DISCRIMINATE ANALYSIS AND PREDICTION OF CORPORATE BANKRUPTCY AS IT APPLIES TO BANKING INDUSTRY. (A CASE STUDY OF UNITED BANK FOR AFRICA (UBA) PLC)

BY

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A PROJECT PRESENTED TO THE POST-GRADUATE SCHOOL

AHMADU BELLO UNIVERSITY, ZARIA, IN PARTIAL FULFILLMENT OF THE REQUIREMENT FOR THE AWARD OF THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION (MBA).

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NOVEMBER, 1998.

DECLARATION

I hereby declare that this project report has been written by me, and that is a record of my own research work. All sources of information and where applicable, other writers' views have been duly acknowledged in the form of bibliography.

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CERTIFICATION

This project entitled: DISCRIMINATE ANALYSIS AND PREDICTION OF CORPORATE BANKRUPTCY AS IT APPLIES TO BANKING INDUSTRY—A CASE STUDY OF UNITED BANK FOR AFRICA (UBA) PLC. BY **SHUAIBU SALEH DASS** meets the regulations governing the award of a Degree of Master of Business Administration (MBA) of Ahmadu Bello University, Zaria and is approved for its contribution to knowledge and literary presentation.

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DEDICATION

THIS THESIS IS DEDICATED

To my wife

Jamila

who had had to cope with my absence at home.

and

My children

Maryam,
Fatimah
and
Rukayya.

May **Allah** bless you all…..

ACKNOWLEDGEMENT

It is my sincere belief that this wholesome study and the project could not have been possible if not for **ALLAH'S** leave. **ALLAH**, I thank you for this and other favours.

I would extend my sincere appreciation to my beloved supervisor, who incidentally is my co-ordinator **Mallam Sani Abdullahi ,** your reward rest with **ALLAH.**

Sulaiman Mamman Mahmud, must be mentioned for he is the architect of this study and for continuing to host me while in Zaria.

Professor, Ilyasu Mohammed, said "you should now go for your Master Degree preferably **MBA**" I thank you for the motivation.

Alh. I. Y. Bawa, Head, Admin. And Personnel NNPC Zonal Office , you have been so helpful, thank you.

Mr. H. O. Oshagbemi, Head Manpower Development,. Your contribution is also acknowledged.

Typing Genius **Abdul-Malik** and lady **Regina your** efforts are being acknowledged too.

I acknowledged with appreciation all your efforts **Mallam Tauhidi** Takuma and **Mall Sani** all of the Business school **ABU Zaria Kongo Campus**.

ABSTRACT

The project is about Discriminate Analysis and prediction of corporate Bankruptcy as it applies to Banking Industry.

Essentially it is the use, simultaneously, of several financial ratios to discriminate between bankrupt and non bankrupt firms, and to predict the likelihood of failure of any corporate entity. The focal point is the applicability of this statistical technique to predicting Banking failure in Nigeria. The Bank chosen for this study in **UNITED BANK FOR AFRICA (UBA) PLC.**

The research was conducted using a multiplicity of approaches. Library review was conducted to peruse the relevant books that had so far been written on the subject. The literature review brought to light the working of other researchers from the introduction of multiple Discriminate Analysis to date. Notably, the Osaze's index was used for assessing the likelihood of success or bankruptcy of UBA PLC. Data Analysis of the Bank was conducted in order to discover the degree of applicability of the method in Nigerian Banking industry.

Finally the research reveals that U.B.A. **PLC** is a successful organisation.

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CHAPTER 1

INTRODUCTION

1.1 GENERAL BACKGROUND

Finance as a field of study is the cornerstone of the enterprise system. General financial management is virtually important to the economy, health of business firms, and to the nation and the world at large. However, proper financial management within the firm will help the business to provide better products at reasonable prices to its customers, to pay higher wages and salaries to its workers and managers and to provide greater returns to the investors who put up the capital needed to form and operate the business. Since the economy - both national and world consists of customers, employees and investors, sound financial management contributes to both individual well - being and the well - being of the general population. Considering its importance, finance should be widely and thoroughly understood, but this is easier said than done. The field is relatively complies, and it is undergoing consistent change in response to shifts in economic condition.

All of these not only make finance stimulating and exciting but also challenging and some times perplexing ".[1]

Finance as a field of study - and an area of responsibility in business organisation, was recognised in the early part of this century. At first it deals with only the instruments, institution and procedural aspects of capital market. However as the century progresses to 1920, technical importation and new industries created a need for more funds. These development resulted in emphasis on financial management rather internal management. The depression of the 1930s necessarily focused the study of finance on defensive aspect of survival, preservation of liquidity, bankruptcy, liquidation, and reorganisations while as the century moved to 1950s finance function took more dynamic roles in modern Company's development. With growing influence it goes far beyond in the records, report, paying bills and obtaining funds, to the more sophisticated analytical process of impressing funds in assets and promulgating the last mix of financing and dividend decisions.

Among the functions of finance is the analysis of financial data. Analysis of financial data, to quote *Meticalf and Fitard*, "*Is a process of evaluating the relationship between component parts of a financial statement of obtain a better understanding of financial position and performance.*" In this direction, for the financial manager to undertake his responsibility effectively and efficiently there must be some tools and techniques which he can rely on to obtain desired result. In recent years one of the widely used and important tool or and techniques is the financial ratio analysis. Studies have shown that financial ratios can be used for the purpose of evaluating a firm performance over a wide range of time. It is useful both as a way of anticipating future conditions and more importantly as a starting point for planning actions that will influence the future course of events. Persistent conclusions have been arrived at over the years that financial ratios are important analytical, planning and control devices.

Some of the Uses of Financial Ratios are:-

Provision of comprehensive information about a prime financial condition;

Determination of firms performance of a prime by the use of standards whenever possible;

Unveiling the problem areas of the firm's resources for necessary connections;

Comparison of firm performance with other firms in the same industry;

Determination of credit worthiness of the borrowing firm;

However, for ratio analysis to be meaningfully interpreted it has to be compared with some standards. The standards used for companion are:

Ratios calculated from the past financial statements of the same firm which can be used to predict future performance;

Ratios calculated using the projected or pro-forma financial statements of the firm;

Ratios of some selected firms especially, the most progressive and successful at the same point in time; and

Ratios of the industry to which the firm belongs.

To this end therefore, there is the need for proper understanding of the efficiency of financial ratio in predicting corporate bankruptcy.

1.2 STATEMENT OF THE PROBLEM

The basic assumption is that Banks as business outfits are always growing concerns. Nevertheless, we must not lose sight of the fact that some banks have high probability of failure, which need to be scrutinised properly before a decision is taken as to their potentials for bankruptcy or success.

A Bank is regarded as technically insolvent if it is unable to meet its current obligations. However, insolvency may be only temporary and subject to remedy. Technical insolvency may be only temporary and subject to remedy. Technical insolvency, then denote only a lack of liquidity. Insolvency in bankruptcy, on the other hand, means that the liabilities of a bank exceed its assets. In other words, the shareholders equity of the Banks is negative. Financial failure thus includes that entire race of possibilities between these two existence.

The remedies for a failing Bank vary in harshness according to the degree of financial difficulty. If the outlook is sufficiently hopeless, liquidation may be the only feasible alternative. However, the failing Bank can be rehabilitated to the gain of creditors, shareholders and society.

It is important to know who gets what if a Bank fails. Notably, in the event of bankruptcy creditors have a prior claim over the claim of other common and preferred shareholders of the firms income, as well as its assets. [4]

Considering the views presented above, a close observation needs to be given Banks in order to ascertain the position of their healthiness or otherwise.

1.3 OBJECTIVES OF THE STUDY

Indeed, the need for this study cannot be over emphasised considering the importance of the topic under study. Over time, a lot of research work has been done on the use of financial ratio analysis in predicting corporate bankruptcy or failure but all the models that were developed in Europe and America have little use and application in less developed economies like Nigeria because:

(a) The ratios developed in these environments (Europe and America) have been generated from large Companies in contrast to those operating in developing countries and:

(b) They are more useful to the developed economies as the availability of sophisticated computing facilities have ensured the generation of large data bases for developing predictive models on business operation.

Based on the above reasons, this study is aimed at testing the Osaze's index of risk in determining whether or not the firm under study is unlikely to fail (successful), have a high probability of failure (need scripted) and or failed (bankrupt).

1.4 SIGNIFICANCE OF THE STUDY

The financial position of the firm is of special interest to a number of people. The suppliers of capital to a firm attempt to analyse the risks and returns associated with supplying that capital. Labour variously try to evaluate the firms ability to pay higher wages and benefits. Government regulatory agencies establish rates and regulations based on analysis of the financial position of given firms.

Finally, the management of the firm may analyse itself in order to identify the potential strengths and weaknesses of the firm. All these people have to do is to evaluate the firm and the process is called *Financial Analysis.*

It is the responsibility of management of any business organisation to see that resources are utilised efficiently and effectively, and that the firm's financial condition is sound and encouraging for the achievement of organisational objective. Performance should be an indication of achievement in terms of good management of organisational resources.

The ability to predict performance is useful and important to management, investors, creditors and individuals in order to take preventive measure such as changing operating policy and re-organisation of the financial structure in case of financial distress. The shareholders being interested in present and future earnings, naturally pay attention to the measure of liquidity and leverage in order to determine the likelihood of a firm's continued existence and also evaluate its profitability.

The firm's creditors are interested in how the firm uses its short-term loan to service its debts in the long-run while also interested in the firms solvency. Hence management can use financial ratios to monitor the firms position from time to time and to be able to predict future performance. In the light of the above, this study hopefully, tends to provide a framework of reference for investors, shareholders, creditors, management and the entire public.

1.5 SCOPE AND LIMITATION OF THE STUDY

The study covers the period of five years from 1993 - 1997. It seeks to evaluate and test the use of financial ration analysis in predicting corporate bankruptcy at it applies to bank firms. The model employed in testing this study is professor Osaze's index of business failure. In this study liquidity, activity, debt and profitability ratios are adequately examined.

Some of the limitations encountered by the researcher are as follows:-

Despite the fact that financial ratios have their own analytical limitations which inevitably applied to this study, some financial statements do not contain enough information for accurate ratios analysis. Another is the unwillingness of the bank under study to give adequate financial statement of their operations.

1.6 DEFINITIONS OF TERMS

The following key terms appear frequently in the course of investigation and their definitions are useful in understanding the text.

WORKING CAPITAL MANAGEMENT: The administration of firms current assets and financing needed to support current assets.

GROSS WORKING CAPITAL: The firm's investment in current assets (like cash, marketable securities, receivable and inventory) [5]

NET WORKING CAPITAL: Current asset minus current liabilities.

SHAREHOLDERS EQUITY (NET WORTH): The capital supplied by stockholders - capital stock, paid-in capital, retained earnings and occasionally certain reserves.

RETAINED EARNINGS: The Balance Sheet account which indicates the total amount of earnings the firm has not paid out as dividends throughout its history; these earnings have been re-invested in the firm.

EARNING PER SHARE (EPS): The net income of the firm divided by the number of shares of common stock outstanding. [6]

DIVIDEND FOR SHARE (DPS) 7; Represent The basic cash flows passed from the firms to its stockholders.

CASH FLOW: The actual net cash, as opposed to accounting net income that flows in (or out of) a firm during some specified periods.

WINDOW DRESSING TECHNIQUES: Techniques employed by a firm to make its financial statements look better to credit analysis.

ASSETS : [8] Representing economic resources, are the valuable possessions owned by the firm ?

LIABILITIES: [9] Are debts payable in future by the firms to its creditors. They represent economic obligations to pay cash or provide goods or service in some future period.

ACCOUNT RECEIVABLES OR BOOK DEBTS: Are the amounts due from debtors (Customers) to whom goods and services have been sold on credit.

BAD DEBTS: [10] The debts which will never be collected.

INSOLVENCY : [11] The inability to pay debt in full prior to bankrupt Act 1861.0

INSOLVENCY IN BANKRUPTCY:

Means that the liabilities of a company exceeds its assets: In other word the network of the Company is negative.

BANKRUPTCY: Preceding in the high court (or certain country courts) for the distribution of the property of insolvent person among his creditors and to relieve him of the unpaid balance of his liabilities.

LIQUIDITY: [12] The ability of an asset to be converted into cash without a significant price concession.

LIQUIDITY RATIOS: [13] (I) Ratios that show the relationship of the firm's cash and other current assets to its current obligation (ii) Ratios that measures a firm's ability to meet short-term obligation [14]

DEBT MANAGEMENT RATIOS/FINANCIAL LEVERAGE: Ratios that show the extent to which the firm uses debt financing [15] (ii) The extent to which a firm uses debt financing. [16]

ACTIVITY RATIO/ASSET MANAGMENT RATIO: Ratios that measure how effectively the firm is using its assets 17 (ii) A set of ratios designed to measure how effectively a firm is managing its assets. [18]

PROFITABILITY RATIOS: A group of ratios showing the combined effect of liquidity, asset management and debt management on operating results [19] (ii) Ratios that relates profits to sales and measurement. [20]

MARKET VALUE RATIOS: A set of ratios that relates the firms stock price to its earning and book value per share. [21]

ANNUAL REPORT: A report issued annually by corporations to their stockholders that contains basic financial statements as well as management opinion of the past year's operations and the firm future prospect. [22]

FINANCIAL RATIO: An index which relates two accounting numbers and is obtained by dividing one number by the other [23]. To new changes and avail itself to new opportunity.[24]

COVERAGE RATIOS: Ratios that relates the financial changes of a firm to its ability to service or cover them.

LIQUID ASSET: These are assets which are either cashed easily or can be converted into cash.

DISTRESS: [25] Is the unhealthy condition of a firm.

STOCK BROKERS: Agents that deals with the exchange of stocks such as shares, debentures and bonds.

C.B.N.: Central Bank Of Nigeria (The apex government bank).

COMMERCIAL BANKS: Bank that accept deposit from individuals and organisations.

MERCHANT BANKS: A merchant bank is a financial institution which performs wide range of activities; financing international trade, accepting bills of exchange etc.

MORTGAGE BANKS: This is a banking designed to encourage financial development in rural communities.

COMMUNITY BANKS: This is a Banking designed to encourage financial development in Rural Areas.

EXOGENOUS FACTORS: Outside organisation factors that influenced the operation of an organisation.

ENDOGENOUS FACTORS: Inside organisation factors that influenced the operation of an organisation.

FOOTNOTES

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CHAPTER TWO

CONCEPTUAL FRAME WORK

2.1 CONCEPT OF FINANCIAL RATIOS

To evaluate a firm's financial condition and performance, the financial analyst needs to perform "check-ups" on various aspects of a firm's financial health. A tool frequently used during these check-ups is a *Financial Ratio,* or *Index*, which relates two pieces of financial data by dividing one quantity by the other. A ratio is defined as "*the indicated quotient of two mathematical expression*" and as " *the relationship between two or more things*."

In financial analysis, a ratio is used as an index or yardstick for evaluating the financial position and performance of a firm. Financial analysis is the process of identifying the financial strengths and weaknesses of the firm by properly establishing relationship between the items of balance sheet and profit and loss account [3]. Financial analysis can be undertaken by management of the firm, or parties outside the firm such as owners, creditor, investors and others. The nature of analysis differs depending on the interest of the analyst for example, trade creditors: are interested in the firm's ability to meet their claims over a very short period of time. Their analysis is therefore, confirmed to the evaluation of the firm's liquidity position. The supplier of long-term debt, on the other hand, are concerned with the firms long-term solvency and survival. They analyse the firm's profitability over time; its ability to generate cash to be able to pay interest and repay principal and the relationship between various sources of funds (capital structure relationships). Long-term creditors do analyse the historical financial statements, but they place more emphasis on the firm's projected or pro-forma financial statements to make this analysis about its future solvency and profitability. Similarly, investors; who have invested their money in the firm's earnings. They restore more confidence in those firms that show steady growth in earnings. As such, they concentrate on the analysis of the firm's present and future profitability. They are also interested in the firm's financial structure to the extent that influences the firms earning ability and risk. Moreso, the ability of the firm to pay dividends and avoid bankruptcy. Finally, management of the firm would be interested in every aspect of the financial analysis. It is their overall responsibility to see that the resources of the firm are used most effectively and efficiently, and that the firms financial positional is sound.

2.2 STANDARDS OF COMPARISON

The ratio analysis involves comparison for a useful interpretation of the financial statements. A single ratio in itself does not indicate favourable or unfavourable condition [5]. It should be compared with some standard of comparison which consists of:

(a) Ratios calculated from the past financial statement of the firm:

(b) Ratios developed using the projected or pro-forma, financial statements of the firm.

(c) Ratios of selected firms, especially the most progressive and successful, at the same point in time, and

(d) Ratios of the industry to which the firm belongs.

2.3 *TYPES OF COMPARISON*

There are three basic ways in which financial ratios are used. [6]

(1) In a cross-sectional approach and

(2) In time series analysis

(3) Current ratio (the ratio of current assets to current liabilities)

1. *The cross sectional approach* involves the comparison of different firms' financial ratios at the same point in time. The typical business firm is interested in how well it has performed in relation to its competitors. If the competitors are also corporations, then their financial statement should be available for analysis. Often the firms performance will be compared to that of the industry leader. This comparison may allow the firm to uncover major operational difference, which if changed, will increase its efficiency. Another very popular type of cross-sectional comparison is to compare the firm's ratio to industry's average.

2. *Time-series analysis i*s done when the financial analyst measures a firms performance over time. Comparison of the firm's current performance to past performance utilising ratio analysis allows the firm to determine whether it is progressing as planned. Developing trends can be seen by using multi-year comparisons; a knowledge of these trends should assist the firm in planning future operations. The rationale behind time series analysis is that the firm must be evaluated in relation to its past performance, any developing trends must be isolated, and appropriate action must be taken to direct the firm towards its immediate and long-term goals. Time series analysis is often helpful in checking the reasonableness of a firm's projected financial statements.

   A comparison of current and past ratio to those resulting from an analysis of proforma statements may reveal discrepancies or over optimism in the pro-forma statements.

3. The current ratio (The ratio of current assets to current liability's) for the present year end could be compared with the current ratio for the preceding year end.

It is important to note that a single ratio does not generally provide sufficient information to judge the overall performance of the firms, only when a group of ratios is used that a reasonable judgement concerning the firm's overall financial statement can be made. Finally, it is necessary to make sure that the data in the financial statements being compared have been developed in the same way.

2.4 TYPES OF RATIOS

The basic types of financial ratios are classified into five fundamental types:

1. Liquidity Ratio
2. Leverage Ratio/Debt management ratio
3. Activity Ratio/Asset Management ratio
4. Profitability ratio
5. Coverage Ratio

As stated earlier no one ratio give sufficient information by which the financial condition and performance of the firm can be judged. Only when group of ratios are analysed could a reasonable judgement be made. Although the number of financial ratios that might be computed increases geometrically with the amount of financial data.

However, for the purpose of this study, we concentrate only on the important ratios.

2.4.1 LIQIDITY RATIOS

It is extremely necessary for a firm to meet its obligations as they become due. Liquidity ratios measure that ability of the firm to meet its current (short-term obligations). From these ratios, much insight can be obtained into the present cash solving of the firm and its ability to remain solvent in the event of adversities. The most common ratios which indicate the extent of liquidity or lack of it are:

i) Current ratio, and

ii) Quick or Acid Test Ratio

i) ***Current ratio*** is given as:-

$$\frac{\textit{Current Assets}}{\textit{Current Liabilities}}$$

The current ratio is a measure of the firm's short term solvency. It indicates the extent to which the claims of short-term creditors are covered by assets expected to be converted to cash in the near future [7]. As a conventional rule, a current ratio of two to one or more is considered satisfactory. This rule is based on the logic that in worse situation, even if the value of current assets becomes half, the firm will be able to meet its obligation. The current ratio represents a margin of safety, that is a "Cushion" of protection for creditors.

The higher the current ratio, the greater the margin of safety; the larger the amount of current assets in relation to current liabilities, the more the firms ability to meet its current obligations. However, the current ratio is a crude and quick measure of the firm's liquidity.

ii. Quick/Acid Test Ratio:

The Acid Test (Quick) ratio is obtained by the total of quick assets divided by total current liabilities [8].

Acid test (Quick) ratio is given as:

$$\frac{\textit{Current Assets - inventory/Stock}}{\textit{Current Liabilities}}$$

The acid test ratio is similar to the current ratio, except for the fact that it excludes inventory from the firm's current assets. The basic assumption is that inventory is generally the least liquid current asset and should therefore be ignored. An asset is liquid, if it can be converted into cash immediately or reasonably soon without a loss of value. This ratio provides a more penetrating measure of liquidity than does the current ratio. Generally a quick ratio of one to one (1:1) is considered to represent a satisfactory current financial condition [10]. Again, which is considered an acceptable value depends highly on the industry in which the company operates.

2.4.2 LEVERAGE/DEBT MANAGEMENT RATIOS

Leverage ratios, which measure the funds supplied by owners as compared with the financing provided by the firm's creditors, have a number of implications [11]. First, creditors look to the equity, or owner supplied funds, to provide a margin of safety. If owners have provided only a small proportion of the total financing, the risks of the enterprise are borne mainly by its creditors. Second, by raising funds through debt, the owners gain the benefits of maintaining control with a limited investment. Third, if the firm earns more on the borrowed funds than it pays in interest, the return to the owners is magnified [12]. For example, if assets earn 10 (ten) percent and debt cost only 8 (eight) percent, there is a 2 (two) percent differential accruing to the stockholders. Leverage cuts both ways, however, if the return on assets fails to 3 (three) percent, the differential between that figure and the cost of debt must be made up from equity's share of total profits. In the first instance, assets earn more than the cost of debt, so leverage is favourable, in the second, it is unfavourable [13].

Fourthly, between debt and equity, debt is more risky from the firms point of view. The firm has legal obligation to pay interest to creditors irrespective of the profit made or losses incurred by the firm. If the firm fails to pay to creditors in time, they can take legal action against it to get payments and in extreme cases, they can take the firm into liquidation [14].

i. ***Total Debt-to-total Asset***-The debt to total assets ratio is derived by dividing a firm's total debt by its total assets;[15]

Debt to-total assets ratio is given as:

$$\frac{\textit{Total debt}}{\textit{Total Assets}}$$

The ratio of total debt to total assets, generally called debt ratio, measures the percentage of total funds provided by creditors [16]. Debt is defined to include both current liabilities and long-term debt.

ii. ***Debt-to-Equity (Networth)***: The debt -to-equity ratio is computed by simply dividing the total debt of the firm (including current liabilities) by its shareholders equity.17

Debt - to - equity ratio is given as:

$$\frac{\textit{Total debt}}{\textit{Shareholders' equity}}$$

It measures the relationship between creditors contribution and those provide by the owners. The creditors would generally like this ratio to be low. The lower the ratio, the higher the level of the firms' financing that is being provided by shareholders, and the larger is the creditor cushion (margin of protection) in the event of shrinking asset values or outright losses.

2.4.3. ACTIVITY/ASSET MANAGEMENT RATIOS

This is designed to measure how effectively a firm is managing its assets, the better the management of asset the larger the amount of sales.[18] Activity ratios are employed to evaluate the efficiency with which the firm manages and utilises it assets. Moreso, it involves a relationship between sales and assets. A proper balance between sales and assets generally reflect that the assets are managed well. Several activity ratios can be calculated to judge the effectiveness of asset utilisation.

i. Inventory Turnover - Ratio,

Also called the inventory utilisation ratio, is defined as sales dividend by inventories.

Inventory turnover ratio is given as :

$$\frac{\textit{Sale}}{\textit{Inventory}}$$

The inventory turnover shows how rapidly the inventory is turning into receivable through sales. Generally a high inventory turnover suggests a good inventory management and a lower inventory turn-over implies excessive inventory levels than warranted by production and sales activities, or a show moving or obsolete inventory.[20]

ii. Average Collection Period:

The average collection period (ACP) is used to appraise amounts receivable and it is computed by dividing average daily sales into accounts receivable to find the number of days that sales tied up in receivable [21]

ACP ratio is given as:

$$\frac{\textit{Receivable}}{\textit{Average Sales per day}} = \frac{\textit{R eceivable}}{\textit{Annual sales/360}},$$

This indicates the length of time the firm must wait after making a sale before receiving payment. The ACP measures the quality of debtors since it indicates the rapidity or slowness of making payments. An excessive long collection period implies a very liberal and inefficient credit and collection performance. On the other hand too low a collection period is not necessarily favourable.[22]

iii. Receivables Turnover Ratio/Debtor Turnover Ratio:

It is obtained by dividing credit sales by average debtors[23]

Debtors turnover ratio is given:

$$\frac{\textit{Sales}}{\textit{Total Assets}}$$

The total assets turnover ratio use the relative efficiency with which a firm utilises its total assets to generate sales.[26] As this ratio increases, there is more revenue generated per Naira to the total investment in asset; so the higher the better.

2.4.4 Profitability Ratios

Profitability is the net result of a large number of policies and decisions. Profitability ratios show the combined effects of liquidity, asset management and debt management on operating results.[28] A company should earn profits to survive or grow over a long period of time. Logically, it could be said that profit is the ultimate output of a company, and it will have no future if it fails to make sufficient profits.[29]

Generally, two major types of profitability ratios are calculated:

1. Profitability in relation to sales and
2. Profitability in relation to investment

PROFITABILITY IN RELATION TO SALES

It is not only important but necessary for firms to generate adequate profit on each unit of sales. If sales lack a sufficient margins of profit, it will be difficult for the firm to cover its fixed cost, fixed charges on debts and earn profit for shareholders.

(i) ***Gross Profit Margin ratio***: The gross profit margin indicates the percentage of each sales Naira remaining after the firm has paid for its goods [30] It is computed by dividing gross profit by net sales.[31]

Gross profit margin is given:

$$\frac{\textit{Net Sales - Cost of good sold}}{\textit{Sales}} = \frac{\textit{Gross profit}}{\textit{Sales}}$$

It is a measure of the efficiency of firms operations, as well as an indication on how products are priced. [32] The higher the gross profit margin the better and the lower the relative cost of the merchandise sold.

(ii) ***Net Profit Margin***: Net profit is obtained when operating expresses interest and taxes are subtracted from gross profit. The net profit margin ratio is measured by dividing net profit after tax by sales.

Net profit margin is given: [33]

$$\frac{\textit{Net profit after taxes}}{\textit{Sales}}$$

It measures the efficiency of the firm's profitability. The ratio also indicates firms capacity to withstand adverse economic conditions.

A firm with a high net margin ratio would be in an advantageous position to survive in the face of falling prices, rising cost of production or declining demand for product than would be the case were it to be low. Similarly, the higher the better.

PROFITABILITY IN RELATION TO INVESTMENT (ROI)

Making profit is not just enough, it has to be compared to the total capital invested by owners and creditors to see whether a firm produces a satisfactory profit on its asset base. Otherwise, it may be misusing its assets.

iii) ***Return on investment/Return of total Assets ratio:***

Measures the overall effectiveness of judgement in generating profit with its available assets. It is calculated as follows.[35]

RIO/Return on total asset is given:

$$\frac{\textit{Net profit after taxes}}{\textit{Total Asset}}$$

The term investment may refer to the total asset or net assets. This ratio measures the rate of return on investment (ROI), or return on assets. The higher the firm's return on investment the better.

iv) ***Return on shareholders' equity (Net worth) or ROE***:

The ratio (ROE) compares net profit after taxes (Minus preferred stock dividends,

if any) to the equity that shareholders have invested in the firm[39] It is computed as follows:

Return on equity (ROE) is given as:

$$\frac{\textit{after Net Profit taxes}}{\textit{Shareholders equity}}$$

Common shareholders are entitled to residual profit. The rate of common dividend is not fixed; the earnings may be distributed or retained in the business.[40] A high return on equity often reflects, the firm's acceptance of strong investment opportunities and effective expenses management.

2.4.5 COVERAGE RATIOS

Debt ratios as earlier discussed are static, and fail to indicate the firm's ability to meet interest obligations[41] Coverage ratio are designed to relates the financial charges of a firm to its ability to service, or cover them[42]

i. Time interest earned[43] OR interest coverage ratio.[44] is determined by dividing earnings before interest and taxed EBIT by the interest charge.

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TIE or interest coverage ratio is given by:

$$\frac{EBIT}{Interest\ charges}.$$

The ratio serves as one measure of the firm's ability to meet its interest payments and thus avoid bankruptcy.[45] Failure to meet annual interest cost can bring legal action by the firms creditors, possibly resulting in bankruptcy.[46] In general, the higher the ratio, the greater the likelihood that the company cover is interest payments without difficulty. It also sheds some light on the firm's capacity to take on new debt.

ii. Total debt coverage ratio:

This ratio is similar to the interest coverage ratio above, except that it measure not only the firm ability to pay its interest charges but also its ability to repay the principal of loans or make sinking funds payments.

Total debt coverage ratio is given by:

$$\frac{EBIT}{Interest + \frac{Principal}{I - T}}.$$

Where t = Tax rate

The reason for principal repayment by I-T is that interest is paid before tax and since both are to be used as denominators, then, the lower the ratio the more risky, that is, from the point of view of the creditor. And the higher the ratio the better for both the owners and the creditors.

2.5 LIMITATIONS OF RATIO ANALYSIS

Although ratios are exceptionally useful tools, they do have limitation and must be used with caution. First, the following are some of the limitation of the ratio analysis.

1. First, ratios are constructed accounting data, which are subject to different interpretations and even to manipulation. For example, two firms may use different depreciation methods or inventory valuation methods, and depending on the procedures followed, reported profit can be raised or lowered.

2. A Financial Manager must also be cautious in judging whether a particular ratio is "good" or "bad", as well as in forming a composite judgement about a firm on the basis of a set of ratios.

For example, a higher inventory turnover ratio could indicate efficient inventory. Management, but it could also indicate a serious shortage of inventories and suggest the likelihood of the firm's running out of items in demand.

3. When financial ratio analysis indicates that the patterns of a firm depart from its industry norms, this is not an absolutely certain indication that something is wrong with the firm.

4. Conversely conformance to industry composite ratios does not establish with certainty that the firm is performing normally and is being managed well.

5. Another limitation of ratio analysis arises from the fact that the methodology is univariate - that is, each ratio is examined in isolation, and the combined effects of several ratios are estimated solely on the judgement of the financial analyst.

6. The ratios are generally calculated from past financial statement and thus are no indicators of factor.[48]

7. When firms use difficult operating and accounting procedures, it maybe difficult to compare their ratios.

8. The situations of companies are never the same. Similarly, the factors influencing the performance of a company in one year may change in another year.Thus, the comparison of the ratios of two companies becomes difficult and meaningless when they are operating in different situations.

9. There is no industry standard as always recommended. To overcome this shortcoming of rationalists, researchers have combine different ratios to form predictive models. The statistical methods most commonly used for this purpose are:

   i) Regression analysis, in which past data are used to predict future values of dependent variable, and

   ii) Discriminate analysis, in which an index is calculated for firm and then used to classify it with regard to its overall financial strength.[49]

2.6 DISCRIMINATE ANALYSIS APPROACH

A number of empirical studies have tested the predictive power of financial ratios. Reliance on certain ratios depends on the analyst's perception of their predictive power relative to the problem at hand: a perception based on either subjective beliefs or empirical analysis. Most estimates of the predictive power of financial ratios are based on the analyst's past experience with them. By their very nature, then these estimates tend to be subjective and to differ from one analysis to the other.[50]Since the beginning of the development of financial ratios, different researchers have in different studies discovered some predictive power of financial ratio and they are as follows:

1.(a) Financial ratios and corporate failure

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2.(b) Financial ratios and corporate risk

3.(c) Financial ratios and bond rating

4.(d) Financial ratios and rapid growth and profitability firms

5.(e) The usefulness of financial ratios to investors in common stock.

FINANCIAL RATIOS AND CORPORATE FAILURE

Past research on the ability of financial ratio to predict some sort of business failure is reviewed as follows:

First, the predictor power of individual ratios based on either the ratios trend or its magnitude and the second category or predictive ability studies. Utilised a multivariate approach. Relying primarily on the statistical techniques, discriminate analysis researchers have been able to use sets of ratios to predict the continuation or otherwise of the firm. The works of the following people in the first category are taken into consideration.

Smith and Winakon (1935) [50] studied a sample of 183 firms which have experienced financial difficulties during the period of 1923-31 and had failed by 1931. They analysed the prior ten years trends of the means of 21 ratios and concluded that the ratio of net working capital to total assets, whose decline began ten years before the occurrence of financial difficulties, was the most accurate and steady indicator of failure. Actually their data indicated that the long-term solvency ratios were equally good indicators.

Fitz Patrick (1931 and 1932) - Followed a different approach by analysing the prior three to five years trends of thirteen ratios of twenty firms that had failed during 1920-29. He studied the data on a case-by-case method of analysis and followed it up by comparative analysis and matched sample of nineteen successful firms. He concluded that his ratios predicted failure to some extent through declining trends, but his best predictors were the net profit to net worth and the net worth to total debt ratios.

Charles L. Merwin (1942). Both of the above studies were culminated in Merwinn's study of a sample of 939. Firms in the period 1926-36. He divided his sample into two groups "continuing" (Successful) and "discontinuing" (unsuccessful) firms and analysed number of ratios of each group. He accomplished this by comparing industry mean ratios of discontinuing firms with "estimated normal" ratios which were estimates of what the discontinuing firms ratios would have been had they maintained the same average ratios as continuing firms. He concluded that three ratios were very sensitive predictors of discontinuance, up to as four to five in some instances. These ratios *were net working capital to total assets, net worth to total dept and the current ratio*. They all exhibited declining trends before discontinuance and were also below the estimated normal ratios.

Beaver (1967) Considered a sample of seventy-nine (79) large firms that failed and compared with corresponding non-failed companies of the same size and industry. The data collected were for the same years. These samples were used to test the predictive ability of thirty financial ratios. The mean values of the ratios for the two samples were compared over the five years prior to failure. He discovered that the mean ratios of the failed firms differs significantly from that for the non-failed firms. It also deteriorated markedly as failure approach. In another study, Beaned (1968) examined the ability to predict failure from changes in market price of stock comprising of four ratios: cash flow to total liabilities, net income to total assets, total dept to total assets with the market behaviours of price on a sample of seventy-nine (79) failed and corresponding number of non-failed firms of approximately same size and Industry. He found that the median market price of the failed companies. The largest price decline occurred in the final year. Beaver concluded that investors adjust stock prices to the deteriorating condition of failing companies. Moreover, he found the evidence to be consistent with investors assessing likelihood for failure on the basis of financial ratios.

Daniel (1968) [55] Employed correction factor analysis and wise regression to select financial statement data and ratios which best correlated with failure and non failure as the dependent variable. The discriminate function was found to have considerable power in identifying failing firms.

Dealing (1972) [55] Using fourteen ratios, studied a pair of thirty two failed and non failed firms for the period between 1964-70 in a discriminant function and he discovered that he could predict bankruptcy three years before the failure.

Administer (1972)[56] Tested the predictive ability of financial ratios on small business starting with fifteen ratios. He concluded that quick assets to correct liabilities, working capital to sales, net income plus depreciation and amortisation to current liabilities, net worth tassels, current liabilities to net worth, inventory to sales incorporated in discriminant function predicted failure for up to three years on commutative data analysis.

Wilcox (1973)57 used a pair samples of fifty failed and non-failed firms over a period of 1949-7. He adjusted both the cash position and cash flow for both samples and used the gambler's run model in which he ranked the risk of bankruptcy of all firms in the sample for five years prior to failure.

Mover (1977)58 Employed Altman's discriminant functions of ratios as parameters generated from a different period (1946-65) on a newly generated data (1965-75) and found that the predictive ability of the model has dropped considerably. He found that the predictive ability of the model to be increasing as he excluded "Super flows" variable from it. He also found the model to be a better failure predictor than other models when he compared them.

Altman (1968)59 used multiple discriminant analysis (MDA) as no one particular ratio is strong enough to measure the performance of a firm. Altman therefore used various ratios on variable in a discriminant function to predict and categorise firms into bankrupt and non-bankrupt. He took 22 ratios and submitted them to linear Discriminant approach (LDA) and came out with ^{5} ratios.

He took 66 organisations, 33 bankruptcy and 33 non-bankruptcy and mixed them up. Then, finally calculated their Z values He defined Z as the overall index or barometer or the temperature and finally arrived at the following:

$Z = a1 \times 1 + a2 \times 2 + a3 + 3 \ a4 \ x4 + a5 \times 5$

$Z = 0.12 \times 1 + 0.014 \times 2 + 0.033 \times 3 + 0.006 \times 4 + 0.99 \times 5$

Where x1 = The ratio of working capital to total assets

x2 = Retained earning to total assets

x3 = EBIT to total assets

x4 = Market value of equity to Book value of total debt

x5 = Sales to total assets

Altman used Z values as follows:

If Z value is greater than 2.99. the firm is healthy

If Z value is less than 1.81 then, the firm is bankrupt.

He later discovered the *critical* or grey zone to be 2.675 and maintained that any Z above 2.675 is non-bankrupt firm below 2.675 to be bankrupt.

Lastly, He discovered that he could predict bankruptcy with an accuracy of 50,72 and 95% for the third, second and first year prior to failure respectively. The model was extremely accurate in classifying 95% of the total sample correct. A type 1 error occurs when we classify a firm as healthy when it is actually bankrupt. A type 11 error also results when a firm is classified as bankrupt when actually it is healthy.

Altman, Haldman and Narayana (1977) 60 , reviewed Altman's study and adopted it to the period 1969-75. They used a sample of fifty-three (53) failed and fifty-eight (58) non failed firms including retailing firms. They employed factor analysis and seventy variables which

were reduced to current ratio, the size of total assets, interest ration, retained earning, return on assets (not income to total assets) and equity to total assets. This was incorporated in a discriminant function and the model predicted failure with 96 and 70% in the last year and the year prior to failure respectively.

FAILURE RATIOS AND CORPORATE RISK

Most of the studies in the area of prediction of corporate risk by means of financial ratios were concluded in the 1970s. The following studies are considered useful to that effect.

Ogler (1970)61,

Developed a credit scoring model for commercial bank loans using twenty one ratios selected from all but valuation ratios category. He found that he could predict good loans with some degree of success. This could be considered as a risk measure for investors.

ATHMAN ETAL (1974) 67

Used discriminant analysis on forty-one (41) ratios and use data on 134 firms. They discovered their model to be useful predictor of risky loans (those with repayment problems).

FALK AND HEINTS (1975) 63

Analysed forty-one industries for two years 1971-72 using average total assets to sales, total assets to working capital and average accounts receivable to sales, as a composite index for each of the industries. Their aim was to analyse the characteristics of each industry as reflected in its financial ratios as to be able to rank them according to risk. They succeeded in ranking a number of industries based on above facts.

FINANCIAL RATIOS AND BOND RATING

A study by Hickman (1948)64 studied the return on corporate bond issued between 1900-1943. He concluded that time interest earned ratio and net profit to sales ratio were useful predictors of defaults on bond issues, whether used jointly or separately. The firms with higher ratio went into default less frequently than those with lower ratios.

SAULNIER ETAL (1958)[65]

Studied the U.S federal landing and loan insurance for the period of 1934-51 and conclude of that firms twits very low current ratio, net worth to total debt ratios were more likely to default on loans. Also, firms with deteriorating current ratios prior to borrowing defaulted about twice as often as those with stable or increasing ratios.

MOORE AND ATKINSON (1961)[66]

Examined the aggregate data involving change in bank credit use and financial ratios during 1955-57. They found that firms with higher current ratio and working capital to total assets, net work to total debt and net profits to net work ratios increased their use of credit more than other firms.

WOJEN LOWER (1962)[67]

Examined the quality of bank loans and analysed those loan that were criticised loans by banks in 1957 from three to total assets debt to total capital, coefficient of variation to total assets, net income to interest and net profit to total assets. This analysis was limited to investment bonds as moody rating.

WESTERN (1970)[71]

Used a multiple regression model counting four variables, the logarithms of earning variability, period of solvency market value of all bonds outstanding and market value of stock to debt ratio, to predict up to sixty-two percent of the actual rating by moody's.

PINCHES AND MINGO (1973)[72]

Analysed 182 bond for one year, 1967. Financial data were calculated on thirty-five different variables. They used factor analysis and M-group multiple discriminant analysis, and they developed a model consisting of six variables subordination (which represents the legal status of bonds) year of consecutive dividends issue size (this indicated that bond ratings and the size of bond issue are related, net income plus interest to inters (coverage ratio) five years means of long term debt or total asset (measuring capital structure) and net income to total assets. The model grouped 182 bonds with 69.7 percent success of actual bond rating by moody.

RATIO AND RAPID GROWTH FINANCIAL AND PROFITABILITY FIRMS

Some of the notable works conducted in this area are as follows:

Horrigan (1965)[73]

Determined that some shot-term liquidity and profitable and unprofitable firms, that the profitable firms showing higher ratios but capital turnover ratios were not significantly different.

Jackend - Off (1962)[74]

Found that financial ratios consistently and clearly distinguished between profitable and unprofitable firms in the period of 1949-1955. The current ratio, the working capital to total assets and net work to total debt ratios of profitable firms were consistently higher but the

relationship of total assets to turn over appeared to be inverse to the size of the firms. In another study of various trade industries in 1956, it indicated that short-term liquidity and long-term solvency ratios of profitable firms were higher, profit margins and inventory turnover of profitable trade concerns were also higher but working capital turnover was lower.

Osaze (1981) [75], In a study on financing rapid growth firms in Nigeria discovered that ratios adequately discriminated between growing and non growing firm.

THE USEFULNESS OF FINANCIAL RATIOS TO INVESTORS IN COMMON STOCK

O'connor (1923) [76]

Used correlation analysis to reduce from 33 to 10 ratios, the number of variables employed in his model for predicting average investors rate of return on common stock and noted that a generally (i.e. less than 0.25) inter-connections existed between the 10 indicated potential effectiveness as predictors. It should be noted, however that O'connor research is only on record for its conclusion has been rejected by a researcher Abdul-Khalik the regression equation and the estimated parameter used by O'connor were invalid for the prediction they were meant. He went on to give his reasons (three) for the assertion he made these reason were accepted by the first researchers and others.

RECENT DEVELOPMENTS IN FINACIAL RATIOS

Investment decision have assumed on important position in the development of financial management, where the first contribution have been made in the area of financial ratio analysis to provide more accurate tools of assessing business performance. The prominent among which is univariate and multivariate analysis most of this have to do with corporate bankruptcy.

UNIVARIATE ANALYSIS

This approach is called Data Analysis. The analysis examines the association between relative risk measures of security and a single accurating variable. The unvariate analysis requires comparing earning with the earnings of the other firms, just as ratios are compared with industrial average. The unvariate analysis was first published by Hall and Brown ,1969. When they examined 269 firms quoted on New York Stock Exchange (NYSE) over the period between 1964 and 1966.

MULTIVARIATE ANALYSIS

As an extension of financial ratio analysis, multivariate analysis deals with the predictor of corporate bankruptcy. There are many contributions, but the most prominent is Edward [1]. Altman's (1968) [77] multi discriminant analysis (MDA). It is not possible to predict the overall financial health of an organisation by using single ratio, Altman, therefore, uses various ratios on the variable in a discriminent function to categorise borrowers into two groups. Those that did and those that did not go bankrupt.

BSLUM (1974) [78]

Developed the failing company model. Using 115 failed and 115 non failed firms during 1954-1968. He selected for each firm in his sample a firm that did not in the same industry, of approximately the same asset size, number of employees; and collected data for the fiscal years.

His conclusion was that the model he used distinguished failing from non-failing firms with accuracy of approximately 94% when failure occurred are of year from the last financial statement date. The model was also 50% correct in predicting failure two years before its occurrence and 70% for three, four, five years prior to actual failure. The failing company model of Blum is provided below

(1) Liquidity:-

(a) Short-term liquidity flow:

(1) The " quick flow ratio" that is cash + note receivable marketable securities + (annual sales) (cost of goods sold - depreciation expenses 12 position.

(2) Net quick asset/inventory

(b) ***Long-term liquidity flow:-***

(3) Cash flow 1 total liabilities

(4) Networth at fair market value 1 total liabilities

(5) Net worth at book value 1 total liabilities

(6) Profitability Rate of return to common stockholder who invest from minimum of three years.

(7) Standard deviation of net income over a period

(8) Trend broads for net income

(9) Scope for net income

(10-12)Standard deviation, trend breaks and scope of the ratio: net quick assets to inventory variables 10, 11 and 12 are only used for the first and second before failure.

OSAZE'S (1985) INDEX OF RISK [79]

This is a financial composite index for predicting corporate failure in Nigeria. The index was developed specially for use in development countries like Nigeria to compensate for the too much reliance in financial ratio analysis and other models developed in Europe and America for prediction of risk in a business or more clearly corporate failure. A detailed analysis is shown in chapter 4.

FOOTNOTES

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CHAPTER THREE

BANKING ENVIRONMENT AND BANKING DISTRESS

In the last five years or so several terminologlies have been used to describe the state of health of Nigerian banks and other non-bank financial institutions. These terminologies include *unhealthy, distress, technical insolvency* etc. But the most commonly used term among all the available alternative is ***distress***. However, form monetary and financial point of view the health of a financial institution is most aptly described by the terms solvency insolvency and liquidity/illiquidity. ***Solvency*** can be defined as the *ability of a bank to adequately meet its long term obligations to its customers and banking public, while* ***liquidity*** *is the ability of a bank to meet its daily obligations to its customers.*

Since the commencement of deregulation in 1986 the Nigerian financial industry has witnessed tremendous growth in terms of numbers, volume and value of transactions. This, coupled with the upsurge in the number of banks, 500 finance houses, 256 primary mortgage institutions about 200 bureau de change, hundreds of community banks, stock brokers, issuing houses, etc. led to stiffer competitions in the industry. Also this unrestricted explosion generated unethical activities and sharp practices with cut-throat competition for survival. In short, the financial sector became a battlefield for the survival of the fittest, with financial institution being forced to take higher risks.

Usually, risks if not well calculated lead, ab-initio to the depletion of financial assets. However, in the financial sector, especially the banks, the degree of investments (risks) is influenced by depositors funds which are short-term in nature. Thus, for a bank to survive it must have the ability to meet its depositors' demand. Inability of any bank to meet this customers' obligation as at when due portends a financial problem.

Typically, financial problems manifest in distress or unhealthy position. The reason for this is simple. An establishment which is unhealthy in the short-run may likely become distressed in the long-run. As mentioned earlier, the two most fundamental problems of a distressed financial institution are illiquidity and insolvency. There is, often, a causal relationship between the two - when the problem of liquidity persists for a very long time, it could lead to forceful sale of assets below their market values. Such forced sales when so large, could lead to insolvency.

Basically, financial distress can manifest itself in any of the following ways:

i) *Illiquidity* resulting in increased demand for resources which cannot be met in the short-run.

ii) Assets liabilities mismatch resulting from poor portfolio management.

iii) Negative net worth which may be covered up by paper profit.

iv) Inproportionately high operating cost resulting from over staffing, over branching, jumbo remuneration packages, internal controls and erection of prestigious office, and other white elephant projects.

v) Deterioration in the portfolio due to accumulation of bad debts and

vi) Management ineptitude - lack of experience, drive and integrity .[1]

In assessing the financial condition of a bank, it is customary to evaluate its capital adequacy, its asset quality, its quality of management (and staff), its level of earnings and the adequacy of its liquidity. Also, experience has shown in Nigeria that ownership structure and type of banks are important factors in explaining the financial condition of a bank. It is sometimes sufficient to evaluate capital adequacy, asset and management quality of a bank because these indices determine the earning level and liquidity position.[2]

3.1 NATURE OF DISTRESS IN BANKING INSTITUTIONS

Up to the middle of 1980s, banking was a respected profession in Nigeria. But with the proliferation of banks from the late 80s and unto the early 90s the quality of banking services started to deteriorate, especially the confidence and ability of banks to honour their obligations to their numerous clients, Great moral decadence, favouritism, avarice, etc., became the order of the day. Management neglect of generally approved standards becomes so rampant that the public confidence in the banking institution became greatly eroded.

Deception, distortion and failure to make full disclosure became a way of life in these banks. It came to a point where the inevitable could no longer be postponed, the bubble burst, hence the distress in the industry.

Since 1992, the incidence of financial distress among financial institutions has become rampant. Operators in all segments of the financial services market have had to cry aloud as their ability to resist further economic financial and political turmoil waned considerably. Commercial and merchant banks, finance houses, community and mortgage banks all have traces of the distress symptom. A good number of financial institution have already gone under while some others are barely managing to maintain a patchy existence. Currently about 50% of banks and non-bank institutions are distressed.

However, distress in banks and other financial institutions is not a financial phenomenon that is peculiar to Nigeria, rather it is a world wide phenomenon which did occur in Nigeria in the early years of banking.

Distress of a financial institution does not occur overnight. It is a gradual process of decay and degeneration which can be corrected if adequate palliative measures are taken promptly.[3]

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3.2 BANK EXAMINATION CRITERIA OF CAMEL

Before any bank or finance institution can be classified as distressed using any of the common nomenclature, it must have been examined and rated using the bank examination criteria of CAMEL.[4]

C - Capital Adequacy

A - Asset Quality

M - Management Competence

E - Earning Strength and

L - Liquidity Sufficiency

These parameters adequately cover every factor required for a sound bank management. Hence the nature of distress can be determined by the severity of the rating. It is therefore necessary at this point to examine these parameters one after the other.

3.2.1 CAPITAL ADEQUACY

This is a measure of solvency i.e. the ability of the capital of the financial institution to meet the assets acquired. A banks capital is normally defined as the shareholder or equity funds available to the bank. Such shareholders funds include :

(1) Paid up capital

(2) Retained earnings

(3) Share premium

(4) Statutory reserves and

(5) The general reserve all free provisions.

Capital adequacy can be measured by the following ratios:

i) $\frac{\textit{Total Capital}}{\textit{Total Assets}}$

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ii) ***Total Capital***
Total Deposits

iii) ***Total Capital***
Risk Adjusted Assets

iv) ***Total Capital***
Total Loans & Advances

v) ***Total Capital***
Fixed Assets

These ratios can be computed from the financial statements or balance sheets of the financial institution. The total capital to total assets ratio is particularly informative as the bank is expected to finance its fixed assets from its internal capital.

3.2.2 ASSET QUALITY

Bank assets determined the extent to which the bank can perform its primary function of credit delivery. Numerically a bank's assets are the summation of its liabilities and its net worth or capital. There is no gain saying that the survival of a bank depends on its ability to acquire the right kinds of assets as well as maintain the right structure and portfolio assets. The key to sound bank management thus lie in possessing assets of the highest yield potentials counter balanced by assets adequate liquidity.

The structure of a bank's assets can be divided into three groups namely:

i) Liquid Assets and Short-term funds

These are assets which are either cash or can easily be converted into cash. These assets are kept in liquid form both for satisfying CBN requirement as well as to provide ready cash for daily transactionary needs of customers. The liquidity index of a bank measure by the ratio:

Cash and short-term fund
Total Assets

It should be noted that because cash on its own cannot generate income, a highly liquid bank may not likely be very profitable if it is not having enough investments in income earning assets.

ii) INCOME Earning Assets

These are assets that are acquired for the purpose of generating income.These assets are selected for their income potentials inaddition to maintaining an acceptable level of risk exposure and guarantee of recovery when the need arises.

The earning power of the bank is measured by the ratio of

$$\frac{\textit{Income Earning Assets}}{\textit{Total Assets}}$$

The higher the ratio the higher the profitability of a bank. Therefore, banks maximise their earning ability by investing the greater part of their assets in IEA.

iii) Non-income earning assets

These are non- income generating properties. They are are either operational assets or fixed assets such as building, computer, vehicles, etc.

3.2.3 MANAGEMENT COMPETENCY

Management of a bank or any other enterprises can be said to be entrepreneurial spirit behind it which optimally utilises the resources at its disposal to meet its objectives of rendering excellent services, securing customers deposits and making profits. Some of the indices used to assess good management in bank include the following:

i) Professional competence

ii) Adherence to banking policies and regulations

iii) Controlling all costs e.g. cost of funds and administrative costs.

iv) Cognitive initiative to strategically forecast and plan to meet the dynamic economic environment.

v) Compliance with properly established internal checks and balances

vi) Sterling leadership qualities which motivate employees to put in their best.

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Any management that optimally satisfies these requirements must be good enough to put bank on sound footing. Apart from these qualitative measures management performance can be technically adjudged based on the following criteria: ***Capital, Growth rate, Earnings Level, Asset quality, level of fraud, etc.***

3.2.4 EARNINGS STRENGTH

This is the ability of the bank or financial institution to make money and subsequently make profit. It is obvious that a company or any business enterprise will not survive if it fails to make profit ensures its survival, both in the short and long run.

The earning strength of a bank can be evaluated by compiling certain ratios from the banks financial statement, such ratio will include:

i) $\frac{\textit{Total Earnings}}{\textit{Total Assets}}$

ii) $\frac{\textit{Total Earnings}}{\textit{Total Capital}}$

iii) $\frac{\textit{Total Earnings}}{\textit{Fixed Assets}}$

iv) $\frac{\textit{Profit before tax}}{\textit{Total Assets}}$

v) $\frac{\textit{Profit before tax}}{\textit{Total Capital}}$

vi) $\frac{\textit{Profit before Tax}}{\textit{Total Number of staff}}$

vii) $\frac{\textit{Profit before tax}}{\textit{Total No. of Management staff}}$

viii) $\frac{\textit{Profit before tax}}{\textit{Total number of branches}}$

3.2.5 LIQUIDITY SUFFICIENCY

Bank liquidity can be determined by the level of liquid assets it has. Such liquid assets like cash and other short term funds can be employed in meeting the bank's transactionary need, precautionary needs against unforeseen demand for cash and CBN liquidity ratio requirements.

As is the case with other rating factors, this can also be evaluated by generating appropriate ratios from the balance sheet figures. These ratio will include:

i) $\frac{\textit{Total Cash in vault and CBN}}{\textit{Total Deposits}}$

ii) $\frac{\textit{Total funds on call}}{\textit{Total liabilities}}$

Does the bank have to resort to overnight borrowing in order to cover its position with the

CBN or its bankers? Is it a regular feature or a once only feature? While a bank must maintain adequate liquid funds, excessive liquidity is not in the best interest of the bank.5

3.3. THEORETICAL BASIS FOR BANK DISTRESS

A number of theoretical explanations have been offered in recent times for distress among financial institutions. Prominent among such theories are:

1) The business cycle theory

2) Credit market conditions Approach

3) Monetary Approach

(1) *THE BUSINESS CYCLE THEORY*

This theory holds that the financial environment responds endogenously to the state of the business cycle or to some displacement that opens up opportunities for profit. This means that financial institutions or businesses are generally more vulnerable to economic shocks during the period of expansion while this does not imply that financial crisis occur at the peak of the business cycle, it suggests that crisis results from systematic forces that develop near the peak.[6]

(2) CREDIT MARKET CONDITIONS APPROACH

The basic argument here is that since the demand for credit is interest inelastic, at the peak of business cycle, any interruption of the supply of credit would trigger a business down-fall. In Nigeria, the high rate of interest on bank credit created debt servicing problems and resulted in the accumulation of bad debt by banks.[7]

(3) MONETARY APPROACH

Friedman (1963)
Advocated that financial crisis need not occur at any particular stage of the business cycle but could develop whenever the central bank's control of the money supply or reserve money is erratic and results in excessive monetary tightening. Banks are suddenly forced to sell assets in order to obtain needed reserves. This forced sale of assets reduced their price, raises bank interest rates, threatens bank solvency and reduces confidence Indeed some experts point to such erratic monetary policies of the CBN as the frequent use of stabilisation securities as having contributed significantly to the current distress in the financial sector.[8]

3.4 CAUSES AND SYMPTOMS OF DISTRESS

Many factors account for the distress situation in our financial environment. These factors are either exogenous (outside the control of the bank) or endogenous (factors within the banking industry). These factors are examined one after the other.[9]

EXOGENOUS FACTORS

1. Adverse Economic Conditions

The performance of any economy has a direct impact on the financial sector. The economic down-turn since the early 1980s is reflected by high inflation. Large fiscal deficits, a heavy debt burden and slow growth arising from the stress in the economy. This resulted in many borrower not being able to service their loans thereby making financial institutions to develop virus. The inability of borrowers to repay their loans give rise to poor quality assets, lower earnings and general illiquidity.10

2. Policy Environment

The monetary and fiscal policies of Nigeria have always changed at such a pace that both players and spectators were at a time confused. Some have been so harsh and unfavourable that they left unhealed scars on the banking sector. Among the various unfavourable policy measures taken., three stand out as having had the most influence on the present level of distress in banks. They are:

i) The Abrupt withdrawal of the public funds from banks in 1989.

Apart from denying the banks the biggest source of loanable funds, this measure was viewed by the banking public as a sign of official mistrust. If the government that licensed these banks cannot trust them, who else is expected to trust them. This, to some experts, is the genesis of bank failure of today.

ii) The use of stabilisation securities and the system of foreign Exchange

Stabilisation securities are instruments of indirect monetary control which is a rigid form of open market operations.The securities re-issued by CBN and are directly allocated to banks without any option or choice, at a price determined by the CBN. Frequent use of this measure renders the banks illiquid.Similarly, the AFAM requirement that banks deposit the Naira equivalent of the forex demand in CBN before each intervention contributes to their illiquidity. In fact the 1994 CBN money and credit guidelines confirmed the as one of the causes of illiquidity in banks.

iii) Enactments Of Money Laundeering Decree

This decree set limits on cash payment through a commercial bank by a person and corporate units to #500,000 and #2 million respectively, and to report payments above that limit to CBN and NDLEA. It also empowers the NDLEA to place any bank account under surveillance and may tap telephone lines and have access to bank's computer data. This decree had discouraged many traders who handle large amounts of cash from passing it through the banking system, thereby denying it much desired liquidity.

3. Deregulation of the Financial System

The ware of deregulation currently sweeping the industry had also impacted on the health of some banks. It has brought about increased competition and innovation with visible traces of strain on the financial system. Some financial institutions, that had previously been protected from competition do not have the management expertise to survive in an increasing complex, volatile and competitive market resulting from the deregulation exercise.[11]

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ENDOGENOUS FACTORS

1. Under Capitalisation [12]

Apart from the initial capital provided by shareholders most of the banks did not have more capital injection one would read in the papers that bank "A" has increased its share capital from amount "Y" to "X" million Naira paid up 80% of this amount of increase. But deep down the records is new funds were paid. All were a cover up, deceiving people (investors or depositors) who rushed to the banks as being financially healthy. Yet all was a white wash or window dressing. In fact, some of the initial capital had been eroded by over drawing of loans granted to directors above the statutory lending limits allowable to directors/shareholders of the banks.

2. Board Room Crisis

There are often serious conflicts of interest among the directors. The Directors and their companies are major borrowers of depositors funds. These conflicts of interests led to the rat race at the expense of the banks development and progress. Some of the directors lack vision and business acumen hence they lack the capacity for strategic or long term planning required for continuity and stability of a business entity. They employed all shades of characters without clean credentials. These fellows are incompetent and inexperience to assume very senior position in the banks. Some who are competent for the job allowed themselves to be used and this landed them into trouble.

Inputs from experienced expert staff in various field within the system, were not harnessed to enable proper appraisal on the financial and technical viability of such decisions. Most of the time, and of the thumb approach in decision making process was adopted and failure was the result.[13]

3. Employment of Chief Executive Officer

For appointment to the post of a chief executive officer of a bank, it is required that apart from the requisite qualification, the person must be a high calibre staff with high moral integrity; the person must have acquired sound experience in various facets of banking: most essentially a sense of humour required to carry other along. "He who governs others, first should be a master of himself". Some worked in one or two departments, the number of years required just for experience to qualify for this position. Some never even become branch managers-a position which could have exposed them to more facets of banking. This was not the case as some who were even exposed, lacked words, discipline and leadership qualities.[14]

4. Employment of Retired Staff by Chief Executive Officer:

One of the conditions the CEOS usually present to their Board when negotiating their employment is to be allowed to employ their trusted and capable hands who they feel will produce the needed results. Some of these supposed trusted hands have been discovered to a ploy to deceive the board. Their employment is to clear grounds to enable them carry out whatever they intended to do and consolidate themselves financially. These purported trusted capable hands; associates wolves and mercenaries, are placed in strategic positions, they in turn bring in their own loyalists also. Dividend loyalty is illegal in any establishment, if at all it should be done discretely. But this is openly done without regard to ownership of the banks. In doing all these, many good and dedicated staff who are more experienced than these staff brought in are relegated to the background. Hence frustration, low morale and demotivation. Latent, negative informal organisation that hinder the progress of the banks are developed. Usually employee morale and motivation are positively gingered if those employed for higher positions are more knowledgeable and verse on the job. Some of them who are brought in and made branch managers, never made profit in the respective branch, they manned and are less concerned and shameless in their dealings. This shows that they are only after the benefit of the position and not the work therein. A good manager without any sinister motive can always work anywhere and with any competent and dedicated staff to achieve the best. Some of them forget that if the banks progresses, their rating go up. But if the banks go under, they sink with the bank. [15]

5. *Other Staff Employment*

Generally, staff of different characters are hired. No proper screening took place. some are hired on the basis of mere references on call cards. Because of this, general attitude to work is deplorable. Some regard themselves as sacred cows. Rules of the organisation are flouted. There is no regard to discipline or decorum staff believe in god-fatherism.

Some made management staff abuse positions because of their lust for the opposite sex, they go for anything in skirts and lose their sense of judgement and rationality. They go to the extent of displacing fellow innocent dedicated subordinate male staff on fabricated, flimsy excuses to pave way for nincompoop female secret lovers. In this kind of situation, they can not manage well or effect discipline on the staff.[16]

6. *Staff Union*

This has never been allowed to exist in the new generation banks which are now mostly distressed. The existence of Staff Unions in older banks made contributions to staff welfare. Staff unions act as check on certain decisions which are not based on equity.17

7. *Ethnicity*

Ethnic bias in appointments and placements to distress in that inexperienced hands were place in sensitive positions requiring tested, experienced hands. Some top management staff tried to fill almost all the vacancies available with people from their own ethnic group without regard to competence.

The greatest harm done to the banking system is that people who should have no business working in banks in the sense that they have no natural calling or inclination at all have found their way into the bank. They therefore bastardise and lower standards with-in the system.[18]

SYMPTOMS OF DISTRESS

Financial distress does not come in one swoop.It is important therefore to identify the early warning signals that can help both management and regulatory authorities to take decisive steps to stem the problems.[19]

The following are some of the negative trends evidencing potential distress in banks.[20]

i) ***Small loan losses***:If persistent they can gradually leave a bank unable to honour its obligations.

ii) ***Drop in earnings***: The net interest margin must be watched for a significant drop could be an indicator of potential distress.

iii) ***High staff Turnover***: High turnover of personnel, particular at the top and middle cadre management levels may be one of the early signals of stress.

iv) ***Recovering liquidity constraints***: Frequent liquidity shortfalls may be the signal of a deep rooted problem.

v) ***Exit of some major Depositors***: The lose of major industry names could be as a result of a weekend competitive ability in the market.

vi) ***Growing incidence of fraud/weak internal structure***

vii) *Inability to meet statutory ratios*

viii) *Negative examination comments*

ix) *Inadequate capital cushion, etc.*

3.5 REMEDIES FOR DISTRESSED BANKS AND THEIR CUSTOMERS

Having identified the causes of financial distress, it is necessary to suggest possible solution to the problem.

1. Deposit Insurance Option.[21]

A major reason for the establishment of a deposit insurance scheme is not only to prevent or minimise incidence of bank failures, but also to handle bank failures and liquidate problems bank assets. The possible options under the insurance approach are:

i) Pay-off

This entails the payment of insured deposits up to the insurable limit of #50,000.00 to the depositors of distressed banks in case liquidation.

ii) Insured Deposits Transfer

The deposits of the failed banks are transferred to another bank preferably within the same locality. The acquiring bank will be given enough cash to cover the transferred deposits. The NDIC then takes over the assets of the failed bank.

iii) Bridge Bank

This involves turning a failed bank over to a new bank specifically set up to assume the assets and liability of the failed bank with little or no compensation to shareholders of the failed bank.

iii) Purchase and Assumption (P&A)

This is a merger-type transaction which involves purchasing the assets of the failed bank and assumption of its liabilities by another insured bank.

v) Open Bank Assistance

This option allows a failed bank to continue to operate without a change in mine. However, it will involves change in ownership and management of the bank; injection of fresh funds in the form of equity and/or loan capital, reorganisation and rationalisation.

Other strategies employed by both the CBN and the NDIC in the management of distressed banks include the following

i) Reconstitution of Management of Distressed Banks:

Here the CBN and NDIC assumes control of the distressed bank, and constitute an interim management Board for the institution. The new board is then mandated to develop a suitable plan for revitalisation of the bank within a given period, usually one year.

ii) Holding Action on Distressed Banks:

This measure places restriction on new lending, capital expenditure and directives on debt recovery and recapitalization by management.

2. *Turn around Management Option* [22]

A turn around situation is a special general management situation typified by limited resources, poor moral, sceptical allies and urgency.The management of distressed banks have a key role to play in evolving turn round strategies for distressed banks.

The general approaches to turnaround management are:

i) Revamping the existing strategy - after diagnosing the root causes of the

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financial decline.

ii) Cost reductions - so as to improve the profitability of the bank.

iii) Asset reduction/retrenchment strategy - improve the cash flow of the firm by measures such as selling off assets no longer needed like land, plant and equipment, reduction of workforce, etc.

iv) Revenue increasing strategy - to increase volume of sales by adopting tighter inventory control, better investments etc.

v) Combination strategy - in a hopeless situation where fast decisive actions are required to restore the financial health of a bank a combination of the above strategies becomes necessary.

3.6 WORLD BANK'S STANDARDS FOR PREDICTING BANKRUPTCY

According to the world Bank's standards, a banking industry is healthy if nearly all the banks in the system are profitable and non-performing loans constitute less than 2% of total assets. On the other hand, a banking industry is in financial distress if up to 20% or more or all banks are non performing and most banks are technically insolvent.

FOOT NOTES

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CHAPTER FOUR

RESEARCH METHODOLOGY

This chapter examines the specific procedure utilised in the course of obtaining data for the research topic under study. It also explains the methodology utilised in the treatment and analysis of the data with a view to providing the basis for easy understanding of the contents of the subsequent chapters.

4.1 METHOD OF DATA COLLECTION

This research work has made effective use of the following as methods of the findings of the study:

1) The use of library research method: through examination of documents; journals, magazines, Newspapers, economic and financial reviews articles and literature relevant to the topic of the study and

2) The use of financial Statements of accounts (Statement of Accounting policies, profit and loss account, and balance sheet) obtained from the Banks under study: This financial statements cover five years.

In essence, the data used for this study is purely from primary source;Indeed the annual financial statement covering five years, (1993-1997). The followings are the two broad methods used in analysing these primary data.

1. Financial Ratio Analysis: As advocated by financial Management scholars like James Van Horne:2 James Van Horne and John M. Machwicz3, Jr. J.Fred Weston and Eugene F. Brigham,4 I.M. Pandey.5 Lawrence Gitman;6 Howard R. Elsic;7 Bradly and Myers 8 to mention just a few in order to help in analysing the healthiness or otherwise of the Banks under study over a five year period;

2. Osaze's index of risk: A financial composite index for predicting corporate failure in Nigeria.9 This is used to help in determining the OSAZE'S INDEX OF RISK.

   A financial composite for predicting corporate failure in Nigeria was developed by B.E. Osaze, (now a professor) in the department of Business Administration, university of Benin. The index was developed to compensate for the too much reliance on financial ratioanalysis and other models developed in Europe and America for prediction of risk in a business or more clearly corporate failure.

THE MODEL:

The Osaze's index of risk was developed after he reviewed the works of Beaver, W.N. (1966); Altman E.I. (1968); Johnson C.G. (1970; Bolton Report (1971); Deakin (1972) Eclmister R.O. (1972); Tham (1975); libby (1975); Tamani M. (1978); Parosh and Tamari (1979); and some other selected ratios. And these ratios in the index were selected as the ones found to be applicable to Nigerian Situation. The table below gives the details of the model:

OSAZE'S INDEX OF RISK

I.	***Net Worth-to-Total Assets:***	***Points***
	Firms with over 50% of Net worth to total assets	12
	41-50%	10
	31-40%	8
	21-30%	6
	10-20%	4
	Less than 10%	0

2. **Retained Earnings Net Profit:**

Firms With over 30% of Net profit	12
21-30%	10
16-20%	8
11-15%	6
5-10%	4
Less than 5%	0

3. **Proift Trend Over 5 Years**

Profits rising each year for five years	16
Profits stable and level each year	12
Profits each year but unstable	10
Loss in any one of the last three years	6
Loss in the first three years only	4
Loss in all five years	0

4. **Earnings Before Interests And Taxes To Total Assets:**

OVER 30%	12
21 - 30%	10
16 - 20%	8
11 - 15%	6
5 - 10%	4
Less than 5%	0

5. **Current Ratio:**

Over 2 turns	12
1.51 - 2.00	10
1.11 - 1.50	8
0.91 - 1.10	6
0.50 - 0.90	4
Less than 0.50	0

6. **Working Capital To Total Assets**

Over 30%	12
21 - 30%	10
16 - 20%	8
11-15%	6
5-10%	4
Less than 5%	0

7. **Cash Flow To Total Debt**

0ver 5 times	12
4 - 5 times	10
2 - 3 times	8
1 - 2 times	6
0.5 - 0.9 times	4
Less than 0.5 times	0

8. **Sales Of Accounts Receivables**

Over 5 times	12
4-5 times	10
2-3 times	8
1-2 times	6
0.5--0.9 times	4
Less than 0.5 times	0

Note: On the basis of this index it was concluded that:

(1) Any firm that scores over 60 points is unlikely to fail or default on a loan.

(2) A firm with less than 40 points has a high probability of failure, while

(3) A firm with between 40 and 60 points belongs to the grey area that must be scrutinised properly before a decision is taken as to its potential for bankruptcy or success.[11]

4.2 RATIONALE BEHIND THE USE OF THE OSAZE'S INDEX OF RISK

Indeed, the reasons advanced by the author of this model justified its use; namely.[12]

1. Even though financial ratios developed in Europe and America are useful indicators of risk in a company, they have little use and application in less developed economies like Nigeria because:

   (a) The ratios developed in these environments (Europe and America) have been generated from large companies in contrast to those operating in developing countries; and

   (b) They are more useful to the developed economies as the availability of sophisticated computing facilities has ensured the generation of large data bases for developing productive models on business operations.

2. The index and weight have evolved from studies of financial statement of failing and failed firms in Nigeria.

3. It was also determined with inputs from bankers and loans offices in Nigeria notably the first Bank of Nigeria, New Nigeria Bank, Union Bank, Bank of the North, Nigeria industrial Development Bank; the Nigerian Bank for Commerce and Industry; and the Small - scale industries Credit Schemes.

4. The index has been tested on a sample of technically bankrupt firms and successful firms of similar ages and sizes (turnover) in Nigeria and the result has been very satisfactory. Example out of a sample of 30 successful manufacturing firms in Nigeria only 2 or (6.7%) has less than 40 points while 24 and above had 65 points. Thus 6.7% of the successful firms were found to be misclassified as bankrupt.

   On the other hand of the matching sample of bankrupt firms, 26 had less than 40 points (a success factor of 65%) and 3 had over 60 points (a misclassification of 10%. Other firms fell into the grey are of 40-60 points thus, necessitating in-depth scrutiny.

5. It is less complicated model for a considered by local financial institutions and decision-makers in determining risk in a company.

6. The author's research and empirical studies reveals that a subjective index of risk, rather than the complicated statistical models developed in Europe and America) is more useful to investors in selecting entrepreneurs for financial assistance based on tests that is aimed at assessing the individual's ability to rationalise operations entailing risks.

7. The model is easily comprehensive by Nigerian non-well educated entrepreneurs/businessmen; bankers and loan officers and the financial market and investors at large.

8. The index is also easily applicable and time saving for the analyst in Nigeria who has little or no access to sophisticated computer facilities for univariate and multivariate analysis.

4.3 SIGNIFICANCE OF THE INDEX

The ability to predict performance is very important to any business. Logically predicting business performance is useful and important to "Management", investors, "Creditors" and individuals in order to make rational decisions. More specially the index indicates whether a firm is successful, failing and entirely failed. The index highlights all pieces of information to interested parties as stated above.

4.4 LIMITATION AND CRITICIM OF THE OSAZE INDEX OF RISK

Some limitations and criticism observed about the index are as follows:

1. The models cannot be termed very satisfactory as claimed at 65% Example Blair's model was accurate at 80% while Altman's was 95%. He also did not measure the

percentage (%) of failed firms he studied 3, 4 and 5 years prior to actual failing to provide better predictive ability of it as other researchers.

2. Most large companies in Europe and America are multi-national companies with branches all other the world. Some branches operate with the same environments as companies from Africa.

3. Sophisticated computing facilities are now (1995) widely available in Africa; for example, check Nigerian Banks. It was not a strong argument even in 1980s when Bob Osaze developed his model as any such models could easily be computerised by large business in Africa including Nigeria.

4. Nigeria was a developing country when the model was developed in the early 80s but was classified before the turn of the same decade by the world bank in 1987 as under-developed. As such the model cannot confidently be used even in Nigeria today (1995) talk less of any African country. Besides, the model cannot be used in isolation.

5. Any Company efficiently managed will succeed regardless of whether or not it is located in developed, developing or under developed countries. This is why it is better to use indices that are likely to indicate actual success or failure whenever they are measured to encourage managerial and economic performances of firms and nations. Example include, Altman's and Blur's indices developed in the U.K and U.S.A have proved successful all over Europe, Japan, Germany, Canada and France and not so rich European countries like Norway and Greece. African cannot be an isolated case. Studied in depth "successful" firms in Nigeria may be actually "Mismanaged" in practice. Therefore, managers in Africa have to be encouraged to acquire managerial competence especially from managers of successful firms in developed countries.

6. As earlier studies like those of Tamari (1977) have pointed out, ratio analysis is usually most problematic with respect to non-quoted firms, (90% of which make up the Nigerian firms) since their financial statements are often incomplete and unreliable. Therefore, the knowledge that the index is subjective prevents its being regarded as a fail-safe analytical and decision making too.[10]

7. The index still required the user to make subjective judgements, especially with regard to the grey areas lying between the upper and lower limits of this index.[11]

4.5 A BRIEF HISTORY OF THE BANK UNDER STUDY

The United Bank for Africa (UBA) Plc, is one of Nigeria's top three commercial Banks. It was established in 1961 by a consortium of 5 (five) International Banks to take over the banking business carried on in Nigeria since 1049 by the British and French Bank Limited. With assets of over #24 billion and 199 branches spread all over Nigeria, the Bank has recorded an impressive growth rate.

UBA is active in all aspects of commercial banking and provides International Banking, trusteeship, share registration, corporate finance and computer services through specialised divisions and subsidiaries.

An aggressive business promotions strategy coupled with a willingness to innovate has earned the bank an enviable position in the banking industry. UBA plc is strongly committed to its social responsibilities and identifies with communities in which it is represented. Nigerian interest constitute 60 percent of the shareholding of the bank. Four of the founding International Banks, namely Banque Nationale del Lavoro and Montel dei Paschi di siena, who altogether, own 40 percent of the shareholding, are still represented on the Board of Directors and continue to make their expertise and resources throughout the world available to assist the Bank and its customers. UBA Plc has branches in New York and Grand Cayman island and a representative office in London. It also maintains correspondent relationship with many banks in Africa and in major countries in the world.

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CHAPTER FIVE

DATA ANALYSIS AND INTERPRETATION

Introduction

This chapter provides a frame work of financial ratio analysis, the analysis and application of Osaze's index of risk associated with united Bank for Africa (UBA) plc. It highlighted the strength and the weakness facing the company based on the data collected from the primary source.

The figures were obtained from the five years (1993-1997) annual financial statements of accounts of the Company (see appendix).

5.1 DATA ANALYSIS AND INTERPRETATION

Below is an analysis of the financial statements of the case study company using the following financial ratios:-

The liquidity ratios [2]. These are ratios which measure the firms ability to meet its maturing short-term obligations:-

1. ***The Current Ratio***:- Is the first test of the solvency of a company It indicates the ability of a company to meets it current maturing obligations.The generally accepted standard in available literature is ***2:1***. It appears that UBA Plc current ratio is above the recommended standard. This shows that the bank has much liquidity needed for discharging their current obligations. The current ratios are: 1.97, 2.00, 3.9, 3.10, and 3.12 in 1993, 1994, 1995, 1996 and 1997 respectively. Therefore, going by the trend of the ratio the result is quite encouraging and satisfactory.

2. ***Debt To total Asset Ratio:-*** This ratio measure the contribution of creditors to the total assets of the organisation.The lower the ratio the better for creditors loses in the event of liquidation and the higher the better for the organisation. U.B.A debt-to-total asset ratio are: 0.97, 0.94, 0.92, 0.9 and 0.90 in 1993, 1994, 1995, 1996 and 1997 respectively this means that the Bank have relied mostly on outside creditors throughout the five years to finance its total asset requirement and not raising funds from owners equity.

In short, by this analysis the creditors are used in magnifying the owner wealth. This, if these trend were to continue U.B.A would find it difficult to borrow additional fund without be reluctant to lend the firm more money and the management would probable be subjecting the firm to risk of bankruptcy if it sought to increase the ratio any further by borrowing funds.

3. ***Debt- to - Equity/Net Worth***:- This ratio measure the relationship between creditors contribution and those provided by the owners.Creditors would generally prefer this ratio to be low. U.B.A's debt -to-equity ratio are: 30.08, 14.39, 11.24, 10.02 and 3.06 in 1993, 1994, 1995, 1996 and 1997 respectively. As could be seen, the decrease trends of the ratios is very good for both the creditors and the U.B.A. This means that there reduction of debt financing year by year. Thus, this shows a sign of good.

4. ***Receivable Turnover:-*** The debtors turnover ratio measures the liquidity of the organisations receivable account or how quick it takes the organisation to collect its receivable. Generally the higher the value of the debtors turnover, the more efficient is the management of credit. In the case of U.B.A the value of trade debtors is satisfactory and favourable because the trend has been on the increase over the years. The ratios are: 1.40, 1.97, 3.42, 4.98 and 5.59 respectively. These suggest that U.B.A. has a small receivable balance as a result of strict credit policy or an aggressive collection policy.

5. ***Average Collection Period***:- This represents the average length of time that the organisation/firm trust wait after a wing a loan before receiving cash.The lower the better for the organisation.Thus, U.B.A in 1993 allowed approximately 75 days; in 1994 it became more lenient and allowed for approximately 95 days, in 1995 it became a bit strict by allowing only 72 days also in 1997 it maintained it strictness by allowing only 55 days. As could be seen the days flunctuate but in recent past (i.e. 1997), the Bank became very strict in granting credit and to some extent in its collection policy. If this trend continue, it will certainly help the situation.

6. ***Total Assets Turnover*** :- This measure the degree of efficiency with which the organisation is using it total assets in the generation of sales. The higher the asset turnover the better for the organisation because it is an indication that the organisation is using its total assets effectively and efficiently.

   Thus, UBA's assets turnover in 1993 was very low but later increased and fell again. The ratios are: 0.13, 0.15, 0.11, 0.15 and 0.14 in 1993, 1994, 1995, 1996 and 1997 respectively. As could be seen, as from 1993, 1995 and 1997. It thus indicated that U.B.A assets were not used to the maximum.

7. ***Gross Profit Margin*** :- This indicates the percentage of each Naira sales remaining after the firm has paid for its goods. It is a measure of the efficiency of the firms operators, as well as an indication on how loan and advances are operated The higher the gross profit margin the better and the lower the relative losses. U.B.A's gross profit margin have fluctuated from year to year. The ratios are; 0.13, 0.04, 0.08,

0.14 and 0.12 in 1993, 1994, 1995, 1996 and 1997, respectively. This result is not satisfactory because all expenses including taxes are yet to be deducted.

8. ***Net Profit Margin:***- This ratio measure the percentage of each Naira acquired remaining after all expenses, including taxes have been deducted. U.B.A's net profit margin are: 0.09, 0.04, 0.08,0.14 and 0.12 in 1993 , 1994, 1995, 1996 and 1997 respectively. The ratios shows that U.B.A managed its operations more efficiently in 1993, 1996 and 1997 respectively.

9. ***Return On Assets:***- This ratio measures the return on investment (ROI). The higher the ROI the better because if measures the effectiveness of judgement in generating profit with its available assets. U.B.A's returns on assets are: 0.01, 0.0005, 0.0003, 0.02 and 0.02 in 1993, 1994, 1995, 1996 and 1997 respectively. The low ratio in 1993, 1994 and 1995 was a result of low profit margin on the operations and the low turnover of total assets which shows that the U.B.A's operating assets were not properly utilised.

10. ***Return On Equity:***- This measure how efficiently a company's management has work for its shareholders i.e. maximisation of shareholder's wealth. A high return on equity often reflects the firm's acceptance of strong investment opportunities and effective expense management. U.B.A's return on equity are: 0.36, 0.08, 0.10, 0.23 and 0.17 in 1993, 1994, 1995, 1996, and 1997 respectively. As could be seen, the trend was on the increase only in 1993, but dropped drastically to 0.08, 0.10 in 1994 and 995 and improved to 0.23 and 0.17 in 1996 and 1997.This also calls for improvement in efficiency or management functions so as to fully maximised the wealth of the shareholders of the Bank.

FINANCIAL RATIO ANALYSIS FOR U.B.A PLC. FINANCIAL STATEMENT (1993-1997) LIQUIDITY RATIOS

	1993	1994	1995	1996	1997
Current Ratio	1.97	2.00	3.9	3.10	3.12
Debt Ratios					
Debt to total Asset	0.97	0.94	0.92	0.91	0.90
Debt to Equity	30.08	14.39	11.24	10.02	3.06

Activity Ratios

	1993	1994	1995	1996	1997
Receivable Turnover ratio	1.40	1.97	3.42	4.98	5.59
Average collection/period	75	95	90	72	55
Total Assets Turnover	0.13	0.15	0.11	0.15	0.14

Profitability Ratios

	1993	1994	1995	1996	1997
Gross profit margin	0.13	0.06	0.11	0.18	0.13
Net profit margin	0.09	0.04	0.08	0.14	0.12
Return on Assets ratio	0.01	0.0005	0.0003	0.02	0.12
Return on Equity ratio	0.36	0.08	0.10	0.23	0.17

5.2 ANALYSIS AND APPLICATION OF OSAZE'S INDEX OF RISK

This section cross-examines the Osaze's index of risk and also the application. (Predicting corporate failure and business risk associated with U.B.A. plc).

ANALYSIS

Below is the Osaze's index of risk- which is a financial composite index for predicting corporate failing in Nigeria (see explanation in chapter four) is used to help in assessing more broadly whether the U.B.A Plc is a successful, failing or failed from entirely. Hence the analysis.

1. ***Net Worth To Total Asset***: This ratio measure the contribution of shareholder equity to the total assets of the organisation. The higher the better for the organisation and the creditors. U.B.A. Net worth to total asset are 4%, 7%, 9%, 11% and 12% in 1993, 1994, 1995, 1996 and 1997 respectively. As could be seen, creditors funds only enjoyed a considerable margin of safety in 1997. Even though from the standpoint of the owners, they are controlling the organisation with little funds. It also indicates that throughout the years the bulk of the organisation the sense that if this trend continue U.B.A. credit worthiness will be at stake.

2. ***Retained Earning To Net Profit:-*** This measure what percentage (%) of net profit is retained within the organisation. Retaining to greater amount of current earnings in the firm means that fewer Naira will be available for current dividend payment. U.B.A. retained earnings to net profit are: 0.85, 0.63, 0.72, 0.80 and 0.93 in 1993, 1994, 1995, 1996 and 1997 between 85% and 93% which implies they use a large proportion of their profit as a source of internal finance which consequently will lower the possibilities of going out to borrow.

3. ***Profit trend over 5 years (Net profit-sales) :-*** This measure the relationship between net profit and sales over a period of time. U.B.A Gross earning has been on the increase over the years, while the net profit also have been increasing. The U.B.A. net profit ratio are: 9%,4% 8%, 14% and 12% in 1993, 1994, 1995, 1996 and 1997 respectively. The increasing trend of the profit year by year indicates U.B.A efficiently in operations.

4. ***Earning before interest and taxes to total asset (EBIT)***. This ratio indicates the power of the firm's assets to generate operating income. The higher the ratio the better in the sense that it represent the contribution of every N1 in the total earnings of the organisation. U.B.A's EBIT to total assets are: 13%,15%,11%,15% and 14% in 1993, 1994, 1995, 1996 and 1997 respectively. Because of the turn over ratio and low profit margin on sale in 1993, and 1995, it is clear indication that of its total assets as was the case in 1994, 1996 and 1997.

5. ***Current Ratio:*** Is the first test of the solvency of a firm. It indicates the ability of a company to meet it current maturing obligations. The generally acceptable standard in available literature is 2:1. Hence the U.B.A's current ratio are: 1.97, 2.00, 3.9, 3.10, 3.12 in 1993, 1994, 1995, 1996 and 1997 respectively. The result so far is satisfactory because this shows that the Bank has adequate liquidity to discharged its current obligations.

6. ***Working Capital to Total Asset:-*** Is a measure of net liquid assets of the firm relative to the total capitalisation. Working capital is defined as the difference between current assets and current liabilities. Liquidity and size characteristics are explicit considered. The higher the better for the organisation. U.B.A. working capital to total assets are 47%, 46%, 50%, 50% and 50% in 1993, 1994, 1995, 1996 and 1997 respectively. As could be seen the situation has been on the increasing rate. This shows that the Bank has adequate working capital.

7. ***Cash flow To total debt:-*** This measure the relationship between total cash flow and total debt. Where cash flow is equal to net profit after tax is depreciation. The higher the ratio the better for both the organisation and the creditor. U.B.A cash flow to total debt are: 9%,9%, 12% and 13% in 1993, 1994, 1995, 1996 and 1997 respectively. The result is a bit satisfactory because there's increasing trend by each year. However, the Bank should try to increase efficiency so as to be able to service its debts.

8. ***Sales - To - Account Receivable:-*** The debtors turnover ratio measure the liquidity of the organisations receivable account or how quick it takes the organisation to collect its receivable.Generally the higher the value or the debtors turnover, the more efficient is the management of credit. The U.B.A. ratios are: 1.4, 1.97, 3.42, 4.98, and 5.59 in 1993, 1994, 1995, 1996 and 1997 respectively.

   The value of the trade debtors is quite satisfactory, because the trend has been on the increase over the years. This means that U.B.A. has moderate receivable balance.

TOTAL POINTS SCORED BY U.B.A. PLC. (1993 - 1997)

YEAR	*TOTAL POINTS SCORED*
1993	56
1994	56
1995	58
1996	70
1997	72

According to this model (Osaze's index of risk) [6] to assess broadly whether a company is successful; failing or a failed firm entirely (predicting corporate failure and determining risk associated with a business); companies are classified into the three groups according to their scores (see details in chapter four).

1. Companies that scored over 60 points when their total scores are added are unlikely to fail.

2. Companies that scored less than 40 points when their total scores are added have a higher probability of failure; and

3. Companies that scored between 40 and 60 points when their total scores are added need to be scrutinised properly before a decision is taken to their potentials for bankruptcy or success. And this is where other subjective factors like management capacity and economic indicators would prove highly invaluable.

Going by the above analysis the U.B.A Plc has succeed in the above first group in 1996 and 1997 when the total scores are added 70 and 72 respectively; which means that the company was successful (unlikely to fail). While in 1993, 1994 and 1995 U.B.A. Plc has fallen into the above third group when the total scores are added 56, 56 and 58 points respectively; which means that the problems lies in the management of the organisation resources and the failure of the management to devise measure of keeping abreast with dynamics in the economy. Hence, the need to be scrutinised properly before a decision is taken to their potentials for bankruptcy or success.

However, on the average the U.B.A Plc is a successful firm. Because the organisation was able to improve from their likelihood situation in 1993, 1994 and 1995 to a successful situation in 1996 and 1997 respectively. Thus, it is a successful firm and there is likelihood in future that the organisation would improve.

5.3 THE APPLICATION: PREDICTING CORPORATE FAILURE AND BUSINESS RISK ASSOCIATED WITH UNITED BANK FOR AFRICA (UBA) PLC (1993 -1997)

		1993			1994			1995			1996			1997		
		Result	**%**	**Point**	**Result**	**%**	**Point**	**Result**	**%**	**Point**	**Result**	**%**	**Point**	**Result**	**%**	**Point**
1.	***Networth To Total Asset***	0.04	4%	0	0.07	%	0.	0.09	9%	0	0.11	11%	4	0.12	12	4
2.	***Ret. Earnings To Net profit***	0.85	85%	12	0.63	63	12	0.72	72	12	0.80	80	12	0.93	93	12
3.	***Profit trend over 5 years period***	0.09	9	10	0.4	4	10	0.08	8	10	0.14	14	10	0.12	12	10
4.	***EBIT to Total Asset***	0.13	13	6	0.15	15	6	0.11	11	6	0.15	15	6	0.14	14	6
5.	***Current Ratio***	1.97	Times	10	2.00	Times	10	3.9	Times	12	3.10	Times	12	3.12	**Times**	12
6.	Working Capital to Total Asset	0.47	47	12	0.46	46	12	0.05	50	12	0.50	50	12	0.50	50	12
7.	Cash flow to Total debt	0.09	9	0	0.09	9	0	0.11	11	4	0.12	12	4	0.13	13	4
8.	Sales to AAccount Recievables	1.40	Times	6	1.97	Times	6	3.42	Times	8	4.98	Times	10	5.59	**Times**	12
	TOTAL SCORES			**56**			**56**			**58**			**70**			**72**

FOOTNOTES

1. U.B.A. Plc 5 years financial statements of accounts (1993-1997)

2. *Van Horne C. James* (1992): Financial Management and policy (eight edition) Prentice-hall Inc. Englewood cliffs. N.J. U.S.A

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5. *Pandey I.M.*Financial Management, Vikas Publishing House, put Limited India.

6. *Brigham F. Eugene and Ramon E. Johnson* (1980) Issues in Managerial Finance the Dryen Press Hisdele, Illinois page 51.

7. *Brigham F. Eugene and Johnson* op. Cit page 50

8. *Dr. B.E. Osaze's* (1985) articles in Nigeria Management Review "Journal of Centre for Management Development page 24.

CHAPTER SIX

Introduction

In this chapter a general summary of the chapters and research findings are provided. Recommendation based on the findings are offered and an overall conclusion of the study is given.

6.1 GENERAL SUMMARY

The research project has tried to examined the efficiency of financial ratio analysis in predicting corporate bankruptcy through the employment of Osaze's index of risk with a view of allaying peoples fear of the financial healthiness or otherwise.

We have in the first chapter seen the introduced, statement of the problem, the objective and significance of the study; scope and limitation of the study.

The second chapter has exhaustively discussed the concept of financial ratios, standard of comparison, various type of ratios such as liquidity, leverage, activity, profitability and coverage and also reviewed the work of some researchers of financial ratios and predictive power on various aspect of firms from corporate failure and risk to bond rating, rapid growth firms and profitability firms to the usefulness of financial to common stock investors and recent developments in financial ratio analysis; the use of univariate and multivariate analysis in predicting corporate failure and bankruptcy. Lastly the work of Professor Bob Osaze i.e. Osaze's index of risk applicable to developing countries was discussed.

In chapter three distress about banking industry was discussed. The nature, causes, symptoms and remedies about banking industry are all highlighted. Moreso, the world bank's standard for predicting banks bankruptcy was stated all in the chapter.

In chapter four the procedures for collection of data were highlighted. The rationale/significance of the index of risk were discussed. Also criticism and or indication of the index were made and a brief history of the bank under study was made.

Chapter Five focuses on the analysis and interpretation of the various data collected. Here, the financial statements of the U.B.A were critically analysed. Financial ratio analysis; Osaze's index of risk and computed tables were used to highlights and verified the problem, so as to plainly convey the vital information, which was interpreted by way of comments.

Finally, in chapter five, the general summary of the chapter and the research findings are offered and an overall conclusion of the study is given. Recommendation were also offered.

6.2 CONCLUSION

Financial ratio analysis could be used to evaluate a firm's financial condition and performance. It serves as check-ups on various aspects of a firms' financial health.

Therefor, U.B.A. Plc as revealed by the study is a successful organisation which means there is efficient management work.

SUMAMRY OF FINDINGS AND PROBLEMS FACING THE U.B.A. PLC.

This section summarises the findings of the study and some problems facing U.B.A. Plc as discussed in the data analysis (Chapter five); viz.:

1. The business of the UBA assets lies in the current assets with almost 70% of the total assets.

2. There is too much gearing in the organisation i.e. to say the level of debt financing is too high.

3. The Bank does not separate the current liabilities and that of long term liabilities in their statement of accounts, therefore this brings problems in computing current ratio for the organisation. To make the application possible the hypothetical figures for current liabilities is used (see appendix).

4. The profitability ratios indicated that the company is not earning sufficient profit compared to its assets.

5. The bank operate a retention policy other than the dividend policy. Because retained earnings carries about 70%.Thus,the financing is almost that of internal.

6. The return on the total assets is very scanty, this shows that the banks has hold an assets above the level it support to hold

7. The osaze's index of risk indicated that the management of the bank has improved efficiency in 1996 and 1996 because in these years the index has indicated success, thus, if the management continue in this way there is every likelihood success would always prevail.

6.3 RECOMMENDATIONS

In the light of the findings of the study, the data analysed (in chapter five)and the problems highlighted facing U.B.A. Plc, the following options, which are the personal recommendations of the writer are deemed useful for the purpose of overcoming or minimising the problems facing the bank:

LIQUIDITY

There is a strong need for U.B.A Plc, to revise their current assets i.e. to know the optional level of current assets it ought to hold as there is too much current assets lying idle.

Thus, the bank should try to know the desired level of their current assets, so as to eliminate the cost associated with holding idle assets.

STATEMENT OF ACCOUNTS

U.B.A Plc should know that statements of accounts is not only useful to government as required for tax purpose; to potential creditors who want to know the level of gearing so as to know whether it is appropriate to give additional financing; or to potential investors who are interested in knowing the profitability and the viability of the bank but it is indeed to academicians and students for an educative research and analysis. From the foregoing therefore, UBA should please in their next statements of accountsseparate current liabilities from long term liabilities so as to allow computation of ratios like current ratio which is current asset/current liabilities.

6.4 IMPLICATION FOR FURTHER RESEARCH

This study would be incomplete if mention is not made of certain areas where further research in greater details is desirable. The areas, to the researcher's opinion include:

1. Determination of financial ratio analysis for African countries

2. Determination of other predicting power of corporate bankruptcy model, classified to be appropriate for under-developed, developing and developed countries.

3. Determination of an appropriate model of predicting corporate bankruptcy that take care of grey zone i.e. zone of ignorance. A model that will tell us success or failure instantly without any further scrutiny.

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APPENDIX

HYPOTHETICAL NOTES ON THE U.B.A. PLC ACCOUNT

CURRENT LIABILITIES

Year	1993	1994	19951	I996	1997
AMOUNT	#11,118.010	#11,352,293	#20,294.537	#21,817,305	#24,744,422



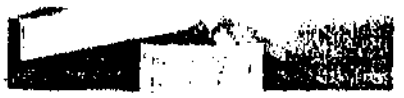
GROUP BALANCE SHEET

As at 31 March, 1997 and 1996

	Notes	GROUP 1997 N'000	GROUP 1996 N'000	COMPANY 1997 N'000	COMPANY 1996 N'000
USE OF FUNDS					
Cash and Short Term Funds	1	[illegible]	18,444,369	19,102,195	18,300,482
Cash Reserve Deposits		[illegible]	1,161,107	1,881,016	1,161,107
Stabilisation Securities		[illegible]	4,196,142	[illegible]	4,196,142
Bills Discounted	2	[illegible]	5,990,820	9,434,635	5,990,820
Investments	3	[illegible]	3,124,844	3,563,701	3,057,994
Loans and Advances	4	[illegible]	8,986,917	18,766,815	8,986,917
Other Assets	5	[illegible]	4,278,614	4,891,546	4,240,550
Fixed Assets	6	[illegible]	2,025,602	2,311,793	2,011,193
		[illegible]	48,208,415	[illegible]	47,945,205
LIABILITIES					
Current, Deposit and Other Accounts	7	[illegible]	37,019,232	[illegible]	37,019,232
Accounts Payable, including items in transit, taxation and dividends	8	[illegible]	6,815,379	[illegible]	6,638,580
		[illegible]	43,834,611	[illegible]	43,657,812
CAPITAL AND RESERVES					
Share Capital	9	[illegible]	300,000	[illegible]	300,000
Reserve for Bonus Issue		[illegible]	-	[illegible]	-
Other Reserves	10	[illegible]	4,073,804	[illegible]	3,987,393
SHAREHOLDERS' FUNDS		[illegible]	4,373,804	[illegible]	4,287,393
		[illegible]	48,208,415	[illegible]	47,945,205
Acceptances, guarantees and other obligations for account of customers (and customers' liability thereon)	11	[illegible]	12,053,854	[illegible]	12,053,854

HAKEEM BELO-OSAGIE)
)
ABBA KYARI) Directors
)
GASTON HOYAMI)

The accompanying notes form part of these Balance Sheets



GROUP PROFIT AND LOSS ACCOUNTS

For the Year Ended 31 March, 1997 and 1996

	Notes	GROUP 1996 N'000	COMPANY 1995 N'000
Gross Earnings		7,430,411	6,972,978
Interest and Discount Income	12	4,416,985	4,416,985
Interest Expense	13	(1,886,411)	(1,580,809)
		2,530,574	2,836,076
Net Loan Loss Recovery	16.1	42,653	42,653
Net Interest Margin		2,573,227	2,878,729
Other Banking Income	14	3,013,426	2,556,003
		5,586,653	5,434,732
Depreciation on Fixed Assets	6	(171,763)	(167,400)
Other Operating Expenses	15	(4,066,221)	(4,021,147)
Profit Before Taxation		1,348,669	1,246,185
Taxation	17.1	(334,111)	(302,338)
Profit After Taxation		1,014,558	943,847
Appropriations:			
Statutory Reserve		(304,367)	(283,154)
General Reserve		(509,991)	(460,493)
Dividend - Proposed		(200,000)	(200,000)
		200	200
Retained Profit: Beginning of Year		2,800	2,800
Retained Profit: End of Year		3,000	3,000
Earnings per 50k share	19	N1.69	N1.57
Dividends per 50k share	19	N0.33	N0.33

The accompanying notes form part of these Profit and Loss Accounts



GROUP CASH FLOW STATEMENT

For The Year Ended 31 March, 1997

			1996 N'000	1996 N'000
Operating Profit				1,348,669
Adjustment for items not involving cash flow				
Depreciation			171,763	
(Profit)/Loss on sale of fixed assets			11,341	
Increase in deposits and other accounts			3,857,645	
Increase/(Decrease) in other liabilities			(1,018,352)	
Increase/(Decrease) in exchange reserves			(52,063)	
(Increase) in loans and advances			(2,766,805)	
(Increase)/Decrease in other assets			332,732	
				536,261
Net cash inflow from operating activities				1,884,930
Returns on investments and servicing of finance				
Dividend paid				(84,207)
Taxation				
Company Tax paid				(43,660)
Investing activities				
Cash reserve deposit			(279,023)	
Purchase of treasury bills			(2,354,981)	
Exchange difference on fixed assets			(226)	
Purchase of fixed assets			(475,790)	
Purchase of Investment			(54,095)	
Stabilisation Securities			-	
Proceeds from sale of fixed assets			25,942	
Net cash outflow from investing activities				(3,138,173)
Net increase in cash & cash equivalent				(1,381,110)
Net increase in cash equivalent at 1 April, 1996				19,825,479
Cash and cash equivalent at 31 March, 1997				18,444,369

		GROUP		COMPANY	
		1997	1996	1997	1996
		N'000	N'000	N'000	N'000
1. Cash and Short-Term Funds					
Cash and short-term funds comprise:					
Cash		862,551	413,203	599,545	413,203
Balances with, and cheques in course of collection on other banks:					
In Nigeria		4,110,150	3,710,856	4,110,150	3,566,969
Abroad	(note 20)	696,199	2,021,732	696,199	2,021,732
Money at call with Banks:					
In Nigeria		918,500	338,500	918,500	338,500
Abroad	(note 20)	12,796,301	10,526,578	12,796,301	10,526,578
Negotiable certificate of Deposit:					
Abroad	(note 20)	—	1,452,000	—	1,452,000
		19,383,701	18,462,869	19,120,695	18,318,982
Provision for Interbank Placements (note 16.1)		(18,500)	(18,500)	(18,500)	(18,500)
		19,365,201	18,444,369	19,102,195	18,300,482
2. Bills Discounted					
Nigerian Government Treasury Bills		9,434,635	5,990,820	9,434,635	5,990,820
3. Investments					
.1 Investment in wholly owned subsidiary					
UBA Trustees Limited		—	—	3,150	3,150
Fed. Government Debt Certificates (Par Bonds) (note 3.2)		4,731,660	5,417,493	4,731,660	5,417,493
Investment in listed companies in Nigeria (note 3.3)		438,282	64,028	438,282	64,028
Market value (N468,157,000; 1996 - N108,549,632)					
Other investments not listed (3.4)		224,846	122,625	60,471	52,625
Less Provision For diminution in value of Par Bond (note 3.2)		(1,569,859)	(2,479,302)	(1,569,859)	(2,479,302)
		3,824,929	3,124,844	3,663,704	3,057,994

.2 During the year the Bank disposed of $10m (Nominal Value) of Par Bonds

The outstanding balance of par bonds ($55.5 Nominal Value) at 31 March 1997 was disposed of after the Balance Sheet date.



13 Quoted Investments	Status	1997 N'000	1996 N'000
P.Z. Industries Plc (M/Value N6,075,000 (1996 N5,625,000)	Floating Debenture	7,500	7,500
C.F.A.O. Nig. Plc. (M/Value N500,000 (1996 N679,922)	Floating Debenture	500	833
Christlieb Plc. (M/Value N1,600,000 (1996 N2,000,000)	Floating Debenture	1,600	2,000
Guinness Nig. Plc. (M/Value N5,001,000 (1996 N3,550,710)	Floating Debenture	5,001	5,001
U.T.C. Nig. Plc. (M/Value N1,600,000 (1996 N2,000,000)	Floating Debenture	1,600	2,000
Smithkline Beecham Plc. (M/Value N4,500,002 (1996 N10,000,000)	Floating Debenture	5,000	10,000
WAPCO PLC (M/Value N36,000,000 (1996 N54,000,000)	Floating Debenture	4,000	6,000
TEXACO Nig Plc. (M/Value N1,800,000 (N2,000,000)	Floating Debenture	2,000	2,000
Nigeria German Chemicals Plc. (M/Value N9,079,000 (1996 N9,079,000)	Floating Debenture	9,079	9,079
C.F.A.O. Nig. Plc. (M/Value N19,615,000 (1996 N19,615,000)	Floating Debenture	19,615	19,615
Nigeria Merchant Bank Plc.	Floating Debenture	-	5,455
Nigeria International Debt Fund	Govt. Debt Certificate	382,387	-
		438,282	69,483
Prudential Provision thereon		-	(5,455)
		438,282	64,028

14 Other Investments			
Rivers State Veg. Oil Ltd.	Equity	4,500	2,700
Nigeria Agric. Insurance Co. Ltd.	Equity	500	500
Nigeria Merchant Bank Plc.	Equity	1,860	1,860
Vehicle Insurance Sinking Fund	Sinking Fund	44,471	38,425
African Export-Import Bank	Equity	10,500	10,500
Central Securities Clearing System	Equity	500	500
Kano Development Bond	Floating Debenture	2,000	2,000
		64,331	56,485
Prudential Provision thereon		(3,860)	(3,860)
		60,471	52,625
Investments of subsidiary company - UBA Trustees Ltd.		164,375	70,000
		224,846	122,625



4. Loans and Advances	GROUP 1997 N'000	GROUP 1996 N'000	COMPANY 1997 N'000	COMPANY 1996 N'000
.1 **Loans and Advances Comprise:**				
Secured against real estate	3,672,725	3,839,567	3,672,725	3,839,567
Otherwise secured	8,885,173	8,247,271	8,885,173	8,247,271
Unsecured	4,726,404	2,746,430	4,726,404	2,746,430
	17,284,302	14,833,268	17,284,302	14,833,268
Less:				
Provision under Prud. Guidelines (Note 16.3)	6,523,487	5,846,351	6,523,487	5,846,351
	10,760,815	8,986,917	10,760,815	8,986,917
.2 **The maturity profile of loans and advances is as follows:**				
Overdrafts	6,156,178	4,554,741	6,156,178	4,554,741
1-3 months	7,144,084	6,363,748	7,144,084	6,363,748
3-6 months	496,114	693,003	496,114	693,003
6-12 months	713,869	658,311	713,869	658,311
Over 12 months	2,774,057	2,563,465	2,774,057	2,563,465
	17,284,302	14,833,268	17,284,302	14,833,268
.3 **The Loans and advances are classified as follows:**				
Performing	10,749,034	8,818,892	10,749,034	8,818,892
Non-performing				
- Principal	2,382,306	2,684,209	2,382,306	2,684,209
- Unpaid Interest	4,152,962	3,330,167	4,152,962	3,330,167
	17,284,302	14,833,268	17,284,302	14,833,268
5. Other Assets				
Payments in advance and sundry accounts	3,787,914	2,814,199	3,771,616	2,776,135
Accounts receivable	1,186,957	1,492,827	1,158,472	1,492,827
	4,974,871	4,307,026	4,930,088	4,268,962
Less: Provision for doubtful accounts under Prudential Guidelines	35,542	28,412	35,542	28,412
	4,939,329	4,278,614	4,894,546	4,240,550



6. **Fixed Assets**

	Land and Buildings N'000	Machinery Furniture and Fittings N'000	Motor Vehicles N'000	Construction in progress N'000	Total N'000
.1 **GROUP**					
Cost					
At 1 April, 1996	1,616,977	1,060,852	125,238	26,836	2,829,903
Additions	81,661	372,108	112,207	4,289	570,265
Transfers	26,836	-	-	(26,836)	-
Disposals	-	(2,776)	(2,397)	-	(5,173)
Exchange difference	1,147	2,195	-	-	3,342
At 31st March, 1997	1,726,621	1,432,379	235,048	4,289	3,398,337
Depreciation					
At 1 April, 1996	142,535	580,154	81,612	-	804,301
Charge for the year	40,942	162,106	32,217	-	235,265
On disposals	-	(1,566)	(1,365)	-	(2,931)
Exchange difference	374	1,492	-	-	1,866
At 31 March, 1997	183,851	742,186	112,464	-	1,038,501
Net Book Value					
At 31 March, 1997	1,542,770	690,193	122,584	4,289	2,359,836
At 31 March, 1996	1,474,442	480,698	43,626	26,836	2,025,602
.2 **COMPANY**					
Cost					
At 1 April, 1996	1,616,977	1,046,625	118,444	26,836	2,808,882
Additions	81,661	365,315	108,824	4,289	560,089
Transfers	26,836	-	-	(26,836)	-
Disposals	-	(2,747)	(2,224)	-	(4,971)
Exchange difference	1,147	2,195	-	-	3,342
	1,726,621	1,411,388	225,044	4,289	3,367,342
Depreciation					
At 1 April, 1996	142,535	575,775	79,379	-	797,689
Charge for the year	40,942	158,034	29,747	-	228,723
On disposals	-	(1,537)	(1,192)	-	(2,729)
Exchange difference	374	1,492	-	-	1,866
At 31 March, 1997	183,851	733,764	107,934	-	1,025,549
Net Book Value					
At 31 March, 1997	1,542,770	677,624	117,110	4,289	2,341,793
At 31 March, 1996	1,474,442	470,850	39,065	26,836	2,011,193

.3 **Land and Buildings Comprise:**

	1997 N'000	1996 N'000
Long-term leasehold land and buildings	1,625,460	1,515,816
Short-term leasehold land and building	101,161	101,161
	1,726,621	1,616,977

.4 **Exchange Difference**
Exchange difference arose from the conversion of fixed assets in overseas branches at the rate of exchange ruling at 31 March, 1997.

.5 **Capital Commitments**
Capital expenditure authorised by the Directors but not provided for in these Financial Statements amounted to N39.35 million (1996 N150 million)

7. **Current, Deposit and other Customers' Accounts**

			GROUP		COMPANY	
			1997 N'000	1996 N'000	1997 N'000	1996 N'000
.1	**Deposits**					
	(i) Demand					
	In Nigeria		12,918,145	10,851,546	12,918,145	10,851,546
	Abroad	(note 20)	1,635,570	6,799,185	1,635,570	6,799,185
			14,553,715	17,650,731	14,553,715	17,650,731
	(ii) Savings		9,842,482	8,749,799	9,842,482	8,749,799
	(iii) Time Deposits					
	In Nigeria		5,172,100	3,127,884	5,172,100	3,127,884
	Abroad	(note 20)	3,781,140	4,081,987	3,781,140	4,081,987
			8,953,240	7,209,871	8,953,240	7,209,871
	(iv) Due to other Banks and non-Banks					
	In Nigeria		5,633,605	2,880,954	5,633,605	2,880,954
.2	**Foreign transfers payable**		537,930	527,877	537,930	527,877
			39,520,972	37,019,232	39,520,972	37,019,232
.3	**Above includes deposits held by persons not ordinarily resident in Nigeria**		-	114,645	-	114,645
.4	**The maturity profile of Deposit liabilities is as follows:**					
	Under 1 month		31,935,227	29,833,300	31,935,227	29,833,300
	1 - 3 months		7,265,227	6,647,144	7,265,227	6,647,144
	3 - 6 months		237,380	317,525	237,380	317,525
	6-12 months		76,536	158,333	76,536	158,333
	Over 12 months		6,602	62,930	6,602	62,930
			39,520,972	37,019,232	39,520,972	37,019,232

.5 Due to other Banks includes uncleared effects and cheques for collection in favour of other Banks in Nigeria.



	GROUP		COMPANY	
	1997	1996	1997	1996
	N'000	N'000	N'000	N'000
14. Other Income				
Income from foreign exchange transactions	836,456	944,924	836,456	944,924
Commission on letters of credit and bills collected	172,058	298,970	172,058	298,970
Commission on turnover	826,235	783,016	826,235	783,016
Commission on transfers and guarantees	627,415	424,021	627,415	424,021
Financial services commissions	119,223	105,072	119,223	105,072
Income from managed funds	550,905	457,423	-	-
Interest on foreign branch tax refunds and other income	350,922	-	350,922	-
	3,483,214	3,013,426	2,932,309	2,556,003
15. Other Operating Expenses				
Other Operating Expenses include:				
Auditors' Remuneration	8,100	6,400	7,500	6,000
Directors' Remuneration (note 23)	5,225	3,486	5,225	3,486
NDIC Premium	183,831	147,104	183,831	147,104

16. Movement on Prudential Provision Accounts

	%	Principal 1997 N'000	Provision 1997 N'000	Principal 1996 N'000	Provision 1996 N'000	Profit and Loss Account N'000
.1 Per Profit and Loss Account:						
Performing	1%	10,749,034	107,490	8,818,892	88,189	19,301
Sub-Standard	10%	98,271	9,827	91,614	9,161	666
Doubtful	50%	61,662	30,831	347,525	173,763	(142,932)
Lost	100%	2,222,377	2,222,377	2,245,070	2,245,070	(22,693)
		13,131,344	2,370,525	11,503,101	2,516,183	(145,658)
S M E Loans			68,619		-	68,619
Investments			3,860		9,315	(5,455)
Interbank Placements			18,500		18,500	-
Other Assets (note 5)			35,542		28,412	7,130
						(75,364)

.2 Movement on provision for Bad and Doubtful Debts has taken into account total recoveries for the year standing at N921,044,227.



		1996	1996
			N'000
.3 Per Balance Sheet (note 4)			2,576,523
Balance brought forward			(60,340)
Provision for current year			2,516,183
			3,330,168
Interest in Suspense			5,846 351

	GROUP		COMPANY	
		1996		1996
		N'000		N'000
17. Taxation				
.1 Per profit and loss account				
Taxation based on the profit of the year:				
- Income Tax		403,355		373,855
- Education Levy		33,655		31,155
(Over)/under provision in previous year		(102,899)		(102,672)
		334,111		302,338
.2 Per balance sheet (note 8)				
Based on the profit of the year as above		334,111		302,338
Balance brought forward		224,627		223,680
Payments during the year		(43,660)		(43,054)
		515,078		482,964

The charge for income tax in these accounts is based on the provisions of the Companies Income Tax Act 1979 amended to date. The charge for Education Tax is based on the provisions of the Education Tax Decree, 1993.

18. Dividends		1996		1996
		N'000		N'000
Proposed (gross) on issued ordinary share capital 20% of N300,000,000 (1996 - 67% of 300,000,000)		200,000		200,000

The proposed dividend is subject to deduction of withholding tax at the appropriate rate.

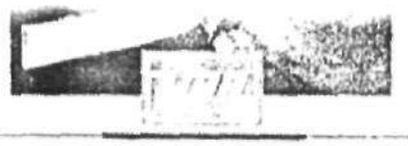


19. **Earnings and Dividends per Share**
Earnings and dividend per share are based on issued and fully paid Capital at 31 March, 1997.

20. **Net External Assets**	GROUP 1997 N'000	GROUP 1996 N'000	COMPANY 1997 N'000	COMPANY 1996 N'000
.1 Asset (note 1)				
Cash and Bank balances held	696,199	2,021,732	696,199	2,021,732
Money at call	12,796,301	10,526,578	12,796,301	10,526,578
Negotiable Certificate of Deposit		1,452,000		1,452,000
	13,492,500	14,000,310	13,492,500	14,000,310
.2 Liabilities (note 7)				
Demand deposits	1,635,570	6,799,185	1,635,570	6,799,185
Time deposits	3,781,140	4,081,987	3,781,140	4,081,987
	5,416,710	10,881,172	5,416,710	10,881,172
Net External Assets	8,075,790	3,119,138	8,075,790	3,119,138

21. **Contingent Liabilities**
At 31 March, 1997 contingent liabilities in respect of litigations against the bank amounted to N26,523,530 (1996 - N20,771,800). The actions are being contested and the Directors are of the opinion that no significant liability will arise therefrom.

22. **Contravention**
During the year ended March 31, 1996, the Bank contravened the provision of the Central Bank of Nigeria Monetary Policy Circular No. 29 of 1995 which stipulates a maximum lending rate of 21% per annum. The penalty of N95,000 was levied and paid during the year ended 31 March, 1997.
The cap on interest rates which was imposed since 1994 was removed with effect from 1st October, 1996 (reference Monetary Policy Circular No. 31 of 1997).



APPENDIX

23. Information Regarding Directors and Employees

	1997	1996
	N'000	N'000
(a) Directors' emoluments		
(i) Chairman	480	136
Other Directors	4,845	3,350
	5,325	3,486
(ii) Other Directors' emoluments include		
Fees	1,725	673
Others	3,000	2,677
	4,725	3,350

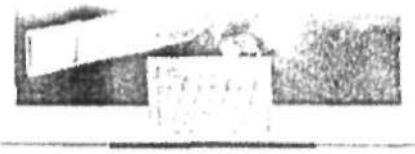
(iii) The number of Directors excluding the Chairman whose emoluments were within the following ranges are:

			1997	1996
			number	Number
Up to	-	N50,000	5	6
N190,001	-	N200,000	5	5
N200,001	-	N210,000	1	-
Over N300,000			7	7

(b) (i) The average number of persons employed by the Bank during the year was as follows:

General Management	216	267
Officers	2,884	2,345
Junior Staff	4,617	5,101
	7,717	7,713

	1997	1996
Staff Cost	N'000	N'000
Staff cost is as follows:		
Wages and Salaries	1,653,443	1,192,475
Staff welfare	939,719	997,066
	2,593,162	2,189,541



GROUP STATEMENT OF VALUE ADDED

Year Ended 31st March

	[illegible]	1996 N'000	%
Gross earnings	[illegible]	7,430,411	
Interest paid	[illegible]	(1,886,411)	
	[illegible]	5,544,000	
Bought in material & services	[illegible]	(1,876,680)	
Net loan loss recovery	[illegible]	42,653	
	[illegible]	3,709,973	100
Applied in the following way:			
To pay employees:			
Salaries, wages and fringe benefits	[illegible]	2,189,541	59
To pay providers of capital:			
Dividend to shareholders	[illegible]	200,000	5
To pay government:			
Direct Taxation	[illegible]	334,111	9
To provide for maintenance of assets & expansion of business:			
Depreciation	[illegible]	171,763	5
Profits retained in the business	[illegible]	814,558	22
	[illegible]	3,709,973	100

Value added represents the additional wealth the group has been able to create by its own and its employees' efforts.



FIVE-YEAR FINANCIAL SUMMARY

For the Year Ended 31 March

GROUP BALANCE SHEET	1996 N'000	1995 N'000	1994 N'000	1993 N'000
Use of Funds				
Cash and short term funds	18,444,369	19,825,479	6,462,560	4,867,029
Cash Reserve deposits	1,161,107	882,084	613,136	437,351
Stabilisation Securities	4,196,142	4,196,142	3,042,103	3,826,088
Bills Discounted	5,990,820	3,635,839	1,946,945	999,413
Investments	3,124,844	3,070,749	890,051	78,105
Loans and Advances	8,986,917	6,220,112	4,317,846	5,428,590
Other assets	4,278,614	4,611,346	5,461,290	6,220,903
Fixed Assets	2,025,602	1,758,633	1,548,048	1,117,690
	48,208,415	44,200,384	24,281,979	22,975,170
LIABILITIES				
Deposit and other Customers' Accounts	37,019,232	33,161,587	18,353,987	18,627,500
Accounts payable, including *items in transit, taxation* and dividend	6,815,379	7,427,488	4,350,600	3,608,521
	43,834,611	40,589,075	22,704,587	22,236,021
CAPITAL AND RESERVES				
Share Capital	300,000	300,000	100,000	100,000
Reserves for Bonus Issue	—	—	—	—
Other Reserves	4,073,804	3,311,309	1,477,392	639,149
Shareholders' Funds	4,373,804	3,611,309	1,577,392	739,149
	48,208,415	44,200,384	24,281,979	22,975,170
PROFIT AND LOSS ACCOUNT				
Gross Earnings	7,430,411	4,659,827	3,643,441	2,930,899
Profit Before Taxation	1,348,669	490,630	213,233	368,077
Taxation	(334,111)	(136,010)	(79,730)	(102,640)
Profit After Taxation	1,014,558	354,620	133,503	265,437
Transfer to Reserves	(814,358)	(254,520)	82,503	224,668
Ordinary Dividends	(200,000)	(100,000)	(50,000)	(40,000)
Retained Profit for the Year	200	100	1,000	769
Profit Brought Forward	2,800	2,700	1,700	931
	3,000	2,800	2,700	1,700
Per 50k share data (adjusted)				
Earnings per share	N1.69	N0.59	N0.22	N0.44
Dividend per share	N0.33	N0.17	N0.83	N0.67
Equity interest per share	N7.29	N6.02	N2.63	N1.23

NOTE: Earnings and dividend per share are based on the issued Ordinary Shares at 31 March, 1997.
Earnings are the After-Tax Profits of each year.



The issued share capital of the Bank is N300,000,000, made up of 600,000,000 Ordinary Shares of 50k each.

The breakdown of shareholders is as follows:

	NO. OF SHARES	%
Nigerian Citizens	360,000,000	60.00
Landspire Limited	184,200,000	30.70
Bankers International Corporation USA	27,000,000	4.50
Banca Nazionale del Lavoro, Italy	14,400,000	2.40
Monte dei Paschi di Siena Italy	14,400,000	2.40
TOTAL	600,000,000	100.00

As at 31st March, 1997, no shareholder except as listed above held more than 10% of the issued and paid up share capital of the Bank.

SUMMARY OF DEALINGS IN UBA SHARES
Dealings in UBA Shares for the period 1st April, 1996 to 31st March, 1997.

			TOTAL	QUARTERLY AVERAGE
April, 1996	-	June, 1996	1,602	520
July, 1996	-	Sept. 1996	1,068	356
Oct. 1996	-	Dec. 1996	748	249
Jan. 1997	-	March, 1997	1,520	506

HISTORY OF CHANGES IN THE BANK'S PAID UP SHARE CAPITAL
Details of shares issued:-

Public Issue		November	26	1970
Scrip Issue	01	July	25	1973
"	02	July	4	1974
"	03	September	11	1975
"	04	March	27	1977
"	05	September	28	1977
"	06	August	2	1978
"	07	July	20	1981
"	08	July	21	1982
"	09	July	20	1983
"	10	September	30	1986
"	11	July	25	1990
"	12	July	18	1994