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The Evolution of the Nigerian Financial System: Problems, Challenges and Prospects

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THE EVOLUTION OF THE NIGERIAN FINANCIAL SYSTEM: PROBLEMS, CHALLENGES AND PROSPECTS*

BY

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Abstract

The paper reviews the evolution of the Nigerian financial system and articulates some of its current problems and challenges for the future, especially in the light of the liberalised trade and exchange regime initiated under the Structural Adjustment Programme (SAP). The paper examines the evolution of the major institutions in the financial system in the context of the changing pattern of economic and regulatory environment in which they operate. It observes that the financial system has undergone substantial changes since 1960 in terms of number and variety of financial intermediaries, the depth and breadth of instruments, as well as the structure of capital and ownership. It identifies the major factors which have influenced the development of the financial system to include the attainment of political independence, the establishment of the Central Bank of Nigeria (CBN), the Nigerian Civil War, the oil boom and its eventual collapse, variations in government financial requirements and the changing views of the monetary authorities about the proper role of the banking system in the national economy.

These changing views of the authorities are reflected in, among other things, changes in the stance of monetary policy and banking regulations; enquiries into the functioning of the economic system, as exemplified by the White Paper on the Report of the Financial Review Committee (1976), the Nigerian Enterprises Promotion Decree (1972) and the Structural Adjustment Programme. Some concrete effects of the above include the creation of local money and capital market instruments, the emergence and physical expansion of financial institutions, the stipulation of radical changes in the capital and ownership structure of banks and substantial decontrol of the financial system.

The paper identifies some of the problems of the financial system as inadequate capital base, imprudent lending practices leading to large and increasing bad and doubtful debts, concentration of credit on the short end of the lending spectrum and substantial depreciation of the Naira exchange rate. Other problems include high-rising inflation rate that has made physical assets more attractive as investment outlets than portfolio assets. SAP-induced challenges and opportunities include the deregulation of interest rates, liberalisation of trade and exchange regimes, the debt conversion programme, privatisation and commercialisation of public enterprises, increased responsibility of the banks in the management of the nation's foreign exchange resources and the determination of the exchange rate and the interest rate structure. The temptation to exploit customers on foreign exchange transactions poses a serious challenge in a situation of acute shortage. It is equally noted that the existing relatively high lending rates discourage investment while the relatively low deposit rates depress savings and mobilisation of resources. This action negates the growth objectives not only of the financial system but also of the economy as a whole. However, the prospects of the industry are very bright. The financial system, the paper concludes, should endeavour to stabilise exchange rates and manage foreign exchange prudently both for its own survival and the achievement of the national objective of economic growth and development.

Introduction

It is now generally recognised that the financial system plays a catalytic role in the process of economic growth and development[1]. As the economy grows, the financial system becomes increasingly deep and broad and its structure also becomes increasingly sophisticated. In the process the system offers a wider range of portfolio options for savers and issuable instruments for investors – a function often referred to as financial intermediation.

In the intermediation process, financial intermediaries engage principally in matching lenders and borrowers. They bring savers and borrowers together by 'selling' debt instruments or securities and deposits to savers for money and lending that money to borrowers. As a result, the lender or investor receives claims on the investment which generally have stable market value and high liquidity. However, financial intermediation does not ensue from the direct lending and borrowing process but arises from the lending-borrowing process which involves the generation and exchange of debt instruments or securities. The securities are then held by the intermediaries in exchange for their lending or parting with liquidity. The point of emphasis, therefore, is that financial intermediaries use their own liabilities to create additional assets; help mobilize funds, garner small sums together to reap economies of scale, and minimise the risk of investor[2].

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1 See Gurley, J.G. and Shaw, S.E. "Financial Aspects of Economic Development", *American Economic Review*, Vol. LCV No. 4, September 1983.

----"Financial Intermediaries and the Saving-Investment Process", *Journal of Finance*, May 1956.

Falegan, S.B. *Redesigning Nigeria's Financial System*, University Press Limited, Ibadan, 1987.

2 Falegan, S.B. Ibid pp. 36–37.

The financial system features a wide array of banking and non-bank financial intermediaries. The banking sub-sector of the system comprises commercial and merchant banks, development banks and the Central Bank as the apex institutions. The non-bank financial institutions sub-sector includes a wide range or organisations operating as 'regulators, facilitators and investors'[3]. The list includes the Securities and Exchange Commission (SEC), the Stock Exchange, Stockbrokers, registrars, insurance companies, pension and provident funds, and investment companies. To this list could be added Finance companies, engaged in fund management, investment counselling, and equipment leasing. However, detailed treatment of these institutions is limited to insurance companies and the National Provident Fund because of time constraint and the dearth of reliable information on many of the non-bank financial intermediaries.

With this background, the paper attempts to review in broad outline, the evolution of the financial system with emphasis on the period since 1960 and articulate some of its major problems and challenges for the future especially in the light of the liberalised trade and exchange regimes adopted under the Structural Adjustment Programme (SAP). The rest of the presentation is in three parts. Part I is an overview of the financial system. Part II outlines the evolution of the financial system while Part III focuses on the problems and challenges of the system. Part IV summarizes and concludes the paper.

PART I

OVERVIEW OF THE FINANCIAL SYSTEM

The Nigerian financial system has undergone substantial changes over the last three decades in terms of the number and variety of financial intermediaries, the depth and breadth of instruments as well as the structure of its capital and ownership. The same observation holds good for the economic environment and the regulatory framework within which the system operates. Nevertheless, the financial system remains relatively under-developed as it is yet to acquire that degree of financial intermediation which the economy requires for rapid development.

By 1960, the 12 commercial banks operating in the country had a total asset of ₦235.8 million and about 190 branches throughout the country. The only merchant bank Phillip Hill (Nigeria) Limited (which later merged with the Nigerian Acceptances Limited (NAL) did very little business. There were no specialised development banks but there were a few non-bank financial intermediaries operating on a very modest scale. They included a few insurance companies, regional government owned finance corporations and loan boards, Co-operative Societies and thrift institutions, the Lagos Building Society (later reconstituted into the Federal Mortgage Bank) and the Post Office Savings Bank. The Post Office savings bank was the single largest non-bank financial intermediary at that time, with over 160 branches spread all over the country. However, it made limited impact on the economy because its funds were invested largely in London, a practice which negated one of the most important aims of setting up savings institutions in less developed countries, namely, the mobilisation of capital for domestic investment[4].

At the end of 1988, there were 41 commercial banks with total assets of ₦59.2 billion and a network of 1,665 branches. Merchant banks at the end of 1988 numbered 24, with a total of 46 branches and total assets of ₦17.2 billion. The four development banks, viz, Nigerian Industrial Development Bank (NIDB), Nigerian Bank for Commerce and Industry (NBCI), Federal Mortgage Bank (FMB), and Nigerian Agricultural and Co-operative Bank between them had assets amounting to ₦2.8 billion at the end of 1988.

In the insurance sector, there are currently a total of ninety-nine companies engaged in life and non-life businesses. Thirty-five of these companies were in life as well as non-life insurance business while 64 were solely non-life insurance companies. The total assets of all insurance companies at the end of 1986 stood at ₦2.5 billion, while the National Provident Fund had a total investment of ₦976.1 million at the end of 1988.

Ownership and Capital Structure

In this section, the review of the ownership structure is limited to the banking system and the insurance companies due to data constraint. For the same reason, the analysis of capital structure is confined to the commercial and merchant banks.

Ownership Structure

Five of the 12 banks operating in Nigeria in 1960 were indigenously owned, but their share of financial intermediation was insignificant. Of the 48 commercial banks at the end of May 1989, 18 were under foreign-Nigerian joint ownership. Seven of the latter number are owned jointly by the Federal Government and foreign interests, 3 were joint foreign and State Government enterprises, while 8 were joint ventures between private Nigerian and foreign interests. Of the remaining 30 commercial banks, 21 were wholly state government enterprises, 1 was a joint venture between a state government and the Nigerian private sector, while 8 were wholly under Nigerian private sector ownership. Ten of the 31 merchant banks had foreign participation. Four of the former were jointly owned with the Federal Government, 5 were joint ventures between private Nigerian and foreign interests and 1 was a 3-way split between the foreign interests, the Federal Government and private Nigerian interests. All but 2 of the remaining 21 merchant banks were wholly Nigerian private sector enterprises.

The commercial and merchant banking sub-sector therefore features a mix of government, private Nigerian as well

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3 Akamiokhor, G.G. "The relationship between non-bank financial institutions and the Exchange commission and the Nigerian Stock Exhange": paper presented at a seminar on non-bank financial institutions, August 13, 1987.

as private foreign participation. Foreign participation remains significant but no longer dominant. There is substantial government presence in commercial banking while private Nigerian interests dominate merchant banking in terms of the number of institutions. The four development banks, Nigerian Industrial Development Bank (NIDB), Nigerian Bank for Commerce and Industry (NBCI), Nigerian Agricultural and Co-operative Bank (NACB), and Federal Mortgage Bank (FMB), continue to be public enterprises owned jointly by the Federal Government and the Central Bank of Nigeria (CBN). A minor part of the NIDB, however belongs to private Nigerian interests. Of the 99 insurance companies, 20 are joint foreign-Nigerian owned while 79 are wholly Nigerian enterprises.

Capital Structure

The total paid-up capital of commercial banks grew rapidly from ₦29.0 million in 1965 to ₦87.9 million in 1975, ₦565.4 million in 1985 and to ₦861.4 million at the end of 1988. The banks' reserve funds grew even more rapidly as a result of high profitability and regulatory requirements on statutory reserves. They have risen from ₦0.6 million in 1965 to ₦33.7 million in 1975, ₦140.8 million in 1980 and ₦983.9 million at the end of 1988.

For the same reasons as for commercial banks, the capital fund of merchant banks rose rapidly and exhibited similar features. Merchant banks' paid-up capital which stood at ₦68.5 million in 1984 increased by 86.9 per cent to ₦128.0 million at the end of 1987. It increased by a further 73.8 per cent to ₦222.5 million at the end of 1988. The banks' reserve funds expanded even faster and by 1988 was almost level with the total paid-up capital.

PART II

EVOLUTION OF THE FINANCIAL SYSTEM

In this section we shall consider the evolution of the major institutions in the financial system including an analysis of the changing pattern of the economic and regulatory environment under which they operated.

Prior to the establishment of the CBN in 1959 the main banks in Nigeria were local branches of banks of the metropolitan countries whose lending and related activities were largely confined to the financing of expatriate businesses which consisted largely of the export of primary commodities and import of manufactures. The banks as such, were mere enclave institutions that had little to do with economic developments' efforts of the country. Indeed their activities in Nigeria were based on decisions made at head offices in the home country. Indigenous merchants deprived of credit from these enclave financial institutions established a total of 25 wholly indigenous banks between 1925 and 1952. These early attempts, however, failed due to inadequate capital base and imprudent banking practices.

The asset/liability structure of the banks was characterised by self-liquidating commercial credit, the virtual absence of term loans and a sizeable portfolio of overseas investments. Indeed the banks were a medium for the export of capital from Nigeria because of the lack of local avenues for short-term investments.

Soon after the establishment of the Central Bank, it assumed responsibility for the Nigerianisation of the credit base through the creation of local money and capital market instruments in which financial institutions could invest their surplus funds instead of in the money and capital markets abroad. However, the banks were not fully persuaded to invest in these instruments until administrative, legislative and regulatory instruments were put in place in line with developments in the economy to make it attractive or mandatory for them to hold the instruments.

Developments in the economy and the changing views of the monetary authorities on the percieved roles of the financial system continued to influence the evolution of the financial system. Developments of note which have influenced the evolution of the Nigerian financial system include the attainment of political independence; the establishment of the CBN; the Nigerian Civil War; the oil boom and the associated economic prosperity; the collapse of the oil boom and the concomitant economic depression; variations in government financial requirements; and the changing views of government on the proper role of the financial system in the economy. The changing views of the monetary authorities are reflected in, among other things, changes in the stance of monetary policy; various banking regulations; enquiries into functioning of the economic system, as exemplified by the white paper on the Report of the Financial Review Committee (1976); the Nigerian Enterprises Promotion Decree (1972) and the Structural Adjustment Programme.

Some of the changes in the role of the financial system brought about by the changing views of the monetary authorities include the creation of local money and capital market instruments, the introduction of the Rural Banking Expansion Programme; the requirement that banks should allocate specific proportions of loans to designated sectors and sub-sectors of the economy; and changes in the ownership structure of banks. The Structural Adjustment Programme (SAP) among other things saw Nigeria change from a rigorously controlled economy involving large government intervention to a virtually decontrolled economy and floating exchange rate. Of particular interest in the post-SAP era is the enormously increased emphasis and responsibility that has devolved on the banks in the area of interest rate and exchange rate determination as well as foreign exchange and external debt management. With this background we shall touch briefly on some of the individual institutions within the financial system.

The Central Bank of Nigeria

It was indicated earlier that the Central Bank at its inception in 1959 inherited a rudimentary financial system in

[4] Central Bank of Nigeria. *Twenty Years of Central Banking in Nigeria*, 1979, p. 31.

which there were a few commercial banks, and non-bank financial intermediaries, but with no organised money and capital markets. During the first decade of its existence, therefore, the CBN concentrated on the important task of promoting the transformation of the rudimentary financial structure of the economy. In fostering the development of the money market the CBN introduced treasury bills (1960), produce bills (1962), treasury certificates (1968), all of which it stood ready to rediscount. It also introduced a Call Money Scheme (1962).

The surfeit of liquidity in the economy in the mid-1970s, associated with the relatively large government revenue from petroleum exports and the dearth of money market assets in relation to the excess funds available to the financial system dictated the need for additional instruments. Consequently, Certificates of Deposit and Bankers' Unit Fund were introduced in 1975 and Stabilisation Securities were introduced in 1976.

The CBN actively promoted the growth of the capital market, starting with that of the Lagos Stock Exchange and the Capital Issues Committee which later evolved into the Nigerian Securities and Exchange Commission (NSEC) in 1978. The CBN also influenced the course and pace of development of the Nigerian financial system via the promotion of the establishment of and continued assistance to development banks. As noted earlier, these institutions which operate largely in the market for medium and long-term capital include the NIDB (1964), NBCI (1973), NACB (1973) and the FMB (1977).

Commercial Banking System

In Part I of this paper, the physical growth of the commercial banking system was highlighted. In this section, attention is focused largely on the trends in the system's assets and liabilities. Commercial bank assets/liabilities increased from ₦235.8 million in 1960 to ₦59.2 billion in 1988 reflecting a compound growth rate of 22.7 per cent (see Table 1). Deposit liabilities grew from ₦137.0 million in 1960 to ₦29.1 billion in 1988 representing a growth rate of 21.9 per cent. In the same period, loans and advances rose at a compound rate of 21.1 per cent from ₦114.0 million to ₦20.1 billion. Investments rose from ₦5.7 million to ₦8.8 billion – a growth rate of 31.2 per cent.

Merchant Banking

The influx of merchant banks in the 1970s was based on expectations that merchant banks would fill the credit gaps which commercial banks either could not or would not satisfy and which were beyond the resources available to development banks. In particular, they were expected to provide the term lending and corporate finance that the economy needed badly for its rapid transformation. Merchant banks were also expected to be active in loan syndication locally as well as internationally. The number of merchant banks rose from one in 1960 through 2 in 1975, to 12 in 1987. The number, however, doubled to 24 in 1988, reflecting the positive influence of the SAP.

The Federal Government's partial take-over of majority interest in some commercial banks in 1976 also applied to the foreign-controlled merchant banks then in operation. However, as indicated earlier, private Nigerian enterprises either alone or in partnership with foreign interests dominate the merchant bank business. The banks were brought within Central Bank credit guidelines of the Central Bank in 1976.

The growth rates of merchant banks' operations were much higher than those of commercial banks, reflecting the remarkable expansion in merchant banking activities. Between 1965 and 1988, total assets/liabilities, deposit liabilities and loans and advances rose by compound growth rates of 42.0, 44.3 and 45.2 per cent, respectively. (see Table 2). Between 1965 and 1988, merchant banks' investments grew by a rate of 40.3 per cent.

The Nigerian Industrial Development Bank (NIDB)

The NIDB, the first of the Development banks was established in 1964 as a private concern, with a paid-up capital of ₦4.5 million held by both domestic and foreign private investors. This ownership structure remained until 1978 when the Federal Government and the CBN acquired 79.3 and 20.2 per cent of the equity capital, respectively. Private Nigerians held the balance of 0.5 per cent. In that year, the capital was raised to ₦200 million and to ₦400 million in 1988, held in the ratio of 59.0, 40.0 and 1.0 per cent by the Federal Government, the CBN and the private sector, respectively. This ownership structure is to change under the on-going privatisation programme, to reduce public sector holding to 70 per cent. The bank had total assets of ₦693.7 million at the end of June, 1988. Its loans and advances stood at ₦391.4 million while investments, all in equity, amounted to ₦34.2 million. (see Table 3).

Nigerian Bank for Commerce and Industry (NBCI)

The NBCI was set up as a wholly owned public sector enterprise to undertake development and merchant banking as well as some commercial banking functions. The initial impetus for its establishment came from the perceived need for funds to finance the transfer of shares under the indigenisation decree of 1974. It took off with an initial capital of ₦50 million held 60 and 40 per cent by the Federal Government and Central Bank, respectively. In 1984, this was raised to ₦200 million and there are moves to increase it further to overcome the erosion in the bank's capital base arising from the sharp depreciation of the Naira. The bank is also to be partially privatised to reduce public sector holding of its equity from 100 to 70 per cent. The Bank's total assets/liabilities amounted to ₦572.5 million at the end of 1988, while total loans and advances and investments amounted to ₦203.0 and ₦20.1 million respectively. (see Table 3).

Nigerian Agricultural and Co-operative Bank (NACB)

The Nigerian Agricultural and Co-operative Bank, (previously known as the Nigerian Agricultural Bank) was set up by decree in November 1972 to channel credit to agricultural production. The bank commenced effective operation in April 1973 with an initial capital of ₦12 million from the Federal Government, of which ₦1 million was equity and ₦11 million was loan capital. In 1978, the share capital of the bank was raised to ₦150 million, subscribed in the ratio of 60 and 40 per cent by the Federal Government and the Central Bank, respectively. At the end of 1988, the bank's total asset stood at ₦736.6 million. Loans and advances amounted to ₦557.5 million while investments stood at ₦2.5 million (see Table 3).

Federal Mortgage Bank (FMB)

The Federal Mortgage Bank emerged from a reconstitution of the Nigerian Building Society which had been established in 1957 as a joint venture by the Federal Government, the Former Eastern Regional Government and the Commonwealth Development Corporation (CDC). The Bank was created by decree in 1977 to provide mortgage credit and co-ordinate mortgage lending on a nation-wide basis. It had an initial capital of ₦20 million of which ₦12.5 million was paid up. In 1978, the equity capital of the company was expanded to ₦150 million held in the ratio of 60 and 40 per cent by the Federal Government and the Central Bank, respectively. The bank's total assets at the end of September 1988 stood at ₦753.9 million while loans and advances amounted to ₦572.2 million (see Table 3).

Insurance Companies

The insurance industry had, especially since the late seventies, become a very important source of credit to the economy. The industry has also become a major investor in Government securities, private sector equity and bonds as well as housing mortgage. Their investment in government securities more than doubled from ₦212.2 million in 1984 to ₦460.6 million in 1985 and ₦822.6 million in 1986. The investment in equity and bonds and mortgages stood at ₦290.6 million and ₦279.6 million respectively. (see Table 4).

National Provident Fund

The National Provident Fund has continued over the years to be a major source of savings and an important investor in government securities. The Fund's total investments which stood at ₦3.5 million in 1963 had risen sharply to ₦20.6 million in 1965 and ₦72.0 million in 1970. It grew steadily all through the 1970s and 1980s and stood at ₦976.1 million at the end of 1988. (see Table 5).

The Stock Exchange

The Lagos Stock Exchange was incorporated in 1960 under the Companies Ordinance as an association limited by guarantee. Between 1961 and 1971 activities at the stock exchange was relatively sluggish as only 14 companies were listed as at the end of 1971. The period between 1972 and 1974, however, witnessed a marked increase in the volume of business as a result of the implementation of the Nigerian Enterprises Promotion Decree (1972) and its subsequent amendments. Consequently, during the period the number of listed securities rose to 34. Today the Exchange has more than come age, with eleven dealing members and 168 securities on the list, made up of 58 Government Stocks, 17 Industrial Loans and Preference Stocks and 93 Equities. There are now three semi-autonomous exchanges in Lagos, Port-Harcourt and Kano.

The Nigerian Securities and Exchange Commission (NSEC)

A Capital Issues Committee was set up in July 1962 to regulate public issues of securities and ensure orderly development of the Capital Market in Nigeria. It was reconstituted into the Capital Issues Commission (CIC) in May 1973 and evolved into the Nigerian Securities and Exchange Commission (NSEC) in April 1978. The main functions of NSEC which has assisted the orderly growth of the capital market include the valuation of shares and debentures determination of the timing and amount of issues of securities.

PART III
PROBLEMS, CHALLENGES AND PROSPECTS

Some of the long-standing problems of the financial system, which are still poignant today have been compounded by recent developments arising from the operation of SAP. Some of the long-standing problems include inadequate capital base, imprudent lending practices leading to large and increasing bad and doubtful debt. Other such problem include the concentration of credit on the short end of the lending spectrum. It should be emphasised that these problems are not common to all financial institutions nor do they apply with equal force to those afflicted.

The major problems of Nigeria's development banks over the years has been the lack of funds. The banks have continued to rely heavily on capital and loan funds from government and on government-guaranteed loans from abroad. Under the Structural Adjustment Programme, their problems worsened as a result of the steep depreciation of the Naira exchange rate following the adoption of the structural adjustment programme. The sharp Naira depreciation brought with it substantial capital loss in respect of investment and credit operations financed with foreign loans. Indeed the consequent erosion of theit base may aggravate the difficulties of raising needed fund both at home and abroad. The proposed privatisation of the development banks would surely provide some relief, more importantly, the positive response of the NIDB and the NBCI in their efforts to substantially raise their share capital poses a challenge to the other development banks to take similar initiative.

Of importance to the financial system is the problem of inflation. With rapid inflation physical assets become more attractive as investment outlets than portfolio assets. This leads to financial disintermediation, thereby frustrating the overall objective of the financial system. Rapid and persistent inflation has serious implications for persistent exchange rate depreciation and expectations of further depreciation. These create speculative demand for foreign exchange and widen the gap between supply and demand, thereby exerting further pressure on the exchange rate. Exchange rate instability erodes confidence in the economy, encourage capital flight and represses financial intermediation.

Many of the SAP-induced changes in the management of the Nigerian economy has created a number of opportunities as well as challenges to the financial system. These changes include the deregulation of the interest rate structure, the liberalisation of trade and exchange regimes, the debt conversion programme and the privatisation and commercialisation of public enterprises. For example, under the new dispensation, the commercial, merchant and development banks now exercise considerable authority in the purchase as well as discretion in the allocation of the bulk of the nation's foreign exhange resources under conditions in which demand far exceeds supply. Trade liberalisation and the domicilliary account arrangement also ensure that private sector foreign exchange earnings flow through the banking system or are kept by them. Consequently a large and increasing proportion of the country's foreign exchange resources is held especially by commercial and merchant banks largely in foreign balances with correspondent banks abroad. Also, under the present dispensation, the banking system is the major facilitator of debt conversion and privatisation/commercialisation programme of government.

There is no gainsaying therefore that as the major operators in the foreign exchange market, great responsibility devolves on the banks for exchange rate stability and the orderly management of the country's external assets. Unless the responsibility for the disbursement and mobilisation of foreign exchange are exercised with high integrity, it could become disruptive not only to the foreign exchange market, but also to the banking system and the whole national economy. Similarly, apart from the great responsibilities which devolve on the banks for the prudent management of the external balances the creditable discharge of their responsibilities under the other programmes demand very sound knowledge of the foreign exchange markets and the ingenuity of the system at attracting foreign private investment to the priority sectors of the economy.

In the same vein, the SAP-induced interest rate liberalisation has a lot to commend it for a more efficient resource allocation, it has been observed that banks now lend at relatively high rates while paying relatively low rates on deposits. Consequently, the spread between deposit and lending rates has been considerably widened. To the extent that the relatively high lending rates discourage investment, and relatively low rates do not adequately stimulate increases in savings, they negate the growth objectives not only of the financial system but also of the economy as a whole.

PART IV
SUMMARY AND CONCLUSION

The paper has reviewed in broad outline, the evolution of the Nigerian financial system over the last three decades. It has also articulated the problems of the system and the challenges posed to it in the light of the liberalised trade and exchange regimes in particular as the country looks ahead to the next 15 to 20 years. It was noted that the financial system has undergone substantial changes since 1960 in terms of the number and variety of financial intermediaries, the depth and breadth of instruments as well as the structure of its capital and ownership.

This was exemplified by the fact that the financial system was only at a redimentary stage in 1960 with only 12 commercial banks with total assets of only ₦235.8 million and about 190 branches and offices throughout the country. There was only one newly established merchant bank and a few non-bank financial intermediaries operating on a very modest scale.

Even more significantly, the financial system at that time made only little impact on the economy because the limited funds mobilised were invested largely in London as there were no appreciable avenues for the investment of such funds. Such a practice it was noted, negated the developmental objectives of the country.

At the end of 1988, after nearly three decades, the Nigerian financial system has evolved into a system that featured a wide array of banking institutions and non-bank financial intermediaries. At that time, there were 41 commercial banks with total assets of ₦59.2 billion and a network of 1,665 branches. Merchant banks number 24, with total assets of ₦17.2 billion with a total of 46 branches. The four development banks – the NIDB, NBCI, FMB and the NACB, between them had assets amounting to ₦2.8 billion. The list of non-bank financial intermediaries that had evolved include the Securities and Exchange Commission (SEC), the Stock Exchange with three semi-autonomous units, Stockbrokers, Registrars, an array of finance and investment companies, pension funds and insurance companies. Insurance companies alone number up to 99 with total assets standing at ₦2.5 billion.

The ownership and capital structure were equally radically different from the situation in 1960 when the 7 largest of the then existing commercial banks were foreign owned and controlled. Of the 48 and 31 merchant and commercial banks only 18 and 10 have minority foreign participation, respectively. The remainder is owned by Nigerian governments and indigenes.

The analysis of the trends in financial system's assets and liabilities showed that their growth were as impressive as the physical growth of the system. Total assets/liabilities, total deposit liabilities, loans and advances and investments of commercial banks between 1960 and 1988 rose at compound rates of between 21 and 31 per cent. The comparative growth rates for merchant banks between 1965 and 1988 were even higher, ranging between 40 and 45 per cent. The assets and liabilities of the other financial institutions showed impressive but lower growth rates.

In the analysis of the economic and regulatory environment under which they operated, the following factors were identified as among those that influenced the evolution of the financial system; the attainment of political independence; the development role played by the CBN; the civil war the oil boom and the associated prosperity; the eventual collapse of the oil boom and the ensuing economic depression; variations in government financial requirements and the changing views of the monetary authorities.

Some of the changes in the financial system brought about by the changing views of the monetary authorities on the perceived roles of the financial system were identified to include: the creation of local money and capital markets and market instruments, the introduction of the rural banking expansion programme; sectoral allocation of credit; changes in the ownership and capital structure of banks and the structural adjustment programme.

In the analysis of the problems, challenges and prospects of the financial system, some of the long-standing problems of the system which are still poignant today and some of which have been compounded by the operation of SAP were identified to include inadequate capital base; imprudent lending practices leading to large and increasing bad and doubtful debts; and the concentration of credit on the short end of the lending spectrum. The problem of capital erosion and its aggravation of the problem of capital inadequacy as a result of the substantial depreciation of the Naira exchange rate was illustrated. It was however emphasised that these problems are not common to all financial institutions, nor do they apply with equal force to those afflicted.

Inflation was identified as an important problem to the financial system as it made physical assets become more attractive as investment outlets than portfolio assets. This in turn leads to disintermediation, thereby frustrating the overall objective of the financial system. Rapid and persistent inflation was also shown to have serious implications for exchange rate instability, speculative demand for foreign exchange and the erosion of confidence in the economy.

Many of the SAP-induced changes in the management of the Nigerian economy which has created a number of opportunities as well as challenges to the financial system were identified to include the deregulation of the interest rate structure the liberalisation of trade and exchange regimes, the debt conversion programme as well as the privatisation and commercialisation of public enterprises. Under the new dispensation, the banks have new areas of profitable operations as well as greater responsibilities in the prudent management and disbursement of the nations foreign exchange resources in ensuring exchange rate stability and in acting as facilitators for these important government programmes.

The challenges posed to the financial system by the observation that banks tend to lend at relatively high rates while paying relatively low rates on deposits as a result of interest rate liberalisation was considered. It was noted that to the extent high lending rates discourage investment and low rates do not adequately stimulate increases in savings, they negate the objectives not only of the financial system but also of the economy as a whole.

It was noted in conclusion that the prospects of the financial system are very bright. It is currently one of the most profitable sectors of the economy that had maintained high profits even during the most depressed periods. The current rush for the establishment of new banks are indicative of the bright prospects of the financial sector. However for the realisation of the prospects, it was emphasised that great responsibility devolves on the financial system for exchange rate stability, prudent management of foreign exchange and the orderly functioning of the system. To do otherwise could be disruptive not only to the financial system but to the whole national economy.

Table 1

COMMERCIAL BANKS' ASSETS AND LIABILITIES (SELECTED YEARS) 1960 – 1988
(₦' Million)

	1960	1965	1970	1975	1980	1981	1982	1983	1984	1985	1986	1987	1988
ASSETS													
Cash and Cash Items	15.9	25.6	46.6	828.7	1,532.1	1,376.1	2,002.0	1,266.7	1,032.1	805.2	1,488.4	2,193.2	2,152.1
Balances with Other Banks	51.8	51.0	20.6	183.8	860.2	869.1	622.8	996.9	836.7	797.3	2,226.7	4,664.0	7,273.66
Loans and Advances	114.0	270.1	351.3	1,537.3	6,379.3	8,604.8	10,277.0	11,100.0	11,503.5	12,170.3	15,701.6	17,531.9	20,051.55
Investments	5.7	15.9	534.0	832.0	3,114.8	2,350.2	3,406.9	5,730.5	9,237.8	10,875.8	5,715.2	8,714.7	8,757.3
Other Assets	48.4	71.7	199.5	926.2	4,454.1	6,277.3	6,353.1	7,604.4	7,456.6	7,299.3	14,447.0	18,724.6	20,991.7
TOTAL	235.8	434.3	1,152.0	4,308.0	16,340.5	19,477.5	22,661.8	26,701.5	30,066.7	31,997.9	39,578.8	49,828.4	59,226.2
LIABILITIES													
Capital Funds	5.9	29.7	57.5	127.2	389.1	497.4	667.7	845.1	966.7	1,128.7	1,298.7	1,545.1	1,932.4
Balances For Other Banks	32.7	–	13.3	38.6	170.7	220.3	333.2	411.3	300.4	310.4	984.7	1,418.6	895.5
Demand Deposit	82.2	123.9	288.0	1,266.8	4,845.9	4,880.8	5,180.7	5,855.6	6,343.5	7,046.2	6,649.8	7,998.0	10,667.9
Time Deposit	17.9	60.7	207.0	1,051.1	3,573.7	3,816.3	4,517.0	5,203.6	6,030.0	6,851.0	7,212.6	9,882.0	7,122.6
Savings Deposit	36.9	80.3	129.7	521.3	1,589.5	1,979.2	2,321.2	2,897.3	3,361.3	3,699.9	4,270.1	5,206.7	11,274.5
Other Liabilities	60.2	9.7	456.5	1,303.0	5,771.6	8,083.0	9,642.0	11,488.6	13,064.8	12,961.7	19,162.9	23,778.0	27,333.3
TOTAL	235.8	434.3	1,152.0	4,308.0	16,340.5	19,477.5	22,661.8	26,701.5	30,066.7	31,997.9	39,578.8	49,828.4	59,226.2

Source: CBN, Annual Reports and Economic and Financial Review.

Table 2

MERCHANT BANKS' ASSETS AND LIABILITIES (SELECTED YEARS) 1965 – 1988
(₦' Million)

	1965	1970	1975	1980	1981	1982	1983	1984	1985	1986	1987	1988
ASSETS												
Cash and Cash Items	–	0.1	14.4	81.0	142.6	294.7	307.5	120.4	70.4	161.0	249.7	291.8
Balances with Other Banks	–	–	5.8	34.0	61.7	111.0	109.6	136.5	197.2	1,151.3	1,736.2	3,262.4
Loans and Advances	1.2	1.3	80.7	400.2	711.9	1,190.2	1,465.9	1,671.9	1,802.9	2,771.5	4,101.3	4,419.1
Investments	–	5.1	18.2	93.8	95.6	343.3	499.8	1,065.9	1,344.8	520.3	1,915.4	1,617.1
Other Assets	6.5	1.3	67.0	399.2	886.9	1,363.7	1,822.1	1,501.2	1,585.8	3,841.2	4,277.4	7,613.2
TOTAL	7.7	7.8	186.1	1,008.2	1,898.7	3,302.9	4,304.9	4,495.9	5,001.1	8,445.3	12,280.0	17,203.6
LIABILITIES												
Capital Funds	1.5	1.5	11.2	26.0	37.2	63.1	85.4	131.5	163.7	191.8	252.6	471.2
Balances for Other Banks	–	–	12.3	8.3	59.6	35.1	67.1	76.5	36.1	80.7	163.5	698.6
Demand Deposit	1.2	1.2	8.6	66.5	122.4	272.3	484.7	511.0	530.5	601.9	560.2	834.8
Time Deposit	–	–	54.8	219.6	328.0	691.3	793.7	970.6	1,318.2	1,739.7	2,822.8	3,982.7
Savings Deposit	0.3	3.2	–	–	–	–	–	–	–	–	–	–
Other Liabilities	4.7	1.9	99.2	687.8	1,351.5	2,240.4	2,874.0	2,806.3	2,952.6	5,831.2	8,480.9	11,216.3
TOTAL	7.7	7.8	186.1	1,008.2	1,898.7	3,302.2	4,304.9	4,495.9	5,001.1	8,445.3	12,280.0	17,203.6

DEVELOPMENT BANKS' ASSETS (1980–1988)
(₦' Million)

	1980	1981	1982	1983	1984	1985	1986	1987	1988
ASSETS/LIABILITIES	**710.7**	**1,270.3**	**1,189.2**	**1,642.4**	**1,155.7**	**1,763.5**	**2,167.8**	**2,284.5**	**2,756.7**
NBCI	134.8	210.6	n.a	283.8	284.3	321.9	374.5	406.8	572.5
NACB	241.2	304.3	345.9	401.5	488.4	499.3	497.7	711.7	*736.6[1]
FMB	334.7	426.0	465.0	541.5	n.a	531.2	638.9	476.6	*753.9[2]
NIDB	–	329.4	378.3	415.6	383.0	411.1	656.7	689.5	*693.7[1]
LOANS & ADVANCES	**399.8**	**769.5**	**778.2**	**1,038.3**	**678.4**	**1,184.2**	**1,329.4**	**938.9**	**1,724.1**
NBCI	64.4	84.7	–	163.9	156.7	158.7	139.3	190.2	203.0
NACB	127.8	192.8	214.1	216.6	326.9	374.9	306.4	318.0	557.5
FMB	207.6	281.0	327.0	400.1	–	447.9	476.5	133.8	572.2
NIDB	–	211.0	237.1	257.7	194.8	202.7	407.2	296.9	391.4
INVESTMENT	**104.9**	**159.4**	**147.0**	**155.8**	**63.7**	**91.0**	**104.6**	**55.1**	**56.8**
NBCI	**10.9**	**19.3**	–	**23.7**	**23.4**	**22.9**	**22.8**	**19.9**	**20.1**
Govt. Securities	–	6.3	–	6.0	6.0	6.0	6.0	6.0	6.0
Private Sec. Bons	–	–	–	2.2	–	–	–	–	–
Equities	10.9	13.3	–	15.5	17.4	16.9	16.7	13.9	14.1
NACB	–	–	–	–	–	–	–	–	–
Equities	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
FMB	93.0	102.6	96.7	79.9	–	36.4	39.4	–	–
NIDB	–	–	–	–	–	–	–	–	–
Equities	–	36.5	49.3	51.2	39.3	30.7	41.4	34.1	34.2
OTHER ASSETS	**36.0**	76.2	144.0	270.4	**162.6**	470.9	389.5	447.2	N.A
NBCI	17.5	30.8	N.A	62.5	–	79.9	122.0	139.9	237.0
NACB	6.5	6.5	60.1	87.1	87.2	266.2	119.2	153.6	N.A
FMB	12.0	15.1	27.0	31.1	N.A.	36.4	39.4	46.3	N.A
NIDB	N.A	23.8	56.9	89.7	75.4	88.4	108.9	107.4	N.A
CASH	132.0	121.2	111.3	82.8	130.5	78.8	64.7	515.8	–
NBCI	4.0	75.7	22.7	21.0	99.7	22.0	49.7	46.2	69.0
NACB	105.9	15.7	70.6	30.7	22.9	32.9	12.6	159.5	N.A
FMB	22.1	27.2	15.2	30.3	N.A.	17.0	N.A.	296.3	N.A.
NIDB	–	2.6	2.8	0.8	7.9	6.9	2.4	13.8	N.A
MONEY AT CALL	–	122.7	82.1	96.8	221.1	227.3	196.0	220.7	–
NBCI	–	–	50.0	12.7	30.0	38.0	40.7	10.5	43.4
NACB	–	88.6	–	66.0	125.5	76.9	58.5	79.4	N.A
FMB	–	–	–	–	N.A	30.0	N.A.	–	N.A
NIDB	–	34.1	32.1	16.1	65.6	82.4	96.8	130.8	N.A

Sources: CBN. Based on Returns from the institutions

[1] Position as at June

[2] Position as at September

Table 4

ASSETS OF INSURANCE COMPANIES (1970 – 1986) LIFE AND NON–LIFE
(₦' Million)

Year	Government Securities	Stocks Shares and Bonds	Mortgages and Loans	Cash and Bills Receivable	Miscellaneous	Total
1970	6.6	9.5	7.5	20.4	2.1	46.1
1975	29.0	20.6	23.8	64.8	48.7	186.9
1980	109.9	121.9	180.9	195.5	340.4	948.6
1981	133.8	145.4	147.3	159.3	428.3	1,014.1
1982	131.7	190.3	217.6	177.1	421.5	1,138.2
1983	204.7	169.4	204.6	145.5	381.7	1,105.9
1984	212.2	199.4	197.9	196.6	527.5	1,333.6
1985	460.6	277.6	297.2	236.1	662.8	1,934.3
1986	822.6	290.6	279.6	289.0	806.1	2,487.9

Source: CBN (derived from data compiled from companies' returns to the Federal Ministry of Finance).

Table 5

CUMULATIVE INVESTMENT OF THE NATIONAL PROVIDENT FUND IN SELECTED YEARS, 1963 – 1988
(₦' Million)

Year	Investment
1963	3.5
1965	20.6
1970	72.0
1975	168.3
1980	389.6
1981	448.3
1982	499.5
1983	562.3
1984	627.6
1985	709.1
1986	792.9
1987	889.7
1988	976.1

Source: National Provident Fund, Annual Report of Activities.

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