve investment corporation. Some funds also invest indirectly in domestic state-owned enterprises.

The International Monetary Fund (IMF) identified five classes of sovereign wealth funds with potentially overlapping functions. These are: Stabilization Funds (this is primarily designed to insulate the budget and the economy against commodity price swings). Savings Funds for Future Generations (this enables the conversion of non-renewable assets into a more diversified portfolio of assets to mitigate the effects of Dutch disease). Reserve Investment Corporations (these assets are still counted as reserve assets and are established to increase the return on reserves, though at a higher risk). Development Funds (designed to help fund socio-economic projects and infrastructure, and usually have large domestic component). Contingent Pension Reserve (particularly to finance social security and health expenditures for rapidly ageing populations). Like other investors, sovereign wealth funds seek to achieve their goals by using financial markets to diversify risk, transfer funds through time, and to maximise returns.

The next group of sovereign wealth funds was established during the oil boom era of the 1970s when oil exporting countries such as the United Arab Emirates, Saudi Arabia, and Alberta established SWFs to absorb excess liquidity that could potentially have adverse effects on their economies.

A new phenomenon?

Sovereign Wealth Funds have been in existence in the international financial system for several decades. Kuwait established the first modern SWF in 1953, eight years prior to its independence in 1961. They are also not alien to the advanced industrialised economies. Norway's central bank has control over the second-largest sovereign wealth fund. What is how-

http://hafsakhawaja.files.wordpress.com/2010/04/dubai_united_arabic_emirates.jpg ever new about SWFs is their size, recent investment trends, countries of origin, and growth rate. The structure, mandates, and objectives of SWFs however vary from country to country and in recent times, they have become important symbols of state capitalism. The earliest sovereign wealth funds were established in the Persian Gulf states in the 1950s following the discovery of crude oil. The Kuwait Investment Authority that was set up in 1953 for the purpose of managing its excess oil revenues is the oldest sovereign wealth fund. The source of seed capital for these SWFs derives from recurring foreign exchange receipts from natural resource exploitation and they are sometimes called commodity funds.

The next group of sovereign wealth funds was established during the oil boom era of the 1970s when oil exporting countries such as the United Arab Emirates, Saudi Arabia, and Alberta established SWFs to absorb excess liquidity that could potentially have adverse effects on their economies. More recently, another round of oil and natural resources boom, and enormous accumulation of foreign exchange reserves amongst non-commodity exporters have thrown up new entrants in the comity of nations with sovereign wealth funds. Countries in this later group are more economically and geographically diverse than their earlier counterparts. They include China, South Korea, Venezuela, Iran, and Algeria. Some of the newer SWFs are from countries that are not commodity exporters and are not necessarily awash with excess financial liquidity.

Sovereign Wealth Fund Rankings

Largest Sovereign Wealth Funds by Assets Under Management

Country	Fund Name	Assets $Billion	Inception	Origin
UAE – Abu Dhabi	Abu Dhabi Investment Authority	$627	1976	Oil
Norway	Government Pension Fund – Global	$571.5	1990	Oil
China	SAFE Investment Company	$567.9**	1997	Non-Commodity
Saudi Arabia	SAMA Foreign Holdings	$472.5	n/a	Oil
China	China Investment Corporation	$409.6	2007	Non-Commodity
Kuwait	Kuwait Investment Authority	$296	1953	Oil
China – Hong Kong	Hong Kong Monetary Authority Investment Portfolio	$292.3	1993	Non-Commodity
Singapore	Government of Singapore Investment Corporation	$247.5	1981	Non-Commodity
Singapore	Temasek Holdings	$157.5	1974	Non-Commodity
China	National Social Security Fund	$146.5	2000	Non-Commodity
Russia	National Welfare Fund	$142.5*	2008	Oil
Qatar	Qatar Investment Authority	$85	2005	Oil
Australia	Australian Future Fund	$78.2	2004	Non-Commodity
Libya	Libyan Investment Authority	$70	2006	Oil
UAE – Abu Dhabi	International Petroleum Investment Company	$58	1984	Oil
Algeria	Revenue Regulation Fund	$56.7	2000	Oil
US – Alaska	Alaska Permanent Fund	$40.3	1976	Oil
Kazakhstan	Kazakhstan National Fund	$38.6	2000	Oil
South Korea	Korea Investment Corporation	$37	2005	Non-Commodity
Malaysia	Khazanah Nasional	$36.8	1993	Non-Commodity
Azerbaijan	State Oil Fund	$30.2	1999	Oil
Ireland	National Pensions Reserve Fund	$30	2001	Non-Commodity
Brunei	Brunei Investment Agency	$30	1983	Oil
France	Strategic Investment Fund	$28	2008	Non-Commodity
US – Texas	Texas Permanent School Fund	$24.4	1854	Oil & Other
Iran	Oil Stabilisation Fund	$23	1999	Oil
Chile	Social and Economic Stabilization Fund	$21.8	1985	Copper
UAE – Dubai	Investment Corporation of Dubai	$19.6	2006	Oil
New Zealand	New Zealand Superannuation Fund	$15.5	2003	Non-Commodity
Canada	Alberta's Heritage Fund	$15.1	1976	Oil
US – New Mexico	New Mexico State Investment Council	$14.3	1958	Non-Commodity
UAE – Abu Dhabi	Mubadala Development Company	$13.3	2002	Oil
Brazil	Sovereign Fund of Brazil	$11.3	2008	Non-Commodity
Bahrain	Mumtalakat Holding Company	$9.1	2006	Non-Commodity
Oman	State General Reserve Fund	$8.2	1980	Oil & Gas
Botswana	Pula Fund	$6.9	1994	Diamonds & Minerals
East Timor	Timor-Leste Petroleum Fund	$6.3	2005	Oil & Gas
Mexico	Oil Revenues Stabilization Fund of Mexico	$6.0	2000	Oil
Saudi Arabia	Public Investment Fund	$5.3	2008	Oil
China	China-Africa Development Fund	$5.0	2007	Non-Commodity
US – Wyoming	Permanent Wyoming Mineral Trust Fund	$4.7	1974	Minerals
Trinidad & Tobago	Heritage and Stabilization Fund	$2.9	2000	Oil
Italy	Italian Strategic Fund	$1.4	2011	Non-Commodity
UAE – Ras Al Khaimah	RAK Investment Authority	$1.2	2005	Oil
Nigeria	Nigerian Sovereign Investment Authority	$1.0	2011	Oil
Venezuela	FEM	$0.8	1998	Oil
Vietnam	State Capital Investment Corporation	$0.5	2006	Non-Commodity
Kiribati	Revenue Equalization Reserve Fund	$0.4	1956	Phosphates
Indonesia	Government Investment Unit	$0.3	2006	Non-Commodity
Mauritania	National Fund for Hydrocarbon Reserves	$0.3	2006	Oil & Gas
UAE – Federal	Emirates Investment Authority	n/a	2007	Oil
Oman	Oman Investment Fund	n/a	2006	Gas
UAE – Abu Dhabi	Abu Dhabi Investment Council	n/a	2007	Oil
	Total Oil & Gas Related	$2,645.7		
	Total Other	$2,129.3		
	TOTAL	[illegible]		

*This includes the oil stabilization fund of Russia.

**This number is a best guess estimation.

***All figures quoted are from official sources, or, where the institutions concerned do not issue statistics of their assets, from other publicly available sources. Some of these figures are best estimates as market values change day to day.

Source: Sovereign Wealth Fund Institute

Sovereign wealth funds are funded from three major sources. The first source is revenue from commodity exports and this is common amongst natural resource-exporting countries. Examples of SWFs held by natural resource-exporting countries include Kuwait Investment Authority, Norway's Government Pension Fund and the United Arab Emirates' Abu Dhabi Investment Authority. The second mode of financing SWFs is through the transfer of assets from a country's foreign exchange reserves and this is common amongst non-natural resource exporting countries such as China, Singapore, and South Korea. The third financing strategy is disbursement from sovereign debt on international markets. When a country does not utilise all the capital it raised from international sources, the remaining funds are often transferred to either its foreign reserve or sovereign wealth fund holdings.

Why countries establish Sovereign Wealth Funds

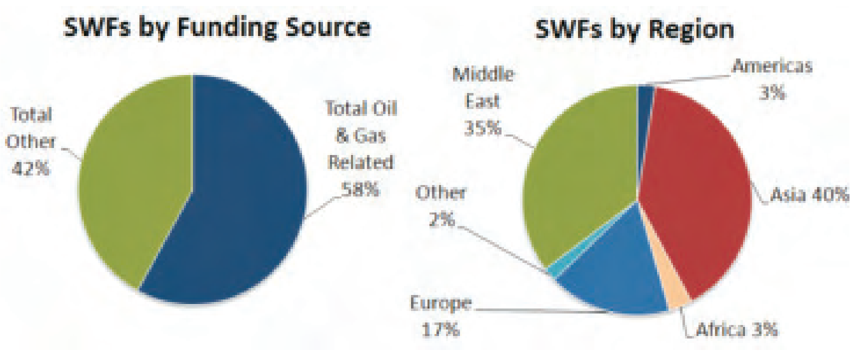
Sovereign Wealth Funds are established by different countries for a number of reasons. Those owned by natural resource endowed countries act as intergenerational transfer mechanisms, where today's export earnings are used to guarantee future government pensions, asset liquidity, and fiscal revenues. In these countries, SWFs also serve the purpose of stabilising government budgets and export revenues which would otherwise mirror the volatility of commodity prices. Countries establish SWFs as a means of diversifying their income sources in order to be able to absorb shocks arising from revenue fluctuations. Most crude oil endowed countries set up commodity stabilisation funds during periods of oil price boom to mitigate the impact of crude oil price volatility on government spending. With continuous rise in crude oil prices, the commodity stabilisation funds metamorphose into sovereign wealth funds as the funds become too large for just stabilisation.

Another reason why natural resource-endowed countries establish SWFs is the accumulation of savings for future generations as natural resources are non-renewable and are anticipated to be exhausted at some time in future. It is believed that setting aside a proportion of today's earnings from natural resources will guarantee future generations some level of prosperity. This genre of SWF is prevalent in the Middle East – home to the largest concentration of sovereign wealth fund money in the world. The region has over thirteen major funds. The main objectives of SWFs in the Middle East region are to secure long term wealth for future generations, generate funds necessary for future pension and healthcare liabilities, and minimise their countries' reliance on oil revenue.

Another group of countries that have established SWFs are those that have accumulated reserves in excess of what may be required for intervention or balance-of-payment purposes.

The source of reserve accumulation for these countries is mostly not linked to primary commodities. This is mostly prevalent in Asia where some countries are experiencing rapid accumulation of reserves and huge current-account surpluses. In the wake of the harrowing regional financial crisis of 1997-98, a number of Asian countries have built up large war chests of foreign exchange reserves in order to guarantee that they would never again be vulnerable to international financial markets and international creditors.

These countries resorted to reserve accumulation as a means of protecting domestic policy autonomy in place of, or in combination with capital controls. Over time, the immensity of these foreign reserves exceeds the typical buffer that a country requires. There was therefore the need to use some of the reserves to make strate-



Source: **Sovereign Wealth Fund Institute**

gic investments by purchasing critical foreign assets hence these countries established SWFs to manage a segment of the reserves. These SWFs are driven by self-insurance and mercantilist motivations. Prominent amongst these countries is China which set aside $200 billion of its record high $1.6 trillion foreign exchange reserves to establish the China Investment Corporation (CIC) in 2007. South Korea also established a SWF in 2005 with holdings today of approximately $30 billion. Another notable Asian country with substantial SWF is Singapore which has SWFs – Temasek (established in 1974 and with assets of $110 billion) and the Singapore Investment Corporation (established in 1981 with assets estimated to be between $200 and $330 billion).

The Nigerian Sovereign Wealth Fund

Following the President's assent of the Nigerian Sovereign Investment Authority (NSIA) Act in May 2011, and the transfer of a seed capital of $1 billion from the Excess Crude Account (ECA) to the NSIA in October 2011, Nigeria effectively established a Sovereign Wealth Fund (SWF). The Nigerian Sovereign Wealth Fund is composed of three separate ring-fenced portfolios namely: the Nigeria Infrastructure Fund, the Future Generations Fund and the Economic Stabilisation Fund. Each component represents at least 20 percent of the total. The Nigeria Infrastructure Fund is a ring-fenced portfolio of investments specially related to and with the object of assisting the development of critical infrastructure that will attract and support foreign investment, economic diversification and growth. Infrastructure that this Fund is expected to focus on include: power generation, distribution and transmission, agriculture, dams, water and sewage treatment and delivery, roads, port, rail, airport facilities, and similar assets that will stimulate the growth and diversification of the Nigerian economy. The Fund is expected to act as a lead investor for domestic and international partners seeking to invest in the development of infrastructure in the country.

The Future Generations Fund is a ring-fenced diversified portfolio of appropriate growth investments for the benefit of future generations. This Fund is targeted at providing future generations with a solid savings base for such a time, when the hydrocarbon reserves of Nigeria are exhausted, with due regard to macroeconomic factors. The Fund will build an intergenerational savings base by investing in longer term assets that generate returns to accumulate wealth for the next generations of Nigerians. The Economic Stabilisation Fund is also a ring-fenced portfolio investment to provide supplemental stabilisation funding based upon specific criteria and at such a time when other funds available to the Federation for stabilisation needs to be supplemented. This will act as a last-resort source of finance during periods of fiscal deficit to protect the integrity of the budget. This stabilisation function will ensure the smooth functioning of government and delivery of key services during periods where revenues from petroleum sales are less than the level anticipated and approved by the National Assembly.

The Nigerian Sovereign Wealth Fund has replaced the Excess Crude Account (ECA) which had acted mainly as a stabilisation fund. The Excess Crude Account (ECA) was established in 2004, with the main thrust of protecting planned budgets against shortfalls due to volatility of crude oil prices. The account was used to save crude oil revenues above a base amount derived from a defined benchmark price stipulated in the federal budget. The

ECA somewhat delinked government expenditures from oil revenues and insulated the economy from external shocks especially during the global economic crisis. Nigeria's ability to weather the storm of the crisis has been attributed to the ECA and the robust external reserves that were built prior to the impact of the economic downturn on crude oil prices. Surging crude oil prices saw the ECA rise almost fourfold, from $5.1 billion in 2005 to over $20 billion by November 2008, accounting for more than one-third of Nigeria's external reserves at that time.

Mitigating Natural Resource Curse

The discovery of a natural resource (especially in a developing country) is potentially beneficial and, simultaneously, potentially calamitous. This is so because it has been established that countries endowed with natural resources paradoxically experience lackluster economic growth. This occurrence has been attributed to a variety of factors, amongst which is the concentration of economic activities in the natural resource sector. Over time, the natural resource sector crowd out economic activities in other sectors by pulling away labour and capital and reducing the competitiveness of non-resource exports. Nigeria like most crude oil producing countries have been plagued with this malaise often referred to as resource curse, paradox of plenty or Dutch disease. This argument has been advanced as the reason why some natural resource endowed countries have development challenges. This is so because there is also the tendency of unrestricted spending of revenue from natural resources which culminates in the disruption of basic economic fundamentals that are sine qua non for the growth and development of the economy.

As countries continue to tinker with measures to mitigate the resource curse dilemma, the option of a sovereign wealth fund is possibly a viable antidote to the malaise. By establishing an infrastructure fund to develop critical infrastructure in the country, Nigeria may well be on track to discovering the missing puzzle in the quest for accelerated economic growth and development. The Infrastructure Fund component of the sovereign wealth fund seeks to assist the development of critical infrastructure in the country, thereby bridging the existing gaps. It will act as a lead investor for domestic and international partners seeking to make investments in the development of infrastructure in the country. By attracting and supporting foreign investment, economic diversification and growth, the fund could provide some of the most basic fundamentals that will kick start productivity in other sectors of the economy.

http://www.photoradar.com/files/imagecache/original_large/photos/users/john2802/untitled-3396.jpg

Nigeria's ability to weather the storm of the crisis has been attributed to the ECA and the robust external reserves that were built prior to the impact of the economic downturn on crude oil prices.

Potential benefits from Sovereign Wealth Fund

Sovereign wealth funds have grown in popularity amongst natural resource endowed countries and also foreign reserve rich countries. Crude oil being a non-renewable resource will someday become history and it will only be fair to future generations to ensure intergenerational transfer of proceeds from current crude oil exploitation. Nigeria's mono-product economy no doubt exposes it to the vagaries of crude oil price volatility in the international commodities market. The SWF is expected to act as a fiscal stabiliser and buffer. With a SWF in place, government budget funding is expected to be more guaranteed as fluctuations in earnings can be smoothened from the economic stabilisation component of SWF. This will engender stability in the funding of government long term projects that would otherwise have suffered the negative impact of revenue fluctuation. The Fund is also expected to facilitate a more effi-

cient allocation of earnings from crude oil by diversifying the country's economic base. This will enable other sectors of the economy to grow as economic activities will no longer be concentrated in the petroleum sector. The SWF symbolizes prudent fiscal discipline and potentially will enable the diversification of the country's assets.

By joining the league of countries with SWFs albeit belatedly, Nigeria's standing in the comity of nations will receive enormous boost as the country will be better placed to negotiate effectively in the comity of nations. SWFs have become veritable tools for international diplomacy and relevance, as countries with substantial SWF are treated courteously since withdrawal of their investments could have disastrous consequences on the economies of some powerful nations. Countries that have been able to use their SWFs as instruments of international diplomacy include China and Russia especially since the global economic downturn. Powerful countries have become somewhat subservient to the whims and caprices of these countries due to their ability to direct the flow of finance in the global economy. Nigeria as Africa's largest crude oil exporter stands to benefit from its SWF as the African continent is expected to become home to one of the largest pools of sovereign wealth funds in the world. As a natural resource rich continent, the era of foreign aid may be over sooner than expected as most aid giving nations are currently grappling with austere economic conditions.

Issues with Sovereign Wealth Funds

Sovereign wealth funds have come under intense scrutiny and have acquired much notoriety in public debates in recent years as a result of their growing role in global financial markets and finance. These criticisms are myriad but bother mostly on their effects on individual firms, capital markets, national politics, and their efficiency. SWFs have been criticised for their tendency to be secretive and political in investment decisions. They however justify their covertness for fear of protectionist response to their investment propositions. There are also national security concerns as SWFs could be used to secure control of strategically important industries for political rather than financial gain. This has raised concerns about the invasive tendencies of SWFs and their ability to meddle in the domestic affairs of foreign countries who are recipients of their investments. This fear could potentially culminate in investment protectionism which could be antithetical to the free flow of investment in the global economy.

Another concern about SWFs is that some countries may not be fully prepared before establishing such funds. Some analysts argue that the mere fact that a country has foreign exchange surpluses does not mean it should establish a sovereign wealth fund. Often times, those countries are still faced with basic economic challenges such as poverty, unemployment and current account deficits. It is argued that in many instances, the foreign exchange reserves are not really earned reserves but are borrowed reserves and as such, the SWF may not be sustainable in the long-run.

Sovereign wealth funds have also been criticised for their ineffectiveness in acting as stabilisers and buffers when the need arises. A study by the International Monetary Fund (IMF) on SWFs in natural resource-exporting countries concluded that there is little evidence to show that sovereign wealth funds have achieved the goal of smoothening out liquidity and government expenditures between times of strong and weak natural resource prices. The study concluded that countries that have SWFs had difficulty in harmonizing fund operations with fiscal policy. It is argued that there is the tendency of conflict between operations of SWF and other economic policies of the government. If both are not properly aligned, the overall objective of government policies may be undermined. The IMF study also discovered a paradox in the relation between SWFs and their home countries – the more reliant a country is on one commodity, the less effective its SWF is in achieving set goals. Another pertinent finding of the study is that only few countries have drawn down from their SWFs holdings for the greater national well being.

The Santiago Principles

Due to the numerous criticisms of sovereign wealth funds and the need to streamline their activities to conform to global best practices, the International Working Group of Sovereign Wealth Funds (IWG-SWF) and the International Monetary Fund (IMF) proposed a set of 24 principles/practices (now known as the Santiago Principles) that assign best practices for the operations of SWFs. The purposes of the Santiago Principles are threefold. Firstly, to identify a framework of generally accepted principles and practices that would properly reflect appropriate governance and accountability arrangements as well as the conduct of investment practices by sovereign wealth funds on a prudent and sound basis. Secondly, to enable home and recipient countries and the international financial markets to gain a better understanding of SWFs; and thirdly, to ensure that, through the pursuit of these principles and practices, SWFs would bring economic and financial benefits to home countries, recipient countries, and the international financial system.

The Santiago Principles are a voluntary set of principles and practices that the members of the IWG/IFSWF support and either have implemented or aspire to implement. The principles seek to support the institutional framework, governance, and investment operations of sovereign wealth funds that are guided by their policy purposes and objectives, and consistent with a sound macroeconomic policy framework. The publication of the Santiago Principles was intended to help improve understanding of SWFs as economically and financially oriented entities in both the home and recipient countries. It is believed that this understanding would contribute to the stability of the global financial system, reduce protectionist pressures, and help maintain an open and stable investment climate. The Santiago Principles are also intended to enable sovereign wealth funds, especially newly established ones, to develop, review, and strengthen their organisation, policies, and investment practices. The principles were drafted taking into cognizance the diversity of sovereign wealth funds; and not all principles were intended to be applicable for all SWFs. Since 2008 when the Santiago Principles were drafted, 25 nations have signed onto the principles.

An Economic Imperative?

Nigeria is believed to have the potential of becoming one of the world's largest economies. A Goldman Sachs report suggested that Nigeria will overtake South Africa and Egypt to become Africa's strongest economy, and that by 2025 could become one of the 20 largest economies in the world and 11th in 2050. Although these predictions may appear ambitious, evidence from the East Asian Economic Miracle gives impetus to the possibility of a dramatic turnaround in the fortunes of a country if fundamental economic principles are backed by political will, and prudent fiscal regime. It has been variously argued that one of the banes of the Nigerian economy is its near complete reliance on crude oil earnings as revenue source. This scenario has continued to thrive due largely to the dearth of infrastructure to support other productive sectors of the economy especially agriculture and manufacturing. By establishing an infrastructure fund to develop critical infrastructure in the country, Nigeria may well be on track to discovering the missing puzzle in the quest for accelerated economic growth and development.

The absence of an institutional framework to manage the proceeds of crude oil earnings from a highly volatile income stream has exposed the country to cycles of booms and busts. There is therefore the need to de-link government expenditure from the fluctuating price of crude oil. Prior to the commencement of its sovereign wealth fund, Nigeria was one of the three member countries of the Organisation of Petroleum Exporting Countries (OPEC) that do not have a sovereign wealth fund. The other two countries are Iraq and Ecuador. Nigeria's best attempt at managing its excess earnings during periods of high crude oil price was the creation of an Excess Crude Account (ECA). The ECA was however lacking in the requisite legality thus making it vulnerable to political exigencies. Another major shortcoming of the ECA is that it was merely a stabilisation fund that warehoused excess liquidity that was used to augment government revenue when it falls below a specified threshold. The sovereign wealth fund however is an all encompassing fund that seeks to serve as a stabiliser, a guarantee fund for future generations, and will also address the dire infrastructure needs of the country. The sovereign wealth fund could be the catalyst the economy requires to jumpstart a holistic growth and development.

(* Sunday Enebeli-Uzor is an Analyst, Zenith Economic Quarterly)

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Foreign Insights

Greece is the word...

* By **Neil Hitchens**

The recent period to the end of October has been one where global equity markets continue to be fixated in real time on the almost daily emergency discussions between the 17 members of the Euro about the fortunes of Greece, how the Greek crisis might possibly tear the Euro apart, the various and seemingly never ending bail outs required to keep Greece solvent and how this impacts both the Euro zone and the entire Western European banking system. In many respects there has not really been much actual progress since early summer in formulating a definitive answer to Greece's woes. Solutions, when proposed, have tended to be short term, stop-gap measures to prevent Greece from defaulting on its near term debt payments, a process which usually involves the transfer of further billions of Euros from German voters' pockets into the bottomless pit of the Greek economy, combined with further seemingly increasingly desperate and sometimes bizarre economic measures to try and cut the Greek deficit - one of which was the suggestion that the Greek government should employ an army of German tax collectors to try something novel and make <u>all</u> Greeks pay <u>all</u> their taxes.

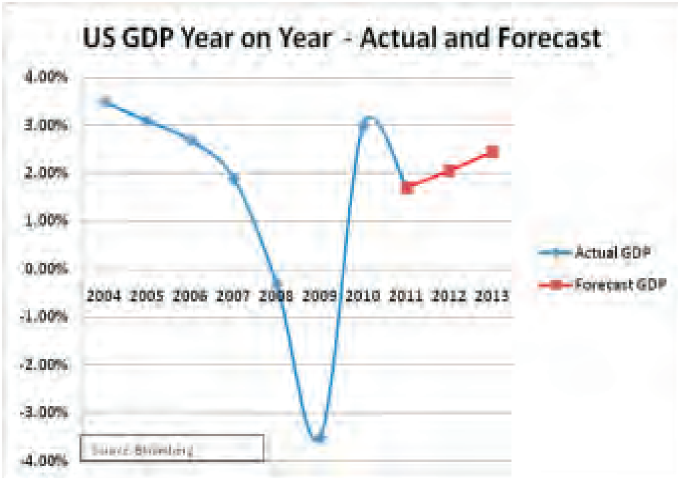
The "talks about talks" about Greece have taken a heavy toll on equity markets, injecting further nervousness about the state of the global economy and whether a double dip recession is on the cards. Certainly growth worldwide has slowed dramatically as the Greek crisis has escalated, but it is too early to tell if this is a precursor to a renewed period of negative growth or whether consumers and house buyers are merely pausing for breath ahead of an upsurge in economic activity.

The continuing hope that the economy of the United States of America will act as one of the engines of growth for 2012 and beyond has, yet again, been called into question. Growth though is still there, it is just <u>*lower*</u> than many had hoped for and as such, irrational trend lines are being drawn showing a desperate economic tale. Yes, GDP has slowed from an annual rate of +2.2% at the end of the 1st Quarter of 2011 to +1.6% at the end of the second. However, some economists

are re-examining their over-pessimistic forecasts and starting to see a slightly more positive trend for the rest of 2011 given recent moves by the Federal Reserve (Fed) to stimulate the economy. However economists still remain intensely divided about the actual GDP numbers to come over the next 18 months. While the graph below shows an average of +1.70% for 2011, +2.05% for 2012 and +2.45% for 2013 the estimates vary widly.

2011 forecasts range between an almost static +0.8% (but note this is still positive "g-r-o-w-t-h")

The problem is that the distraction of the European crisis has put a negative stance on all economies. Our feeling though is that the US will eventually surprise on the upside and that in 2012 it will end up growing nearer +3% with a probable over +3% figure for 2013.



to a racier +2.50%; 2012 estimates are between +0.40% and +3.90% and for 2013, +1.00% to +4.50%. The problem is that the distraction of the European crisis has put a negative stance on all economies. Our feeling though is that the US will eventually surprise on the upside and that in 2012 it will end up growing nearer +3% with a probable over +3% figure for 2013.

However the US hasn't exactly been helping itself on the world stage. The showdown in Congress between the Tea Party Republicans and the Democrats in August merely delayed the inevitable downgrading of US Government debt from AAA to AA+ - AAA being the highest possible grade of debt and something that many countries will do almost anything to maintain. While it was never actually going to be a question of the US being unable to pay its debt bill, the Republicans managed to take it to the wire in an attempt to prove a rather odd political point.

However, as has been seen in the past when Japan's debt was similarly downgraded, there has been no actual aversion to holding US Debt at this lower credit level. The US remains the largest debt issuing nation on earth and as such irrespective of its ratings will always maintain a proportionately large weighting in any bond index. The US has also been fortunate this quarter where with the highly volatile equity markets, debt has become the safe


Athens, Greece

http://2.bp.blogspot.com/-HyhqZniPaCo/Tdkwc5UCNmI/AAAAAAAAAsE/ppGMT6J89uU/s1600/Athens+001.jpg haven commodity of choice for many investors.

The US and the Federal Reserve - Stick or "Twist"?

The Fed changed its plan of attack in September in its efforts to breathe new life into a flabby, but not dead, economy. Instead of further rounds of quantitative easing, which has longer term negative impacts on the US economy in terms of higher potential inflation, they instead initiated 'Operation Twist', an open market move whereby the supply of shorter term debt (3 years or under) was increased and a similar amount of longer term debt was simultaneously retired from the market. This has the impact of flattening the yield curve and promoting capital inflows while at the same time strengthening the US Dollar. This was first tried in 1961 at the height of the Cuban Missile Crisis and it worked well in reducing the spread (difference) between long and short term rates. It was, though, considered a failure at the time, but historical re-evaluation of this process has shown that it wasn't allowed to continue for long enough to be truly effective.

In 2011, though, this time it is both different and not so different.

This year and next around US$ 400 billion of bonds with maturities of between 6 and 30 years will be purchased and issuance of the same amount of bonds with a maturity of 3 years or less will begin. This is an attempt to do what Quantitative Easing (QE) tries to do but without printing more money and expanding the Fed's own balance sheet which in turn actually avoids the inflationary pressure that QE brings.

I for one, think that the Fed are actually thinking 'with their heads on' for once and it is a rather shrewd move even if markets had further immediate jitters at this announcement with the Dow Jones falling 284 points on September 21st, the day of the announcement, 391 points the next day only to recover the 20th Septembers' close by September 29th.

The impact can be best illustrated by viewing the changes in the US Government Yield curve for the year to date. The 30 year yield has shrunk from 4.336% to 3.133% which has lead to the price of the 30 Year Note rising from $98.58 to $126.53 a capital gain of $27.95 or + 28.35%. Similar but less dramatic price rises are also to be found along the curve. The 10 Year Bond yield

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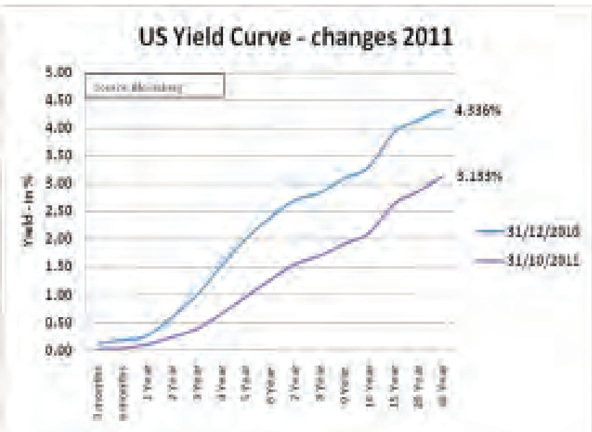


fell from a 3.37% yield to 2.115% and the price rose from \$94.39 to \$107.01, +\$12.62 / +13.37% and even the 2 year note saw its yield more than halved from 0.65% to 0.242%.

As the yield curve has shifted along its entire length the spreads between the Long/30 year bond and other maturities has actually stayed reasonably constant. The 30 Year-20 Year spread has drifted this year ever so slightly from 0.20% to 0.28%, the 30 Year - 10 Year has stayed constant at 1.03% and the 30 Year-5 Year spread has hardly moved from 2.33% to 2.17%.

This should, normally, be an unprecedented move in modern times. It is unlikely to be repeated in the near term unless there is an unparalleled flight to safety due to some crisis as yet unimagined. This event might happen if there was a full-blown repeat of the 2008 banking crisis when the 30 year yield plunged that year from 4.357% on 13th November 2008 to bottom out at 2.522% on 18th December 2008. A price move for the 30 Year Bond in this period was one from \$102.36 to \$140.91, an eye watering rise of 37.66% in 5 weeks while the financial world nearly collapsed around us. As they say, 'Never say Never', but unless the probable Greek default comes as a totally complete and utter shock, it is unlikely that we will see such a move in the near term.

It is hoped that this slightly odd method of financial and economic stimulation from the Fed will help stabilise and then reinvigorate the US Housing market as lower longer term interest rates will have a positive impact on overall mortgage rates by pushing them lower and keeping them at these levels for longer. This in turn should help boost housing sales and new housing construction which in turn will stimulate other areas of the economy and hopefully start bringing down the overall unemployment rate from over 9% back to its 30 year average of around 6.3%, hopefully even lower in time.

IF positive momentum does start appearing sooner than expected in the distressed housing sector then it will be worth re-examining some sector specific plays in the S&P 500.

The worst performing sector year to date has been the Household Appliances Sector which has a single member - Whirlpool (WHR) - the manufacturer of washing machines, fridges and air conditioning equipment. Despite yielding 3.88% with further dividend growth to come, priced at end of October at \$50.81 it is still some -54% off its recent peak of \$112.42.

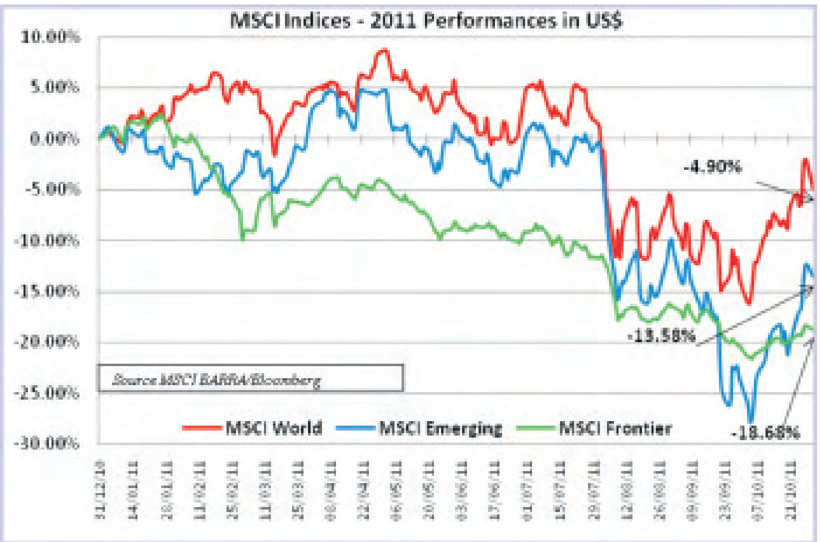
Other less distressed but still underperforming housing plays include the Constructions Materials Sector, -29.46% as at 31st October, again a single stock play in Vulcan Materials (VMC - Price \$31.29) which produces construction aggregates, at multi year lows but one to watch.

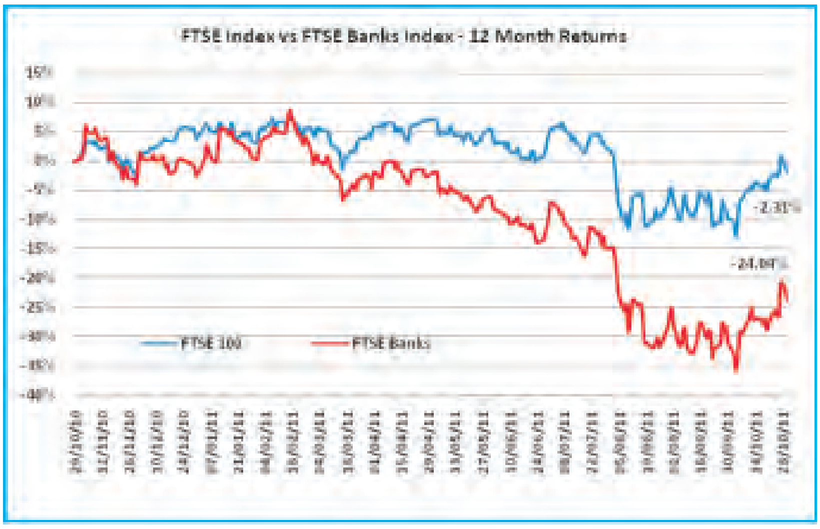
The Home and Office Furnishing Sector is also starting to throw up some interesting situations - stocks such as La-Z-Boy (LZB, Price \$10.16), Knoll Inc. (KNL, \$15.25) or Kimball Inc. (KBALB, \$5.625) are seeing the first tentative signs of being possible 'Buys'. While all these stocks

It is hoped that this slightly odd method of financial and economic stimulation from the Fed will help stabilise and then reinvigorate the US Housing market as lower longer term interest rates will have a positive impact on overall mortgage rates by pushing them lower and keeping them at these levels for longer.

are probably not quite ready enough for the moment they are worth having on your scratch pad for further investigation.

Unfortunately we will not know exactly when Operation Twist will work its way fully through the US economy. It is most likely that definitive signs of a full blown US recovery will not be visible until mid 2012 - something that president Obama must be acutely aware of. It is going to be nip and tuck to see if the US recovers in time for him to be successful in his re-election bid. Election Day 2012, November 6th, is a mere 372 days away. Obama had better start worrying now.





Equities - is it really time to go back into the market?

The past few months, it must be admitted, has not been a great time to hold equities in any sort of index tracking portfolio.

But after probably the worst summer for equity markets in a generation, October returned some of the best results seen in this month in nearly ten years. Yet, similar to those school reports we all intermittently feared, the final verdict was one of 'Could have done better'.

Yet again, as we have already noted, the centre of the equity storm was Europe with the epicentre continuing to be Greece. Just as we all thought that after a seemingly daily diet of emergency meetings between the European Central Bank (ECB), Germany, France and the other members of the Euro Zone, there was a definitive solution to the Greek problems, Premier Papandreou decided that turkeys really can vote for Christmas and attempted to put the Greek bailout to a plebiscite. The Greek Premier decided, 5 days after Greece received the bailout terms, that this was not only an opportunity for all Greeks to vote on the terms of the second (official) rescue package but is an opportune moment to use this as a confidence vote in his own leadership. This was a doomed gamble on his part, buoyed, seemingly, by a single opinion poll at the end of October that showed more than 70% of voters want Greece to stay in the Euro. This move is something that both France and Germany have, basically, refused to allow and as such the pressure likely to be exerted on Greece going forward will be even more strong, hard and painful.

Sometimes words fail us about the magnitude of such a high risk move. Equity markets certainly took complete and utter fright at this move, reversing in 48 hours what had been a rally of over two weeks length.

However during this most recent re-

porting period several ‘known knowns’ resolved themselves. Most importantly the Libyan crisis was finally resolved on October 20th with the death of Colonel Qadaffi, admittedly under somewhat dubious circumstances. But this is one more conflict resolution that as we write, appears to be having a positive effect on Libya. Those loyal to the previous regime have laid down their arms, oil production is in the process of being cranked back to previous levels, Western countries have unfrozen the assets of the country and an Arabian version of democracy is being actively touted.

So far, so good. However, let us revisit this country in 6 months time when daily life has gone back to what passes for normal and the new democracy has had time to bed in properly.

The UK and Ireland - time to think the unthinkable?

The reintroduction of such uncertainty that, it had been hoped, had dissipated out of the equity markets has been viewed with an element of strong dismay. It has also re-opened old fissures in the Italian and Spanish bond and equity markets. Strangely though, there was not quite such a bad reaction from either the Portuguese or Irish markets, which may mean we have reached some sort of low water mark here.

Irish markets especially seem to have shrugged off earlier fears of a default, but that could most probably be explained away in the short term because all Irish Banks have effectively been nationalised and the hard pressed Irish tax payer can see some light at the end of this particular tunnel. It is perhaps time to dust off those Irish and UK Equity buy lists and prepare to go back into the markets. As we have cautioned before AVOID financial stocks in their entirety as this is the great unknown with many UK banks at risk of some 3rd party contagion in the future even if they themselves do not directly hold Greek, Italian or Spanish Government Debt.

However the UK and Irish economies - historically intertwined - both seem to be weathering the tornado ripping through mainland Europe. Irish GDP was most recently measured as growing +2.3% a great change from the -8.3% reading in March 2009. The UK, despite being the larger and more sluggish economy had a higher than expected Q2 reading of +0.5% to give an overall reading of about +2.0% for 2011. While of course, such predictions can be blown off course by external events there is growing evidence that despite the economic hardships being thrown at the the Irish and British consumer, they are still spending; retail stocks are not collapsing and while the overall picture does remain uncertain there are pockets of sporadic growth to be found.

In London, the FTSE 100 share Index is now showing a serious level of mismatching performances between financial stocks and overall indices.

The basic performances show a net underperformance of -21.73%.

Also, as Financials are part of the All Share Index as well, stripping out their actual point contribution to the FTSE brings into stark focus the damage done to the index.

The Points deductions for the past year are:

Bank	FTSE points Equity	Performance
HSBC	-78.0	-16.05%
Lloyds	-54.7	-52.86%
Barclays	-38.8	-27.36%
Royal Bank of Scotland	-13.7	-45.68%
Standard Chartered	-33.0	-19.19%

The FTSE in this time went from 5,675.16 to 5,544.22 = -2.31% or -130.94 points

If you add back in the points ‘lost’ of -218.20 points the FTSE would have risen 87.26 points or +1.54%.

Over the same period of time there have been solid performances from many constituents of the FTSE 100; Burberry, the fashion retailer, is + 31.6%, Unilever, +15.95%, Legal & General, +10.06% or Bunzl, +9.07%. There have also been some non-bank disasters such as Kazakhmys Mines, -29.52%, Cairn Energy, -23.66%, Rio Tinto, -16.13% and Carnival Cruise Lines, -15.13%.

While we do not rec-

http://upload.wikimedia.org/wikipedia/commons/4/48/Westminster_palace.jpg

It is perhaps time to dust off those Irish and UK Equity buy lists and prepare to go back into the markets. As we have cautioned before AVOID financial stocks in their entirety as this is the great unknown with many UK banks at risk of some 3rd party contagion in the future even if they themselves do not directly hold Greek, Italian or Spanish Government Debt.

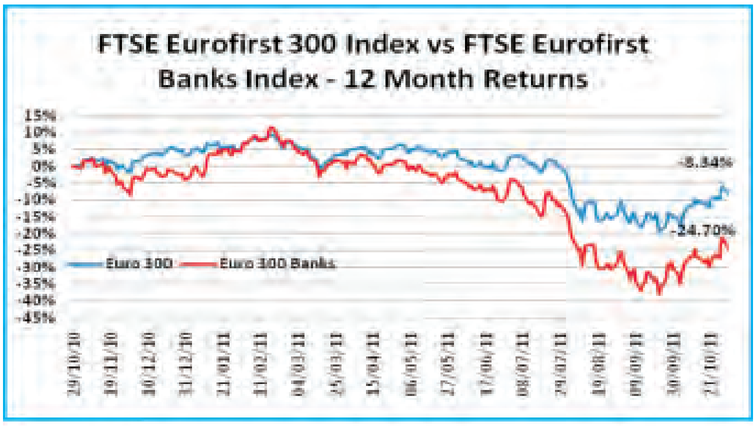
ommend clients buying new equity positions at the moment, it is certainly NOT the time to be selling. On a technical basis the FTSE 100 has found a new floor around 5,400 which was until a few weeks ago a major resistance to the Index as it climbed from a level of around 5,000. In Ireland the ISEQ (Irish Stock Exchange Quotient) has also performed in a similar fashion. Previous upside resistance at 2,600 is now downside support. Both indices are showing signs of moving higher in the near term. While we do not advocate finite predictions the possibility of the FTSE topping out at around 5,900 and the ISEQ at around 2,900 - some 7% or so from current levels, this augurs well for a possible New Year rally.

Equity markets in both Europe and the US tell the same picture of the disaster wrought by banking stocks and the perils of being in them merely because ‘They are in the Index’ - never a good reason to hold something that is so obviously a drag on any portfolio.

http://www.winwallpapers.net/w1/2011/07/China-Wallpapers.jpg

In Europe, where indices have generally been more widely affected by the Euro crisis the bank have underperformed the EuroFirst Index by -16.36%.

Globally, again the same story is evident with a net unchanged performance for the year for the main index but a -12.43% underperformance for the bank.



This is why careful stock selection in the hands of a practiced manager - what is called ‘activist’ asset management - will bring enhanced results for investors. Merely because a stock or a sector is in an index is a bad way to justify its inclusion in an equity portfolio. Each and every stock has to be in a portfolio for a reason. If it starts to underperform or move erratically against the market then the stock should first be watched closely and if the trend is downwards you should not be afraid to close this position, at a small loss if necessary, rather than hang on for grim death and take a hit of 40%, 50% or more, as investors in a wide variety of bank stocks have this year. Stop losses are there for a reason - to **Stop** you Losing Money if a stock falls.

That said I believe that now is the time to start looking at what stocks to buy globally.

If Greece does explode there will be plenty of bargains to be had for the investor who has kept his cash in the bank. Even if Greece does not go to the wall, indices may well start building

It is possible China could use this weakness as a chance to boost its overall copper inventories for when industrial production picks up, but this is a long shot call. Prices are likely to remain around current levels.

longer term strong support levels just around where we are now to possibly spring a surprise in 2012 and 2013 with overall index rises in low double digits possible for both years. If the global economy behaves and shows signs of life, then hang on to your hats! Equities should rally fast into such good news.

Even if you are not buying at the bottom, buying into a trend is a sensible thing to do as the "Trend is Always your Friend". As we continually advise investment clients the difficult thing is to buy rising stocks in rising markets - however it is both possible and probable with the right investment manager to guide you.

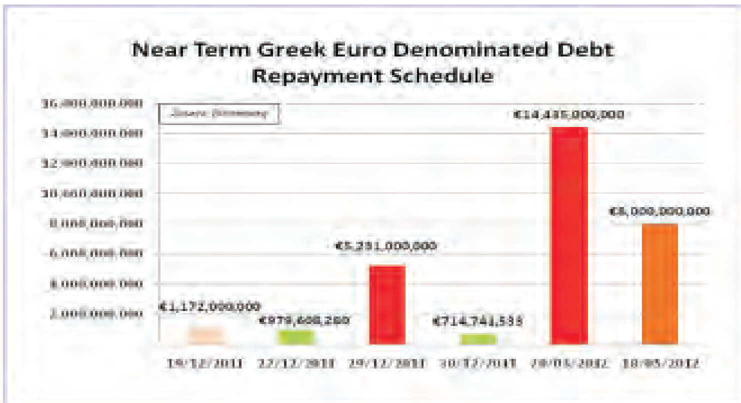
Commodities near term volatility but what next?

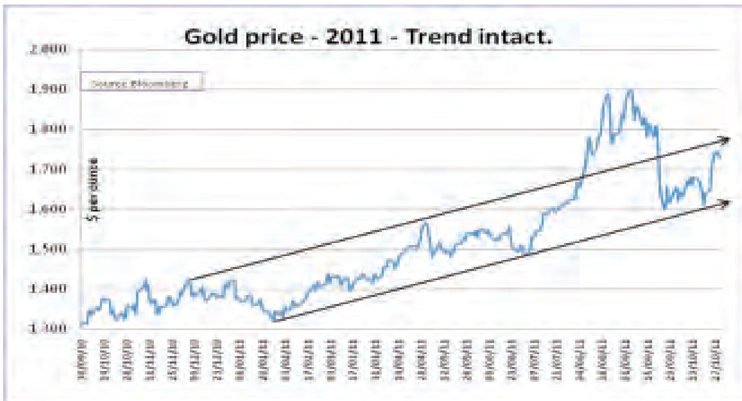
The frothy global macroeconomic situation has started to overspill into commodities. Having reaped the benefits of emerging market demand and a weaker US Dollar, commodity prices overall remained at higher levels during July and August this year, despite overwhelming economic evidence of slowing global growth - slowing mind you, not contracting. Over the past weeks, in certain areas, what was initially a series of small retreats has turned into a headlong flight from the more risky assets - something we previously noted might happen.

Oil has been quite volatile this month with a drop of West Texas to $75.87 on the 4th October on Euro sovereign default jitters. However recent price moves which saw WTI close at $93.19, a +22.83% rise from the lows, show that oil at present is moving more in line with equity markets than with underlying fundamentals. The resolution of the Libyan 'crisis' with the death of Qaddafi on October 20th, should under normal circumstances have led to a fall in oil as Libyan Sweet Crude supplies are due to resume properly under the new regime. However it is probable over the next couple of months that WTI will trade between $90 - $100 and Brent will hover between $105 and $115 as macro factors such as what is looking like a cold Northern Winter are partially offset by increased global oil production.

It is in base metals that we are seeing inventory build up combined with slowing demand - a combination that is usually toxic for the price of any such commodity. Aluminium climbed to $2,600 a tonne in July before resuming an almost continuous downward path to end this month at $2,200=. The potential for any concerted recovery looks dim as despite the new lower price making a significant number of smelters unprofitable, production slowdown in China is being seen - a distinctly negative perspective.

Copper - the darling of the markets earlier in 2011, stalled badly after hitting $9,000 a tonne and above on the fears of a slowing in the growth of mining output. The 25% correction in September to $6,800 is the reality bit that demand was a fairly obvious call. However even though the price has stabilised around $7,500 or so inventories of the metal as tracked by the London Metal Exchange (LME) are





now some 25% higher than a year ago. It is possible China could use this weakness as a chance to boost its overall copper inventories for when industrial production picks up, but this is a long shot call. Prices are likely to remain around current levels.

Cereal prices are also in somewhat of a mixed mood. Softening wheat prices last spring were justified on the back of Russia and the Ukraine re-starting exports. However when panic peaks on financial markets, speculative factors go out of the window and grains prices have seen a near 20% fall since September. Add into the equation a better than expected US harvest and what is likely to stay around its depressed 625 cents a bushel for some time to come.

In precious metals the story continues to look more positive for investors.

Unlike other commodities, precious metals first gained on the negative economic news as investors sought safe havens. The sharp correction in September was, as can now be seen, caused by fears of a short term liquidity crisis, where investors would have had to cash in their investments in precious metals merely to survive. However, current volatility aside Gold, Platinum and Palladium prices should remain positive going into year end. Interest rates are still at ultra-low levels, and concerns about sovereign debt and the general health of the global financial system will continue to support investor demand. We remain confident that gold prices will remain at current or higher levels for the near term while the possibility of a retest of the recent all time high of $1,900 cannot be ruled out in the next three months. **BUY on dips**.

Greece - the imponderable question rumbles on

Greece has increasingly fewer moves left ahead of what looks like a probable complete and utter capitulation within the next few months. The near term debt repayment schedule just for its Euro denominated debt makes for grim reading.

While the first two repayments (which will have to be counterbalanced by the issuance of new debt to replace them) on December 19th, of the 4.4% Greek Republic (Current Yield 100%), or on 22nd December of some Zero coupon paper (Yield 196%) should be manageable, the real problems begin with the 29th December 0%'s

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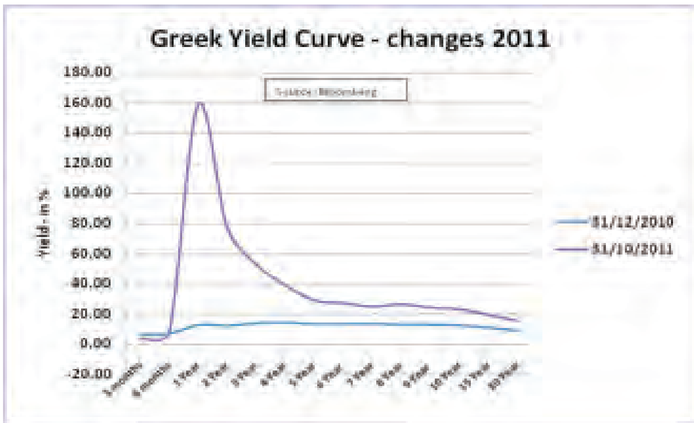
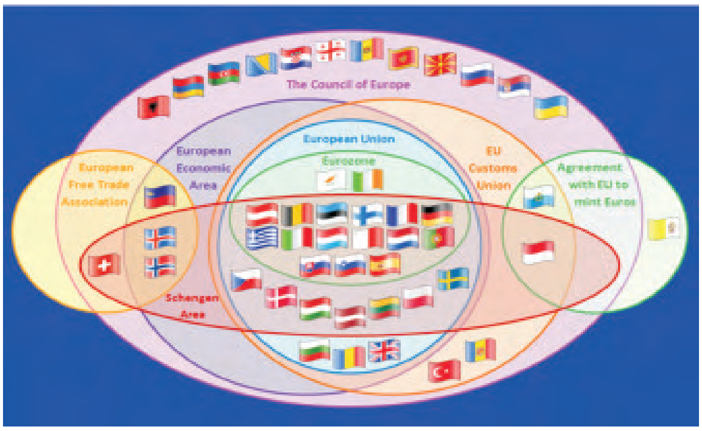
(Yield 99.5%) where some € 5.2 billion needs to be refinanced. If by some miracle this passes without a hitch then we run into more problems when the 4.3% of March 2012 matures.

Much as it pains me to say, the only reason all this is being allowed to happen is because the Euro is anything but a pure and simple currency - from the outset it has been a political creation by the French and Germans but has always lacked the fiscal stability and budgetary unity required to ensure it works perfectly.

A transfer of total economic sovereignty by the 17 Euro members to the Germans is not going to happen easily, if at all. In the past, single European currencies have worked, most notably under the Roman Empire some 2,000 years ago - but here we had not only fiscal unity, but legal, economic, cultural and linguistic as well. As such it is highly likely that we will limp on for many more months in a similar vein





with economic momentum slowing and the political will of the EU Elite most likely being thwarted by that democratic barometer of good sense, the European voter.

Realistically though, Greece has reached the end of the road.

While the charade about the current situation will continue for a many more months Greece will eventually have to accept the inevitable. If you look at the explosion of the Greek Yield curve this year it will be obvious to anyone who isn't a French or German leader that the markets have 'sussed' the Greek economy for what it is - a complete and utter shambles. The end is inevitable; it is just a question of how long the life support mechanism of continuous cash injections from the European Central Bank can continue.

The recent seismic shifts in the yield curve, especially at the shorter end where 1 year rates have exploded this year from 12% to 160% tells the real tale of how markets perceive the chances of Greece being able to rescue itself.

NONE. Greece is a complete and utter **AVOID.**

And you wondered why trying to understand Europe was so complicated...?

The above official EU Organisational chart shows the highly convoluted 'logic' of how the EU itself "works".

Right at the centre are the 17 members of the Eurozone surrounded by the other members of the European Union itself.

Surrounding all of this is the EU Customs Union which includes four micro states, the Vatican, Monaco, San Marino and Andorra but also Turkey.

However overlapping this is the European Economic Area which additionally includes Norway, Iceland and Liechtenstein. Switzerland voted against joining this but is included as part of the European Free Trade Association.

To cloud matters further there are also a series of other European and not so European Countries who have observer status at the Council of Europe- countries such as Albania, Kazakhstan, Macedonia Ukraine and Russia.

In Short...... "**Confused - You will be!"**

(* By Neil Hitchens, Senior Relationship Manager, Zenith Bank (UK)

An Appraisal of MORTGAGE As Security For Bank Lending in Nigeria

* By Deji Olanrewaju & Seun Oke

By virtue of the financial intermediation role of banks, banking is the very foundation upon which the fabrics of any economy are built. This all-important role of financial intermediation is most effectively discharged through bank lending. Given this fact, bank lending will not be possible unless it is hinged upon an assurance of recouping the money lent out. Security is highly emphasized in Nigeria because of the volatile economic climate, inconsistent government policies and the paucity of credit information on borrowers which make the granting of credit more risky than it is in more developed economies.

As shall be discussed subsequently, mortgage provides the best option for such security if the mortgage transaction is entered into with the right premises confirmed. It is however an admission of reality that mortgage transactions do not always secure the recouping of the money lent out due to certain defects in the transaction which shall be dealt with.

This work shall appraise mortgage as a security for bank lending in Nigeria. This appraisal shall involve a definition of key terms; types of mortgages; advantages of mortgage over similar transactions; the investigation of title to the mortgage property; problems militating against mortgage as an effective security for bank lending; and requisite solutions thereto.

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CONCEPTUAL CLARIFICATIONS

Mortgage

The Court of Appeal in ***Suberu v. A.I.S.L. Ltd***[1]**,** adopting the definition *in Strouds Judicial Dictionary*[2] defined a mortgage thus:

"A mortgage is a conveyance of land or an assignment of chattels as a security for the payment of a debt or the discharge of some other obligation for which it is given. The security is redeemable on the payment of discharge of such debt or obligation, any provision to the contrary notwithstanding."

The conveying party is called the ***mortgage;*** the lender is called the ***mortgagee*** while the debt for which the security is created is called the ***Mortgage debt.***

In **Stanley v. Wilde,** Lord Lindley M.R. defines a mortgage as; "a legal or equitable conveyance of title as a security for the payment of debt or the discharge of some other obligation for which it is given subject to a condition that the title shall be reconveyed if the mortgage debt is liquidated".

It is, therefore clear from the foregoing definitions that a mortgage is a conveyance of title to property that is given as security for the payment of a debt or performance of duty, the claim over which will be extinguished upon repayment and at which time the title conveyed will be conveyed back.

From the foregoing elucidations, the following features of a mortgage can be identified:

Conveyance of interest in land or some other properties by the mortgagor (this could be legal or equitable interest depending on the mode of creating the mortgage). The legal incident of the transaction,

(1) therefore, is that the owner of the mortgaged property becomes divested of the right to dispose of it until he has secured a release of the property from the mortgagee.

(2) The conveyance or the transfer is not absolute as it is subject to redemption upon repayment of the sum advanced;

(3) Consideration (loan i.e. money) must flow from the mortgagee to the mortgagor; and

(4) As a legal consequence, thereof, the mortgagor and the mortgagee have mutual rights of action and duties arising from such transaction.

Some transactions are similar to a mortgage in certain respects, it therefore, becomes imperative at this juncture to identify the distinctions which make the mortgage transaction stand out from these other transactions.

Security

Security is something pledged to guarantee fulfillment of an obligation, especially an asset guaranteeing repayment of a loan that becomes the property of the creditor if the loan is not repaid[1]. Security is therefore an insurance against unforeseen developments as it provides the banker with a cushion to fall on if every other avenue fails.

From the bankers' perspective, there are basically two types of security namely: real and personal security. Real security involves interest in some tangible property (such as land, goods, or chattels of different kinds) or intangible property (such as chooses in action) as security for loan or advances.

Personal security on the other hand involves a guarantor. It entails either a general contract of underwriting, to be primarily liable for the debt or default of another person as an indemnity contracts or an accessory – contract by which the promisor undertakes to be liable only on the inability of the principal debtor or insufficiency of his assets to meet his obligation as in contract of guarantee.

Characteristics of Bank Securities

Some essential characteristics of bank securities include:

a) Sufficiency: The value of the bank security must be adequate to cover the bank's entire exposure. In order not to be stung by possible downward fluctuations in value, it is necessary to leave sufficient margin between the value of the security and the amount advanced as loan.

b) Valuation: A good banking security must be capable of being valued objectively. Besides, its valuation must be free from any form of sentiments.

c) Good Title: The efficacy of a mortgage transaction depends on the security of title. The title of the customer to the property must not be questionable and the land must have been registered and must be free from any encumbrances in order to have a good title also a search at the land registry should reveal that the land mortgaged to the bank actually belongs to the customer. So also share certificate deposited by the customer must bear his name.

d) Enforceability: The security contract once legally perfected should remain legally binding and enforceable. If the customer defaults, and any problem arises, the bank should not find it difficult to seek legal assistance and the security should not be capable of being invalidated. The bank should ensure that it takes all necessary steps in perfecting its security; also the security will be invalidated due to lapses or lacunas.

e) Easy Transfer of Title: The title of the property used as security must be easily transferable from the depositor to the bank. Similarly after payment of debt the title to the property must be easily re-assignable to the depositor without much problem. For this purpose, the transfer of title in a legal charge is much easier than transfer of title in a legal mortgage on a landed property.

In general, the type of security demanded by a bank depends on the following:

1) The amount of the loan
2) The nature of the facility being sought
3) The duration of the loan
4) The integrity and financial strength of the borrower.

Bank

Section 66 of BOFIA (Banks and Other Financial Institutions Act, 2004) defines a bank as any bank that is licensed pursuant to the provisions of the Act. This definition is not helpful for the purpose of this discourse.

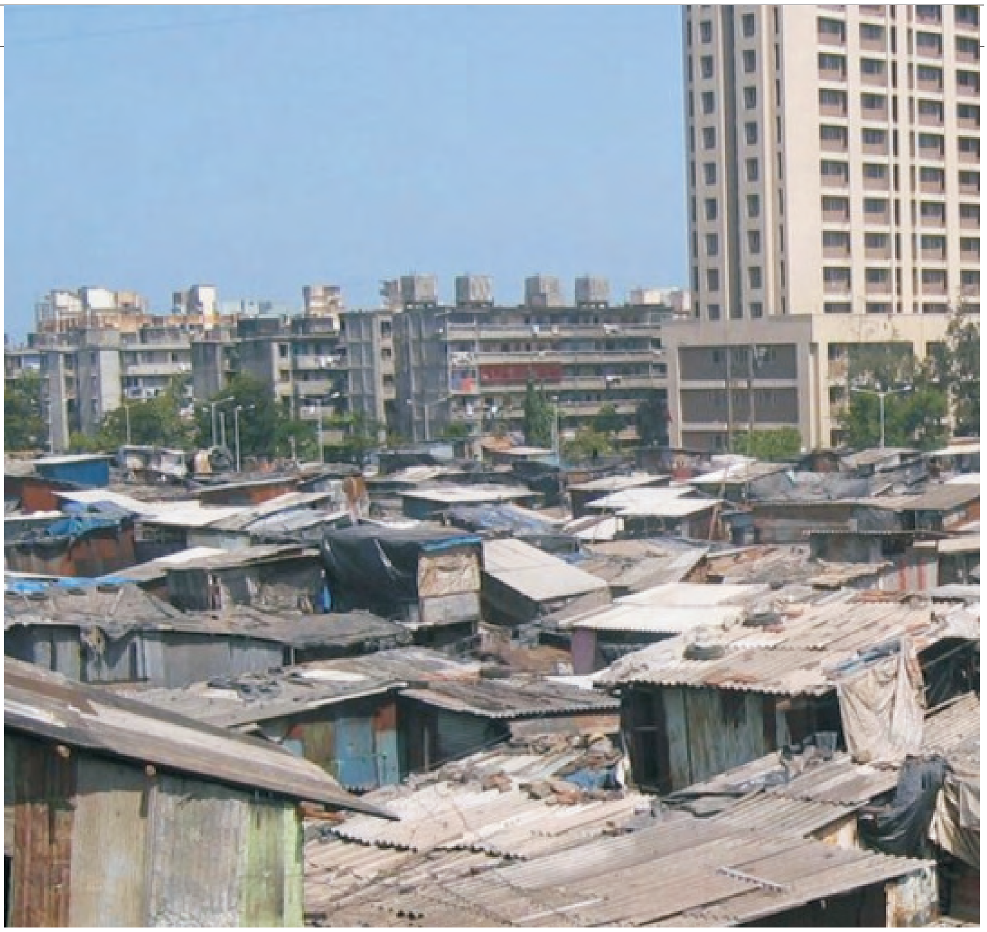
A bank, as far as this work is concerned, is an institution charged with the responsibility, *inter alia*, of financial intermediation in a particular society. Financial intermediation is the process of channeling funds from those who have money to those in need of money, often in the form of loan and other credit facilities.

TYPES OF MORTGAGE

There are two types of mortgages namely: legal mortgage and equitable mortgage.

Legal Mortgage: A legal mortgage involves the transfer of legal interest in land, whether leasehold or freehold, to the creditor (mortgagee) on condition that the legal title will be retransferred if the secured debt is repaid as at when due (subject to the equitable rights of the mortgagor). Legal mortgage is the best form of security because it offers certain and effective remedies on default without burdening the creditor with actual possession of the property before defaults occur. For example, a legal mortgagor can foreclose unlike an equitable mortgagor who has to resort to the court to exercise his right of sale.

A legal mortgage creates a superior interest and gives priority over all creditors, with respect to prior or subsequent non-registered mortgage. Priority is de-



termined according to the date by which each mortgage was registered.

Creation of Legal Mortgage: The creation of legal mortgage in Nigeria is dependent on where the property is situated. Three jurisdictions can be identified for this purpose, namely: under the Registration of Title Conveyancing Law (1959) States; the Conveyancing Act States (1882); and the Registration of Title Law (1994).

1) **Conveyancing Act States**
No statutory provision governs the mode of creation of legal mortgages in these states; the applicable law is therefore still the common law subject to modifications introduced by the Land Use Act, 1978. Stemming from the effect of the Land Use Act which is to extinguish the concept of freehold interests in land[2], the relevant principles are those relating to a legal mortgage of leasehold interest at common law. Two ways of creating a legal mortgage of leasehold interest at common law are:

a) Assignment of the entire leasehold interest of the mortgagee subject to a provision for cesser on redemption.

b) Sub-demise with a provision for redemption when the loan is redeemed.

While a legal mortgage created by assignment transfers to the mortgagee the mortgagor's unexpired interest there being no reversionary interest in the mortgagor, that created by sub-demise does not remove the mortgagor's reversionary interest.

2) **Property and Conveyancing Law States**
For properties situate in these areas, *Section 109 of the Property and Conveyancing Law, 1959* provides for two ways of creating a legal mortgage over leasehold interest in land, namely:

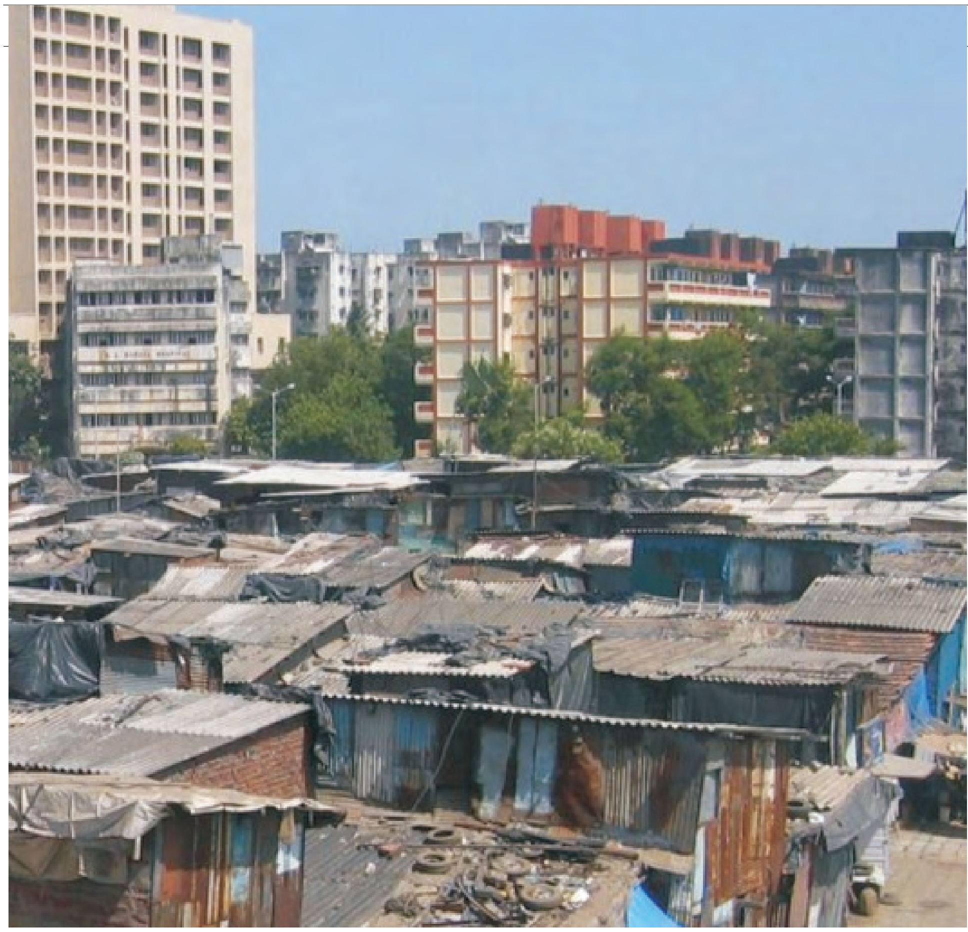
a) A sub-demise for a term of years absolute, less at least one day than the term vested in the mortgagor, and subject to a provision for cesser on redemption;
b) Charge by way of legal mortgage: where the mortgagor has a right of occupancy or a sublease, he may decide to create a charge by deed expressed to be by way of legal mortgage.

3) **Registration of Title Law**
The Lagos State *Registration of Title Law, section 18* provides that; the registered owner of land may in prescribed manner charge the land or lease with the payment of money to the like extent as if the land was not registered land. The charge is completed by entry in the register of the particulars of the mortgage and the registration of the charge in the land registry Form 5.

Equitable Mortgage
An equitable mortgage is one which the creditor or the mortgagee receives only an equitable interest in the property. Any form of agreement involving transfer of equitable interest in land or property as security for loan is essentially an equitable mortgage. Equitable mortgages are the preferred method of creating security for a short-term loan; but it is not as secured as the legal mortgage as it is susceptible to fraud.

Creation of Equitable Mortgage
An equitable mortgage can be created by;
1) Deposit of title deeds.
2) An agreement to create a legal mortgage and
3) Equitable charge of the mortgagor's property
4) Equitable Mortgage of Registered Land

Equitable mortgage can be used in the following circumstances:
a) Where the mortgage sum is small
b) Where the time for repayment is short; and
c) Where there is urgency in the transaction or the mortgagor is in urgent need of the fund which cannot wait for the long process of perfection of title such as securing the governor's consent.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Advantages of Legal Mortgage over Equitable Mortgage

1) Enforcement: It is easier to enforce a legal mortgage unlike an equitable mortgage which cannot be enforced unless by court order.

2) Priority: Where there is a legal mortgage and equitable mortgage created over the same property, the legal mortgage will have priority of interest because where there is *equity, the law prevails.*

3) Fraud: Fraud is more prevalent with equitable mortgage than with legal mortgage, since the documents are registered under the latter.

ADVANTAGES OF MORTGAGE OVER SIMILAR TRANSACTIONS

Mortgage is not the only option open to banks in their lending operations. Other forms of security exist outside mortgage to which they may turn. However, the use of mortgage is pervasive over other forms of transactions. It is therefore pertinent to examine the uniqueness of mortgage as a security for bank lending and its preferablity over other options.

Advantages over Pledge

1) From the perspective of the customer, a pledge involves the delivery of possession as security for the keeping of a promise or the payment of a debt. This means that the pledgor will be deprived of the opportunity to make use of his property until he repays the loan. This makes a pledge less attractive compared with a mortgage.

2) From the perspective of the bank, since the pledgee has no interest in the pledged land other than possession, the pledgee cannot ordinarily sell the land without a court order on the principle of *nemo dat quod non habet*[3] and *once a pledge is always a pledge*[4]. A legal mortgage on the other hand offers the power of sale to the bank should the customer default in payment.

Advantages over Lien

1) A mortgage can be created by a bank with the agreement of a customer unlike a lien which only arises by operation of law. For this reason, a mortgage is a more attractive option for bank lending.

2) A possessory lien usually confers on the lienee a right of retention so that except in some special cases the lienee cannot obtain his interest in the property by sale, so also he possesses no right of foreclosure either by law or equity. A mortgage on the other hand, offers the bank with the power of sale and foreclosure.

Advantages over a Charge

A charge unlike a mortgage is a mere appropriation of specific property for the discharge of an obligation without transfer of title or possession to the obligee. The charge obtains no estate at all in the land, but has merely a right of payment out of the property. An equitable chargee cannot foreclose because he acquires no title under the charge and therefore has nothing which can be made absolute, although his interest in the security can be realized by obtaining the appointment of a receiver of the rent and profits and, if it becomes necessary, by a judicial sale.

Advantages over a Conditional Sale

A conditional sale refers to a transaction where a property or land is sold to a person with right reserved for the vendor to repurchase it upon the occurrence or non-occurrence of certain conditions. A mortgage may be preferable to a conditional sale because of the mutual remedy it vests in the mortgagee and mortgagor.

INVESTIGATION OF TITLE

The efficacy of a mortgage depends on the security of title. For this reason therefore, it is pertinent to briefly examine the steps involved in the investigation of title for a mortgage security. There are two issues that the mortgagee should be concerned with before advancing a loan on security:

a) The title of the borrower; and

b) The value of the property

The essence of investigation is to ensure that the mortgagor is in fact the owner of the property he is giving as security to the bank; that he has not already charged the property in favour of another bank or creditor and that there are no encumbrances against the mortgage property.

The practice is for the legal department of the bank to instruct external solicitors to conduct searches on the mortgage property. The solicitor should be thorough in establishing the worth of the title documents using known conveyancing techniques prescribed by law. After the search, the solicitor writes a report that is sent to the bank for consideration.

The following should be covered in a search report:

1) Date of search
2) Name of borrower
3) Name of person giving security, if different from borrower
4) Description of property
5) Title of the borrower or person giving the security
6) Encumbrances, registration and other adverse facts as may be observed from;
   (a) Physical inspection of the land or building
   (b) The register at the land registry
   (c) Register at the Corporate Affairs Commission
   (d) The memorandum and articles of association of the borrower (if a company) in respect of land holding
   (e) Government acquisition: whether the property is within the area compulsorily acquired by government or proposed to be so acquired.
7) Conclusion, stating in unequivocal terms that the borrower or person giving the security has a good title (or otherwise) to the property and has an unencumbered power to charge it to the bank as security for a loan[5].

The mortgagee may at any time withdraw from the transaction if not satisfied with the mortgagor's title.

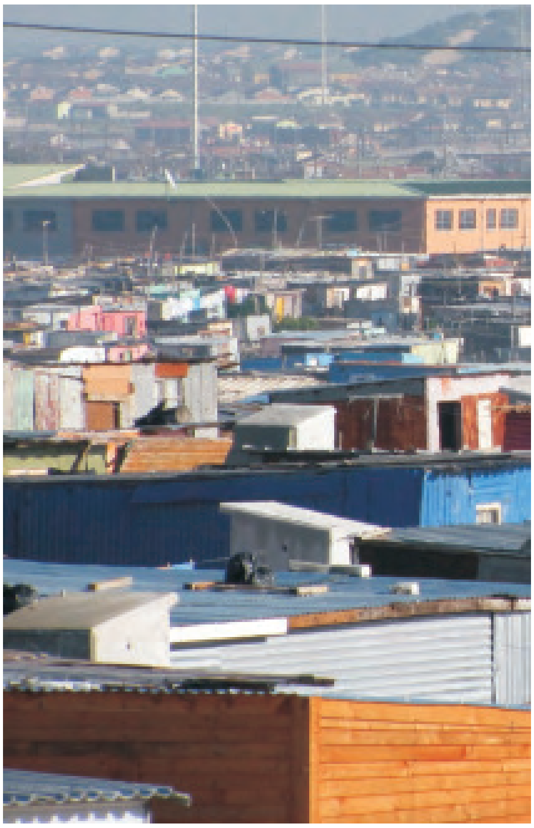
PROBLEMS MILITATING AGAINST MORTGAGE AS AN EFFECTIVE SECURITY FOR BANK LENDING IN NIGERIA

Notwithstanding the preferability of mortgage over other transactions as a security for bank lending in Nigeria, certain problems which bedevil the transaction make it less attractive than it should be. These problems shall now be discussed *seriatim.*

1) Defects in Title: A fundamental truism about mortgage is that the efficacy of mortgage transactions depends on the security of title. Since the security of the mortgage property is the assurance that the mortgagee relies upon it as a cushion in the event that the mortgagor defaults, it would amount to business suicide if that title turns out defective. A mortgagor with a bad title cannot give a good security since he cannot give what he does not have in line with the maxim, *nemo dat quod non habet.* The reason for this problem is that many of the titles to land in Nigeria are defective and banks, sometimes through their negligence in investigating title, have lost mortgage security to defective titles.

2) Valuation: This is another problem which stems from improper investigation of the mortgage security. Sometimes, insufficient margin is left between the value of the mortgage property and the amount of the advance. Also, due to lack of a thorough and objective valuation of the mortgage property, many banks are not able to recover a portion of the loan advanced.

3) Governor's Consent: Section 22 of the Land Use Act requires the governor's consent to be obtained for the alienation of any interest in land. The consequence of a failure to obtain this consent is that the conveyance will be rendered void by virtue of section 26 of the Act. This provision cost Savannah Bank a fortune in ***Savannah BANK Ltd. v. Ajilo***[6] were the Supreme Court held that failure to obtain governor's consent is at the detriment of the mortgagor. Although, the



court relaxed its stance in ***Awojugbagbe Light Industries Ltd. v. Chinukwe and Anor***[7]***,*** this does not totally absolve banks of this problem.

4) Limitation Statute: Section 12(1)(a) of the Limitation Law of Lagos State limits a mortgagee's right of action to enforce a mortgage to 12 years from the date when the right of action accrued which is the date for repayment with regard to the principal sum and interest. In ***Lewis v. Plunket***[8]***,*** it was held that once the right of the mortgagee is statute barred, the mortgagor is entitled to have the title deed back without paying money due under the mortgage. Thus, banks which do not enforce their mortgage security within 12 years run the risk of losing the money advance as loan.

5) Equitable Rights of a Mortgagor: The mortgagor's equitable rights, namely: the equity of redemption and the equitable right to redeem, also constitute a problem for banks in using mortgage security. The equity of

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redemption is the right of the mortgagor to recover the security by discharging his obligations under the mortgage within the duration of the mortgage contract. The equitable right to redeem on the other hand is the right of a mortgagor to redeem notwithstanding that the date for repayment has elapsed. These rights are beneficial to the mortgagor but often create problems for the bank (mortgagee). For example, where the mortgagor is unable to redeem on the legal due date, he may still redeem by virtue of his equitable right to redeem before the property is finally auctioned[9]. Moreover, these rights cannot be waived by agreement as held in ***Seton v. Slade.*** Any agreement, term or condition which purports to restrict or suspend redemption till a certain date will be perceived by the court as a clog on the mortgagor's equity of redemption[10].

6) Bad Loans: Some banks, perhaps in ignorance of the importance of mortgage security, advance loans without the requisite collateral security or with insufficient security. The recent incidence in Nigeria whereby the Central Bank of Nigeria (CBN) discovered that some commercial banks granted loans not backed up with adequate security illustrates this problem. In furtherance of this discovery, the CBN Governor sacked the Managing Directors of Oceanic Bank and Intercontinental Bank, Cecilia Ibru and Erastus Akingbola respectively.

7) Government Acquisition: Although the title to property may be in order, there may be a problem with regard to the compulsory acquisition of property by the government. Since the Governor is the custodian of all lands within the state, he may acquire such lands for public purposes in which case compensation should be paid. Compensation is however not payable where the property, for example is not backed up by building approval or survey plan. Banks who accept such defective mortgage security run the risk of losing their money as they will be unable to receive compensation from the government to realize the mortgage security.

8) Macro-Economic Instability: Macro-economic instability may also constitute a problem in the bank use of mortgage as security for lending. Economic instability may affect the value of the mortgage property. This is especially where the property used as security is personal property or a *chose in action*. The recent crash in the value of shares in Nigeria illustrates this point. Land is, however, a relatively better security as it is less prone to depreciation in value.

9) High Interest Rates: Banks are often moved by economic conditions to increase their interest rates. This in turn scares away potential mortgagors who do not see the feasibility of collecting loan facilities with exorbitant interest rates.

10) Capacity: Capacity is an important element of the mortgage transaction. Mortgages to infants, for example, are void and unenforceable under the *Property and Conveyancing Law, 1959*. The risk, here is that loans advanced to infants under a mortgage transaction will not be recoverable by the bank. This problem stems from the negligence of the bank in investigating the capacity of the mortgagor.

11) Fraud: Fraud is another problem bedeviling mortgage as a security for bank lending in Nigeria. Unsuspecting banks sometimes fall prey to dubious and fraudulent mortgagors who offer defective titles as security. It is pertinent to add that equitable mortgages are more susceptible to fraud than legal mortgages.

PROPOSED SOLUTIONS TO THE PROBLEMS

The above problems water-down the attractiveness of mortgage as a security for bank lending. These problems may however, be averted or at least ameliorated by adopting the following recommendations:

With regard to the problem of **defective title, valuation, capacity and fraud,** banks should in order to avoid falling prey to the problem of

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defective title, carry out proper investigations should be conducted into the title of the mortgagor and the valuation of the mortgage property. In order not to be stung by possible downward fluctuations in value, it is necessary to leave sufficient margin of safety between the value of the security and the amount advanced as loan. This is also to avoid being stung by **macro-economic instability.** The capacity of a prospective mortgagor should be thoroughly investigated in the light of the consequence of advancing loan to an infant. Banks should endeavour to opt for legal mortgage over equitable mortgage.

To avert the problem of **governor's consent,** banks should endeavour to incorporate into the mortgage, a requirement for obtaining governor's consent. They should also not advance any loan facility without the fulfillment of this condition.

With respect to **limitation statutes,** banks should not delay in enforcing their rights of sale and foreclosure. Like the maxim goes, *vigilantibus et non dormientibus, jura subvienent,* equity aids the vigilant and not those who sleep on their rights. Banks should foreclose or exercise their right of sale without delay or apply to the court for the appointment of a receiver depending on the nature of the mortgage. This also applies with regard to the problem of the **mortgagor's equitable rights.** Banks are advised not to insert any term which may act as a clog on the mortgagor's rights mentioned above. This is in the light of the courts attitude to such terms as stated by Muntka-Coomasie J.C.A in Ahaneku v. Iheaturu[11] "*in view of equity, the essential object of mortgage is to afford security to the lender, and as long as security remains intact there is no justification for expropriating the propery of the mortgagor merely because of his failure to make prompt payment"*. Thus, imposing a penalty of additional interest rate upon default of payment will be void[12].

With regard to the problems of **government acquisition** and **bad loans**, proper and thorough investigations should be conducted by banks before advancing loans. The property should be properly investigated to confirm that the building plans and other documents are in place to entitle the bank to government compensation in the event of a compulsory acquisition of the property. Also, banks should not be swayed by the good reputation of the mortgagor in bypassing the requirement of good collateral security. The Central Bank should also ensure that corporate governance is effective and strict, and uncompromising in banks to avoid a repeat of the bad debt history in the Nigerian banking sector.

CONCLUSION

In conclusion, the utmost desirability of mortgage transactions to banks cannot be denied as they yield a huge proportion of bank profits through interest rates. However, this attractiveness is watered down by the problems identified above. Banks should adopt the solutions proposed to ensure that the scale of pros and cons is tilted in their favour, rather than against them.

(*Deji Olanrewaju & Seun Oke) are both lecturers of the department of International Law, School of Law & Security Studies, Babcock University, Ilisan, Ogun State.)

END NOTES

[1] Microsoft Encarta 2009. 1993 – 2008 Microsoft Corporation.

[2] It is noteworthy that an assignment by the mortgagor of the totality of his interest in the mortgaged property in any of the states governed by the property and conveyancing legislations is not void, but takes effect as a conversion of the interest or estate so assured to the mortgagee into a term of years as held by the Nigerian Supreme Court in Nigeria Housing Development Society Ltd. v. Ogundepo, per Coker J.S.C.

[3] Adjei v. Dabanka (1930) WACA 63.

[4] Okoiko v. Esadalue

[5] Imhanobe, S.O, Legal Drafting and Conveyancing, Second Edition (Sylvester Imhanobe Legal Research Ltd, 2007) p 370 – 372.

[6] (1989) 1 N.W.L.R.)Pt. 97) 305.

[7] (1995) 4 S.C.N.J. 162.

[8] (1937) Ch. 306

[9] See Federal Administrator General & Ors v. Cardozo & Ors (1973) 1 ANLR (Pt. 2) 154.

[10] Howard v. Harris

[11] Suit No. CA/E/131/87 (1995) 2 NWLR.

[12] See Reeve v. Lisle.


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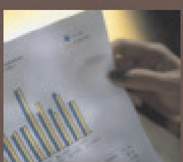


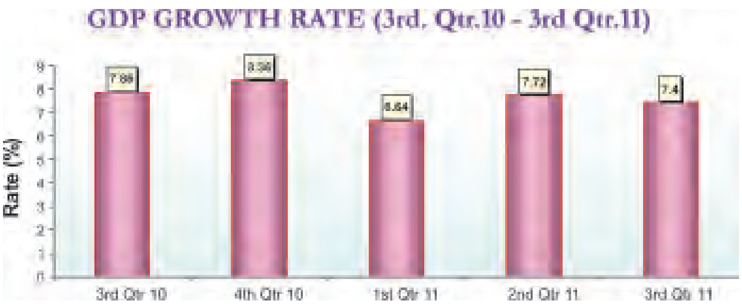
Ibrahim Abubakar

MACROECONOMIC ENVIRONMENT

The Nigerian economy in the third quarter 2011 recorded some major improvements. While some of the indictors got off to a solid start but stalled somewhat along the line, others maintained a strong momentum all through. Inflation figure, for instance, inched up slightly despite hitting the authority's single digit target at a point. Gross Domestic Product (GDP) contracted slightly but ended higher than expected. The nation's currency, the naira, lost grounds against other major currencies. The foreign exchange reserves shrank slightly during the quarter. The Monetary Policy Rate (MPR) was raised in efforts to keep the lid on inflation. In the capital market, bearish sentiments dominated activities once again. However, in the international crude oil market, prices remained relatively strong despite some major fluctuations.

GROSS DOMESTIC PRODUCT

Growth in Nigeria's Gross Domestic Product (GDP) was estimated at 7.4 percent in the third quarter 2011 as against the 7.8 percent recorded in the same period in 2010. Real GDP growth was mainly driven by the non-oil sector. Despite being the peak flood period in the Southern parts of the country, good rains and early harvests in the northern region continued to boost agriculture as a major contributor to GDP. For the oil sector, the dividends of the Amnesty Deal with the Niger Delta militants continued to yield positive results despite a slight drop in production due to operational constraints experienced by some of the oil producing companies. Real GDP growth rate in 2011 is projected at 7.85 per cent which is slightly lower than the 7.87 percent recorded in 2010.

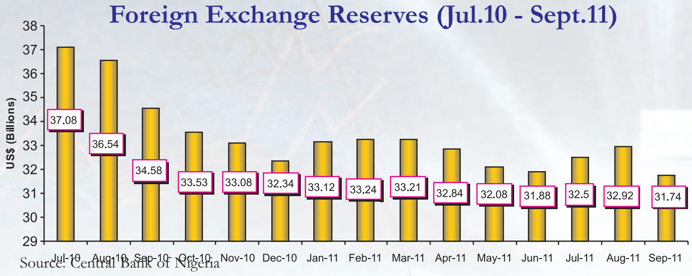


Source: National Bureau of Statistics

INFLATION

The Year-on-Year inflation rate ended the third quarter where it left off despite decelerating for much of the period. Inflation rate ended the quarter at 10.3 percent in September. However, against expectations, the headline rate was brought down to a single digit figure of 9.4 percent in July and 9.3 percent in August, the lowest level since May 2008. Inflationary pressure moderated significantly due to the harvest of early maturing crops such as maize, tomatoes, vegetables, potatoes and fruits. Despite the positive signs however, higher prices of household items such as building materials, diesel, kerosene and electricity charges resurfaced in September. In the months ahead, inflationary threats remain due to anticipated capital budget releases running up to year end; increased government borrowing to finance the fiscal deficit in the 2011 budget; the recent upward revision of electricity tariff and the anticipated deregulation of petroleum product prices, among others.

Source: National Bureau of Statistics



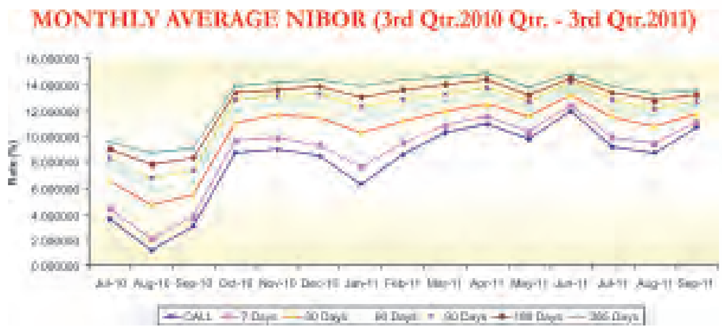
Source: Central Bank of Nigeria

EXTERNAL RESERVES

The nation's external reserves shrank marginally in the third quarter 2011 despite a sharp pick up in output and crude oil receipts. External reserves recorded impressive gains earlier in August, gaining about $4.1billion to $35.9billion. The buildup was due to inflows of royalties into the federation account as well as foreign capital injection. Leakages however remained as the surge was short-lived. Unable to plug the holes, external reserves tumbled back to $31.8billion as at end September 2011, capable of financing up to 14 months of imports. The authorities attributed the development to huge costs of refined petroleum products subsidy; Joint Venture Cash Call (JVC) as well as high import bills. In the near to medium term, the authorities project improvements in the stock of external reserves as a result of higher crude oil prices and output.

INTEREST RATE

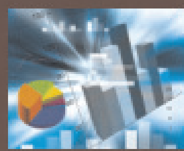
In a move widely anticipated, the CBN maintained its hawkish stance and raised its key interest rate twice during the third quarter. The first hike came a bit higher than expected in July when the apex bank lifted its Monetary Policy Rate (MPR) by 75 basis points to 8.75 percent. The second increase in September, coming earlier than anticipated, lifted the MPR by 50 basis points to 9.25 percent, in bid to hold back inflation.

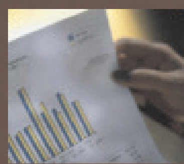


Source: Financial Markets Dealers Association of Nigeria (FMDA)

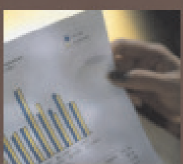
Source: Financial Markets Dealers Association of Nigeria (FMDA)

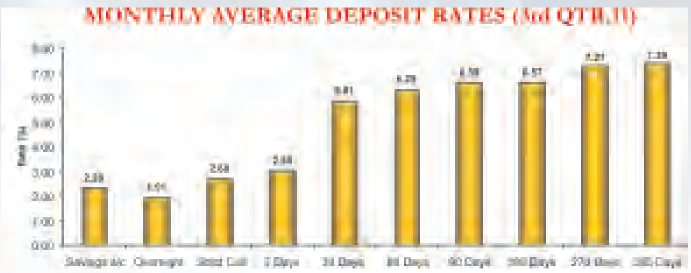
The average interbank rate witnessed significant swings during the quarter. For instance, rates on the call and 7 Day tenors dropped as low as 7 and 7.9 percent, respectively in August, despite the upward review of the MPR in July. The market was awash with liquidity coming from a total of N1.3trillion FAAC allocations shared among the three tiers of government. Rates however picked up in August as a result of aggressive mop up operations by the apex bank. The upswing was nevertheless short-lived as about N616billion trickled down the system in August.





Facts & Figures





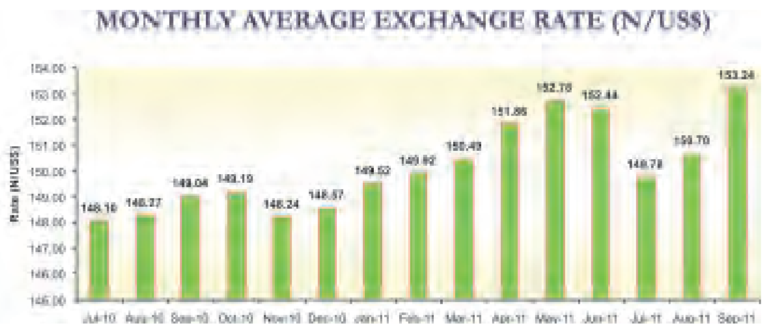
Source: Financial Markets Dealers Association of Nigeria (FMDA)

Despite the inflows, rates inched back up in September due to huge NNPC remittances and WDAs funding.

In terms of cost of borrowing, the average Prime Lending Rate (PLR) inched up slightly due to risk aversion. Despite lending rates remaining at elevated levels (hovering around 17 percent), it nevertheless eased in September due to extension of guarantees to some rescued banks in August.

Returns on the average deposit rate remained relatively stable across most investment horizons, with volatility higher on the longer term tenors.

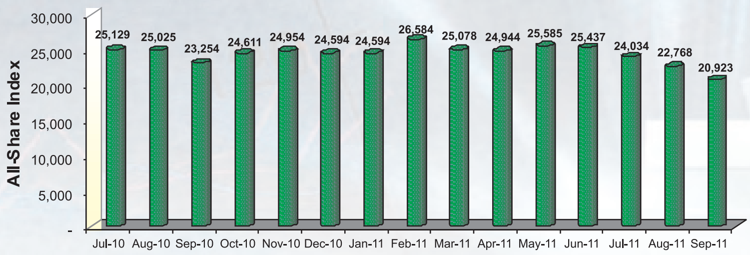
EXCHANGE RATE



Source: Central Bank of Nigeria

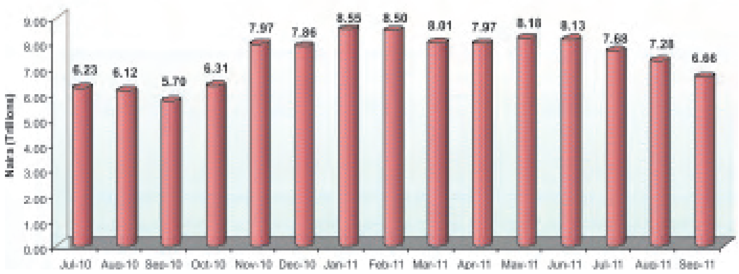
The nation's currency, the naira, depreciated close to record low levels in the third quarter 2011, losing grounds against major world currencies, but closing around CBN's target. It finished the period within whiskers of its weakest target limit at about N154/US$. The naira witnessed volatile movements against the US dollar, reaching record low levels in the interbank market. Stronger demand for the greenback resurfaced earlier in August with the nation's currency coming under severe pressure from downstream oil companies; foreign investors and multinationals repatriating dividends. In its twice weekly auctions, the CBN offered about $9billion and sold $9.2billion against the $11.6billion demanded during the period. The gap was nevertheless filled by inflows from oil majors and telecoms companies. To check speculative bids, the CBN lifted restrictions placed on dollar purchases by Bureaux de Change (BDCs) and sold $10million to all banks operating BDCs. The nation's currency nevertheless, reached its lowest level in more than two years when it reached N157.92/US$ at the interbank market, trading outside the weakest edge of its target (+/-3 percent). The premium between the official and the interbank rate widened to 3.2 percent as at end September 2011, compared to 1.2 percent in June. In the months ahead, pressure on the naira is expected to moderate as foreign investors take advantage of higher rates of return.

ALL SHARE INDEX (ASI) (3rd Qtr.11 - 3rd Qtr.11)



Source: Nigeria Stock Exchange

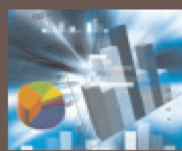
CAPITALISATION NSE MARKET CAPITALISATION (3rd Qtr.10 - 3rd Qtr.11)

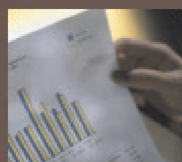


Source: Nigeria Stock Exchange

CAPITAL MARKET

The capital market ended the third quarter with heavy losses retreating to earlier low levels despite slight gains in June. It was a grim end to the quarter as the All-Share Index (ASI) and market capitalization finished disappointingly lower at 20,373.00 and N6.49trillion, respectively, down from 24,980.20 and N7.98trillion in the preceding quarter. The ASI suffered its biggest drop for more than 21 months, slashing about 18 percent compared to 9 percent in the same period in 2010. With the market at a crossroad, risk aversion crept in as some investors positioned themselves to withstand a possible further market depression. The nationalization of three deposit money banks sent the market into a free fall in August with investors losing about N591billion as their stocks were delisted from the market. With the absence of positive news, funds were transferred to the money market and cash holdings rather than to equities. Investors waited nervously for the outcome of the September 30th recapitalization exercise. Despite the uncertainties however, a glimpse of colour in an otherwise dull quarter came with the submission of Transaction Implementation Agreements (TIA) to the Securities and Exchange Commission by five of the rescued banks and their new investors/partners. Confidence was further boosted as a number of quoted companies such as Flour Mills of Nigeria; PZ Cussons and Seven-Up Bottling Company paid impressive dividends of N2.00; 86kobo and N2.00, respectively. Market fundamentals remained strong as the NSE admitted N25billion Edo State Infrastructural Development Bond on the daily list.

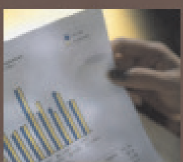




Facts & Figures








OIL & GAS

Crude oil prices declined in the third quarter of 2011, back to the levels a year earlier. Oil prices tumbled more than 17 percent, the biggest percentage loss since the second quarter of 2010. Prices were last witnessed that low in September 2010. Oil prices which hit about $114 a barrel in May this year has since slumped 31 percent, owing to worries about the prospect of the global economy. Nigeria's brand of crude oil, bonny light, shed $16, its weakest quarterly performance in five quarters. It traded within a band of $79-$95 per barrel. Industry analysts attribute the slump in crude oil prices to several factors such as the Euro zone's debt crisis; slowdown in China's manufacturing output; weaker demand in the United States despite the summer driving season as well as expected return of oil exports from Libya. At the end of the joint EU-OPEC Energy Dialogue in Vienna, Austria, both parties identified threats to price stability coming from lower economic growths, consumer country policies, discriminatory taxation, industry costs, technology as well as human resources.

Oil Prices: Monthly Average Price Movements (3rd Qtr.10 - 3rd Qtr.11)