THE MANAGEMENT OF COMMERCIAL BANK PORTFOLIO- A CASE STUDY OF KANO CO-OPERATIVE BANK

AHMED ADO B.Sc. (BUS. ADMIN)

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Department of Business Administration
Faculty of Administration
Ahmadu Bello University
Zaria.

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CERTIFICATION

This project report entitled THE MANAGEMENT OF COMMERCIAL BANK PORTFOLIO :- A CASE STUDY OF KANO CO-OPERATIVE BANK by Mr. ADO AHMED meets the regulations governing the award of the degree of MASTER OF BUSINESS ADMINISTRATION of Ahmadu Bello University, and is approved for its contribution to knowledge and literary presentation.

Dr. O. P. Gupta — Date 8/9/85
Chairman, Supervisory Committee.

_____ Date _____
Member Supervisory Committee.

_____ Date _____
Member Supervisory Committee.

Dr. J. G. Donli — Date _____
Head of Department.

Professor G. E. Osuide — Date _____
Dean, Post -Graduate School.

DECLARATION

I hereby declare that this project for the award of Master of Business Administration of the Ahmadu Bello University, Zaria, is a project of my own work. This particular project relates to the Management of Commercial Bank portfolio as it applies to Nigerian situation. A case study of Kano Co-operative Bank was conducted so as to reveal the implications of Commercial Bank management in Nigeria. It is hoped that the entire work will contribute towards solving the problems of Commercial Banking in Nigeria and Kano Co-operative Bank in particular. It has not been previously presented in any applications for higher degree.

I wish to point out that all informations collected for the entire write-up are clearly acknowledged by means of references. All errors of omission and commission in the work are entirely mine.

ADO AHMED		6/9/85
NAME OF STUDENT	SIGNATURE	DATE

The above declaration is hereby confirmed.

Dr. O. P. Gupta		8/9/85
NAME OF SUPERVISOR	SIGNATURE	DATE

A C K N O W L E D G E M E N T

I wish to express my gratitute to Allah for enabling me complete this project. I am very grateful to the entire members of staff of Business Administration department of Ahmadu Bello University, particularly the academic staff. I particularly thank my Supervisor Dr. O. P. Gupta and the MBA co-ordinatorr Mr. U. Janakiraman for their assistance and guidance throughout my course. My special appreciation goes to the Head of Department Dr. G. J. Donli and the distinguisned Professor N. R. Chatterjee from whom I gained alot of valuable practical and theoritical knowledge.

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A B S T R A C T

Portfolio Management in a commercial Bank is not an easy task. It involves deciding on the type and composition of various assets to maintain given the level and composition of the deposit liabilities. This is done in such a way that safety and profitability is ensured. In the management of Commercial Bank portfolio these two objectives are found to contradict one another.

This project analyses the problem of commercial Bank Portfolio Management as it relates to Nigerian situation with particular reference to the case of Kano Co-operative Bank. In so doing the past operations of the Bank have been analysed with the view to identifying the degree of effectiveness and efficiency with which the problem of portfolio management was handled.

In the course of the analysis, the various regulations in the Nigerian banking industry have been considered, with the view to exposing the extent to which such regulations affect the efficiency with which Commercial Banks manage their portfolio of assets.

The number of findings will certainly go along way towards contributing to the ways to go about solving the problems of Commercial Bank portfolio management in Nigeria, and Kano Co-operative Bank in particular.

D E D I C A T I O N

This Project is dedicated to my Wife, Mrs. Rabi Ahmed, and my twin daughters, Karimatu and Salimatu. Who missed me during my absence for the studies.

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CHAPTER ONE

1.1 INTRODUCTION

An individual Bank can be seen as economic unit that aims at maximizing profit. To attain this goal certain Portfolio of assets are held within certain contraints imposed by the nature of Banking. Given the characteristics and distribution of liabilities held, efforts are geared towards structuring the the portfolio in such a way that returns are maximized within the constraints the banking system imposes. A bank has to conserve its position and its assets, little loss can be afforded. The reward for good banking is in most cases modest but pernalities for poor banking are considerable. For this reason a Bank must operate with rather narrow profit and loss margins. The amount of Capital being employed as compared to the total amount dealt in is usually small. Given such a situation loss must be minimized while the tendancy should be towards profit maximization.

Safety and produlence is of particular importance in commercial banking. A Bank has the crucial responsibility to pay on demand without notice a considerable amount of its deposit liabilities. A large demand on liquidity is not in most cases being experienced by a Bank, but it is obvious that Bank should expect a rather large fluctuations in demand on their liquidity.

This fluctuation must be honoured without any delay to ensure reputation and continued existence. Banking unlike other forms of business cannot afford slack in business. The other aspect of banking that constrast the need to maintain liquidity is that a Bank makes a living through putting the money at its display to work. This brings about the problem of survival without jeopardizing the safety of the institution. The act of banking therefore is to trade off between being safe and at the same time profitable.

Conceptually Bank assets can be divided into components such as reserves, investments and Loans. The management policies and decisions serve to identify and measure the interrelationship among these elements. Decisions concerning Loans and investment strategies are closely linked to management of Bank liquidity position. In managing liquidity position a Bank is confronted with the problem of trade off between liquidity and profitability. Liquid assets provide zero or low returns, Bank Managers must constantly analyze the opportunity cost involed in not reducing liquid assets and increasing higher yielding assets.

Management policies in a commercial Bank are therefore more concerned with the management of current assets and current liabilities. This involves deciding on the nature and composition of the assets to maintain in relation to the liabilities.

The purpose of this study is to determine the degree of effectiveness and efficiency with which the management of Commercial Bank assets and liabilities were being handled in Kano Cooperative Bank. That is determine the extent to which the problem of portfolio of assets diversification with the view to profit maximization was being handled.

It is important to point out that this study does not intent to explore into the details of portfolio management theories which have been well developed. The use of the phrases Portfolio Selection, portfolio of assets, portfolio diversification and portfolio management is limited in this study. The use of such phrases is used to describe the art of Bank Management that involves deciding on the types of assets to be maintained, in a form of portfolio of assets, with the view to profit maximazation.

An observation at the performance of the Bank for the period between 1980 and 1984 reveals that during this period the Bank started experiencing decline in profit and later losses were recorded. This is a symptom of problems somewhere. The purpose of this study is to try and identify these problems. With the problems identified, an opportunity will open to enable reasonable suggestions to be made with the view to remedy the situation.

Before proceeding with the study an interview was conducted so as to accertain the various views held by people as to what the problems of the Bank are. Based on the interview the following problems were highlighted:-

1.2 Problem Statement

1.2.1 Problems Associated With Lending Policies and Procedures

Here the arguement is that there is no clear lending policies and procedures, closely linked to the absence of such policies is the political influence on the Bank, resulting into the managements inability to have freehand in conducting the affairs of Bank. External forces played a major role in the granting of Loans, this resulted into the considerable percentage of the loans going into bad and daubtful category.

1.2.2 Problem Of Liquidity

One of the issues related to problem of liquidity is the small size of the paid up capital. At the point of inception the authorized Capital was ₦3 Million (1977), this was increased to ₦6 million and ₦10 million in 1978 and 1983 respectively. Despite the increase in the amount of the authorised Capital, out of the amount issued ₦3,889,781 is fully paid. The amount fully paid for is certaily small and so creating poor liquidity as a result of the unsound capital base.

Most of the money used for lending came from Central Bank reserve account, the overdrawing of which produces considerable amount of burden on the profit and loss account resulting from the interest charges.

Another issue related to liquidity problem is the absence of government patronage. Most of the major accounts owned by the state Government are not in the Bank. The Government has not as well given encouragement to the Co-operative unions to settle the balance on the shares alloted to them, amounting to N1.2 million. The absence of government patronage has had alot of influence on the part of the individuals and business organizations. Allthese have serious implications on the liquidity of the Bank against the level of services it is expected to render.

1.2.3 Problem of Overhead

The Bank with small amount of Capital base coupled with the tramendous amount of services it is expected to render is faced with the problem of high overhead expenses. The expectation for service comes from both the public and the Central Bank. From the point of view of the public the Bank is expected to render the normal Banking Services and the Central Bank under the rural Banking Scheme, expects the opening of a specified number of rural Branches.

(ii) To make necessary suggestions as to the ways improvements can be made towards more effective and efficient management of the Bank.

1.3 Hypothesis Statement

A hypothesis is an untested Statement of causal relationship between two or more variables. A hypothesis sets the ground for a research to be carried out to determine the causal relationship between variables. The outcome of the study will either validate the hypothesis or make it invalid. The outcome of the study in most cases does not agree with the hypothesis, however the determination of causal relationship is always the case. The statement of hypothesis based on the information gathered, for the purpose of this study is as follows:-

"The absence of concious management effects in determining the type and composition of portfolio of assets to hold at various times resulted into the poor operations of the Bank".

1.4 The Methodology

The approach used involved literature review on the various aspects of Commercial Bank Management. This has been related to the various regulations that Banks will have to comply with. Data was collected through interviews with the Senior Management and Senior Staff of the Bank, through the use of yearly final accounts, and through access to the various consolidated accounts at the headoffice. The researcher had the opportunity to interview the General Manager, the two assistants of the General Manager and the Secretary of the Bank. Free access was given to all books of account. The data collected was analysed to determine, from the theoritical frame work, the extent to which it relate to the conditions of the Bank.

1.5 Period Covered

In the literature review the period covered is between 1980 and 1984. This involved relating the Commercial Bank Management to the various regulations in Nigeria within that period. In analysing the case of Kano Cooperative the entire period from 1977 to 1984, that is from its inceptional period, is covered. This is with the view to exposing and comparing the management practices from the time of its inception to the time when certain problems started to signal. The period covered therefore is not much to be burden.

1.6 Organization of the Study

Chapter one being an introduction is followed by chapter two which forms the literature review as related to the banking regulations in Nigeria. Chapter three analyses the case of Kano Co-operative. Problems and Prospects of Kano Co-operative Bank are in chapter four. Chapter five forms summary and recommendation.

CHAPTER II

2.1 Introduction

The purpose of this chapter is to examine the underlying principles governing the management of Bank assets. In practice the management of Bank assets is a complicated process, it involves satisfying number of requirements which in most cases are contradictory. The most important requirement of any Commercial entity is profit maximazation. Banks are no exception to this rule. In attempt to maximize profit a Bank maintains portfolio of assets that contribute more towards attaining this objective. But this must have to be within certain constraints imposed by the nature of Banking. The amount of Capital employed in any Bank is modest in relation to the total Sum dealt in.

With modest capital employed this calls for loss minimization. In considering the principles underlying the management of Bank assets the various constraints will be considered with special reference to Nigerian situation.

The problem of banking operation is to resolve the conflict between profit maximazation on one hand and safety of employing the acquired assets into earning assets on the other. This involves deciding on how to allocate the resources into assets with various degree of liquidity, profitability and risk. Cash is regarded as the premier asset, converting cash into other assets involves taking risk. The degree of risk taken determines the amount of interest income that a Bank can earn. Employing cash in assets that are considered to be Superior implies Sacrificing higher returns but ensures higher degree of safety. Conversely assets with higher returns have higher risks associated with them. Therefore management of Bank assets attempts to trade off between profitability through acquiring earning assets and safety by maintaining non-earning assets. Another problem involves deciding on allocating resources into Loans and investment. That is deciding on the portfolio of earning assets to maintain.

In ordering priorities where profitability and safety contradict in deciding on the type of assets to hold, safety should be placed first before profitability. In deciding what sort of assets to maintain decision should be based on the institutional advantage that exists in holding such assets.

In deciding on the portfolio of assets to maintain, safety given first priority, meeting the reserve requirement is considered first. This is the legal frame work of the management of Bank assets. The legal reserve requirement has two implications, one from the point of view of the depostors and two from the point of view of the Central Bank of Nigeria. A Bank must maintain sufficient cash to meet the demand on deposit that customers can make without notice, this has legal implications and it determines the continuity and safety of the Bank. From the point of view of the Central Bank, the Banking decree 1969 has provided that by"virtue of section 40 of the Central Bank of Nigeria act", the Central Bank shall from time to time based on the monetary policy that it wants to adapt, stipulate a minimum holding of cash reserve, specified liquid assets, special deposit, and stabilization securities that a licence bank shall maintain. The ratios are always specified in the annual Central Bank of Nigeria Monetary policy guidelines. In 1984 for example. The reserve requirement based on the sizes of the Banks is given as below:

2.1 1984 Cash Reserve Requirements

Class	Total Deposit Liabilities	
A	₦300 million or more	5.00%
B	₦100 million or more but less than ₦300 million	4.00%
C	₦30 million or more but less than ₦100 million	3.00%
D	Less than ₦30 million	2.00%

The size of the liquidity ratio has been 25% over the years. Maintaining the reserve requirement therefore ensures safety because of legal implications from the point of view of the customers and the Central Bank. Without meeting this legal requirement the continuity of the Bank is certainly at a stake.

However one can argue that the legal reserve requirements in most cases result into a Bank Maintaining assets in liquid form far more than what safety may warrant. Holding such assets may simply be viewed for no any other reason than to meet what the Law imposes. In fact holding excess liquid assets does not guarantee safey on the part the Bank in the longrun. But where the law specifies the legal reserve requirements and in as much as the Bank satisfies these requirements and maintains liquid assets to a level that it is confident to satisfy cash demand there is no viability in holding excess cash over and above this level. A Bank should maintain cash as minimum as possible because the actual safety of a Bank comes from maintaining earning assets. In deciding on the portfolio of the earning assets however, a Bank should first of all consider the need to have assets with closeness to cash in anticipation of the Cash demand and legal reserve requirement.

This calls for establishing the protective reserve known as the Secondary reserve. The protective reserve takes the second place interms of priority after the primary reserve. The protective reserve consists of assets that can easily be converted to cash without a loss on the principal invested. Safety is place first while earning is given the Second priority. This reserve is maintained for forecastable and unlikely but possible demands for Cash. It is made up of assets that can be regarded as liquidity instruments. These liquidity instruments are avilable in money market which is defined as "the active market for money and close money substitutes which financial institutions and other rel y on to provide the liquidity needed in the usual course of their operation". Liquidity instruments include money at call, balances held with other Banks, government treasury bills (available at weekly auction) treasury certificates (with maturity between one and three years), commercial papers (such as promisory notes), and Bankers acceptances.

Maintaining Primary and Secondary reserves is for the purpose of establishing a safe ground, After establishing this any excess cash should be directed towards what can be termed as the business of Banking, that is lending. Lending is employing cash into normal banking risk. Because of the risk associated with lending which is higher compared to other assets, it takes the third priority. The return from this is however higher.

In determining the amount of loan to grant the genuiness of loan demands should act as a guide. Once all the genuine demands for loans are met the excess cash balances should be employed in acquiring investment assets through open market investment.

In a nutshell Banks allocate their assets in order of priority based on safety and profitability, where safety and profitability conflict, Safety should take the higher priority. Primary reserve requirements placed first followed by protective reserves. These two serve the safety need for liquidity. The loan portfolio comes after these two for profitability and Longterm Safety. The investment portfolio which straddle both sides of loan portfolio features for the second time after the loan portfolio to prevent holding of ideal cash and ensure profitability.

The next part of the chapter will be devoted to detailed examination of the individual components of the portfolio of assets maintained by a typical Bank within the provisions of law for the reasons of profitability and Safety. The section is divided into three, management of liquidity, management of Loans and management of investment. The conclusion will centre on other aspects of management relevant to portfolio management.

2.2 Liquidity Management

As pointed earlier a Bank should maintain certain amount of resources in form of cash and near cash assets to meet the legal requirements. The legal requirements includes on one hand the need to meet the demand by depositors and the need to meet the Central Bank regulations on the other. Meeting these needs therefore is for safety reasons from the point of view of the Bank. But this does not call for maintaining excessive cash balances because doing so is not in the interest of the Bank. For example, if one considers the fact that some of the deposits drive their source from time and savings deposits on which interests are being paid, holding excess cash will mean incurring losses. This creates a situation where a Bank will not be able to build its reserves which are vital to the continuity of its existence. The factors determining the degree of liquidity that a Bank maintains will now be examined.

2.2.1 Legal Reserve Requirements

Section 12 subsection (1) of the Banking decree 1969 states that "every licenced Bank shall maintain a holding of cash reserves, special liquid assets, special deposits in Central Bank and stabilization securities as the case may be, not less in amount than as may from time to time be prescribed by the Central Bank of Nigeria act"

This section of the Central Bank act empowers the Central Bank to, based on the monetary policy guideline that it wants to impliment vary the different reserve requirements.

2.2.2 Cash Reserve Requirement

(Introduced 1976)

This is a minimum of cash balances that is expected to be maintained by each Bank as specified by Central Bank in the annual Central Bank of Nigeria monetary policy guidelines. Banks are classified into four categories based on their sizes for the purpose of specifying the cash reserve requirement. From 1980 to 1984, below shows the various cash reserve requirements associated with each class:

Table 2.2 Cash Reserve Requirement 1980-1984

Class	Total Deppsit liabilities	1980	1981	'82	'83	'84
A	₦300 million or more	6.25%	5%	5%	5%	5%
B	₦100 million or more but less than ₦3 million	5%	4%	4%	4%	4%
C	₦30 million or more but less than ₦100 million	3.5%	3%	3%	3%	3%
D	Less than ₦30 million	2.5%	2%	2%	2%	2%

The amount of reserve maintained is non interest earning. From 1979 the Central Bank went to the extent of assuming the responsibility of calculating on monthly bases the cash reserve of all the Banks. Each bank use to be debited with amount of the cash reserve requirement as a percentage of the total demand deposits, where an increase in the total demand deposit features. Where a decrease results the Banks is credited and the reserve account debited. It can be seen that a Bank cannot depend on its cash reserve requirement to meet demand on deposits, or use it as a bases for increasing the level of loans or investments. The cash reserve requirement therefore is not a protective asset.

2.2.3 Stabilization Securities

Stabilization securities were introduced in 19 . They were issued at 4% and placed with banks based on increases in their savings deposit accounts within N20,000 limit. It was based on the policy objective of 1976 directed towards moping excess liquidity, maintaining price stability and encouraging savings. These securities were not to be included in determining the liquidity ratio This placed considerable amount of restriction on the Bankers ability to invest in earning assets and so had serious implications in the management of the portfolio of assets with the view to profit maximization. Stabilization Securities were phased out during the 1979/80 fiscal year.

2.2.4 Special Deposits

The Central Bank can call for special deposits from the Banks, depending on the monetary policy, Such special deposits are excluded from the eligible assets that are considered as liquid. This action greatly affects the liquidity of Banks as such reduces their ability to expand credit.

2.2.5 Other Forms of Deposits

Other forms of deposits include compulsory deposit for Imports, deposit for the shortfall of Loans to agriculture and residential building, the shortfall with regards to the specified ratio. All these are not considered to be part of the eligible liquid assets of a Bank. This places real constraints with regards to the ability to expand credit.

2.3 Liquidity Ratio

The Central Bank also specifies the ratio that has to be maintained between the eligible liquid assets and the total demand liabilities. This is the liquidity ratio, which has been specified as 25% over the years.

$$\text{Liquidity ratio} = \frac{\text{Total eligible liquid assets}}{\text{Total current liabilities}}$$

2.3.1 Liquid aAssets Include

Cash held by banks as balance in vault
Balances held with Central Bank (shortfall on loans to agriculture, residential building, reserve requirement, compulsory deposits for imports are excluded from this)
Balances held with other Banks in Nigeria (excluding uncleared effects)
Nigerian treasury bills
Nigerian treasury Certificates
Money at call with other Banks
Certificate of deposits held (of not more than 18 months to maturity)
Government Securities (of not more than 3 years to maturity).
Bankers Unit fund

A more detailed discussion will be made on some of these items under investment portfolio.

2.3.2 Current Liabilities Include:

Current, Savings and time deposit account balances; Certificate of deposits(of not more than 18 months. maturity)
Balances due to other Banks.
Balances held for external office (less balances due from external office)

The Central Bank regulatory measures are seen as aimed towards tackling the problems of under capitalization, inadequate resources and inadequate liquidity in the banking system. This started with the 1952 ordinance which developed up to the time of establishing Central Bank of Nigeria. All efforts were directed towards improving operations of the Banking System in order to engender and sustain public confidence in banking and thereby improving the general banking habit of the community. The regulatory effects also aim at eradicating malpractices in banking. This is ensured through the routine inspection by the inspectorate department of the Central Bank to ensure compliance with all the guidelines given by the Central Bank.

However the number of regulations on the commercial Banks place considerable amount of constraint from the point of view of their liquidity and hence their ability to determine the portfolio of assets to maintain with the view to profit maximization. Once the legal reserve requirement has been met, under normal circumstances any excess fund should be employed at the descretion of the management within the a safety requirements and the profit motive. The next priority after the primary reserve as earlier stated is the protective or the Secondary reserve.

2.4 Secondary Reserve

The Secondary reserve is maintained for two reasons, namely to prevent holding cash which is not an earning asset, and to invest insuch earning assets that can easily be converted to cash with no less on the Original Principal with the view to meeting likely, remote and uncertain demand for cash. Prudence here ensures higher return and at the sametime maintenance of adequate liquidity. In this respect the management should match the assets with the time period which the liquidity is desired. Assets used to meet volatile demand deposits fluctuations and seasonal Loan demands will appropriately be different from assets used to meet possible residual outflow of Savings deposits and secular increases in Loans.

Seasonal demands for loan should be matched by assets that mature close to the time when demand arises or ones that can be converted to cash without their value falling, examples, balances held with other Banks and treasury bills. The liquidity need for cyclical or secular increases in cash or loan demands may be held in longer term liquidity instruments example government securities with maturity over three years.

Seasonal movement of cash demand are attributed to things like festivals (Sallah and Xmas), weather (agricultural loans). There also use to be a coincidence between loan highs and Deposit lows . This characterised a situation where customers demand for loans follow withdrawal from their deposit account likewise loan repayments is followed by lodgements into deposit account. To the extent that a Bank has a concentration of customers with similar economic characteristics, causes of peak for cash demand and loan demands coincide with low deposits. The Community may be single industry community or agricultural community.

Random demand for cash on the other hand unlike the seasonal demand cannot be anticipated. A Bank should however make provision for such movements.

Treasury bills holding by Commercial Banks was promoted by the Central by making it possible to rediscount such bills at par without loss. The issue of treasury bills has been on weekly bases since 1963 and the fact that they have been considered as among the assets that meet the statutory liquid assets requirements of commercial Banks, they form a major component of the assets of most commercial Banks.

2.4.3 Treasury Certificate

To enhance the development of money market and increase the governments ability to borrow ,treasury certificates were introduced in 1968. Treasury Certificates are issued with one or two years maturity period. Their easy convertibility to cash without loss on the principal invested and their inclusion in the specified elligible liquid assets of commercial Banks make them attractive to such institutions. In fact between 1969 and 1977 between 88 and 98 percent of the total issue was held by commercial Banks.

2.4.4 Call Money Fund

The call money Scheme was introduced in 1962 with the aim of creating an avenue where commercial Banks can invest their surplus funds on a temporary overnight basis. In this Scheme commercial Banks were expected to deposit cash with Central Bank for the purpose of clearing. The money in excess of the amount required for clearing was transfered to the call money fund and an interest slightly below the one paid on treasury bills was paid on such overnight balances. This Scheme was phased out in 1974 as a result of fall in investment outlet for excess fund following shortages of goverment short term debt instruments.

2.4.5 Certificates Of Deposit

These were introduced in 1975. They were classified into negotiable certificates of deposit and non-negotiable certificates of deposit. These are interbank instruments of liquidity that are aimed towards aiding the flow of excess fund from commercilal banks to Merchant Banks. The issue are by merchant banks and held by commercial Banks with maturity varying between 3 and 36 months. However they can be rediscounted at Central Bank. This makes them liquidity instruments and they form part of the Commercial Banks e ligible liquid assets.

From the above one can see that the source of acquiring liquidity instruments by commercial banks is the money market. In Nigerian situation the money market can be considered to be not fully developed and highly regulated by the government through the Central Bank. This has a very serious implication from the point of view of commercial Banks decision with regards to the portfolio of liquidity instruments to maintain. The Central Bank determines to a very large extent the volume and cost of the different types of instruments available in the market. The interest structure has been regulated and kept relatively below what would have been under free market mechanism of demand and supply. The structure of the banks portfolio of assets and the subsequent profitability of such portfolio is greatly determined by the various regulatory measures.This left little freedom to the commercial Banks ability of using their descretion in selecting the portfolio of assets.

Another government influence comes as a result of the situation whereby the Government has been the major source of supply and the major user of the money market funds, it determines the direction and pace of the activties in the money market.

To sum it all the interest rates the returns and maturity of most of the instruments are determined by the Government. With regards to the private securities, commercial Banks are bared from purchasing company stocks, shares, debentures and similar securities quoted in the Stock exchange. The need for resource optimization in commercial Banks therefore has been greatly constrained.

As a result of the regulatory nature of money market commercial Banks in Nigeria experienced excess liquidity during the Oil boom, evident by the monetary ease policy adapted between April, 1972 and March, 1976 aimed towards moping excess liquidity. During depression however banks face the problem of tight liquidity, this was clear reason for the "stringent monetary restraint policy" of 1981 to 1982 aimed at curbing credit expansion due to tight liquidity. The excessive regilation has created a situation whereby commercial banks have not been given a freehand to manage their affairs in such a way to take care of the future ew events. A situation is created whereby attempts to solve problems are made after the problems are already around. The attempts towards solution has always been from the Central Bank.

Lending is the cornerstone of the banking operation because it contributes more to the profitability than other portfolio of assets and by being the Key element in creating and maintaining depositor relationship.

Because of the impotant position taken by loan in the portfolio of assets of a Bank there is need for clear policy statement in this area. Philosophy and concepts of lending include statement of standards guidelines, and limitations. The policy should be in writing and all parties concerned should have a clear understanding of the policy objectives. Written policy is normally produced by the board of Directors and is important that it conforms with the objectives of the organization and at the same-time exhibit some degree of flexibility. The policy statement should take care of the desirable level of interest, compensatory balances, nature and types of acceptable collateral securities, sectoral allocation, and type of borrowers.

The lending policy should be such that it incorporates the basic principles of good lending. Before discussing the basic principles of lending it is important to point out that the implementation of the lending policy will come after meeting the primary and secondary reserve requirements and the excess money over this has been established.

2.6 Elements Of Lending Principles

2.6.1 Purpose

(ii) Meeting The Credit Needs

One of the purposes of Bank lending is to meet the credit needs of the community in which it operates. The recognition of this function is very important. Likewise it should be recognized that not all types of credit needs can be met by a commercial Bank. Because some by virtue of their capital nature and the long term nature are not institutionally advantageous for a commercial Bank to participate. Recognition of the area of Credit which the Bank can fill and the formation of policies based on this is very important.

(ii) Maintaining Depositor Relationship

Loans should have as one of their objectives, maintaining relationship with customers particularly business organizations. Most customers maintain deposits for the purpose of enjoying Loan facilities should the need arises. To ensure deposits Banks should strive towards meeting these demands for the purpose of maintaining the relationship.

(iii) Profitability

For the purpose of continuity profit must have to be achieved to build sufficient reserves. Lending therefore should have profit as its motive.

2.6.2 Safety

Loans though considered to yield higher returns than other form of assets do not break the rule of higher risks associated with higher returns. It is considered the most risky form of asset maintained by Banks. One risk associated with loans is that of repayment, that is tha chances that the amount given out will not be recovered. The second risk is that of liquidity of the Bank. If lending results in low liquidity the chances of not meeting the legal requirements from the point of view of the customers and the monetary authorities are higher. Lending policy should therefore determine the level of risk to be taken.

2.6.3 Suitability

A particular lending level may satisfy all the above objectives from the point of view of a particular bank, namely, satisfying the community, the depositor, bankers profitability and safety needs but may not be suitable for technical reasons. Lending in Nigerian Banks is regulated to meet the economic and monetary policy measures. The regulation is through the monetary policy guidelines. In policy formulation therefore banks should take into account these guidelines to make their lending policy suitable. Likewise one may not expect policy not to exclude lending for financing gambling, betting and any formsof similar speculative ventures.

2.7 Policy Formulation

Well formulated lending policy and a careful lending practice is important if a Bank is to perform the lending function efficiently and effectively. The policy statement based on the above principles should state the size of the loan portfolio, the nature of the loans, the loan terms, the loan granting and servicing.

2.7.1 Policy Regarding Size of Loan Portfolio

Once a Bank has met the reserve requirements and has made adequate provisions for liquidity needs through acquiring the appropriate liquidity instruments, any excess fund should be utilized into the basic business of banking that is lending. A policy statement however will have to be based on the ability and willingness to meet the community's sound demand for credit. The ability will be determined by the banks liquidity and the quality of its staff. Once this has been established then the other consideration is the community's need for credit which is assessed through the number and types of applications received. This method is no longer effective, there is growing need for bank officers to search for genuine loan applications and establish the present and future needs of the present customers.

The outside look needs a formal market research to establish the credit needs, this done with the view to meeting the challenges of other com petitive sources of credit. Policy regarding size of the Loans to be granted will be based on the banks ability and genuine credit need of the community. Another consideration with regards to the size of the loans is size of capital of the Bank. The capital account of the Bank reflects its ability to absorb losses as such the individual Loans and the aggregate loans as a matter of policy should not exceed certain predetermined proportion in relation to the total capital of the Bank.

2.7.2 Type Of Loans

Policy need to be formulated on the type of loans to be granted. This should be based on the credit needs of the community, type of deposits maintained and the extent to which fluctuation in the interest rate structure can be accommodated. The type of loans to be granted should be based on the Central Bank monetary policy guidelines, which stipulate the proportion of Loans that are to be made to the various sectors of the economy.

2.7.3 Loan Terms

Lending terms, as a matter of policy, should be based on interest rates, compensatory balances, repayments and collateral security.

The interest structure is determined by factors that are beyond the control of a particular Bank. The interest rate under normal circumstances, is determined by the forces of demand and supply. During boom the demand for loans is normally high and hence higher interest rates. In depression the reverse is the case. The supply for cash is determined by the level of saving and the monetary policy as it affects credit.

Banks within the constraints of demand and supply manipulate the interest rate in granting loans. The forces of demand and supply determine the ceiling for lending. The floor is set by the cost of lending, cost of servicing and the probality of loss. The interest rate is an area that lending policy will have to considerer among other areas.

Lending terms also include, in most cases the need for the borrower to maintain certain compensatory balances as precentage of the total loan facilities. This is done with aim of screening and differentiating the applicants. From the point of view of risk, such balances will reduce the amount of loss in case of default.

The specification of repayments with regards to the loans is very important area of policy making which, states the amount and period of repayments for the various categories of loans. Loan should be repaid as planned, the repayment should have its source from assets or profit of the borrower, rather than from forced liquidation. Policy regarding repayment period in most cases will reduce the chances of repayment through forced liquidation.

In the event of default if no concrete provisions are made to take care of such situation a bank will incure considerable amount of loss. Hence eventhough a bank has established a loan to be sound in terms of purpose, repayment and suitability the need to have protection against default is important. The need for policy formulation regarding collateral Securities associated with the various Loans must be considered.

2.7.4 Organization

In granting loans there is need to specify the unit of authority at various levels. It is impracticable to expect that all loan applications will have to be cosidered at the board of directors level, hence the need to delegate authority with regards to amounts and nature of Loans to handled at lower levels. It is important to note that the entire responsibility of granting loans as a matter of policy should rest with the bankers who happen to have the technical know-how. Directors lack knowledge regarding banking and are bound to be influenced by subjective rather than prudent considerations. Policy formulation with regards to organization for lending need to be based on how best the exercise can be efficiently and affectively performed. As part of the organization, monitering has to be given an important priority and it should form a unit of the organization.

This section has attempted to show the various complications associated with lending by commercial Banks. Safety is of great importance, this considers the risk associated with repayments, liquidity and continuity. Profitability consideration on the other hand is for the attainment of banks objectives in the shortrun and the longrun. It is important however to point out that commercial Banks in Nigeria have considerable degree of constraints placed on them with regards to their ability to grant loans. The granting of a particular type of loan may be seen to satisfy all the purposes that a bank may require, namely meeting its objectives, meeting the demands of the community, and being safe, but granting may not be possible. This is because such loans may not suit the conditions imposed by the monetary policy guidelines of the Central Bank of Nigeria. A brief examination of the degree of restrictions with regards to lending by commercial Banks is important.

The control by the government through central Bank on the banking system is considerable. Besides setting a limt to bank credit through aggregate ceiling on the rate of expansion, the Central Bank of Nigeria goes to the extent of prescribing sectoral and sub-sectorial allocation of loans and advances.

Toensure compliance with some of the allocations, Banks are compelled to deposit shortfalls on the certain Loans, where they have not granted up to the specified ratio. Below shows the aggregate credit expansions on from 1980 - 1984 and the sectorial allocation of credit for 1983 as per Central Bank of Nigeria guidelines.

Table 2.3 Aggregate Credit Expansion

	1980	1981	1982	1983	1984
Aggregate Credit Expansion	30%	30%	30%	25%	25%
Banks with Loans and Advances not exceeding ₦100m.	40%	40%	40%	35%	35%

Table 2.4 Sectorial Distribution of Loans

		1983
A.	Preferred Sector	61
(i)	Production	10
	Agriculture	
	Mining	2
	Manufacturing	36
	- Agro-allied industries	(3)
	- Other Maf.	(33)
	Construction	13
	- Residential	6
	- Others	7
(ii)	Services	12
	Public Utilities	3
	Transportation and Com.	9
(iii)	Exports	2
(iv)	Development inst.	1
	TOTAL	76

Table 2.4 cont.

B. Less Preferred Sectors	1983
(v) General Commerce	16
Imports	6
Demostic Trade	10
(vi) Others	8
Credit and Fin. Inst.	1
Government	3
Personal & Prefessional	4
TOTAL B	24
A + B	100

2.8 Investment Portfolio

As mentioned earlier the portfolio of assets maintained by a Bank is based on priority which takes into account legality, safety and profitability. The first priority involves maintaining funds to meet the legal requirements with regards to customers and Central Bank requirements. The second priority involves making the necessary provisions for practical reasons which involves meeting liquidity needs through maintaining liquidity instruments. The next priority involves utilizing the excess fund to meet the demand for loans for practical reasons.

After meeting all these requirements any excess fund should be invested by acquiring assets in the financial market. The investment decision therefore can be seen to struddle on both sides of the Loan portfolio. On one side the decision is based on meeting the liquidity needs, on the other side it is based on acquiring income generating instruments with the view to absorbing excess fund that are not required in the near future. It is this second aspect that is the concern of this section.

Investment of this nature involves acquiring longterm government stocks and Corporate stocks. Commercial Banks in Nigeria are barred from acquiring any form of coporate stocks, bonds and debentures as contained section 13 sub-section of the Banking decree. For this reason the longterm investment of commercial Banks in Nigeria is limited to federal government stock with maturity over three years and other instruments that are not considered part of the elligible liquid assets.

2.9 Conclusion

The management of portfolio of assets in the commercial Banking system is highly regulated. The regulation ranges form specification of the reserve requirements, and liquidity ratio to the type and allocation of credits that a Bank can make. The type of liquid assets that a Bank can maintain is as well limited so also the longterm investment instruments. Government participation in the financial market affecting both the capital and money markets is a serious constraint that commercial Banks will have to recken with.

However within these constraints commercial Banks have some degree of freedom in management of their affairs. Based on their positions banks can decide on the portfolio of liquid assets to maintain, from the ones available. Decision with regards to extending Loans to each particular sector can be accessed based on merit for doing so within the lending principles, policies and practices. Decision can be made as to whether to invest in longterm stocks or not. Whatever the case the various constraints have greatly affected the banks ability to operate with higher profitability, effectiveness and efficiency that would have been the case where the constraints have been normal banking operation constraints.

CHAPTER III

KANO CO-OPERATIVE BANK-
CASE ANALYSIS

3.1 Introduction

Kano Co-operative Bank was established on the 1st of April, 1976. The main objective of the Bank was to assist in financing Co-operative Socities. This was going to be possible through providing greater access to banking services for such societies and their members than the ones provided by other commercial banks. In financing the cooperative societies it was expected that its operations would be guided by certain cooperative principles and practices. The Bank was however licenced as a full commercial Bank, hence this could have provided a wider opportunity for deposit base, which could be used to provide greater services for the cooperative socities and its members.

The initial authorized capital was ₦3 million which was increased to ₦6 million and ₦10 million in 1976 and 1980 respectively. However the increases in the authorized capital has not yet being issued. Out of the authorized capital ₦1.2 million was fully paid up as at 31st March, 1976, ₦2,346,341 by March 1977, and ₦2,666,463 by March 1978. As at the end of financial year 31st March,1984 the fully paid up capital was ₦3,889,781. With Kano State Government subscribing nearly 99% of fully paid capital.

Only 1% of the fully paid-up capital subscribed by the cooperative unions. A balance of ₦1.2 million is yet to be paid in full by the cooperative Unions, this represents the amount alloted to them.

The purpose of this chapter is to analyse the extent to which the portfolio of assets of Kano Co-opearative was being managed. This will be within the framework of the commercial Bank portfolio management contained in the previous chapter. The analysis start by considering the liquidity management aspect, the Loan portfolio aspect and then investment portfolio management aspect. It is important to mention that the period to be covered will be fromMarch 1977 to March 1984. This is for the fact that the first report of its operation was on March, 1977 and so covering this entire period will provide a greater insight into the operations of the Bank.

3.2 Liquidity Management

This is the most crutial aspect of portfolio management of Bank assets. It has an important place from the point of view of legality and continuity. On the one hand it involves complying with the Central Bank of Nigeria regulation concerning the cash reserve requirements and the liquidity ratio. On the other hand it involves making sufficient provisions, in form of cash and liquidity instruments, to meet customer demand in such a way that the amount of cash held is not unnecessary higher than required. This section is therefore divided into primary reserve requirements and the secondary reserve requirements.

3.2.1 Primary Reserve

(i) Cash Ratio

The Central Bank of Nigeria computes on monthly basis the amount of reserve that each Bank should maintain with Central Bank, Based on the total demand liabilities. The amount arrived at is debited against the current account of the particular Bank and credited into a reserve account. The determination of the amount to be transfered to the reserve account, therefore, is beyond the control of the individual Banks.

Below shows the amount that should feature in the reserve account of Kano Co-operative Bank, the computation is based on the cash ratio to total demand deposit as prescribed by Central Bank in each of the respective years. The actual amount in the reserve accounts are reproduced for the purpose of comparison

Table 3.1 Reserve Account Balances

Financial year ended March	Total Demand Deposit	Specified Cash Ratio		Balance In The Reserve Account Amount	% Of DEMAND DEPOSIT
		Ratio	Amount		
1977	18,359,952	5%	917,545	687,115	4%
1978	26,253,363	5%	1,312,668	939,466	4
1979	20,683,090	5%	1,034,959	905,605	4
1980	31,086,826	3.5%	1,090,822	1,101,851	3.5
1981	40,514,235	3%	1,215,427	685,884	2
1982	27,500,928	2%	5,500,189	- . -	-
1983	27,673,437	2%	553,469	(1,692,551)	-
1984	25,637,505	2%	512,750	296,958	1.2%

It will be observed that the balances in the reserve account as at the end of each financial ended 31st March were below the stipulated cash ratio to total demand deposit. This could be attributed to two reasons. Firstly either at the end of the each of the financial year the Central Bank has not effected the necessary transfer of the appropriate amount from the current account commensurate with the increase in the total demand deposit or there were debit balances in the current account. At the end of each financial year from 1977 to 1979 the cash ratio was stipulated as 5% of the total demand deposit, the balances in the reserve account for each of the financial years were 4% of the total demand deposit. The specified cash ratio for 1980 and 1981 were 3.5% and 3% respectively.

The balance in the reserve account for the financial year ended March, 1980 agreed with the specified 3.5%, while that of 1981 was $2\frac{1}{2}\%$. The lack of harmony between balances in the reserve account as a percentage of the total demand deposit, and the specified cash ratio may be due to the time lag in the computation and transfer of the appropriateamounts to the reserve account by the Central Bank.

For the financial year 1982 and 1983, the reserve account showed a nill and debit balances respectively. This was because the balances in the current account of the Bank for each of these years were debit balances. The implication of this, will be elaborated further in the later sections. It is however important to emphasise that the transfer of the appropriate amount from the Banks current account to the reserve account is the responsibility of the Central Bank, the amount transfered depends on the total demand deposit and the specified cash ratio as contained in the Central Bank yearly financial monetary guidelines.

(ii) Liquidity Ratio

The liquidity ratio as prescribed by the Central Bank monetary guidelines as contained in the yearly circular to all Bank, as earlier mentioned, has been 25%. The table below will enable the computation of the liquidity ratio of the Bank for the purpose of comparison.

Table 3.2

CURRENT ASSETS

	1977	1978	1979
Cash balances held	241,279	197,122	505,907
Balances held with other Banks	393463	11,010,778	13,092,772
CBN Current account	193,520	10,404399	1,270,428
Other Banks in Nigeria	199,943	606,379	11,822,344
Banker unit fund	1330,000	2330,000	- -
Treasury Bills	12440,000	10,000000	- -
Treasury Certificates	1385,000	- -	- -
Bills discounted	-. -	-. -	-.-
Total Elligiable liquid assets	15789742	23537900	13600,679

	1980	1981	1982
Cash balances held	916,200	840,147	1,506,185
Balances held with other Banks	23,540885	20,837310	(2,300,136)
CBN Current account	4,459261	44,44968	(7,232,057)
Other Banks in Nigeria	19,081624	15,892342	4,931,921
Banker unit fund	- . -	- . -	- . -
Treasury Bills	- . -	- . -	- . -
Treasury Certificates	- . -	- . -	- . -
Bills discounted	- . -	500,000	- . -
Total Elligiable Liquid assets	24,457085	22,227457	6,438,106

	1983	1984
Cash balances held	1,142,922	1,136,815
Balances held with other Bank	(2,880,908)	(8,388,188)
CBN Current account	(3,771,432)	(9,766,466)
Other Banks in Nigeria	890,529	1,378,278
Banker unit fund	- . -	- . -
Treasury Bills	6 . -	- . -
Treasury Certificates	- . -	- . -
Bills discounted		
Total Elligiable liquid assets	2,033,446	2,515,093

The purpose of the table below is to arrive at the total eligible liquid assets for each of the financial year ended. It is important to note that the period between 1982 and 1984 exhibited certain perculiarities particularly with respect to "Balances held with other Banks" which all showed debit balances. These balances were arrived at as analysed below.

Table 3.3 Analysis Of Balances due from/ To Other Banks

	1982		1983	
Bals. due from from other Bnaks				
CBN Curr. Acct.	2,055,208		5,723,793	
Banks in Nigeria	4,957,239	7,012447	929,976	6,653,769
Bals. due to other Banks				
CBN Curr.Acct.	8,008,912		7,802,674	
Cash Reserve	1,278,353		1,692,551	
Banks in Nigeria	25,318	9312583	39,452	953,677
		(2,300136)		(2,880,908)

	1984		
Bals. due from from other Banks			
CBN Curr. Acct.	3,713,170		
Banks in Nigeria	1,408,300	5,121,478	
Balances due to other Banks			
CBN Current Account	13,479,636		
Cash Reserve	- . -		
Banks in Nigeria	30,030	13,509,666	
		(8,388,188)	

The above table shows the computation of the balances due from other Banks net Balances due to other Banks for the period 1982, 1983 and 1984. All these show debt balances an indication of net liability against the Bank.

Table 3.4

CURRENT LIABILITIES

	1977	1978	1979	1980
Current Account	4,030,788	10,997,395	13,605,764	18,310,068
Savings Account	371,756	832,571	959,082	1,399,535
Deposit Account	13,948,408	14,432,397	6,118,244	11,377,223
Short term	11,915,491			6,928,479
Fixed term	2,032,917			4,448,244
Balance due to other Banks				
CBN	- . -	- . -	- . -	- . -
Overseas	- . -	- . -	- . -	- . -
Total Current Liability	18,350,952	26,253,363	20,683,090	31,086,826
Total eligible liquid assets	15,789,742	23,537,900	13,600,679	24,457,085
Liquidity Ratio	86%	90%	66%	79%

	1981	1982	1983	1984
Current Account	19,114,760	11,381,662	10,744,598	15,709,486
Savings Account	2,054,332	2,415,598	2,837,903	3,404,279
Deposit Account	19,345,143	6,471,612	7,476,229	6,523,740
Short term	14,809,880	5,491,113	4,593,301	3,761,058
Fixed term	4,535,263	980,511	2,882,920	2,762,896
Balance due to other Banks				
CBN	- . -	7,232,057	3,771,432	9,766,466
Overseas	- . -	- . -	2,843,275	- . -
Total Current liability	40,514,235	27,500,928	27,673,437	25,637,505
Total eligible liquid assets	22,227,457	6,438,106	2,033,446	2,515,093
Liquidity Ratio	55%	23%	7%	10%

It can be observed that for the period between 1972 and 1981 excess liquidity was maintained. In 1972 and 1978 all forms of liquidity instruments featured, namely, Bankers Unit Fund, Treasury Bills, treasury certificates and balances due from other Banks.
In 1977 over ₦12 million out of the ₦15.8 million eligible liquid assests was in form of of treasury Bills, Bankers unit fund and treasry certificates took ₦1.3 million and ₦1.4 million respectively. The decision to maintain assets in form of highly liquid assets in 1977 could be attributed to the composition of the demand deposit. Almost ₦14 million out of the ₦18 million total demand deposits, almost 86%, was in form of shorterm deposits which could be highly volatile.In the year 1978 balances with Central Bank current acccunt took ₦10.4 million while treasury bills took ₦10 million out of the total ₦23.5 million eligible liquid assets, while Bankers unit fund took ₦2.3 million.
The ₦10.4 million balance in the Central Bank current account should have been invested in income earning assets instead of being left in the Central Bank current account. During this year, the decision to maintain assets in highly liquid form could as well be attributed to the composition of the demand deposit.

For this year out of the ₦26 million demand deposit ₦14 million was in form of deposit account balances, the shorterm deposit account taking considerable percentage of the total deposit account balances. It is important to mention that over 90% of the total deposit account balances for the years 1977 and 1978, and the following year comprised of government deposit accounts which in most caser were shorterm deposit. Such accounts could be highly volatile and so the decision to maintain highly liquid assets.

For the remaining period 1979 to 1984, except in 1981 when bills discounted amounting to ₦.5 million appeared the only liquidity instrument was balances due from other Banks. The percentage of this to the total eligible liquid assets for each of the period is shown below.

Table 3.5 Balances Due From Other Banks

Balances due from other Banks as a percentage of the total amount deposit.	1979	1980	1981	1982	1983	1984
	86%	79%	68%	76%	45%	56%

One may not see the justification for maintaining the liquid assets in just one form, when other higher yielding liquidity instruments were available.

The years 1982, 1983 and 1984 showed a low liquidity ratio 23%, 7% and 10% respectively. The poor liquidity position during this period could be attributed to insufficient investment in liquidity instruments, increase lending and decline in the total demand liabilities. The analysis below will clarify these points, with respect to the year 1982.

Table 3.6 Changes In Account Balances

Deposit Accounts

Year	Balance	Change
1981	19,345,143	
1982	6,471,612	12,873,531

Current Accounts

Year	Balance	Change
1981	19,114,760	
1982	11,381,662	7,733,098

Loan Account

Year	Balance	Change	
1981	20,021,090		
1982	25,262,993	5,241,903	25,848,532

The total decrease in deposit and the current account during 1982 added to the total increase in Loans amounted to ₦25,848,532. As at the end of 1981, the total eligible liquid assets stood as ₦22,227,457. The total decrease in deposit liability plus the increase in loans therefore was far in excess of the total liquid assets.

This resulted into the overdrawing of the Central Bank current account. The Central Bank currentaccount was overdrawn to the tune of ₦7,232,057, This, net balances held with other bamks left a totalliquidity 0f₦₦2,300,136.

In the year 1983 Loans increased by over ₦8 million, without any corresponding increase in deposit liabilities to back the increase. This placed greater pressure on the liquidity position bringing it dawn from 23% to 7%

The non significant increase in loans and the increase in current account and savinga account balances increased the liquidity position slightly during 1984 period from 7% to 10%, though deposit accounts balances decreased from 7.5 million to 6.5 million.

The poor liquidity position for the period between 1982 and 1984 was brought about by decrease in the total deposit in the form of the volatile deposit and current account balances and increase in Loans. The net change was far in excess of the total eligible liquid assets resulting into the overdrawing of Central Bank current account to meet the net application of fund.

3.2.2 Secondary Reserve

An observation at the secondary reserve requirement will reveal how important it is to invest in liquidity instruments. This decision should be based on the composition of the demand deposit which reveals the volatility of each item of the deposit. As pointed in the previous chapter lack of sufficient provisions to meet changes in cash demand will lead to a serious liquidity problem. The decision to lend should only be made after sufficient provision is made in form of liquidity instruments. The graph below will assist in identifying the need for such provision to meet changes in demand for cash.

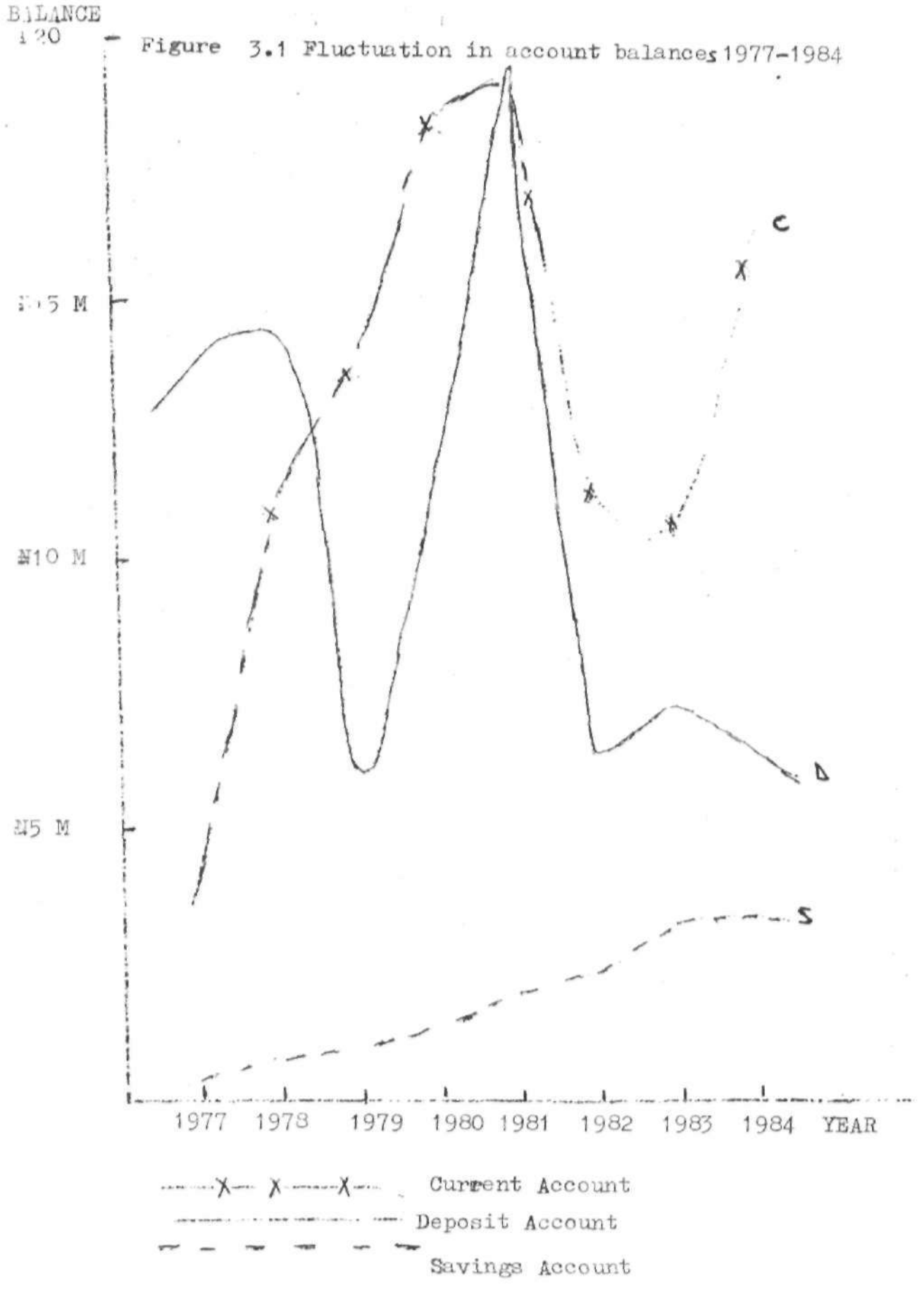


Figure 3.1 Fluctuation in account balances 1977-1984

To explore into the need for maintaining the secondary reserve requirement in form of liquidity instruments, it will be helpful to start by commenting on the individual accounts,

1) Savings Account

The savings account exhibited a fair rate of stable growth and hence the amount deposited in form of savings can be confortably invested in longterm assets such as loans.

11) Current Account

This exhibited a growth for the period from 1977 to 1980 and then a decline then it started to grow again in 1983. Current account is therefore more valatile than the savings account. But a prediction can be made as to the lowest level that the current account balances can fall. This can be made with some degree of accuracy and used as the basis of determining the amount that can be invested in the liquidity instruments to meet the fluctuation in demand from current account holders.

(iii) Deposit Account

Considerable percentage of the deposit accounts were held by the State and Local governments. Over the period between 1977 and 1984 between 70 and 90% of the deposit accounts were in form of shorterm deposit accounts. Government accounts by nature are highly volatile. This fact has been proved by the graph above.

From the graph above one can see that from 1977 to 1981 the liquidity instruments maintained were high, This could be for the fact that greater percentage of the total demand deposits were in the form of goevernment deposits which were highly volatile. This created a situation whereby eventhough the Bank had considerable amount of balances, this had to be maintained in safety assets other than risk assets that fetch higher income. The sharp decline in the deposit account balances in 1979 led to a sharp decline in the liquid assets, but not below the current account balances. The increase in the deposit account during the period 1979 to 1981 was matched by an increase in the liquid assets, this indicated the managements conciousness of the volatile nature of the deposit accounts.

However from 1981 when loans jumped to ₦19.5 million from 1980 level this started to drain the liquidity and so the absence of sufficient provisions for the volatale deposit accounts and to some extent the current accounts. The fall in the deposit account balances and current account balances resulted into the poor liquidity position, which became so low in 1983 and 1984. This was because the amount that should have been invested in liquidity instrument to meet the increase in demand went to finance loans and advances.

Therefore the Bank Management did not realise the implications of the volatile nature of the deposit and current accounts. This resulted into utilization of funds from these accounts into Loans instead of the liquidity instruments. The composition of the demand deposit and the increase in loans resulted into the liquidity problem of the period between 1981 and 1984.

3.2.3 Composition Of The Liquidity Instruments

Deciding the amount of assets to maintain in form of primary reserve is not the only important consideration but also the composition of such assets. The portfolio of the liquidity instruments is important with regard to obtaining higher returns from such portfolio.

In 1977 and 1978 the portfolio of the liquidity instruments was highly diversified. The remaining period between 1979 and 1984 consisted of only balances held with other Banks.

3.3 Loan Management

In determining the level of loans to be granted the factors to be considered include the Central Bank expansion ceiling , the existing level of loans and advances, the liquidity position of the Bank, and whether sufficient provisions have been made to meet the changes in cash demand. The lending policy should as well guide the amount of loans to be granted.

Where the total loans and advances of Bank does not exceed ₦100 million, expansion of the loans could be based on the total demand liabilities instead of the total loans granted. This is in accordance with the Central Bank monetary policy guidelines. Kano Co-operative Bank never exceeded the ₦100 million as such the various Central Bank monetary policy guidelines allowed the Bank to expand loan up to 70% of its deposit liabilities from 1977 to 1982 and up to 60% from 1983 to 1984. The table below shows the various levels of lending and the increases in the lending levels over the period in question.

Tablee 3.7

Loan Expansion

	1972	1978	1979	1980
Total Loans	2,143,646	4,440,842	9,641,940	9,646,940
Increase	- . -	2,247,196	2,695,495	2,510,603
% Increase	- . -	107%	61%	35%
% Of Loans to Deposit Liabilities	11%	17%	34%	31%
Max. Expansion	70%	70%	70%	70%

Table 3.6 (continued)

	1981	1982	1983	1984
Total Loans	19,500,362	24,267,823	31,624,159	30,184,713
Increase	9,853,422	4,767,461	7,361,336	- . -
% Increase	102%	24%	30%	- . -
% Of Loans to Deposit Liabilities	48%	88%	114%	118%
Max. Expansion	70%	70%	60%	60%

The loans and advances expanded 10% and 102% in 1978 and 1981 respectively. It was above the 70% expansion limit set by the Central Bank, in 1978.

During its early years of operation, the lending levels of the Bank in comparison to its total deosit liabilities were low. In 1977 the total deposit liabilities was ₦18.4 million, the total lending was ₦2.1 million whi while the loan stood as ₦4.4 million. The reluctance to use a greater percentage of the total deposit liabilities for loans could be for obvious reasons. This period being the early period of its existence and the fact that government shorterm deposit constituted a greater percentage of the deposit liabilities.

Such deposits were highly unstable and so no considerable amount of confidence existed to utilize such deposits towards granting loans. Out of the total deposit liabilities of 18.4 million in 1977, ₦11.9 million was in shorterm deposits, while in 1978 out of the ₦26.3 million deposit liabilities ₦14.4 was in form of shorterm deposit.

The loans and advances as a percentage of the deposit liabilities continued to remain low up to 1980 when it was 31% of the total deposit liabilities. All this could be associated with the composition of the deposit liabilities. When loans jumped from ₦9.6 million in 1980 to ₦19.5 million in 1981, this coupled with the subsequent increases in loans resulted into the liquidity crisis in the later yaers. A clear indication of the implication of volatile accounts as it affects credit expansion. In 1981 while the total loans stood as ₦19.5 million, the total deposit liabilities stood as ₦40.5 million. This one would expect tob be a confortable position, because the total loan was only 48% of the total deposit liabilities while the total liquid assets were 49% of the total deposit liabilities. In this same year however the total balance in the deposit account was ₦19.3 million which was over 47% of the total deposit liabilities.

In the year 1981 one would expect that the level of loan in relation to the total deposit liabilities as reasonable enough. This was because loans were only 48% of the total deposit liabilities. But the composition of the deposit liabilities created the subsequent liquidity problem. When the balance in the deposit account dropped from ₦19.3 million to ₦6.5 million in 1982, a 66% drop. The current account balances also dropped from ₦19.1 million to ₦11.4 million in 1982, a 40% drop. The overall total of the deposit liabilities dropped from from ₦40.5 million to 27.5 million, a ₦33% drop. The total decrease in the deposit liabilities as a result of the drastic decrease in the deposit accounts which consituted a greater percentage of the total deposit liabilities coupled with the decrease in the current account balances resulted into the total liquidity position of the Bank falling from ₦22.2 million in 1981 to ₦6.4 million in 1982. This was very serious position in termsof liquidity. This clearly shows how loan expansion without due consideration been given to the composition of the total deposit liabilities could lead to a serious liquidity problem.

With the level of liquidity at ₦6.4 million in 1982, loans expanded from ₦24.2 million in 1982 to ₦31.6 million in 1983.

The total deposit liabilities did not increase sufficiently to improve the liquidity position, there was only a slight change from ₦27.5 level in 1982 to ₦27.7 million in 1983. This resulted into further deterioration in the liquidity position. From the ₦6.4 million level in 1982 to ₦2 million in 1983.

In 1984 loan expansion was halted and the level brought dawn to ₦30.2 million the increase in deposit was not significant enough as such the liquidity position did not improve much , the increase was only by about ₦.5 million, from the ₦2 million level of 1983.

The lending trends without due consideration as to the composition of the deposit liabilities, and the absence of sufficient provision to meet the likely increases in cash demand resulted into the liquidity problem that started in 1982. This created a situation whereby the Bank had to overdraw its current account with the Central Bank to meet the demand for cash. The current account was overdrawn to the tune of ₦7.2 million, ₦3.8 million and ₦9.8 million in 1982,1983, and 1984 respectively.

The above analysis would show the extent to which the absence of concious management efforts existed with regards to loan management.

With regards to organization for loan granting and controls an investigation revealled that the procedures for collecting and processing of loan applications existed in the form of Branch manual instructions. Here the various steps to be taken on receipt of applications were stipulated up to the point when application in excess of the amount that branch manager could approved were to be sent to head office. The problem associated with organization for lending will be considered in the next chapter, under problem identification.

This chapter has analysed the case of Kano Copperative from the viewpoint of managing the portfolio of assets. The liquidity and the loan management aspects were considered and the problems associated with each identified. It was discovered that during the later period under review in sufficient provisions were made with regards to meeting liquidity needs. Loans expanded during the same period without due consideration given to the liquidity position. These and other problems will be enumerated in more details in the next chapter.

CHAPTER iV

Problems And Prospects Of Kano Co-operative Bank

The poor performance of Kano Cooperative Bank is a symptom of problems pertaining to the management of the Bank. Based on the analysis in the previous chapter, this chapter aims at enumerating the problems confronting the Bank. It is believed that once such problems are elliminated the Bank will have alot of prospects. This chapter will also identify some of the prospects that will open to the Bank through solving the existing problems.
The problems identification is divided into three, namely liquidity and loan management aspects and other management problems.

4.1 Liquidity Management Problem

The liquidity management aspect centres on ensuring that sufficient provisions are made in form of primary and secondary reserves to meet the legal requirements from the point of view of the customers and the Central Bank regulations. This aspect is concerned notonly with the total amount of liquidity maintined butalso with the nature and type of liquid assets held.
Primary reserve is the most liquid form of asset maintained, in form of cash, to meet the daily cash requirements.

Cash holding does not earn profit as such holding excess cash should be avoided. Once sufficient primary reserve is maintained excess cash should be diverted into earning assets. This however should be done with the view to the need for meeting forecastable demand for cash. The second priority therefore is to hold protective reserve known as secondary reserve.

This is made up of assets that are termed as liquidity instruments, assets thatcan easily be converted to cash to meet foreseable and unforseable cash demand, without making any loss on the principal invested. The nature and types of liquidity instruments to maintain should be based on the composition and hence the volatility of the deposit liabilities. So that liquidity instrument are held such that their maturity coincide with the period of cash demand, or they can easily be cashed to meet such demands without loss. Management of liquidity is not an easy task ; but the above concepts can show how obvious it is. The entire banking operation depends on how well sufficient provisions forliquidity needs are made. Investments, lending and any other form of banking operation have bases on sufficient provisions for liquidity needs.

Based on the analysis in chapter three it was discovered that Kano Cooperative Bank during the period under review, entered into liquidity crisis. The reasons for this are as follows:

4.1.1 Insufficient Provisions For Liquidity Needs

In making provisions for liquidity needs, the factors to consider include not only the total deposit liabilties, but also the composition and so the volatility of the deposit liabiltis. The case of Kano Cooperative between 1977 and 1981 was such that considerable percentage of the total deposit liabilities consisted of shorterm government deposit accounts. Such accounts are by nature highly unstable. As such in providing for liquidity requirements the amount to be held should be considerable enough to meet the volatility of such accounts. The current account deposits also constituted a greater percentage of the total deposit liabilities. Current account balances were also discovered to be unstable. The figures below show the various percentages of the current and deposit account balances in relation to the total deposit liabilities.

Table 4.1 Percentage Of Current and Deposit Accounts To The Total Deposit Liabilities

	1977	1978	1979	1980	1981
Percentage of total deposits					
Current Account	22	42	66	58	47
Deposit Account	77	53	30	35	47

Considering the degree of volatility of these accounts, a drastic fall in one or both of the accounts will certainly place considerable amount of presure on the liquidity position of the Bank. One would expect the total liquidity position, at any point in time, to be sufficient enough to meet the possible changes.

In the previous chapter it was shown that from 1977 to 1980, sufficient liquid assets were held to meet any likely increase in demand for cash. But from the 1981 financial year the liquidity position was poor as a result of, among other things, loan expansion. As at the end of 1981 financial year the total deposit liabilities was over ₦40 million while the total liquid assets stood as just over ₦22 million. The liquidity ratio at this time was 55%. One would expect this to be a favourable condition. But considering the composition of the total deposit liabilities, out of the ₦40 million, current and deposit accounts balances took a total of over ₦38 million, each taking just above ₦19 million. The situation was such that only ₦22 million was covering the volatile ₦38 million. The implications of the volatility of these accounts were shown when their balances fell in the preceeding periods.

The current balances fell from ₦19 million balances in 1981, to ₦11 million in 1982, while of deposit account fell from ₦19 million to ₦6 million. This resulted into the total liquidity position as at the end of 1982 financial year falling to just over ₦27 million. This was a serious position from the point of view of liquidity. It is important to point out that, one would not expect the current and deposit account balancess to fall so drastically. The factors that led to this were, the economic conditions which might have affected the current accounts, and the fact that greater percentage of the total deposit account consisted of the volatile shorterm government accounts. These conditions were seen to be ignored by the management in making provisions for liquidity needs.

As a result of the presure on the liquidity position, the account of the Bank with Central Bank had to be overdrawn to the tune of ₦7 million in 1982 to meet the cash withdrawals. In 1983 and 1984 the account was overdrawn to the tunes of ₦3.8 million and ₦9.7 million respectively. In the absence of such facility extended by the Central Bank the bank could have become insolvant which could lead to bankruptcy.

The overdrawing of the Central Bank account, going by the banking act, attracted certain penalties in form of fines and interest charges. This placed yet another pressure on the liquidity position of the Bank. The liquidity position during the period under review remained so low. In 1983 and 1984 there were no improvements. The total liquidity in 1983 and 1984 was ₦2 million and ₦2.5 million respectively.

Therefore insufficient consideration with regards to the composition of the total deposit liabilities, in making provisions for liquidity need leads to liquidity crisis, eventhough the total liquid assets may appear to be sufficient to cover the total deposit liabilities. The insuffcient provision for liquidity needs was one of the causes of poor operations in Kano Co-operative, a sign of poor liquidity management.

4.1.2 Overlending Without Sufficient Provision For Liquidity Needs

The amount of total loans to be granted should be considered only after sufficient provision is made in form of cash and liquidity instruments to meet the likely demand for cash. As at the end of 1980 financial year the total liquid assets stood as just over ₦24 million against the deposit liabilities of around ₦31 million.

This was a favourable position from the point of view of liquidity and sufficient room existed to acquire more earning assets in form of liquidity instruments and loans. During 1981 Loans expanded from ₦10 million level at the end of 1980 to ₦20 million. During the same period the totalliquid assets fell from ₦24 million to ₦22 million. The total deposit liabilities at the end of 1981 was ₦41 million. The liquidity position therefore was 55%. With this condition one would not expect loans to expand drastically during the subsequent periods. Loansunder this condition should only increase when more deposit were attracted by the bank or repayment from existing laons were secured. Contrary to this loans expanded to ₦25 million and ₦33 million in 1982 and 1983 respectively. The loan expansion and the fall in the deposit liabilities resulted into the liquidity position falling to ₦6 million in 1982 and ₦2 million in 1983. The total deposit liabilities for 1982 and 1983 were ₦27.5 million and 27.7 million respectivelys so that the liquidity ratios were 23% for 1982 and only 7% for 1983. During the year 1984 Loan expansion was halted for obvious reasons of poor liquidity position.

Insufficient provision to meet the likely cash demand coupled with the rapid expansion of credit led to the serious liquidity crisis. Creating a situation whereby as at the end of 1984 financial year only ₦2.5 million liquid assets covered ₦25 million deposit liabilities, a serious position. It violated the Central Bank monetary policy guidelines which specifies 25% liquidity ratio. If not because of the opportunity given to the bank to overdraw its account with Central Bank during 1982, 1983 and 1984, to the tune of ₦7 million, ₦3.8 million, and ₦9.8 million respectively, the Bank could not have survived the liquidity crisis.

4.1.3 Volatility Of Government Account

The Bank being wholly owned by the State goverment should receive greater attention and patronage from the state and local governments. This is to enable the purpose for which the Bank was established to be met. Most of the accounts maintained by the state and local governments fluctuate considerably. This create considerable amount of constraits on the part of the management in deciding how to make good use of such volatile accounts. Some accounts maintained by the government in form of current accounts, shorterm and fixed term deposit accounts one would expect them to be stable.

Under such assumption the management may decide to utilize such balances, based on the confidence on their stability to acquire earning seeassets such as loans. Heavy withdrawals from such accounts by the government as the case during 1982 would certainly have serious impact on the Bank. Government being the major holder of the total deposit liability of the bank creates a great constrait by not maintaining longer term deposits.

4.1.4 Poor Capital Base

The business of banking is such that success does not depend on the total capital employed. The total capital employed compared to the total amount dealt in is usually small. Success depends on how much deposit the Bank is able to attract and manage. Eventhough this statement might be the fact concerning banking, sound capital base is certainly important in banking, just like any other business concern.

The amount of capital emlpoyed should be sufficient enough to be used in acquiring fixed assets and other forms of assets need for its operations.

As at the end of the 1984 financial year the total paid up capital of the Bank was only ₦3.9 million, eventhough the authorized capital was increased to ₦10 million. With poor capital base the Bank's ability to acquire fixed assets has been limited. This created a situation whereby the head office and the main branch in Kano are in rented acommodation, and also the two new branches opened at Maigatari and Karaye towns. With insufficient capital base and the losses recorded over the years, this resulted into pressure placed on the deposit secured.

The need to acquire fixed assets and losses incurred over the years place great pressure on the deposit liabilities, contributing greatly to the liquidity problem. The problem of liquidity is compounded if one considers the fact that the rent being paid on the acommodations for both the Bank and its staff. Sufficient capital could have enable the Bank to avoid renting and also the losses incurred cculd have been absorbed by the capital.

4.2 Loan Management Problem

After sufficient provisions for liquidity needs are made any excess funds should be directed towards lending. Regarded as the most risky form of assets maintained by a Bank. But the main business of banking is lending. For the loan management aspect of bank to be successful there should be clearly formulated policy and procedure regarding lending, lending should be under a sound organizational setup, and the lending activity should be well coordinated and controlled. The following problems were found to exist in Kano cooperative in the area of lending.

4.2.1 Absence Of clear Lending policy

Any particular Bank should have a clear policy regarding lending, Policy should specify the areas that the Bank wishes to extend credit, policy regarding size, Security to be obtained and repayment terms should as well be spelt out. Such policies should be clearly understood and strictly adhered to. The policies should aimed at achieving the organizational objectives.

The Central Bank of Nigeria through the annual monetary policy guidelines specifies the expansion cieling and sectorial allocation of loans. This not withstanding, the individual Banks have some degree of freedom in deciding the area to extent credit facilties and so the need to have policies regarding loans.

Kano Co-operative Bank was established to satisfy the loan requirements of cooperative Societies and its members, but the Bank was given a full licence to operate as a commercial Bank. Eventhough this has been the case there is need to define the specific areas, as a matter of policy, that the Bank wishes to satisfy from the point of view of meeting loan requirements.

As at now no policy regarding the area that the Bank wishes to extent credit facilities exists.The Bank eventhough constrained by its size attempts to satisfy sectors that it cannot fully finance. In some cases the financing of certain sectors was carried only to certain points from where the Bank could not proceed further. This resulted into most of the customers seeking for further assistance from other Banks.

Another area that calls for policy formulation is the size of loans to be granted. Some loans were discovered to be far in excess of what the Bank could confortably acommodate. There were certain loans that exceeded the one-third of the paid-up capital, this violated the normal banking priciples of risk aversion, and the section 13 (i) a of the Banking degree 1969. If policy regarding size of lending existed this risky situation could been avoided.

The terms of loan specifying the securities needed for each particular type of loan and the terms of repayment need policy formulation. The absence of policy in this area created a situation where considerable percentage of the loans were not secured, where the securities were obtained one discovers that considerable percentage of the securities have not beenperfected. So that in most of the default cases the Bank had no alternative than to declare such loans as bad and doubtfull.

Repayment period of all catergories of loans should be specified and strictly adhered to as a matter of policy. No policy regarding repayments exists. In some cases accounts that were found to have no reasonable repayment efforts were extended additional credit facilities.

4.2.2 Lending Procedures Not Adhered To

The procedures regarding lending in Kano Co-opearative Bank have been spelt out in the branch accounting manual. But it was discovered that those procedures have not been adhered to and most of the staff concerned with the handling of loan applications were not conversant with the procedures spelt out.

4.2.3 Outside Influence

Closely linked to the above problem is the effect of outside influence. It was discovered that most loans were approved as a result of the outside influence, through the members of the Board of Directors. The outside influence is particularly eminant during the political period, 1979 to 1983. The organization for lending was such that the Board of Directors have the responsibility of approving loans of certain amounts. The composition of the Board was such that the members do not know what banking practice entails. Approvals were based on certain considerations other than the prudence that banking practice required.

4.2.4 Poor Organization For Lending

Under normal cicumstances the approval of certain loans should be done by a management committee. The committee should base the approvals on policies and viability of extending such loans. In Kano Co-operative most loans were approved by individuals at the branch or head office. This was done independantly with little or co-ordination. This was as a result of lack of adherance to the procedures. From the point of view of approvals at the branch level, it was discovered that officers approve loans far in excess of their limits of authority. The headoffice approvals were in most cases done without clear understanding of the actual position of the accounts to accertain their conducts.

The absence of co-ordination resulted into granting of loans that later turnout to be bad doubfull.

4.2.4 Absence of Control

Based on the liquidity position and other considerations the management should specify the level of loan expansion during a particular period, this is based on control purposes. Besides setting the credit ceiling the management should ensure the monitaring of loan approvals by the branches and the repayments of the existing loans. The absence of control resulted into most branches approving loans far in excess of their limits of authority. Repayments also were not forth coming in many accounts and issues were not raised in most cases. A situation was created whereby most loan accounts went out of control.

4.3 Other Management Problems

The success of banking operation depends on how well organized the business is, depends on the quality of staff and how well co-ordinated and controlled their activities are.

Sound organization ensures the spelling out of duties and the relationship of the various units. Authority and responsibilities of the various units need to be spelt out. There is need for all the members of the organization to understand the responsibilities and authority of each unit in the organization.

The set-up in Kano Co-operative Bank is such that at the head office level one finds the following departments, namely, Administration/inspection department, operations department, accounts department,advances department, premises department, and secretarys department.

The adminstration/inspection department handles routine and special inspection and reports to the General Manager. This department is headed by the assistant general manager administration who is also the chief inspector. Eventhough the department has been formed as adminstration/inspection department all it does is routine and special inspection and reports the findings to the General Manager. This department also takes charge of the premises department.

Operations department headed by assistant manager handles loan applications and the advances department is under this department.

The accounts department maintains the consoldated accounts of the Bank and takes charge of the general expenses of the Bank.

The Secretary/ legal advisers department handles personnel and legal matters.

Eventhough an attempt has been made to identify the functions of the various department, in practice the functions of the various departments duplicate in most cases, this has been as a result of absence of clearly stated schedule of responsibilities. This has resulted into alot of conflicts in the discharge of the day to day affairs of the Bank.

As a result of the absence of clear organizational setup at the head office level, the activities of the various branches are not well coordinated and controlled.

In the area of staffing, it was discovered that it is only at the head office level that well qualified professionals exist. At the various branhces only few competant officers exist. The survey revealled that even those that are qualified and those with potentials are poorly motivated. This can be linked to the poor setup at the head office level. The sporadic training provided is not sufficient enough to bridge the gap between the job requirements and the level of competance of most of the staff.

4.4 Prospects of Kano Co-operative Bank

One cannot doubt the fact that there exist a lot of prospects that Kano Co-operative can exploit. To exploit the prospects the problems enumerated above must be eliminated. For one thing, Kano City is a commercial Centre, and the entire state is an agrarian state. With improved services the Bank can attract considerable amount of deposits from the business community around. In fact the existence of prospects is clear if one considers the performance of some recently opened Banks.

Through agricultural loan financing a lot of prospects can be exploited, if one considers the current trends of going back to the land. Financing of small scale industries within the state can greatly contibute towards boasting the Banks image. This will enable the Bank and such industries grow together.

4.5 Conclusion

This chapter has attempted to identify some of the problems confronting Kano Co-operative Bank. Solving such problems will open a lot of prospects to the Bank. The recommendations as to how to go about solving such problems will be outlined in the next chapter.

CHAPTER V

SUMMARY AND RECOMMENDATIONS

5.1 Summary

A commercial Bank like any other form of business organization aims at profit maximization. However one unique characteristic of commercial banking is that the amount of capital in relation to the total sum dealt is usually small. With modest capital this calls for greater need for prudence in the management of banking operation. Banking unlike other forms of businesses cannot afford slackin its operations. Operations will have to be within certain profit and loss margin. The profitability of commercial banking depends on how well the acquired assets are employed into earning assets. Employing funds into earning assets contradicts the safety need to maintain assets in form of cash to meet customer demand for cash.

Management of Bank portfolio of assets involves ensuring safety on one hand and profitability on the other. The safety consideration in commercial Bank centres on the need to maintain sufficient liquid assets to meet cash demand and the Central Bank regulations.

Hence the priority that takes the first place in the commercial Bank management is holding sufficient primary reserve to meet obligations from the point of view of the customer and the Central Bank of Nigeria regulations which has legal implications.

Once primary reserve requirement has been met the safey of the Bank is not ensured through holding excess cash. The longterm safey depends on how well the excess cash is employed into earning assets. In employing excess cash into earning assets the first priority is to acquire assets that can easily be converted to cash to meet likely and forecastable demand fo cash. By doing this a protective reserve will be created that ensures safety on onehand and profitability on the other. The protective reserve or the secondary reserve consists of liquidity instruments whose maturity dates should coincide with the period when demand for cash is likely to occur. Alternatively such instruments should be such that they can easily be converted to cash to meet the likely changes in demand for cash.

Once the primary and secondary reserves have been created and they are sufficient enough to meet the likely changes in liquidity requirements, any excess should be directed to what can be termed as the business of banking, that is lending. Lending is the most profitable and at the same time the most risky aspect of banking. For this reason there is need for a well formulated lending policy amd procedure. The policy specifying the nature, size and conditions of loans to be granted. Lending should as well be under sound organizational setting, should be well co-ordinated and controlled.

The management of commercial Bank after meeting all the genuine loan demands should divert any excess fund into acquiring lomgterm investment instruments such as shares, bonds and debebtures. The Nigerian banking indutry is however prevented by the banking decree 1969, from investing in such instruments.

The management of commercial Bank portfolio therefore, is involved with deciding the amount and diversification of primary reserve, secondary reserve and loans to maintain. The success of the management depends on how well the choice is made.

In the case of Kano Co-operative the following problems were identified in the previous chapter:

Liquidity management problems

- Insufficient provisions for liquidity needs.
- Loan expansion without sufficient provisions for liquidity.
- Poor capital base.
- Valatility of government account

Loan management problem.

- Absence of clear lending policy
- Lending procedures not adhered to
- Poor organization for lending
- Absence of co-ordinated lending practice
- Absence of control
- Outside influence

Other management problems

- Poor organizational setup
- Poor Staffing

Solving these problems will open alot of prospects for the bank if one considers the position of Kano as a commercial centre and the total opportunities existing in the whole state. The following recommendations will help alot towards eliminating these problems.

5.2 Recommendations

5.2.1 Intensify Recovery to Improve Liquidity position

As at the end of 1984 financial year the total loans stood as ₦33,506,779, and the total deposit liabilities as ₦25,637,505 with the total liquid assets of only ₦2,515,093. This was a serious positionregarding liquidity. With loans constituting greater percentage of the assets held and the poor liquidity position there is need to reverse this position through recovering the existing loans.

5.2.1 Attract More Deposit

The recovery efforts alone might not do much towards improving the liquidity position. The success of any Bank depends on how much deposits it is able to attract and manage. Efforts should be made to attract more deposits through improving the services of the Bank.

The government being the major shareholder should increase its depositsand patronize more with the Bank. Depositsby the government should be on longerterm basis to enable the Bank recover from the present crisis.

5.2.2 Overhead Reduction

The overhead over the years has been considerable. As at the end of 1984 financial year the total overhead was ₦2,584,539. Considering the size of the Bank this figure is too high. Overhead can be reduced by checking the amount of rent paid on the rented acommodation for the Bank and its staff. At the end of 1984 financial almost ₦2 million had been spend on the proposed staff quarters. This should be disposed and the proceeds used to acquire permanent acommodation for the Kano branch and the head office. This will reduced the rent payments.

The number of vehicles maintained by the Bank should also be reduced. At the end of 1984 financial the total value of the motor vehicles stood as ₦149,839. Maintaining such vehicles contributes greatly to the high overhead.

The staff strenght should also be checked to be reduced to a reasonable size.

5.2.3 Policy Formulation

A clear lending policy should be formulated. The policy should state the segment of the community that loan facilities are to be extended to. Policy regarding size, repayments, and control should be formulated.

5.2.4 Procedure.

The procedure regarding handling loan applications should be stricly adhered to. All staff handling loan applications should be well coversant with these procedures. A committee for appraising loan applications within certain amounts should be formed, which should consist of the management staff instead of the Board of directors.

5.2.5 Organization

Genrally the organizational setup of the bank needs be reviewed so that concerted management efforts can be made with regards to the management of the Banks affairs. A management committee should be formed to periodically appraise the position of the Bank to determine the amount of primary reserve, secondary reserve, and the loans to hold in the portfolio of assets with profitability and safety as the key consideration.

This will ensure a co-ordinated effort as opposed to the present situation where the management staff never meet to consider these factors.

A monitoring committee should be setup to monitor the activities of the branches from the point of view of loan granting and loan repayments. This is for control purposes. The monitoring committee should as well ensure the perfaction of all securities and should work hand in hand with the inspectorate department of the Bank.

5.3 Conclusion

Commercial bank, like other form of businesses exists to make profit. The profitability of commercial banking depends on how well the acquired assets are employed into earning assets. Employing assets to earn income in commercial banking contradicts the safety need to maintain assets in form of cash to meet the customer demand for cash. Management of Bank portfolio of assets involves ensuring safety on one hand and profitability on the other. The management of risk in banking is such that safety should always be given higher priority. For this reason the management of commercial Bank portfolio should give primary consideration to the need for meeting the legal obligations from the point of view of the customer and the Central Bank. This calls for maitaining primary reserve in form of highly liquid assets. Once the primary reserve requirement has been met which does not earn income, any excess money maintained does not amount to prudence. The excess money should be used to acquire earning assets, with priority given to the need for meeting likely and forecastable demand for cash. Hence the acquisition of liquidity instruments with maturity dates coinciding with the forecastable dates whendemands for cash are likely to occur.

Holding liquidity instruments is mainly for safety reasons, profitability is the secondary reason.

Once the primary reserve requirement and secondary reserve requirements are met, any excess cash should be used to acquire assets that are termed as risky form of commercial Bank assets. Lending is considered the main business of banking, but it should be made only after safe ground has been created through holding primary and secondary reserves. Lending should be on the basis of well formulated policy and procedure and should be under sound organizational setup. Where excess cash remains after meeting the viable loan demands, such excess should be diverted to acquire longterm assets such as shares and bonds. But the banking regulations in Nigeria does not allow the acquisition of such instruments by commercial Banks.

The management of commercial Bank portfolio therefore invloves deciding on the amount and diversification of the primary reserves and loans to maintain. The success of the management depends on how well the choice is made.

The case of Kano Co-operative Bank has shown that the management has not succeeded in identifying the amount and the degree of diversification of the various assets to hold. During the early period of its operation primary and secondary reserve requirements were met through acquiring the various forms of liquidity instruments with the view to providing safety and profitability. In subsequent years the only liquidity instrument found in the liquid assets component was "balances due from other Banks". This did notensure profitability. The safety need in the later years was not ensured. This was because the level of total liquid assets in relation to the total deposit liabilities remained considerably low. This low level of liquid assets was maintained in the face of volatile government accounts that constituted a greater percentage of the total deposit liabilities.

From the point of view of loans it was discovered that inspite of the low level of total liquid assets in relation to the total deposit liabilities, loans continued to increase by considerable amounts over the years. This further incresed the poor liquidity position. To the extent that the Bank had to overdraw its account with Central Bank to meet the withdrawals from the current and deposit accounts, whose balances declined considerably during the period under consideration.

The management of commercial Bank portfolio ensures safety and profitability. It involves determining the primary reserve, secondary reserve and the loan's level to maintain. The absence of this concious management effort in Kano Co-operative resulted into the lossess incurred during the period under review, and the poor liquidity position, which if not because of the bumper provided by Central by allowing the Bank to overdraw its account could certainly have resulted into the bank been declared bankrupt.

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