LENDING PRACTICES OF NIGERIAN COMMERCIAL BANKS AND THEIR ROLE *AS* PROVIDERS OF FUND TO BUSINESS ENTERPRISES
(A CASE STUDY OF AIB LIMITED)

BY

AMINU HAMMAYO
MBA/ADMIN/03227/1993-94

SEPTEMBER, 1999

TITLE PAGE

LENDING PRACTICES OF NIGERIAN COMMERCIAL BANKS AND THEIR ROLE AS PROVIDER OF FUNDS TO BUSINESS ENTERPRISES

A CASE STUDY OF AFRICAN INTERNATIONAL BANK LTD

BY

AMINU HAMMAYO
MBA/ADMIN/03227/1993 94

BEING A PROJECT SUBMITTED TO THE DEPARTMENT OF BUSINESS ADMINISTRATION, FACULTY OF ADMINISTRATION IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF THE MASTER DECREE OF BUSINESS ADMINISTRATION (MBA) OF THE AHAMDU BELLO UNIVERSITY, ZARIA NIGERIA

SEPTEMBER, 1999

CERTIFICATION

This project entitled **"LENDING PRACTICES OF NIGERIAN COMMERCIAL BANKS AND THEIR ROLE AS PROVIDERS OF FUNDS TO BUSINESS ENTERPRISES: A CASE STUDY OF AFRICAN INTERNATIONAL BANK LTD" by Aminu Hammayo** meets the regulations governing the award of the degree of Masters of Business Administration (M.B.A.) of Ahmadu Bello University, Zaria and is approved for its contribution to knowledge and literary presentation.

Mal. I.F. Okeji — 3/9/99

Name and Signature of Supervisor — Date

M S Ali — 18/12/2001

Name and Signature of External Examiner (Prof. O.A. Zakraden) — Date

H. O. D. Okai — 8/01

Prof J.U Umoh — 21/12/04

Name and Signature of the Dean Post Graduate School — Date

DECLARATION

Some of the materials used in the project were taken from various books, journals and reports, which have been acknowledged in the reference.

The rest are entirely the work of the writer.

Amma Hammaya
STUDENT

SUPERVISOR

DEDICATION

This work is dedicated to the memory of my late father who set me on track in the pursuit of education and to my mother who has remained my strongest pillar of support.

ACKNOWLEDGEMENT

My gratitude goes to Allah Subhanahu wata'ala who makes everything possible. My appreciation goes to Mallam Ibrahim F. Okeji (MIFO) who painstakingly went through the work and guided me accordingly.

I would also like to say a big thank you to Sani Sulaiman for providing us accommodation at Zaria through out the course work and to the members of our unforgettable group of Abdullahi M. Gumel, Hassan Bello, Haliru Dikko, Abbas Jega and Manir Shehu with whom we burnt the midnight oil.

My appreciation also goes to my wife, Amina and our children Auwal and Fadil for their support and understanding.

ABSTRACT

The main purpose of this work is to examine the sources of bank finance available to business enterprises: and the problems encountered in obtaining them. It will also attempt to look at the problems militating against the perfonnance of banks in the provision of such finance. A case study of African International Bank Limited will be made to buttress the position.

The study looks at the development of commercial banks ,their development in Nigeria and the types of credit facilities they offer. The study also sought probe into commercial lending & effectiveness of lending practices of African internal onal bank Ltd. in carrying out the above. The primary sources of data consist of information derived from the banks officials and interviews with some customers while the secondary sources include the bank's annual reports and review of relevant literature: Annual reports aid statement of accounts of central bank of Nigeria and the Nigerian deposit insurance corporation.

The study reveals a great similarity in the various lending practices and constraints faced by commercial banks. While there has been growth in levels of credit, the maturity distribution, security pattern & repayment methods have been unsuitable. A few large establishments have monopolized credits making it difficult for the vast majority of small-scale industries to secure access. The emphasis on provision of security has also tended to limit credit to that group.

Nigerian commercial banks have been inefficient in mobilization of personal savings thus limiting their credit lending abilities whilst their marketing efforts were found to be largely limited to image enhancing

advertisements rather than innovative product and service development geared toward the attraction of deposits.

The prohibitive cost of borrowing has discouraged same and consequently depressed investment in the productive sectors.

Borrowers were often found to withhold relevant and reliable information thus complicating assessment and escalating the banks risks.

Suggestions proffered from this work include;

- Reorientation and retraining of bank personnel in techniques adapted toward the country's development needs.
- Delegation of processing and accessing authority to bank branches in order to increase their discretion towards customer's credit requests.
- Government should assist banks by establishing rediscounting / refinancing facilities on the commercial banks" loans as a cushion for mismatching of deposits and loans maturities while also providing a policy on technical support for the entrepreneur.
- Formation of cooperative societies will assist in generating credit to members while bodies like manufacturers association of Nigeria should be encouraged to develop banks for assisting their members.
- Low bank density could also be resolved where the central bank promotes the development of community banks and encourage the establishment of bank branches after borrowers must have demonstrated their managerial competence to successfully execute their projects.
- Further study is necessary in the future to assess and examine developments in the banking system; the effects of bank performance and the way forward particularly considering the dynamism of the system.

TABLE OF CONTENTS

Topics		Page
Title		i
Dedication		ii
Declaration		iii
Certification		iv
Acknowledgement		v
Abstract		vi
Table of contents		vii - ix
CHAPTER 1		
1.0	Introduction	1
1.1	Statement of the problem	5
1.2	Objectives of the study	6
1.3	Significance of the study	7
1.4	Limitations of the study	8
1.5	Organization of the study	8
1.6	Definition of terms	10
CHAPTER 2		
2.0	Literature Review	12
2.1	Functions of Commercial Banks	12
2.2	Development of Commercial Banking in Nigeria	16
2.3	Types of Credit Facilities offered by Nigerian Commercial Banks	27
2.3.1	Overdrafts	28

2.3.2 Loans 29

2.3.3 Corporate Finance 30

2.3.3.1 Project Financing 30

2.3.3.2 Loan Syndication 32

2.3.3.3 Equipment Leasing 32

2.3.4 Contingent Facilities 33

2.3.5 International Trade Finance 34

2.3.5.1 Export Financing 35

2.3.5.2 Discounting Drafts and Advances 35

2.3.5.3 Letters of Credit 36

2.4 Financing Criteria 37

2.4.1. Amount Required 37

2.4.2 Purpose of the Facility 38

2.4.3 Repayment Arrangement 38

2.4.4 Tenor 39

2.4.5 Security 39

2.4.6 The Borrower 40

CHAPTER 3

3.0 Research Methodology and Historical Background of Africa International Bank Limited

3.1 Research Methodology 42

3.1.1 The Research Design 42

3.2.1 Data Collection Method 42

3.2 Historical Background of African International Bank 43

CHAPTER ONE

1.0 INTRODUCTION

Business firms bring together economic factors of production in order to produce economic goods and services to satisfy people's needs. To achieve this, such firms must have funds.

All kinds of business activities directly or indirectly involve the acquisition and use of money. Thus any business manager is interested in the subject of finance because among most crucial decisions of any business are those that relate to finance. The raising of funds and using them to create production and generate returns to the suppliers of such funds are called the finance functions of the firm.

Funds adequacy constitutes the lifeblood of any business. Hence, a carefully identified and excellently promoted business can be strangulated by inadequacy of funds to keep it breathing for its growth.

Finding sources to provide an adequate supply of funds is a prime concern to management of both large and small business firms. Most business firms continuously face the

problem of raising funds and rationing it among its various uses. In fact, the success of a firm's operation often depends on how effectively the firm performs its functions of acquisition and distribution of money. The business manager must decide when, where and how to acquire funds to meet the firms investment needs.

A business enterprise can raise funds through its own earnings, equity funds or borrowed funds. The sources of funds can be classified into two broad categories, institutional and non-institutional sources. Institutional sources include those provided by institutions, that act as financial intermediaries such as banks, insurance companies, investment companies, provident funds; pension funds among others.

Non-institutional sources include funds generated from the owners that are the traditional sources of capital; trade credits, accruals and retained earnings among others.

A great number of firms are started as proprietorships owned by one person or as family businesses. Alternatively, there may be a partnership of few individuals who come

together to launch the enterprise. The advantage of the latter is that the individuals can pool their resources where as individual might find that he lacks the maximum amount necessary to get started on sound financial basis.

An individual or family business may start of the basis of the proprietors own accumulated savings earned by him elsewhere which will form the capital base of the business. However, in a much bigger firm, particularly the limited company, capital acquisition is easier through the issue of shares and retained earnings.

KASHIM IBRAHIM LIBRARY

Be that as it may, the funds so generated will then most likely be supplemented by bank facilities. The businessman cannot however borrow as much as he likes at the market rate of interest. The bank will be concerned with the risk of non-repayment due either to the failure of the concern or deliberate default by the borrower. Normally, a maximum amount is fixed based on the estimated reliability of the customer. The level of this maximum will vary according to the bank's knowledge of the customer and of the risks of the venture.

Since this knowledge will generally be limited, the amount of facility offered will tend to correspond roughly with the value of the firms existing assets since these provide the collateral for the facility. The greater the value of these assets, that is the net worth of the firm, the greater the chances of the bank being repaid in the event of bankruptcy.

While bank facilities may be crucial to the entrepreneur, particularly in the early stages of expansions, they will not form a large part of the total capital employed in the enterprise. On the other hand, the practice is for banks to allow borrowing more or less within the range of the fixed maximum allowable. This flexibility means that most bank facilities being sought by businesses are more important as sources of short-term finance; acting as a cushion of liquidity.

However, of greater significance is the generally acknowledged inadequacy of financial resources in the developing countries, more so in Nigeria as characterized by low level of income and by disparities in both distribution of

meager income as well as wide variations in the saving propensity at different levels of income.

IBRAHIM IBRAHIM LIBRARY

Relief is provided by the activities of the financial institutions by mobilizing financial resources from the surplus sectors of the economy and in channeling the funds so mobilized to the deficit sectors of the economy. The role of financial institutions is the development of facilities and financial instruments, which makes the performance of mobilizing and distribution of resources possible.

Evidently, it follows that banks have vital roles to play by making their vast financial resources available for financing and promoting business firms. Commercial banks as integral part of the financial system have played a major role in capital formation and finance of the business sector.

1.1 STATEMENT OF THE PROBLEM

The main purpose of this research work is to examine and elaborate the major sources of bank finance available to business enterprises and the problem encountered in obtaining them. The generality of the people are of the opinion that businesses in Nigeria do not receive adequate

financial assistance from financial institutions especially commercial banks.

This study will therefore analyze and explain how business enterprises in Nigeria have been financed by commercial banks and the problems, which militate against the performance of the banks in the provision of such finance.

1.2 OBJECTIVES OF THE STUDY

The fundamental objectives of the study are enumerated as follows:

(i) The study will discuss in a broader perspective various finance facilities made available by the commercial banks.

(ii) The study will attempt to determine how business enterprise can benefit from such services, what are the requisite conditions to be fulfilled and to what customers' group are the various funding facilities available.

(iii) The study will take an analytical review of how effective and efficient commercial banks have been performing their finance function, identify the problems associated with the administration and

marketing of these services and problems militating against maximum utilization by the business customers.

(iv) Additionally, the study will seek to identify strategies for resolving the problems in (iii) above, bringing into light areas of performance that need improvement and the modalities of doing same.

KASHIM IBRAHIM LIBRARY

1.3 SIGNIFICANCE OF THE STUDY

The study will be of great use to business managers of both private and corporate organizations whose knowledge of the diverse finance functions of commercial banks and how to utilize it is limited. Similarly, it will be of immeasurable value to management; credit and other officers of banks associated with credit administration.

The findings will provide useful information and will be of academic interest to students of banking and finance; accounting; economics; management sciences and other related disciplines and institutions of learning in furtherance of academic pursuit.

The focal point will be to make an analysis of the existing lending practices of Nigerian commercial banks in aggregate.

1.4 LIMITATIONS OF THE STUDY

A number of factors have limited the scope and depth of this research. Some of the limitations include:

1. In obtaining data relating to the aggregate bank performance, only those data reported in the CBN Annual Reports and Economic and Financial Review were readily available.
2. Data made available by African International Bank Limited has mostly been restricted to those extracted from the Annual Reports of the Bank for the period 1991-1997.
3. Wide spread as well as time constraint has not permitted the researcher to visit the entire branches of the bank.
4. The duty of secrecy and confidentiality has limited the provision of specific examples and instances of the bank's customers access to available credit lines.

1.5 ORGANISATION OF STUDY

Financial institutions comprising among others commercial banks are so much relevant in the area of capital formation

because they make funds available for investments and personal uses. African International Bank Limited is one of such institutions that provide loans; overdrafts; advances and other types of facilities to its customers.

The first chapter is an introduction to the study and highlights its importance.

The second chapter deals with review of literature. Most of the reviews are from textbooks; papers; journals etc. This highlights the functions of commercial banks, types of facilities available to banks customers, the development and credit administration in Nigerian commercial banks among other things.

The third chapter contains the research methodology highlighting the research design and data collection methods.

Chapter four will provide the analysis of the data highlighting performance measures and allocation of credit to various categories of borrowers.

The final chapter will consist of summary, conclusion and recommendations.

1.6 DEFINITION OF TERMS:

Business: The organized effort by individuals or a corporate entity to produce goods and services and to reap reward for their effort.

Branch Banking System: This refers to the characteristic of having a few large banks with a wide network of closely linked branches extending through out the country.

Capital Formation: The process of adding to economy's productive capacity.

Collateral: Property made available to the lender by the borrower should the latter default on his contract obligation of payment.

Credit Guidelines: This is the broad outline of regulatory framework and monetary policies established and imposed

26 APR
Ahmadu Bello

by the Central Bank of Nigeria in a specific fiscal year for compliance by banks and other financial institutions.

Demand Deposits: These are funds made available by depositors to banks but are also funds available to the same depositors on demand. It is considered a part of the total money supply.

KASHIM IBRAHIM LIBRARY

Default Risk: The risk that a borrower will not pay interest and principal as agreed on debts.

Financial Intermediation: Process of mobilizing savings from the surplus units and channeling such a way as to bring about a productive utilization of idle funds.

Liquidity Preference: The preference for holding more liquid assets rather than illiquid assets.

Loans Maturity: The date on which a debt obligation becomes due.

476968

CHAPTER 2

2.0 LITERATURE REVIEW

We shall in this chapter enquire into the important aspect of commercial banks lending taking a look at the wide range of services offered. An understanding of the various types of lending facilities of these institutions is necessary to the extent that one will be able to say whether or not they have been efficient in terms of the functions defined.

As a prelude to this; the functions of commercial banks as well as their development in Nigeria will be highlighted. In the end, a study of the background of African International Bank will be presented.

The following classifications will be used in the course of the review.

2.1 FUNCTIONS OF COMMERCIAL BANKS

Commercial Banks could be described as financial institutions licensed to undertake retail-banking services through a network of branches. They usually operate with a broad deposit base consisting mainly of demand and time

deposits. The activities of these banks are regulated by the Banking Ordinances of 1952 and 1958 and by the Banking Act of 1969.

In line with the Enterprises Promotion Act of 1977, the Federal Government acquired majority (60%) equity holding in all erstwhile expatriate commercial banks in Nigeria.

Commercial banks perform a number of functions, which are enumerated and discussed thus:

(i) **Banking Services:** Commercial Banks operate three types of transactional accounts namely: current, savings and time deposit accounts for their personal or corporate customers. These accounts give rise to a variety of banking relationship including lending, payment, transfer of funds etc. Banks provide funds through loans and advances; overdrafts and other forms of credit for production and consumption needs. The banks provide a system that effects the settlement of their customer's financial transactions with third parties. The banks clearing system provides an efficient avenue for clearing customers debt obligations

with third parties without resort to the movement of physical cash.

(ii) **Economic Functions:** Banks are expected to conform to avowed national objectives and identify fully with the aspiration of the Nigerian nation by participating in the financing of economic programmes of national priority. The sectoral allocation of credit enables banks to grant more credit to the high priority sectors of the national economy. They also assist in the formulation of monetary policy and serve as channels through which those policies are implemented.

In addition; commercial banks are expected to actively facilitate the transformation of the rural environment by promoting the rapid expansion of banking facilities and services in rural communities thereby encouraging banking habits among rural dwellers.

Most importantly, commercial banks are expected to serve as vehicles for the creation of credit in the form of loans and advances for small-scale farmers and entrepreneurs.

(iii) **Business Advisory Services:** This kind of service is to assist the corporate clients of commercial banks in developing viable business projects by providing advice in many areas of business operations. These areas include capital management and methods of keeping property business accounts for new enterprises.

KASHIM IBRAHIM LIBRARY

(iv) **Insurance Services:** Some commercial banks apart from managing their own insurance through subsidiaries established for such purpose, also offer professional advice to their corporate clients on insurance matters particularly in the area of international trade.

(v) **Foreign Exchange Functions:** As Authorized Dealers commercial banks provide a range of foreign exchange services including providing information and advice on current foreign exchange regulation and procedures including documentation to facilitate foreign travel through the provision of travelers cheques and other money transmission and International trade settlement instruments such as letter of credit and Bills for collection.

(vi) **Agency Functions:** A number of circumstances occur when banks act as agents for their customers. For example banks establish subsidiary companies to act as executors and trustees of wills. In such capacities, they help to administer their deceased clients estates including businesses.

(vii) **Stock Broking Services:** Some commercial banks have set up subsidiary companies to act as Registrars to companies as well as their own institutions. As dealing members of the Nigeria Stock Exchange, banks sponsor companies seeking quotations on the stock exchange, buy and sell securities on behalf of their clients and help to market quoted securities in the capital market.

2.2 DEVELOPMENT OF COMMERCIAL BANKING IN NIGERIA

The origin of the Nigerian Banking System dates back to the colonial period. The activities of the extraterritorial merchants in the former West African colonies and the establishment of settled territorial governments created the need for locally based financial institutions. For many years, cash payments had been replacing the old barter

system and the British Silver Currency was increasingly used in trading transactions. There was therefore the need for an institution that would take over the importation of those coins, distribute them and absorb any surplus.

In 1891, the Chairman of the Elder Dempster and Company, the shipping firm that ran the regular steamship service between Liverpool and the West African Coast approached the African Banking Corporation based in South Africa to open a Branch in Lagos. The Branch was opened in January 1892 but within a year, Lagos was hit by Dempster and Company, took it over in March 1893 and ran it as a private bank until December 1893 when a new public company was registered in England under the title of Bank of West Africa with an authorized share capital of Sterling Pound 100,000 of which Sterling Pound 30,000 was paid up. The new bank opened its first branch in Lagos in January 1894.

In 1899, some foreign trading firms in Eastern Nigeria under the leadership of the Royal Niger Company set up a bank of their own called the Bank of Nigeria. For 13 years, this bank competed with the Bank of British West Africa Limited before the latter absorbed it. As a result of this

merger, the Bank of West Africa Limited became the only banking institution in Nigeria, and with the establishment of the West African Currency Board in 1912, it was made the sole agent of the currency Board for the custody and distribution of currency.

In 1916, the colonial bank, which hitherto had operated only in West Indies, opened a Branch in Lagos and within four years had fifteen branches in West Africa. In 1925, it was taken over by Barclays Bank to form together with the Anglo Egyptian Bank and the National Bank of South Africa, the new Barclays Bank Dominion, Colonial and Overseas (DC &O).

Indigenous merchant quite early that the existing banks could not meet their needs and accordingly between 1928 and 1952, 25 indigenous Banks were established. The last of these indigenous Banks established by the local merchant class, to assist them get financial assistance required to promote their trade, was the Industrial Bank in 1930. The establishment of Nigeria Mercantile Bank opened in 1931 followed this but which also went into voluntary liquidation in 1936.

The third indigenous banking venture – the National Bank Ltd, incorporated in 1931 has existed till the early nineties when it became distressed. The establishment of African Continental Bank only to become distressed similarly followed it.

KASHIM IBRAHIM LIBRARY

It is quite evident that the founders of these early indigenous banks were inexperienced in banking, accounting or management. The banks themselves had poor capital base. The failure of many of these banks between 1945 and 1952 created sufficient anxiety for the colonial Government that finally in 1952, Mr. G. D. Paton was sent down from London to inquire into the operation of the Nigeria Banking System. His report led to the first legislation, the Banking ordinance 1952, aimed at regulating the business of Banking in Nigeria. That ordinance like its successor in 1958 embodied important features for the regulation of the banking industry such as systems of licensing, minimum capitalization; liquidity ratio; maintenance of Reserves and Bank Supervision.

To the indigenous banks that have operated so far without strict control, the package of requirement expected of them under the 1952 ordinance was most unexpected and in their circumstances, unattainable. By the time the provision of the ordinance began to take effect in 1954, 21 of the 25 indigenous banks had collapsed and the expatriate banking sector tightened its grips on the banking industry in Nigeria.

The determination to localize the control of credit and to ensure the safety and soundness of the banking system inspired the establishment of the Central Bank of Nigeria in 1958 wholly owned by the Federal Government, to perform traditional central banking functions and serve as the pivotal national financial institution. Mr. G. D. Paton became the first Governor of the Central Bank of Nigeria. The Central Bank was superimposed on the existing financial institutions to direct the banking industry towards the achievement of defined national objectives.

The establishment of the CBN offered the indigenous banks the opportunity of operating under a set of well-defined body of regulations geared towards their safety and the

protection of depositors. Expatriate banks, on the other hand, were being constantly required to adapt their operations to local needs and seek out and use local investment outlets for their resources. However, these banks were in law merely overseas branches of their metropolitan parent companies. They fulfilled their responsibilities to their Headquarters by operating within the targets set worldwide for all overseas branches. In order to bring the banks within the ambit of the Nigerian law, the companies decree of 1968 was enacted which obliged all companies operating in Nigeria to register as Nigerian companies under the Nigerian company law.

In order to provide banking to a wider sector of the population and to provide banking facilities to the rural areas, many of the new states created in 1967 established their own banks. The consideration inspired the creation of the New Nigeria Bank Limited, the Pan Africa Bank Limited and the Mercantile Bank of Nigeria Limited. They developed along side the existing state owned banks, the National Bank of Nigeria, the African continental Bank and Bank of the North Limited, which was established in 1959. With the exception of the latter, all the others are now classified as

distressed and have been taken over by the Nigeria Deposit Insurance Corporation (NDIC).

With the end of the Civil war in 1970 and the rapid magnetization of oil resources, the revenue of the Federal government grew by leaps and bounds making government a net creditor to the banking system.

KASHIM IBRAHIM LIBRARY

At the same time the Government identified its priorities viz agriculture, small and medium scale industries, housing, rural development etc. These sectors were however remained starved of funds needed and this evidently tended to suggest that the banking system was not responding sufficiently to the development needs of the country.

Accordingly in 1973, the Federal Government announced its decision to intervene more directly in commercial banking activities by acquiring 40% of the equity capital of the three largest expatriate banks: Barclays Bank of Nigeria Limited, Standard Bank of Nigeria Limited and the United Bank for Africa Limited. In his broadcast of the 1973/74 Budget, the Head of the Federal Military Government declared the objective of the Governments participation in

commercial banking as follows: "The aim of this participation is for the Government to get intimately involved in commercial banking activities so as to guide them to operate to the maximum benefit of the economy. This is as much in their interest as it is the interest of the country".

Furthermore, in 1977, following the reclassification of Banking as a schedule II business in the Nigerian Enterprises promotion Decree 77, the Federal Government acquired additional 20% in the said three banks and 60% share holding in the remaining eight foreign banks.

In order to ensure that banks operate in sympathy with the national development aspirations, the Federal Government accepted the recommendation of the Okigbo commission on the financial system to define the objectives of the banking system in the following terms.

a) To facilitate effective management of the national economy.

b) To provide non-inflationary support for the economy.

c) To achieve greater mobilization of saving and it's efficient and effective channeling.

d) To ensure that no viable project is frustrated simply for lack of funds.

e) To insulate the economy as much as possible from the vicissitudes of the international economic sense.

f) To assist in achieving significant transformation of the rural sector.

g) To assist in achieving greater integration and linkages in agriculture, industry and commerce.

KASHIM IBRAHIM LIBRARY

The summary effect of the Federal Government intervention in commercial and merchant banking in 1977 was that virtually all the banks operating in Nigeria then became controlled by either the states or Federal Government. Thus in one fell swoop, the Nigeria banking industry changed hands from private ownership to being essentially a functional extension of the civil service.

However, with the deregulation policy of banks in the seventies and eighties and the introduction of the Structural Adjustment Programme in 1986, with economic deregulation as one of its cardinal objectives; measures introduced into the banking system include over that period:

i. Relaxation in the licensing of new banks;

ii. Introduction of Domiciliary Accounts in Nigeria;

iii. Introduction of Interbank Foreign Exchange Market;

iv. Withdrawal of public sectors fund to the CBN

v. Deregulation of interest rate structure;

vi. Promulgation of the new Central Bank of Nigeria and banking Decrees No. 24 and 25 of 1992;

vii. Privatization of commercial banks in which the Government has share holding.

The general objectives are the great economic efficiency and better resources allocation through less government intervention.

Perhaps the most profound and visible manifestation of banking deregulation in Nigeria was the relaxation in entry controls during the period 1986-90. The period witnessed the phenomenal increase in the number of licensed banks from 43 in 1986 to well over 120 in 1990. The new entrants like their ancestors in the fifties and seventies were mostly traders who perceived the link between their trading activities and ownership of banks.

With maximal overheads and high volume transactions, many of the new banks began to declare huge profits, which in turn attracted new entrants by demonstration effect. This rapid increase in the number of banks has greatly watered down service standards and increased depositor risks. Many of the banks hardly undertake beyond financing trade and round tripping scare foreign exchange resources.

The promulgation of the Central Bank of Nigeria (CBN) Decree No. 24 and the Banks and Other Financial Institutions (BOFI) Decree No. 25 in 1991 was an important milestone in the deregulation of the finance industry and was also the most significant banking legislative development since independence. The two decrees vested vast powers of the Central Bank for the control and supervision of the Banking finance industry.

Prior to the promulgation of the decrees, one of the problems plaguing the Nigeria financial system was the lack of adequate legal framework for effective regulation and supervision of the banking system. The repealed CBN act 1958 and the 1969 Banking Act were not only inadequate but were ridiculed with ambiguities.

The BOFI Decree in particular vests the Central Bank with the powers to deal with any ailing bank and failed bank. Furthermore, with the approval of the president, the Central Bank can assume control and management of a failing bank for nominal value for the purpose of restructuring it or liquidating it. This further enhanced the mechanism for resolving banks in the system thus complementing the provisions of the NDIC Decree No. 22 of 1988.

In the light of the foregoing, a number of banks were affected and have been liquidated thereby bringing more sanity to the industry while the existing ones have remained under scrutiny to date to determine their healthiness.

2.3 AVAILABLE TYPES OF CREDIT FACILITIES OFFERED BY NIGERIAN COMMERCIAL BANKS

One of the traditional areas of activity of the banking industry is that of credit provision to its customers.

Commercial banks offer funding facilities for long-term projects and overdrafts to cope with working capital needs that may arise therein.

Their loans and advances are for short medium and long-term borrowers. Their sound financial examinations help to ensure that customers' projects are more viable and profitable. They act as a double check against the like hood of project failure

In a broader sense, credit is based on the confidence in a debtor's ability to make a money payment at some future time. Its existence involves a lender, who extends credit and a borrower, to whom the credit is extended.

The reason for credit is found in the need or desire of individuals and business firms to obtain economic goods ahead of their ability or desire to pay for them.

Credit facilities include the following, which are discussed briefly:

KASHIM IBRAHIM LIBRARY

2.3.1 OVREDRAFT

This is the most widely used type of short-term finance for the augmentation of the working capital needs of businesses. It is a facility to draw cheques without notice, and without funds up to a prearranged limit. It is legally

repayable on demand and generally renewable on annual basis or sometimes less depending on the arrangement, subject to justifiable need for the overdraft; credit worthiness of the borrower and other factors. It is pertinent to note that overdraft is granted subject to a customer operating a current account.

2.3.2 LOAN

A loan is usually granted to assist a customer to meet non-recurring item of expenditure. It is usually granted to finance a specific need such as construction or finance of any asset or something of that nature. A loan is usually paid in agreed installment until its liquidation.

Loans may be short-term, medium term or long term and are repaid within one year, over one year but less than five years and over five years respectively.

Short-term loans are mainly granted to meet working capital requirements of the enterprise, while medium term loan is required to fund hardcore overdrafts in a restructuring of facilities arrangement. Long-term loans are associated with large capital-intensive projects. It is usually used to finance the acquisition fixed assets of longer life span.

2.3.3 CORPORATE FINANCE

Corporate finance refers to all those fund financial activities that are required to put a firm on a sound financial position. It is difficult to state the limit of corporate finance since the array of advice and assistance that can be rendered are many and vary.

The primary objective of corporate finance is the provision of financial assistance as well as ensuring effective management and utilization of funds made available. The following are example of corporate finance available:

2.3.3.1 PROJECT FINANCING

This is also known as project loan. It embraces the various methods that banks often use to finance the construction of new projects or ventures on a basis whereby repayment is anticipated from the revenue stream generated by the project.

In addition to arranging for finance, commercial banks also assist in assessing the intrinsic economics of the project to determine if the project is feasible under project financing

method. The bank will on the basis of such assessment structure the project to achieve a feasible trade off between its acceptable risk exposure and resource commitment against the requirement of the lender for limited financing. Project finance requires a proper understanding, careful supervision and follow up of the project normally backed up by advisory services. The analysis of a project finance loan proposal involves a decision based on the review of a projection or forecast rather than of historical earnings or data.

Some of the common characteristics of project financing situations are:

KASHIM IBRAHIM LIBRARY

a). The financing of a new project or start up operation or major expansion as an independent economic unit.

b). The borrower represents the project itself with the source of repayment being the projects own cash flow.

c). The venture are normally very large, complicated at times by government involvement, and a desire for off balance sheet credit arrangements.

2.3.3.2 LOAN SYNDICATION

Many at time; the size of loan required is too large so much so that one bank may be unable or unwilling to provide the entire requirement.

A consortium of banks through what is called loan syndication may thus provide such a loan. Usually a decision is taken in order to spread the risk between the consortiums.

When large-scale projects are undertaken, borrowing requirement very often invariably exceed lending limits of a single bank. Loan syndication thus provides the required sources of finance.

2.3.3.3 EQUIPMENT LEASING

Leasing is a method of financing which enables a company to rent industrial equipment instead of buying it outright. It is a contract between a lessor (owner) and a lessee (user) for the hire of a specified asset selected from a manufacturer vendor of such asset by the lessees in which the lessee has

possession and the use of the asset on the payment of specified rent over a period of time.

KASHIM IBRAHIM LIBRARY

The most important distinguishing feature of leasing as a source of finance for capital investment is the separation of ownership on one hand and possession and use on the other. Leasing is suitable for large and costly assets such as aircrafts; computers or major plant and equipment.

Under the arrangement, no capital outlay is involved and requires no cash deposit or down payment. The only disbursement required is the fee payable to the bank that undertakes the lease. The thrust of this most flexible form of finance hinges in affording the user access to a capital asset without necessarily owning it.

476968

2.3.4 CONTINGENT FACILITIES

These are non-cash facilities of a contingent nature usually given at the request of the customers to facilitate their operation.

KASHIM IBRAHIM LIBRARY
RECEIVED
26 APR 2005
Ahmadu Bello University

When a contingent facility is granted, the bank assumes prime-liability and if called upon, honours its obligation by

HG

paying up. It must do so irrespective of whether the customer has fund or not. Obviously, the liability may seen to involve no real commitment of fund except the customer to whom the facility is granted fails to honour his side of the agreement. The bank assumes a likely liability as soon as contingent liability is accepted by it. The liability is only relieved if the customer satisfies the requirement under the agreement. The bank normally ensures that the facility is covered in full by cash security or any other security except where the customers' integrity is undoubted for the value of the transaction is called upon to do.

Contingent facilities come in form of bonds and guarantees, which banks give on behalf of customers involved in capital projects. This enables the customer to avoid or post pone an actual outlay of cash.

2.3.5 INTERNATIONAL TRADE FINANCE SERVICES

Bank credit is usually extended to international trade finance in a variety of ways including export financing, discounting drafts and advances and letters of credit.

The primary purpose of international banking is to facilitate international financing and commercial transaction. The following are examples of international trade finance services provided.

2.3.5.1 EXPORT FINANCING

Banks usually assess the requirements of exporters based on peculiarities and design a suitable mode of financing. For instance, pre shipment finance could be made available in the form of procurement finance i.e. purchase of goods for exports, working capital and production.

Production finance is provided or the production of goods with the export market in view. On the other hand post shipment finance bridges possible cash shortage in the period between shipment and receipt of export proceeds. Such funds could be used for stock acquisition to ensure continuity in the export business.

2.3.5.2 DISCOUNTING DRAFT AND ADVANCES

The sale of goods by a Nigerian exporter usually gives rise to a foreign bill. A bill of exchange is drawn and sent to the foreign buyer for acceptance. A time or insurance draft

drawn by a seller on the buyer and accepted by such buyer is called a trade acceptance. Banks usually purchase, at a discount, trade acceptance from the payee thereby financing a company's receivables.

The discounting bill is similar to working an advance upon the security of the bills.

KASHIM IBRAHIM LIBRARY

2.3.5.3 LETTERS OF CREDIT

Letter of credit is a mode of payment in international trade for import and export transactions. The bank undertakes, on behalf of the customer to pay a specified amount, if certain conditions stipulated in its terms are met. This is a letter granting credit to some other person. The issuer of such a letter undertakes therein to answer to the addresses for the obligation of the person who made the request for the letter to be issued.

An exporter who is a beneficiary of a letter of credit can use the reputation of that bank that issued the instrument to obtain payments whilst the goods are in transit. He may also obtain immediate payment for issuance letter of credit by granting a bank in his county to negotiate the shipping documents.

2.4 FINANCING CRITERIA

In order to make sound lending there is no doubt that it is necessary to have a wide experience of business and the ability to judge peoples character and financial acumen accurately. While some people rarely make lending, most others need to adopt a logical approach when considering requests for facilities to ensure that the correct decision is reached. The traditional approach to bank lending suggests that the "CANONS OF LENDING" should be considered before facilities are granted. The cannons are discussed thus:

2.4.1 AMOUNT REQUIRED

It is important to determine fairly accurately how much finance is required. A cash budget and estimate of cash receipts and disbursement during a specific period in the future will be required. For companies and partnership, financial statements must be submitted covering a specific period. This will enable the bank to build up a picture of the business, and in this way the capital resources of the business will be determined. The bank will also evaluate the

adequacy of the amount required. The customer's contribution to the project is very important. The contribution made must be reasonable, as this will determine the level of commitment towards the project. The higher the contribution to the investment the greater will be the determination to succeed and make profits.

2.4.2 PURPOSE OF THE FACILITY

The purpose of borrowing must be definite. What the business intends to use the facility for will determine the type and structure of the loan. Money to be used for inventory purchase will require quick repayment than money required for buying fixed assets. There are some ventures which banks will never agree to finance such as gambling, betting etc.

2.4.3 REPAYMENT ARRANGEMENT

Before agreeing to a facility, it is importance to be satisfied that full repayment is possible within a reasonable period of time. Overdrafts usually granted for trading purposes should be fluctuating and self-liquidating while loans usually granted for capital expenditure and other specific purpose should have a specific repayment

programme agreed at the outset. It is important to ensure that sufficient profits and cash flow can be generated to repay an advance granted for capital expenditure. If the source of repayment is from sale of assets or proceeds of a completed contract, it should be ensured that the income cannot be diverted.

As repayment of every loan and advance is expected from future earnings, a borrowing customer must be able to submit a simple cash budget. Loans and advances can only be repaid from future profits generated from operations as long as the business remains a going concern. Therefore it is necessary to ensure that by granting bank facilities, the company will make more profits.

KASHIM IBRAHIM LIBRARY

2.4.4. TENOR OF THE FACILITY

To secure a bank loan, the request must be properly structured. Ideally long-term loans should be used for fixed assets as well as permanent working capital needs while overdraft and other short-term facilities provide normal working capital to finance inventories and receivables.

2.4.5 SECURITY

To be considered a good security the assets offered should be relatively easy to value; of steady and increasing value; possible for the bank to obtain title and reasonably easy to realize should such action be considered necessary. Such security taken should always be perfected.

Security however, only serves as buffer, something to fall back on if the expected source of repayment should fail. An advance must be granted on the strength of the feasibility of the purpose for which it is required. However, since the best plans may go astray and real loss may be sustained, security is intended to minimize or eliminate such losses. The real security for any advance remains the character of the borrower.

2.4.6. THE BORROWER

The management and business manager seeking loan for their business must be able to pass to the test of reliability, personal integrity, honesty, ability, intelligence, dedication to work; knowledge of the basic operations of the business and experience generally.

The bank would want to know whether or not the business manager has adequate knowledge about the proposed venture. This will enable banker determine whether or not the borrower will use the facility to advantage and repay it within the agreed period.

From the foregoing, it can be seen that a banker has to assess the peculiarities of the business set up and those charged with its management fairly accurately before he can determine the business credit worthiness.

securities for the account of others or the assumption of guarantees and other warranties for others or the effecting of transfer and clearing and such other transactions as the Minister may on the recommendation of Central Bank of Nigeria by order published in the Federal Gazette designed as banking business".

African International Bank Limited was incorporated in August 1979 with its Registered Head office at 13c Murtala Muhammed way Kano. It started operation as Bank of Credit and Commerce International Nigeria Limited, a private limited Banking company in partnership with the Bank of Credit and Commerce Holdings (Luxembourg) S. A. The bank commenced operation in November 1979.

Under a technical arrangement, BCCI Holdings (Luxembourg) provided technical support until March 1991 when the bank began the process divesting the 40% shares of the foreign partners.

Necessary approvals were obtained in July 1991 in the wake of the BCCI crisis; the name was changed to African International Bank Limited and the 40% share holdings

BCCI was divested and sold to Nigerians. The Registered Head office changed to 18 Ibrahim Taiwo Road, Kano.
The Bank was established to perform among other things the following functions like any other bank:

i. Acceptance of savings; current; call and fixed deposits from retail and corporate customers.
ii. Provision of credit facilities to customers and organizations especially the priority sectors of the economy.
iii. Provision of long, medium and short-term loans and overdrafts to various categories of customers.
iv. Provide professional advice on investment opportunities to customers.
v. Undertake transaction of foreign trade on behalf of customers and
vi. Provide finance to corporate bodies by discounting their Bills of Exchange.

African International Bank Limited offers a wide range of specialized services tailored to meet the often diverse and numerous needs of its selected clientele and provide among others the following:

a) **Retails banking services**

This includes maintenance of current; savings and deposit accounts and the facilitation of local remittances.

b). **Corporate Banking Services**

These includes loans and advances; overdrafts; Bonds; Guarantees and Indemnities; Commercial Papers; Bankers Acceptances; Exports; Imports and other specialized credit.

c) **Treasury/Investment Services**

This takes care of funds/deposits placements; funds management; and negotiation of certificates of deposits.

d) **International/Foreign Operations Services**

This deals with import and export letter of credit; documentary collections; foreign currency domiciliary accounts and foreign exchange.

e) **Advisory Services**

This deals with export business promotion and management; portfolio management; project finance;

Investment Advisory Services; corporate finance and so on.

African International Bank Limited currently operates with a network of 50 branches that provides outlets spreading almost across the entire country.

The branches are located at Abuja; Aba; Ohafia; Yola; Nnungudoe; Odekpe; Okija; Onitsha; Azare;Bauchi; Fikayel; Ladi Bida; Maiduguri; Abavo; Efurun; Benin; Enugu; Birniwa; Kaduna; Zaria; Ibrahim Taiwo Road. Kano; Kano City; Kurnan Asabe; Murtala Mohammed Road Kano; Tofa; Yargaya; Illo; Kaiama; Agbowa-Ikosi; Apapa; Braod Street; Ikeja; Ilupeju; Ketu; Marina; Tafawa square; Victoria Island; Ibogun-Igbeda; Oluponna; Ibadan; Ilora; Gidan Galadima; Jos; Pilgani; Port Harcourt; Bakura; Sokoto; Chediya; Gusau and Ngelzarma.

In addition to the full pledged branches; the bank operates cash centers at Ochanja Onitsha; Nortex Kaduna; Kurmi Market Kano; Idumota Lagos; NAFCON Port Harcourt and Ogbomoso Road Abuja. These as well as the branches are connected online real time.

The management of the Bank operates from the Central Office at the AIB PLAZA on Akin Adesola Street Victoria Island while the International Banking Department as well as the Treasury and Investment Banking Department operates from 112 Broad Street Lagos.

KASHIM IBRAHIM LIBRARY

CHAPTER FOUR

4.0 DATA ANALYSIS AND PRESENTATION

The research work seeks to consider commercial banks lending function in aggregate. Most of the data used were generated from the Central Bank of Nigeria Annual Reports and statement of Accounts; the Economic and Financial review as well as the reports of the Nigeria Deposit Insurance Corporation (NDIC).

Specific data were picked from the Annual report of African International Bank Limited and the Second Schedule to illustrate the aggregate performance.

The data analysis reveals a great similarity in the various lending practices of commercial banks as well as in the constraints faced.

In the analysis; consideration was given to those indices that serve as a measure of lending performance of banks.

4.1 PERFORMANCE MEASURES ANALYSIS

4.1.1 AGGREGATE COMMERCIAL BANK CREDIT

Among important indices for analyzing the performance of banks; the volume of aggregate credit over the years will tend to suggest, by its increasing trends, the positive development achieved.

Table 4.1 below presents the aggregate commercial banking system credit to the economy.

(N MILLION)

END OF MONTH/YEAR	COMMERCIAL BANKS CREDIT TO		TOTAL
	GOVT. SECTOR	PRIVATE SECTOR	
DECEMBER 1991	5,883.70	31,763.20	37,646.90
,, 1992	1,470.00	43,436.90	44,906.90
,, 1993	28,457.40	66,384.00	94,841.40
,, 1994	37,885.70	94,761.50	132,647.20
,, 1995	17,365.00	147,971.70	165,336.70

The commercial banking system credit to the private sector exhibited rapid growth over the years. The implication of

this is that the contribution of the banking system towards the financing of private business enterprises has rapidly increased hitting over N165 Billion in 1995 as against N37 Billion in 1991. Looking at the contribution of African International Bank Limited separately, the trend has shown similarities with the industry.

Table 4.2 below gives an insight of the level of growth of the net total and loans and advances of the bank between the year 1991 and 1997 after loan loss provision:

₦Million

YEAR	1991	1992	1993	1994	1995	1996	1997
TOTAL LOANS & ADVANCES	295	549	665	1,125	1,562	1,952	4,205

It is important however in spite of the increasing level of commercial banks credits, to make comparison against the corresponding deposit since commercial banks control over 80% of the resources in the banking system.

Table 4.3 provides the total deposits liabilities of commercial banks between 1991 and 1995.

₦ Million

YEAR	1991	1992	1993	1994	1995
TOTAL DEPOSIT LIABILITIES	52,408	76,073	120,277	142,399	186,374

Source: CBN Annual Report and Statement of Account 31/12/95

The average loan to deposit ratio in percentage were as follows for the years under review;

YEAR	%
1991	62.8%
1992	53.5%
1993	48.4%
1994	60.9%
1995	63.8%

With this in mind, the commercial banks can be said to have performed well particularly when noting the rate of growth between 1993 and 1995.

It is however worth noting that the position of African International Bank Limited in the period 1991 to 1997 has shown significant deviation from the aggregate ratios provided for the commercial banks.

The total deposit liabilities as well as the ratio of loans/advances to deposits for the period is provided for AIB Limited as follows.

₦Million

YEAR	1992	1993	1994	1995	1996	1997
DEPOSIT	2,960	2,903	3,287	4,787	8,180	9,739
RATIO OF LOANS TO DEPOSIT	19%	23%	34%	33%	24%	43%

Source: Annual report of Accounts of AIB Limited for various years.

Kindly note however that there is a significant improvement in the ratio in the year 1997 with the ratio increasing from 24% in the previous year to 43%.

4.1.2 COMMERCIAL BANKS BRANCH NETWORK STRUCTURES

Another index for judging commercial banks performance for their intermediation role and lending function is their branch network structure. This is indicated by how effective they perform their financial intermediation role by channeling resources from savings surplus economic units to saving deficit units.

Table 4.5 below shows the number of commercial banks and their branches between 1992 and 1995.

YEAR	NO OF COMMERCIAL BANKS	NO OF BRANCHES
1992	66	2275
1993	69	2479
1994	65	2404
1995	64	2351

Source CBN Annual Report & Statement of Accounts.

The figure will tend to suggest that there is the need for improvement so as to enhance the potential access of the general public to commercial banking facilities. As at 1995, the average number of persons per bank branch stood at 25,220.

It should however be noted that the decline in the number of branches over the years 1993 - 1995 was as a result of the distress of some commercial banks and their subsequent closure by the Central Bank of Nigeria.

KASHIM IBRAHIM LIBRARY

The African International Bank Limited has maintained its number of branches over the last ten years up to 1997 even though it has plans to increase its branch network.

The significance of the figures is to illustrate the banks density ratio. This development influences the level and efficiency of banks intermediation role.

Commercial banks have the capacity of extending their activities and branches centers even though with a bias towards economically active centers. They tend to

HG
1412.N6

KASHIM IBRAHIM LIBRARY

concentrate mainly in large urban centers where industries and commercial activities are intense.

The fact however remains that there is a large volume of untapped financial resources in the inter-land rural areas with over 70% of the countries population which still remains largely sterilized because they have not been mobilized and channeled adequately.

It is believed that with the establishment of effective and adequate branches network to the rural community, there will be increase in the deposit base of banks as well as the tendency for induced lending activities.

The loans and advances granted to rural borrowers have shown a marked increase. Between 1986 and 1990 the increase amounted to over 500%. In 1994, loans to rural borrowers stood at N1, 602.2 million constituting 33% of the rural deposit. This is 17% short of the prescribed minimum target by the Central Bank of 50%. However, in 1995, loans to rural borrowers amounted to N8, 659.3 million representing 98.3% deposit mobilized by rural bank branches. There is however a lot more resources that could

still be tapped if the branches network could be expanded so that numerous agricultural loans and small industrial projects will be adequately funded.

4.1.3 LOANS AND ADVANCES TO SMALL SCALE ENTERPRISES

The loans and advances to small scale enterprises expressed as a percentage of total loans and advances in comparison to the minimum targets set by the Central Bank of Nigeria indicated low performance and compliance from the early eighties up to 1986 and 87.

The negative deviation from the target in 1986 was 6% while in 1987 it was 2.3%.

A higher level of performance was however achieved as positive deviation from the target in 1988, and 90 stood at 5%, 7.3% and 9% respectively.

The trend of meeting the target has continued even though at a lower range compared to the late eighties.

In 1994 for example, reported bank loans to Small Scale Industries were in line with policy targets. At N29, 552

million, loans to small-scale enterprises constituted 23.6% of total loans granted against the target minimum of 20%. In 1995 it amounted to N32, 374.5 million representing 22.4% of the total as against the policy target of 20%. Banks have therefore of late barely kept above the minimum target presented.

Lending activities should be intensified for financing small-scale industries and cottage industries in the rural areas, which are the bedrock for large industrial projects and consequent economic development.

4.1.4 MATURITY PATTERN OF LOANS AND ADVANCES

The maturity patterns of the loans and advances of banks hardly altered over the years. Although banks have been more active in providing finance over the years as shown by increasing aggregate loans granted, the maturity structure has remained virtually unaltered. They have remained preponderantly short term of the orthodox self-liquidating type.

Between 1987 and 1990, the proportion of banks aggregate advances maturing within one year ranged between 78 and 79 percent. The remaining 22% or so falls due for payment

after one year. The trend has remained into the nineties even though fluctuating over the years.

The situation in African International Bank Limited tends to portray the same picture even though in varying proportions.

Table 4.6 below shows the analysis of loans and advances of AIB Limited by maturity percentage:

KASHIM IBRAHIM LIBRA

MATURITY	1995	1996	1997
Within 12 Months	95.6%	66.2%	84.2%
After 12 Months	4.4%	33.8%	15.8%

The bulk of commercial banks loans and advances are usually allocated in short term unsuitable form. Short-term working capitals that are self-liquidating in nature, consumer loans of less than a year and loans to new business are not usually granted in the required form. For lending to be appropriate, loans to agricultural and manufacturing sector especially the infant manufacturing and agro allied

industries must be of medium and long-term nature. This is in order for the resources to march the long-term productive activities of the sectors.

One of the explanations of this pattern of orientation of loans of commercial banks is that their liabilities are repayable on demand or at short notice and they must therefore lend in short term.

This argument may not be tenable as the repayment is in fact not required in total at a particular time.

Nigerian banks are largely not forth-coming to adopting or initiating innovative structures that would enhance customer's satisfaction and aid by creating credit.

4.1.5 SECURITY PATTERN OF LOANS AND ADVANCES

The security aspect is a very important issue in bank lending in Nigeria. The type of security to be obtained by a Bank depends on the amount of the credit, the duration of the payment and the nature of the transaction.

From the interviews held with the officials of the Bank, most of the security demanded by the banks may consist but not exclusive of the following:

(i) Title of land as evidenced by Certificate of Occupancy etc.
(ii) Stock and Share, Bonds and Life Insurance Policies.
(iii) Company's assets.
(iv) Corporate and Government Securities Trust Receipts.
(v) Personal Guarantees and other financial assets i.e. monetary deposits.

The collateral standards are tenably but undesirably foreign. This is because these are borrowed as part of the banking practices of foreign banks from which the majority of the banks in the country, which are now largely indigenised, evolved and are still affiliated.

What makes them practically undesirable is that they do not fit the banking and financial environment of the country.

Insurance life policies, conveyances, stock and shares certificates and similar collateral are usually available from

the borrowers when requested in advanced countries. In developing countries like Nigeria, these are not common. Thus the insistence on availability of collateral as a prerequisite for advances by Nigerian commercial banks only serves as a restriction on aggregate credit that could be created.

In addition to insisting on rather hard collateral standard, banks put excessive emphasis on security for advances. In developed countries, collateral can be furnished with relative ease.

Table 4.7 provides the analysis of the loans and advances of African International Bank Limited by security before loan loss provision from 1995 to 1997.

(₦ 000)

Security	1995	1996	1997	1998
Against Real Estate	641,975	1,007,97	1,727,904	2,807,784
Other Secured	836,937	985,299	2,275,582	1,238,489
Unsecured	235,420	328,155	478,776	1,140,056
TOTAL	1,714,332	2,321,432	4,488,262	5,186,329

A very high percentage of AIB Limited lending is secured. The level of unsecured lending has however continued to rise steadily over the years under review.

According to the officials, the amount of loan and advances given out to the customers without security depends on the integrity of the borrowers and the calculated risks.

Nigerian banks must appreciate the role of collateral in credit operation and the peculiar nature of the economic environment. A good collateral security should serve to improve credit worthiness, enough to enable the

management to give out economically desirable loans and not used to restrict credit.

4.1.6 REPAYMENT PATTERN

The maturity and repayment pattern of loans are clearly related. The repayment schedule, as distinct from the maturity of a loan, is an important factor appropriate in lending. An advance that has a repayment schedule out of time with cash flow ability of a borrower is not likely to be helpful to him. It is often desirable for business enterprises to recover a term loan with repayment schedule tuned to cash flow.

A high proportion of loans and advances granted by commercial banks were of the overdraft nature payable within 12 months. For example, in African International Bank Limited, loans and advances for which repayment was required within one year was 66% in 1996 while in 1997 it rose to over 84%.

The repayment pattern is same to the cross section of the commercial banks. Non-availability of data made the illustration of aggregate repayment structure impossible.

Criticisms have been made of overdrafts as a source of finance.

In response to this criticism, banks have put up the argument that overdraft facilities extended to firms are rarely terminated completely and some advances run until they become in effect medium or long-term finance. The borrower may thus rely on it as a permanent part of the firms finance capital.

KASHIM IBRAHIM LIBRARY

It is noteworthy that the view above makes it clear that only the "Viable firm" can hope to use overdraft this way. Yet it is the "Unviable firms" that mostly need the facility. In developing countries like Nigeria, the number of viable firms is quite scanty. More importantly are the present small, struggling; unviable firms, which are in the majority, that hold the key to the growth and development of the economy. Equally important to them is the extension of term loans.

A more realistic approach to lending would have been a situation where there is tendency for lending to industry to

take the form of term loans with period ranging between five to seven years and sometimes longer and with repayment pattern geared to such particular circumstances.

4.1.7 ANALYSIS BY PERFORMANCE

One important measure of the performance of the credits of commercial banks is the analysis and classification as to whether they are performing or non-performing. The higher level there is, of non-performing credit, the higher the risk that depositor's obligations will not be met. It also leads to the inability to grant more credits.

A review of such analysis for African International Bank Limited tends to suggest that there is a pattern of increase in the level of non-performing credits over the years.

The ratio of non-performing credits as a percentage of total credits was about 15% in 1995, rising to 21% in 1996; dropping to about 12% in 1997 but rising significantly to 32% in 1998.

This means that either the beneficiaries of the facilities are not utilizing it well or their endeavours are not

justifiable giving adequate returns for repayment and continuous survival in business.

4.2 MARKETING

A banker has to attract customers to sell deposits and has to attract them to buy loan and advances. The marketing is essential because of the existence of too greater a quantity of funds outside the banks in relation to the total money supply.

Banks have not been able to mop up the excess liquidity and create more credit. If banks were to market their services effectively, customers will be attracted to deposit money as a result of which a greater sum of money would be mobilized and given a credit multiplier of such funds mobilized, the bank will be in a position to ultimately create credit.

4.3 COST OF CAPITAL

Looking at the movement of the rates of interest in Nigeria, we would notice that the Central Bank Minimum Rediscount Rate (MRR), which is the rate at which other banks borrow from the Central Bank and determines the rate at which

they in turn lend to their customers rose from 4 .5 % in 1970 to 17% in 1990.

Consequently with deregulation and market philosophy of the Government, the commercial banks lending rate rose from 26% in 1992 to 60% in 1993. Average interbank call rate, which closed at 46% in December 1992, fluctuated between 60 and 120% in 1993.

In 1994, the Federal Government fixed the interest rate at 21% and such was maintained until 1998 when more deregulation policies were introduced thus allowing the interest rates to further go up.

The rate of interest when compared to between 5 to 12% obtainable in developed countries suggests that the cost of capital is very high. Such high rates are bound to discourage investment especially in the directly productive sector of the economy.

These high costs of capital will only hamper and restrict borrowing.

4.4 PROBLEM & CONSTRAINSTS

Commercial banks have proffered problems and constraints, which restrict their lending capacity. These constraints are classified under three broad categories.

4.4.1 EXTERNAL CONSTRAINTS EXERCISED BY THE MONETARY AUTHORITY

One of the constraints is known as legal and regulatory constraints. Typical of this constraints is the category found in section 13.1 of the Banking Decree of 1969 which restricts the total amount a bank can lend to one customer to maximum of 33.3% of the sum of the paid up capital and statutory reserve of the Bank.

Other regulatory constraints on bank credit are those arising from the Central Banks use of the power conferred on it by the law. Specifically, banks operate within the constraints of section 12 of the Banking Act, which stipulates that:

"Every licenced bank shall maintain a holding of cash reserves; specified liquid assets, special deposits in the

Central Bank of Nigeria and stabilization securities as the case may be, not less in amount than as may from time to time be prescribed by the Central Bank".

The Central Bank also prescribes interest rate structure for the banking system and the loan stratification guidelines limiting total bank lending to some categories of borrowers.

This is also an important regulatory function with respect to selective credit, which allows different sectors to progress in line with priority placed on the sectors.

KASHIM IBRAHIM LIBRARY

4.4.2 THE INTERNAL CONSTRAINTS

These constraints are internal to the banks and limit their operation. Prominent among these constraints are capital availability; deposit base level; credit policy and management effectiveness. One function of capital is that of supporting the credit risks when a bank is called upon to assume its normal lending business. Capital adequacy is a function of the assets and the volatility of the liability.

Another internal constraint is the banks lending policies. The supply of credit, all things being equal, depends on a

lending policy. At present banks are expected to maintain a deposit lending ratio of between 60% and 65% but not exceeding 70%. The nature of deposits with the commercial banks is a function of their lending behaviour and this explains the rigid adherence to short term lending by the commercial banks.

Commercial Bank lending is therefore predetermined by the nature of their deposit. Most of the monies deposited are call money repayable on demand, which accounts for their lending being mostly on short-term basis.

Another constraint is the lack of adequate delegation of authority to branches to ease customers' negotiation of finance as well as limited knowledge of credit by bank officials.

Above all however, the fear of default by customers is one major constraint the banks have had to contend with.

4.4.3 ENVIRONMENTAL CONSTRAINTS

These are constraints imposed by the environments under which banks operate, notable among which are economic

climates of the country, customer's reactions as well as government fiscal measures.

476968

In a situation where the economy is undergoing a down turn, lending will be adversely affected as demand would be seriously affected significantly by the customers' attitude to lending. In a situation where applicants are known not to cooperate with banks in supplying necessary documents and securities and or are known not to have good books of account and record of their business, lending under that environment is charged with a lot of risks ranging from the account becoming bad, diversion of funds for other activities other than the one proposed for which the loan was granted.

Thus the purpose for which the loan was granted becomes difficult to monitor.

CHAPTER FIVE

5.0 SUMMARY, RECOMMENDATION AND CONCLUSION

This study examine the operations and analysis of commercial banks lending function vis-à-vis their financial intermediation role of mediating between those who have surplus funds scattered in different places and aggregating them in lump sums for employment by those who require to borrow funds for productive utilization.

5.1 SUMMARY OF FINDINGS

The data presented revealed that these institutions had grown tremendously in the last six to seven years. Total loans and advances had increased many folds during this period. There had also been a phenomenal rise in the number of the commercial banks in the country with a corresponding increase in their branch network.

In spite of this development there is no corresponding improvement in their lending operations. The maturity distribution, security pattern and repayment methods of the bank loans and advances have been most unsuitable and

rather inconsistent with the realities of the Nigerian economy and especially the majority of enterprises in the private sector.

It has been pointed out how unduly and undesirably short-term the maturity of the loans and advances are. Given the fact that the financial support required by a large majority of our economic units is necessarily medium to long-term in nature, as a result of their infancy; the maturity patterns of the bank financial assistance must alter if the assistance is to be of any use.

The undue emphasis being placed on the demand for security by these institutions also circumscribes their lending function. Overall about 80% of their loans and advances are secured. Compared to banks in developed countries of the world, the lending attitude demonstrated by these data is undesirable. It has undoubtedly become a harm string to loan demand and supply in the developing environment like Nigeria because of inability of prospective borrowers to furnish security.

For business enterprises majority of which need medium and long-term advances, the repayment pattern exhibited is unwelcome. It can be observed that loans and advances repayable by overdraft method have been increasing in comparison with those repayable by other methods.

All these indicate compelling evidence that the Nigerian banks have over time become more and more liquidity conscious and more risk. Consequently they have put decreasing proportions of their total resources in loans and advances of medium and long term duration with corresponding repayment pattern and with the strict condition attached to security being de-emphasized.

Presence of the banks in the urban areas and a few other places has facilitated savings to some extent. However, being urban oriented, they are not structured to undertake risks, expenditure and work involved in financing, administering and supervising a large number of small scale industries spread in remote areas. Credit given out are being monopolized by the few large established firms, making the credit provided too small in terms of needs of

the vast majority of the small scale industries as against a handful number of well established large scale enterprises.

The Nigerian commercial banks in their structure are still ill equipped for effective mobilization of personal savings. Banks offices and branches are too few and far between in relation to the population and size of the country. It follows by the same taken that is also ill equipped for effective lending.

KASHIM IBRAHIM LIBRARY

Marketing bank services have been limited to advertisement aimed at image building rather than development of new products and services to identify and exploit the gap in the financial market. Banks have adopted an armchair posture of waiting for business to come rather than going out to solicit for business.

The limited and inadequate extent to which banks provide lending related services leaves a lot to be desired. The role of a banker is more complex than that of simply being a provider of finance. It involves building an intimate business relationship with the customer, understanding his project and problems, threats, opportunities and generally

finding out what further services are required by the customer in order to match resources to needs always and of course profitably. Unlike the situation in developed countries; very many banks in Nigeria have no business advisory services unit.

The cost at which the borrowers access funds is too high. The interest rates rose from 26 % in 1992 to 60 % in 1993. Such high rates of interest are bound to discourage borrowing and consequently investment, especially in the directly productive sectors of the economy.

The management and control of bank lending has been inadequate and much is expected in this regards. In general, they do not have an organized and systematic approach to corporate planning and control. This appears one of the reasons why most of the banks operate without a written loan policy.

On the part of the borrower, general scarcity of relevant and reliable information coupled with unwillingness on their part to cooperate in the exchange of information apparently

make the bank undertake greater risk and make assessment of the prospective borrower more difficult.

Commercial banks have also being subjected to operate under numerous directives and guidelines prescribed by the monetary authorities. Somewhat, the authorities have impelled desirable behaviour and record modest achievement in their monetary policy goals.
For the banks, however these regulations to a large extent are pains and restraints they could do without.

5.2 RECOMMENDATIONS

The following are the recommendation which are considered necessary and which arose from the research.

The maturity distribution, repayment pattern and security methods of the bank loans and advances should be modified to meet the realities of the Nigerian business environment and economy. The banks would do well by placing more emphasis on the financing of the private sector activities covering long, medium and short-term investment in industry, agriculture and small-scale indigenous enterprises.

Effective lending requires after sales services, finance counselling and advice. Banks should be technically equipped to appraise long-term project. They should establish Corporate Finance divisions or Business Advisory units to offer specialist advice to their numerous customers to complement their lending activities.

This in turn requires creative management in banking; the type that is very dynamic and constantly strive to make optimum contribution to the development of the private sector, such that orthodox practices are completely revolutionized. Also the operational orientation that favours established customer and reject outright a loan application from a new client should be re-examined.

The situation prevailing in Nigeria seems to necessitate employing certain positive measures to improve the quality of bank personnel especially bank management.

They should be sufficiently re-oriented to banking techniques more suited to the country's special development needs and at the same time be of the right caliber capable of providing financial facilities and assessment of credit

470903

worthiness of the customer in a more efficient manner than hitherto obtained.

The area of manpower training should be developed to facilitate the desired increase in the pool of available skilled manpower for the banking industry. There is also need to make the bankers aware of the economy wide implications of the lending activities so that they may better appreciate the need for development financing. Bank workers should be trained in corporate business development and be more innovative.

RECEIVED
Bello Uni

With adequate technical expertise, authority should be delegated to the branch manager to give them greater latitude to process and assess loan application and the credit worthiness of local business to quicken the negotiation of finance. Understanding the peculiarities of local industries needs would also be a catalyst to lending activities of the banks.

KASHIM IBRAHIM LIBRARY

Banks should also adopt marketing concept in banking, which implies expansion-oriented attitude in overall strategy. Bank should seek after and develop committed customers.

HG

They should create opportunity via introduction of new and more attractive financial products enough to induce people to increase their rate of savings of their funds within the banking system.

Savings could further be facilitated to a large extent by extending their services to the non-urban areas to bring the savings institutions nearer to the people and to make their utilization more attractive in terms of cheaper cost of service and higher returns, thus encouraging banking habit in the rural communities. The quality of services provided by the banks should be improved upon by quickening the act of obtaining basic financial services in more easily accessible manner. A more vigorous marketing strategy and tactics will be in the right direction to make customers aware of the available financial facilities.

The Nigeria commercial Banks do not engage seriously in corporate planning; as a result they may only respond impulsively to emerging opportunities. The banks as a step to efficient loan management must begin to plan for organizations as these corporate plans provide the framework of functional plans. Management of the banks

should formulate credit policies and within the framework of the Central Bank guidelines plan their aggregate and inter-sector distribution of loans and advances. This will serve as a guideline to effective lending practice. An important aspect of this exercise will involve communicating the lending policies of the banks to the general public.

476968

The capital base of the banks determine the amount of loan that can be committed to a single client and set a limit to the amount of deposit a bank can attract. The size of capital also influences the degree of confidence in the bank. Thus an increase in the capital base of the commercial bank is an important strategy in boosting the banks intermediation role, particularly where there are legally prescribed capital and capital deposit ratio. In such a situation, the size of the credit could be a constraint.

Government can also help directly by way of establishing facilities for rediscounting or refinancing the term loans of the commercial banks. Banks have traditionally talked of the risk and inappropriateness of lending on a long-term basis of funds they have borrowed at short-term. If refinancing facilities are available, the banks are likely to

become confident to hold a higher proportion of their loan portfolio in term loans.

Government can also make more efficient commercial bank lending by assisting in ensuring that right technical ability exist to the borrowing firms to make effective use of the financial resources. For this reason, Government must come out with a bold and ingenious programme of technical support for budding entrepreneurs in the country. There are various ways by which government can do this. Effective dissemination of technical know-how and technical services information, good use of feasibility studies, project identification and articulation can also play a part.

The basic units of production in developing countries like Nigeria are typical small-individual craftsmen and artisans, smallholder commercial and industrial business and farming. The sheer number will make attempts to extend credit facilities to these small units impossible. The formation of these units into corporate organizations with larger resources and increase credit worthiness will provide a desirable answer.

Special interest group banks should also be encouraged. A developing phenomenon in the banking industry is the tendency by special interest group to apply for banking license. Manufacturing Association of Nigeria (MAN) is promoting the Manufacturing Association of Nigeria Merchant Bank. Other special interest group banks like Farmers Bank, Small Scale Industries Bank should be developed.

The problem of low bank density in the rural communities can be resolved if the Central Bank actively promote the development of community or regional banks as a matter of deliberate policy. The difference between rural branches of commercial banks and community banks is that one is imposed by the established banks and the other is promoted by the communities themselves to serve their own needs based on the cultural and communal relationship subsisting among each community and provided with technical and operational support from the Central Bank.

This can also enhance the desired wide geographical spread of investment in the country.

The monetary authority should further consider the setting up of small firms' investment companies - qualifying for special tax exemptions for provision of equity finance for small firms.

Individuals seeking to use bank credit facilities must be able to show that they are credit worthy, financially trustworthy, and able to repay loan, as agreed. They must be able to provide information relating to their business development, such as past accounts, records of profits and turnover, meaning; they must learn and keep modern accounts.

Prospective borrowers must be able to sell their projects successfully to their prospective financiers. The individuals must therefore approach financiers with well prepared and carefully thought out and articulated feasibility studies of their projects. They must not expect the bank to supply the entire capital they want. They must have a stake in the project by contributing or being able to contribute an agreed proportion of the capital required. In addition, they must be able to provide acceptable collateral securities as

evidence of their faith in themselves and the feasibility of the project.

Finally, prospective users of bank's credit facilities must demonstrate their managerial competence to execute the project successfully.

5.3 CONCLUSION

The study has dealt extensively with the role of commercial banks as financial intermediaries and precisely in relation to their financing of business enterprises. However, the findings and recommendation will be found to be of invaluable contribution if they are carefully examined and adopted for implementation.

5.4 SUGGESTION FOR FURTHER STUDY

Banking activities and financing of business enterprises is very dynamic. Thus in the face of intervening changes and development in the banking system and economy in general, new roles will surely emerge for the banks. More so, the Nigerian banking system is undergoing a tremendous development in terms of performance.

Further study will therefore be necessary in the future to re-examine and assess and reflect this largely developments, their effects on bank performance and the industry entirely.

BIBLOGRAPHY

BOOKS

(1) A.C. DURRY (1982), Finance House, Waterlaw Publishers

(2) A.J. Murreh & Allen, Sykes; The Finance and Analysis of Capital Projects London, Second Edition.

(3) Casimir, Emman Agene, (1991), Foreign Exchange and International Trade in Nigeria Gene Publications, Lagos.

(4) Donelson, T.H. (1979) Lending in International Commercial Banking Macmillan.

(5) Femi, Adekanye (1983), A Practical Guide to Bank Borrowing Graham Born.

(6) G.O. Okonkwo (1980), The Nigerian Financial System, Macmillan

(7) Ralph K. Osayameh (1980), Practice of Banking: The Nigeria Institute of Bankers Vol. 2. F.A. Publishing Co. Inc.

(8) I. Livingstone; O. Teriba L.V.P. Diejomeh (1987); Economics West Africa

(9) Sawyerrs, P.S. (1975); Modern Banking - The Challenges of Business Mc Graw Hill Inc. 2nd Edition.

JOURNALS

(1) Zayyad H.R. (1994) Deregulation of Banking System: Its Impact on the Nigerian Economy: Paper presented at the 3rd NNDC Alumni Seminar, NNDC Newsletter Eleventh Edition; January - June 1994.

(2) Orimolade, W.A. & Adewale, "Industrial Equipment Leasing in Nigeria: Problems and Prospects.

(3) Oyekan, J.A. (1978) "Project Financing" Paper presented at the 13th Annual Bankers Seminar of Nigeria Institute of Bankers at the University of Lagos.

(4) Wright, A.W. (1976) "Bankers Preferences" London: BPL Bankers Magazine.

REPORTS

476968

(1) African International Bank Limited Annual Report 1991 - 1997

(2) CBN Economic Financial Review & Reports (Various Issues 1993 - 1996)

(3) CBN Annual Reports and Statement of Account 1994 - 1995

(4) NDIC Annual Report & Statement of Accounts 1992 – 1993.