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Special remarks at the CBN Executive Seminar on "Financial Sector Development, Economic Growth and the Nigerian Economyâ€.

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Special Remarks

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The Governor, Central Bank of Nigeria,
Deputy Governors,
Departmental Directors,
Branch Controllers,
CBN Executives,
Distinguished Resource Persons,
Ladies and Gentlemen.

1. It is my honour and pleasure to make these special remarks at this opening ceremony of the 19th edition of the annual in-house Executive Seminar organised by the Research Department in collaboration with the Human Resources Department. As usual, the Seminar is aimed at availing the Executives of the Bank the opportunity of brainstorming on contemporary issues in the domestic and global economies. In this regard, the theme of this year's Seminar "**Financial Sector Development, Economic Growth and the Nigerian Economy"** is quite germane, given the current efforts of the Bank in repositioning the sector to play its catalytic role of financial intermediation and financing growth.

2. Indeed, a well-developed financial sector plays an important role in the overall economic development of any country. This is why many countries in the world have undertaken one form of financial sector reform or another over the past decades to minimise vulnerabilities, which often result in financial crises, economic slowdown and huge fiscal costs. The goals of such reforms are always directed at invigorating the economy and putting it on the path of sustainable growth. It is within this context that the significance of the theme of this year's Seminar can also be situated.

3. Theoretical and empirical studies on the nexus between finance and economic growth are replete in the literature. Empirically, there are three strands of opinion on the nexus between financial development and economic growth. The first is premised on the view that the direction of causal relationship proceeds

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from financial development to growth. The second is that growth impacts financial development, while the third embodies a symbiotic view of a bi-directional causality between financial development and economic growth.

4. Modern growth theory identifies two specific channels through which the financial sector might affect long-run economic growth, namely its impact on capital accumulation (including physical as well as human capital) and the rate of technological progress. These effects arise from the intermediation role provided by financial institutions, which enable the financial sector to mobilise savings for investment, facilitate and encourage inflows of foreign capital and optimise the allocation of capital between competing uses.

5. Experience in some countries has shown that the financial sector, if properly developed, could serve as an engine of growth through the promotion of rapid economic transformation of a nation. Another important role of the financial sector is the redirection of savings from a less desirable form to a more desirable one; e.g. from a relatively liquid and short-term form to a relatively longer-term form.

6. Financial sector development can be measured by its efficiency and competitiveness, range of financial services that are available, diversity of institutions which operate in the sector, amount of money that is intermediated through the sector, the extent to which capital is allocated to private sector, the response to market signals and regulation, and stability of the sector.

7. Distinguished Ladies and Gentlemen, let me state that the financial services industry can only support economic growth if the financial institutions are largely sound and efficient, and have proper governance structures that would guarantee investors' confidence in the system. The main anchors for the attainment of these objectives essentially relate to proper financial regulation and supervision as well as the overall institutional and legal framework governing contractual relationships among economic agents.

8. In Nigeria, the evolution of the financial sector has had a chequered history in terms of stability and instability. Prior to the reforms of 1986, the financial sector in Nigeria was highly repressed. Interest rate administration, selective credit controls, ceilings on credit expansion and use of reserve requirements and other

direct monetary control instruments were typical features of the banking sector. Entry into banking business was restricted and semi-public or government agencies owned majority of the financial institutions that dominated the financial services industry, such as banks and insurance companies. Operations in the sector were a lot riskier as there was no deposit insurance to provide safety net for depositors. The financial environment was generally inefficient, illiquid and insolvent, as evidenced by negative capital adequacy ratios and complete erosion of shareholders' funds, leading to lower return on assets.

9. The neo-liberal era witnessed the dismantling of the regime of economic and financial controls to pave way for increased reliance on market forces in 1986, in line with the general philosophy of economic management under the Structural Adjustment Programme (SAP). The reform measures implemented included, deregulation of interest and exchange rates control, removal of sectoral credit allocation and removal of restriction on free entry into banking business subject to meeting the conditions for obtaining a banking licence. A major reform was the establishment of the Nigeria Deposit Insurance Corporation (NDIC) in 1988 to provide safety nets and strengthen the regulatory and supervisory framework. The liberalization of the financial system, no doubt, engendered reasonable level of competition among the banks. But with a paucity of good managerial prowess and unbridled growth in financial institutions and instruments, systemic distress that was akin to those witnessed in the days of zero regulation of banks set in. The development led to high rates of inflation, large government deficits, inadequate capital base as well as fraud in the financial institutions, particularly banks, resulting in its limited impact in terms of improvement in the efficiency of the allocation of resources in the economy.

10. In response to these problems, the CBN in 2004, initiated and implemented another reform in the sector – the Bank Consolidation Programme. The thrust of the policy was to grow the banks and position them to play pivotal roles in driving development in other sectors of the economy, as well as induce improvements in their operational efficiency.

11. Furthermore, the capital market was deregulated, prudential guidelines were issued to compel banks to adopt a uniform standard for risk asset classification and loan loss provisioning and the indirect monetary policy instruments were adopted. In addition, the mandate of the Bank, as derived from

the 1958 Act of Parliament, has been amended in 1991, 1993, 1997, 1998, 1999 and 2007 to confer greater powers on the CBN in the areas of banking supervision and examination, monetary management and enforcement of prudential standards in the banking industry.

12. In terms of market developments, the Bank carried out a number of reforms in the Nigerian payments system and continued to ensure effective monitoring of existing and planned payments system initiatives. Consequently, there have been improvements in the payments system. For instance, the clearing cycle has been reduced from 21 working days to T + 2 and efforts are being made to further reduce it to T + 1. In addition, the banking environment has become increasingly competitive as evidenced by the emergence of various banking products such as electronic payment cards and products, including automated teller machines (ATMs), point-of-sales (POS), debit cards, credit cards, internet banking, telephone banking, and mobile banking. The Bank developed and issued guidelines to operationalise all these products. Furthermore, the Bank had licensed a central switch to carry out all switching transactions in the country.

13. Distinguished ladies and gentlemen, in the wake of the recent global financial crisis, and in realisation that financial instability can affect the macroeconomic environment with adverse consequences for economic activity, price stability and the monetary policy transmission process, the Bank articulated a blueprint for reforming the Nigerian financial system, in general, and the banking sector, in particular, in the next ten years. The blueprint tagged "**The Alpha Project Initiatives of the CBN"** was built on four pillars of enhancing the quality of banks, establishing financial stability, enabling healthy financial sector evolution and ensuring that financial sector contributes to the real economy.

14. Consequently, the Bank is intensifying efforts towards strengthening regulatory and supervisory framework and enhancing monitoring of the operations of the Deposit Money Banks (DMBs) to ensure that they remain safe, sound and healthy and contribute to the growth and development of the economy. In addition, the recent Cash-less Policy of the Bank is aimed at addressing the currency management challenges in Nigeria, as well as enhancing the payments system. The Nigerian economy is heavily cash-oriented in the transaction of goods and services. The huge cash transaction increases the

operational costs of the banking sector, which is passed down to the customers in the form of high service charges and high lending rates. As Executives of the Bank, we are expected to explain to the public the rationale behind most of its policy stance so as to reduce rumours and speculations.

15. The number of bank branches had increased from 3,247 in 2003 to over 5,837 in 2010, while employment in the sector rose from 50,586 in 2005 to 71,876 in 2010. Overall, the financial development efforts have engendered stable macroeconomic environment evidenced by the relatively high GDP growth rate, low inflation, relatively stable interest and exchange rates and enhanced capacity to further support growth in the economy.

16. Distinguished ladies and gentlemen, there is no doubt that these reforms and initiatives have taken financial development in Nigeria to a new height. The types of institutions offering financial services, aside from the conventional banks, now include other financial institutions such as the discount houses, primary mortgage institutions, microfinance banks, finance houses, non-interest banks and development finance institutions, etc. The number of financial products has also increased and includes the use of e-money products such as web payment (internet), point-of-sale, mobile payments, among others. The depth of the financial sector, as measured by the ratio of broad money supply (M_2) to GDP increased to 42.7 and 38.9 per cent at end-December 2009 and 2010, respectively, compared with 23.4 and 19.8 per cent at end-December 2003 and 2004. The intermediation efficiency of the banks, as measured by the ratio of currency outside banks to broad money supply, improved, as it fell to 9.7, 8.6 and 9.4 per cent at end-December-2008, 2009 and 2010, respectively, from 20.8, 20.3 and 20.0 per cent, at end-December 2003, 2004 and 2005.

17. Although the Nigerian financial services environment has improved significantly following the reform efforts of the CBN, critical questions regarding their further development for increased economic growth and development remain. These include the need for: intensive efforts at deepening the reforms in the financial sector, facilitating rural financial reforms in order to achieve financial inclusion in the economy, developing the capital and insurance markets, legal reforms, issues of frequent distress in the system, huddles in liquidation process and payment of private depositors, insecurity of life and property, and strengthening supervision of financial institutions to avert systemic distress in the country.

18. In the light of the foregoing, I once again, urge you participants in this very important Seminar, to critically examine the issues and come up with appropriate recommendations that will assist the Bank, as both a regulatory/supervisory authority and monetary policy maker, in overcoming the challenges posed by the deregulation/liberalisation of the financial environment in particular, and advances in IT and globalisation, in general.

19. We have carefully selected experts and seasoned professionals and academicians in the relevant fields as facilitators for this Seminar. I have no doubt in my mind that they will do justice to the issues involved and by the end of their presentations, you will be better informed. Once again, I urge you to make use of this opportunity by devoting maximum time and attention to all the deliveries and actively participate in all discussions.

20. Before concluding these remarks, I wish to thank the Governors for honouring our invitation to grace this occasion and the tremendous support he has given the Department, in particular. I wish you all a rewarding Seminar and fruitful deliberations.

Thank you for your attention.