THE IMPACT OF DEREGULATION POLICY ON THE NIGERIAN FINANCIAL SYSTEM

BY

BELLO MOHAMMED MUKTAR
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DEPARTMENT OF BUSINESS ADMINISTRATION
FACULTY OF ADMINISTRATION
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ZARIA.

1999

DECLARATION

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

BELLO Muhammad Muktar		03/04/20
NAME OF STUDENT	SIGNATURE	DATE

CERTIFICATION

This prouject entitled "THE IMPACT OF GUIDED DEREGULATION POLICY ON THE NIGERIAN FINANCIAL SYSTEM" by BELLO MOHAMMED MUKTAR, meets the regulations governing the award of the Degree of Master of Business Administration of Ahmadu Bello University, Zaria and is approved for its contribution to knowledge and literary presentation.

SUPERVISOR — DATE

Prof. A. D. Sheidu — 17/6/2000

EXTERNAL EXAMINER — DATE

HEAD OF DEPARTMENT — DATE

DEPT. OF BUSI ESS ADM'N
Sign.
Date
Institute of Admin A. B. U. Zaria

DEAN, POSTGRADUATE SCHOOL — 2/3/05 — DATE

DEDICATION

This work is dedicated to my lovely wife KHAIRAT and my SON MUSTAPHA.

ACKNOWLEDGEMENT

My greatest and gratitude goes to the Almighty Allah for his blessings and guidance which has brought me successfully to the end of this course.

I remain grateful and thankful to my supervisor Mallam Ibrahim Fari Okeji (MIFO) for his patience and and guidance without which this work would not have been completed.

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ABSTRACT

The introduction of Structural Adjustment Programme (SAP) with its instruments of implementation have brought radical transformation of the Nigerian economy. These tools of SAP, aimed at correcting the imbalance inherent in the economic system have had a profound influence on the manner and ability with which the banks cany out their activities.

The guided deregulation policy so far has had the effect of increasing tremendously the level and scope of activities of the Nigerian banks such that their asset base, earnings and profitability have shown remarkable increase since inception of sap in 1986.

A number of factors have in cumulative and progressive fashion produced the trend toward deregulation in the financial service industry and in the banking sector in particular. It was discovered that many of the regulations put in place to curb excessive competition have rather produced costly inefficiencies in the provision of financial services and reduced consumer choice.

The financial system have been going through the greatest expansion since the mid-eighties as evidenced by the increase in the number of banks during the era of deregulation to more than twice their number prior to deregulation.

There has in addition, been a significant improvement in the efficiency of banking services as a result of increase in the use of computer technology, product innovations and competitiveness of the banking industry.

The era of deregulation has therefore ushered in more opportunities and new roles for the banks to play through which they are expected eventually to contribute greatly toward the growth and restructuring of the Nigerian economy.

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LIST OF ABBREVIATIONS

BOFID	-	Banks and Other Financial Institution Decree
CBN	-	Central Bank of Nigeria
COBM	-	Chartered Institute of Bankers
ECPER	-	Emwai Centre for Political and Economic Research
FEM	-	Foreign Exchange Market
FITC	-	Financial Institution Training Centre
FMBN	-	Federal Mortgage Bank of Nigeria
FMF	-	Federal Ministry of Finance
FSRCC	-	Financial Service Regulatory Control Committee
GDP	-	Gross Domestic Product
ICON	-	Investment Corporation of Nigeria
IFEM	-	Inter-Bank Foreign Exchange Market
IMF	-	International Monetary Fund
LTD	-	Limited
MRR	-	Minimum Rediscount Rate
NACB	-	Nigerian Agricultural and Cooperative Bank
NAL	-	Nigeria Acceptance Limited
NBCI	-	Nigerian Bank for Commerce and Industry
NDIC	-	Nigeria Deposit Insurance Corporation
NSE	-	Nigeria Stock Exchange
PLC	-	Public Limited Liability
SAP	-	Structural Adjustment Programme
SEC	-	Security Exchange Commission
SFEM	-	Second Tier Foreign Exchange Market
UDB	-	Urban Development Bank
%	-	Percent

ABSTRACT

The introduction of Structural Adjustment Programme (SAP) with its instruments of implementation have brought radical transformation of the Nigerian economy. These tools of SAP, aimed at correcting the imbalance inherent in the economic system have had a profound influence on the manner and ability with which the banks carry out their activities.

The guided deregulation policy so far has had the effect of increasing tremendously the level and scope of activities of the Nigerian banks such that their asset base, earnings and profitability have shown remarkable increase since inception of sap in 1986.

A number of factors have in cumulative and progressive fashion produced the trend toward deregulation in the financial service industry and in the banking sector in particular. It was discovered that many of the regulations put in place to curb excessive competition have rather produced costly inefficiencies in the provision of financial services and reduced consumer choice.

The financial system have been going through the greatest expansion since the mid-eighties as evidenced by the increase in the number of banks during the era of deregulation to more than twice their number prior to deregulation.

There has in addition, been a significant improvement in the efficiency of banking services as a result of increase in the use of computer technology, product innovations and competitiveness of the banking industry.

The era of deregulation has therefore ushered in more opportunities and new roles for the banks to play through which they are expected eventually to contribute greatly toward the growth and restructuring of the Nigerian economy.

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CHAPTER ONE

INTRODUCTION

1.1 Introduction

Before independence up to fairly recent times. It is obvious that agriculture has been the mainstay of the Nigerian economy. It has contributed a great deal towards the growth of the economy especially with regard to the volume of employment generated for the country's labour force. This contribution accounts for between 70 to 80 percent of the overall labour force and constitutes the country's major source of food and raw materials[1].

Despite the fact that most of the agricultural production has been largely of the peasant type consisting of subsistence output, the large number of individuals engaged in it is sufficiently great for the sector to account for about 60% of the Gross Domestic Product (GDP) in the late 1960s and early 1960s[2], hence constituting dominant sector and the major source of foreign exchange earnings and government revenue. However, with the discovery of petroleum, the agricultural sector gradually lost its importance to the mining and drilling sector with crude oil becoming the major source of the country's earnings and revenue.

The mining sector now the leading sector rose from a contribution of GDP of less than 1% in 1950 to about 18% in 1973/74 and to as high as 37.5% in 1980[3].

Nigeria's crude oil production and exports have significantly contributed to the country's ability to earn foreign exchange overtime, as well as being the dominant source of government revenue. For instance, government revenue from petroleum is represented by a rise from about 1.0% in 1985 to 63% in 1974[4].

The oil boom of the 1970s brought about a higher standard of living for the Nigerians which lead to the country becoming heavily dependent on imports financed by the foreign exchange earnings. This in turn led to the stunting of the nation's economic growth and development.

As a result of the structural imbalance in the economy brought about by over-reliance on crude oil the country's major source of foreign exchange earnings and government revenue, along with the subsequent fall in oil prices in the world market, the Nigerian Government had resorted to the adoption of various regulatory and fiscal policies during the early 1980s in an attempt to correct the imbalance. Such measures include economic stabilization policy popularly known as "Austerity Measures" introduced by Alhaji Shehu Shagari Administration. The measures were based on payments and trade controls, and the economy was highly regulated. The measures were not effective enough because they were addressed to the symptoms rather than the root causes of the economic problems and the government succeeded in creating more complex and fundamental problems which include bad structure and organisation of production, ill-defined pattern of consumption and distribution, the improper use of state machinery, corruption, mismanagement, scarce resources and increase in external debts.

These distortions in the economy led the Federal Government to embark on the Structural Adjustment Programme (SAP) in July 1986 which was primarily aimed at effectively altering and restructuring consumption and production patterns of the economy as well as eliminating price distortions and heavy dependence on export of crude oil and importation of consumer goods, improving resilience and increasing its sensitivity to market force.

Deregulation being one of the key components of the SAP is essentially a tool through

which some of the objectives of SAP are to be achieved and it involves the removal of certain government restrictions that were previously imposed on the organs of the financial sector and economic activities in general.

Such policies of deregulation which affect the financial system include:

The Second-Tier Foreign Exchange Market (SFEM) created for the purpose of the exchange value of the Naira to be determined by market forces.

Floating of interest rates.

Not allowing depositors in foreign banks to be used as collateral for security domestic loans.

These measures have so far transformed the banking in a direction which is putting the sector into shape.

The financial system under the era of deregulation recorded certain prospects. The biggest prospect of the system is the impact of customers services in a competitive business environment, with many banks chasing after a limited number of customers and there were pressures on banks to offer more competitive services.

In the pre-deregulatory policy, most of the banks products introduced had rendered no direct service to corporate and individual customers because the regulatory environment did not encourage the rendering of such services, and the objective of most bankers was to generate a stable fool of revenue and sufficient net interest margin to cover over heads and reasonable return on capital.

However, the situation changed when newly licensed banks in the country started responding aggressively to competitive pressure precipitated by, the policy. The environment became more conducive for innovation, the upsurge in the number of banks did not only reduce the market share of the existing banks but had awakened stiff competition in the industry as new products and services were being unveiled more frequently in the financial market.

Thus, pre-deregulatory period was characterised with fixed exchange rate and interest rate, during the implementation of the deregulatory policy, interest rate being one of the allocative instruments in a market economy were deregulated and banks were allowed to charge different interest rates to their various customers.

The banking sector which looks sluggish in responding to the challenges of growing economy during regulation policy recorded certain prospects and turned out to be the fastest growing sector during the implementation of the deregulation policy in Nigeria.

1.2 Statement of the Problem

The introduction of the Structural Adjustment Programme (SAP) ushered in a new era of challenges to the Nigerian financial system. The new reforms brought with it new policies that have serious repercussion on the operations of the Nigerian banks. These effects were both positive and negative.

There has been a proliferation of new banks, competition has intensified, there has been an increase in innovation and sophistication in product and service delivery. Even as the new changes creates new business opportunities, it has also engendered challenges and problems.

This write-up is aimed at studying the impact of guided deregulation policies on the financial sector operation in the country.

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1.3 Objective of the Study

This study is primarily aimed at examining how the policies of the government under guided deregulation since the inception of SAP have affected the banking industry's ability to perform their functions and how well they have adjusted their operations in response to the new challenges posed by the changes in government policies.

It will also attempt to determine to what extent the impact of guided deregulation have enabled banks to contribute towards the attainment of rapid economic development and restructuring of the distortions in the Nigerian economy.

An attempt will also be made to compare the pre-SAP period with the present guided deregulatory period. A look will be taken at the Assets and Liabilities of banks. An analysis will also be made of the challenges of guided deregulation in the financial system or industry. It will also determine whether banks witness more growth and development during the deregulation economic policy than pre-deregulation policy in Nigeria.

The study will in addition offer some recommendations on how the performance of the Nigerian financial system may be improved to enhance their effectiveness in contributing towards realising the nation's goal of economic recovery and self-reliance.

1.4 Significance of the Study

It has become increasingly necessary for the Central Bank of Nigeria (CBN) to deregulate the financial sector, particularly the commercial banking sector prior to the deregulation era, the big four banks control more than 70% of the banking operation in Nigeria. The major banks involved are: First Bank of Nigeria, United Bank for Africa, Union Bank of Nigeria and Afribank PLC. The 1976 indigenisation decree which gave majority share equity participation to Nigerians did not solve the problems posed by the dominance posed by the

dominance of these banks.

The problems among others include discrimination in granting of loans and advances to foreign entrepreneurs and starving the indigenous investors of funds, reparation of huge profits, gross inefficiency in service delivery etc.

This clearly indicates that majority shareholding does not mean controlling the operation of these banks. The control were still in the hands of the foreign owners. Furthermore, there was the problem of high interest rates which many indigenous entrepreneurs can not afford.

In order to correct these anomalies, the government through the Central Bank of Nigeria decided to deregulate the banking industry as part of the overall deregulation of the economy in line with, SAP since 1986. This meant allowing the forces of the market to determine the value of Naira, interest rates and allowing for more banks to be established to compete with the older ones. These measures have to some extent reduced the profitability of the older banks and improved the efficiency of the banking industry.

This study is significant in the sense that it will help determine whether the deregulatory measures will provide the desired direction in the level of economic activities. Or, whether the measure would be a curse rather than blessing on the industry.

1.5 Scope of the Study

The Nigerian financial system comprises the regulatory/supervisory authorities as well as banks and non-banks financial institutions.

This thesis covers the operations of the regulatory authorities and the banking institutions (commercial and merchant banks) in Nigeria during the pre-SAP and the present deregulatory periods. It will analyse the impact of guided deregulation policy on the performance and challenges of the financial sector. It will also cover policies on total bank

deposits, loans and advances, profitability etc.

The study shall examine the various instruments used and some developments in the financial sector during the regulatory period.

1.6 Limitation of the Study

When this project was initially conceived the intention was to carry out an indepth study by both using primary and secondary data. It was hoped that primary data could be obtained through administered questionnaire and personal interview. However, when a preliminary investigation was carried out bank staff were not prepared to divulge information to any outsider.

Therefore, the major limitation encountered in this study involved obtaining of data through questionnaires. The officers and management of the banks were unwilling to grant audience to the researcher and even when contact was made, just few officers provided the required information or data through personal interview. On the other hand, some officers termed such data or information as "secret".

Financial and time constraint was a major problem in carrying out the study. Inadequate financial resources hindered me from going to all necessary places. Sufficient time was not on my side. Another limiting factor is that guided deregulation is a recent phenomenon in Nigeria. Documented data on the topic is limited hence the accuracy of deductions arrived at in the reports is not guaranteed, and room is therefore made for the possibility of such erroneous deductions. However, despite these limitations, the research was still carried out successfully and hopefully, parties to which the findings are significant may find it useful for their various purpose.

In short primary and secondary sources were used. These include interview granted, use banks and annual reports, CBN periodicals, financial journals and publications textbooks etc.

1.7 Definition of Terms

Deregulation Policy:

Deregulation Policy refers to the fiscal and monetary measures which seek to remove regulatory controls on the activities of economic actors in order to enhance their competitiveness in the markets.

Laissez Faire:

That is, free for all banking with no licensing requirement and no regulation of any sort of control the operations of a bank.

Bank:

BOFID No. 25 of 1991 defined banks as "the business of receiving deposits on current account, savings account or other similar account, or paying or collecting cheque drawn by or paid in by customer, provision of finance or such other business as the CBN Governor may by order published in Gazette designate as banking business".

Distressed Banks:

These are banks with problems relating to illiquidity, poor earnings and non-performing assets. The extreme case of distress is referred to as insolvency which implies that a bank's liabilities are more than its assets.

Prudential Guidelines:

These are guidelines and practices which all licensed banks are required to adhere to in reviewing and reporting their performance, particularly in the areas of credit portfolio

classification and disclosure; provision for non-performing facilities; interest accrual; classification of other assets; and off balance sheet engagements.

1.8 Structure of the Study

This study takes critical look at the impact of guided deregulation policies on the financial system in Nigeria. The project is organised into five chapters.

The first chapter, which is the introduction, reviews the guided deregulation in the Nigerian financial system.

The literature review is contained in chapter two. It is centre on the structure of Nigerian economy before SAP, banking regulation and deregulation policies and developments in the system.

The method of data collection is discussed in the third chapter, while the presentation and analysis of data makes the forth chapter.

The thesis is summarised in the fifth chapter and conclusion was made and appropriate recommendations were given.

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2. Ibid, pp. 6-7
3. Ibid, p. 8
4. Ibid, p. 58.

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CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

In order to understand what is meant by deregulation in an economy, it is simpler to first begin with a definition of economic regulation.

Regulation in its broadest sense refers to all of the controls which government imposes on the economy and businesses of all kinds. Although government all over the world has always reserved the right to control general economic activities, its participatory and regulatory roles were traditionally most felt in the area of public utilities such as electricity, water etc. Regulation of these enterprises were to avoid competition which is regarded as wasteful and also to prevent abuse of monopolistic power. Over time, government control of economic activities has grown and extended beyond these and now embraces diverse control on both the domestic and external sectors of the economy.

In many cases, regulation has shifted from mere controls of economic activities to included government intervention or participation in non-traditional economic activities with the ultimate goal of fostering competition and improving economic efficiency.

Excessive regulation especially in the developi countries, creates many problems apart from the fact that it does not always achieve its primary aims. Inevitably, as a result of such problems arising from too much regulation, a process of deregulation is embarked upon which is basically aimed at removing all the unnecessary controls that tend to inhibit economic performance in both the private and public sectors of the economy.

The introduction of SAP in 1986 was a unique opportunity for Nigeria to review all the existing controls on economic activities in support of the restructuring of the economy.

2.2 The Structure of the Nigerian Economy

Before the advent of oil, agriculture was the mainstay of Nigeria's economy. Its principal exports, cocoa, groundnut, palm oil, rubber, cotton and timber, constituted the engine of growth as well as source of foreign exchange. As the backbone of the economy it accounted for more than 70% of the country's exports and contributing 40% to the Gross Domestic Product (GDP), at independence, peasant farmers were largely responsible for the sustenance of the economy. The marketing board surpluses provided investment funds for broadening the base of the economy.

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The oil boom of the mid-seventies brought some changes in the Nigerian economy without right neglect of the agricultural sector. With the increased revenue as a result of oil boom, government increased its intervention in the economy and this resulted in the rapid proliferation of parastatals and multiple public investments many of which could be best described as "white elephant projects". Between 1970 and 1980, Federal Government revenue rose from ₦67.6 million to ₦12.2 million while the expenditure rose from ₦531.9 million to ₦9.7 billion respectively with more than 66% of this amount going into capital projects[2].

The manufacturing industries durino this period was also proliferated due to the enhanced revenue from oil. These industries depended largely on imported inputs of capital equipment, raw materials, spare parts and other essential inputs. The industrial sector thus generated little or no backward linkage effects with agriculture in terms of the latter providing raw materials for the agro-based industries. However, due to government renewed interest in this sector it received a lot of protection from external competition. It grew by 11.5 percent

annually between 1970-1971, and 1972-1973 and by an annual compound rate of 15.6 percent between 1974-1975 and 1977/78. The growth rate of the sector declined in the late 1970s and early 1980s due to shortage of industrial inputs occasioned by declines in oil revenues. The domestic output declined by 13.2 percent in 1984 compared with the decline of 4.7 percent in 1983. Its contribution to the GDP which increased from 7.42 percent in 1980 to 13.25 percent in 1983 declined to 11.48 percent and 11.75 in 1984 and 1985 respectively[3].

The development of infrastructural sectors of transport, power, poor communication, energy, water supplies etc. during this period was no less dependent on the external sector as most of the equipment, facilities, spare parts, technical know-how etc. for setting them up and maintaining them had to be procured from abroad through the use of hard currencies.

2.3 The Major Characteristics of the Nigerian Economy Before (1986) The Advent of SAP

The problem of the Nigerian economy started in the early 197os due to increased government intervention in the level of economic activities. With the enhanced revenue from the oil boom the government development programmes designed to accelerate the pace of development and growth. Furthermore, it affected not only the investment, production and consumption pattern of the economy but also its socio-cultural values, political aspirations, style of economic management as well as the policies and programmes that were implemented over the years. For instance, during the decade of 1976-1986, the share of consumption in total expenditure grew from 68.49% to 89%, while investment in capital formation remained disastrously low. From 31.51% in 1976, Gross Capital Formation declined continuously to as low of 9.2% in 1986.

To sustain this very high level of consumption, the country not only relied on the revenue base provided by the oil boom, but also depleted reserve and resorted to the rapid accumulation of debts. The maturity structure of these debts put a lot of strain on the resources of the government and affected her ability to repay them. The collapse in the price of oil in the international oil market found the country to face with overwhelming liquidity crises.

In the pre-SAP Nigeria, the economic and social deficiencies included the following[5].

1) Reduced external earnings as a result of a fall in the price of crude oil in the international market.

2) A debt-ridden treasury.

3) Over-valued currency.

4) Reduced agricultural production which culminated in the country being a net importer of food in the late seventies and early eighties.

5) Balance of payment deficit as a result of excessive importation.

6) Low industrial growth.

7) An economy laden with subsidies.

8) High level of unemployment.

9) Capital flight, etc.

It was against this background of total collapse of the economic system that the General Babangida Administration embarked on the Structural Adjustment Programme in July 1986.

The SAP was aimed to achieve the following objectives:

a) Restructure and diversity the productive base of the economy in order to reduce dependence on the oil sector and on imports.

b) Achieve fiscal and balance of payment over the period.

c) Lay the basis for a sustainable non-inflationary or minimum inflationary growth.

d) Lessen the dominance of unproductive investment in the public sector, improve the sectors efficiency and intensity the growth potentials. Various measures have been put in place to achieve these objectives, including economic deregulation.

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2.4 The Genesis of Deregulation Policy

The genesis of deregulation policy can be traced back to the Physiocrats era - the period before the Mercantalist Doctrine of 15th and 16th century or the rise of Maxima economics. The Physiocrats believed in the role of nature and maintained that the society should be ruled according to natural law in which soil is the source of wealth and in which private ownership and right to acquire it should be unmolested by the government interference.

The Mercantlist Doctrine of 15th and 16th century was a sharp contrast to the Physiocrat economic view. This doctrine maintained that wealth can be generated by protecting an economy from foreign competition. This was the first doctrine that encouraged state intervention in economic activities[6]. Today this doctrine is equivalent to the term "government regulation policy".

The Mercantilist doctrine was challenged by the publication in 1776 of "An inquiry into the nature and causes of the wealth of nations" by Adam Smith. His view was based on Laissez faire which means nature should be allowed to operate freely without government

interference. He argued that a human being is naturally the best judge of his own interests and should be left alone to pursue these in his own way. The physiocrat economic view become more popular because of Adam Smith's economic principle, and in 1817, the Mercantilist doctrine was serious attacked and ridiculed by the publication of David Ricardo's paper titled "Principles of Political Economy and Taxation" which threw more light on the laissez-faire principle that economic growth and well being cannot be engineered by the State and this became the economic orthodox.

In early 1960s Milton Friedman, who led neo-classic economists draw the attentions of the world to the negative effects of distortion and mal-allocation of resources that resulted from government interference in economic activities. The collapse of the Bretton Wood's fixed exchange rate system in early 1970 and the global stag-inflation of the 1980s, advanced the thoughts of the neo-classic economists. The need to improve productivity to remain competitive increased with the integration of economics as a result of advances in telecommunication and information technology, thus force the world to rethink the role of government in economic development and enhance this was the beginning of the introduction of the "deregulation policy"[8].

Based on the historical background of deregulation policy, an International Monetary Fund (IMF) economist noted recently that "Experience teaches that deregulation is the best means of economic reforms. It enables the private investors, domestic or foreign to take over all the risks and opportunities of an enterprise".

Based on the above fact, the Nigerian economy was deregulated in 1986. Prior to this year, several measures were taken to revamp the ailing economic situation of the country. Such measures include economic stabilization policy popularly known as "Austerity Measures"

in 1982. The measures were based on payments and trade controls, and the economy was highly regulated.

In October 1985, the Federal Government declared a 15 month economic emergency period in pursuit of further economic stabilization. The major action was the compulsory deduction from workers salaries and company profits. In January 1986, 80 percent of petroleum subsidy was removed. The various measures drastically reduced the supply of raw materials and spare parts to the independent manufacturing sector leading to extensive plant closure, low capacity utilization and retrenchment of workers. Investment both by the public and private sector shrank and the depression deepened, external debt outstanding rose to over $18 billion out of which about $5 billion represented trade arrears and external debt services obligations rose to about 32% of exports[10]. Despite all the problems in the economy during the period, the banking industry was heavily regulated which later created more problems which did not allow it to achieve its primary aims. As a result deregulation policy was adopted with the expectation to rationalise the use of scarce resources especially foreign exchange so as to enhance allocative efficiency, promote industrial diversification and stimulate domestic production not only to broaden the supply based of the economy but to expand non-oil exports[11].

2.5.0 The Rational for Regulation and Deregulation

2.5.1 The Rationale for Regulation

Every human endeavour requires one form of regulation or the other to ensure inter alia that the operations play according to the rules. Banking industry is no exception and need a large dose of regulation of its critical role.

Regulations may come in different forms, they may be in form of customs, rules or legislation. Without legislation, economic and financial system would drift to unwanted directions and this might lead to disorder and chaos.

Many governments today, generally seek by legislation and regulation to control the banking sector so that it operates in the desired direction with regards to the level of aggregate economic activity and well-being of the society in general.

The question now is "why regulate"? Koch J.V. (1980) advance five reasons why markets are subject to economic regulations. These were mainly[12]:

a) When undesirable market structure exist. The existence of an imperfect market structure (perhaps evidence by fewness of firms) tend to higher prices, reduce output (economic) rents being earned by firms that market.

b) The desire of society to conserve and efficiently use scarce sources. Certain natural resources are found in limited quantities and in absence of regulation a zero private price would be attached to the use of the resources. Hence, in order to increase social benefit, its use regulated and right to use is licensed.

c) When there are significant economic externalities associated with activity of firm in a market.

d) Certain types of economic competition and behaviour are considered to be socially undesirable, such as price fixing usually which is an out growth of the type of market structure relating to market in question.

e) Liberation distrust of accumulated power whether political or economic in character such an attitude may result in regulation even when the actual

behaviour of the firms in the market falls to be noteworthy.

Nwanko G. O. classified regulation into four categores:[13]

i) Structural (capital requirements, ownership),

ii) Prudential (permissible activities, liquidity, capital/loan ratio),

iii) Fair play (lending to staff and directors, venting of advertisement and returns).

iv) Monetary (interest rate, sectoral allocation, rate of loan expansion).

While Dan Azu is of the opinion that rules and regulations are needed to ensure that the Units "operate within the laws of the land, maintain a minimum standard, protect members of the public against abuse and exploitation, contribute to the development objectives, minimise the incident of collapse and ensure that the operations are not against the progress of the nation[14].

According to Hyacinth Oduoza (1988), he clearly stated the rationale for deregulating banking activities. These include[15]:

i) To build up trust and confidence in the public. Bankers of former years seldom enjoy good public image, this is true in the past. Now customers are dissatisfied over the poor services of the banks. From the customer's view point, banks are unpopular. Institutional controls comes in to ensure that adequate services are provided at reasonable cost to the public.

ii) to ensure the orderly growth of the economy. Bankers create money and if they are allowed to operate without regulation and restrictions, they can over-expand the liquidity of the economy and cause monetary instability which leads to macro economic problems like inflation.

iii) To ensure the banks are solvent and liquid. These two factors give confidence to the monetary authority as well as the members of the public.

iv) Assist in achieving significant transformation of rural banking. The introduction of rural banking programme is primarily responsible of this.

Regulation is necessary but it should not be too much to enable the financial system not to perform. Regulation or legislation should be made to foster economic activities.

Without legislation laissez faire attitude would pervade the economy and this might lead to economic disorder and chaos. Economic and financial system would be disrupted, hampered and devoid of growth.

2.5.2 Rationale for Deregulation

As stated earlier, deregulation is an attempt to allow free market mechanism to operate with a view to facilitating better allocation of resources to permit better efficiency in the markets.

Deregulation refers to those fiscal and monetary measures which seek to remove regulatory controls on the activities of economic actors in order to enhance their competitiveness in the markets.

It is to deliberately and systematically liberalise structural and operational guidelines which have hitherto impinged upon economic growth and profitability of economic actors. It should be noted that deregulation is a continual process of examining the existing regulatory framework with a view to deregulating when appropriate and regulating when necessary to allow market forces greater role in the pricing system.

The theoretical basis or rationale for deregulation can be appreciated by examining two competing hypotheses on the role of banks in saving-investment process:

The Financial Repression Hypothesis and the Neo-Structuralist Hypothesis. These hypothesis offer conflicting views on the effects of deregulation in the banking system on economic development.

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The Financial Repression Hypothesis theory is associated with the work of Cameroon (1972) McKinnon (1973) and Shaw (1973). It holds that ... financial development would contribute most significantly to economic growth if the authorities were not to interfere in the operations of the financial institutions. There central argument is that indiscriminate financial regulation (repression) distorts financial prices and reduces the real rate of growth and the real size of the financial system[16]. Measures such as the imposition of foreign exchange controls, interest rate ceilings, high reserve requirements and the suppression of private capital markets can all increase the flow of domestic resources to the public sector.

Successful financial restriction is hence exemplified by higher proportion of funds from the financial system being transferred to the public at a very low cost.

Selective or sectorial credit policies are common components of financial restriction, used to encourage private investment in what the government regards as priority activities. Interest rates on loans for such approval investments are subsidized.

McKinnon and shaw maintained that to the extent that bank observe loan rate ceilings, non-price rationing of loanable funds must occur. Credit will be allocated not according to expected productivity of the investment projects but according to transaction cost and perceived risk of default. Loan rate ceiling discourage risk taking on the part of financial institutions: risk premia cannot be charged when ceiling are binding and effective. Hence, a large proportion of potentially high-yielding high-risk investments. Subsidized loan rates encourage high delinquency and default rates reduce flexibility and increase fragility of financial systems.

McKinnon and Shaw demonstrated that liberalizing the interest rate and abolishing non-price credit rationing will increase the incentive to save and invest and raise the average efficiency of investment. It will also deter enterprises from undertaking low yielding investment, as they will not be profitable under high interest rates.

Hence, the average return on investment will increase. The rate of economic growth will rise in this process and shift the saving function (McKinnon 1973)[17].

On the other hand, Siglitz and Weiss (1981) developed a theoretical model which shows that financial liberalization will not guarantee efficient allocation investment fund, as banks will engage in a voluntary credit rationing[18]. They showed that if banks cannot assess perfectly the credit worthiness of potential borrowers, (because the cost of doing so may be very high) raising loan rate interest will not necessarily increase a bank's expected rate of return, even if there is excess demand for loans at the existing loan rate. Hence, contrary to McKinnon and Shaw's models allocative efficiency is not guaranteed even when interest rates are liberlized. Broll and Gilory (1986 p. 365) also showed that when information costs about borrower's riskiness are high, a bank's expected return from lending may not increase even with an increase in collateral requirements[19]. All these happened because investors that choose to borrow at high interest rate or high collateral requirement will tend to choose riskier projects and banks will avoid them since expected return from leading to them will be low.

It is, therefore, evident that efficient resources allocation when the banking industry has been liberalized cannot be guaranteed Cho (1986), therefore, advised that the development of an efficient equities market, as a supplement to the banking industry, is necessary for the success of any liberalization programme.

The Neo-structuralist models (such as those of Taylor (1983) and Van Wijinbergen (1982) assert that financial liberalization, that result in interest rates and exchange rate devaluation, can produce cost-pushed stagflation (an acceleration in the inflation rate) and a reduction in the rate of economic growth at the same time.

The most important feature of Neo-structuralist models is the importance of unregulated financial institutions, which are assumed to be more efficient due to the absence of Central Bank control, such as reserve requirement. Taylor (1983) and Van Wijinbergen (1982) pointed out that whether liberalization of interest rates does increase the total real supply of credit depends on the required reserve ratio and on whether the increase deposits come as a result of liquidation of investment or reduction in the deposits of unregulated financial institutions[20]. They, however concluded that, in practice, financial liberation is likely to reduce the rate of growth by reducing the total supply of credit available to business firms. The same conclusion was reached by Buffie (1984, p. 320), who remarked that "once we allow for repercussion in the curb (or informal) market, financial liberalization becomes a perilous undertaking". Hence, to enhance economic growth, the models advocate a reduction in the reserve requirement ratio or the payment of the market loan rate on required reserve.

Although the predictions of the Neo-structuralist thesis have been supported by empirical studies, the main intellectual basis for International Monetary Fund (IMF's) financial sector analysis and policy over the past decades are those propounded by McKinnon and shaw.

However, the most credible explanation for deregulatory specter which is haunting most developing countries swore those espoused by price Waterhouse. This is an accounting firm which succinctly explained the rationale for deregulation, when it was observed in its publication, "The economic stocks of the 1980s and the consequent shrinking of international

credit in response to the debt crises have convinced many developing countries to rely more on market forces to develop their economics and financial sectors. In an effort to promote financial deepening and domestic capital formation, developing countries have moved to liberalize interest rates and capital control and to phase out directed credit policies, a number of countries are privatizing State-owned financial institutions".

Finally, the idea of deregulation is fast catching in Western Europe as well. For instance, in United Kingdomn, comprehensive privatisation drive is illustrative of this fact, so also in France. The less developed economics of the "South" with their various structural adjustment programmes are also adopting the idea of deregulation and applying same to some of their sub-economic sectors.

2.6 The Nigerian Financial System

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A financial system is a conglomerate of various institutions, markets, instruments and operators that interact within an economy to provide financial services. Such services may include resource mobilization and allocation; financial; intermediation; and facilitation of foreign exchange transactions to enhance international trade, among others. The financial system plays a significant role in the process of the economic growth and development of the country. As the economy grows, the financial system becomes increasingly deep and broad and its structure becomes increasingly sophisticated. In the process the system offers a wide range of portfolio options and issuable investments for investor - a function often referred to as financial intermediation[21].

The Nigerian financial system comprises the regulation/supervisory authorities as well as banks (area of study) and non-bank financial institutions. the regulatory/supervisory authorities are the Federal Ministry of Finance (FMF), Central Bank of Nigeria (CBN), Nigerian

Deposit Insurance Corporation (NDIC), Securities and Exchange Commission (SEC), National Insurance Commission, Federal Mortgage Bank of Nigeria (BMBN), and the National Board for Community Banks (NBCB). The CBN is the principal regulator and supervisor in the money market with the NDIC playing a complementary role. The CBN exclusively regulates the activities of finance companies and specialisation/development finance institutions such as the Nigerian Industrial Development Bank (NIDB), the Nigerian Bank for Commerce and Industry (NBCI), and the Nigerian Agricultural and Cooperative Bank (NACB). The SEC is the apex regulatory/supervisory authority in the capital market. The Nigerian Stock Exchange (NSE) is a self-regulatory or user-regulatory institution. The registrars, stock brokers and issuing houses that also interact in the market complete the chain of the capital market.

In 1997, amendment was made to CBN Decree No. 24 of 1991, the CBN is to report to the Presidency through the Federal Ministry of finance. Also with effect from January, 1997, the CBN has effectively assumed the leadership of all the banking institutions in the financial system. In this regard, the CBN now has the responsibility for controlling and supervising all commercial, merchant and community banks, the People's Bank, finance companies, discount houses, primary mortgage institutions, bureaux de change and all development banks.

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2.7.0 Evolution of Banking in Nigeria

2.7.1 Commercial Banking in Nigeria

The African Banking Corporation was the first modern commercial bank to open a branch in Lagos in 1892. Its existence was made difficult by the trade recession which hit Lagos in that year. The bank was taken over by Elder Dempster and Company which ran it as a private bank until December 1894 when the Bank for British West Africa (now called

First Bank Nigeria PLC) as organised and registered in London with an authorised share capital of $10,000 (pounds)[22].

The next was Barclays Bank DCO (new Union Bank Nigeria PLC) which was established in 1917. In 1949, the third expatriate bank was established called the British and French Bank (now called United Bank for Africa PLC).

The expertise banks came principally to render services in connection with international trade, so their relations at that time were purely with the expatriate trading companies and government. They largely ignored the development of Nigerian entrepreneurship.

The banks controlled about 90% of aggregate bank deposit from 1914 to the early 1930s, several abortive attempts were made to establish locally owned and managed banks to break foreign monopoly or domination.

In 1929 the first indigenous bank was formed and it was called industrial and commercial bank. Later many banks were set up. They include National Bank of Nigeria, Agbonmagbe, African Continental Bank. Most of the banks set up failed due to under capitalization, poor management and aggressive competition from the expatriate banks. Indeed the period between 1892-1952 was a free-for-all banking.

The banks failures during the period necessitated the need for banking legislation and control of banking in Nigeria. The government set up a Commission of inquiry - the Panton Commission. The outcome led to the enactment of Banking Ordinance of 1952.

In 1958, the CBN was established and took off in July 1959. Indeed, 1959 can be regarded as a watershed in the annals of banking industry in Nigeria. It was not only the CBN that was established in 1958, but also the foundation of Nigerian Money and Capital Markets were laid in that year.

With the banking ordinance of 1952 and 1958 laying the legislative background and foundation, the amendments of 1961 and 1962 plugging the observed loopholes and deficiencies in the system, and the 1969 Banking Decree consolidating and improving on previous legislation, commercial banking in Nigeria was poised to take off in the 1970s. During this period commercial banking witnessed two major developments. The first is the partial indigenisation of the banking system through Nigerian Enterprises Promotion Decree of 1972. The second is the establishment of many state owned commercial banks. This developments has led to an unprecedented increase in the number of commercial banks operating in the country.

Finally, with the introducing of SAP in 1986, the Nigerian banking environment was deregulated in line with the spirit of the new reforms. This has led to a substantial increase in the number of commercial banks operating in the country to take advantage of the liberalized environment but still some banks have become distressed, 13 as at January 1988, The number of commercial banks as at December 1986 was 64 with 2,402 branches as at December 1996.

2.7.2 Merchant Banking in Nigeria

Merchant banking operations began in 1960 but its activities did not really develop until mid-7os. It started with two small companies; Philip Hill Nigerian Ltd. and Nigeria Acceptance Ltd. They both operated between 1960 and 1969 and then merged to become what is known as NAL Merchant Bank Ltd.

Following the merger, Nigerian Acceptance Limited (NAL) remain the only merchant bank operating in the country until 1973 when a license was issued to United Dominion Trust Bank Nigeria Limited (U.D.T.) entered the market.

After some years other merchant banks were established such as First National City Bank of New York and First National Bank of Chicago were licensed in 1974.

The Indigenization Decree (60:40% indigenous/expatriate equity ownership of the banking industry), the oil boom of 1970s and the third national development plan helped to increase merchant banking activities in Nigeria.

In September 1979, the American Merchant Bank Limited an affiliate of First National Bank of Boston was licensed to operate. This was the first merchant bank to be sponsored by a private Nigerian investor in collaboration with foreign banking interest. Many more banks were licensed during the year.

After 1979, many merchant banks were given license to operate in Nigeria. By the end of December 1996, there were 51 merchant banks with 147 branches, while their total assess amounted to ₦111,2666.9 million, compared with ₦91,801.3 million in 1995.

2.8.1 The Nigerian Banking Scene

In seeking to discuss the issue of deregulation in the Nigerian banking system, it would be expedient to take an overview of the system over the years so as to fully understand the rationale behind the various regulations that have been established.

The Nigerian banking scene before 1986 was characterised by changes designed to promote banking in the country. For the purpose of this analysis, I will divide the period into phases, viz:

2.8.2 Banking in the Era of Unregulated (Absences of Regulation or Laissez Faire Era 1894-1952)

This period is also referred to as the free banking era. It is characterised by two main features. One is an absence of any banking legislation. Anybody could set up a banking company, provided he registered under the company's ordinance.

The second feature of the period is that it was during this free banking era that the three biggest foreign banks and the two biggest indigenous banks were established. Banking business during this period was also monopolised by these foreign banks, the African Banking Corporation which was established in 1892. The bank changed its name to Standard Bank and to the present First Bank of Nigeria PLC. The second foreign bank is Barclays Bank DCO established in 1917 (the present Union Bank of Nigeria PLC), and the British and French Bank (1948), the forerunner of the present United Bank for Africa PLC.

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In the indigenous sector, about four banks were established. These included the National Bank of Nigeria Limited 1933 by the then Western Regional Government-African Continental - 1045, Agbonmagbe Bank now Wema Bank PLC - 1945; the Nigeria Formers and Commercial Banks Limited - 1947. These banks were established principally because of the alleged discrimination by the foreign banks against indigenous entrepreneurs. Unfortunately, however, these indigenous banks offered little or no competition to the foreign banks essentially because of their weak capital base and poor managerial capacity. There was obviously a dearth of qualified and experienced banking professionals in the early years of banking in Nigeria.

Consequently, all but three of the indigenous banks failed. These failures caused losses to depositors and generated government's concern over the desirability of enacting a legislation

that would stipulate conditions for healthy banking operations. This naturally led to the Patron Commission which was to enquire into the business of banking in Nigeria and make recommendations to the Government in the form and extent of control which should be introduced.

Although the Commission submitted its report on 25th October, 1948, it was not until 1952, four years later, that the first ever banking legislation was enacted.

2.8.3 Banking in the Era of Limited Regulations 1952-1958

The enactment of Nigerian Banking Ordinance in 1952 introduced some form of regulations into the Nigerian banking scene. The ordinance laid down the standard and procedure for the conduct of banking business by prescribing the mandatory minimum capital requirement for banks and introduced regulations to check bank failures. This period also marked the beginning of State-support for and assistance to indigenous banking. Indeed, the survival of some of the indigenous banks during this period was predicated on the support and assistance they received from their various governments. However, only those indigenous banks established during the period all failed. The failures of this era were attributed largely to the monopolistic structure of the banking industry which allowed foreign banks to enjoy exclusive patronage from the British firms.

2.8.4 Banking in the Era of Intensive Regulations 1958-1986

The period 1958-1986, which may be aptly described as the regime of intensive banking regulations, began with the enactment of the Central Bank of Nigeria Act of 1958 which gave legal backing to the establishment of the central Bank of Nigeria. The CBN Ordinance or Act introduced important regulation designed to promote orderly commercial banking and prevent the establishment of unliable banks. The Act empowered the CBN to

promote and integrate the Nigerian financial system. Thus, the CBN was able to outline regulatory measures to efficiently stem the tide of bank failures that followed the first banking boom. Consequently upon this new encouraging climate, more commercial banks sprang up in the country. For instance, between 1959 and 1960 eight commercial banks were established bring the total number of commercial banks to 12 which increased further to 17 by 1962.

Under the 1968 Companies Act, foreign based banks operating in Nigeria were obliged to incorporate in the country.

During the period, also, government acquired controlling shares in a number of foreign banks including the big three[1] commercial banks namely First Bank, Union Bank and United Bank for Africa. Two other sources of banking regulations were the Banking Act of 1969 and Exchange Control Act of 1962. The Banking Act of 1962 generally provided for the regulation and control of the monetary and financial system, specifically, it made provisions for the granting of licences to banks while imposing restrictions on the activities of licensed banks. The Act also made provision for the CBN to exercise its powers in maintaining monetary and financial stability in the economy, the stipulation of liquidity and capital adequacy requirements, certain categories of investments banks cannot undertake as well as limits on interest rates and bank lending to the private sector. The Exchange Control Act of 1962 was not aimed at banks directly, but since foreign exchange transactions are mostly carried out through banking system, the existing foreign exchange regulations would necessarily restrict the actions of the banks. The 1962 Act, whenever it was vigorously applied during periods of scarce foreign exchange resources, ensured that foreign exchange was allocated to the priority sectors of the economy.

Other banking legislation during the period include the Banking Decree of 1969, the Banking (Amendment) Acts of 1970, 1972 and 1979[23].

2.8.5 Banking in the Era of Pre-Deregulation 1892 and 1986

The banking industry has gone through considerable transformation in over hundred years. There have been times of prosperity as well as times of crises. The industry have also experienced banking in absence of regulation and presence of intensive regulation.

Pre-deregulation era covers the period when banking began in Nigeria and when the policy of financial and guided economic regulation was adopted and implemented. This represent a period totalling 95 years, from 1892-1986.

2.8.6 Banking in the Era of Post-Regulation 1986 To-Date

In the month of July 1986, the government embarked upon a programme of economic deregulation with the adoption of Structural Adjustment Programme (SAP). The essence of the policy package was to remove or at least to reduce the degree of the observed situations in the economy and a situation which had constituted a major hindrance to the efficient allocation of economic resources. Subsidies were to be removed, price and exchange controls lifted, government companies and essential parastatals privatized or commercialized while additional policies were to address the disadvantage structure of the economy.

The banking and financial sector were also to benefit from the economic and financial reforms. A policy of financial liberalization was adopted which in essence made for easier entry into the banking industry and encouraged the establishment of a variety of financial institutions[24]. The foreign exchange market was deregulated. This represented a major development within the economy's adjustment programme.

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In January 1987, interest rates were deregulated and banks were allowed to fix their deposit and lending rates based on market forces. In 1994, the government came out with a measure whereby the lending rate was pegged at a maximum rate of 21 percent. This include all administrative and other charges. While the maximum rates payable on savings and deposits were fixed at between 12 and 15 percent. The exchange rate was also fixed at ₦22 to a dollar. By this time 1987, many more banks had been licensed. Indeed, one of the most significant development in the industry since deregulation has been the sheer rate of physical expansion. This brought with a lot of positive changes. The practice of arm chair banking had changed. Positive innovation were the ultimate result of the financial liberalization policy. Banks designed and developed a variety of competing products to gain an upper hand in whatever segment of the market constituted their focus. Of course, the ensuring competition and the need to control the inflationary pressures which resulted from the considerable devaluation of the Naria caused interest rates to rise sharply. This, in turn, encouraged domestic savings while the industrial sector found it difficult to cope with the rates. Perhaps for the first time in many years, banks enjoyed positive real rates of return on their investments[25]. Hitherto, they had subsidized investors since the lending rates had been lower than the rate of inflation.

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In 1988, the Nigerian Deposit Insurance Corporation (NDIC) was established. This supervisory body was saddled with the responsibility of insuring and thereby safeguarding depositors' funds. Banks were expected to compulsorily insure their deposits by paying an annual premium representing a percentage (1/16%) of their deposit liabilities. The need was exemplified by the large credit exposure of a number of licensed banks within their short period of existence as well as the losses which may occur as they take upon themselves undue risks

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in their aggressive pursuit to survive completion. The capital requirement of banks have been reviewed several times from ₦12m - ₦30m - ₦50 and now to ₦500 million for commercial banks and ₦10m - ₦20m - ₦40 and now to ₦500m for merchant banks. The recent paid up capital of ₦500m for both commercial and merchant banks has to be paid latest by December 1998. Failure for a bank to meet up the requirement will be rendered distress.

Another major policy was designed to aid the supervision of banks as well as to ensure that the true quality of banks' assets were revealed and true cash profits were also declared.

In 1991, the ceiling on interest rates was re-introduced. This followed hues and cries from the industrial sector and the attendant steady increase in general price level. There were also accusations levelled against banks to banks to the effect that they offered very high interest rates which had little bearing to market dictates only to now diver the funds to finance the seemingly more lucrative foreign exchange activities.

During the period steps have been taken to allow greater foreign participation in domestic investment. Also foreign can now hold up to 80% equity in large scale agricultural ventures. This large measures of decontrol in over areas of the economy, other specific incentives and debt conversion programme are also expected to enhance the creation of an "enabling environment and to lead to greater participation of foreigners in domestic investments. All these measures has a far reaching effects".

2.9 The Nature and Functions of Banks in Nigeria

Banks play crucial roles in transforming the economy of Nigeria. This they do by mobilizing financial resources from surplus and lending them to the deficit areas. This encourages investment into productive areas of the economy thus promoting growth.

Central Bank of Nigeria (CBN)

The CBN is the highest financial institution in the country. It is the only one with branches in State capitals[28]. It is the government representative in the financial system and act as banker to the government. It was established in 1958 and it became fully operational on the 1st of July, 1959.

The main functions of the CBN can be broadly be categoriesed into three. These are the banking functions, the monetary functions and the development functions.

The Banking Function

The main banking function of the CBN include:

i) Insurance of currency,

ii) Banker and adviser to the Federal Government,

iii) and banker to, and supervisor of commercial, merchant banks and other financial institutions.

These functions are performed by specialised department of the CBN.

Monetary Functions

The CBN has a primary responsibility for formulating monetary policies. The Central Banks' Monetary Policy Proposals, after they have been reviewed and accepted by the Federal Government, are normally incorporated into the budget each year. A few days later after the budget has been released, the Central Bank of Nigeria issue a Monetary Policy Circular, which spells out the revised monetary regulation in detail.

The Development Function

To promote economic development, the CBN has contributed immensely to the creation and development of financial markets to mobilise and channel savings for economic growth.

To aid the development of money market, the CBN introduced instruments such as the Treasury Bills, Treasury Certificates, Certificates of Deposits etc.

The CBN has been directly involved in the creation and development of capital market institutions such as Nigerian Stock Exchange and the Securities and Exchange Commission. The Bank has also played an active role in the promotion of development - oriented banks such as Nigerian Industrial Development Bank (NIDB), Nigerian Agricultural and Cooperative Bank (NACB), Nigerian Bank for Commerce and Industry (NBCI), Urban Development Bank (UDB) etc[27].

Other development function worth mentioning include its roles in national economic policy formulation, maintaining external reserves and exchange control.

Merchant Banks

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Merchant banks operate under the same statutory and CBN regulations as are the commercial banks. They often engage in wholesale banking serving corporate bodies and institutions. In other words, they engage in the same set of activities as the commercial banks except that they cannot engage in retail banking. They constitute a watershed between commercial banks and the development finance institutions.

Merchant banks provide term deposit facilities with varying maturities tailored to the requirement of their clients.

The main services provided by merchant banks are made up of two broad categories.

1. Banking:

Acceptance credits, documentary credits, short and medium term loans and advances, certificates of deposits, equipment leasing, project finance, foreign credit and loan syndication.

2. Corporate Finance:

That is financial advice on company securities floatation, private placement, stock exchange quotation, mergers and acquiescence, capital reconstruction, trusteeship investment, advisory services, portfolio management, issuing of government bonds and loan stocks, issuing of equities, preferences and debenture stocks.

As a hybrid between commercial banking and development banking, merchant banks compete with commercial banks for bank deposits, commercial bills and other trade bills on the other hand, and with development finance banks for term loan and other investment banking services on the other. However, unlike the development finance institutions which rely largely on equity funds and shareholders loans, and unlike commercial banks which enjoy virtually cost free deposit base, merchant banks in Nigeria buy virtually all their funds through payment of interest on fixed term deposits arising from inter bank deposits placement or issues of credits.

Commercial Banks:

These banks occupy the largest part of the market in the banking industry, in terms of geographical spread. They are owned by various combinations of Government, institutional investors and individuals.

Commercial banks perform retail banking functions individuals, governments and corporate organizations. Prominent among products offered by them include:

a) Keeping of accounts of general public

b) Offering loans and advances

c) Acting as agent to customers

d) Selling Travellers Cheques

e) Safe-keeping of valuables

f) Investments in agricultural/industrial enterprises

g) Providing information to customers

h) Opening letter of credit for customers

i) Facilitating change of currency

j) Facilitating investment information.

2.10 Various Instruments of Deregulation Policy

Deregulation policy aimed at strengthening the resistance of the economy to shocks, improving its resilience and increasing its sensitivity to market forces. Specifically, deregulation of financial system is aimed at strengthening and enhancing the performance of the regulatory framework and also improving the reliance of the banking industry on market forces.

In pursuing the above aim, various instruments were outlined by the authority, some of which are discussed below.

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1. Deregulation of Interest Rate:

Interest rates are the rental payment for the use of credit by borrowers and return for parting with liquidity by lenders. The primary role of interest rates is to help in the mobilization of financial resources and to ensure the efficient utilization of such resources in the promotion of economic growth and development. it is crucial in financial intermediation which involves transferring funds from surplus units in an economy to deficit units. In general, interest rates are useful in gauging financial market condition and they are a major toll in monetary policy.

In the pre-SAP/deregulation policy, the level and structure of interest rates were administratively determined by the CBN. Both deposit and lending rates were fixed by the bank based on policy decisions.

Within the general framework of deregulation economic policy embarked upon by the government in 1986 to enhance competition and allocation of resources, the CBN introduced a market-based interest rate policy in 1987, that is, interest rate being one of the allocative instruments in the market economy was deregulated by authority and banks were allowed to charge different interest rates to various customers which should reflect the supply and demand conditions in the market for loanable funds. In the process, resources would be efficiently allocated, as firms with the highest marginal efficiency of capital would receive greater share of any available financial resources.

The deregulation of interest rates made it flexible and gave banks a free hand in determining their deposit and lending rates according to market conditions through negotiations with their customers. However, the minimum rediscount rate (MRR) which is the rate charged by CBN for lending to banks and rate for discounting of bills, is still fixed by the Central Bank in line with changes in overall economic conditions.

In furtherance of the flexible interest rate policy, the CBN introduced an auction-based system for the issue of treasury securities (treasury bills and certificates) in 1989. Under the system, authorized dealers submitted competitive bids through which the issue rate emerged instead of the CBN fixed rate in the past.

The behaviour of interest rates in the period of deregulation shows that the performance has been mixed. It has enhanced and stimulated share rise in the public's investment in financial assets. But the high interest rates have also tended to discourage new investment spending on real assets, particularly in the small and medium scale businesses.

However, interest rate deregulation policy has provided a more conducive environment for financial intermediation.

2. Second-Tier Foreign Exchange Market (SFEM)

Foreign exchange is the means of payments for international transactions. It is made up of convertible currencies that are generally accepted for the settlement of international trade and other external obligation. The foreign exchange market is the medium of interaction between sellers and buyers of foreign exchange in a bid to negotiate a mutually acceptable price for the settlement of international transactions. The objectives of the market include the provision of an avenue for the exchange of national currencies into those that are acceptable for international transactions and the emergence of an effective mechanism for exchange rate determination and allocation of foreign exchange. The major participants in the foreign exchange market were authorised dealers, the public sector, including the CBN, the private sector, especially the industry sector and correspondent bank abroad. Authorised dealers were banks and other entities granted license or permitted to deal in foreign exchange.

Prior to deregulation policy, adhoc measures were used to determine the exchange rate and economic objectives played a major role in determining Naira exchange rate. In between 1960 and 1973, Nigerian currency was pegged to the pound sterling on 1:1 ratio and was later devalued by 10%, the policy was changed in 1981 to gradual depreciation against dollar. The major shortcoming of this exchange control system was its inability to achieve internal balance in the currency under the system was a major obstacle that made the achievement of internal balance difficult, because of this, the system was discharged in 1986 in order to evolve an exchange rate mechanism that would be more responsive to prevailing economic conditions.

The Second-tier Foreign Exchange Market (SFEM) came into being on September 26, 1986, when the determination of the Naira exchange rate was made to reflect market forces, and exchange rate became an active instrument of economic, management and the rate derived in the market served as the means for the allocation of foreign as opposed to the foreign system where it was administratively determined.

The objective of SFEM is to evolve a realistic market determined exchange rate for the naira so as to reduce demand for foreign exchange to available supply and to reduce the pressure on the balance of payments. Such a realistic exchange rate is expected to eliminate the distortions in all the major sectors of the economy, reduce imports, stimulate exports, encourage efficient import substitution, encourage capital inflow and growth. The SFEM operational framework was first based on dual exchange rate system which involves two exchange rates, the first-tier rate which include debt service payment, expenses of embassies and the second- tier rate which was determined by auction at the SFEM.

In July 1987, Unified Exchange Rate System was introduced where the first and second-tier markets were merged into an enlarged Foreign Exchange Market (FEM) and all transactions were subjected to market forces. The merger increased demand pressures and contributed to the persistent depreciation of the Naira exchange rate between July and November 1987. In 1988, the inter-bank market (where banks were allowed to transact official foreign exchange between themselves) was separated from the official market and an autonomous market for privately sourced exchange emerged with its independent rates. The autonomy market was highly destablising as its rate depreciated continuously. This result in its subsequent merger with the FEM to form the Inter-bank Foreign Exchange Market (IFEM) in January 1989.

The official exchange rate in this market again became highly depreciated and the parallel market premium was substantially reduced. To further reduce exchange rate instability, the CBN modified the inter-bank procedures in December 1990 when the DAS was re-introduced in August 1991 when it introduced the modal weighted average method of exchange rate determination.

As a result of the persistent instability in the foreign exchange market, reflected in the wide divergence of the rates between the official and parallel market, the CBN adopted a completely deregulated system of the foreign exchange trading on march 5, 1992. Under the system the CBN buys and sells actively in the market and also supplies in full all requests for foreign exchange made by the authorised dealers.

In concise, SFEM is a market established by law buying and selling of foreign exchange at market determined rates. it is intended to ensure more efficient utilization of the country's scarce foreign exchange resources.

3) Privatization and Commercialization

These terms have been defined in Decree 25 of 1988 in section 14 thus: "Commercialization means the reorganisation of enterprises wholly or partly owned by the Federal Government in which such commercialized enterprises shall operate as profit making commercial ventures and without subventions from the Military Government and "Commercialize" shall be construed accordingly[28].

Privatization means the relinquishment of part or all of the equity and other interests held by the Federal Military Government or its agency in enterprises whether wholly or partly owned by the government and "privatize" shall be construed accordingly[28].

Section 3 of Decree 25 of 1988 supra provides for the establishment and composition of a technical committee which was appointed by the government.

A stipulation aim of the SAP/deregulation policy is to enable the private sector play a more decisive leadership role in the economic development of the country. Private enterprise implies that the ownership of business are placed in the hands of the people or groups are out to maximize profit through providing products and services.

It was in the light of the above facts, the government embarked on privatization and commercialization programme in 1989 as one of the deregulation instrument. The aim of the programme is to improve the performance of the public owned enterprises, improve funding, reduce burden on government.

During the implementation of the programme, banks played a role of financial physicians to the business sector by undertaking indept preliminary studies of the enterprises under consideration and based on their studies, they gave valuable advice both on the present and future of government action.

The name of the Committee was later changed to Bureau of Public Enterprises. It was embarked by the government as an instrument of deregulation policy to minimize sector inefficiency and in effective performances and banks played a vital role during the implementation of the programme.

4) Trade Liberalization

Under the deregulation policy efforts were made to encourage more export against less import by embarking on trade liberalization with the abolition of import and export licensing, and exchange control on current transaction. Also, the requirement that Nigerian residents should surrender their foreign exchange earnings to the Central Bank of Nigeria was abolished,

and all exporters and foreign exchange earners were entitle to 100 percent of their foreign exchange earnings which they must repatriate and keep in their domiciliary accounts which they can draw freely[30].

Various measures were employed in order to obtain full trade liberalization, the measures were employed in order to obtain full trade liberalization, the measures include the following:-

i) Export prohibition were abolished (export of grains and tubers were because of the consequent shortage);

ii) The export licensing requirement was reduced to barest minimum;

iii) Commodity Board was dissolved to encourage primary production of export product;

iv) A new export finance facility, the refinancing and rediscounting facility was introduced by the CBN to assist private exporters through their banks to finance the market facilities;

v) A duty/suspension scheme was introduced in 1987 to enable exporters to import raw materials and intermediate products for use in the manufacture of export products free of import duty and other indirect taxes and charges;

vi) Enactment of the customs and excise tariff consolidation decree in early 1988, in which import duty and excise rates were specified with a longer time horizon for making their custodians.

Financial institutions, commercial banks in particular were being utilized to implement the above measures. This aspect of deregulation instrument has engendered keen competition among banks for deposits as well as bankable export projects. Saving mobilization as a

cardinal functions of the bank was encouraged as all the measures on trade liberalization, especially exchange earning measure, were carried out through various banks. Banks played an important role during deregulation policy via trade liberalization.

5) Abolition of Price Control Board

One of the requirements of deregulation is less emphasis on controlling prices, as the banks believe that price control leads to higher consumption and lower productivity.

prior to deregulation policy, price of certain goods and services were being fixed and/or determined by the government agents and production of some goods and services were subsidized. With the introduction of deregulation policy, price control system was abolished and prices are being determined by the forces of demand and supply in the market and subsidies were being withdrawn as principal requirement of deregulation policy.

The mitigation of price control generated more income in the economy, hence mobilization of funds by banks was highly encouraged during the deregulation policy[31].

2.11 Recent Development in the Financial System

The financial system especially the banking industry witnessed various developments due to the implementation of fiscal and monetary policy during the guided deregulation policy. The following major development are therefore discussed:

i) Creation of Nigerian Deposit Insurance Corporation (NDIC):

Deposit insurance is a financial guarantee instituted as a measure of safety for the banking system to protect depositors. It ensures that the depositors does not lose all his money in the event of a bank failure and promotes the stability of the banking system[32].

The promulgation of Decree No. 22 of 15th June, 1988, saw the advent of the NDIC in Nigeria. It was established to insure bank deposits thereby helping to promote a safe and

sound banking system, protect depositors' interest and further inculcate banking habit among people. It is an autonomous regulatory body with powers among others, to examine the books and affairs of insured banks and other deposit taking financial institutions. Licensed banks are mandated to pay a premium of (1/16%) of their deposit liabilities and depositors' claim is limited to a maximum of ₦50,000 in the event of a bank failure[33].

In January this year (1998), 25 banks, 13 commercial banks and 13 merchant banks were declared distressed and liquidated by the government with effect from Friday 16 January 1988. Between May/June 1988, the NDIC made provision for the payment of deposits to customers of the distressed banks. A maximum of ₦50,000 was paid to customers who have more than ₦50,000 in their various bank accounts with the distressed banks. The NDIC is expected to pay about ₦16 billion to depositors of the distressed banks out of a total of over ₦30 billion deposits all over the country.

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The NDIC is an independent body and acts as an additional regulatory authority in the supervision of banks regarding management practices and suggest ways by which banks can reduce the risk of failure and loss of depositors. Ultimately, the corporation has the power to restrict the activities of banks of banks found not to be in compliance with regulations or to advise the shut down of banks that are deemed to be insolvent.

The NDIC Decree No. 22 of 1988 was amended to give it more power to the corporation to deal with insured banks and to act independent of the CBN on some matters affecting problem banks. The corporation can also take over the management of a bank where such action becomes necessary to protect depositor's interest.

In concise, the NDIC took off effectively in February 1989 with the aim of providing deposit insurance and related service for banks promoting confidence in the banking industry.

ii) Establishment of Bureau-De-Change in 1989:

The establishment of Bureau-De-Change by private entrepreneurs is to serve the needs of people with small demand for foreign exchange. The establishment of it in 1989 was authorised by the Federal Government to eliminate the parallel market or reduce the activities of the market and it was intended to protect Nigerians from buying fake foreign currencies from the swindlers in the parallel market[24].

iii) Withdrawal of Government and Parastatals Deposits:

In May, 19789, the Federal Government directed the withdrawal of all State and Federal Ministries and their parastatals fund from banks and transfer them to the CBN. About ₦8.27 billion was involved. The measure was aimed at reducing excess liquidity in the financial system and removing the availability of cheap funds which banks used to float CBN's credit guidelines.

The withdrawal of the deposits saw a sharp decline in bank deposit liabilities as from June 1989 and a liquidity squeeze in the banking industry. This led to some banks experienced serious liquidity crisis. But with effect from 1st January 1997, the CBN cease to operate all commercial banking business. All accounts of parastatals were taken back to commercial banks.

Eventually, the CBN and NDIC had to provide liquidity for several troubled banks to sustain the inter-bank transactions and forestall the possibility of bank failures.

iv) Minimum Paid-Up Capital:

There have been increase in the minimum paid up capital requirement from ₦50,000 and ₦50,000 for commercial and merchant banks respectively to a uniform level of ₦500 million in 1997[35]. Banks are required to meet this requirement not later than 31st December, 1989. Banks which fail to meet the requirement by that date shall have their licenses revoked while new banks shall comply fully with the new capital requirement before they are licensed.

This is aimed at stabilizing the banking system in view of the greater banks are exposed to due to liberalization, the volume of business of the banks and the gross devaluation of the Naira.

v) Liquidity and Funds Management:

In order to ensure adequate liquidity for the banking system, all banks are directed to maintain a minimum liquidity ratio of 30%, implying a maximum loan to deposit ratio of 70% and minimum cash reserve ratio of 30% total deposit liabilities. This is to ensure adequate liquidity of all banks, guarantee the availability of funds for the withdrawal needs of depositors and guide their funds management.

vi) Introduction of Prudential Guidelines:

The guidelines was issued by CBN in November 1990, and aimed at ensuring a stable, safe and sound banking system, it have two major components namely: the rules or agreed behaviours and the monitoring and scrutiny compliance.

Banks are expected to ensure prudent management of assets, and guarantee the safety of depositors' funds and to adhere strictly to safe and sound banking practices, maintain adequate internal control measures to prevent incidence of fraud, forgeries and other financial malpractice to ensure stability and engender confidence in the system.

vii) Failed Banks (Recovery of Debt) and Financial Malpractice in Banks Decree No. 18 of 1994:

This is to facilitate the prosecution of those who contributed to the failure of banks and to recover the debt owned to the failed banks.

Another major development was the inauguration of a Financial Services Regulatory Coordinating Committee (FRSCC) by the CBN in 1984. The aim is to coordinate and

standardise the regulatory policies of all financial institutions in the system with a view to evolving some corporation among regulatory agencies. The CBN granted forbearance to finance companies operating in Nigeria whereby they were given a maximum of four years to amortize their classified assets portfolio against their current profits. The minimum borrowing of the finance companies had been reviewed downward from ₦100,000.00 to ₦50,000.00 since 1994.

viii) Other Decrees to regulate The Financial System

Three important decrees to further regulate the financial system were promulgated in 1995. These were: Money Laundering Decree No. 3; the Nigerian Investment Promotion Commission Decree No. 16; and the Foreign Exchange (Monitoring and Miscellaneous Provisions) Decree No. 17. The Money Laundering Decree is mainly to prevent drug money and other illegally acquired assets from entering into the financial system in order to forestall the damaging effects of such monetary injection. The Decree limits the maximum amount of cash payments that can be made or accepted to ₦50,000 for an individual and ₦2 million for corporate bodies, respectively. Amount in excess of these limits are to be reported to appropriate authorities.

The Nigerian Investment Promotion Commission, among other things, is charged with the responsibility of encouraging, promoting and coordinating investment activities in Nigeria. it is also compared to initiate the support measures which would enhance the investment climate in Nigeria for both citizens and foreign investors. it is also empowered to register any enterprise in which foreign participation is permitted and to allow foreign enterprises to buy shares of any Nigerian enterprise in any convertible foreign currency.

The Foreign Exchange (Monitoring and Miscellaneous Provisions) Decree established an autonomous foreign exchange market. The Decree empowers the CBN, with the approval of the Finance Minister, to issue guidelines to regulate the procedures for transactions in the

market as well as other matters which may enhance the effective operation for the market. The Decree provides for any convertible foreign exchange to be traded in the market. It also allows an individual, resident in or outside Nigeria, to investment in any security in Nigeria. The Decree provides that any cash transfer in excess of US dollar 10,000 is subject to the approval of the Bank, while the Minister should be furnished with such information on a regular basis.

In 1997, the CBN Decree 24 and BOFI Decree 25 of 1991 were amended. The highlights of the amendments include the withdrawal of the autonomy of the CBN with its supervision placed under the Federal Ministry of Finance. However, the powers of the Bank over the institutions within the financial system were enhanced by the Decree. Institutions which were hitherto outside the control the Bank are now placed under its direct supervision. These include primary mortgage institutions, community banks, people's bank as well as development finance institutions (DFIs).

A new insurance decree was also promulgated which stipulates new capital requirements for insurance companies and also created the Nigerian Insurance Commission as the regulatory organ in the industry.

In January 1998, the government announced the establishment of Abuja Stock Exchange.

A computerized trading system was introduced in Nigerian Stock Exchange to facilitate trading on the floor of the exchange to enhance processing and settlement of transactions and facilitate the internalization of the exchange.

The most recent development in the financial system happen in September ending this year (1988) when the Federal Military Government of General Abdulsalami Abubakar gave the permission to merchant banks operators to engage in commercial banking services if they so wish.

With this development the merchant banks operators have dual role to play for the betterment of their business and the economy.

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CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter states clearly what was done and how it was done in carrying out the study. It also states clearly the population of the study, instruments used, procedure and method used in the course of obtaining data for the research topic under consideration. It also explains the method used in the treatment and analysis of the data with the view of providing the basis for easy understanding of the contents of the subsequent chapter.

Various sources exist for a researcher in conducting research work, these are primary and secondary sources.

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Primary sources are those that the researcher is physically present to observe events as they occur or, through questionnaire administration and other methods such as personal interview, telephone, etc., is able to obtain information about the phenomenon to be studied; while secondary sources involve the use of existing documents, the interpretation and analysis of which gives the researcher answers to his/her problems.

In carrying out this study primary source was used. Personal visits were made to some banks in Zaria and Kaduna for the purpose of the study. Banks such as Central Bank of Nigeria, Kaduna Branch, Habib Bank Ltd. Headquarters Kaduna, First Bank Kaduna, Union Bank of Nigeria Kaduna, Savannah Bank Kaduna, United Bank for Africa PLC, Afribank PLC, Zaria etc. were visited and oral interview was granted to some top management executives, middle level managers, and other staff of the banks. Some gave useful answers. The oral interview necessary to find out particular policies of guided deregulation that affect the financial system.

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The data gathered from the oral interview and other findings were explained theoretically.

Secondary Source

Since guided deregulation is something of a recent development in Nigeria not many textbooks could be found on it. In this regard, extensive use of CBN's publications such as Bullion, statistical bulletin, annual reports and accounts, Economic and Financial Reviews, have been used. It is in these documents that all financial institutions' assets, liabilities, liquidity ratios, etc. are found.

Other secondary sources widely used in the research include work of prominent scholars, authors, journals, magazines and papers presented at seminars, newspaper articles like Business Concord, Business Times etc.

3.2 Nature and Selected Population of Study

A sample is representative of the entire population, while a population refers to the totality of all elements, subjects or members that possess a specified set of one or more common characteristics.

In view of the fact that deregulation does not affect only one part of the country to the exclusion of the other parts, and that it was not possible to make studies of particular banks, the author has taken the entire population (country) for the study, again, since what applies to a particular bank or bank branch may not be applicable to another bank branch, it is necessary that the entire financial system (with particular reference to commercial and merchant banks) should be considered.

3.3 Description of Instruments Used

In order to gather data that would provide information on the operations of banks in a deregulatory economy extensive use of primary and secondary data was used. The research work actually commenced with the collection of relevant textbooks on financial institutions and other materials such as the publications of the CBN, financial papers such as Business Concord, Business Times and other daily newspapers.

The researcher used President Kennedy Library, Kashim Ibrahim Library, Department of Business Administration Library, all of Ahmadu Bello University, Zaria. Other libraries include CBN Kaduna Branch, Habib Bank Nigeria PLC Headquarters.

3.4 Procedure for Data Collection

As earlier indicated, the major source of information for the research work is derived from primary and secondary sources. The research method that has been extensively used is that of documentary research which embraces the use of existing records and published reports. The areas carefully examined in these records and reports include assets and liabilities, loans and advances, liquidity ratios etc. of banks.

In this study two periods have been considered. The pre-SAP period and the deregulatory period.

CHAPTER FOUR

DATA PRESENTATION AND ANALYSIS

4.1 Introduction

The banking policy reforms brought about by the guided deregulation policy is aimed at strengthening and enhancing the performance of the regulatory framework and improving the reliance of the banking industry on market forces.

The programme through its various instruments have been able to pursue these basic objectives and its impact has been felt virtually in all sectors of the economy. Prior to the introduction of the programme, Nigeria banks have been somehow slow in responding to the challenges of the growing economy. However, during deregulation policy, the banking industry has been seen as the fastest growing sector of the economy.

In this chapter, various variables are to be examined to know if the banking industry has experienced better performance during the programme than the pre-deregulation era.

Also the impact of deregulation on the efficiency of banks in Nigeria will be examined.

The data collected for the study is presented and analysed in this chapter.

4.2 Analysis of Data

Commercial and merchant banks, generally, operated under a more favourable macro-economic environment in 1996, compared with the preceding year. Notably, inflationary pressure abated while interest and exchange rates remained stable with the full deregulation of interest rates during the fourth quarter of the year and removal of all mandatory credit allocation mechanisms, the enabling environment for healthy competition in the financial sector was being provided. In addition the problems of distress and malpractice in the system were

more seriously tackled through the implementation of the Failed Banks (Recovery of Debts) and Financial Malpractice Banks Decree No. 3 of 1995. Reflecting lastly the positive impact of these developments, the performance of the banks showed market improvement as their total assets, deposit liabilities, loans and advances as well as capital/reserves increased substantially.

The performance indicators of banks showed marked improved in their operations. Taking 1992 to 1996 for example, the commercial banks in 1996 accounted for 82.7 percent and 88.4 percent of the banking system's total assets and deposits, respectively, compared with 83.5 and 89.2 percent in 1995. They also accounted for 76.5 percent of the total capital/reserve, down from 79.5 percent in 1995.

At ₦536,067.9 million in 1996, total assets/liabilities of all commercial banks rose by ₦72,386.7 million or 15.6 percent, compared with the ₦139,669.3 million or 43.1 percent increase in 1996. The growth rate averaged 36.4 percent annually between 1992 to 1996. (See Table 4.1).

Total assets of merchant banks increased to ₦111,586.2 million from ₦81,801.3 million in 1995. (Also, see Table 4.1).

Therefore when one compares the total assets (aggregate of commercial and merchant banks) for period before guided deregulation e.g. 1985 and period during guided deregulation policy e.g. 1996, one would find out that the year 1985 total aggregate is ₦36,999.0 million while that of 1996 is ₦647,644.1 million.

In the final analysis, one will conclude that there is greater improvement of banks assets in 1996 when compared with 1985.

Loans and advances constitute the most activities for both commercial and merchant banks. The loans and advances are usually of short, medium to long term in nature.

Table 4.1 ***Commercial and Merchant Banks' Assets (₦1 Million)***

Year	COMMERCIAL			MERCHANT		
	Total Loans & Advances	Total Investments	Total Asset	Total loans & Advances	Total Investment	Total Assets
1980	₦6,379.1	₦3,114.8	₦16,340.4			₦1,008.2
1981	8,604.8	2,350.2	19,477.5	₦400.2	₦93.3	1,898.7
1982	10,277.0	3,406.9	22,661.8	711.9	95.6	3,302.9
1983	11,100.0	5,730.4	26,701.5	1,405.4	343.3	4,304.9
1984	11,503.4	9,237.3	30,066.7	1,671.8	599.8	4,496.9
1985	12,170.3	10,676.8	31,997.8	1,802.9	1,065.9	5,001.1
1986	15,701.5	5,223.3	39,678.8	2,771.5	1,344.8	8,445.3
1987	17,531.9	8,712.6	49,828.4	4,101.3	520.3	12,280.9
1988	20,044.9	7,565.2	58,027.2	4,419.1	1,915.4	17,103.6
1989	22,221.2	4,606.4	64,874.0	5,987.5	4,017.1	21,786.9
1990	26,083.9	10,067.8	82,957.8	7,588.1	3,837.5	27,402.2
1991	31,762.4	7,453.5	117,511.9	13,787.7	5,800.7	37,945.9
1992	41,576.4	8,459.2	181,736.1	13,000.5	4,152.9	50,542.4
1993	49.251.1	37,334.2	250,600.5	18,764.4	6,348.1	69,976.9
1994	87,854.1	40,721.0	315,541.5	25,500.6	4,414.0	91,801.3
1995	139,404.3	6,589.9	463,671.3	25,500.0	. . . 5,800.6	91,801.3
1996	157,568.8	13,285.6	. 536,057.9	33,516.6	5,904.9	111,586.2

Source: CBN Economic and Financial Reviews (Various Years)

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Commercial banks loans and advances, the major component of the banks' aggregate credit to the economy, totalled ₦157,568.8 million at the end of December 1996, representing an increase of ₦17,343.4 million or 12.4 percent compared with ₦50,460.4 million or 56.2 percent increase in 1995.

In the case of merchant banks the share loan and advances also increased by 19.9% to ₦33,516.6 million compared with increase of 61.4% in 1995 and average growth of 27%.

The increase in the amount of loans and advances as given in Table 4.1 is due to increase in the number of people making services due to awareness created by the deregulation policy, which enhanced the deposit mobilization of banks. The banks maintained a steady growth in its loans and advances over the years, rising from ₦13,973.2 million in 1985 to ₦191.085.4 in 1996.

Mobilization of deposit liabilities of both commercial and merchant banks was enhanced during the implementation of deregulation policy in Nigeria. Table 4.2 shows commercial and merchant banks liabilities from 1980 to 1996. (Pre- and post-deregulation periods).

Deposits constitute the primary sources of funding of the banks' assets portfolio. From the table, one can see that all the banks have generally undergone a phenomenal growth in their deposits.

Table 4.2 Commercial and Merchant Banks' Liabilities 1980-1996 Deposits (₦1 Million)

Year	COMMERCIAL				MERCHANT			
	Demand	Time	Savings	Total	Demand	Time	Savings	Total
1980	4845.9	3573.7	1589.5	10009.1	66.5	2196	-	286.1
1981	4880.9	3816.8	1979.2	10676.9	122.4	328.0	-	450.4
1982	5180.7	. . 4517.0	2321.2	12018.9	272.3	691.3	-	963.6
1983	5855.6	5203.6	2876.3	13251.9	484.7	793.7	-	1278.4
1984	6343.5	6030.0	3361.3	14908.4	511.0	793.7	-	1481.6
1985	7064.2	6851.0	3699.9	16776.1	530.5	970.6	-	1848.7
1986	6649.8	7217.6	4270.2	17771.0	601.9	1318.2	-	2341.6
1987	7998.0	. 9682.0	5206.7	20422.3	560.2	1738.7	-	3383.0
1988	10667.9	11274.5	7122.7	29065.1	834.8	2822.8	-	4817.6
1989	10188.0	7739.1	9237.8	27164.9	1294.4	3982.8	-	3799.6
1990	15588.8	10175.0	13013.5	38777.3	2363.4	3946.2	-	6309.9
1991	22049.0	10964.4	19395.3	52408.7	2022.2	5007.0	-	7029.2
1992	33639.7	16202.0	25231.8	76073.5	3302.9	8342.5	-	11645.4
1993	51511.5	31005.2	37078.4	119595.1	5668.3	13548.3	-	19216.6
1994	66271.4	26216.9	49910.8	147006.6	9048.8	11589.5	-	20638.3
1995	81665.5	30641.2	62686.6	174993.3	6339.9	11101.1	-	17601.0
1996							-	

Source: CBN Statistical Bulletin, Vol. 2, December 1995.

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Table 4.2 presents the structure of liabilities of both commercial and merchant banks. It depicts the increase in both banks deposits, there was decrease in the deposits in 1989 from ₦29,065.100 in 1988 to ₦27,164.900 in 1989 for commercial banks. Merchant bank deposit liabilities dropped from ₦4817.6 million in 1988 to ₦3799.6 in 1989. It later went up after 1989.

This decrease was due to interest rate war among banks. This led to designing of new products by some banks to entice customers.

In the final analysis, it shows that there was a substantial increase of deposit liabilities during deregulation period than period before it. The increase or growth could be explained by the competitiveness of the banking industry brought about deregulation and liberalization of bank licensed by the government.

Table 4.3 shows that commercial banks have complied fully with the policy guideline with respect to the maturity structure of its loans and advances. The guideline stipulated that the share of their short-term credit (maturing within 12 months) should not exceed 20 percent.

The table also indicates that there was preference for short-term credit over long-term credit. This reflect the riskiness of long-term loans and the easy gains associated with short-term loans.

Table 4.3 **Maturity Structure of Commercial Banks' Loans and Advances (Percentage)**

Year	On Call	Within 6 months	Between 12 months	Between 1-3 months	Between 3-5 months	After 5 years	Total
1980	52.6	13.0	11.8	10.8	6.6	4.9	100.0
1981	53.0	11.0	12.9	8.9	7.9	6.	100.0
1982	52.1	15.6	10.0	8.7	7.7	5.9	100.0
1983	50.0	20.0	9.9	8.7	9.1	2.2	100.0
1984	50.4	17.4	10.1	8.9	7.3	5.8	100.0
1985	52.5	18.7	10.2	8.2	5.2	4.2	100.0
1986	54.0	15.7	10.5	17.8	6.8	5.2	100.0
1987	52.2	15.1	12.4	9.0	6.2	5.1	100.0
1988	53.6	16.6	12.2	8.0	8.0	4.1	100.0
1989	53.3	14.8	11.7	7.8	5.2	4.2	100.0
1990	48.1	18.6	11.9	11.9	5.0	5.2	100.0
1991	51.3	19.7	11.7	7.5	5.4	5.6	100.0
1992	53.8	20.2	12.2	7.8	6.0	5.9	100.0
1993	54.2	21.7	12.3	7.9	6.0	6.1	100.0
1994	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
1995	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
1996	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
1997	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

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N.A. = Not Available.

Source: CBN Statistical Bulletin, December 1995.

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Table 4.4 **Maturity Structure of Merchant Banks' Total Loans and Advances (Percentage)**

Year	On Call	Within 6 months	Between 12 months	Between 1-3 months	Between 3-5 months	After 5 years	Total
1980	7.2	8.1	5.0	42.9	22.2	3.9	100.0
1981	6.4	7.6	11.6	45.3	18.9	10.2	100.0
1982	12.4	6.9	21.2	27.2	19.3	12.0	100.0
1983	17.6	7.1	18.1	18.3	22.0	16.9	100.0
1984	21.6	4.9	15.5	21.7	21.9	14.4	100.0
1985	20.0	5.2	14.4	20.8	20.5	19.1	100.0
1986	16.4	5.5	17.9	20.3	18.8	21.1	100.0
1987	17.5	9.1	16.0	21.3	17.8	18.3	100.0
1988	15.9	7.4	15.6	19.9	25.8	15.4	100.0
1989	17.9	12.3	16.9	19.9	19.8	13.2	100.0
1990	1.58	15.4	6.5	17.9	18.3	16.1	100.0
1991	25.4	11.1	13.6	18.1	19.7	12.1	100.0
1992	20.5	15.9	6.8	18.2	19.5	12.8	100.0
1993	24.9	16.2	7.1	18.7	20.0	13.4	100.0
1994	n.a.	n.a.	n.a.	. . n.a.	n.a.	n.a.	n.a.
1995	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
1996	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
1997	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Source: Computed from various issues of CBN Statistical Bulletin.

In table 4.4, the merchant banks complied fully with the policy guidelines with respect to loans and advance maturing within 12 months whose maximum had been fixed at 20 percent in the 1990s.

Liquidity ratio is the ratio of total specified liquid assets to total current liabilities.

The minimum liquidity ratio specified for both the commercial and merchant banks is 30 percent with the proportional minimum shares of Treasury Bills and Treasury Certificates in each bank's liquid assets fixed at 10 percent. Placement with discount houses is counted as part of a bank's liquid assets for the purpose of meeting the statutory liquid ratio, while the only inter-bank placements that were fully secured by eligible instruments rediscountable at the CBN were to count as part of a bank's liquid assets.

Table 4.5 indicates that the liquidity position of merchant banks was seriously threatened in the early 1990s. This was contrary to the situation in commercial banks that were washed with excess liquidity during the same period. The increase in deposit liabilities and bank's reluctance to grant long term. Loans and advances at maximum leading rate which was fixed at 21 percent in 1991, largely contributed to the excess liquidity in commercial banks.

Excess liquidity was pronounced in the commercial banks as their average liquidity ratio exceeded the stipulated minimum by 9 percent as shown in table 4.5. Merchant banks on the average barely maintained the required minimum liquidity ratio of 30 percent. This development was expected as merchant banks sometimes source part of their deposits from commercial banks.

Table 4.5: Liquidity Ratios of Commercial and Merchant Banks (Percent)

Year	Commercial Banks	Merchant Banks
1980	47.6	45.0
1981	38.5	41.8
1982	40.5	49.1
1983	54.7	81.1
1984	65.1	82.2
1985	65.0	93.7
1986	36.4	47.9
1987	46.5	41.9
1988	45.0	34.0
1989	40.3	27.0
1990	44.3	31.2
1991	38.6	30.3
1992	29.1	26.2
1993	42.2	31.8
1994	48.5	50.1
1995	-	-
1st Quarter	40.8	36.4
2nd Quarter	39.4	39.2
3rd Quarter	32.9	30.7
4th Quarter	33.1	30.5

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Source: CBN Statistic Bulletin.

The earning of a bank determines to a large extent its relative efficiency. This is because, the viability, as well to undertake risky investments depends rather crucially on good profit being earned.

Table 4.6 Earnings of Commercial Banks (₦'million)

Year	Gross Earnings	Profit before tax	Profit after tax
1985	2,462,431	411,764	231,541
1986	3,108,942	479,150	338,165
1987	4,215,421	661,856	439,748

Source: 1988/89 Nigeria Banking, Finance and Commerce, Extract from commercial banking industry under SAP. A Project by Gbadeyan Rotimi.

In the above table there is increase in gross earning of commercial banks during the period of deregulation due to available business climate in the financial system.

Table 4.7: Summary of Commercial and Merchant Banks' Activities (₦ million)

AGGREGATE OF COMMERCIAL AND MERCHANT BANKS

Year	Capital and Reserves	Total Assets	Deposit Liabilities	Loans and Advances
1992	11,809.4	232,278.5	87,738.2	54,799.9
1993	10,876.4	341,743.5	143,583.0	75,076.0
1994	9,148.1	393,975.1	166,130.5	107,075.8
1995	13,833.7	555,472.7	208,850.3	168,170.9
1996	17,425.3	647,644.1	255,030.6	191,085.4

Source: CBN Annual Report and Statement of Accounts, December 1996.

Finally, in the analysis of the above table, one would find out that the total assets of both commercial and merchant banks rose from ₦36,999 million in 1985 to ₦647,644.1, ₦647,644. This development is remarkable.

The deposit liabilities of the banks have increased sharply from ₦18,624.8 million in 1985 to ₦255,030.6 million in 1996. Loan and advances was granted to all sectors of the economy most especially the preferred sector (agriculture and manufacturing). As at December 1996, the loans and advances totalled ₦191,085.4 million. The activities of the banks have contributed a lot to the Nigerian economy.

4.3 Financial Regulatory Framework

In order to fully appreciate the significance of deregulation that has been embarked upon in the industry, it would be expedient to review the regulatory framework and performance of the banking industry prior to the adoption of SAP. This was the era when the banking system was characterised by series of regulations which were rightly meant to guarantee the survival of the system itself. It should, however, be noted that many of the banking regulations of this period are still in force today.

Perspective of Banking Regulations:

The Nigerian banking scene before 1986 was characterised by systematic changes designed to promote banking in the country. The changes may be categorised into[3] three phases: namely, the era of laissez-faire banking (1894-1952), era of limited banking regulations (1952-1958) and the regime of intensive regulations (1958-1985)[1]. During the first phase, banking business was monopolised by foreign banks, principally the African Banking Corporation, Barclays Bank and the British and French Bank. Alleged discrimination against Nigerians by these banks led to the establishment of some indigenous banks which unfortunately offered little or no competition to the foreign banks essentially because of their weak capital base and poor managerial capacity. Consequently, all but three of the indigenous banks failed.

The enactment of the Nigerian Banking Ordinance in 1952 introduced some form of regulation into the banking scene. The Ordinance laid down the standard and procedure for the conduct of banking business by prescribing the mandatory minimum capital requirement for banks and introduced regulations to check bank failures. However, all the indigenous banks established in the country during this period also all failed. The bank failures of this era were attributed to the monopolistic structure of the banking industry which allowed the foreign banks to enjoy exclusive patronage from the British time.

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The period 1958-1986, which may be aptly described as the regime of intensive banking regulations, began with the enactment of the CBN Act of 1958 which gave legal backing to the establishment of the CBN. This Act empowered the CBN to promotion and integrate the Nigerian financial system. Thus, the CBN was able to outline regulatory measures to effective stem the tide of bank failures that followed the first banking boom. Consequent upon this new and encouraging climate, more banks sprang up in the country. For instance, between 1959 and 1960, eight new commercial banks were established, bringing the total number of commercial banks to 12 which increased further to 17 by 1962.

Under the 1968 Companies Act, foreign-based banks operating in Nigeria were obliged to be incorporated in the country. During this period also, the government acquired controlling shares in a number of foreign banks including the **"Big Three"** commercial banks, namely, First Bank, Union Bank and the United Bank for Africa. Two other sources of banking regulations were the Banking Act of 1969 and the Exchange Control Act of 1962. The Banking Act of 1969 generally provided for the regulation and control of the monetary and financial system. Specifically, it made privations for the granting of licenses to the banks while imposing restrictions on the activities of licensed banks.

The Exchange Control Act of 1962 was not aimed at banks directly, but since foreign exchange transactions are mostly carried out through the banking system, the existing foreign exchange regulations would necessarily restrict the actions of the banks.

Nature of Banking Regulations

Having outlined the sources of the banking regulations, it is necessary to examine their various forms and how they were applied to SAP. Four categories of banking regulations will be considered - statutory regulations, Central Bank's guidelines, other regulations incidental to performing the functions of the CBN and monitoring enforcement[2].

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a) Statutory Regulations

The main statutory regulations are specifically stated in the banking laws - the Central Bank Act (1958) and the Banking Act (1969) etc. Some of the regulations specify the requirements for the maintenance of reserve funds, disclosure of interest by Directors and other bank officials, keeping books of account, restriction on payment of dividends and other activities of banks. These and other rules are designed to protect all the interest groups in banking development - shareholders, management, workers, customers, as well as the banking system and the economy generally.

Other objectives of the banking regulations are to ensure that banks have honest and dedicated staff, keep books of accounts to enable them render regular returns to the regulatory authorities within the prescribed time limit. It is also designed to give direction to the banks in preparation and publication of profit and loss accounts and balance sheets and the appointment and powers of Auditors - all of which are expected to enhance sound banking practices and enable the banks to carry out major functions of financial intermediation.

b) Central Banking Guidelines

The Central Bank is empowered to make other rules which are to foster monetary stability and a sound financial structure. These extra rules are usually reflected in the regular Central Bank's guidelines to banks. In the period before SAP, the important regulatory instruments were the stipulation of cash reserve requirement and liquidity ratio, the call-up of special deposits and issue of stabilization securities, as well as the direct regulation of interest rates and growth and sectoral distribution of bank credit.

c) Regulations Arising From Some CBN Functions

Apart from regulations arising directly from the statutes or the regular CBN guidelines, other rules emanates from certain functions of the Central Bank. For example, as the bankers' bank, the CBN decides the amount of overdraft it can allow each bank. It has also the opportunity to advise the banks or to hold consultations with them. For example, the Bankers' Committee meetings provides opportunities for interactions with the banks. The Central Bank also uses its supervision of cheque clearing houses to monitor the activities of banks.

d) Monitoring and Enforcement

The CBN monitors the activities of the licensed banks in order to assess their compliance with regulations. One way is the appraisal of their statutory returns to the CBN. This enables the CBN to analyse banks' performance with a view to determining what new strategies to adopt to enhance future performance. Such analysis also help the banks to make recommendations to the government on policies affecting banks. In the process of supervising the affairs of banks, defaulters are detected and are usually penalized.

Appraisal of Banking Regulations

The effects of banking regulations in Nigeria prior to SAP could be described as mixed. While some of the effects were statutory, others could be considered counter-productive. Banking regulations - whether statutorily or discretionally administered by regulatory authorities - had some salutary effects on the banks and their customers. They, no doubt, positively influenced the viability of banks in Nigeria. Between 1951 and 1952 for example, about 17 new indigenous banks were established, but only one survived beyond 1954. The free banking period, especially before the banking ordinance of 1952, no doubt, encouraged the factors which lead to bank failures. Following this ordinance and subsequent banking laws - the CBN Acts and the 1969 Banking Act, banks failures gradually disappeared from the Nigerian scene at that time. This will tend to corroborate the view that the protection of banks has been the Central aim of regulations.

Despite the benefits just highlighted, a number of problems arose from the banking regulations, especially in the period immediately before SAP, and questioned the entire mode of banking regulation. The main approach to banking regulation in the period before SAP involved the use of direct controls. The major areas of default were the cases where the banks had room and incentive to manoeuvre. For example, on the average, most banks defaulted on the ceiling imposed on their credit expansion and the guidelines on the sectoral allocation of their credit. The rapid increase in the number of banks since the 1970s increased the burden of monitoring individual banks and therefore made enforcement of regulations more difficult. Efficiency of the system was reduced as banks were allowed the same proportional expansion in credit irrespective of the level of their efficiency.

Above all, regulations gave too much room to fraudulent corrupt practices within the system.

4.4 Measures of Regulation

Deregulation as it affects the banking industry came with SAP which has assigned a pivotal role to market factors in the pricing and allocation of resources for development. The measures of deregulation so far implemented in the banking system cover such areas as interest rates, licensing of new banks, sectoral allocation of credit, withdrawal of public sector deposits, the use of an auction method in the issuing of treasury securities etc.

To enhance competition and efficiency in saving mobilization and resource allocation, the tight control over interest rates has since 1987 been removed. The removal is to enable banks charge market rates, of interest and also pay competitive rates to economy into many sector/sub-sectors for the purpose of allocation of bank credit which had left the banks with little or no discretion in their credit operations has also been revised to ensure greater flexibility for banks[3]. The number of sectors was first reduced to eight in 1985 to four in 1986 and further to two in 1987 with agriculture and manufacturing rated as high priority sectors, while all other sectors, constitute the second category. It is hoped that the entire classification would in due course be abrogated when the system has acquired a built-in feature that would not unduly discriminate against productive activities.

Furthermore, to enhance competition, minimize oligopolistic practices and restricted entry into the banking industry, the government has continued to license more banks, irrespective of pressures for restraint, provided proprietors of proposed new banks show evidence of ability to operate on professional basis. Consequently, the period of SAP has witnessed an upsurge in the number of new commercial and merchant banks. For instance, between 1986 and 1990, a total

of 46 new commercial and merchant banks opened for business, and about 25 others had been granted licenses but did not start at that time.

The need to protect the system from adverse effect of the lenient policy of licensing new banks necessitated the raising of the minimum paid-up capital of commercial and merchant banks to ₦500,000.

The period of deregulation has also witnessed a number of strategic institutional changes in the banking system in Nigeria designed to prepare the industry of further deregulation. Among these was the take-off of NDIC charged with the responsibility of insuring bank deposits against bank failure and also ensuring safe and sound banking practices through effective monitoring and supervision of banks, in collaboration with the CBN. Recently, NDIC/CBN decreed 26 banks distressed.

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To remove the easy access that banks had to funds and encourage innovation and competition in the industry, public sector deposits were withdrawn from the system but in January 1997 it was reversed.

Another notable action was the introduction of treasury securities whose principal objectives are the promotion of greater reliance on market forces in the determination of yields on government debt instruments through market determined interest rates and efficient management of public debt.

The process of guided deregulation outlined above is expected to ultimately culminate in the adoption of the indirect techniques of monetary management which use market-oriented instruments of the monetary and credit control. These would involve the use of cash reserve/liquidity ratio requirements, and open market operations instead of credit ceilings to target the desirable level of money supply and credit that would guarantee stable, non-

inflationary economic growth. With a view to targeting broad money, the CBN in its 1991 monetary and policy guidelines redefined the cash reserve requirement on the basis of all deposit liabilities of the banks. The issue of stabilization securities for mopping excess liquidity in the system has assumed some significance and it is envisaged that more market-based CBN securities would emerge in the future.

4.5 Performance of the Banking System in a Deregulated Economy

The role of financial intermediation means that financial institutions, of which the banking system occupies a central position, mobilize financial resources from the surplus units and channel them towards the deficit units to those areas of the economy where they are needed for investments.

In fulfilling this important function of financial intermediation therefore, banks perform certain basic functions within the economy. Banks solicit for accept deposit which are payable at the depositor's instance. The primary responsibility of banks towards the depositors in this regard is that of providing safe custody for such deposits and ensure that the depositor has access to such money when the need arises. Using the deposits mobilized as their stock in trade, banks create money in the economy through granting of loans and advances, at a price to be repaid along with the principal loan. Credit extension (of various forms) is the singular most important source of income for banks.

Banks also provide system for making payment to settle both business and personal transactions, and international financial obligations on behalf of their customers.

Banks' contribution significantly to real development as a result of the role they play in the saving/investment process through the stimulation of savings, the financialization of saving

and their ability to ensure the most efficient transformation of these saving into real capital. Hence the banks form ready tools in the hands of government as vehicle for monetary policy implementation. The way in which banks perform these functions may well determine the degree of success of the development efforts, particularly if they make conscientious effort to mobilize reservoirs of idle funds for allocation to entrepreneurs for investment in projects with the highest rates of social return.

In performing their various functions, banks are expected to ensure prudent management of assets, and guarantee the safety of depositors' funds.

They are expected to adhere strictly to safe and sound banking practices, maintain adequate internal control measures to prevent incidence of fraud, forgeries and other financial malpractice to ensure stability and engender public confidence in the system. Herein lies the concern of the monetary authorities and hence the need for prudential regulation by the regulatory authorities.

The regulation and deregulation of banking activities have great impact on banking activities.

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4.6 Impact of Guided Deregulation Policy on the Financial System

The full impact of deregulation on the financial system can hardly be sufficiently evaluated since most of the expected effects can only be fully apparent in the medium to long term. Besides, the financial system is still subject to some fundamental direct controls which will likely obscure for sometime the effects of the reforms already undertaken. In the last eleven years, some positive and negative developments have been observed in the system which may be directly or indirectly attributed to the deregulation undertaken so far.

4.6.1 Positive Effects

1. Growth in Number of Banks

The period of deregulation has witnessed an increase in the number of banks in the country. In 1986, there were 29 commercial banks and 12 merchant banks with 1367 and 27 branches respectively. As at December 1996, the number of commercial banks and merchant banks and their branches rose to 64 and 2,402, and 51 and 147 respectively[4]. See table 4.8.

With these development, there is keener competition in the industry, through the emergence of new financial products in the money market.

Table 4.8 Number of Commercial and Merchant Banks Branches in Nigeria

Year	Commercial Banks' Number	Branch	Merchant Banks' Number	Branch
1970	14	273	1	-
1971	16	318	1	-
1972	16	367	1	-
1973	16	386	2	-
1974	17	403	3	-
1975	17	436	5	-
1976	18	463	5	-
1977	19	487	5	1
1978	19	609	5	7
1979	20	666	6	7
1980	20	733	6	12
1981	20	682	6	15
1982	22	984	8	19
1983	25	1101	10	24
1984	24	1242	11	25
1985	28	1290	12	26
1986	29	1360	12	27
1987	34	1476	16	33
1988	42	1659	24	46
1989	47	1849	34	56
1990	58	1934	49	74
1991	65	2018	54	84
1992	65	2269	54	116
1993	66	2252	53	122
1994	65	2397	52	142
1995	64	2362	51	142
1996	64	22402	51	147
1997	n.a.	n.a.	n.a.	n.a.
	n.a. = Not Available			

Source: CBN Statistical Bulletin (Various issues

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2) Competition

The deregulation of the banking industry has ushered a new wave of competition among banks for customers and innovative services. A number of banks are positioning and re-positioning themselves within the industry in direct response to competitive forces.

The deregulation of interest rates in 1986, has engendered very keen competition in the banking system, resulting in the adoption of new strategies by banks to attract deposits and encourage savings. As a result, total financial savings have risen from ₦11.5 billion in 1986 to over ₦50 billion at the end of 1997.

3) The Promotion of Safe and Sound Banking Operation

The only way banks can effectively perform their rightful roles in any economy is by operating on safe and sound basis. Safe and sound banking practices assist the banking industry to remain healthy. As a result, many banks are constantly positioning and repositioning themselves in order to be relevant in the competitive banking environment during deregulation policy[5].

4) Use of Technology

The intense competition in the banking industry during deregulation policy has made computerization imperative. Banks have achieved varying degrees of computerization with equally varying result on the quality of customer service delivery. They succeeded in cutting waiting time per customer and there is still considerable room for improvement in customer service delivery through the use of computer technology[6].

In general, the policy of deregulation has made banks to be more creative and innovative in discharging their duties. This resulted in introduction of many products and catchy phrases to win the patronage and confidence of the general public.

4.6.2 Negative Effects

In spite of the improvements highlighted above, the banking sector is still beset with a number of problems although these have not been due solely to but probably accentuated by the process of deregulation. Prominent among these are poor management, increase in fraudulent practices, inadequate infrastructure and scarcity of professional staff. The problem of dearth of managerial staff has manifested in frequent turnover of bank executives, frauds, forgeries, litigations, weak internal controls and contravention of statutory banking regulations[7]. Large scale frauds in the system also derived from the predominance of banking documents most of which could easily be forged.

The expectation that the increase in the number of banks would result in a significant improvement in the quality of bank services has unfortunately not materialised. Rather, the general impression appears to be that, even though the so-called era of "arm-chair" banking has gone, the quality of banking service in terms of the promptness of the services and courteousness to customers has not improved appreciably.

The introduction of prudential guidelines in November 1990 by the CBN has affected the ability of banks to generate enough income from their credit portfolios. This has been due to the build-up of non-performing assets. These guidelines have also affected the asset quality and capital adequacy of banks. As a result, the ability of banks to grant credit has been seriously eroded and this has far reaching consequences on long-term investments in the economy.

Similarly, the weak capital base has made it increasingly difficult for banks to meet their obligations to clients.

Consequently, some of them have been declared distressed, see table 4.9.

A number of indicators have developed for measuring the state of distress in a financial institution. Most of them are variants of CAMEL rating. CAMEL is an acronym for capital adequacy, asset quality, management, earning and liquidity. A financial institution is said to be distressed where valuation by the supervisory authorities depicts the institution as deficient in the following performance criteria:

a) Gross under capitalization in relation to level of operation.

b) High level of classified loans and advances.

c) Illiquidity reflected in the inability to meet customers' cash withdrawals.

d) Low earning resulting from huge operational costs.

e) Weak management reflected in poor credit quality, inadequate internal controls, high rate of fraud and forgeries and

f) Inability to meet the paid-up capital[8].

For the non-bank financial institutions e.g. insurance companies, distress is indicated when they fail to send statutory returns on a timely or regular basis.

Table 4.9. Distressed Banks - Commercial Banks

1. Allied Bank Nigeria PLC
2. Amicable Bank of Nigeria Ltd.
3. Commerce Bank Ltd.
4. Commercial Trust Bank Ltd.
5. Cooperative and Commerce Bank Ltd.

6. Credit Bank Ltd.

7. Highland Bank of Nigeria PLC.

8. Lobi Bank of Nigeria Ltd.

9. Mercantile Bank (Nigeria) PLC.

10. North-South Bank Nigeria PLC.

11. Pan-African Bank Ltd.

12. Pinnacle Commercial Bank Ltd.

13. Progress Bank of Nigeria PLC.

Merchant Banks:

1. Abacus Merchant Bank Ltd.

2. ABC Merchant Bank Ltd.

3. Century Merchant Bank Ltd.

4. Continental Merchant Bank Ltd.

5. Crown Merchant Bank Ltd.

6. Great Merchant Bank Ltd.

7. Group Merchant Bank Ltd.

8. ICON Ltd. (Merchant Bankers)

9. Merchant Bank of Africa ltd.

10. Nigeria Merchant Bank PLC.

11. Prime Merchant Bank Ltd.

12. Royal Merchant Bank Ltd.

13. Victory Merchant Bank Ltd.

SOURCE: New Nigerian Newspaper, Monday, January 26th, 1998.

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4.7 Prospect and Challenges of Deregulation Policy on Nigerian Financial System

It was clear that banking regulations during the early evolution of the banking industry in Nigeria serve some useful purpose, especially in ensuring the viability and stability of the industry. Furthermore, excessive regulations encouraged the banks to adopt various methods to circumvent the direct credit controls by window-dressing statutory returns to the monetary authorities, practices which severally lowered the impact of the banking system while taxing the resources and efforts of the Central Bank in trying to monitor compliance with the various regulations. Perhaps, the most serious shortcoming of the banking industry under the regulations was the tendency towards the promotion of a sub-optimal pricing and allocation system of financial resources resulting in disincentives to saving and inadequate resources for investment.

On the other, deregulation has encouraged saving mobilization and improved access to bank loans. Deregulation has brought a significant increase in number of banks operating in the country, keener competition, new bank products, increase in loan and advances etc. although there are of course a number of problems which have emerged or accentuated with deregulation. Among these are high cost of lending, poor services rendered to customers, fraudulent practices etc. On the balance, however, there is no gainsaying the fact that the advantages of deregulation have so far out-weighed the negative effect, given the background of the economic problems which led to the adoption of SAP. And as with SAP itself, there is hardly a more viable structural growth of the system and consequently sustaining an orderly growth and development of the Nigerian economy.

Deregulation of the banking system would involve the use of indirect instruments of monetary and credit control which relies on market-based instruments such as cash reserve and liquidity ratio requirements and open market operations to regulate the monetary base and

therefore the banks' money creation capability[9]. Although it has its limitations, the advantages of this system of monetary management are overwhelming. The instruments involved are easy to administer and are flexible. Moreover, they do not interfere with competition among banks, while they encourage greater efficiency in the use of funds.

The use of market-based instruments of monetary and credit control is also incompatible with the existence of insolvent or sick banks. Such banks must improve their performance in order to survive under the new control system. The monetary authorities would still need to make regulations to ensure stability of the system e.g. new financial reporting standards, prudential guidelines etc.

From the foregoing, it is obvious that deregulation of the banking industry would in fact impose more responsibilities on bank executives than hitherto. Banks' executives must continue to be effective and innovative in the way they manage the affairs of their banks if they must stay in business. Besides, bank officials must now see themselves as being jointly responsible for any illegal activities involving their banks. Furthermore, one would expect that, since the effective use of instruments of indirect monetary and credit control would require prompt supply of reliable data from banks, banks' executives must have to ensure that the accounts of their banks are balanced promptly. This would call for a comprehensive computerization programme of banking operations if such statutory returns are to be made as required. Finally, it is necessary to emphasize the importance of a comprehensive training scheme for all cadres of bank staff in different aspects of the knowledge and skills involved in effective banking operations under the regime of deregulation.

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In conclusion, it needs to be restated that the health of an economy depends on its ability to generate growth, ensure price stability, boost employment and enhance equitable distribution of income in the medium to long term. It is against this criterion that the success of Nigeria's experiment with guided economic deregulation must inevitably be assessed. I believed that the firm view that the pace of attaining a self-sustaining growth and stability enhanced in an environment which is devoid of inhibiting bureaucracy and where private initiative and creativity through unfettered and dynamic entrepreneurship is enthroned. Owing to the pivotal role of a viable banking system in the development of the economy, bank executives must see themselves as having a unique opportunity in helping to shape the direction of the Nigerian economy. While it is legitimate for bank executives to want to derive maximum short-run benefits from the system, it should be recognised that it is only when the economy experiences a genuine and lasting transformation that such benefits can be sustained. It is therefore of utmost importance for banks and their executives to regard themselves as part of a whole that is in dire need of tangible progress.

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CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary

This study has been directed towards finding out the impact of guided deregulation policy on the Nigerian financial system with particular reference to the banking sector.

It also examined the changing role of banks and their responses to the challenges brought about by SAP with regards specifically to its deregulatory policies.

The study has been divided into five chapters. Chapter one contains the background of the study. It explains the circumstances that led to the introduction of deregulation. The chapter also explains the objectives and significance of the study. In this vain it recognises that the stability of the financial structure prospect of a country's economy.

Chapter two deals with the literature review. It gives background to the Nigerian economy and the major problems which bedeviled the economy before the advent of SAP. The various regulatory controls which were imposed on the financial system, various instruments of deregulation policy, recent developments in the system, impact, prospects and challenges of the policy were examined.

Chapter three presents the methods used for data collection from various sources. It also gives the description of the various instruments used and areas of coverage.

Chapter four deals with data presentation and analysis of the study. The various data collected and used for the study have been analysed in this chapter.

Chapter five gives a summary of the whole thesis work, made conclusion of the study and made useful recommendations.

5.2 Conclusion

Competitive pressures have been an import-force in shaping the financial system. In an environment where competition is allowed to thrive, industries are bound to evolve more efficiently than otherwise, since the implementation of SAP, much progress has been made in the banking system when compared with the pre-SAP period.

Most of the regulatory controls adopted in Nigeria during the pre-SAP period only served to restrict competition, thereby leading to costly inefficiencies in the provision of financial services.

With guided deregulation policy in force, borrowers can borrow from any bank they feel from borrowing and the banks are seriously competing in order to survive. In terms of efficiency of banks, they have made significant improvement since the onset of deregulation. This is particularly true of their quality of service and management. However, the new products and innovations leave much to be desired as the banks offer seemingly attractive benefits to the customer but in actual sense are not really different from the conventional products previously offered.

Banking in a deregulated environment offers many challenges as it brings about intense competition, demands, technical competence and professionalism. Management competence, capital adequacy and quality of personnel are some of the elements that have been introduced into the system which banks are striving to attain. With these goals in view, the economy will be the ultimate beneficiary of such a banking environment.

Banks have witnessed relatively better performance during deregulation policy.

Finally, it should be noted that deregulation does not mean complete absence of regulation but to deregulate when appropriate and regulate when necessary.

5.3 Recommendations

For the Nigerian financial system to achieve and develop to an enviable height the following recommendations should be adhered to:

The monitoring aspect of the implementation of the policies and guidelines introduced by the government to achieve objectives should be improved to enhance strict compliance with the monetary guidelines. Effective monitoring should also ensure that problems that confront the implementation of these guidelines are identified and resolved both at micro and macro levels.

The government should continue to enact Decrees/Acts whenever necessary to control activities of the financial system. The guided deregulatory policy should be continued because of its importance to nation building. Deregulation is like a double-edged sword, when handled rightly, it works wonders.

The government should merge the dual exchange rate together for effectiveness.

Since the minimum paid-up capital have been increased to ₦500 million for commercial and merchant banks, the premium charged by NDIC at 15/16 of one percent of the total deposit liabilities should be reduced.

Banks should adhere strictly to safe and sound banking practices, maintain adequate internal control measures to prevent incidence of fraud, forgeries and other financial malpractice to ensure stability and public confidence in the system. Professional training in modern management, banking and finance, with strong in-built attachment programmes to match theory with practice, has become imperative to develop the manpower which could serve as a reservoir for the formation of groups of experts to practice in the economy.

The financial system especially the banking sector should embark on self-regulatory system. The Chartered Institute of Bankers or the committee forming a disciplinary committee to take action against erring banks even without the intervention of the CBN.

On the issue of banks becoming distressed in the economy, I would recommend that the government should provide financial assistance to troubled banks as a strategy of steering them out of distress. Under the strategy, a problem bank should receive "accommodation bill" a type of interest free loan payable to the corporation only after the bank has fully revived.

Another measure is outright liquidation. Any distress bank that cannot survive after the above measure is taken, outright liquidation of that bank(s) should be made.

Rehabilitating of insolvent banks can also be made through the following ways restoring profitability by restructuring the institution's staff, operations, cost structure, and physical infrastructure and upgrading management in the hope that a new staff will improve decision making, risk management and system control.

The CBN should be fully independent from the Federal Ministry of Finance for effective and efficient functioning.

The non-banking sector of the financial system should be deregulated in order to improve their efficiency in productivity so that they can contribute more to the Nigerian economy.

If all or some of these recommendations are adhered to, the financial system will ensure more effectively the engine of growth and development of the economy.

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