

NIGERIAN BANKING REFORM: RECENT ACTIONS AND FUTURE PROSPECTS

Duncan Alford*

INTRODUCTION

Since his appointment in the summer of 2009, the new Governor of the Central Bank of Nigeria, Lamido Sanusi,¹ has introduced a spate of reforms in response to the global financial crisis and the mismanagement of certain Nigerian banks. Major changes to the financial industry are under way in Nigeria, the most populous nation in sub-Saharan Africa, the eighth most populous nation in the world, and the seventh largest exporter of oil.² The CBN under Sanusi intends to raise the quality of bank supervision and bank operations to a world standard and has signaled its more interventionist role in the Nigerian economy.

This article briefly reviews the history of Nigerian banking, places this latest reform effort within the context of that history, analyzes this reform effort, and then suggests some implications of these reforms for Nigeria and for potential investors in Nigerian banks and the Nigerian economy generally.

BRIEF HISTORY OF NIGERIAN BANKING

A formal legal structure to banking in Nigeria is a relatively recent invention (See **Chart A** for a timeline of the history of banking in Nigeria). Prior to 1952 there was no legislation governing banking in Nigeria. In 1892, the British Bank of West Africa (“BBWA”)

Associate Professor of Law, University of South Carolina School of Law, Columbia, SC, USA. I would like to thank Rachel Atkinson for her able assistance in researching the Nigerian banking system.

¹ *Nigeria: New Central Bank Governor*, Africa Research Bulletin 18, 277 (May 16-June 15, 2009).

² *Nigeria: A BRIC in the Making*, Global Investor (Oct. 1, 2009).

began its operations in Nigeria.³ In 1917 Barclays Bank became the second expatriate bank to operate in Nigeria after BBWA.⁴ In 1933 the National Bank of Nigeria, the first indigenous bank, was founded and operated successfully.⁵ After World War II, British rule over Nigeria weakened with the passage of the 1946 Constitution that gave a majority of the seats in the National Assembly to native Nigerians.⁶ The Nigerian government began to regulate banking with passage of the Bank Ordinance of 1952.⁷ A motivation for passage of the 1952 Ordinance was the failure of 21 of 25 Nigerian banks in the period from 1947 to 1952.⁸ The creation of the Central Bank of Nigeria by the Central Bank Ordinance of 1958 further strengthened the bank regulatory structure of Nigeria. The Central Bank began full operations on July 1, 1959.

The 1960s and 1970s saw more financial institutions being created and a greater role of the Nigerian government in regulating and owning banks in Nigeria. The Indigenous Enterprises Promotion Decrees of 1972 and 1977 set a policy of government ownership of significant portions of the economy. As a result, the Nigerian government took ownership of 60% of the equity in expatriate banks operating in Nigeria, including First Bank, Union Bank, and United Bank of Africa.⁹

Until 1979, banks wholly owned by state governments or banks predominately owned by the federal government dominated the Nigerian banking industry.¹⁰ After 1979, privately held

³ Richard Fry, *Bankers in West Africa: The Story of the Bank of British West Africa Limited* 23 (1976). Emeka Offor, A Critical Evaluation of the Role of the Central Bank of Nigeria in Ensuring Corporate Governance in Nigerian Banking Post Consolidation vii, Aug. 31, 2008, at www.ssrn.com. BBWA is the predecessor to the current First Bank of Nigeria.

⁴ G.O. Nwankwo, *The Role of Banks in the Nigerian Economy* 30 in U. Joy Ogwu, R. Omotayo Olaniyan, eds., *Nigeria's International Economic Relations: Dimensions of Dependence and Change* (1989). Barclays is the predecessor to the current Union Bank of Nigeria.

⁵ Fry, *supra* note 3, at 216-17.

⁶ Fry, *supra* note 3, at 181.

⁷ *Reforms-Experts Task CBN on Trust and Confidence*, AllAfrica.com, March 15, 2010.

⁸ *Id.*

⁹ Abel Ezeoha, *Structural Effects of Banking Industry Consolidation in Nigeria: A Review*, 8 J. of Banking Reg. 174 (2007).

¹⁰ Nwankwo, *supra* note 4, at 32.

banks began to emerge again in Nigeria,¹¹ but the federal government dominated banking until the introduction of the Structural Adjustment Program in the mid-1980s.¹²

In 1986, the Nigerian government, as a condition of an agreement to borrow from the International Monetary Fund, introduced a Structural Adjustment Program that generally required economic liberalization and decreased government regulation and ownership in much of the economy.¹³ Bank licensing requirements were significantly eased resulting in a large increase in the number of banks operating in Nigeria. From 1985 to 1992, the number of banks increased from 40 to 120 banks, the highest number to that point in time.¹⁴ (See **Chart B** for details on the growth in the number of banks in Nigeria.) During this period in 1988, the Nigerian Deposit Insurance Corporation was created to offer deposit insurance to depositors in failed banks. Later in 1991, the Bank and Other Financial Institutions Decree was enacted and brought the supervision and regulation of all financial institutions, not just banks, under the Central Bank of Nigeria. Prior to this time, supervision of non-banks was shared between CBN and the Ministry of Finance.¹⁵

¹¹ *Id.*

¹² Ezeoha, *supra* note 9, at 174

¹³ *Id.*

¹⁴ *Id.* at 160

¹⁵ Central Bank of Nigeria, Bank Supervision Annual Report 44 (2008).

RECENT REFORMS

2004-2005 Consolidation

The current reform effort by Governor Sanusi follows a significant reform effort begun by his predecessor Charles Soludo in 2004 that resulted in the consolidation of the banking industry in Nigeria. Charles Soludo took office as Governor of the Central Bank of Nigeria in June 2004. The following month Soludo announced a new policy to increase the minimum paid in capital of banks to 25 billion naira (US\$ 173 million) from 2 billion naira (US\$ 14 million). Banks were required to obtain this capital by the end of December 2005, roughly 18 months from the policy announcement.¹⁶ The clear intent of the policy was to consolidate the existing banks into fewer, larger, and financially stronger banks. In 2004, the banking industry of Nigeria consisted of 89 banks. The industry was fragmented into relatively small, weakly capitalized banks with most banks having paid in capital of US \$10 million or less.¹⁷ The best capitalized bank had capital of US \$240 million as compared to Malaysia where the least capitalized bank had capital of US \$526 million at the time.¹⁸ Most of the smaller banks were family-owned and privately held.¹⁹ However, the industry was heavily concentrated, with the ten largest banks controlling 50% of the assets and deposits in the Nigerian banking system.²⁰

The result of this new, much larger capital requirement was the consolidation of banks into larger entities. During this 18 month period, there were a number of mergers and acquisitions among Nigerian banks in order to meet this new capital requirement.²¹ In the end,

¹⁶ Nicholas Norbrook, *Nigeria Banks: Consolidation to Follow the Crackdown*, Africa Report 89-90 (Oct.-Nov. 2009).

¹⁷ Ezeoha, *supra* note 9, at 161.

¹⁸ *Id.* at 162.

¹⁹ *Id.*

²⁰ *Id.* at 161.

²¹ Ezeoha, *supra* note 9, at 170-71 Table 6 in this article details the transactions and lists the surviving banks.

the 89 banks that existed in 2004 decreased to 25 larger, better capitalized banks.²² Thirteen banks did not meet the deadline for increasing their capital and their banking licenses were revoked.²³

Special Examination of Banks – August and October 2009

On June 4, 2009, Lamido Sanusi, former managing director of First Bank, took office as Governor of the Central Bank of Nigeria. Early in his term, he empanelled a special joint committee of the Central Bank of Nigeria and the Nigerian Deposit Insurance Corporation to conduct a special examination of all 24 universal banks in Nigeria.²⁴

On August 14, 2009, the CBN announced the results of the examination of 10 banks and determined that five banks were insolvent – Oceanic Bank, Union Bank, Afribank, Finbank, and Intercontinental Bank.²⁵ The aggregate percentage of non-performing loans of these five banks was 40.81%.²⁶ In addition, these banks were chronic borrowers at the Expanded Discount Window (“EDW”) of the CBN indicating that they had little cash on hand.²⁷ To improve the banks’ liquidity, CBN, as the lender of last resort, injected 420 billion naira (roughly US \$2.8 billion) into these banks in the form of a subordinated loan.²⁸ These banks in aggregate represented significant systemic risk as they held approximately 30% of the deposits in the Nigerian banking system.²⁹ In addition, the CBN referred the results of their examination to the Economic and Financial Crimes Commission for prosecution of criminal action. For instance,

²² *Id.* at 169

²³ *Id.*

²⁴ Osasu Obayiuwana, *Banking Sector in Turmoil...Again*, New African 48 (Oct. 2009).

²⁵ *If a Bank is Sick, the Signs Are Self-Evident*, Says Sanusi, This Day, Aug. 16, 2009. Union Bank, Intercontinental Bank and Oceanic Bank are systemically important banks.

²⁶ *Banking Post-Consolidation - Morning after the Shock*, This Day, Aug. 23, 2009.

²⁷ Lucky Fiapa, Sanusi *First Time Out*, Vanguard, Aug. 15, 2009.

²⁸ *Nigeria Sacks Heads of Five Banks*, BBC News, Aug. 18, 2009.

²⁹ *Invasive Surgery*, The Economist, Oct. 24, 2009.

Cecelia Ibru, Managing Director of Oceanic Bank, was accused of fraudulent activity, including allegedly employing staff for the bank through a recruitment firm she controlled and claiming rent for new branches opened by Oceanic.³⁰ Other senior executives of the insolvent banks have also been charged with crimes. In an unprecedented move, Sanusi published a list of the names of debtors of non-performing loans held by Nigerian banks.³¹

Subsequently, the CBN completed its special examination of the remaining 14 universal banks in Nigeria to determine their solvency. As a result of this audit, on October 3, 2009, the CBN dismissed the CEO's of three additional insolvent banks – Bank PHB, Spring Bank, and Equatorial Trust Bank – and injected an additional 200 billion naira into these banks.³² A fourth bank, Unity Bank, was determined to be insolvent but had sufficient liquidity to meet its current obligations. Similar to the banks receiving capital injections after the August 2009 audit, these three banks received funds through the Expanded Discount Window of the Central Bank of Nigeria in the following amounts: Bank PHB (64 billion naira), Spring (80 billion naira), and Equatorial Trust (56 billion naira of which 30 billion has been repaid). The CBN appointed new managing directors for each of these eight banks. Sanusi has stated clearly that these actions were not intended as a nationalization of these banks, rather they were intended to prevent a serious disruption of the banking system.³³ Thus far, eight banks have received 620 billion naira or approximately US\$ 4.1 billion from the CBN,³⁴ representing 2.5% of Nigeria's entire 2010 GDP of US \$ 167 billion.³⁵ Following the special examination and during the period from December 2008 to December 2009, Nigerian banks wrote off loans equivalent to 66% of their

³⁰ A. Abdulaziz, *How Ibru Looted Oceanic Bank*, AllAfrica.com, Jan. 25, 2010.

³¹ Nigeria's Central Bank Publishes List of Defaulters, Africa Today, Aug. 24, 2009. CBN Advertorial, Aug. 18, 2009, at http://www.cenbank.org/OUT/PUBLICATIONS/PRESSRELEASE/GOV/2009/ADVERTORIAL_18082009.PDF

³² Bank Crisis – CBN, *Aondoakka Dragged to Court*, This Day, Oct. 20, 2009.

³³ *CBN Will Not Keep Stakes in Troubled Banks* – Sanusi, The Daily Trust, Oct. 2, 2009.

³⁴ Biodun Omojola, *Then Came Another Three*, Africa Today 22 (Nov. 2009).

³⁵ The Economist Group, *The World in 2010* 111 (2010).

total capital; most of these write offs occurred in the eight banks receiving loans from the CBN.³⁶ After the completion of the audits, the CBN itself noted, “[W]e have come to the end of the *first phase* of the process of restoring financial sector stability .”³⁷

The special examination also revealed some banks operating in Nigeria were financially sound. In particular, Access Bank, Zenith Bank, GT Bank, and Firstbank were relatively well-capitalized.³⁸ In addition, the foreign-owned banks operating in Nigeria were similarly examined and found to be sound. These included Stanbic-IBTC, a subsidiary of South African-owned Standard Bank, Standard Chartered Nigeria, Citibank Nigeria, and Ecobank.

Realizing that its dramatic action after the first audit would shake foreign investor confidence in the Nigerian banking system, Governor Sanusi in August 2009 travelled to London to explain these actions to investors and correspondent banks of the affected Nigerian banks.³⁹ In addition, the CBN took the extraordinary action of guaranteeing all foreign credit lines and interbank placements and has extended the guarantee until Dec. 31, 2010.⁴⁰

Other Reforms Under Sanusi

The CBN under Sanusi’s leadership has also instituted significant changes in accounting practice for Nigerian banks. In June 2009, Sanusi issued a policy requiring Nigerian banks to adopt a common accounting year for 2009.⁴¹ By year end 2009 all banks must change their accounting years to the calendar year, and all subsidiaries of the parent bank must follow the same accounting year. Different reporting years for Nigerian banks made financial comparison

³⁶ J.P. Morgan, Nigerian Banks 13, March 15, 2010 (available on INVESTEXT).

³⁷ Central Bank of Nigeria, Press Statement on Outcome of Special Examination of 14 Banks, Oct. __, 2009 (emphasis added).

³⁸ J.P. Morgan, *supra* note 36.

³⁹ Central Bank of Nigeria, Public Statement, Aug. 18, 2009.

⁴⁰ J.P. Morgan, *supra* note 36, at 15.

⁴¹ Nigeria Finance: CBN Governor Pledges Financial Sector Reform, EIU Viewswire, July 21, 2009. Central Bank of Nigeria, Circular to All Banks and Discount Houses on Common Accounting Year End, June 18, 2009, 234-9-46236401, 234-9-46236418, BSD/DIR/GEN/CIR/VOL.2/004.

difficult among banks and limited transparency of bank financial results.⁴² The CBN's stated purpose for this policy change was "to further enhance the level playing field in the banking sector post-consolidation."⁴³ The CBN is also seeking banks to adopt International Financial Reporting Standards ("IFRS") by the end of 2012.⁴⁴ Currently, most banks follow Nigerian GAAP while some Nigerian banks with international operations have issued their 2009 financial statements using IFRS.⁴⁵ On January 18, 2010, CBN issued a circular detailing the type and format of financial information that must be disclosed by banks in their annual financial statements.⁴⁶ As illustrated by these actions, CBN is aggressively pursuing accounting reforms to improve disclosure to regulators, investors, and depositors regarding the financial health of Nigerian banks.

In January 2010, the CBN issued regulations limiting the terms of CEO's of banks to a maximum of ten years which will require some sitting CEO's to resign by July 31, 2010.⁴⁷ The intent of the regulation is to improve corporate governance of Nigerian banks by avoiding the "sit-tight syndrome" where bank executives manage the bank as a personal business as opposed to a publicly held corporation accountable to shareholders, depositors, and government regulators.⁴⁸ CEO's are limited to two renewable five year terms and are disqualified from serving as a director for three years after their second term as CEO expires. The rule applies retroactively. Three currently sitting CEO's – Tony Elumelu of United Bank of Africa, Jim Ovia of Zenith Bank, and Akinsola Akinfemiwa of Skye Bank – will be required to resign by July 31, 2010. Sanusi expects a similar rule to be imposed on bank auditors and non-executive directors

⁴² Nigerian Banking Sector: Slow Progress, IS Emerging Markets Monitor (Aug. 2009).

⁴³ CBN Circular, June 18, 2009.

⁴⁴ EIU Viewswire, *supra* note 41. IFRS - Nigeria's Convergence Report Out December, AllAfrica.com, Nov. 23, 2009.

⁴⁵ J.P. Morgan, *Nigerian Banks A Step in the Right Direction*, June 22, 2009 (available on INVESTEXT).

⁴⁶ Central Bank of Nigeria, Minimum Information to be Disclosed in Financial Statements for the Year Ended December 31, 2009, 09-462-6403, 09-462-36418, BSD/DIR/GEN/CIR/04/004.

⁴⁷ *Bank CEOs – Going, Going*, AllAfrica.com, Jan. 30, 2010.

⁴⁸ *Id.*

in the near future.⁴⁹ This new policy resulted from the special examination discussed earlier that revealed serious corporate governance deficiencies among the insolvent banks. While some commentators have commented that life directorship is not consistent with company law, others have criticized this policy arguing that its retroactive application is counter to Nigerian law, it usurps the rights of shareholders in electing management, and that there is no evidence linking the length of executive service to fraud committed by corporate executives.⁵⁰

Likewise, in March 2010, the Central Bank of Nigeria announced its plans to dismantle a central tenet of banking regulation in Nigeria – the exclusivity of universal banks as the vehicle for conducting banking in Nigeria. The CBN plans to categorize banks by function and allow a variety of banks to operate in Nigeria with varying levels of capital depending on the bank’s function as opposed to the single current minimum capital of 25 billion naira (approximately US \$173 million).⁵¹ The intent is to allow the creation of banks that would serve different market segments, such as small and medium-sized enterprises, and to phase out the “one size fits all” requirement by September 2011.⁵² Each type of bank would apply for a different license. This policy is a fundamental reversal of the consolidation policy of 2005 and is likely to encourage the development of an increased number of financial institutions in Nigeria.⁵³ Critics of the proposed policy argue that the CBN does not have sufficient regulatory staff, in either number or professional skill, to supervise various types of banks.⁵⁴ Similarly, the private sector may not

⁴⁹ Sanusi Lamido Sanusi, *The Nigerian Banking Industry: What Went Wrong and the Way Forward* 13, Speech at Bayero Univ., Feb. 26, 2010, at www.cenbank.org [hereinafter Sanusi Speech].

⁵⁰ *Bank CEOs – Going, Going*, AllAfrica.com, Jan. 30, 2010.

⁵¹ Emele Omu, *CBN to Categorize Banks*, AllAfrica.com, Jan. 12, 2010.

⁵² *Id.*

⁵³ *Id.*

⁵⁴ *Experts React to CBN’s New Policy for Banks*, Daily Trust, March 17, 2010.

have a sufficient number of trained bank professionals to staff these new types of financial institutions.⁵⁵

A key component of the second phase of banking reform in Nigeria is the removal of toxic assets or non-performing loans from the books of the banks receiving government support. To that end, the Ministry of Finance and the CBN have introduced a bill⁵⁶ in the National Assembly that will create an asset management company which will purchase toxic assets from the banks.⁵⁷ The legislation is currently under consideration by the Nigerian National Assembly. In early March 2010, the legislation received its second reading and will likely become law. While the bill only provides 10 billion naira as the corporation's initial capital,⁵⁸ the CBN expects that the asset management company (AMCON) will require capital of 700 billion naira⁵⁹ and that it will be operational by September 2010.⁶⁰ AMCON will focus its purchases of non-performing loans from the eight banks that have received government support. (See **Chart C** for a current listing of banks in Nigeria.) There are an estimated 1.06 trillion naira of non-performing loans in the Nigerian banking system.⁶¹ The concept behind the AMCON bill is a good bank – bad bank approach where AMCON will purchase the toxic assets from the banks and the banks after this purchase will have “clean” balance sheets. The bill grants broad powers to AMCON to purchase, maximize the value of, and eventually sell these non-performing loans.⁶² After these transfers, the banks will be relieved of funding pressures from these non-performing loans because investors and depositors will have more confidence in the bank and its

⁵⁵ *Id.*

⁵⁶ Asset Management Corporation Act of Nigeria 2009, H.B. 348, at <http://www.nassnig.org/legislation.php?page=8>

⁵⁷ CBN Press Release, March 5, 2010, at www.cenbank.org. The CBN first began discussions regarding the asset management company in November 2009.

⁵⁸ AMCON Act, §2.

⁵⁹ *Stakeholders Raise Objections, As Battle for Soul of AMC Rages*, AllAfrica.com, Jan. 12, 2010.

⁶⁰ J.P. Morgan, *supra* note 36, at 4.

⁶¹ *Stakeholders Raise Objections, As Battle for Soul of AMC Rages*, AllAfrica.com, Jan. 12, 2010.

⁶² AMCON Bill, §§ 29-51.

future stability.⁶³ Very important tasks will be to determine what entity will fund AMCON – the public or private sector – and what price will be paid for the toxic assets. The CBN states that AMCON’s purchase of non-performing loans will be “based on terms aimed at strengthening the balance sheets [of the banks] with a focus on asset quality, improving liquidity and capital adequacy as well as on reducing debt overhang relating to the stock market in order to stimulate activity in the capital market.”⁶⁴ Critics of the bill note that it focuses on banks only and does not deal with the distress in the capital markets, particularly securities firms that lent on margin with bank stock as collateral. AMCON will require personnel with specialized skills to deal with the non-performing loans and related collateral that it will purchase in the near future and such qualified personnel are in short supply in Nigeria.⁶⁵

CBN will also encourage the development of the financial infrastructure of Nigeria. In early January 2010, the first privately owned credit bureau was established in Nigeria – CRC Credit Bureau.⁶⁶ Previously, lenders had little information regarding the credit history of borrowers and principally relied on their own internal data. CRC Credit Bureau, owned by a partnership of 12 Nigerian banks,⁶⁷ the International Finance Corporation, Accenture, and Dun & Bradstreet, will collect credit information from lenders, utilities and other providers of credit in Nigeria.⁶⁸ The CBN endorsed the creation of the credit bureau and pledged its support in encouraging lenders to use the bureau’s services.⁶⁹ While the existence of a credit bureau will enhance the provision of credit in Nigeria, the credit bureau faces some significant challenges to

⁶³ J.P. Morgan, *supra* note 36.

⁶⁴ Central Bank of Nigeria Communiqué No. 66 of the Monetary Policy Committee, Nov. 3, 2009.

⁶⁵ *Stakeholders Raise Objections, As Battle for Soul of AMC Rages*, AllAfrica.com, Jan. 12, 2010. *AMC Will Enhance Credit Bureau Activities in the Country*, AllAfrica.com, Feb. 8, 2010.

⁶⁶ *How Credit Bureaus Will Revive Economy*, Daily Trust, Feb. 23, 2010.

⁶⁷ The twelve banks include Diamond Bank, Access Bank, Bank PHB, First Bank, First City Monument Bank, Guaranty Trust Bank, Intercontinental Bank, Oceanic Bank, Stanbic IBTC, Standard Chartered Bank, Union Bank and United Bank for Africa.

⁶⁸ Daily Trust, *supra* note 66.

⁶⁹ *CBN Endorses Banks’ Alliance on Credit Bureau*, Daily Champion, Jan. 18, 2010.

its operations: the lack of an acceptable unique identifier of individuals in Nigeria; the general lack of understanding of credit bureaus and their operations; the lack of reliable, accurate data collection systems; and weak consumer protection laws and rights generally.⁷⁰

In a statement early in his tenure as CBN governor, Sanusi stated that increased foreign ownership of Nigerian banks, while not preferable, would be possible.⁷¹ This statement is a significant change of policy that generally supported Nigerian control of its banking system, which originated with the indigenization policies from the early 1970s. Sanusi reiterated the possibility of foreign ownership of banks after the August 2009 bail out and the dismissal of the CEO's of five Nigerian banks.⁷² Sanusi predicted that by the end of the financial crisis, the number of Nigerian banks may be reduced from 24 to roughly 15 banks.⁷³ Whether the acquiror is a foreign bank or Nigerian bank, CBN policy will limit an individual bank's market share to 20% of banking assets in the country.⁷⁴ The CBN is interested in attracting investors to purchase the eight government-supported banks, but insists that the investors must be interested in investing in Nigeria for the long term, and they must "possess the expertise for risk management, corporate governance and overall management."⁷⁵

Once AMCON is established and funded, a further consolidation of the banking industry focusing on the eight government-supported banks is likely. The most likely acquirors are the better capitalized Nigerian banks such as Zenith Bank, United Bank of Africa, GT Bank, and First Bank or the foreign banks currently operating in Nigeria, Standard Chartered, Citi, and Stanbic-IBTC. The CBN has a slight preference for foreign banks with existing operations in

⁷⁰ Central Bank of Nigeria, Banking Supervision Annual Report 51 (2008).

⁷¹ *Nigeria Opens to Foreign Takeovers of Banks*, World News Connection, June 22, 2009.

⁷² *Nigeria: Bank Bail Out*, 46 Africa Research Bull. 18363 (Aug. 16 – Sept. 15, 2009); Kunle Aderinokun, *Sanusi-We Didn't Go to UK to Sell Five Banks*, This Day, Sept. 2, 2009.

⁷³ EIU Viewswire, *supra* note 41.

⁷⁴ *Financial Institutions to Own Only 20% or Less of Sector*, Africa Today, Oct. 26, 2009.

⁷⁵ *CBN to Implement Strict Regulation on Banks*, Vanguard, Jan. 13, 2010.

Nigeria to be the consolidators⁷⁶ because they can tap sophisticated management expertise and have already shown their commitment to invest in Nigeria. Several of the Nigerian banks have indicated their intention to raise additional capital funds. United Bank of Africa, First Bank, and GT Bank each has expressed their intention to issue bonds in the amounts of 500 billion naira, 500 billion naira, and 200 billion naira, respectively.⁷⁷ In fact, GT Bank successfully listed 13.5 billion naira (US\$ 90 million) of unsecured bonds in March 2010, the first such issuance by a Nigerian corporation since 2006.⁷⁸ A third group of potential acquirers includes South African banks not already operating in Nigeria, in particular First Rand Bank, Standard Bank, and Nedbank.⁷⁹

Based on statements by Sanusi and CBN officials, the eight government supported banks will not remain independent once AMCON has purchased their toxic assets. Foreign ownership of these banks will aid in raising capital from international markets and in transferring needed skills to Nigerian bank employees.⁸⁰ In the short term, foreign bank ownership will bridge the skills gap present in the Nigerian financial services industry.⁸¹

Governor Sanusi has also noted that the Central Bank of Nigeria itself is not without fault in the current financial crisis.⁸² Since consolidation in 2005, the CBN did not conduct a single routine examination of a Nigerian bank⁸³ -- an astonishing revelation. After the first two phases of bank reform are complete, Sanusi plans for the CBN to conduct an organizational review to determine how it can be restructured to improve bank supervision.⁸⁴

⁷⁶ J.P. Morgan, *Nigerian Banks 2*, Jan. 12, 2010 (available on INVESTEXT).

⁷⁷ J.P. Morgan, *Nigerian Banks 10*, Oct. 9, 2009 (available on INVESTEXT).

⁷⁸ GT Bank lists Nigeria's first corporate bond in years, *AFX International Focus*, March 18, 2010.

⁷⁹ J.P. Morgan, *Nigerian Banks 1*, Jan 28, 2010.

⁸⁰ *Id.*

⁸¹ J.P. Morgan, *supra* note 36, at 11.

⁸² Sanusi – *CBN for Shake Up*, AllAfrica.com, Dec. 24, 2009.

⁸³ *Banks Not Examined Last 5 Years, Says Sanusi*, This Day, Jan. 8, 2010.

⁸⁴ Sanusi – *CBN for Shake Up*, *supra* note 82.

SANUSI'S FRAMEWORK FOR BANKING REFORM

The above paragraphs describe the rapid, almost frenetic, reform efforts of the CBN and Governor Sanusi to contain the near collapse of the Nigerian banking system since the summer of 2009. Some critics complained of the speed and the lack of coordination of these various regulatory changes by the CBN. On Feb. 26, 2010, Governor Sanusi, in a speech at Bayero University, Kano, to mark the university's annual convocation, set forth his framework for reform of the financial system of Nigeria.⁸⁵ In a forceful and uncharacteristically frank speech by a central bank governor, Sanusi analyzed the reasons for the financial crisis and then described the four pillars upon which financial reform in Nigeria will rest. Sanusi argues that eight factors caused the financial crisis: “(1) macroeconomic instability caused by large and sudden capital inflows, (2) major failures in corporate governance at banks, (3) lack of investor and consumer sophistication, (4) inadequate disclosure and transparency about [the] financial position of banks, (5) critical gaps in regulatory frameworks and regulations, (6) uneven supervision and enforcement, (7) unstructured governance and management processes at the CBN/weaknesses within the CBN, and (9) weaknesses in the business environment.”⁸⁶

The reform program advocated by Sanusi rests on four pillars: (1) enhancing the quality of banks, (2) establishing financial stability, (3) enabling healthy financial sector evolution, and (4) ensuring the financial section contributes to the real economy.⁸⁷ In his February speech, Sanusi elaborated on each.

⁸⁵ Sanusi Speech, *supra* note 49.

⁸⁶ *Id.* at 5.

⁸⁷ *Id.* at 12.

Pillar 1: Enhancing the Quality of Banks

Under this first pillar, the CBN will create “industrial remedial programs.”⁸⁸ Laws must be enforced, and all criminal cases need to be pursued to completion. Selective prosecution based on the political influence of the accused can no longer be allowed. The corporate governance of banks must be enhanced. Good governance is good business, and this principle must guide CBN and bank policy. The CBN will issue new corporate governance guidelines, require banks to update their corporate governance statements, and educate board members about their responsibilities. The CBN will create a new amnesty program under which current directors can make full disclosure of any conflicts without penalty.⁸⁹ Banks above a certain size will be required to create international advisory panels on corporate governance.⁹⁰

The CBN plans to implement risk-based supervision to international standards and will conduct a systematic review of current banking regulations and guidelines with the goal of raising to “world-class standards the supervision processes, technology and people within the various financial regulators.”⁹¹ Consumer protection is part of the reform program. The CBN will become the consumer’s advocate and create a consumer protection department within the CBN. Eventually, this new department will become an independent Nigerian Financial Ombudsman Service.⁹² The CBN will transform itself by reorganizing its staff to achieve better supervision of banks and to better disclose its own operations.⁹³

⁸⁸ *Id.*

⁸⁹ *Id.* at 13.

⁹⁰ *Id.*

⁹¹ *Id.*

⁹² *Id.* at 14.

⁹³ *Id.*

Pillar 2: Establishing Financial Stability

Sanusi notes that Nigeria’s economy has underperformed compared to its potential. As part of maintaining systemic stability, Nigeria must address the volatility of oil prices and must harness its oil resources “for strategic investment purposes.”⁹⁴ In the past, “privatization [of government-owned enterprises] became a polite name for nepotism and cronyism.”⁹⁵ Sanusi calls for the adoption of “a more interventionist, directional economic policy” in Nigeria.⁹⁶ In maintaining systemic stability, the Financial Stability Committee (“FSC”) and Monetary Policy Committee (“MPC”) of the CBN are the primary regulatory vehicles. The FSC will focus on maintaining systemic stability,⁹⁷ and the MPC will focus on price stability and avoiding asset bubbles.⁹⁸

The CBN must develop new macroprudential rules to aid in avoiding severe financial crises. Some possibilities include limiting lending to the capital market to a portion of the bank’s net worth, prohibiting the use of depositor’s funds for proprietary trading (the Volcker rule), and adjusting required capital levels depending on the risk profile of the financial institution.⁹⁹ In addition, the CBN will maintain a stable exchange rate and is unlikely, at least currently, to impose capital controls or limit investment from abroad.¹⁰⁰ The CBN will champion “directional economic policy” to improve basic infrastructure in Nigeria and will “encourage reforms to improve Nigeria’s business environment including property rights, rule of law, ease of doing business and investor risk.”¹⁰¹ Sanusi notes that certain foreign nations, such as Malaysia, Brazil and Korea, have successfully developed their economies by targeting foreign direct investment

⁹⁴ *Id.* at 15.

⁹⁵ *Id.*

⁹⁶ *Id.*

⁹⁷ *Id.* at 16.

⁹⁸ *Id.*

⁹⁹ *Id.* at 17.

¹⁰⁰ *Id.*

¹⁰¹ *Id.* at 18.

to priority sectors. At a recent meeting of the leaders of Nigeria's 24 universal banks and a committee of governors, three sectors – power, transport infrastructure, and agriculture – were identified as priorities for investment.¹⁰²

As part of its development policy, the CBN must balance its target of low inflation against economic growth and poverty alleviation. Sanusi states the CBN will maintain price stability and also become “an active player in the economic development space.”¹⁰³ However, when setting inflation targets, the CBN will set such “targets that are compatible with our growth and poverty alleviation objectives” and indicates that single digit inflation may no longer be an absolute price stability goal.¹⁰⁴

The CBN will also encourage the further development of capital markets by “developing an infrastructure for a corporate bond market, more accessible equity markets, supporting deeper venture capital and micro-finance of new businesses and establishing a sustainable private equity environment, potentially with government seed capital.”¹⁰⁵ As part of this economic development agenda, Sanusi calls for the expansion of the Excess Crude Account¹⁰⁶ to become a full-fledged stabilization fund that “quarantines oil-related excess liquidity before it reaches the Nigerian banking system.”¹⁰⁷

¹⁰² *Id.* at 18-19. The meeting was held in Enugu during December 2009.

¹⁰³ *Id.*

¹⁰⁴ *Id.* at 19.

¹⁰⁵ *Id.* at 20.

¹⁰⁶ Excess Crude Account is a fund containing revenues from royalties, the petroleum profit tax and crude oil sales in excess of amounts set forth in the federal government's annual budget. The account is managed by the Ministry of Finance of Nigeria.

¹⁰⁷ Sanusi Speech, *supra* note 49, at 20.

Pillar 3: Enabling Healthy Financial Sector Evolution

According to Sanusi, consolidation of the banking system into a smaller number of financial institutions is not an end in itself,¹⁰⁸ a statement contradicting his predecessor Soludo's policy. Considering other developing nations such as Brazil, Turkey, Malaysia and Indonesia, several different banking industry structures could serve Nigeria well. The CBN does play a major role in deciding on the structure of the Nigerian financial system. Sanusi notes that "foreign ownership played an essential role in raising standards in the industry" in Turkey, Brazil and Malaysia.¹⁰⁹ Similarly, foreign banks in Nigeria could also raise standards.

The CBN is reviewing the one-size-fits-all banking model and will attempt to introduce more diversity into the Nigerian banking industry.¹¹⁰ One conclusion from the recent special examination of Nigerian banks was that the recent consolidation of the banks in 2005 placed "pressure on banks to deliver high returns to their shareholders after the rapid expansion in their capital base post-consolidation" resulting in "the highly risky behaviour that led to the collapse of some of the banks."¹¹¹

Pillar 4: Ensuring the Financial Sector Contributes to the Real Economy

The recent rapid financialisation in Nigeria did not benefit the real economy. The CBN will advocate for an increase in policy lending programs.¹¹² Again, Sanusi looks abroad for successful examples of policy lending, particularly Japan, Korea, China, and Viet Nam. In those countries, the state provided seed financing for new businesses. In addition to policy lending, the CBN governor will emphasize his role as economic advisor to the President, take the lead in

¹⁰⁸ *Id.* at 20.

¹⁰⁹ *Id.* at 21.

¹¹⁰ *Id.*

¹¹¹ *Id.*

examining “critical issues of economic development,” and create a pilot program with one of the 36 states in Nigeria regarding social economic development.¹¹³

Sanusi concluded his address by noting “a sustainable growth path can be achieved only through substantial and fundamental economic reform” which requires the political will to “reduce corruption and uphold the rule of law.”¹¹⁴

CONCLUSION

Sanusi’s rapid regulatory reforms since July 2009 will result in significant changes in the structure of the Nigerian banking industry and will likely create opportunities for banks and investors already operating in Nigeria and those new to the Nigerian market.

(1) Further consolidation of Nigerian banks is very likely. The eight banks supported by the CBN will become attractive targets once their toxic assets have been transferred to AMCON. Likely purchasers include the better capitalized Nigerian banks that have not received government support; foreign banks already operating in Nigeria – Stanbic-IBTC, Standard Chartered, and Citibank; and certain foreign banks, particularly those from South Africa. Sanusi’s stated intention is to encourage foreign ownership of banks in order to transfer management expertise and skills lacking in Nigeria.

(2) A variety of institutions will provide financial services in Nigeria in the future. The “one size fits all” universal banking model will weaken and the CBN will license institutions to provide different services (corporate banking, small and medium sized business lending, Islamic

¹¹² *Id.*

¹¹³ *Id.* at 22.

¹¹⁴ *Id.* at 22.

banking) to different markets. This change in licensing requirements will create opportunities for financial service providers, other than commercial banks, to enter the Nigerian market.

(3) The CBN will play a more interventionist role in the Nigerian economy. Under Sanusi, the CBN will expand its role in promoting economic development and may even ease its inflation target in order to grow the economy and alleviate poverty.

However, in order for all of these reforms to succeed, the pervasive corruption in the Nigerian economy¹¹⁵ and the weak rule of law must also be addressed. The rapid pace of reform under Sanusi does not appear to be slowing. A key development to watch is the progress of the AMCON bill and the subsequent operation of AMCON – its success (or failure) will be a harbinger of the long-term effectiveness of Sanusi’s reforms to the Nigerian banking system.

¹¹⁵ Nigeria is ranked 130 out of 180 countries based on the prevalence of corrupt practices. Transparency International, Corruption Perceptions Index (2009), at www.transparency.org.

BANKING IN NIGERIA -- TIMELINE

ERA OF BRITISH INFLUENCE

1886 – Royal Niger Company is chartered which begins Britain’s effective control over Nigeria.

1912 – West African Currency Board is established.

1914 – Area is united as the Colony and Protectorate of Nigeria.

1933 – The National Bank of Nigeria, the first indigenous bank, breaks the monopoly of foreign banks.

1952 – 1952 Banking Ordinance, enacted after a banking collapse, establishes a minimum capital requirement, and is intended to minimize the rate of bank failures. Prior to this Ordinance, there was effectively no legal framework for banking in Nigeria.

1958 – 1958 Banking Ordinance enacted to prevent foreign control of banks.

1958 – 1958 CBN Ordinance establishes the Central Bank of Nigeria (“CBN”).

1959, July 1 – CBN operations commence.

FIRST REPUBLIC (1960 – 66)

1959 – Several banking ordinances in 1959, 1961, 1962, 1964 and 1969 attempt to correct known defects in the system and close loopholes in previous legislation.

1960, October 1 – Nigeria gains full independence. The First Republic begins.

1961 – Establishment of the Lagos Stock Exchange, predecessor to the Nigeria Stock Exchange.

1962 – CBN and Banking Ordinances are amended to end the tie between CBN currency operations and the WACB.

1966, Jan. 15 – Military coup ends the First Republic.

1966 – Massacres of Igbos create tribal tensions leading to civil war.

INTERVENING YEARS (1967 – 78)

1967 – Outbreak of civil war between Nigeria and the Republic of Biafra.

1969 – Banking Act amending the 1958 Bank Act gives CBN more authority and increases the lending limits of banks.

1970 – Civil war ends.

1972, July 3 – Decimal Currency Act institutes use of the Naira instead of the Nigerian Pound.

1972 – Nigeria Enterprises Promotion Decree implements an indigenization policy and results in the partial nationalization of foreign-owned banks. The national government purchases controlling interests in the three largest banks.

1975 – Economic Commission of West African States (ECOWAS) formed. Nigeria is a founding member.

1978, Sep. 21 – New Constitution establishes the Second Republic.

THE SECOND REPUBLIC (1979 – 83)

1979 – Second Republic begins under Shagari.

1979 - 1979 Constitution enacted.

1979 – Amendments to 1958 Bank Ordinance increase the minimum capital requirement and delineate the differences between commercial and merchant banks.

1983 – Discussions begin with the International Monetary Fund and the World Bank as the Nigerian government “began to contemplate stabilization and adjustment measures.”

1983, Dec. 31 – Military coup ends the Second Republic. Maj. Gen. Buhari becomes Head of State.

THE INTERVENING YEARS II (1984 – 92)

1985, August – Buhari government “peacefully overthrown” by Maj. Gen. I. B. Babanagida.

1985 – Babanagida’s government embarks on the Structural Adjustment Program with the IMF.

1986, June – The Structural Adjustment Program, including currency devaluation, trade liberalization, reductions in both public spending and employment, and privatization of state-owned enterprises, begins.

1988 – Decree 22 creates the Nigeria Deposit Insurance Corporation, an affiliate of CBN, which has supervisory and insurance authority.

1991 – Banking and Other Financial Institutions Decree revamps the legal framework for establishment of banks in Nigeria.

1991 – CBN Decree establishes greater control over the conduct of monetary and banking policy by CBN. Previously, the CBN and the Ministry of Finance shared responsibility for the licensing and supervision of banks.

1991 – Debt rescheduling with the Paris Club.

1992 – Debt reduction agreement with the London Club.

THE THIRD REPUBLIC (1993 – 98)

1993, June 12 – Third Republic elections are overturned by Babanagida. Government is handed over to Ernest Shonekan on August 27.

1993, Nov. 17 – General Sani Abacha forces Shonekan’s resignation and becomes President.

1994 – Measures related to SAP are essentially abandoned.

1994-6 – The number of distressed banks quickly starts rising, and the CBN assumes control of such banks.

1998, June 8 – Abacha dies. Government now headed by General Abubakar.

FOURTH REPUBLIC (1999 – PRESENT)

1999 – New Constitution written; local and state elections held; Olusegun Obasanjo takes office as President of Nigeria.

1999 – Universal Banking Guidelines of 1999 amends Banking and Other Financial Institutions Decree of 1991 and introduces universal banking.

2002 – Economic and Financial Crimes Commission established to fight financial corruption.

2003 – Obasanjo becomes President after a disputed election.

2003 – Code of Best Practices dealing with the ethical operations of banks and other public companies issued by the CBN.

2004, May 29 – Charles Chukwuma Soludo becomes CBN governor.

2005 – The Paris Club reduces Nigeria’s debt by \$18 billion, subject to Nigeria repaying the \$12 billion debt outstanding by March 2006.

2004 – 2006 – Soludo’s reforms of the banking sector focus on raising the minimal capital requirements to 25 billion Naira and reducing the number of banks from 89 to ultimately 24.

2006 – CBN issues Code of Corporate Governance to help guide the management of banks post-consolidation.

2006, April – Nigeria repays debt owed to the Paris Club.

2007- Nigeria repays most of its London Club debt.

2007, May 29 – Umaru Yar’Adua takes office as President of Nigeria.

2009, June 4 – Sanusi Mallam Lamido Sanusi appointed governor of CBN and begins an aggressive reform program.

CHART B -- NUMBER OF BANKS IN NIGERIA

1960 – 2010

Year	Total Banks	Commercial Banks	Merchant Banks
1960	12		
1970	15	14	1
1975	22	17	5
1980	26	20	6
1985	40	28	12
1990	107	58	49
1998	89	51	38
2000	90	56	34
2001	89	89	0*
2004	89		
2010	25		

Source:

Abel Ezeoha, *Structural Effects of Banking Industry Consolidation in Nigeria: A Review*, 8 J. of Banking Reg'n 159 (2007).

* Universal banking practice was adopted in 2001.

CHART C -- NIGERIAN BANKING INDUSTRY – CURRENT STRUCTURE 2010

(includes foreign owned banks)

	Large Scale Banks	Small to Medium-Sized Banks	Government-Supported Banks
Bank Composition	7 banks	7 banks	10 banks
Listed Banks	Stanbic-IBTC, Zenith, UBA, GTBank, FirstBank	Ecobank, Diamond, Access, Sterling, Fidelity, FCMB, Skye	Oceanic, Intercontinental, Union, Afribank, Finbank, BankPHB, Spring, Wema, Unity
Unlisted Banks	Citi, Standard Chartered		Equatorial

Source: J.P. Morgan, African Equity Research, 2010.