EVALUATION OF METHODS FOR REGULATING THE BEHAV1OUR OF COMMERCIAL BANKS IN NIGERIA

BY

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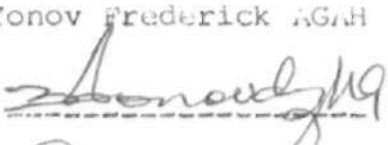
DEDICATION

This Thesis is dedicated to the memory of my mother, Mrs. Mbase Gbashaikwe Agah, and father, Mr. Gbashaikwe Agah.

DECLARATION

I hereby declare that this thesis is a product of my own research work and that it has not been accepted in any previous application for a higher degree. All sources of information in this study, have been specifically acknowledged by means of reference.

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SIGNATURE: 

DATE: 13th Sept, 1984

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This study has drawn greatly on the two recent publications on the Nigerian financial system by G.O. Nwankwo (1980), and P.N.C. Okigbo (1981), in attempt to capture the realities of the banking system in particular and the Nigerian economy in general.

I am particularly indebted to my first supervisor, the late Dr. A.O. Nwani, who not only encouraged me and gave me the desired direction in the course of this study but also made useful suggestions at the initial stages of the study. I sincerely pray that almight God grants his bereaved family the fortitude to bear the irreparable loss. I am also highly indebted to my present supervisor, Dr. U.I. Ezenwe,both for his willingness to take over the supervision and his guidance and understanding throughout the period of the study. His advice and suggestions on how to improve the quality of the thesis were particularly useful. I am therefore most grateful for the invaluable contributions of these two people.

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Needless to add that I am solely responsible for all errors and omissions contained in it.

September, 1984. Y. F. Agah

ABSTRACT

Commercial banks as financial institutions, can and do contribute to economic growth and development Their effectiveness in performing this role however depends as to whether their operations and policies are in line with the demand-following approach or supply-leading approach to the development of financial institutions- This study is based on the theory that commercial banks while operating as profit maximizing institutions, do possess behaviour patterns on which the monetary authorities must act in order to ensure that the desired objectives of the economy are achieved.

In Nigeria, the demand-following approach was adopted during the colonial period, but since independence, policy emphasis has shifted to supply-leading finance. This notwithstanding, the features of the banking system which emanated from the demand-following development still persist today among several other unsavourly effectso

Based on the objectives of the economy ana the specific goals of the policy instruments, the regulatory methods deployed by the Central Bank have not been able to achieve their ultimate targets Indeed, the Bank has been saddled with regulatory tools which are in principle unapplicabla for the. purpose of stabilzing the economy. While it has experimented with some, it is yet to apply others. The structural circumstances of the economy have further rendered some, if not all, the ultimate objectives of policy unachievable.

TABLE OF CONTENTS

	PAGE
DEDICATION	ii
DECLARATION	iii
ACKNOWLEDGEMENT	iv
ABSTRACT	vi
LIST OF FIGURES	viii
LIST OF TABLES	ix
CHAPTER ONE: INTRODUCTION	1
1.1 The Role of Money and Financial Institutions in the Economic Development of Nigeria	1
1.2 Objectives of the Study	6
1.3 The Outline and Scope of Study	8
CHAPTER TWO: COMMERCIAL BANKING	13
2.1 Review of Related Literature	13
2.2 Commercial Banking in Nigeria	20
2.3 The Structure of the Commercial Banking System	23
2.4 Operations and Policies of Commercial Banks in Nigeria	32
2.5 Banking Services	47
CHAPTER THREE: THE CENTRAL BANK OF NIGERIA	54
3.1 Organization of the CBN	58
3.2 The Relationship Between CBN and the Commercial Banks	61
3.3 CBN Relationship with Government	63
3.4 The Regulation of the Commercial Banks	68

PAGE

CHAPTER FOUR: EVALUATION OF METHODS FOR REGULATING COMMERCIAL BANKS 78

4.1 Objectives of Central Bank Policy 78

4.2 Evaluation of Methods Taken to Achieve Objectives 82

4.3 Appraisal of Policies 120

CHAPTER FIVE: SUMMARY AND CONCLUSIONS 141

5.1 Summary 141

5.2 Recommendations 146

5.3 Conclusions 150

SELECTED BIBLIOGRAPHY... 151

LIST OF FIGURES

I. Organization Structure of the Central Bank of Nigeria 59

LIST OF TABLES

TABLE NUMBER	TITLE OF TABLE	PAGE
2.1	Commercial Bank's Registered in Nigeria up to 1980.	21
2.2	Statewise Distribution of Commercial Bank Offices as at September 1980	25
2.3	Capital Ratios for Nigerian Commercial Bank's 1969-1980	35
2.4	Liquidity Ratios for Nigerian Commercial Bank's 1969-78	39
2.5	Sectoral Distribution of loans and Advances.	45
2.6	Sectoral Distribution of Loans and Advances (percentage) 1969-79	45
2.7	Pre-tax Profits Total Deposits and Shareholders' Funding for Selected Commercial Banks in Nigeria.	50
4.1	Interest Rate Structure, 1 April 1975.	94
4.2	Interest Rate Structure, 1 April 1977.	94
4.3	Interest Rate Structure, 1980	95
4.4	Changes in Minimum Cash Requirement for Nigerian Commercial Banks.	102
4.5	Commercial Bank Loans and Advances classified by purpose (Percentage Distribution) 1972-75.	112
4.6	Commercial Bank Loans and Advances Classified by Purpose (Percentage Distribution), 1976-81.	143
4.7	All Cities Quarterly Consumer Price Index, 1970-77.	123
4.8	Rural Banking Programme, Allocation of Identified Centres.	125

CHAPTER I

INTRODUCTION

1.1 The Role of Money and Financial Institution in the Economic Development of Nigeria.

Money and financial institutions are generally known to play important roles in the growth and development of any economy. There is therefore great need for them to be closely regulated and controlled in a manner capable of achieving a given set of objectives for the economy. It is in fact on this principle that this study is based.

Economists have expressed a wide variety of views and opinions on the role of financial institutions in promoting and facilitating economic growth and development. This controversy arises on the one hand from whether the development of financial institutions is necessary for economic growth and development particularly for developing countries including Nigeria. On the other hand, the controversy is as to which approach in the development of financial institutions would bring about a more effective financial system in general and banking system in particular.

The contention that financial institutions can and do contribute to the development of an economy is widely held[1]. Its proponents argue that, "economic theory and economic theory both assure us that the existence and development of a superstructure of financial institutions and financial instruments is a necessary, though not a sufficient condition of economic development"[2]. They all therefore attribute a positive effect to financial institutions in the development process. This accord notwithstanding, they differ greatly as regards the relative magnitudes of impact attributed to banks and other financial institutions in developing economies like Nigeria.

The other side of the argument is closely associated with John G. Gurley[3] who expresses skepticism about the emphasis and prominence attached to financial development as separate from other institutional choices a country makes to advance growth. It is worth mentioning here that he does not however doubt or question the effectiveness of the development of financial institutions as such. Rather, he insists on the existence of alternative techniques that may also prove feasible in a country's development effort.

The second and, infact, the central issue in the controversy over the role of financial institutions in economic development is whether the development of financial institutions precedes and therefore plays an important role in economic development, or whether it passively adjusts to the growth of the economy. These two views form the major approaches to the development of financial institutions. If the development of financial institutions passively adjusts to the growth of the economy then we have the "demand-following" approach. On the other hand, if financial institutions precede and therefore play an important role in economic growth and development, we have the case of the "supply-following" approach.

The demand-following approach to the development of financial institutions is a situation whereby, "as the economy grows, it generates additional demand for financial services which bring about a supply response in the growth of the financial system"[4]. A major feature of this demand following approach is that its contribution to economic development is minimal and may even be an obstacle

to economic development. In addition, bank operations in this approach are characterized by caution and lack of innovation, specializing in short-term commercial loans. The demand-following approach therefore "explains the lack of financial institutions in most developing countries simply as an indication of the lack of demand for their services" which "implies that finance is essentially passive and permissive in the growth process"[5].

The supply-leading approach on the other hand is a situation whereby financial institutions are created before demand for their assets and liabilities becomes evident; thus acting as a leading sector. They therefore play a more active role in the industrialization and over-all economic development of the areas in which they operate. This is possible because "supply-leading finance transfers resources from the traditional non-growth producing sectors to the modern sectors of an economy with higher growth potential. Such a transfer of resources may be achieved by collecting the savings via new bank credits"[6]. The supply-leading approach is also able to induce growth because of its ability to promote entrepreneurship.

Therefore, in this approach, "financial institutions and the supply of their financial assets, liabilities, and related financial services are created in advance of demand for them by the entrepreneurs in the modern growth inducing sectors. It has two functions, to transfer resources from non-growth sectors to modern sectors and to promote and stimulate an entrepreneurial response in these modern sectors"[7]. It stimulates and develops this entrepreneurial

response (where it does not exist) by extending non-financial services to economic units; and may even participate in the promotion and control of industrial as well as other types of enterprises.

It is pertinent to observe here that the supply-leading approach to the development of financial institutions is more applicable to the circumstances of Nigeria in particular and developing countries in general. This is because when economies develop and mature up to a certain stage, they tend to depend less on financial institutions for finance and entrepreneurship. In addition to this, innovation finance removes other major obstacles to economic development that are absent in mature economies[8]. It would seem plausible therefore to say that the supply-leading approach is more applicable in the early stages of economic growth and development, a situation in which Nigeria presently finds herself.

> The demand-following approach was utilized in the development of financial institutions in Nigeria during the British colonial period. This contributed to the development of an enclave economy. Since independence, and with the use of the supply-leading approach, more dynamic monetary and financial institutions have been established for the purpose of aiding economic growth and development in a meaningful form[9].

A note must however be made of the fact that the "mere existence" of a financial arrangement which is an important prerequisite for influencing the mobilization and allocation

of capital; and in changing savings into productive investment to stimulate the development process in Nigeria "does not guarantee" the achievement of economic growth and development in a meaningful form.

To begin with, the way in which financial institutions perform these functions in the growth and development of the Nigerian economy will greatly determine not only their contribution but also the success of the development effort. In addition, whether or not they make a positive and substantial contribution to economic development will depend primarily on the structural characteristics of the system, and the law, regulations and the customs that govern their effectiveness.

The structural characteristics of the financial system may be regarded as the "essemble of ratios and relationships, quantitative and other, that characterize the components of the system and tie it into the economy of which it is a part"[10]. Such relationships in the Nigerian case may include: density, measured either as a ratio of the number of bank or non-bank offices to the entire population or to area; size of the financial institutions within the system; geographical concentration or dispersion of bank and non-bank institutions.

The financial structure may also be determined by the strenght and character of the demand for financial services, and the attitude of official policy of the government towards the system. Being an integral part of the economy, if there is no demand for its services, the financial system will naturally not exist. However, "granted that it does exist,

its structure will be shaped very largely by the actions of the political authorities in the form of laws, decrees, regulations and by more direct participation such as government ownership"[11].

It is against this background and belief of what a well managed and virile financial system can contribute to the economic growth and development of Nigeria given the right stimulus and direction that the Central Bank of Nigeria was established in 1958. The Bank was charged with the responsibility of developing an effective institutional framework required of a modern financial system. It was thus hoped that the Bank would take steps to consolidate its position as an effective monetary authority responsible for the mobilization of funds for the growth and development of the Nigerian economy.

1.2 Objectives of the Study:

In recent times, commercial banks in Nigeria have been experiencing high levels of excess liquidity and are known to have not adequately adhered to the credit guidelines of the Central Bank. The problem of excess liquidity is due to the fact that with the increasing revenues accruing to the government from the oil sector, its total debt to the banking system has considerably reduced. Obviously, this excess liquidity has affected other macroeconomic variables, particularly the price level in the Nigerian economy.

From a policy point of view, this development seems to suggest that the Central Bank as the sole monetary authority has been incapable of applying effective monetary policy to counter these adverse tendencies. Yet this suggestion

poses the question as to whether the Bank actually has the appropriate policy tools at its disposal and therefore is only incapable of effectively applying them individualy or co-ordinating them collectively.

Nevertheless, this study recognizes the fact that commercial banks are profit maximizing institutions with economic behaviour patterns on which the Central Bank must operate to control and regulate such behaviour patterns in a manner capable of achieving a given set of desired economic goals. It therefore becomes necessary to tie them by legislation or otherwise to the Central Bank in order that they observe general regulations concerning capital structure, liquidity management, resources and public disclosures among others.

The problem this study is therefore concerned with is to examine and evaluate how the Central Bank of Nigeria has been able to establish and create a financial system; and regulate the behaviour of commercial banks. The role of government policy, its nature and impact on the behaviour of these banks would also be examined and evaluated.

The study would particularly seek to examine the following issues:

(a) the structure and operations of the Nigerian commercial banking system;

(b) the policy instruments that exist for the regulation of commercial banks;

(c) the impact of the present policies on bank behaviour and the extent of their effectiveness;

and (d) recommend policies for future use in order to improve the commercial banks' behaviour and

operations, and their overall contributions to the realization of the desired objectives of the Nigerian economy.

1.3 The Outline and Scope of Study

Studies on monetary theory and policy have shown the relative effectiveness or ability of the Central Bank to control and regulate commercial banks in order to achieve the desired goals of an economy. In Nigeria, the financial system has witnessed many legislations and government policies in the form of incentives, ownership or equity participation among others.

To be precise, the Central Bank of Nigeria Ordinance enacted in 1958 experienced major amendments in 1962, 1968 and a highly comprehensive amendment in February, 1969. All these were with the hope of strenghtening the Bank's control over the credit operations of the commercial banks, oblige them to hold certain amounts of government securities and to channel private sector credit to directly productive activities. The bank also requires them to hold minimum cash reserves, special deposits and stabilization securities.

During the decade covering the Second and Third National Development Plans, 1970 - 1980, the banking sector experienced more direct government participation and this was as a result of "the recognition of the increasing importance of the sector for the orderly growth and development of the economy"[12]. The Federal Government acquired 60% equity participation in the three major commercial banks namely, the First Bank, Union Bank and United Bank for Africa. In addition, while the Nigerian

Enterprises Promotions Decree of 1972, further greatly affected the structure of ownership in the banking industry, the "small indigenous" banks have consolidated their positions into "big" organizations comparing favourably with the long established "expatriate" banks.

It is hoped that this study will contribute by showing whether the change in the structure of ownership of commercial banks in Nigeria has significantly affected their behaviour patterns. The study will also attempt to show whether other developments in the economy have influenced their co-operation and adherence to the Central Bank's monetary policy guidelines; and their identification with the prescribed objectives of the Nigerian economy. It would also be interesting to find out if the above circumstances have in any way influenced or determined the effectiveness of bank regulation instruments in the economy. In addition to the above, it is hoped that the study will provide an insight towards a better appreciation of the nature of bank behaviour and its regulation in other countries that share Nigeria's background and experience. It may therefore be appropriate to describe this study as the "effectiveness of bank regulation" with a view to contributing a little more understanding to the complex nature and problems of bank regulation, particularly in a developing economy like ours.

The second chapter discusses commercial banking in Nigeria with particular emphasis on its structure, operations and policies, and the nature and quality of banking services. The third chapter examines the Central Bank of Nigeria pointing out the legal framework for the regulation of

commercial banks in Nigeria. Chapter Four investigates and appraises the various monetary and banking policies that have been employed during the period studied. The purpose of the chapter being to establish the effectiveness or otherwise of policy instruments given the circumstances of the Nigerian economy. The major conclusions of the study are summed up in Chapter Five with appropriate policy recommendations.

Financial institutions are subdivided into commercial banks and non-bank financial intermediaries. This study will restrict itself to the control and regulation of the commercial bank category. This is because, commercial banks through their demand-deposit operations, create money since demand deposits are capable of circulating as a means of payment in the modern sector of the economy. It is with this concept of money and ability to create it that conventional theory of government control of commercial banks/ through a Central Bank is based, In addition, commercial banks may not be restricted in their investment operations by limitations imposed by previous receipts of deposits as may be the case with the other category of financial institutions.

In the Nigerian context, it is the commercial banking system that is more developed and therefore more important from the point of view of the execution of monetary policy. It could be observed therefore that these differences certainly warrant different principles of control and regulation; and relative importance attached to each category. This study therefore seeks to examine only such principles.

In terms of policy, the study will lay greater emphasis on the domestic aspects of bank regulation and control and only examine briefly the external situation or objective of external equilibrium. The reason being that, if not for recent developments in the country since 1981, the issue of the external value of the Naira and the problem of balance of payments have since the advent of the oil boom come to assume a low policy priority. The recent developments would therefore be considered only in attempt to throw some light on the ability of the Central Bank to combat them.

The above aspects and issues of concern to the study will be considered mainly for the periods of the Second and Third National Development Plans, 1970-80. The choice of the period is based on the fact that it was during these plan periods that more concerted efforts were made at restructuring the Nigerian economy; and in addition the banking system started experiencing the effects of the comprehensive Banking Decree Amendments of February, 1969. Comparisons will however be made with the period 1960-69 and earlier periods where this is deemed necessary.

FOOTNOTES

1. Among those who held this view are: Minsky, H.P., "Central Banking and Money Market change", Quarterly Journal of Economics, Vol.71, May 1957; Gerschenkron, A., Economic Backwardness in Historical perspective: A Book of Essays, Harvard University Press, Mass. 1962; Patrick, H; "Financial Development and Economic Growth in Underdeveloped Countries" Economic Development and Cultural change, Vol.14 No.2, Jan. 1966; Adelma, I., and C. Morris, Society, Politics and Economic Development: A Quantitative Approach, John Hopkins Press, Baltimore, 1967; Goldsmith, R., Financial Structure and Development, Oxford University Press, London 1972. Shaw, E., Financial Deepening in Economic Development, Oxford University Press, London, 1973.

2. R. Goldsmith, Ibid., P.408 (emphasis mine).

3. J.G. Gurley, "Financial Structures in Developing Economies" in Fiscal and Monetary Problems in Developing States, (ed) D. Krivine, Praeger, New York 1967. Also "Review of Banking in the Early Stages of Industrialization", American Economic Review, Vol.57, 1967.

4. Nwani, A.O., The Role of Monetary and Financial Institutions in the Economic Development of Nigeria: 1800 - 1970, Unpublished Ph.D. Thesis, The Florida State University, 1972; p.1.

5. Ibid, p.2.

6. Abdi, A.I., Commercial Banks and Economic Development: The Experience of Eastern Africa, Praeger Publishers, New York, 1977, p.19.

7. Nwani, A.O., op. cit., p.4.

8. Abdi, A.I., op. cit., p.20.

9. Nwani, A.O., op. cit., p.6 (emphasis mine).

10. Cameron, R., (ed), Banking and Economic Development: Some Lessons of History, Oxford University Press, New York 1972, p.9.

11. Ibid., p.9.

12. Central Planning Office, Lagos, Third National Development Plan 1975 - 80, Vol.I.

CHAPTER II

COMMERCIAL BANKING

2.1 Review of Related Literature

Throughout history, economists have expressed varying views about the importance and role of money in economic theory. There are at least three schools of thought on this subject, namely: the Mercantilist, the Classical and the Keynesian. These somewhat divergent views have however evolved into a common contention today where it is believed that money can only play a neutral and passive role in a primitive economic system serving as a means of facilitating exchange between members of a community in which there is little specialization. In a complex economic system, however, money "becomes a dynamic factor capable of itself influencing the size of national income, individual incomes, demand for both consumer goods and producers' goods as well as the volume of savings and investments"[1].

It is against this background that monetary policy which takes effect through variations in the volume of purchasing power has come to play important roles in an economy, namely, stabilizing the economy in the face of inflation and deflation, through the growth and decline of money supply; stimulating the economy and thereby reducing unemployment, and bringing about overall economic growth. Wrightsman (1971) defines monetary policy as the "deliberate effort of the central bank to control the money supply and credit conditions for the purpose of achieving certain broad economic objectives"[2].

In Nigeria, the problem of bank regulation goes beyond attempts to control money supply and hence influence the real aspects of the economy. It encompasses attempts by the Central Bank of Nigeria to create a financial system and develop the people's confidence in the financial institutions; and overall legislation, particularly as it affects the banking system.

Various studies[3] have been conducted on the Nigerian financial system and they all seem to accept this view and stand. However, attention has been focused on the structure and effectiveness of the system rather than the effectiveness of the specific regulatory instruments of the Central Bank as a sole monetary authority which obviously are necessary for achieving an effective financial system.

Early studies on the Nigerian banking system divide commercial banks into four categories. These are the expatriate banks, government-owned indigenous banks, private indigenous banks, and mixed banks[4]. This division mainly was on the basis of the structure of ownership, that is, equity participation, management and control. It is however apparent that this classification is no longer necessary today as the minimum Nigerian participation has been raised to 60% of equity. Nwankwo (1980) therefore indicates a distinction between indigenous and mixed banks. The former are banks which are wholly owned and managed by indigenous Nigerian interests while the mixed banks as the name applies are owned and managed by Nigerian and foreign interests[5].

Both the indigenous and expatriate categories however had more peculiar characteristics. Brown (1966) notes that

the expatriate banks for example had a "low branch density in relation to population, the branches were concentrated at the commercial centres (one-half of all banking offices were allocated in seven towns!), the expatriate banks also maintained close contacts with Europeans by whom the banks were extensively used". On the other hand, the banks had little contact with Nigerians, and the degree of mutual confidence was considerably less"[6]. What this actually implies is a discrimination against Nigerians which reflected itself in the interest rates and other charges that were used for them by this category of commercial banks. There was thus need for changes in the system of bank charges by these banks which would help accomplish increased use of the banking system, and further increases in bank credit particularly to Nigerian businessmen.

The indigenous banks category on the other hand was characterized by "inexperienced executives, their assets illiquid, their capital in short supply and many unsavourly features were noted"[7]. This was infact in harmony with Newlyn and Rowan (1954), who had observed that "the benefits of the indigenous banks were still potential than actual; noting that their existing situation was unsatisfactory because of the various unsavourly and speculative features in some of their operations; the inexperience of many of their executives; the illiquidity of their asset portfolios; and their lack of capital"[8]. This situation infact gave rise to the massive bank failures of the 1950s.

To correct some of the adverse tendencies noted by Brown, the interests of the depositors were further protected

through changes in the Central Bank's powers of supervision and control over banks through stiffer statutory requirements regarding share capital and reserve funds. Between 1967 and 1969, the Federal Government reviewed both the Banking Act and the Central Bank of Nigeria Act[9] almost after a decade of their enactment. Infact, they were amended and subjected to a number of significant and rather far-reaching changes in their provisions. Teriba (1969) appraising these amendments concluded that "with the changes in the Nigerian banking legislation between 1967 and 1969, the regulatory framework of the Banking system in Nigeria has been drastically overhauled. Apart from strenghtening the banking system, the powers of the Central Bank over the economy have been considerably increased by widening both its control span and the opportunities for effective monetary policy"[10]. He went on to remark, "it is important to remember that the permissiveness of the law is one thing, the attitude and actual administration of it by the Central Bank is another"[11].

Despite the almost drastic regulatory laws, the structure of the Nigerian Banking system appeared to have remained the same even in terms of contribution. "There were features of foreign domination, ineffective indigenous institutions, unnecessary direct government funding and interference in the operations of many of the institutions"[12]. Given the foreign domination, ownership and control of the system, whereas it "had all the trappings of a modern system", these "features of its structure, ownership, management and control, and operations clearly needed to be reformed"[13]. It was in the light of this report that the Federal Government with

effect from 30 September 1976, acquired 60% participation in all the expatriate banks. In principle, therefore, there are no longer expatriate banks in the country.

The indigenization of the Nigerian banking system cannot be said to have been without problems and set-backs. Nwankwo (1980) is of the opinion that the exercise has failed. He attributes this to the fact that the policy was not carefully thought out since the progenitors of indigenization believed that ownership was the root of the problem; and majority ownership of the system has not succeeded in ensuring the transfer of mind and management. Added to this is the fact that just as the institutions in the system have been set up haphazardly, so also have measures to improve their operations come haphazardly; and what is more, indigenization of the commercial banking sector is muddled and involves contradictory policies over the expatriate banks. Indigenization aims at ownership, control and management of the economy, but by a strange fallacy of composition, the federal government abandoned management and control to the minority equity share holders[14].

After noting that it may be wrong to conclude that the influence of the banking system is all-pervasive, although its direct influence is limited to the modernized sectors of the economy, Brown (1966) had hoped that as the monetization and modernization of the Nigerian economy proceeds, the banking system should come to have much more immediate effect on the average Nigerian[15]. It would therefore be right to point out that this was one of the major objectives that the Central Bank of Nigeria was expected to achieve; with the

creation of an environment suitable for effective monetary policy as the ultimate goal.

The growing monetization of the Nigerian economy has however been accompanied by the ever increasing problems of inflation, balance of payments, excess liquidity in the banking system and several other institutional and structural problems. The problem of excess liquidity in particular which was first highlighted in 1974 became more pronounced in 1975. The stock of money expanded at the unprecedented rate of 73.5 per cent during the year due mainly to the continued monetization by the government of its earnings from petroleum. The concomitant inflationary effect was agravated by the substantial increases in salaries and wages accompanied by the payment of arrears in the public and private sectors. With the huge increase in the flow of deposits to commercial banks, and the excessive and growing accumulation of liquid funds in the banking system, the need of finding suitable investment outlets for the banks short-term surplus funds became urgent, and overall monetary stability appeared severely threatened[16].

It is important to emphasize at this point that this development did not mean a lack of investment outlets for the surplus funds of the commercial banks. Indeed investment opportunities existed in the agricultural sector and small scale industries and businesses among others. But that these outlets were not utilized raises yet another question as to whether the Central Bank is infact capable of controlling and directing bank credit to those sectors of the economy that it is most needed.

Thus, all these monetary developments with their attendant problems posed for the Central Bank a challenging problem of how to control and manage a financial system and a monetary expansion, the main source of which it had little direct control. It is convenient to attribute this situation to the relationship between the Central Bank and the Federal Ministry of Finance whereby because of the latter's treasury function, it tends to influence the Central Bank's policy options to the extent that the Bank is often forced to abdicate some of its regulatory functions in pursuit of those policies that aim at meeting the government's treasury requirements in any financial year. However, it is on this note that it is considered proper to reiterate that it is how the Central Bank in the face of all problems has employed the tools at its disposal in regulating commercial banks; and how effective these tools have been that is the prime objective of this study.

Any study that involves the application of policy instruments in an economy should first seek to capture the basic and fundamental realities of such an economy. In this regard therefore, this study would examine commercial banking in Nigeria taking into account its structure, operations and policies, the economic environment and regulatory pressures. The Central Bank of Nigeria would also be considered with particular reference to its evolution and policy tools paying special attention to the Amendments to its Act and how they influence its regulatory capacity. It is only after establishing this framework that this

study would critically evaluate the regulation of commercial banks in the Nigerian economy.

To adequately achieve its objective, this study will be theoretical, descriptive, analytical, and will use documentary data from the following sources:

(i) Central Bank of Nigeria:
  (a) Economic and Financial Reviews;
  (b) Annual Reports and Statements of Account;
  (c) Monthly Reports;

(ii) The Annual and Monthly reports of selected commercial banks; and

(iii) Federal Annual Budgets during the period studied.

2.2 Commercial Banking in Nigeria:

The history of Commercial Banking in Nigeria dates as far back as 1892 when the first bank, the African Banking Corporation was established. Before this time however, the need for banks and their services did not arise as the economic environment which prevailed then was that of trade by barter or predominantly commodity currencies. It was therefore not until coins were regularly used for cash transactions that banking became feasible[17]. In this regard therefore, it would be pertinent for us to describe commercial banking in Nigeria as a relatively recent development. Despite this, the banking system has grown rapidly both in terms of size and quality of banking services thus witnessing the establishment of many commercial banks since 1892[18]. Some of these banks have however since failed but as at 30th September 1980, there were as many as 20 registered banks operating in the country with a total of 749 branches[19].

TABLE 2.1

COMMERCIAL BANKS REGISTERED IN NIGERIA UP TO 1980

S/NO	COMMERCIAL BANKS	DATE ESTABLISHED	REMARKS
1.	African Banking Corporation	1892	
2.	Bank of British West Africa	1894	Now First Bank Nig. Ltd.
3.	Anglo-African Bank	1899	Merged with BBWA in 1912
4.	Barclays Bank DCO	1917	Now Union Bank Nig.Ltd.
5.	The Industrial & Commercial Bank	1929	Failed 1930
6.	The Nigerian Mercantile Bank	1931	Failed 1936
7.	National Bank of Nigeria	1933	
8.	Agbonmagbe Bank	1945	Now Wema Bank
9.	The Nigerian Penny Bank		Failed 1946
10.	Agrican Continental Bank	1947	
11.	The Nigerian Farmers & Commercial Bank	1947	Failed 1952
12.	British and French Bank	1948	Now UBA Ltd.
13.	Merchants Bank		Failed 1960
14.	Pan Nigerian Bank	1951	Failed 1954
15.	Standard Bank of Nigeria	"	"
16.	Standard Bank of Nigeria	"	"
17.	Nigerian Trust Bank	"	"
18.	Agroseas Credit Bank	"	"
19.	Onward Bank of Nigeria	"	"
20.	Central Bank of Nigeria	"	"
21.	Provincial Bank of Nigeria	1952	"
22.	Metropolitan Bank of Nigeria	"	"
23.	Union Bank of British Africa	"	"
24.	United Commercial (Credit) Bank	"	"
25.	Cosmopolitan Credit Bank	"	"
26.	Mainland Bank	"	"
27.	Group Credit & Agric Bank	"	"
28.	Industrial Bank	"	"

S/No.	COMMERCIAL BANKS	DATE ESTABLISHED	REMARKS
29.	West African Bank	1952	Failed 1954
30.	Muslim Bank	1958	"
31.	Banque de L'Afrique Occidentale	1959	Now IBWA Ltd.
32.	Bank of Lagos	"	
33.	Berini (Beirut-Riyad) Bank	"	
34.	Bank of the North	"	
35.	Bank of America	1960	Now Savannah Bank Nig. Ltd.
36.	Chase Manhattan Bank	1961	Merged with IBWA in 1965
37.	Bank of India	1962	Now Allied Bank of Nig. Ltd.
38.	Arab Bank		Now Nigeria-Arab Bank
39.	Co-op Bank of Western Bank	"	Now Co-op Bank Ltd.
40.	Co-op Bank of Eastern Nigeria	1961	
41.	Kaduna Co-op. Bank Ltd.	1972	
42.	Kano Co-op. Bank Ltd	1976	
43.	Pan African Bank		
44.	Mercantile Bank (Nig) Ltd	1971	
45.	New Nigeria Bank	1970	
46.	Bank of Credit and Commercial Inter. (Nig) Ltd.		

Source: Central Bank of Nigeria, Lagos, various publications.

While this study would not endeavour to examine the evolution and historical background of Nigerian commercial banks in greater detail for reasons of space, it is worth mentioning

that over the years, the system appears to have gone through five major periods of change. These are, the free banking era (1890-1952), the pre-central banking era (1952-1959); the bank legislation era (1959-1970); the indigenization era (1970-1977); and lastly the Post-Okigbo era (since 1977)[20].

It is pertinent too to observe that each of these periods possessed its own unique features which may largely be said to have affected the development of commercial banking in Nigeria. In sum, therefore, it is these features and factors perculiar to each of these periods that when meshed, have produced the kind of banking system we have today.

2.3 The Structure of the Commercial Banking System.

The twenty commercial banks operating in Nigeria can be classified into two broad discernible categories - indigenous and mixed banks based on the structure of ownership. The indigenous banks are Nigerian dominated and consist of such banks as African Continental Bank Ltd, Bank of the North Ltd, Co-operative Bank Ltd, Co-operative Bank of Eastern Nigeria Ltd, Kaduna Co-operative Bank Ltd, Kano Co-operative Bank Ltd, Mercantile Bank of Nigeria Ltd, National Bank of Nigeria Ltd, New Nigeria Bank Ltd, Pan African Bank Ltd, and Wema Bank Ltd.

Conversely, the mixed banks category is made up of the following commercial banks: Allied Bank (Nig) Ltd, Bank of Credit and Commerce Internationa, First Bank (Nig) Ltd, International Bank for West Africa Ltd, Nigeria - Arab Bank, Savannah Bank of Nigeria Ltd, Societe Generale Bank (Nig)

Ltd, Union Bank (Nig) Ltd, and United Bank for Africa Ltd. On the basis of available evidence, it can be said that this category contains the largest commercial banks in the banking system by any criteria of size. The indigenous banks on the other hand are either single-state owned or inter-state owned with the latter being relatively larger in terms of branches, deposits and the volume of loans and advances.

The picture that emerges from the above is one of a predominance of indigenous ownership in the banking sector of the Nigerian economy. For example, at the end of February 1976, the authorized and paid up capital of all commercial banks in the country was ₦126.3 million and ₦93.1 million respectively. The mixed banks accounted for 47.9% of the authorized and 49.2% of the paid up capital. The indigenous banks accounted for 52.1 of and 50.8% respectively[21]. It is important to note however that this ownership is mostly public than private with federal and state governments collectively owning the bulk of the equity.

The development of commercial banking in Nigeria has not been accompanied by an even distribution of bank offices and services; and the lop-sided nature of banking development as a feature of the commercial banking system is therefore easily apparent. The ultimate consequences of this have been a low banking density both in terms of offices in relation to the geographical area and population; and the concentration of bank offices in urban and commercial centres. These problems are clearly illustrated in Table 2.2 below.

TABLE 2.2

Statewise Distribution of Commercial Bank Offices as at September 1980

State	No of Bank Offices[1]	% of Total	Estimated Population[2]	Estimated Area(sq km)	Persons per Bank	Area per Bank
Anambra	57	7.6	2943483	15770	51640	27667
Bauchi	19	2.5	1193674	16813	62824	88489
Bendel	58	7.7	2435849	38061	41997	65622
Benue	21	2.8	3041194	63740	144818	303524
Borno	26	3.4	2990526	116589	115020	448419
C. River	25	3.3	3600000	29164	144000	116656
Gongola	21	2.8	3002808	102067	142990	486033
Imo	52	6.9	3288340	13032	63237	25062
Kaduna	40	5.3	4098385	70293	102459	175733
Kano	42	5.6	5774842	42123	137496	100293
Kwara	24	3.2	2309338	73403	96222	305846
Lagos	131	17.5	1443567	3535	11019	2698
Niger	51	2.0	2389338	73403	159289	489353
Ogun	29	3.8	1551946	20241	53515	69797
Ondo	42	5.6	2727675	18165	64944	4325
Oyo	69	9.2	5158884	42862	74766	62119
Plateau	22	2.9	2026657	56245	92120	255659
Rivers	34	4.5	1800000	21172	52941	62271
Sokoto	22	2.9	4538803	945588	206309	429945
Total	749	100	56315309	911266	75187	121664

Sources: 1. Adeniyi, O.A., op. cit., P.184.

2. 1963 Population census figures.

As can be seen, the Nigerian economy is underbanked. There are as many as 75,187 persons per bank office and the geographical area per office is as high as 1,216.64 square kilometers. These ratios contrast very sharply with those of developed and other developing countries. In the United Kingdom, it is 4,000 persons per bank office, 6,000 persons per office in the United States of America, one bank office to 14,500 persons in Japan, and 52,000 persons per bank office in India[22].

The distribution of bank offices among states in Nigeria reveals a heavy concentration in Lagos despite the fact that the population of Lagos state is only 2.5% of that of Nigeria. The state also has an average density of 26.98 square kilometers per bank office. In contrast, some states are very worse off in the distribution of banking services; and in particular are the cases of Benue, Niger and Sokoto states. For Benue state, we have 144,818 persons per office and an office to 3,035.24 square kilometers. Sokoto state on the other hand, has 206,309 persons per bank office and 4,299.45 square kilometers to an office. Equally revealing is the concentration of more than half of the total number of bank offices in the country in the six southern states of Lagos, Ondo, Oyo, Bendel, Imo and Anambra who jointly share between them 409 branches.

This study notes the lack of current official population figures; and the fact that the above analysis may not potray the true position as at the period studied. Projections

of the 1963 census figures have however not revealed a radically different picture. But even within the above states, there are lop-sided developments. An analysis of the location of commercial bank offices in Nigeria at the end of December 1975, showed that out of the 93 bank offices in Lagos state, 35 are in Lagos city; out of the 50 offices in Oyo, 24 are in Ibadan; and out of the 46 in Bendel state, 12 are in Benin city; and out of the 34 bank offices in Anambra state, 12 are in Enugu[23].

The uneven distribution of banking services as demonstrated above may be accounted for by many factors principal among which are the adoption of the demand-following approach in the development of bank offices by Nigerian commercial banks, the concentration around regional capitals and commercial centres, and the lack of a conscious policy to direct and develop the interest of commercial banks in rural banking. The establishment of state owned banks also accounts for the disparity among states. Nevertheless, the above factors are plausible if we consider the expansion in bank offices after the creation of states and more local governments in 1976.

The lop-sided banking development has many serious implications for the overall development of the Nigerian economy as it impedes the development of the banking habit and the mobilization of savings. Most people have to travel long distances to avail themselves of banking services; and in addition, because of the many persons per bank

branch, services at most branches are poor. A common feature is long queues with people struggling to get served. The poor services also include vital bank transactions like mail transfers and cheque clearnace which may take up to a month or more. This problem may however be explained by the poor communications system in the country; one expects that the commercial banks in order to provide effective and efficient services to their customers shouls have developed ways and means of solving this problem.

Another prominent feature of commercial banking in Nigeria is that of poor bank management. "In the face of existing expatriate quotas consequent upon the indigenization of personnel, the banking industry like other industries in Nigeria is faced with the problems of recruiting and training the right calibre of staff"[24]. This situation has given rise to understaffing and inexperienced staff in most commercial banks. Even where banks spend time and resources to train their staff, these are very often lost to competitors who may offer higher salaries and better conditions of service. What is more, many a staff are known to be reluctant to work in rural areas and as such often refuse transfers and consequently withdraw their services.

A feature which is the direct consequence of the poor bank management problem is the high rate of fraud and irregularities that plague the commercial banking system. These have reached alarming proportions and range from cash

shortages to forgeries and collusions. There are indications however that bank managers have not always been given a free hand to manage their branches. It is therefore not unusual for a branch manager to reject a loan application only to receive instructions from "above" to grant the facility. At times, pressures may come from the extended family set-up of our societies. Whichever of these cases apply, there is ample evidence that bank managers in Nigeria are often subjected to both family and political pressures and they often make decisions which do not depend solely on economic and banking principles, nor in accordance with prudent bank management.

Banking lending by commercial banks operating in Nigeria like in many other developing countries is characterized by a heavy concentration in the financing of general commerce, short magurity of loans and advances, and most important is the fact that only a small volume of bank loans are made to Nigerians. It has been shown that around 90% of loans mature within 12 months and under 10% within one to five years; and it is also known that the highest proportion of total loans made by one expatriate bank to Nigerians in 1969, was 35% with another expatriate bank recording a low proportion of 7%. Explanations to this natu e of bank lending are not difficult to find. In the first place, the concentration of bank lending in the financing of general commerce owes largely to the dominance of commercial banks with foreign origins whose primary interest is to finance this type of activity since they were originally established for this purpose, apart from their operating on the bills-only

principle which stipulates that a good loan is self-liquidating.

Secondly, that Nigerians get a small amount of loans has often been explained by the insinuation that the expatriate (mixed) banks discriminate against them. Although Nigerians responded to this by establishing their own banks, these often lack capital and in most cases are unable to attract substantial private deposits and thus are not always in a position to adequately meet the credit demands of Nigerians. The fault in this matter may however lie in Nigerians themselves. It is common knowledge that our businessmen hardly keep detailed and accurate records; and are often prone to display total disregard towards their financial obligations. Most of them do not repay their loans and may even regard them as their share of the "national cake". Furthermore, some businessmen hardly spend their loans on the projects for which they are made. Such loans end up being spent on ceremonies and the marrying of more wives. All these no doubt make loans to Nigerians very risky and unattractive. Nevertheless, as the nature of business organization in the economy is gradually changing, it is hoped that commercial banks would also respond by changing their attitudes.

It is important to reiterate at this point that all the features of the commercial banking system highlighted above militate against the mobilization of savings and the cultivation of the banking habit. It is this realization

taking into account the important role commercial banks are expected to play in the growth and development of the Nigerian economy that has given rise to the involvement of government and the Central Bank in the banking system. Thus, "the absence of a commercial banking system, predominantly indigenous which would ensure adequate attention to local businessmen in whatever sector they belong as well as the absence of an adequate and flexible capital market, dictate that the Central Bank cannot stand aloof in the tasks of expanding capital formation demanded by the new plan"[25].

The above background formed the basis of government intervention in the banking system which is yet another prominent feature of commercial banking in Nigeria today. Government intervention in the banking system has been in the form of establishing financial institutions with the sole objective of directly financing activities in real estate construction, agriculture and industrial sectors as a way stimulating development in these sectors. The government also establishes certain schemes or programmes to be adopted by the commercial banks; and example of this is the Agricultural Credit Scheme being implemented on its behalf by the Central Bank of Nigeria. To further enhance its position in the banking system, government also has embarked upon the indigenization or ownership of the system through direct participation in banking both in terms of share participation and the appointment of Directors. State governments on their part have embarked upon the establishment of their own banks and the

decade covered by this study has witnessed many of such banks. This development has greatly increased the level of co-operative banking within the system.

The involvement of the Central Bank on the other hand, has been by controlling the volume and direction of finance to the private sector through the issuing of Annual Monetary Policy Circulars which set out credit guidelines indicating the volume and distribution of commercial and merchant bank credit, including loans to indigenous persons and institutions.

2.4 Operations and Policies of Nigerian Commercial Banks.

It is common of institutions like commercial banks, in the face of competition, to make claims as to their various contributions to the realization of the objectives of an economy in which they operate. In many cases, these claims are deliberate and aimed at making customers to identify the bank as patriotic and thus attracting more deposits and business. In the light of these circumstances, the only was for us to perceive the true behaviour of commercial banks is through the examination of their balance sheets.

The balance sheets of commercial banks operating in Nigeria have been examined at several intervals of time. One thing to note however is the fact that most of these past analyses (particularly Nwani and Brown) cover periods that give cause to their being plagued with several problems some of which are purely statistical. In the first place, during these periods none of the banks (except those operating exclusively in Nigeria) published separate figures of their

Nigerian operations. Furthermore, the figures given by those banks who happened to be operating exclusively in Nigeria were often difficult to interpret[26]. Incorrectness of records in terms of misclassification and misrepresentation of certain items were noticeable. It is however a matter of fact that these problems are not very much relevant now as the compilation and presentation of records by both the indigenous and mixed banks has greatly improved. What is more, since the 1969 Amendments, banks cannot include their overseas operations jointly with the Nigerian. It is therefore possible for an analysis now to reveal the real nature of policies and operations of commercial banks in Nigeria today.

This section considers the following aspects of commercial bank operations in Nigeria: capital, deposit liabilities, loans and advances, liquidity and investments including the policies associated with these. An examination of these aspects is highly important as it is capable of indicating the actual sources and uses of bank funds; and their liquidity position from which the profitability of bank funds can be ascertained. Such an analysis is further capable of showing how banks in Nigeria have been able to reconcile their dual and apparently conflicting obligations (of maximum liquidity to their depositors and maximum profitability to shareholders) which give us an insight into the availability of investment outlets and their various forms. Lastly but most important for the purpose of this study, this analysis will help us show the extent to which conventional central bank regulation and

control techniques can be or have been used[27].

Table 2.3 depicts the capital ratios for Nigeria commercial banks during the period under review. An examination of the structural changes that have occurred in some of the items shows that commercial bank capital increased from ₦57.5 million in 1970 to ₦201.7 million at the end of December 1977. This shows an increase of more than 250%. This growth which has been steady and gradual can be accounted for by several factors. One of these is the increase in the minimum capital requirement by the 1969 Banking Decree Amendment which raised minimum capital to ₦0.6 million for indigenous commercial banks; and also increased the percentage of net profits that banks had to transfer to reserve from 12% to 25% until reserves equaled paid-up capital and 12% there-after.

Another reason for the increase and growth in commercial bank capital is the increased tempo of economic activity under the Second and Third National Development Plans. This means that the statutory capital requirements notwithstanding, bank capital would have increased all the same; and this follows logically from its role in and response to increased pace of economic activity. Bank capital while providing for start-up costs, is important in acquiring fresh assets, absorbing operating losses and future expansion plans. It also serves as a protection for depositors such that in times of liquidation, it would reduce the losses that depositors and other creditors would otherwise be required to share. In this way therefore, "bank capital inspires the

TABLE 2.3

Capital Ratios for Nigerian Commercial Banks 1969-80
(N'm)

	1969	1970	1971	1972	1973	1974	1975	1976	1977	1980
Capital & Reserves	54.3	57.5	70.3	76.8	86.1	100.0	127.2	157.0	201.7	-
Total Deposits	401.0	625.3	651.2	793.8	1,013.0	1,693.9	2,839.2	4,164.3	5,235.2	10,009.2
Demand Deposits	185.5	289.0	285.3	336.9	430.7	720.7	1,266.8	2,185.2	2,980.1	4,846.0
Time Deposits	120.7	207.0	211.4	256.0	351.8	686.5	1,051.0	1,270.0	1,325.0	3,573.7
Savings	94.7	129.7	160.2	201.0	224.5	286.7	521.3	709.2	930.1	1,589.5
Assets	757.4	1,147.2	1,275.9	1,437.5	1,772.0	2,811.1	4,308.1	6,371.4	8,630.9	-
Capital-Deposits Ratio (%)	13.5	9.2	10.8	9.7	8.5	5.9	4.5	3.8	3.9	-
Capital-Assets Ratio (%)	7.2	5.0	5.5	5.3	4.9	3.6	3.0	2.5	2.4	-

Source: Central Bank of Nigeria, Various Publications.

confidence of depositors and regulatory authorities in addition to serving to regulate the expansion of loans and investments such as the 1:10 ratio currently required of banks in Nigeria"[28]. Infact whereas regulatory authorities cannot directly influence the day to day activities of a bank and its profit making capacity, they do possess the power to require banks to maintain adequate capital and comply with relevant capital ratios which would enhance their continued viability and increased confidence by depositors.

The growth in the capital of Nigerian commercial banks has been accompanied by astronomical growth in deposit liabilities. Between 1970 and 1980, commercial bank deposit liabilities increased by over fifteen times from ₦625.8 million in 1970 to 10,009.2 million at the end of 1980. The highest increase in deposits occurred in 1975 when total deposits rose from ₦1,693.9 million in 1974 to ₦2,839.2 million in 1975. Also significant increases occurred between 1979 and 1980. Developments in the structure of bank deposits are also worth mentioning. During the period studied, demand deposits increased from ₦289.0 million in 1970 to ₦4,846.0 million in 1980. The growth in demand deposits was relatively small between 1970 and 1973. A significant increase was however recorded between 1974 and 1975. This growth was short lived as it declined in 1977 and thereafter. Developments in demand deposits as a proportion of total deposits has also been along the same lines. Time deposits which increased from

₦201.0 million in 1970 to ₦3,573.7 million in 1980 did not however change as a proportion of total deposits. Savings on the other hand, declined from a peak of 25% in 1972 to 15% in 1980.

The above developments in the growth and composition of commercial bank deposit liabilities between 1970 and 1980 can be explained by several factors principal among which are the increase in the level of monetization in the economy and the growth in banking facilities, increases in incomes as a direct consequence of the Udoji Awards, government deficit financing and increased expenditures from the oil boom.

What is evident is that the phenomenal increase in deposits has resulted in a downward trend in the capital ratios. The Capital-Deposits Ratio which demonstrates the relationship between bank capital resources and deposits which was at its highest in 1971, declined to 3.9% in 1977. Similarly, the Capital-Assets Ratio which is a measure aimed at ascertaining the extent to which commercial bank capital could absorb unexpected losses and still protect depositors and creditors has also continued to decline. The effect of these declining capital ratios on risk and the overall adequacy of capital need not be over-emphasized.

In the above circumstances, the deteriorating capital ratios have raised the serious question of capital adequacy for Nigerian commercial banks. This is despite the fact that capital ratios are not usually excellent indicators of

capital adequacy; they however do serve a useful purpose in terms of the initial screening of the capital position of the commercial banks by supervisory and regulatory authorities. The basic requirement therefore is for banks to have a certain level of minimum capital in order to ensure that capital performs its basic functions. It is worth mentioning that the issue of bank capital differs greatly from one commercial bank to another and the nature of their operations, the financial system and the risky nature of loans and advances. It is indeed these differences that actually make the identification of which amount of capital is adequate for capital to play its normal functions difficult, if not impossible.

It can however be observed that most Nigerian commercial banks after discovering that the increases in deposits beginning from 1973 have deteriorated their capital ratios, and hence threatened their liquidity positions, decided to call in their loans and advances together with restricting their lending activities. This indeed is yet another plausible reason that explains the high liquidity rate in the banking system during that period of time; and why credit was not extended to the several investment outlets which had existed.

Central to commercial bank operations in Nigeria is the issue of how they manage their liquidity positions. Bank liquidity in general represents the closeness of assets to cash; and the strategy adopted by banks for dealing with uncertainties and emergencies forms their liquidity policy.

TABLE 2.4

Liquidity Ratios for Nigeria Commercial Banks: 1969-78 (N'M)

	1969	1970	1971	1972	1973	1974	1975	1976	1977	June 1978[a]
Total Deposits	401.0	625.8	651.2	793.8	1,013.0	1,693.7	2,839.2	4,164.3	5,235.2	5,270.0
Loans and Advances	231.2	342.2	489.4	603.3	740.6	915.0	1,475.6	2,072.5	2,994.8	3,632.1
Assets	757.4	1,147.2	1,275.9	1,437.5	1,772.0	2,811.1	4,308.1	6,371.4	8,530.9	-
Total Liquid Assets	279.2	581.2	373.3	466.8	495.8	1,109.8	1,618.5	2,198.5	2,036.1	2,086.5
Investment	2.2	5.7	10.3	10.1	7.4	22.9	104.9	295.6	601.4	-
Cash and Cash Items	25.2	46.6	38.4	43.8	65.9	331.4	828.7	1,094.0	851.8	-
Loan Deposit Ratio (%)	57.7	54.7	74.5	76.0	73.1	54.0	52.1	49.8	57.2	68.9
Loan-Assets Ratio (%)	30.5	29.8	38.4	42.0	41.8	32.5	34.3	32.5	35.1	45.1
Liquidity Ratio (%)	69.6	92.9	57.3	58.8	48.9	65.5	57.0	52.8	38.9	39.9

Source: Central Bank of Nigeria, Various Publications.

a. Okigbo, P.N.C., op. cit., P.98.

The importance of liquidity is borne out of the fact that it indicates an assurance to depositors that they would be able to obtain their deposits under almost all circumstances. Liquidity thus can be said to represent a defense against the effect of extreme pressures on a bank that would represent a loss of confidence by depositors and lead to a situation whereby depositors would collectively attempt to withdraw their deposits.

The liquidity position of commercial banks operating in Nigeria is statutorily defined. Despite this, it is pertinent for us to perceive commercial bank liquidity by examining certain relevant ratios and relationships between the balance sheet items; of importance is the Loan-Deposit Ratio and the maturity of loans and securities. Table 2.4 shows the loan-deposits ratio for commercial banks operating in the country. The ratio rose from 54.7% in 1970 to 76.0% in 1972. It fell from 73.1% in 1973 to an all time low level of 49.8% in 1976. The Loan deposit ratio indicates that banks in Nigeria have a large proportion of their interest earning assets in loans and a small proportion in securities. This development may be attributed to the lack of a securities market particularly between 1971 and 1973 when the ratio soared.

It is important to point out that banks in Nigeria are statutorily forbidden to invest in real estate, and in the absence of a developed money market, the best alternative was to invest in loans and advances. Also the increase in the

credit operations of the banks immediately after the civil war explains the soaring ratio; in addition is the effect of the indigenization policy. It is however worth observing that, with increase in money market instruments between 1973 to 1976 and increased activities at the Lagos Stock Exchange, this ratio has been affected.

The liquidity ratio on the other hand has little significance in the explanation of the policies and operations of Nigerian commercial banks. This is because what constitutes liquid assets is statutorily defined and this has been altered by policy at many times during the period covered by this study. This happened in 1972, 1975 and 1979. The composition of the liquid assets portfolio of the banks and choice of instruments for the liquidity requirement has therefore been greatly widened between 1970-80. In this way, the liquidity ratio has not been affected or influenced solely by developments in the banking system but through changes in specifications by policy. Nonetheless, "the ratio is of importance particularly for annual review of developments in terms of compliance of the commercial banks with the stipulations of central bank" [29].

The structure and composition of commercial bank loans and advances is worthy of further analysis. Loans and advances are injected into four broad sectors of the Nigerian economy, namely:-

i) Production - agriculture, forestry and fisheries, manufacturing, minning and quarrying, real estate and constructions;

ii) General commerce - bills discounted, domestic trade, exports and imports;

iii) Services - public utilities, transportation and communication; and

iv) Others - Credit and financial institutions governments, personal and professional and miscellaneous.

Tables 2.5 and 2.6 show the sectoral distribution of commercial bank loans and advances from 1969-70. During this period, commercial bank loans and advances increased by more than twelve times from ₦351.4 million in 1970 to ₦4,250.8 million at the end of September 1979. As astronomical increase was recorded between 1969-72 when loans and advances more than doubled from ₦242.7 million to ₦619.6 million. Another upsurge in loans and advances was recorded between 1974-75 when they increased from 24.5% to 53.2%, and have been on the decline since then. The increase in loans and advances between 1970-72 owes largely to the massive reconstruction and rehabilitation by the government following the end of the civil war. Thus, to ensure the success of this effort, attempt was made to increase the level of loans and advances in the economy and to all sectors. In addition, while the commercial banks in the war affected areas resumed operations after the civil war, the other banks also increased their scope of operations to include the war areas.

On the other hand, the decline in the growth of loans and advances between 1972-75 may be attributed to the high prices prevailing at that time and the considerable efforts made to control these emerging inflationary pressures. Thus, attempts by government to stop the inflationary trends led to directives being given to the commercial banks to decrease their loans and advances especially in the non-productive sectors. The structural changes that occurred between 1974-75 were mostly as a result of the impact of the Udoji Awards. In general however, it can be said that most of the structural changes in loans and advances during the period studied are as a result of decisions of the central Bank and the state of general economic conditions. This is in the sense that increases in loans and advances tend to reflect the overall growth of the economy which not only generates demand for bank credit but also creates opportunities for bank lending.

The changes in loans and advances are also mirrored in their sectoral distribution. In the production sector, changes occurred between 1972-73 following the introduction of target percentage shares for each of the sectors in place of credit ceilings. In the agricultural sub-sector, total loans and advances have increased both in volume and share of loans from a meagre ₦7.0 million in 1970 to ₦277.0 by the end of September 1979. In terms of the proportion of loans going into the sector, this increased from 2.0% to 6.5% during the same period. Significant improvements

TABLE 2.5

Sectoral Distribution of Loans and Advances 1969-79
(₦'M)

SECTORS	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	Sept. 1979
Agriculture, Forestry and Fishing	4.4	7.0	9.2	9.2	27.6	27.4	37.4	79.6	139.1	229.0	277.0
Manufacturing	41.9	76.4	119.8	114.0	182.3	258.5	410.7	609.0	837.8	1138.0	1233.0
Mining and Quarrying	3.1	6.6	11.6	10.2	6.3	12.2	16.3	14.6	37.7	39.4	45.8
Real Estate and Construction	17.7	26.0	37.4	49.2	76.6	97.8	212.8	412.3	662.1	882.9	986.6
General Commerce	126.6	167.6	221.2	222.2	267.1	284.9	403.7	531.0	712.0	868.7	782.0
Transportation and Communication	9.8	19.0	31.8	44.4	51.7	66.0	82.0	180.7	233.6	284.5	305.8
Credit and Financial Institutions	4.7	2.8	5.8	14.2	11.8	21.7	51.6	57.0	95.6	150.8	100.7
Government and Public Utilities	6.6	1.8	7.2	14.2	28.7	39.0	54.4	77.9	131.5	131.5	215.0
Personal and Professional	11.5	23.2	33.2	62.0	43.0	62.4	84.8	98.5	137.6	203.9	181.3
Miscellaneous	16.5	21.0	24.8	40.0	64.5	68.6	83.6	68.6	85.7	123.9	125.6
Total	242.7	351.4	502.0	589.6	753.5	938.3	1437.5	2122.9	3074.7	4109.7	4252.8

Source: Central Bank of Nigeria, Various Publications.

TABLE 2.6

Sectoral Distribution of Loans and Advances 1969-79 (Percentage)

SECTORS	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	Sept. 1979
Agriculture, Forestry and Fishing	1.8	2.0	1.8	3.3	2.9	2.9	2.6	3.8	4.5	5.7	6.5
Manufacturing	17.3	21.7	20.9	19.3	24.2	27.5	28.6	28.7	27.2	28.1	28.9
Mining and Quarrying	1.3	1.9	2.3	1.7	0.8	1.3	1.1	0.7	1.2	1.0	1.1
Real Estate and Construction	7.3	7.4	7.5	8.4	10.2	10.4	14.8	19.4	21.5	21.8	23.2
General Commerce	52.2	47.7	44.1	37.7	35.4	30.4	28.1	25.0	23.2	21.4	18.4
Transportation and Communication	4.0	5.4	6.3	7.5	6.9	7.0	5.7	8.5	7.6	7.0	7.2
Credit and Finance [illegible] Institutions	1.9	0.8	1.2	2.4	1.6	2.3	3.6	2.4	3.1	3.7	2.4
Government and Public Utilities	2.7	0.5	1.4	2.4	3.8	4.2	3.8	3.7	4.3	3.2	5.0
Personal and Professional	4.7	6.7	6.6	10.5	5.7	6.7	5.9	4.6	4.5	5.0	4.3
Miscellaneous	6.8	5.9	4.9	6.8	8.5	7.3	5.8	3.2	2.8	3.1	3.0
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Computed from Table 2.5

have occurred in the manufacturing sector which is usually a large credit user. Commercial bank loans and advances to the subsector experienced an enormous increase from ₦41.9 million in 1969 to ₦1,233.0 million in 1979. The proportion of loans going to this subsector was for the first time the highest outside general commerce as from 1976-78. But as at September 1979, credit to the general commerce sector again exceeded it.

Another subsector in the production sector that has attracted loans and advances is real estate and construction. The proportion of loans and advances to this sector increased from 7.2% in 1969 to 23.2% in 1979. This increase owes largely to the increased government spending in this sector with the construction of such infrastructures as roads, airports, ports and allied construction activities. All these necessitate considerable working capital requirements on the part of the construction companies; and this perhaps accounts for the increases in loans and advances to the construction sector.

Loans and advances to the General Commerce sector while experiencing increases in total volume from ₦126.6 million in 1969 to ₦782.0 million at the end of September 1979, have declined in terms of the proportion going to the sector from 52.2% to 18.4% during the same period. Developments in this sector can be explained by the fact that, while the domestic trade component has shown greater stability, imports have seriously declined proportionately

following restrictions in fiscal and trade policies adopted by government in the interest of the country's balance of payments.

All the remaining sectors, while recording increases in the volume of loans and advances injected into them, have been reasonably stable in their share of total loans and advances. Thus the proportion of loans and advances going to mining and quarrying has been consistently below 2.0%. Loans and advances to transportation and communication, credit and financial institutions, personal and professional sectors have been relatively irregular, rising and falling over the years during the period under review.

2.5 Banking Services.

Commercial banks apart from providing the most important bank services of acceptance of deposits, provision of payments mechanisms both at home and abroad, and the provision of credit, do provide other ancilliary services which are vital and deterministic for an affective banking system. With the continued growth and expansion of the Nigerian banking system, it is necessary for us to briefly examine whether this growth has been accompanied by improved quality and adequate banking services. These services range from domestic to overseas.

In an economy like ours that is highly dependent on importables be it raw materials or food/consumer items and overseas travel; and with the control of foreign exchange by government, the banks have come to play a vital role in assisting the Central Bank in processing applications for

foreign exchange. They offer telegraphic and mail transfers, banker's drafts and cheques. These have meant the improvement in the speed, safety and conveniences of economic transactions and also provides a favourable method of settlement for importers.

Other banking services offered by commercial banks centre on the settling of transactions through the provision of note and coins in the right denominations at the right time. This service is highly expensive and time-consuming but facilitates transactions which would be greatly disrupted if customers cannot collect money in precise denominations for the purposes of payment for goods and services.

In a country with underdeveloped money and capital markets like Nigeria, Commercial Banks play a useful role through the receipt of applications for new issues of stocks and shares on the Stock Exchange from the public. Infact some of the banks participate actively in investment management whereby it is possible for a customer to entrust the management of his investments completely to the bank. In this case, the customer gives the bank written authority to buy or sell securities on his behalf; and the bank ensures that the customer's holdings of stocks and shares are managed in his best interest.

The operation of economic and consultancy services by commercial banks has greatly come to be of great assistance to investors in Nigeria today. These departments study developments in the economy, individual industries and in

some cases, some overseas countries. In this way they are always in a position to provide necessary information to their customers including technical partners. Similarly, banks may provide references on their customers for purposes of their financial standing, line of credit and credit worthiness to both individuals and firms who may be dealing with them.

Commercial Banks also now provide services in the line of safe custodies for the safe-keeping of documents and other valuables which may be placed in their strongrooms at the various branches.

There is no doubting the fact that while the provision of banking services in Nigeria has greatly improved, there is still more room for improvement. An important thing that must however be mentioned here is the high cost of these services both in terms of charges for ancilliary services and the cost of loans. The reasons for this are not very easy to come by. But in general, commercial bank operations in Nigeria are apparently costly because of the high cost of staffing and training particularly of Nigerians who may often have to be trained abroad; and the high incidence of frauds and bad debts. All these have increased the cost of banking operations and impeded the improvement of banking services in addition to increasing their costs.

The situation highlighted above however becomes belated if we consider the profit figures of the commercial banks. against their total deposits and shareholders' funds.

TABLE 2.7

Pre-tax Profit, Deposits and Shareholders' Funds for Selected Commercial Banks in Nigeria
(₦'m)

Bank	Year ended 31st Mar/Dec. 1978	Mar/Dec. 1979	Mar/Dec. 1980	Mar/Dec. 1981
First Bank (Nig) Ltd				
- Profit before tax	34.72	40.61	31.01	50.70
- Total Deposits	1,229.29	1,247.19	2,162.98	2,262.01
- Shareholders' Funds	51.98	64.49	99.38	141.78
Union Bank (Nig) Ltd				
- Profit before tax	n.a	22.91	35.12	60.20
- Total Deposits	n.a	1,282.18	1,624.59	2,318.28
- Shareholders' Funds	n.a	67.39	81.65	104.92
United Bank for Africa Ltd.				
- Profit before tax	34.97	n.a	41.37	42.87
- Total Deposits	992.2	n.a	1,576.23	2,407.22
- Shareholders' funds	52.98	n.a	77.60	94.31

Source: Annual Reports of the various Banks for 1984, 1983 and 1981.

Table 2.7

Table 2.7 depicts this position between 1978 and 1981. This researcher wishes to note particularly the difficulty he had in obtaining these figures from the Annual Reports of the Commercial banks. It is interesting to know that past copies of these reports were neither available at the various branches he visited nor at the area offices in Kaduna and Kano. It is for this reason that the figures do not reflect the whole period covered by the study. ₦.

As the table shows, the profits of the Union Bank for example rose from ₦22.91 million weighed over total deposits and shareholders' funds of ₦1,282.18 million and ₦67.39 million respectively in 1979 to over ₦60.20 million against shareholders' funds of ₦104.92 million and total deposits of ₦2,318.28 million in 1981. It is clear therefore that these banks have made high profits from their operations. It would thus be proper to suggest that commercial banks operating in the country invest more of their profits in order to expand and improve the quality of their services. The Central Bank may make a special provision on this and monitor the implementation of same.

FOOTNOTES

1. Hanson, J.L., Monetary Theory and Practice, MacDonald and Evans Ltd, London 1970, p.219.

2. D. Wrightsman, An Introduction to Monetary Theory, The Free Press, New York 1971, P.173.

3. Some of these are:
Iwuagwa, E.O., Capital Formation in Nigeria, some Financial and Economic Implications; Ph.D. Thesis, University of Wisconsion, 1957; W.O. Uzoaga, An Analysis of the Monetary and Banking system of Nigeria Ph.D. Thesis Fordham University, 1961; D. Barry, Indigenous and Foreign, Bank Behaviour in Nigeria, and A.O. Nwani, op. cit.

4. See in particular, A.O. Nwani, P.62 and C.V. Brown, The Nigerian Banking System, George Allen and Unwin Ltd, London 1966, Pp.30 - 31.

5. G.O. Nwankwo, The Nigerian Financial System, The Macmillan Press Ltd., London 1980,P.64.

6. C.V. Brown, op. cit., P.184.

7. Ibid, P.188.

8. Newlyn, W.T. and D.C. Rowan, Money and Banking in British Colonial Africa, The Clarendon Press, Oxford 1954, P.213.

9. The most important of these Decrees are (i) The CBN Act (Amendment) Decrees 1967, Decree No.35 of August 3, 1967 retroactive from April 1, 1967;(ii) The CBN Act (Amendments) No.3 Decree 1968 of September 18, 1969 retroactive from May 9, 1969; (iii) The Banking Decree 1969.

10. Teriba, O., "The 1967-69 Banking Amendments in Nigeria: An Appraisal of Financial Adaptation in an under-developed War Economy" Nigerian Journal of Economic and Social Studies, Vol.11, No.1, 1969, P.36.

11. Ibid, P.36 (emphasis mine)

12. Report of the Committee on the Financial System, Lagos, December 1976, P.11.

13. Ibid, P.11.

14. Nwankwo, G.O., Op. cit., P.82.

15. C.V. Brown, op. cit., P.182.

16. Central Bank of Nigeria, Annual Report and Statement of Accounts, 1975, P.50.

17. Okigbo, P.N.C., Nigeria's Financial System, Structure and Growth, Longman Group, Essex, 1981, P.75.

18. Table 2.1 shows the list of Commercial Banks that have been registered in Nigeria up to 1980. Those banks that have since failed are indicated in the remarks column.

19. Adeniyi, O.A., The Law and Practice of Banking in Nigeria, University of Ife Press, Ile-Ife, 1981, P.184.

20. Nwankwo, G.O., op. cit., Pp.45-53.

21. Ibid, P.64.

22. Ibid, P.65.

23. Odoh, N.O., "Fundamental Problems of Banking in Nigeria" in The Foundations of Nigeria Financial Infrastructure (ed) J.K. Onoh, Croom Helm Ltd, London, 1980, P.75.

24. Nwankwo, G.O., op. cit., P.67.

25. Central Planning Office, Lagos, Second National Development Plan 1970 - 74, P.71.

26. Brown, C.V., op. cit., P.37.

27. Nwankwo, G.O., op. cit., P.58.

28. Uzoaga, W.O., Money and Banking in Nigeria, Fourth Dimension Publishers, Enugu, 1981, P.96.

29. Okigbo, P.N.C., op. cit., P.106.

CHAPTER III

THE CENTRAL BANK OF NIGERIA

The Central Bank of Nigeria (CBN), established by the Central Bank Ordinance of 1958 did not start operations until 1 July, 1959. Before its existence however, Nigeria had experienced a currency board system - the West African Currency Board (WACB). The WACB itself was established in 1912 by the colonial government following the recommendations of the Emott Committee for the purposes of issuing currency and legal tender. It was also to perform the following principal functions: "financing the needs of the export trade of expatriate firms operating in West Africa; and to eradicate the confused, inconvenient and unsatisfactory currency position in British West Africa"[1]. It is therefore evident that the WACB was established primarily to serve the interests of the colonial authorities and aid in their bid to exploit their West African colonies to the fullest.

With its kind of objectives and mode of operation, it did not take long for most Nigerian nationalists of that time to regard and see the WACB as being absolutely incapable of taking good care of Nigerian interests. Indeed, their major and strongest arguments against the Board were based on its weaknesses and defects which among others included the contention that it had no room for monetary management. It was thus believed that since the currency of the Board was not independent, the currency in circulation was directly linked to the

balance of payments with automatic parity with sterling and therefore could not be managed. In essence, this meant that since the WACB had no control over money supply in the currency area, it apparently lacked the necessary powers to initiate and execute monetary policy.

The above believe was further strenghtened by the fact that the WACB apart from not having any African on its board, did virtually nothing "to train Africans in the art of monetary management or to develop indigenous banking and other financial institutions"[2]. It was also against this background that Nigerian nationalists profusely demanded for the establishment of a central bank for their country taking into account their political development, conditions of the Nigerian colonial economy and the agitations for independence. It could therefore be said that the major objective of these nationalists was thus not only to break the monopoly of expatriate banks but also to have their kith and kin develop the art of banking in readiness for further responsibilities in an independent Nigeria. The nationalists also saw a central bank as an important factor if the economic development of an independent Nigeria was to be vigorously pursued and achieved with every expediency. One important conclusion worth reaching at this point in the face of the above is the fact that nationalism from every indication was a major and crucial factor in the establishment of the CBN.

The above conclusion notwithstanding, the background leading to the establishment of the CBN can best be described as highly controversial. This is in the sense that whereas

the colonial administration was pushed into looking for ways and means of creating a central bank in Nigeria, the reports of the various committees on the issue held greatly varying conclusions. The first report was that by J.L. Fisher who was appointed to "inquire into the desirability and practicability of establishing a central bank in Nigeria as an instrument for promoting the economic development of the country". In his report, Fisher unambiguously concluded that, "... it would be inadvisable to contemplate the establishment of a central bank at the moment which could operate satisfactorily in such a narrow field. Moreover, it is hard to see how a central bank could function as an instrument to promote economic development of the country"[3].

An important factor for this conclusion by Fisher was the absence of an indigenous banking system and other financial institutions that are necessary for the effectiveness of a central bank. It was in this regard that the report had hoped that with the development and growth of the above, the establishment of a central bank would be a logical and useful step. But given the nationalist feelings prevalent at that time, this recommendation by Fisher was met with strong resistance as the nationalists saw the Central Bank as the only hope for their objective of rapid economic development; and this acquired more significance as there were continued efforts towards independence.

The second report on the desirability and practicability of establishing a central bank in Nigeria was by a World Bank Mission which visited the country in 1953. This report was

of the view that the continued political and economic advancement of Nigeria is bound to lead to the establishment of a Central Bank. The Mission therefore felt that if the management of foreign assets and issue of currency were delayed, this would amount to delaying that time when Nigerians would be able to perform these functions themselves[4]. Needless to add that this report was good news to the nationalists.

It was on the basis of this World Bank Mission Report that Mr. J.B. Loynes was appointed to make recommendations on the establishment of a Nigerian central bank, the introduction of a Nigerian currency and other associated matters. In particular, Loynes was to advise on:

(a) the establishment of a Federal institution to perform central banking functions;

(b) the introduction of a Nigerian currency and the administration of such a currency so as to preserve its external value and its acceptability within the country;

(c) the relationship of the federal institution to the federal and regional governments; to government institutions, to the commercial banks and to the public; and

(b) the role of such an institution in the development of a local money and capital market[5].

It is often contended that had Loynes not been given specific terms as to the fact that there would be a central bank and he should advise as to how best it should look like, he too like Fisher would have certainly seen no need for it.

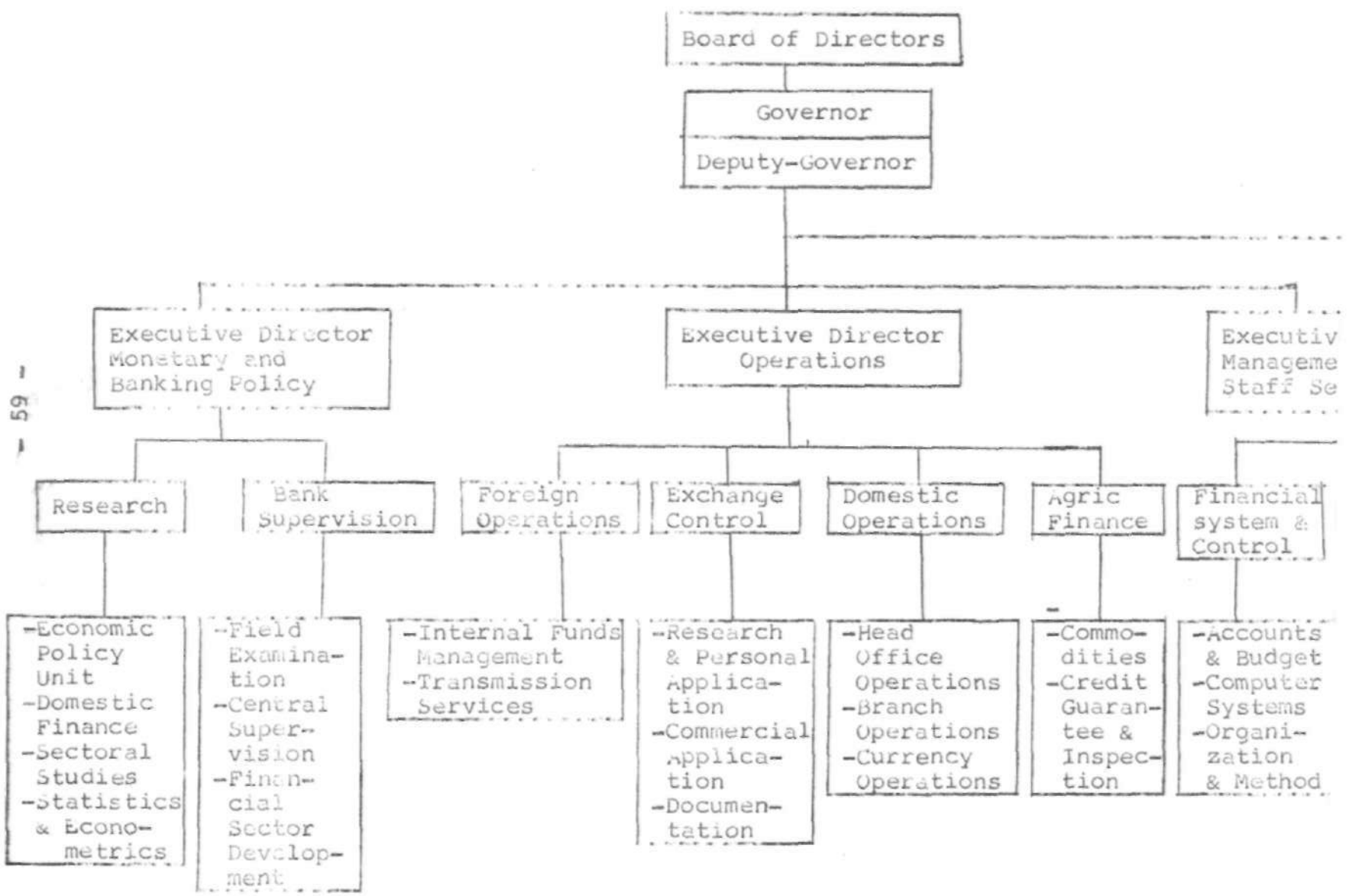
Nevertheless, the recommendations of Mr. Loynes finally culminated in the establishment of the Central Bank of Nigeria in 1958.

3.1 Organization of the CBN

The current organization structure of the CBN is illustrated by figure I below. At the top is the Board of Directors which is responsible for the policy and the general administration of the affairs and business of the Bank. The composition of the Board by the 1958 Ordinance was made up of a Governor (who was Chairman and Chief Executive), Deputy-Governor and five other directors who were part-time members. This set-up was however significantly changed in 1978 when the CBN was re-organized following the recommendations of the Financial System Review Committee (1976). The Board of the CBN now consists of thirteen members; Governor, Deputy Governor, three Executive Directors, and eight other part-time Directors.

Appointment to the Board is subject to several statutory conditions. The CBN Ordinance indicates that both the governor and his deputy should be persons of financial experience; and shall devote the whole of their professional experience to the service of the Bank, and shall not hold any office other than the one in the Bank. The part-time directors are required to be persons of recognized standing and experience in financial affairs and are statutorily required not to act as a delegate on the Board from any federal or state authority, or from any commercial, financial,

CHART I



Source: Central Bank of Nigeria, Lagos, Twenty Years of Central Banking in Nigeria 1959-79, P.49.

agricultural, industrial or other interests with which he may be or may have been connected.

It is further provided that a director shall hold office for three years and be eligible for re-appointment. Members of legislative houses, director or salaried official or shareholder of any licensed bank under the provisions of the Banking Ordinance or officers in the public service of the Federal or state governments are excluded from being appointed to the Board. Lastly, the 1958 Ordinance invested the power to appoint the Governor of the Bank and his deputy in the Governor-General. But since the fall of the first republic, these appointments were made by the Head of State during the military era and are presently being made by the President-in-council.

As Figure I shows, the CBN is divided into three broad divisions each of which is headed by an Executive Director. These divisions are further sub-divided into ten departments with departmental directors incharge of each. Each of these departments performs specialized functions in line with the broad outlines of policy and the day-to-day operations of the Bank. The Monetary and Banking Policy Division for example is responsible for and exercises the power to control and supervise the operations of all banks in the country. The Research Department of this division handles research and collection of national and international financial data with continuous systems analysis to provide information for management and policy decisions on which

the Bank's advisory function depend[6]. The division also advises on developments in monetary management and prepares and publishes valuable periodicals which now constitute the most regular, dependable and up-to-date sources of financial data in the country.

3.2 The Relationship Between CBN and the Commercial Banks

It is important to note that a central bank is conventionally only one of many institutions in a financial system except that it is an apex institution occupying the commanding heights of the system. It does not therefore operate in isolation but is dependent and interrelated with other financial institutions. Infact in most cases, specific laws and regulations are made to tie all other financial institutions to the central bank; and on the basis of this principle therefore, it can be said that there exists a definite relationship between the CBN and the commercial banks in the Nigerian banking system.

One of the traditional but important functions of a central bank is to act as a banker to other banks (bank of last resort). In performing this function, the CBN not only serves as a clearing house for cheque clearing by the commercial banks but also the banks can borrow from it and rediscount bills to meet their operational problems. The overall objective here is for the CBN to seek the co-operation of other banks in order to promote and maintain adequate and reasonable services to the public and ensure high standards of conduct and management through the banking system in pursuance of the national interest[7].

The CBN was also established to regulate and control the commercial banks. "The 1958 Ordinance gave the CBN the power to require the Commercial banks to maintain any given ratio between certain specified liquid assets and demand deposits and between these liquid assets and time and savings deposits"[8]. The CBN Amendment Act 1962, further strenghtened the control of the CBN over other banks by linking rates of interest charged on advances and other credit facilities by licensed banks to a minimum rediscount rate of the CBN subject to a stated minimum rate of interest in addition to further requiring other banks to hold specific liquid assets which were to include notes and coins, balances at CBN, net balances at other banks in Nigeria, treasury bills, in-land bills of exchange, promissory notes rediscounted at the Central Bank and money at call[9]. Furthermore, the regulatory powers of the CBN were further increased by the 1967-69 Amendments which laid emphasis on "the direct methods of controlling bank liquidity. In addition to strenghtening the variable liquid asset ratio technique, the CBN has been given new additions to its armoury of direct techniques of controlling bank liquidity"[10].

It is important to mention here that the statutory position of the CBN is not restricted to powers to regulate and control but also includes the power to compel compliance with its requests and regulations. There is also a provision for penalties for non-compliance. Thus, "each bank is statutorily required to furnish the CBN with information to

ensure compliance with liquidity ratios for example. Also each bank is subject to penalties for non-compliance with various aspects of the regulations: for example, the penalty for non-compliance with the indigenous loan requirement is ₦2,000[11].

3.3 CBN Relationship With the Government

Like other central banks in developing countries, the CBN did not evolve from a major commercial bank like the Bank of England but rather was established by government. Despite this background, the ordinance establishing the CBN is rather explicit on what is its expected relationship with government. This relationship is one whereby, the CBN is conceived as an independent arm of government. Thus, the Ordinance completely excludes government representation on the Board of the Bank; and even civil servants from the civil service of the Federal and States governments are excluded. In addition, the Ordinance empowers the CBN to independently pursue monetary and banking policies and other duties with little interferrence. In precise terms, the Ordinance provides that the Board of Directors of the Bank shall be responsible for the policy and general administration of the affairs and business of the Bank. What this means in effect is that the law does not recognize any direct relationship between the government and the Board of Directors of the CBN.

But from the practice of Central Banking, the CBN, is both banker and financial adviser to government; statutorily

responsible for the banking and foreign exchange transactions of the Federal government both internally and externally. It is empowered to receive and disburse Federal Government monies and keep accounts thereof without remuneration for its services. The Bank may also make temporary advances to the Federal Government in respect of temporary deficiencies of the budget revenue. However, the total amount of such advances outstanding at any time should not exceed 25% of the estimated recurrent budget revenue approved by the National Assembly for the fiscal year in which the advances are made. All such advances should be retired by the end of the fiscal year in which they are granted; otherwise the Bank is not allowed to grant further advances in any subsequent financial year until the outstanding obligations have been made good. The CBN is also entrusted with the issue and management of Federal government loans publicly issued in Nigeria upon such terms and conditions as may be agreed between the Federal Government and the Bank.

All the above responsibilities of the CBN imply an indirect and/or direct relationship with the government and its other agencies particularly the Federal Ministry of Finance. The constitutional functions of the Ministry of Finance is responsible for the collection and disbursement of all monies of government; and the formulation of mainly short-term fiscal and financial policies. The primary pre-occupation of the Ministry therefore is to meet government financial requirements for a given financial year. The

Central Bank in contrast, has to reconcile its obligations to government with its major long-term policies which are aimed at the overall long-term growth and development of the economy. These policies include the promotion of monetary stability, management of reserves, promotion of sound financial structure and the development of a money and capital market.

From every indication, this relationship between the CBN and the Ministry of Finance does possess in-built possibilities for conflict. Much as the the divergence of opinion on monetary policy between the CBN and government began to emerge as far back as 1966[12], an atmosphere of seemingly quiet co-operation still exists and there has hardly been any glaring dispute between the two for the supreme authority over monetary matters. This is not disregarding the fact that the CBN has come out on several occassions to say that while it is committed to policies that will promote the overall economic objectives of the country, it does not intend to abdicate its responsibility for monetary policy and the pursuit of its overall objectives.

Of particular interest in the CBN-Government relationship is the role of the Federal Minister of Finance[13]. It is not clear whether Federal Ministers of Finance do adequately perceive their responsibilities as political heads of the ministry and its relationship to the CBN. But what is clear is for the Minister to refer to the CBN as if it were just another arm of the Ministry of Finance, and as if it operated on his instructions. The impression thus created in budget

speeches (at least before 1966) was that the CBN operated on the instructions of the Minister of Finance[14]. It was in attempt to clarify the position that the 1968 CBN Amendment Decree specified that:

(1) The Board (of Directors of the Bank) shall keep the Commissioner of Finance informed of the monetary and banking policy pursued or intended to be pursued by the Central Bank.

(2) The Commissioner shall from time to time if he disagrees with the Board on the monetary and banking policy pursued or intended to be pursued by the Central Bank, so inform the Board of his disagreement thereto, and the Commissioner may submit his representation and that of the Central Bank on the disagreement to the Federal Executive Council.

(3) The Federal Executive Council may in writing, after considering the representation, direct the Central Bank as to the monetary and banking policy to be pursued and the direction shall be binding on the Board which shall forthwith take all steps necessary or expedient to give effect thereto[15].

The 1968 Amendment Decree also empowered the Minister of Finance to approve the opening of accounts for other persons in Nigeria, the holding and selling of shares/ debentures of any corporation/company. The Minister may also require the Federal Director of Audit to examine the accounts of the CBN. The Act also requires the CBN to

submit returns to the Ministry of Finance, in form of annual and monthly reports. All these provisions it must be added create avenues for an ambitious Minister of Finance to usurp the position of the Board of the CBN by attempting to dictate monetary policy pursued or intended to be pursued.

The possibility of this development with all its inherent dangers notwithstanding, this study subscribes to the belief that:

> If the relationship between the commissioner and the Governor and between their advisers is cordial and close, there would be no room for conflict. But conflict is bound to arise if the CBN reads and interprets its role and powers under the Decree in complete isolation, without reference to the powers equally conferred on the commissioner not only under the same decree but also under other equally binding laws and decrees. Both are dealing with the same variables, but one is more under pressures that are not only economic and monetary, but even more so, are also political and social, whereas the Central Bank, in its splendid 'cork-lined' structure, can afford to contemplate the longer term consequences of politically and socially inspired policies of the Commissioner[16].

There is no gainsaying that the circumstances of the relationship between the CBN and the Federal Ministry of

Finance have greatly influenced the types of policies currently embarked upon by the Bank. The extent of this influence would however be examined in the next chapter when we consider the various factors undermining the overall effectiveness of the CBN.

3.4 The Regulation of Commercial Banks

It is often argued that banking general "is one of the most closely regulated and price controlled industries in the world; capital structure, sectoral allocation of loans, liquidity ratio, and a host of other regulations which relate to prudential and credit control requirements are imposed by the monetary authrotities"[17]. In Nigeria, the history of commercial bank regulation is no doubt a recent phenomenon. The evolution of commercial banking was not immediately accompanied by regulation until the several unsavoury effects and tendencies capable of creating instability in the banking habit were noticed. Regulation was therefore only introduced in 1952 following the Paton Report of 1948. Thus the 1952 Ordinance for the regulation of the business of banking was enacted as a direct result of bank failures and irregularities; and the need for further guidance and support for African banking as was recommended by a World Bank Report.

The regulation, control and supervision of the banking industry in Nigeria is the responsibility of the CBN in as much as it is statutorily required to work in close consultation with the Federal Ministry of Finance. The Principal areas of control have been establishment conditions, capital, licensing, reserves and liquidity requirements.

The establishment of a commercial bank in Nigeria is itself regulated and controlled. Both the Companies Act (1968) and the Banking Act (1969) impose strict governmental regulations on the activities of Nigerian commercial banks. The companies Act makes a distinction between a Nigerian and a foreign owned company including banks. All banks operating in Nigeria must be locally incorporated and hence be Nigerian companies. Even foreign banking companies which before the Act were incorporated outside Nigeria were in respect of their Nigerian operations deemed to have become incorporated under the Act as a separate entity from the parent company incorporated overseas, and in whose name a place of business was established in Nigeria. "With the passing of the Banking Act in 1969 and the Securities and Exchange Commission Act in 1979, the conditions governing the establishment and operations of banking business became more clearly stated. Strict controls were imposed on granting of licence, opening and closing of branches, amalgamation, requirements on minimum paid-up capital, maintenance of reserve fund and certain other activities of the banks"[18].

The 1952 Ordinance allowed banking only by a company which in order to be registered must have a nominal capital of ₦50,000 and paid-up capital of at least half of that amount. Applications were made to the Financial Secretary who was empowered to pay special attention to the bank's liquidity ratio, paid-up capital and reserves. He was further authorized to withdraw the licence of any bank if its affairs

were conducted contrary to depositors' interests. The requirements were amended in the 1958 Ordinance which required the Federal Minister of Finance to consider applications in public interest while also classifying capital requirement into ₦25,000 for indigenous banks and ₦400,000 for the expatriate banks. Reference to nominal capital was also dropped. But with the 1967/69 Amendments, "instead of the former minimum paid-up capital of ₦400,000, an indigenous bank was to have a minimum of ₦700,000. Similarly, an expatriate bank is to have a minimum paid-up share capital of ₦1.5 million instead of merely giving the Minister as provided under the old law, a satisfactory undertaking to keep assets worth at least ₦500,000 within Nigeria at all times"[19]. Only a transitional period of six months was allowed to existing banks to comply with the new capital requirements.

The CBN is also statutorily empowered to control the reserves of commercial banks. The 1952 Ordinance required commercial banks to pay 20% of profits into a reserve fund before the payment of dividend and until the amount in reserve fund equal paid-up capital. Payment of dividend was also prohibited until capitalized expenditure had been written off. The 1958 Ordinance later increased this ratio to 25%. The 1967/69 Amendments in addition, required a transfer of 12½% of net profits to be made where the amount of reserve funds is equal or is in excess of the paid-up share capital. The CBN also has power to require commercial banks to maintain a ratio of 10-30% between paid-up capital

and statutory reserves on one hand and total deposits on the other.

Just as the CBN plays an important role in the licensing of commercial bank's, it is also of significant importance in the revocation of such licences. It is provided that the Federal Minister of Finance, on the recommendation of the CBN and with the approval of the Federal Executive Council, may revoke any licence granted to a bank as a separate authority to operate. The affected commercial bank is however entitled to notice so that it may make representations as to why its licence may not be revoked. In the same view, the CBN may take over the management of a commercial bank and in cases of bankruptcy, "where a licensed bank becomes unable to meet its obligations or suspends payments, the assets of such bank in the Federation shall be available to meet all deposit liabilities of the bank in the federation and such deposit liabilities shall have priority over all other liabilities of the bank"[20].

The effects of the above conditions on the formation and operations of commercial banks in Nigeria are quite obvious. In particular, it has become increasingly difficult for Nigerians to establish banks without some sort of government assistance or enter the banking industry. These conditions have however greatly reduced the possibility of banks failing due to undercapitalization and thus developed more public confidence in the banking system. They have also ensured the safety of bank deposits in addition to protecting the interest of depositors.

The liquidity of commercial banks is another area that is closely regulated and controlled. The 1952 Ordinance required commercial banks to maintain an adequate degree of liquidity. Proof of this was to be furnished to the Financial Secretary on request. Although the liquidity positions of banks were not clearly defined, a bank's licence could be revoked. The 1958 Ordinance however was more precise. Section 8 of the Ordinance required banks to maintain a holding of specified liquid assets not less than such amount as may be specified /by the CBN from time to time. It was an offence if a bank did not furnish information to the CBN about its liquidity position, or allow its liquid asset ratio to fall below the minimum rate specified, or grant advances without the CBN's prior approval if the liquid asset ratio is below the minimum specified. This definition of liquid assets was however changed by the 1962 Amendment which went further to give the CBN discretion in applying the liquid assets requirement and those assets that may be used by commercial banks in meeting this requirement. Of particular importance in this regard was the treatment of balances at other banks, overseas assets and CBN specification of what foreign assets could be treated as liquid assets.

The 1967/69 Banking Amendments in Nigeria further increased the scope of CBN control of bank liquidity. The changes introduced affected mainly the variable liquid assets ratio, variable cash reserve ratio, and supplementary reserve requirements such as special deposits and stabilization securities. The possible range of liquid assets was increased

to include a new type of public debt instrument, the Treasury Certificate; and all externally - held foreign assets were excluded from the portfolio of reserve-eligible assets. In addition, the CBN was empowered to vary both the composition of any specified liquid asset and the proportion of the different categories of assets that may from time to time be held by a commercial bank. The cash reserve ratio was a new development and for the first time, the CBN was empowered to require commercial banks to maintain a given ratio between cash reserves and specified classes of deposit laibilities. The application of this tool was discriminatory as the banking system was for this purpose classified into three categories in terms of size of deposits and higher cash reserve ratios were to be maintained in that order.

The new amendments also made provision for the CBN to require commercial banks to maintain, over and above the legal minimum cash and/or liquid assets, some additional reserves in the form of special deposits and stabilization securities. Special deposits were to be maintained by the commercial banks at the CBN Head Office and were expressed as a percentage of the total of any specified deposit laibilities or increase in deposit liabilities. Such deposits could not be treated as specified liquid assets for the purpose of satisfying the requirements of either the liquid asset ratio or the cash reserve ratio. The CBN has the discretion to charge interest which should not be more than one per cent below the Treasury Bill issue rate. Stabilization securities on the other hand, are issued at such rate of

interest and under such conditions of sale, amortization, negotiability and redemption as the Bank may deem appropriate for the purpose of maintaining monetary stability of the economy in Nigeria. In particular, the Bank is given the power to sell or place any such securities with banks by allocation, reserving the right to levy fines against recalcitrants and to prohibit such institutions from extending new loans and advances or from undertaking new investments[21].

It must be observed at this juncture that the control of commercial bank liquidity represents an indirect method of controlling bank credit which of course is always the aim of monetary policy. Thus all things being equal, "a reduction in the volume of commercial bank liquid assets is expected to force these banks into curtailing their credit operations while an increase is expected to produce the opposite effect"[22]. Apart from this, commercial banks in Nigeria are also subjected to direct control of their credit operations by the CBN. This is done through the fixing of the annual rate of expansion of commercial bank credit, sectoral allocation of bank credit, and fixing of the indigenous credit quota. Thus, the CBN is "empowered to fix ceilings not only on the volume of loans, advances and discounts outstanding at a commercial bank but also for the different categories of such loans, advances and discount"[23]. The Bank can also fix ceilings on increases in such loans, advances and credits within a specified future period of time.

It can be seen from the above that the control and regulation of each of the above areas of Commercial Bank operations in Nigeria requires a specific tool or combination of tools; and these have been used over the years. Furthermore, as can be seen, the regulation of commercial banks in Nigeria also involves government regulation particularly in terms of legislation as witnessed by the several amendments to the original Central Bank of Nigeria Ordinance, the 1968 Companies Act, and the Banking Act (1969); and the imposition of several other conditions that govern the banking business. In conjunction and supplementary to government regulation, the CBN also employs monetary policy tools at its disposal in the control of the behaviour of commercial banks operating in Nigeria.

The Bank has the following tools in its armoury:

(i) Variable discount rate, interest rate structure and bank charges;

(ii) Open market operations;

(iii) Variable liquid assets and liquidity ratio;

(iv) Moral suasion;

(v) Selective credit control;

(vi) Cash reserve requirements;

(vii) Special deposits; and

(viii) Stabilization securities[24].

To complement these tools, the CBN also issues annual credit guidelines or monetary policy circulars to commercial banks which contain specific directives to the banks in respect of their general operations as they affect the Nigerian economy.

The methods mentioned above have been applied singly or jointly at different times to achieve the prevailing objectives of the economy at such times. Some of them have however never been applied or are yet to be used. The question then that readily comes to mind is to what extent have these methods been effective in achieving the set targets and specific objectives of the Nigerian economy? This indeed is the subject that would be discussed in the next chapter.

FOOTNOTES

1. See the appendix for the full text of the regulations defining the duties of the West African Currency Board.

2. Nwankwo, G.O., Op. Cit., p.3.

3. J.L. Fisher, The Desirability and Practicability of Establishing a Central Bank in Nigeria as an Instrument for Promoting the Economic Development of the Country, Government Printer, Lagos, 1956, p.18.

4. Nwankwo, G.O., Op. cit., P.4.

5. Ibid, P.5.

6. Ibid, P.12.

7. Ibid, P.16.

8. Brown, C.V., Op. Cit, P.147.

9. Federal Republic of Nigeria, CBN (Amendment) Act 1962, Nos. 17 & 19.

10. Teriba, O., Op. Cit., P.49

11. Nwankwo, G.O., Op. Cit., P.17.

12. See CBN, Annual Report and Statement of Accounts 1966, Pp.13-14.

13. The words Commissioner and Minister have been used inter-changeably as they refer to the same office.

14. Brown, C.V., Op. Cit., Pp.143-144.

15. CBN Act (Amendment) (No.3) Decree, 1968, Clause 3.

16. Okigbo, P.N.C., Op. Cit., P.254.

17. Asabia, S.O., "Prospects of Commercial Banking in Nigeria", The Nigerian Trade Journal, Vol.28, No.4, 1981, P.21.

18. Adeniyi, O.A., Op. cit., P.19.

19. Teriba, O., op. cit., P.59.

20. The Central Bank of Nigeria Act (Amendment) No.3 Decree 1968, Clause 37.

21. Teriba, O., op. cit., P.53.

22. Ibid, P.49.

23. Ibid, P.55.

24. Central Bank of Nigeria, "Memo to the Financial System Review Committee" (Mimeograph), 1st June, 1976, P.91.

CHAPTER IV

EVALUATION OF METHODS FOR REGULATING COMMERCIAL BANKS

4.1 Objectives of Central Bank Policy

As pointed out earlier, the regulation of commercial banks is usually aimed at achieving specific economic objectives. But one of the most difficult tasks for regulatory authorities is the identification of objectives of policy. This is because, monetary and banking regulations are also expressions of monetary policy since they affect the volume of money in the economy. But the distinction between them exists in the sense that commercial bank regulations are often rigid as they may not be easily amendable to changes in economic conditions; and their objectives are often too broad and hence not clearly defined. Monetary policy on the other hand, is clearly recognized with precise objectives. Because of the circumstances of the economy and our level of development, the above distinction cannot be easily made and is not absolutely necessary. We can thus consider the specific objectives of monetary policy jointly with the over-all objectives of regulation authorities and their instruments, moreover they reinforce and complement each other.

For the purposes of this study, the objectives of the regulatory authorities are examined from three viewpoints. One is the broad national objectives. This is so because as an integral part of the Nigerian

economy, the banking industry also has to contribute to their achievement. We would also consider the broad objectives of the commercial banking system and the Central Bank; and lastly the specific objectives of the regulation instruments. The National objectives as annunciated by the Second National Development Plan and re-affirmed in the Third Plan are to establish Nigeria firmly as:-

i) a united, strong and self-reliant nation;

ii) a great and dynamic economy;

iii) a just and egalitarian society;

iv) a land of bright and full opportunities for all citizens; and

v) a free and democratic society[1].

These objectives much as they are broad and long-term in nature, they no doubt provide the nation with guide-posts in its quest for social justice, economic advancement and political stability. How effective regulation techniques have been towards the achievement of these goals is a subject that will soon be considered.

For the commercial banks, the following objectives are pertinent and based on the Report of the Financial System Review Committee (1976): facilitate the transformation of the rural environment by rapid expansion of banking facilities and services and banking habit in the rural and near-rural communities. Undertake more medium and long-term lending to the extent consistent with banking prudence. They should identify fully with Nigerian aspirations by financing those economic programmes of national priority; and lastly use a significant part of

their profits to improve the quality of the services they offer[2]. These objectives are aimed at achieving an effective banking system which can help in the mobilization of rural savings, bring the banks in line with Nigerian aspirations and control in ownership and management thus avoiding the banking institutions from being manipulated to the disadvantage of the Nigerian economy.

The objectives of the Central Bank of Nigeria are also worth further mentioning. These are, to issue legal tender currency in Nigeria, maintain external reserves in order to safeguard the international value of that currency, promote monetary stability and a sound financial structure in Nigeria, and act as financial adviser to the Federal Government. The importance of these objectives can be seen from the need for rapid economic development of Nigeria, increasing the banking habit and level of monetization in the economy.

The monetary regulation and control objectives of the Bank can be dervied from the above broad objects set for it by the Act establishing it. These are relative stability of domestic prices, equilibrium in the country's international payments position, and rapid and sustainable rate of economic growth; and a high rate of employment. This later objective has not been emphasized in the Nigerian context. One important thing to realize however is that emphasis on these objectives and their pursuit has varied from time to time, depending on the prevailing economic circumstances or conditions. It is only in this

regard that we can appreciate the changes that have occurred in the objectives of the policies of the Central Bank since its inception.

In the immediate period following its establishment, particularly between 1959-62, the major objective of the Central Bank of Nigeria policy was that of maintenance of a strong currency i.e. the creation of a national currency that would be as strong and as respected as the one it was replacing. The Bank's position during this time therefore was that of the issuer of currency and currency management. It can therefore be said that the first and foremost objective of the Central Bank of Nigeria as was even conceived by the government was the issue of currency and its management in Nigeria so as to command respect and confidence both at home and abroad.

However, with the launching of the First National Development Plan 1962-68, and the shortfall in revenue accruing to government for its execution, the lack of public and private savings and the fact that even the anticipated external finance was not forthcoming, the Central Bank of Nigeria was forced to move out of its conservative stance to adopt a more dynamic role for the development of the Nigerian economy. Furthermore, the outbreak of the civil war gave rise to increased government expenditure and deficit financing by government became the major objective at that time to which the Central Bank of Nigeria responded. Objective of policy which initially was for the execution of the First Plan

shifted with the outbreak of the war to successful prosecution of the war and the raising of finance for that purpose.

During the period under review, some of the immediate objectives after the war were the reduction of the inflationary pressures, balance of payments which had deteriorated before and after the war; increasing government revenue as well as reducing its reliance on the banking system. Monetary policy thus centred on the redirection of credit to the productive sectors of the economy by way of guidelines, and ceilings on loans and advances.

By the second half of the 1970s, because of revenues accruing from the oil sector, revenue to government was no longer an objective and the government depended less on the banking system. The balance of payments position also significantly improved. But as a result of increased government spending of oil revenues, decrease in its borrowing, the Udoji Awards and proceeds from indigenization, the banking system started to experience unprecedented levels of excess liquidity. Excess liquidity thus became a major policy objective together with the containment of inflationary pressures. The policy emphasis thus shifted to the control and direction of commercial bank credit with a view to stimulating the output of goods and services and increasing the levels of savings and investment in the economy.

It has been shown that the operations and objectives of the Central Bank in a developing economy like Nigeria's are aimed at more than the control and

regulation of bank credit. They include the development of a financial system conducive to regulation and eradicating the defects in our monetary arrangements since "the absence of a commercial banking system which is predominantly indigenous, which would ensure an adequate and flexible capital market dictates that the Central Bank of Nigerian cannot remain aloof in the task of expanding capital formation as demanded by the new plan"[3]. From the above therefore it can be reiterated that the role of the Central Bank cannot be restricted to that of a regulator in Nigeria like several other developing countries. This is because whereas the monetary and financial systems of most developed countries were already developed when the central banks were established, these are still to evolve in the less developed countries. In addition, the institutions to be controlled and the credit system to be regulated have still to evolve to necessitate a regulator. Thus, the role of the Central Bank of Nigeria has to be conceived in the context of evolving a sound financial infrastructure required for rapid economic development. Indeed, the Central Bank of Nigeria has from our experience taken the lead in evolving some of these institutions and instruments that are essential for the efficient mobilization of savings and allocation of resources that is consistent with development objectives.

As is evident, these objectives have been pursued simultaneously rather than separately and whereas some of them may be mutually re-inforcing, most of them are

by definition incongenial and incompatible. In the first instance, measures aimed at controlling inflationary pressures may as well lead to favourable developments in the balance of payments; and similarly, economic growth and development is apparently compatible to the objective of full potential output. On the other hand, the pursuit of economic growth creates monetary instability and inflation through its effects on aggregate demand and investment. In addition, policies aimed at correcting a balance of payments deficit may only defeat the full-potential output objective. In this regard therefore, the pursuit of monetary policy objectives and its exact effects make the task difficult for the regulatory authorities.

4.2 Evaluation of Methods Taken to Achieve Objectives.

It must be realized that it is one thing to have defined objectives and regulatory instruments and another to effectively apply them. To effectively apply regulatory instruments, the monetary authorities must have knowledge of their strength to ensure that they are applied in correct dosages. Similarly, the authorities also need know to a large extent how soon the effects would be felt in order to prescribe the appropriate timing of policy. The question is, does the Central Bank of Nigeria actually understand the timing and strength of its policy instruments? Furthermore, is there any evidence that the application of instruments has been relatively unpredicatble? It is worth emphasizing that in theory, the strength of regulation

policies is determined by the elasticities of the functional relations in the economic system.

The above apart, it is the objective of this study to consider in this section how the Central Bank of Nigeria has applied each of the instruments in its armoury, over time with particular emphasis on the period covered by this study; and whether these instruments or methods have actually achieved the desired objectives or produced the desired impact. It would also be our interest to see whether and how the instruments have affected the behaviour patterns of the commercial banks. Another thing that we would like to find out is if the Central Bank of Nigeria has been able to achieve the overall objectives set for it. This is in the sense that some of the objectives considered above are so fundamental that none of the instruments is capable of directly achieving them.

4.2.1 Open Market Operations.

Although open market operations is one of the techniques of control at the disposal of the Central Bank of Nigeria, there is no evidence that it has ever been used. Open market operations as a technique of monetary control is used by the Central Bank with a view to influencing and regulating the primary reserves of commercial banks which constitute the basis of their power to creat demand deposits or their credit granting potentialities. The tool is particularly useful in economies where financial

markets [illegible] are highly developed, fully integrated and supplied with a large variety of market instruments. Thus the primary objective of open market operations is "monetary expansion through additional reserves to reduce shortages, or monetary contraction to reduce surpluses capable of undesirable effects on money supply"[4]. Open market operations therefore serve to influence interest rates, change the cash reserve of commercial banks and hence their ability to grant credit, and directly affect the money supply as it affords the public the alternative of holding cash balances or the securities involved. It is on this basis or connection that open market operations by the central bank is capable of absorption or release of bank reserves, influencing

of interest rates and influencing of the structure of interest rates.

The tool of open market operations from the above is not of ready and useful application in economies with unsophisticated financial systems and undeveloped and poorly integrated financial markets. Thus, because of the narrow market for securities, small flow of savings available for investment and the incomplete pattern of government securities available to the public coupled with the fears of prospective investors with respect to the stability and liquidity of the market, open market operations is of little relevance to Nigeria. Indeed the technique in its true sense has never been applied

in Nigeria by the Central Bank of Nigeria. This is because even though the Central Bank of Nigeria has been engaged in such activity as the direct sales and purchase of government securities and stocks, this action merely represents its role as a fiscal agent than open market operations in so far as the Bank has no control over them. For the action to constitute open market operations, it should first of all have to be initiated by the Central Bank of Nigeria and aimed at absorbing excess liquidity funds in the money and capital markets, maintenance of bank reserves at appropriate levels for the purposes of monetary policy, expansion of the market in government securities as well as preservation of orderly conditions in the market.

Perhaps it is the effects of open market operations in the absence of the necessary institutional framework that has restrained the Central Bank of Nigeria from experimenting with the tool. Because of the narrowness of the market for securities, large purchases and sales of securities by the Central Bank of Nigeria are likely to stimulate large price fluctuations. In fact open market operations in a financial system like ours in conditions of high excess liquidity, large sales of securities would be required to impinge seriously on commercial banks' liquidity ratios or positions. Huge sales would not only affect security prices but also government debt; and very often, the monetary authorities may end up as net buyers even though they started as sellers. Central Bank

of Nigeria subscriptions and holdings of Treasury Bills, Treasury Certificates, Development Stocks vindicate this fact.

In any case, even if the financial institutional constraints are removed, open market operations because of its general and indirect effects would have limited if any usefulness at all given the economic circumstances of Nigeria, and in particular, the need to stimulate economic growth without abdicating the objective of price stabilization. It remains therefore to be said that the Central Bank of Nigeria has been armed with a weapon which is only effective and applicable in developed economies but of no consequence for its capacity to regulate commercial banks in Nigeria.

4.2.2. Moral Suasion

Moral Suasion as a method of commercial bank regulation has been available to the Central Bank of Nigeria since its inception. In general, this is the exposition by the monetary authority of the rationale of its policy measures. It thus consists of "oral and written statements, published reports, testimony before governmental bodies, and speeches before members of the public by officials of the monetary authority endeavouring to explain current monetary policy"[5]. But as a method of regulation, moral suasion rather than being an explanation of measures being carried out by the Central Bank, is an exercise of pressure upon the commercial banks through exhortations. It thus consists of specific requests by

the Central Bank of Nigeria to the commercial banks that they voluntarily adopt certain restrictive measures which may be quantitative or qualitative in the interest of the economy or in a manner that enhances the achievement of a given set of economic objectives.

The Central Bank of Nigeria has heavily relied on this weapon in attempt to get the commercial banks behave correctly. The application of moral suasion is manifested in the various guidelines to the commercial banks. The major objectives of these guidelines has been to ensure the expansion and growth of banking facilities through the opening of rural branches, increased credit to the productive and favoured sectors in order to encourage local productions, correct and increase the inadequate credit to Nigerians and participation in medium-term and long-term lending among others.

Most of the moral suasion is done through the Bankers' Committee which provides a forum for the Central Bank of Nigeria and the leaders of the banking community including unofficial and formal meeting. The objective of these meetings is the development of mutual confidence and respect between the Central Bank of Nigeria and other banks. For instance, during every address at the Annual Dinner of the Institute of Bankers since the indigenization policy, "every Governor of the Central Bank has used the occasion to urge the banks to finance industry and agriculture and to lend money to Nigerians to enable them buy foreign businesses under the indigenization exercise"[6].

Moral suasion as a method of regulation has not been very effective in Nigeria. Most important among the factors that account for this is the dual loyalty of the dominant foreign commercial banks both before indigenization and with the advent of Nigerian ownership. This is because, "their philosophy of bank credit, sympathy for the foreign economic policies of their countries of origin and home office directives transcended the persuasions of the host government and the Central Bank"[7]. Foreign control of the management of the dominant commercial banks accounts for this dual loyalty. This underscores the believe that moral suasion is likely to be more successful where the commercial banks have fully identified with the overall objectives of the host economy. Besides, the number of principal commercial banks in Nigeria is so small that their persuasion need not have been difficult since moral suasion is more effective where the number of institutions to be persuaded is very small. This is more the reason why moral suasion has been least feasible in the United States where the Federal Reserve Bank has to be suasive with thousands of independent commercial banks.

The failure to provide for sanctions which commercial banks should look upon and expect as consequence of failure to be persuaded has also gone a long way to weaken the method of moral suasion in regulating the behaviour of commercial banks in Nigeria. This is because, sanctions would have greatly influenced and enhanced the bargaining position of the Central Bank of Nigeria vis-a-vis the

commercial banks it was persuading. This point is of relevance if we consider the response of commercial banks to appeals from the Central Bank of Nigeria now that they are aware that the Bank may recourse to statutory measures if they should fail to comply or be persuaded.

The non-specification in appeals and duration of the period for which moral suasion by the Central Bank of Nigeria is intended has created opportunity for opposition to build against the method and this has rendered it ineffective. Most of the suasions have been for the commercial banks to adopt long-term measures in aid of the control of inflation, and the development and growth of the Nigerian economy. These suasions are therefore too broad and the nature of the occasion for their application is hardly right. The moral suasion weapon is known to be more effective in times of war or national emergencies. This appears to explain why the banks co-operated during the civil war but have thereafter come to think less of their obligations.

4.2.3. Variable Discount Rate, Interest Rate Structure and Bank Charges.

One of the principal activities of the commercial banks is lending the funds that they borrow and earning the difference between the lower rate they pay and the higher rate they receive. Banks also engage in holding of Treasury Bills and other short-term government bonds which indeed is another major activity. It is on their ability to borrow and the role of the Central Bank as a lender of last resort that the rediscount rate as a method

of regulation and control derives its importance.

Effective discount policy however requires that the discount rate be related to other market rates and remain in touch with them. Despite this, "a given change in discount rates may in some circumstance express a shift in direction or intensity of policy. In other circumstances however, a change may merely represent a technical adjustment designed to maintain the existing degree of restraint or ease, when variations in the strength of credit demands have caused market rates to move substantially above or below the prevailing discount rate"[8]. The bank rate must therefore lead in the adjustment of market rates at least in the short-term; and particularly interest rates charged by the banks are anchored to it.

In Nigeria, the Minimum Rediscount Rate (MRR) of the Central Bank of Nigeria is the rate to which all other charges for loans tend to adjust. But due to "the dependent nature of the Nigerian colonial economy, up to the 1960s, interest rate structure in Nigeria adjusted to the rediscount rate of the Bank of England"[9]. It thus reflected the credit and monetary conditions of the London Market. It was to correct this situation that the 1962 Central Bank of Nigeria Act Amendments linked interest rates of commercial banks operating in Nigeria to the MRR of the Central Bank of Nigeria, and indeed this was the first step in domiciling the control and regulation of our deposits. This process was however

completed by the Banking Decree 1969 which apart from giving the CBN power to prescribe the minimum and maximum rates chargeable by each bank, extended the power to regulate interest rates of commercial banks to cover all rates.

The CBN has been making use of the discount rate and interest rate weapon for some time as indicated above. This is evidenced by either increases or decreases in the discount rate and other interest rates. The MRR itself was changed three times between 1962-68. "In January 1963, when it was reduced by ½ per cent to 4 per cent; in December 1964 when it was raised by 1 per cent to 5 per cent; and in May 1968 when it was reduced by ½ per cent to 4½ per cent"[10]. Tables 4.1 - 4.3 show the changes that have occurred in the structure of interest rates during the period studied.

Changes occurred in the structure of interest rates in April 1975 when in view of the overall high liquidity in the economy, lower interest rates were approved. Accordingly, the MRR was reduced by 1% from 4½% to 3½%. Produce Paper Rediscount Rate was also reduced from 6% to 4½%. The Treasury Bills Rate was reduced to 2½% from 4%. The changes also affected the minimum and maximum lending rates which were reduced from 7% to 6% and from 12% to 9% respectively. On the other hand, the minimum deposit rate was raised to 4% from 3% and the maximum limit which had formerly been at 6% scrapped.

TABLE 4.1

Interest Rate Structure 1 April, 1975

	Rates up to 31st March 1975 Per cent	Rates from 1st April 1975 Per cent
(a) Minimum Rediscount Rate	4½	3½
(b) Produce Paper Discount Rate (Marketing Board)	6	4½
(c) Treasury Bills	4	2½
(d) One-Year Treasury Certificate	4½	(To be retired as they mature)
(e) Two-Year Treasury Certificate	$4\frac{5}{8}$	(To be retired as they mature)
(f) Lending Rates		
(i) Minimum	7	6
(ii) Maximum	12	9
(g) Deposit Rates		
(i) Minimum	3	4
(ii) Maximum	6	No maximum

Source: First Report of the Anti-Inflation Task Force, October 1975, P.26.

TABLE 4.2

Interest Rate Structure 1 April 1977

	Before April 1977 Per cent	1st April 1977 Per cent
Minimum Rediscount Rate	3½	4
Treasury Bills Rate	2½	3
One-Year Treasury Certificates	3	3½
Two-Year Treasury Certificates	$3\frac{1}{8}$	$3\frac{5}{8}$
Produce Bill Rate	4½	5
Stabilization Securities	-	4½
Deposit Rates		
(i) Savings (Minimum)	4	4
(ii) Time (Minimum)	Negotiable	3
(iii) Federal Savings Bank	5	5
Lending Rates		
(i) Minimum	6	6
(ii) Maximum	10	10

Source: Central Bank of Nigeria, Lagos, Monetary Policy, Circular No.9.

TABLE 4.3

Interest Rate Structure, 1980

	Interest Rates (%)
(i) Minimum Rediscount Rate	6
(ii) Treasury Bill Issue Rate	5
(iii) Treasury Certificate (1 Year)	5½
(iv) Treasury Certificate (2 Year)	6
(v) Federal Government Stock	7–8
4 - 8 Years maturity	7
9 - 14 Years maturity	7½
15 - 20 Years maturity	7½
21 - 25 Years mathrity	8
(vi) Deposit Rates (Commercial Banks)	
Savings	6
Time Deposits with 7 days notice	5
Time Deposits for one month	5½
Time Deposits for 1–3 months	5½
Time Deposits for 3–6 months	6
Time Deposits for 6–12 months	6¼
Time Deposits for over 12 months	6½
(vii) Lending Rates:	
Minimum	7½
Maximum	11½
(a) Preferred sectors maximum	9½
(b) Less Preferred sectors maximum	11½
(c) Agricultural Credit Guarantee Scheme	5–6
(d) Residential Housing Costing not more than ₦100,000	6
(e) Agricultural Production	6
(viii) Specialized Institutions:	
(a) Federal Savings Bank - Savings Deposits Rate	6
(b) Nigerian Ind. Dev. Bank (lending Rates)	8½–11
(c) Nigerian Bank for Commerce & Industry (lending Rates)	8½–11
(d) Nigerian Agric. Bank Lending Rates for:	
Agricultural Production	6
Agricultural Commodities Marketing	8–11
(e) Federal Mortage Bank - Savings Rate	6–7
Lending Rates	6–11
(i) Residential Housing	6
(ii) Commercial Property	7–11

Source: Central Bank of Nigeria, Annual Report and Statement of Accounts, 1981, P.9.

With the inflationary situation getting to a critical level, a Task Force was appointed which recommended the use of discriminatory rates through a flexible interest structure such that loans for the non-directly productive sectors should attract higher interest rates than loans for the productive sector. In the 1977/78 Budget, the interest rate structure was again altered. The MRR and Treasury Bills Rate were raised by ½% from 3½% and 2½% to 4% and 3% respectively. Similarly,the Produce Bill Rate was raised from 4½ to 5%. A new instrument, stabilization Securities was also introduced with an interest rate of 4½%. The policy objective of these changes was mainly to curb the inflationary pressures prevailing in the economy.

The interests structure was further used in the 1978/79 financial year with a view to "promoting savings, checking inflation, improve resource allocation, encourage domestic non-bank financial institutions to buy government bonds, to finance development projects and attract foreign investment"[11]. Accordingly, the MRR was raised from 4% to 5%. The Treasury Bill Rate was also increased by one percentage point to 4%. Interest on government stocks were classified and all minimum deposit rates were increased by between one-half and two percentage points. The minimum and maximum lending rates for the less preferred sectors were raised to 7% and 11% respectively while interest rates for the preferred sectors of manufacturing, agriculture, mining, building and construction were put

at a maximum of 9% - one percentage point higher. The Agricultural Credit Guarantee Scheme, Residential Housing and Agricultural Production were to attract interest rates of between 4 - 6% and 6% respectively.

Yet, a general upward revision of all interest rates by one percentage point was introduced in April 1980. This structure is given by Table 4.3; and as it depicts, the range of lending rates for the preferred sectors and sub-sectors for loans maturing within three years is 7½ - 9½% while loans to these sectors maturing after three years could carry up to a maximum of 11%.

Apart from changing the structure of interest rates, the CBN also regulates and controls other bank charges. In particular, it requires banks to use only the Reducing Balance Method in calculating interest charges on loans repayable in agreed instalments. "The use of any other method such as the Discount Method of Simple Interest (Straight Line) method for such loans results in charging more than the contracted rates and would amount to a breach of Central Bank's directives on interest charges"[12]. Interest on savings accounts are required to be calculated on the balance existing on the customer's account on the 15th of each month. The CBN also requires that loans for residential building construction shall be for a minimum of 15 years.

Although the Central Bank of Nigeria as we have shown above has been applying the interest rate weapon for the

purposes of regulation, it remains to be seen whether the method is effective and desirable. To begin with, the various changes that have occurred in the Discount rate have been to say the least of little significance. This is primarily because, with the backwardness of the economy, the responsiveness of private demand for bank credit to changes in interest rates has been low. While this may owe to the high level of internal financing among private enterprises, recent studies[13] on the demand for money in the Nigerian economy indicate an interest elasticity of demand for money so low and insignificant as to be close to zero. This means that changes in interest rates are hardly likely to be decisive in investors' plans and decisions to invest; as what is important for the Nigerian investor is not as much as the rate of interest but whether or not credit would be available at all. As such, the terms on which credit would be available to a prospective Nigerian investor are haraly of any significance and infact do not matter.

The ineffectiveness of the rediscount rate as a regulatory technique is further accounted for by the substantial increases in commercial bank liquidity both as a result of oil revenue, government deficit financing and the level of monetization following the creation of the Federation Account by the 1979 Constitution. With the Federation Account and the Revenue Allocation Formula, all federally accrued revenues are statutorily shared out to the States. The Federal Government cannot therefore chose as to whether

these should be monetised and in what proportions. The State Governments variously collect their allocations which are then expended as they deem fit. Added to this is the fact that the increased creation of development banking institutions like Nigerian Bank for Commerce and Industry, Nigerian Industrial Development Bank, and the Nigerian Agricultural and Co-operative Bank under government sponsorship have undermined the reliance of the private sector on loans from the commercial banks.

Evidence exists that the commercial banks have for several reasons resisted the interest rate structure of the Central Bank of Nigeria. One of these is the liquidity they experience from the limited or lack of outlets for investment of their funds. Secondly, increases in interest rates payable on Treasury Bills and other obligations as contained in the structure have been inadequate to compensate them for the high rates they are required to pay on deposit accounts. This is evidenced by the fact that the banks in observing the range of interest rates, tend to apply the maximum rates within the range. The consequences of the above are the frustration of Central Bank of Nigeria efforts towards the development of banking habit among small savers; and the high cost of bank credit which investors or manufacturers often pass to their consumers through higher prices.

But the Central Bank of Nigeria itself has not help matters as it is apparent that its application of the

interest rate weapon is inconsistent with its policy objectives. "Given the high rate of inflation, rather than promote savings, check inflation, improve resource allocation, attract foreign investment and encourage non-bank financial institutions to buy government bonds, the negative interest-rate structure has surely done the contrary. It has certainly encouraged capital flight from the country in quest of higher interest earnings overseas and it certainly has not encouraged non-bank financial institutions to invest in government bonds. In a most recent issue of such bonds, the Central Bank took up as much as 92 per cent of the total issue in its capacity as the underwriter of government bonds"[14]. It therefore remains to be said that the developments highlighted above have indeed resulted in the impairment of the efficacy of the interest rate structure as an instrument of commercial bank regulation and control. Nonetheless, the method still serves a useful purpose - that of an indicator of the direction of monetary policy and the attitude of the monetary authorities to general developments in the Nigerian economy.

4.2.4. Cash Reserve Requirements

As mentioned elsewhere in this study, the Central Bank of Nigeria is empowered to require commercial banks to maintain a given minimum amount of cash deposits at its Head Office in Lagos; which deposits are excluded from the liquid assets of the banks for fulfilling

statutory liquidity requirements. A variable cash reserve ratio like this in a country without a developed money and capital market which render open market operations ineffective, is an effective regulatory instrument and a close substitute to the technique of open market operations. When the cash reserve ratio is changed, an "immediate and direct influence is exerted on funds available for bank credit - a high ratio reduces the availability of bank funds while a low ratio has the opposite effect"[15].

The cash reserve ratio is expressed as a ratio of total demand deposits plus time deposits on which a commercial bank pays its depositors interest of less than 2½% per annum. The stipulated cash reserve vary as ratios are differentially prescribed. Thus for this purpose, commercial banks are categorized into four classes depending on the size of their deposit liabilities. Class A banks are those with deposits of ₦300 million or more, class B are those with deposits of ₦100 million or more but less than ₦300 million. Class C on the other hand consists of commercial banks with deposits of ₦30 million or more but less than ₦100 million while those banks with deposits less than ₦30 million constitute class D.

TABLE 4.4

Changes in the Minimum Cash Requirement for Nigerian Commercial Banks.

Category of Bank	Amount of Deposit Liabilities	Required Minimum Cash Reserve Ratio (%)		
		Up to March 31, 1979	April 1, 1979	April 1, 1980
A	₦300 million and over	12.5	6.25	5.0
B	₦100 million or more but less than ₦300m	10.0	5.0	4.0
C	₦30 million or more but less than ₦100m	7.0	3.5	3.0
D	Less than ₦30 million	5.0	2.5	2.0

Source: Central Bank of Nigeria, various publications.

Table 4.4 depicts the changes that have been made in the cash reserve ratio. There is no gainsaying that variation of the method has been downward. This may as well owe to the reduction in the high excess liquidity of the commercial banks. The technique was infact first applied in 1976 with a view to mopping up and containing the high liquidity positions of the banks. Thus with significant drop in the level of liquidity, the CBN has continued to reduce the ratio first by half in 1979 and between 0.5% and 1.25% in 1980. While the decrease has been rationalized in terms of the liquidity positions of the commercial banks, it appears to be a contradiction of policy objectives during the period since the effort to contain the credit operations of the banks in attempt

to reduce the inflationary pressures has been a major objective. Therefore, the reduction appears to only weaken rather than maintain monetary stability.

One important thing to note is the fact that this technique is discriminatory. "A uniform ratio might penalize the small banks while at the same time it may not bring the desired effect unless extreme ratios have been adopted"[16]. Thus a uniform application of the cash ratio to all banks alike irrespective of size bears the mark of inflexibility and would by impinging differently on banks impart unfairness into the banking system. Nevertheless, one percieved weakness of the weapon in this regard is the concentration on deposit liabilities. It could be very effective if it is also applied on bank assets or other parameter. Afterall it is common knowledge that "commercial banks in Nigeria differ also in terms of assets structure, capitalization, operational experience, geographical concentration and nationality of equity capital. It is therefore important that all these factors need be taken into account before arriving at any categorization of the banks for the basis of reserve requirements"[17].

In any case, the effectiveness of the cash reserve ratio depends on the application and co-ordination of other regulation methods as it is only capable of achieving very little on its own. Thus any variation in the cash ratio not accompanied by appropriate actions like open market operations, variation in the liquid asset ratio,

may lead to a change in the distribution of commerial banks' assets as between bills and cash, rather than a shift in their overall liquidity position. This is because of a possible trade-off of some assets to meet the cash reserve requirement.

4.2.5. Stabilization Securities

The power to use stabilization securities as an instrument of regulation and control is granted under the 1968 CBN Amendment Decree; these being its own securities which can "be issued at such rate of interest and under such conditions of maturity, amortization, negotiability and redemption as the Bank may deem appropriate"[18]. Under the Decree, the CbN can sell to, allocate to, or repurchase from any banking institution. It can redeem or amortize the securities. Infact these securities are non-negotiable, non-transferable, and non-eligible for statutory liquidity ratios.

The major objective of this method is the maintenance of monetary stability. It is indeed a very strong weapon since the sanctions for non-compliance are severe. To begin with, the banking institutions are under law obliged to accept whatever volume of issue is allocated to them. Where they fail, or refuse to accept or buy, the CBN is empowered to prohibit them from extending new loans and advances and from undertaking new investments until full compliance with the directive has been obtained. The CBN may also under the law levy fines not exceeding ₦100 against the institution for every day during the period

which the default continues.

Despite the fact that this weapon was acquired in 1968, and even in the face of high inflationary pressures with the commercial banks using their excess liquidity positions to further worsen the situation, stabilization securities as a regulation technique were not applied until April, 1976. In application, stabilization securities are based on increases in a bank's savings deposits of individual savings accounts of not more than ₦20,000 each. Thus in the 1976 application, they were based on increases in each bank's savings deposits over the level outstanding on 31st March 1976, and attracted an interest rate of 4% per annum. The interest rate of issue was however raised to 4½% in 1977 with a view to encouraging banks to mobilize savings.

One other important aspect of this method is its use as a money market instrument; they have been issued since 1976 to mop up idle cash balances of participating banks. Such participation is mandatory for banks with savings deposits of ₦50 million and above. They are required to invest 50% of the increase in savings deposits over the level in the preceding year in the securities. An interest rate of 5½% per annum is paid, while the banks are required to pay 5% on savings deposits.

There is no doubt that the power to issue stabilization securities and conduct what looks like open market operations without necessarily going through the market and depending on market forces to determine their interest

rate given the CBN overcomes all constraints associated with them in the circumstances of the Nigerian economy. Moreover, since financial institutions have no choice but to comply, the technique is as good as open market operations and therefore well suited and of much relevance to a developing economy like ours. But despite its application, the major objective of monetary stability is yet to be realized. One of the reasons for its failure is the increased monetization of oil revenue by the Federal Government. The resentment of the commercial banks has also rendered the instrument ineffective; and this is re-inforced by their tendency to discourage potential savers wishing to open savings account deposits. The instrument would also have been more effective if other investors were permitted to purchase the securities rather than their being restricted to the commercial banks. This indeed would not only have diffused their monetary impact but also where there is a good response, significantly reduce money supply particularly during times of inflationary pressures.

4.2.6. Variable Liquid Assets and Liquidity Ratio.

The Central Bank of Nigeria has power to prescribe the liquidity requirement for all commercial banks and also vary the composition of the liquid assets. These two instruments represent attempts at the direct control of commercial bank liquidity which in itself entails an indirect control of bank credit as the ultimate aim of

policy. The efficacy of this method notwithstanding, it is yet to be meaningfully applied.

Specified liquid assets comprise notes and coins which are legal tender in Nigeria, balances at CBN and any licensed bank in Nigeria, Money at call in Nigeria, Treasury Bills and Certificates issued by the Federal Government of Nigeria, inland bills of exchange and promissory notes rediscountable at the CBN. These should together constitute not less than 40% of each bank's portfolio of the specified liquid assets during any month. The CBN has power to vary both the composition and proportion of these specified liquid assets.

The liquidity ratio was specified at 30% under the 1958 Ordinance and was reduced to 25% under the 1962 Amendment and has never been altered again to date. Apart from this, it is important to add too that the ratio between types of deposits has also not been varied. What has only happened in effect is the variation in the composition of liquid assets and the reduction in the external component in 1962 and its final abolition in 1966. But the most important thing about this method is the creation of a government securities market as an enhancement of one of the policy objective - the creation of a local money market which provides a suitable outlet for the investment of funds in a manner to satisfy the needs for liquidity and earnings by the commercial banks. Although the problem of a narrow money market in the economy still persists, the advantage

however is the reduction in the export of cash surpluses by commercial banks in search of investment outlets.

Worthy of further comment is the non-alteration of the liquidity ratio since 1962. It is observed that the actual liquidity ratio maintained by the banking system has risen and is well above the legal minimum. This is attributable to increased deficit financing by government which has increased liquid-earning assets of the banks. The monetization of oil money as has been noted earlier is also crucial. In these circumstances, for the CBN to have applied an effective liquidity policy capable of restraining the credit operations of the commercial banks would have meant a substantially high ratio. But the problem is that since the liquidity ratio is not discriminatory, a level higher than the 25% minimum is bound to adversely affect the small banks and would thus be inequitable, perhaps to the extreme. It is common knowledge as we have said earlier that most of these small banks presently experience problems in meeting the minimum liquidity requirement.

Infact from all aspects it is contended that the liquidity ratio does not have the potential for counter-cyclical adjustment of bank liquidity and credit. This is because a high ratio may only cause banks to increase their portfolio of liquid earnings assets which may involve a rechannelling of bank credit from the private sector to the Federal Treasury. The liquidity ratio is therefore weak and may not act as a restraint on the expansion of bank credit.

4.2.7. Special Deposits

Special Deposits like stabilization securities are a supplementary reserve requirement weapon which was given to the Central Bank of Nigeria under the 1968 Amendment for the purpose of requiring commercial banks to maintain some additional reserves over and above the legal minimum cash and/or liquid assets. The Decree empowers the Bank to "from time to time require commercial banks to maintain with it, at its Head Office and for a specified period, special deposits expressed as a percentage of the total of any specified deposit liabilities and/or of an increase in deposit liabilities, or the equivalent of the absolute increase in such deposit liabilities"[19], over an amount outstanding at a certain date. Special deposits are not eligible as one of the components of specified liquid assets and the Central Bank of Nigeria may at its own discretion pay interest on them, except that such interest at its highest should be one percent below the Treasury Bill issue rate.

Special deposits as a method of regulation are capable of influencing the lending capacity of the banking system by freezing cash as a form of bank assets which normally serve as a buffer for advances. The instrument thus has as its primary objective reduction of the liquidity of the commercial banks and hence restrain deposit expansion; and it is for this purpose that it has been applied in Nigeria. By the middle of 1971, inflationary

pressures were high and as a result of importers local currency advance deposits with the banks for which foreign exchange was yet to be collected, bank liquidity rose to alarming proportions and the Central Bank of Nigeria decided to use the special deposits weapon to both moderate the inflationary pressures and liquidity. On 10 June, 1971, the Central Bank of Nigeria in a circular letter directed that banks whose level of short-term external liabilities was above ₦20 million should deposit the local currency counterpart of the excess with it on/or before 30 June, 1971.

The introduction of Special Deposits did have some effect on the liquidity of the commercial banks among other developments. The liquidity ratio of the commercial banking system slumped from a high 92% at the end of May to 69.6% at the end of June[20]. But because this was well above the statutory requirement of 25%, commercial banks still had enough room to increase loans and advances. Another important impact was on the Treasury Bills market where commercial bank holdings fell from ₦338.9 million in May to ₦160.3 million at the end of June. Treasury Bills discounts by the Central Bank of Nigeria also rose from a mere ₦5.8 million in May to ₦150 million in June. Lastly, the ability of the commercial banks to take up new issues of Treasury Bills was also greatly reduced[21].

Despite the relative effectiveness of the methods as demonstrated above, it has never been used again despite the apparent higher rate of inflation in the economy.

All the same this does not undermine the several advantages of this instrument as a method for regulating commercial banks. The weapon can be used by a simple stroke of the pen and unlike open market operations, it does not operate through a market. One other advantage is the fact that it is purely an instrument of regulation rather than of treasury finance. For the commercial banks, it could be "an income earning asset with a comparatively less adverse effect on the earning capacity of banks and therefore a more palatable tool of control to commercial banks who, as economic entities, operate largely by minimizing operational costs or maximizing profits"[22].

4.2.8. Selective Credit Control

Selective control of bank credit is the major regulation instrument most used and relied upon by the Central Bank of Nigeria since 1964. It entails the direct control of bank credit by fixing a ceiling on the annual rate of expansion of commercial bank credit; fixing of ceiling and proportional allocation of bank credit to the various sectors of the economy; regulating by law advances to indigenous businesses and the requirement that all applications for loans in excess of a specified amount be submitted to Central Bank of Nigeria for prior approval. The objectives of these which are obvious are to ensure that adequate credit goes to the productive sectors to expand production as a cure against inflation; curb consumption and thereby dampen the pressure on price increases and ensure that adequate credit is granted to Nigerians by the commercial banks.

TABLE 4.5

Commercial Banks' Loans and Advances Classified by Purpose
(Percentage Distribution) Performance, 1972-75

Category of Borrower	Prescribed Targe		Actual Performance				Average Deviation from Target			
	Monetary Circular No.5	1975	Apr-Dec 1972	Apr-Dec 1974	Apr-Dec 1974	Apr-Dec 1975	1972	1973	1974	1975
Production	45.0	48.0	38.1	38.3	43.6	44.2	-6.9	-6.7	-1.4	-3.8
Agriculture	4.0	6.0	2.4	3.1	3.1	2.5	-1.6	-0.9	-0.9	-3.5
Manufacturing	30.0	30.0	25.1	24.0	28.4	27.3	-4.3	-6.0	-1.6	-2.7
Mining & Quarrying	4.0	2.0	1.9	1.6	1.2	1.3	-2.1	-2.4	-2.8	-0.7
Real Estate & Construction	7.0	10.0	8.1	9.6	10.9	13.1	+1.1	+2.6	+3.9	+3.1
SERVICES	11.0	10.0	7.7	8.1	7.5	7.5	-3.3	-2.9	-3.5	-2.5
Public Utilities	3.0	2.0	0.7	0.4	0.8	1.2	-2.3	-2.6	-2.2	-0.8
Transport & Communications	8.0	8.0	7.0	7.7	6.7	6.3	-1.0	-0.3	-1.3	-0.8
Total A	56.0	58.0	44.8	46.4	51.1	51.7	-10.2	-9.6	-4.9	-6.3
GENERAL COMMERCE	32.0	32.0	35.7	34.4	30.0	30.4	+3.7	+2.0	-2.0	-1.6
Bills Discounted	2.0	2.0	1.1	1.5	1.9	1.8	-0.9	-0.5	-0.1	-1.7
Domestic Trade	10.0	12.0	12.6	13.4	11.4	10.3	+2.6	+3.4	-1.4	-0.2
Exports	10.0	8.0	11.0	10.1	8.2	6.1	+1.0	+0.1	-1.8	-1.9
OTHERS	12.0	10.0	18.5	19.2	18.9	17.9	+6.5	+7.2	+6.9	+7.9
Credit & Financial Inst.	1.0	3.0	2.5	1.6	1.9	2.5	+1.5	+0.6	+0.9	-0.5
Government	2.0	2.0	1.3	2.1	2.4	3.4	-0.7	+0.1	+0.4	+1.4
Personal & Professional	6.0	4.0	8.5	7.6	6.5	6.0	+2.5	+1.6	+0.5	+2.0
Miscellaneous	3.0	1.0	6.2	7.9	8.1	6.0	+3.2	+4.9	+5.1	+5.0
Total B	44.0	42.0	55.2	53.6	48.9	48.3	+10.2	+9.6	+4.9	+6.3
Total = A + B	100.0	100.0	100.0	100.0	100.0	100.0	-	-	-	-

Source: Central Bank of Nigeria, Annual Report and Statement of Accounts, various years.

TABLE 4.6

Commercial Banks' Loans and Advances Classified Purpose (Percentage Distribution) Performance 1976-81

Category of Borrower	Prescribed Target					Average Performance					Deviations from Target				
	1976	1977	1978	1980	1981	1976	1977	1978	1980	1981	1976	1977	1978	1980	1981
PRODUCTION	48.0	48.0	50.0	56.0	56.0	52.1	53.5	55.6	60.8	59.4	+4.1	+5.5	+5.6	+4.8	+3.4
Agriculture	6.0	6.0	6.0	8.0	8.0	3.8	3.9	4.9	6.8	7.2	-2.2	-2.1	-1.1	-1.2	-0.8
Mining	2.0	2.0	2.0	2.0	2.0	0.9	1.2	0.9	0.9	0.9	-1.1	-0.8	-1.1	-1.1	-1.1
Manufacturing	30.0	30.0	32.0	36.0	36.0	29.4	27.8	27.6	30.8	30.9	-0.6	-2.2	-4.4	-5.2	-5.1
Agro Allied	..	-	-	-	3.0	-	-	-	-	..	-	-	-	-	-
OTHERS	..	-	-	-	33.0	-	-	-	..	..	-	-	-	-	-
Construction	10.0	10.0	10.0	10.0	10.0	18.0	20.6	22.2	22.8	20.4	+8.0	+10.6	+12.2	+12.8	+10.4
Residential	..	5.0	5.0	6.0	6.0	-	3.9	3.8	6.2	6.4	-	-1.1	-1.2	+0.2	+0.4
Others	-	5.0	5.0	4.0	4.0	-	16.7	18.4	16.6	14.0	-	+11.7	+13.4	+12.6	+10.4
SERVICES	10.0	10.0	10.0	12.0	12.0	9.2	9.1	8.2	8.5	9.2	-0.8	-0.9	-1.8	-3.5	-2.8
Public Utilities	2.0	2.0	2.0	3.0	3.0	1.0	1.1	1.5	1.6	1.6	-1.0	-0.9	-0.5	-1.4	-1.4
Transport & Communications	8.0	8.0	8.0	9.0	9.0	8.2	8.0	6.7	7.0	7.6	+0.2	0.0	-1.3	-2.0	-1.4
Exports	-	-	-	5.0	5.0	-	-	-	1.5	1.4	-	-	-	-3.5	-3.6
Dev. Financial Institns.	-	-	-	-	2.0	-	-	-	..	..	-	-	-	-	..
Total A	58.0	58.0	60.0	75.0	75.0	61.3	62.6	63.8	70.8	70.0	+3.3	+4.6	+3.8	-4.2	-5.0
GENERAL COMMERCE	30.0	30.0	28.0	17.0	17.0	25.1	23.6	21.6	17.3	16.9	-4.9	-6.4	-6.4	+0.3	-0.1
Exports*	6.0	6.0	6.0	-	-	3.7	3.1	2.0	..	..	-2.3	-2.9	-4.0	-	-
Imports	10.0	10.0	8.0	6.0	6.0	9.9	9.2	8.9	6.4	6.7	-0.1	-0.8	+0.9	+0.4	+0.7
Domestic Trade	12.0	12.0	12.0	11.0	11.0	10.3	10.4	9.8	10.3	10.2	-1.7	-1.6	-2.2	-0.7	-0.8
Bills Discounted	2.0	2.0	2.0	2.0	-	1.2	0.9	0.9	0.5	-	-0.8	-1.1	-1.1	-1.5	-
OTHERS	12.0	12.0	12.0	8.0	8.0	13.6	13.8	14.6	11.9	13.1	+1.6	+1.8	+2.6	+3.9	+5.1
Credit & Financial Inst.	3.0	3.0	3.0	1.0	1.0	2.9	2.9	3.5	2.5	3.3	-0.1	-0.1	+0.5	+1.5	+2.3
Governments	2.0	2.0	2.0	2.0	2.0	1.9	3.1	3.5	2.2	3.2	-0.1	+1.1	+1.5	+0.2	+1.2
Personal & Professional	4.0	4.0	4.0	3.0	3.0	5.3	4.8	4.7	4.0	3.5	+1.3	+0.8	+0.7	+1.0	+0.5
Miscellaneous	3.0	3.0	3.0	2.0	2.0	3.5	3.0	2.9	31.1	3.1	+0.5	0.0	-0.1	+1.1	+1.1
Total B	42.0	42.0	40.0	25.0	25.0	38.7	37.4	36.2	29.2	30.0	-3.3	-4.6	-3.8	+4.2	+5
Total = A + B	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0					

Source: Central Bank of Nigeria, Annual Report and Statement of Accounts, various years.

Although the ceiling on the rate of growth of bank credit have been in use since 1964, it was not until 1968 that they acquired a legal basis under the 1968 Amendments. But it is worth noting that after their introduction in 1964, credit ceilings and guidelines had to be withdrawn in November 1966 following the introduction of a policy of monetary ease given the prevailing political crisis and the prospect of the economy approaching a possible contraction. They were however re-introduced in 1969 under what is now popularly known as Monetary Policy Circulars. By April 1972, absolute ceilings were removed on the rate of expansion of bank credit but the Central Bank of Nigeria continued to specify the pattern of distribution of bank credit to various sectors with relatively high proportions of increase specified for the productive sectors.

At re-introduction following the recommendations of the Anti-Inflation Task Force (1976), (the aim was to hold increases in bank credit at more sustainable levels), the ceiling on aggregate permissible increase in commercial banks' loans and advances was fixed at 40%. But in the 1978/79 fiscal year, due to the mounting inflationary pressures and the need to further curtail aggregate demand, the 40% ceiling was reduced to 30%; and has been maintained at that level since then. However, "small banks whose loans and advances were below ₦100 million were allowed to continue to operate within a credit ceiling of 40%. Alternatively, they could expand credit up to 70% of their total deposit liabilities excluding government

deposits maturing within six months"[23].

Sectoral allocations used to regulate the distribution of commercial bank loans and advances to the various sectors of the Nigerian economy have been of marginal consequences. Between 1972 - 75, aggregate loans and advances of commercial banks fell short or exceeded the prescribed ratios for almost all sectors. Table 4.5 illustrates this point. Despite emphasis on the preferred production sector, loans and advances fell below the prescribed ratios except for the real estate and construction sub-sector. Loans and advances to the less productive sectors of General Commerce and "Others" on the other hand exceeded the allocations. It can however be observed that with the introduction of sectoral allocation and ceilings, aggregate loans and advances to the various sectors have improved, as average deviations from target have declined.

It was the failure of the banks to closely adhere to the guidelines that caused the introduction of sanctions for non-compliance with the credit guidelines as shown below:

Period of Default	Penalty
1st month	Warning
2nd month	Payment of $\frac{1}{8}$% of the excess credit
3rd month	Payment of $\frac{1}{4}$% of the excess credit
4th month	Payment of $\frac{3}{8}$% of the excess credit
5th month	Payment of ½% of the excess credit
6th and subsequent months.	Payment of 1% of the excess credit

Thus, on the basis of the above, "where a bank grants more than the prescribed percentage of credit to a less productive sector, it receives a warning for the first month. On subsequent months of default, the bank is required to pay the Central Bank of Nigeria a graduated penalty expressed as a percentage of the excess credit from $\frac{1}{8}$% to 1% for the fifth month". On the other hand, where a bank's monthly credit to agriculture, and residential and construction sectors, falls short of the prescribed minimum, the Central Bank of Nigeria is empowered to require such bank to deposit the amount of the shortfall with it for as long as, and to the extent that the shortfall continues. These deposits are neither to attract interest nor count toward liquidity requirements.

There is no doubt that the introduction of sanctions or their threat brought about improvements in the compliance of the commercial banks with the credit guidelines. The situation is depicted by Table 4.6 which shows that within the first three years following the introduction of penalties, commercial banks loans and advances to the production sector were for the first time closer to the prescribed minimums. However, only the minimum requirement for the construction subsector was exceeded; but even here, loans and advances to residential construction were less than the prescribed minimum target. By 1980, the position had reversed as the loans and advances to the less productive sectors once again exceeded the prescribed minimum targets.

But then, the fundamental problem with this instrument still remains and this is the manner in which loans and advances are classified. It has been observed that most of the commercial banks tend to have difficulty in determining how best to classify loans and advances to meet the prescribed ratios. In the absence of specific guidelines and details on classification from the Central Bank of Nigeria, they often use their discretion. Perhaps it is this that accounts for the lumping of too many things under the "Others" sector. The consequences of this situation cannot be over-emphasized as banks could meet prescribed ratios without meaningfully contributing to the growth and development of such sectors.

The tackling of the problem of inadequate credit to Nigerians by the "guidelines" has been with a view to satisfying and fostering the achievement of government policy that commercial activities are gradually passed to Nigerians. The minimum requirement in this regard was fixed at 35% in April 1970 with an indigenous business defined to mean a business wholly owned by Nigerians. But in April 1972, this was raised to 40% and for this purpose, Nigerian businesses were defined to mean those businesses that are owned 51 - 100% by Nigerians. In the 1979/80 fiscal year, the ceiling on bank credit to indigenous borrowers stood at 70% of which 10% was reserved for small business enterprises; but this component was again raised to 16% in 1981. The distribution of this

component among small scale enterprises wholly owned by Nigerians is based on their annual business turnover as follows:

A. Up to ₦25,000 - - - - - - - - - - - - - 1.6%

B. Over ₦25,000 and up to ₦50,000 - - - 1.6%

C. Over ₦50,000 and up to ₦100,000 - - - 3.2%

D. Over ₦100,000 and up to ₦200,000 - - 4.0%

E. Over ₦200,000 and up to ₦500,000 - - 5.6%[24]

Although commercial banks have been adhering to the minimum loans to indigenous borrowers requirement, they tend to fall short of the prescribed minimum target in respect of small scale enterprises. But the potential of this weapon is obvious as it is capable of changing the orientation of the lending policies of some of the commercial banks which had hitherto been discriminating against Nigerians. This method further supplements the policy of indigenisation as it provides the indigenous enterprises with the financial resources necessary for their performance of the roles expected of them.

The last but not the least aspect of the Central Bank of Nigeria "guidelines" is the requirement that loan applications exceeding a specified amount should be submitted to it by commercial banks for its approval. The major objective of this is to prevent commercial banks from jeopardizing their solvency with an excessive concentration of risks. This apart from ensuring that the stability of the banking system is maintained, is capable of checking

the monopoly power of big businesses to commercial bank credit. It is needless to add that this method of regulation helps in ensuring that no commercial bank makes credit available to any borrower such that the sum involved is more than $33\frac{1}{3}\%$ of its paid-up capital and reserves as is required by the Banking Act.

On the whole, it is considered pertinent to say that whereas the commercial banks complied with the guidelines initially, the weapon was to fail woefully in later years. This called for the modifications we have seen, and yet compliance cannot be described as excellent. That is to say that overall performance cannot be regarded as encouraging. This may be attributed to three factors:

> First, the guidelines did not discriminate among banks as to the sizes and types of market situation they face. Second, the Bank relied on moral suasion to secure compliance and no sanctions were either prescribed or imposed against non-compliance. Third, the guidelines were restricted to the commercial banks alone; the merchant banks who were operating and competing as commercial banks were not included[25].

We can therefore say that with the inclusion of the merchant banks in the guidelines, the potentials of this instrument have been increased and it will continue to remain one of the Central Bank of Nigeria's most reliable methods of regulation.

4.3 Appraisal of Policies.

In the light of the discussion outlined above viz, the policy objectives of the Central Bank of Nigeria and the measures it has so far used in attempt to achieve these objectives, it is important that we now consider the crucial question of the overall effectiveness of the Central Bank of Nigeria both as an institution and its policy actions. There is no doubt that this is not an easy task. This is so because, to give a good evaluation we need to have "full knowledge of the complex chains of causation among policy instruments, targets and objectives"[26]. This is compounded by the fact that monetary and banking policies are only part of the totality of interlocking economic policies which are designed to influence the pace and direction of our development. In this regard, some of the changes in objectives may as well have resulted from exogenous factors. It is these circumstances therefore that make our task difficult; and for reason of space we would endeavour not to dwell on this in greater detail. For the purposes of this study therefore, policy objectives shall be weighed against actual achievements other influences notwithstanding; although these would be formally noted.

It can be said with reasonable confidence that the Central Bank of Nigeria has been able to a large extent to establish a Nigerian currency that enjoys the confidence of the public both internally and externally.

It has also been reasonably able to manage this currency. In addition, when the need for financing the 1962-68 Development Plan in the first instance and later the execution of the civil war arose, the Central Bank of Nigeria responded positively by providing a cheap money policy which aided both deficit financing by government and enhanced the mobilization of local financial resources. But between 1970-80, it would be proper to assess the policies of the Central Bank in the light of its dual role as a regulator and that of a promoter.

As a regulator, the Bank has endeavoured to maintain satisfactory standards of efficiency of the commercial banking system. Thus, the principal objectives of monetary policy measures employed during the period under review have been to restrain the general level of credit expansion; to sustain expansion of credit to the more productive sectors of the economy in order to stimulate the production of goods and services; to increase the level of savings and investment and to reduce the persistently high liquidity of the banking system, in order to maintain monetary stability.

The control of bank credit has been relatively successful as expansion and sectoral allocations have been reasonably within the prescribed limits. But as has been pointed out earlier, there is still room for improvement. In any case, other measures are desirable to ensure that the induced expansion in productive capacity through selective control of bank credit

yields its products. On the other hand, the effective control of the liquidity of the commercial banking system has always eluded the Central Bank of Nigeria; regardless of the fact that partial moderations have been achieved. Even this marginal deflation in the liquidity of the banking system has been at the expense of mounting unemployment, falling incomes and declining production. The result of this is the under-utilization of capacities and increasing scarcity of products and mounting inflation. This in essence conflicts with the ultimate objective of containing inflationary pressures in the economy.

We can therefore go on to say that the objective of monetary and price stability has not been achieved by policy measures during the period studied. The composite price index between 1970-77 in Table 4.7 shows a continued increase. We can see that prices increased by 2.8 times in seven years compared to 1.7 times for output in real terms during the same period. The conclusion we are left with therefore is that monetary and banking policies have been unable to adjust and contain inflationary pressures in the Nigerian economy.

It is in its promotional role that the Central Bank of Nigeria has recorded significant successes. Right from the onset, the Bank has pursued the objective of development of the banking habit with the realization that the banking arrangement in the country was not conducive to rapid improvement in banking in Nigeria. The problems of the

lopsided nature of the banking system, inadequate, inaccessible

TABLE 4.7

All Cities Quarterly Consumer Price Index, 197?-77.

Quarter	1	2	3	4	Average for Year	% Increase
1970	145.2	153.4	155.0	155.8	150.6	--
1971	166.5	182.5	177.4	179.1	174.1	15.6
1972	184.7	185.6	173.6	172.9	179.6	3.2
1973	182.6	194.5	189.6	203.9	189.9	5.4
1974	206.2	218.6	219.6	224.0	214.7	13.4
1975	262.1	195.7	305.0	312.4	287.8	34.1
1976	336.3	343.7	352.0	359.9	348.1	12.1
1977	376.3	407.4	446.4	458.9	423.1	21.5

Source: Okigbo, P.N.C., op. cit., P.19.

and inconvenient facilities for the masses of the people prevailed. Added to this were inadequate resources, under-capitalization and the illiquidity of the banks which resulted in bank failures and thus threatened the development of the banking habit. To eradicate these features, the bank has embarked on a host of measures backed by government policies. Prominent in this direction is the Rural Banking Programme. This programme is designed by the Central Bank of Nigeria to extend banking services and habits to the rural areas. But because this may involve increased operations costs for the commercial banks, the following incentives were provided:

i) exclusion of credit extended in a rural branch from determination of a bank's adjusted capital ratio to its loans and advances;

ii) a maximum of 45 percent set-off of capital cost on a rural branch in the year of expenditure; and

iii) monopoly of banking services for a reasonable period in the rural centre of branch location[27].

Table 4.8 shows that during the first phase of the programme (1977-80), 200 rural bank branches were to be opened. At the end of December 1980, the target was six branches short and these were taken over to the second phase (1980-83). By December 1981, the total number of rural branches had risen to 199 while 38 branches had been opened under the second phase. This programme also achieves the mobilization of rural savings. "At the end of the first phase (end-June 1980) a total of ₦116.4 million was outstanding as deposits in all the rural branches ... Total loans and advances of these rural branches amounted to ₦22.4 million. Thus, the ratio of total loans and advances to deposits by these branches was 19.2% at the end of the first phase varying from 9.8% for wholly indigenous banks to 28.2% for jointly owned banks"[28].

This programme is in no doubt in line with supply-leading financial development that is desirable for the development of the economy. But apart the problems

TABLE 4.8

Rural Banking Programme, Allocation of Identified Centres

Banks	Allocation under first phase	Completed end of June 1980	Completed end of Dec. 1980	Dec. 1981	Allocation under second phase	Completed end of Dec. 1981
A.C.B.	16	16	16	16	19	4
Allied Bank(Nig) Ltd	6	6	6	6	7	-
Bank of Credit and Commerce Inter.	-	-	-	-	6	1
Bank of the North	6	6	6	6	19	-
Cooperative Bank Ltd	5	3	5	5	8	-
Co-operative Bank of L/Nig. Ltd	7	4	4	7	8	-
First Bank(Nig) Ltd	40	39	39	40	37	11
I.B.W.A. Ltd.	11	10	10	40	13	6
Kaduna Co-op. Bank Ltd	3	3	3	3	6	1
Kano Co-op. Bank Ltd	6	4	6	6	6	2
Mercantile Bank of Nig. Ltd	3	3	3	3	6	2
National Bank of Nigeria Ltd	15	15	15	15	19	-
New Niger Bank Ltd	4	4	4	4	9	-
Nigeria-Arab Bank Ltd	7	5	7	7	6	-
Pan African Bank Ltd	5	5	5	5	6	-
Savannah Bank of Nig. Ltd	7	7	7	7	11	-
Societe General Bank of Nig. Ltd	-	-	-	-	6	1
Union Bank (Nig) Ltd	27	27	27	27	36	6
U.B.A. Ltd	27	27	27	27	32	2
Wema Bank Ltd	5	4	4	4	6	24
TOTAL	200	186	194	199	268	38

Source: Central Bank of Nigeria, Annual Report and Statement of Accounts 1981, P.36.

that are common to a programme of this nature, its implementation has compounded the situation. In the first phase, the commercial banks were not taken into confidence in the identification of the locations; rather it was the State Governments that were used. This generated a lot of controversy as communities opposed certain locations and the governments tended to concentrate on local government headquarters. In this way, the volume of business for many of the branches was seriously affected; and the desirable scheme of rural banking was "sacrificed to the convenience of bureacrats in local government administration and political horse-trading to the utter neglect of a larger interest of the rural economy"[25]. Furthermore, the incentives are subject to abuse as the concession of capital adequacy makes deposits unsafe and the rural bank credit could be extended to urban dwellers. Also the concession of monopoly kills competition and thus the provision of effective banking services. There is therefore need to de-emphasize the present procedures. Close co-operation between the Central Bank of Nigeria and the commercial banks in the identification of centres is necessary. In doing this, economic principles more than anything else should be paramount in order to ensure that deserving communities get bank branches which would thus be fully operational.

In furtherance of this objective, the Central Bank of Nigeria has also endeavoured to create money and capital markets; and the increase in financial instruments in these

is indicative of giant strides in the achievement of the ultimate objective. In addition, through bank supervision and examination, coupled with stringent controls, the Central Bank of Nigeria has largely curbed bank failures which has greatly improved and sustained public confidence in the banking system. Participation in the establishment and staffing of such financial institutions like the Lagos Stock Exchange in 1961, and other development financial institutions like the Nigerian Industrial Development Bank 1964, Nigerian Bank for Commerce and Industry and Nigerian Agricultural and Co-operative Bank 1973, are all among the Bank's achievement in its promotional role. The present impact of these institutions on the overall development of the Nigerian economy further enhances the achievement of its objectives to organize and provide development finance.

It would be appropriate to briefly examine the indigenization of the commercial banks at this point. This policy was embarked upon by the government to correct the lopsided ownership and management of the principal commercial banks in the country - the expatriate banks. The aim of this government participation is to get government intimately involved in commercial banking activities so as to guide them to operate to the maximum benefit of the economy. Whereas the aim therefore is to achieve and retain for Nigerians, the ownership, control and management of the banking sector, management has been abdicated to the minority expatriate shareholders. The objective was

abdicated for the fear that government interference in the daily administration of banks may result in the possible impairment of efficiency. The government therefore rightly or wrongly chose to restrict its interference to the appointment of chairmen and some members of the Board of Directors based on equity participation and the specification of economic and social objectives for the banking system through policy statements.

The question to be asked is, have the behaviour patterns of the commercial banks been influenced by the indigenization policy in the right direction? The answer is certainly in the negative. This is because even though majority ownership has been achieved, the control and management of the banks is still in the hands of the foreign minority shareholders. This means that, the institutional and operational re-orientation of the commercial banks is yet to be achieved; and this was the actual problem with the leading expatriate banks. We must therefore reiterate the fact that these banks were established primarily to finance foreign trade between the colonies and their home countries, and they have come to view their roles as such. Thus, the mere fact that these banks are now indigenous by way of ownership does not "make them immune from the institutional limitations in the system nor absolve them from the dual and conflicting obligations which any banker in his daily operations undertakes"[30].

While it has been identified that policy measures during the period covered by this study did not achieve most of the specific objectives of policy instruments and the commercial banking system, it can also be shown that they were not in consonnance with some of the national objectives. The directives by the Central Bank of Nigeria to the commercial banks to grant loans to individuals for the purchase of foreign businesses under the Nigerian Enterprises Promotion Decree and the special privileges attached to them does not in the least help the achievement of the national objectives of a just and egalitarian society, and a land of bright and full opportunities for all citizens. Much as it could be argued that the Government had envisaged the benefits of this policy to accrue to all Nigerians, there is no doubting the fact that its implementation has been to the contrary. It is indeed difficult therefore to conceive how a scheme under which a few individuals are given opportunities to amass wealth achieves egalitarian objectives bearing in mind the fact that it is not everybody that has access to banking facilities and can equally procure a loan.

Furthermore, the inability of the Central Bank of Nigeria to stabilize prices through an effective deployment of its instruments has not enhanced the achievement of most if not all the national objectives. As has already been stated by the Anti-Inflation Task Force, a high rate of inflation poses a great threat to national unity and social harmony as it affects the real incomes and standards of living of different classes differently. The persistent inflation has led to a distortion in the pattern of resource allocation or income distribution in the economy which is no doubt detrimental to economic and social development.

The point to be made is that rather than attain a just and egalitarian society through the minimization of income and opportunity differentials, inflation does not aid the reduction of these inequalities as it redistributes incomes in favour of those with higher incomes and businessmen. Last but not the least, inflation affects our very existence as a free and democratic society. This is in the sense that a minimum level of welfare is a necessary condition for the survival of free and democratic institutions. This suggests that a free and fair society cannot long survive in a situation of gross disparity in the distribution of income and wealth. But then this is one of the products of the inflationary pressures in the Nigerian economy today.

A host of problems have necessitated the failures pronounced for the instruments and policies of the Central Bank of Nigeria. Of particular importance is the policy-making and implementation process. What has been revealed is the fact that the main brunt has been borne by fiscal policy with monetary and banking policy consistently playing a very minor and subordinate role. Even these have had cause to be re-inforced by direct measures by government. In these circumstances, several strands of policy are brought into force to the extent that none is perculiarly emphasized and monitored nor directed at achieving any single over-riding objective. This indeed has rendered the monetary and banking policies of the Central Bank of Nigeria ineffective even where they would have otherwise been effective.

The structural rigidities and contradictions of the economy may as well account for some of the failures. This is based on the notion that the measurement of the effectiveness of monetary policies involves the determination as to whether policy is expansionary or contractionary; and the indication of financial variables the central bank should seek to control. It is in this view that a distinction is usually made between indicators of policy and targets of policy. Indicators of policy therefore inform the observer whether policy has become easy or has tightened. Targets of policy on the other hand, are of two types, the ultimate and intermediate targets. The ultimate target refers to those variables that measure the performance of the economy. For example, the rate of inflation, rate of unemployment and rate of growth. Similarly, intermediate targets are generally those financial variables on which the central bank is assumed to exert a fairly significant influence bearing in mind the fact that due to problems of lags and uncertainty, the impact of policy does not work directly between policy instruments and the ultimate targets. This is due to the existence of relationship between the intermediate target and the ultimate target; like the one that may exist between money supply and the rate of inflation.

The intermediate targets are influenced by adjusting the instruments of policy which are variables over which the central bank has total and exclusive control. In selecting a target for appraisal of policies therefore,

two basic criteria are used. The good target should be one that is controllable by the central bank. This means that the bank should be able to determine the value of the target within a fairly narrow range over a reasonable period of time. In addition, the linkages between the intermediate target and the ultimate target or policy goals should be fairly close and predictable. This is saying that, a given change in the target should consistently produce the same change in the ultimate goals.

It is however noteworthy that the structure of the economy may be such that if we select a target over which the central bank has tight control, linkage between the target and ultimate goals may be weak. On the other hand, if we select a target with close linkages to the rest of the economy, that may be a target which the central bank has only weak control. This indeed is the problem we face in the circumstances of the Nigerian economy.

This study notes the fact that there is no concensus among economists as to what variable monetary policy uses as a lever to control the economy, and would not draw itself into this controversy. But the following key variables of monetary policy are worth mentioning, namely, commercial bank deposits the quantity of money, interest rates, total bank credit, and bank loans and advances among others. It is the inability of these targets to meet the criteria already mentioned above that makes the use of a quantitative index in this circumstance inappropriate,

the general controversy notwithstanding. Empirical studies already done on the Nigerian economy demonstrate this problem; and without necessarily abdicating our primary objective of being descriptive, we would briefly review a few of them.

Osagie (1974) in examining the macroeconomic relationships in the Nigerian economy, drew up the following structural relationships[31]:

$G = C_1 + gZ$ .... (govt. revenue function ..... (1)

$F = C_2 + bG$ .... (govt. expenditure function .... (2)

$S_m = C_3 + aF + eCx$ ... (money supply function) ... (3)

$E = C_4 + hSm + jZ$ .... (aggregate expenditure function) ...(

$M = C_5 + kE + 1Pr$ .... (import function) .... (5)

$P = C_6 + nPm + qSm$ ... (price level function) ... (6)

In order to facilitate the identification of the impact of selected key exogenous variables on some endogenous variables, he further derived a number of reduced form equations from equations (2) to (6) as shown below:

$F = C_2 + Dc_1 + bgZ$ ..... (7)

$Sm = C_3 + ac_2 + abc_1 + abgZ + eCx$ ..... (8)

$E = C_4 + hc_3 + hac_2 + habc_1 + hagbZ + heCx + jF$ ... (9)

$M = C_5 + kc_4 + khc_3 + khac_2 + khabc_1 + khabgZ +$
$kheCx + jF + 1Pr$ ..... (10)

$P = C_6 + qc_3 + qac_2 + qabc_1 + nPm + qabgZ + qeCx$ ... (11)

The partial derivatives of equation (11) with respect to Pm, Z, and Cx when taken would produce the impact multipliers. First derivatives with respect to the exogenous variables on the other hand, would produce the impact multipliers

for the other equations.

Based on data from secondary sources, he established that (1) there is a positive relationship between crude oil exports and both government revenue and expenditure; (2) money supply is not exogenously determined by Central Bank but endogenously determined by developments in the oil industry as well as the level of commercial bank loans and advances; (3) aggregate expenditure is shown to be positively related though non-significantly to crude oil exports, commercial bank loans and advances and government expenditure and; (4) both import prices and crude oil exports are positively and sifnigicantly related to the index of domestic prices, while commercial bank loans and advances are negatively but insignificantly related to P; thus suggesting that the nature of inflation in Nigeria is partially structural[32].

Ajayi and Ojo (1981) in testing the generally held view that inflation within an economy can be explained by variations in the present and past values of the quantity of money, used the model,

$$\dot{P}_i = g(\dot{M}_i) \quad \ldots\ldots\ldots\ldots\ldots\ldots \quad (12)$$

where $\dot{P}_i$ is changes in prices and $\dot{M}_i$ is changes in the money supply. But since changes in the quantity of money may affect prices through some kind of adjustment process, the above was reduced to,

$$\dot{P} = f(\dot{M}_{it}, \dot{M}_{it-1}, \dot{M}_{it-2}, \ldots) \quad \ldots\ldots \quad (13)$$

Based on quarterly data from 1960-72, they established from the results that inflationary trends in Nigeria cannot be adequately explained by looking at the money supply alone[33].

The list of empirical studies reaching similar conclusions is inexhaustible. In this regard, it could be observed that government monetization of large and increasing volume of foreign exchange receipts from oil has exacerbated the inflationary pressures. The principal source of the change in money supply is not the commercial banks and thus lies outside the control of the Central Bank. Any extreme monetary measures of restraint on bank credit would therefore not restrict money supply substantially. Rather it would even create industrial financial crises that could further lead to recession and stag flation. The only possible option here is for the Bank to influence the public to forego their liquidity preference through higher interest rates as this could assist in the reduction of money supply. It is also clear from the above that the nature of inflation in Nigeria like other African countries is basically structural[34]. Thus, prevailing price increases may not therefore reflect the ineffectiveness of anti-inflationary measures of control applied by the Central Bank, the fact that the adequacy of such measures is in doubt notwithstanding.

It could therefore be argued that these structural inadequacies as they affect the transmission process of

policy instruments have also contributed greatly to the ineffectiveness of monetary and banking policies in Nigeria. Added to this is the unwillingness and reluctance of the Central Bank of Nigeria to push its regulatory policies further enough to ensure success or monitor the achievement of same. There is no doubt that the circumstances of the economy call for this cautious attitude coupled with the fact that commercial banks are known to oppose strong regulators; but this may as well be its own unmaking.

The response of the commercial banks to regulatory pressures is also worthy of comment. Rather than confront the authority of the Bank, commercial banks in Nigeria have clearly indicated a willingness to co-operate. In doing this, one is of the opinion that they have tended to exploit some of the loopholes in the instruments and guidelines of the Central Bank of Nigeria. A prominent example here is the classification of loans and advances mentioned earlier. The banks may use any of the following to meeting the ratio of credit to the agricultural sector - "a loan to a "bona fide" farmer for production, or to a transporter for movement of agricultural produce, or to a food processing industry or to an importer of food items"[35]. Examples of this nature abound for the various monetary and banking measures being employed by the Central Bank of Nigeria. It can therefore be said that such attitudes may have partially contributed to the failure of the policy instruments of the Central Bank of Nigeria in

achieving their ultimate targets.

The philosophy of the Central Bank of Nigeria may also be responsible for the seemingly ineffectiveness of its regulatory methods. This is because most of the regulatory instruments aim at the reduction of or stimulation of aggregate demand in the economy depending on the direction of policy. The Central Bank of Nigeria has however adopted a supply-inducing approach rather than demand reduction. This is saying that whereas the effective control of inflation for example calls for a curtailment of aggregate demand, the approach of the Bank rather than do this seeks to expand or increase supply and the very effect of this is expansionary. Thus even though an increase in supply may be induced, it is not likely to be of any effect and the increase in demand as a result of that policy action would have further incensed the impetus of the inflationary pressures. One cannot however blame the Bank for this as it is based on the realization that demand-reducing policy would only stagnate and reduce our pace of development. In any case, we cannot lose sight of the fact that this approach has led to the ineffectiveness of most of the instruments.

FOOTNOTES

1. First Report of the Anti-Inflation Task Force, Federal Ministry of Information, Printing Division, Lagos, October 1975, P.

2. Government White Paper on the Report of the Financial System Review Committee, Government Printer, Lagos, 1977.

3. Second National Development Plan, op. cit., P.71.

4. Uzoaga, W.O., op. cit., P.174.

5. Aschheim, J., Techniques of Monetary Control, The John Hopkins Press, Baltimore 1961, P.99.

6. Nwankwo, G.O., op. cit., P.36.

7. Uzoaga, W.O., op. cit., P.133.

8. Board of Governors, Annual Report for 1957, P.14 in J. Aschheim, op. cit., P.87.

9. Okigbo, P.N.C., op. cit., P.68.

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11. Ibid, p.33.

12. Research Department, Central Bank of Nigeria, "Developments in the Nigerian Economy During the First Half of 1980", (Mimeograph), P.35.

13. See S. Tomori, "The Demand for Money in the Nigerian Economy", Nigerian Journal of Economic and Social Studies, November 1972; O. Ojo, "The Demand for Money in the Nigerian Economy: Some Comments", Nigerian Journal of Economic and Social Studies, March 1974; O. Teriba, "Some Methodological Issues and Further Evidence", Nigerian Journal of Economic and Social Studies, March 1974.

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15. Enuenwosu, C.E., "The Role of Monetary Policy in the Control of Inflation in Nigeria". Inflation in Nigeria, Proceedings of a National Conference, H.M.A. Onitiri and K. Awosika (eds), Nigerian Institute of Social and Economic Research, Ibadan, 1982, P.293.

16. Ibid, P.293.

17. Teriba, O., op. cit., P.32.

18. Central Bank of Nigeria Amendment Decree 1968, Section 2, Sub-section 7.

19. Teriba, O., op. cit., P.52.

20. Enuenwosu, C.E., op. cit., P.262.

21. Ibid, P.263.

22. Teriba, O., op. cit., P.53.

23. Central Bank of Nigeria, Lagos, Annual Report, op. cit., P.7.

24. Central Bank of Nigeria, Lagos, Annual Report, 1981.

25. Nwankwo, G.O., op. cit., P.

26. Nemedia, C.E., op. cit., P.13.

27. Olasore, O., "Rural Banking: Strategies and Policies of Government and Central Bank", Bullion, July 1979, P.53.

28. CBN, Annual Report, op. cit., P.35.

29. Uzoaga, W.O., op. cit., P.271.

30. Nwankwo, G.O., op. cit., P.78.

31. Osagie, E., "Macroeconomic Relationships in an Oil Producing LDC: Implications for Inflation Policy", in Onitiri, H.M.A. and Keziah Awosika, op. cit., Pp.178.181.

where Z = annual export value of crude petroleum at current prices;

Pm = import price index;

Pr = relative price of imports, that is import price index Pm divided by the consumer price index, P;

Cx = Commercial bank loans and advances;

Sm = Money supply;

G = Federal Government revenue;

F = Federal Government expenditure;

P = Consumer price index.

32. Ibid, P.182.

33. Ajayi, S.I. and Ojo, C.O., Money and Banking: Analysis and Policy in the Nigerian Context, George Allen and Unwin Ltd., London, 1981, P.230.

34. Central Bank of Nigeria, "Origin and Development of Inflationary Trends in African Countries", Association of African Central Banks Conference held in Addis-Ababa, August 1974, (Mimeograph).

35. Uzoaga, W.O., op. cit., P.123.

CHAPTER V

SUMMARY AND CONCLUSION

5.1 SUMMARY

It is now important that we briefly summarize what has been said so far noting our major conclusions and suggesting appropriate policy recommendations. We have shown that whereas economists are agreed that financial institutions can play a leading role and thus act as a catalyst in the development process of an economy, they tend to differ on the modality of the financial system that best achieves this objective.

There are those who believe that financial institutions need be passive and cautious, only responding to the demand for their services. This is to ensure that they play a leading role without necessarily stimulating monetary instability and inflation. Others however believe that for financial institutions to meaningfully contribute to the development of an economy, they must be dynamic and willing to lead, finance and service the economy. They should therefore make their services available such that demand responds to them rather than is believed by the first school. It is necessary to reiterate that as a requisite, a good super-structure of financial institutions and instruments is necessary for this purpose. The study dwells on the fact that, the mere existence of these in a developing economy does not guarantee that financial institutions would play the role expected of them. They must therefore be closely regulated and controlled, and their effectiveness will depend on how

well this is done.

We have seen that the demand-following approach to the development of financial institutions prevailed during the colonial era and this resulted in the unsavoury features of the Nigerian commercial banking system. Of more significant consequences was the alleged discrimination against Nigerians by the expatriate banks which in the wake of Nigerian nationalism gave rise to attempts to form indigenous banks. But since regulations governing the commercial banking system were very laxed, this resulted in massive bank failures. It was to get rid of these failures and encourage the banking habit that the first attempts at controlling the banking business were made. The Banking Ordinance 1952 strenghtened the noose that caused most of the mushroom banks to fold-up.

With the persistent requests and pressures from Nigerian nationalists, the controversy on the establishment of the Central Bank of Nigeria was started. They won and the Central Bank of Nigeria Ordinance was passed in 1958. This was indeed a major landmark in monetary and banking policies in Nigeria; and a necessary condition for the economic advancement of the country. The Bank has its primary objectives, as the establishment and management of a Nigerian currency that would have the confidence of the public both at home and abroad; the promotion of sustainable rate of economic growth and development; maintenance of balance of payments equilibrium; maintenance of reasonable price stability; and the establishment and control of a sound financial system. All these point to one direction, to facilitate the economic development of

Nigeria. Emphases on these objectives we have noted have varied over time with all but except one being prominent during the period studied.

We have recognized that in a developing economy like ours with an underdeveloped financial system, the commercial banking system is most prominent, and the commercial banks while operating as profit-making organizations, do possess some behaviour patterns on which the Central Bank can act with a view to achieving some of the above objectives. The capacity of the Central Bank to influence the behaviour of the commercial banks is defined by legislations as to establishment conditions, capital requirements, and the monetary policy instruments in its armoury among others.

Our evaluation has revealed that most of these methods have been ineffective in achieving their ultimate objectives for example price stabilization, for reasons already mentioned. The Central Bank is however yet to use some of the instruments at its disposal. Some have however been employed for different purposes at different times. The use of Treasury Bills for example has not been for the purposes of regulation but to provide Treasury finance for government and this explains why they were phased out as the government's revenue position improved. What can be said is that, by not applying or continously experimenting with its regulatory methods, most of them have lost touch with the overall development and circumstances of the economy in which they are expected to operate.

It has however been observed that the Central Bank of Nigeria has been considerably effective in its promotional roles. The commercial banking system has expanded and new institutions have been established. This is as a result of the unwillingness of the Bank to restrict itself to what is commonly referred to as the traditional functions. Rather, it has been adventurous enough to move in and attempt to develop the financial system in order to ensure that it does have a system to regulate, and its policy instruments are workable. In the area of foreign exchange control, the Central Bank has stemmed the outflow of short-term funds through the stringent administration of exchange control regulations.

However, the unsavourly features still remain. Bank lending is still dominated by the self-liquidating principle and banking development is still lop-sided and lagging behind the pace of development for the rest of the economy. Bank services are still poor and cases of fraud and forgeries are rampant as is evidenced by reports in most of the national daily newspapers.

The relative ineffectiveness of the regulatory methods and ultimate ineffectiveness of monetary and banking policies may not however be blamed on the instruments entirely but also on the circumstances of the economy in which they operate. This is because apart from improper use or timing of existing tools, and the structural deficiences of the economy are partially responsible for their failure. In any case we cannot rule out doubts about the potential and efficacy of monetary and banking policies as major

economic control devices. This notion borders on the inability of the Central Bank of Nigeria to influence appropriate targets. As has been shown, Monetary and Banking policies tend to achieve their objectives in an indirect manner; they affect the ultimate goals only through their effects on aggregate demand by exerting direct influences on commercial bank reserves, money supply and interest rates. Although the choice of an appropriate "target" among these depends on its ability to have the most direct and predictable effect on aggregate demand; and which is subject to most accurate control, our study of the Nigerian economy has revealed that not only is the relationship a farce but also does the control of some of these targets fall beyond the powers of the Central Bank. Thus, the Bank is not in a position to control by way of its instruments the money supply which emanates from the monetization of oil revenues accruing to government and the fact that interest rates are institutionally determined. All these coupled with the obvious conflicts among specific policy goals that are not simultaneously achievable and the supply-inducing policy of the Central Bank have given rise to the failure of the policies.

Other constraints on monetary and banking policies include those imposed by important social objectives, the pursuit of which may conflict. Also is the fact that other policy weapons like fiscal policies share the same objectives. In this regard, monetary and banking policies cannot claim whatever successes or failures that have been made in achieving or failing to achieve such goals as control of inflation, balance of payments deficits and promotion of the rapid growth of the Nigerian economy.

5.2 Recommendations:

Based on the structure of the Nigerian economy in general and the banking system in particular, the nature and problems associated with the regulatory instruments and their objectives, this study now considers it pertinent to make the following policy recommendations:

1. It is the view of this study that for the commercial banking system to achieve its objectives, there is need for further improvement in the lop-sidedness, investment channels, management, services and reduction of frauds. More banks and branches are needed with a view to changing the structure of the financial system.

2. The laws relating to the operations of the banking system are long overdue for a review. This is necessary in order to bring them in line with the present circumstances of the economy. In particular changes are needed in the powers of the Minister of Finance. Another important area to consider in the review is the leadership of the Central Bank. It is contended that for the Bank to re-assert itself and play a leading role in the formulation of monetary and banking policies, it is necessary that its leadership be of the highest calibre. The appointment of non-professionals hardly knowledgeable in financial matters can largely be said to account for the present sub-ordinate position of the Bank vis-a-vis the Federal Ministry of Finance.

3. It has been seen that changes in ownership have not affected the operations and policies of Nigerian commercial banks; there is therefore need that majority ownership now include effective management and control by Nigerians.

4. There is every indication that the average Nigerian customer is very much ignorant of the operations, services and requirements of the commercial banks. For the effectiveness of the banking system to be felt, there is need for public education centring on all facets of bank operations, customer credibility and the status of the banks as institutions. These campaigns can be embarked upon by the commercial banks with the Central Bank monitoring.

5. There is need for more concerted efforts to significantly increase credit to agriculture, industry, and small-scale business. This will enhance the achievement of the objectives of these preferred sectors and expedite the transformation of the Nigerian economy.

6. The Central Bank must start experimenting with the regulatory methods as this would put it in a position to modify and bring them into bearing with the objectives of the institutions which they seek to influence. Moreover, we have seen that the direct methods of control like Selective control of bank credit and cash reserves among others are more effective and realistic in the circumstances of the Nigerian economy than the conventional regulation methods of open market operations, moral suasion etc. This study therefore recommends that emphasis should shift to those methods that show greater promise and potential in the stabilization of the Nigerian economy.

7. A developing economy needs a large volume of savings if the expanding capital needs are to be met without necessarily stimulating inflationary pressures. The Central Bank of Nigeria must therefore gear up the banking system which definitely

is ill-equiped for the effective mobilization of the savings of the economy. The study therefore recommends the establishment of adequately specialized institutions which may by legislation be limited both in geographical spread and areas of operation, thus being suitably located and operated to carry out savings programmes. Such programmes must take into account the habits of the people where they are located in order to appeal to the generality of the public.

8. Interest rates as an instrument of regulation in order to be effective, would require a careful analysis and estimation of the credit needs of the economy, the degree of substitution among assets and public preference structure. In this way, the financial system can be opened up as a free market with the Central Bank monitoring the interest rate structure and applying it as an instrument of regulation.

9. It has been seen that inflation was accentuated by the rapid monetization of oil revenue resulting from increased government expenditure. In future, it is recommended that government expenditure must be limited to enable the Central Bank have control over money supply. This indeed is a pre-requisite in ensuring the effectiveness of the regulatory instruments.

10. To avoid the problem of conflicting objectives and policies, and incongenial policy instruments, a consistent co-ordination of these is recommended. Moreover their individual effects cannot be easily isolated.

11. The dependent structure of the economy needs transformation; and in particular, with the recognition

of crude-oil as a wasting asset, Central Bank policy measures must in the future be aimed at the diversification of the economy. It spells disaster for the economy to continue to depend on a wasting asset.

12. To further instil public confidence in the banking system, the Central Bank should adopt measures aimed at stemming the high tide of frauds in the banking system. Newspaper Reports such as these - Daily Times, 12 November 1974, 15 April, 1980; Business Times, 28 November, 1978; and New Nigerian 30 July, 1974 and 29 September, 1979 vindicate this point and suggestion. The list is indeed inexhaustible.

13. The commercial banks should now be encouraged to be more involved in term-lending. Policy measures should also be adopted to achieve this objective. This is one of the ways through which the effectiveness of the banking system could be achieved.

14. The supply-management policy of the Central Bank despite its short-comings should be continued and intensified. It is recognized that it is only this approach that facilititates the achievement of accelerated economic growth and development for the country.

15. The ineffectiveness of policies as has been identified here can be partly attributed to the seemingly ineffectiveness of the Bank Supervision Department of the Central Bank. It can be said that most of the present unsavourly effects observed in the banking system could have been avoided if the department had been performing its functions. Non-compliance by commercial banks and the misclassification of loans and advances would have also been noticed.

It is therefore hoped that the department would gear up in its efforts to ensure a healthy banking system. Even in cases where offending banks are penalized, their activities need not be taken for granted as the hardships they mete to their customers are capable of undermining the development of the banking habit in Nigeria.

5.3 Conclusion:

It is the conclusion of this study that the above notwithstanding, the test of the regulatory instruments lies in ensuring the promotion and sustainment of growth and development coupled with the effective control of tendencies by the commercial banks and government to stimulate monetary instability and inflation. There is need for continued co-operation between the monetary and fiscal authorities. Since the treasury functions of the Ministry of Finance in so far as they impinge on debts management may affect the monetary policies of the Central Bank and vice-versa, close co-operation between the Bank and the Ministry of Finance does not therefore entail treasury dominance. A deeper understanding of the techniques, limitations and possibilities of monetary management in the 1980s must be strenghtened for the fight against inflation. But then the success or failure of the instruments in influencing commercial bank behaviour in the right direction does not entail final solutions or loss of hope in our ensuring that commercial banks play their proper role in the development of the Nigerian economy. What is expected is the acquisition of new approaches and strenghtening of the old ones.

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