THE IMPACT OF LIQUIDITY SEQUEEZE ON TREASURY MANAGEMENT

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D E C L A R A T I O N

I hereby declare that this project has been written by me based on research findings conducted personally by me. And that to the best of my knowledge no other project of this nature has been written and presented in any form anywhere for any higher degree. All materials used for the research from other sources have been duly acknowledged in footnotes and bibliography.

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C E R T I F I C A T I O N

This project report entitled "THE IMPACT OF LIQUIDITY SQUEEZE ON TREASURY MANAGEMENT" by ALIYU IBRAHIM meets the regulations governing the award of the degree of Master in Business Administration of Ahmadu Bello University, Zaria and is approved for its contribution to knowledge and literary presentation.

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D E D I C A T I O N

This project is dedicated to: my wife HAJIA HAFSATU JUMMAI ALIYU and children, ZAINAB, AHMED, and NAFISAT; my Parents and those close friends who have given me the encouragement to pursue the course of study to its logical conclusion.

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

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A B S T R A C T

Treasury Management, which has to do with the management of the liquidity resources of any organization, involves planning, controlling, and monitoring the sourcing, disbursement and investment of the available financial resources.

Managing the treasury in an efficient and desired manner can be jeopardized in the event of any form of squeeze especially as it concerns the changes in the external variables which may be beyond the contemplation of the organisations. The financial institutions particularly the banks, and the government organizations have been subjected to many forms of policy measures which have not been in their favour. The study has been undertaken, therefore, to unearth the extent of the impact of such liquidity squeeze on treasury management.

It has been discovered from the study that the barrage of policy measures in the past by the government and the apex bank has put the banks and the government organizations in quagmire. Some banks have collapsed while many others have become distressed. The government organizations have been compelled to engage in staff rationalisation beside the fact that they cannot engage in meaningful capital projects towards enhancing the welfare of the citizenry.

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CHAPTER ONE

INTRODUCTION

1.1 THE OVERVIEW OF THE STUDY

Funds in form of financial resources constitute the lifeblood of any organisation, be it bank, institution, entity, ministry, parastatal, an office, club or society. The financial resources happens to be the hub around which the operations of an organisation revolve. Funds, without exaggeration, constitute the heartbeat of any organisation. This, in view of the fact that the existence of an organisation will be in jeopardy in the absence of financial resources.

The crux of the matter is how to ensure the availability of funds at the appropriate time that they are needed for the organisation's use. This is very pertinent in view of the fact that, more often than not, the root cause of most crisis in the organisations is the non-availability of funds in terms of dire need for their use. Paradoxically, the excess amount of financial resources in terms of its availability has been known to cause some problems to organisations. Hence the ideal situation is to have the desired amount of funds that can be enough to meet commitments; current operations, future financial obligations and exploiting unexpected opportunities in the course of normal activities of an organisation.

The availability of the desired amount of funds to take care of the operational needs of an organisation does not transcends beyond liquidity. To ensure that an organisation has the appropriate liquidity, the acquisition of funds has to be planned for and its allocation controlled so as to ensure its judicious and efficient utilization. This presupposes that to ensure liquidity for an organisation, the sourcing of funds has to be planned for, its allocation budgeted for and its utilization strictly controlled so that the entity does not run out of funds. Liquidity for an organisation is sine qua non with the achievement of the strategic objectives of survival, growth, profitability and continued patronage by the public - both the current customers and the propective ones.

In the banking business, funds (or simply money) constitute the stock in trade. The availability of funds in the desired amount, therefore, is imperative towards ensuring banks' survival, growth, profitability and continued patronage by the customers. Above all, the funds have to be available towards meeting the demands of the depositors (or the customers) in terms of making payment to them through the withdrawals of their deposits. The absence of funds - a situation of cash strap or illiquidity - can and has infact spelt some calamities for the banks. Such misfortunes are the financial distress and total collapse which has led to the liquidation of some banks even since the advent of the banking business. For the banks, therefore, ensuring liquidity constitutes their main

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pre-occupation. Empirical evidence supports the claim that the absence of funds or liquidity puts the existence as well as the fortunes of the banks in utter jeopardy.

Managing the liquidity position of the organisation involves treasury management. Liquidity management, in essence, is the integral aspect of treasury management. Infact some writers posit that liquidity management is synonymous with treasury management. Such claim is hinged on the fact that the conerstones of treasury management are essentially the same with liquidity management. These are planning, controlling and monitoring the sourcing, disbursing and investing the available financial resources with the sole purpose of guiding against running out of funds, holding excessive cash and keeping cautious watch over the inflows and outflows of funds. Moreso, managing the treasury involves hedging against financial embarrassment - which can arise out of illiquidity - minimisation of borrowing costs and maximisation of investment income, necessarily within the liquidity needs of the organisations.

The efficient management of the treasury becomes a mirage in the event of any form of squeeze, which normally arises out of the behaviour of external variables that are beyond the control of the organisations. Such variables do influence the inflows and outflows of funds in organisations. In essence, the cash balance as available to organisations, cash disbursement needs or payment schedule or maintaining reasonable level of liquidity have critically been determined or influenced by the variables which are

beyond the contemplation of the organisations. The banking sector has been receiving barrage of monetary policy measures from the government and the apex bank which has put them in a quagmire. The usual reasoning is that all these are meant to direct the operators of banks so that they do not engage in operations that can be very inimical to the fortunes of the economy.

In the government circle, the management of the treasury is based largely on the provisions of the constitution, the highest law of the land. The organisation of the public treasury at all the levels of government is in line with the constitutional provisions. Then, does it mean that the operators of government organisations do not face any financial squeeze? The answer is simple. Far from it. Their position has not been better than the banks. Infact, they normally go cap in hands begging for loans from the banks in the events of financial squeeze. Squeeze is normally imposed largely by the operators of these government organisations themselves. Empirical evidences abound that confirm this ascertion. It means that the financial squeeze being experienced in the government organisations arises out of the presence of human factor.

It is against this background that the study is undertaken with a view of analyzing the extent of the impact of liquidity squeeze on treasury management.

1.2 STATEMENT OF THE PROBLEM

The management of the treasury in an efficient manner presupposes the availability of funds. These funds are normally sourced both internally and externally. But the bulk of the funds for the organisations' use is normally sourced externally. And these external sources are beyond the control of organisations. At best they can only device some means with which to induce the investors to deposit their money with them.

Inducing the members of the public to keep their money or funds with organisations such as the banks is subject to the influence of the government and the apex bank. The influence can come in form of the usual monetary policy measures which are meant to curtail the activities of these organisations. In most cases, the measures so adopted by the government and the CBN might not be favourable to the fortunes and operations of the banks. The advent of SAP in 1986 has brought with it a number of measures meant to revamp the economy but which have never been beneficial to the fortunes of the banks.

The apex bank has been under the believe that excess liquidity exist in the banking system. As a result of such believe, the monetary authorities have adopted stringent and tight monetary measures with which to reduce the level of liquidity with the banks. The banks on their own part have been complaining that such measures are only punitive in nature since they have affected their operations as well

as the fortunes which should have accrued from their activities.

The monetary policy measures so adopted by the monetary authorities have brought a catalogue of woes to the banking industry. The most glaring aspect of the implication of such of-measures is the liquidity squeeze on the banks.

The concern of the researcher has to do with this pertinent question: What is the extent of the impact of such liquidity squeeze on the treasury management especially in the banks? Herein lies the statement of the problem for this research work.

1.3 PURPOSE OF THE STUDY

The main purpose of the study is embedded in the concern of the researcher to determine and analyze the extent of the impact of liquidity squeeze on treasury management in the banking institutions. The objectives of the study, therefore, revolve around the followings:

1. To determine how the banks normally source their funds.

2. To ascertain the uses to which the banks normally commit their funds.

3. To determine on a comparative basis, the sources, the uses and the control measures on funds in government organisations.

4. To determine the various measures of the government and CBN that have been responsible for the liquidity squeeze.

5. To determine, on a comparative basis, the sources of liquidity squeeze in the public organisations.

6. To ascertain the impact of the liquidity squeeze on treasury management in the banks.

7. To identify the various survival strategies as adopted by the banks with which they have ensured that their operations were not totally crippled.

8. To profer some suggestions that can make the organisations device some hedging against and for the management of liquidity crisis.

1.4 SCOPE OF THE STUDY

The study covers the management of treasury in both public and private organisations with particular emphasis on the banking institutions. In the analysis of treasury management in the banking sector, all the types of banks are involved in the study. For the public organisations, the three levels of government (federal, state, and local council) are considered.

For the study, the various monetary policies of the government and the CBN are examined and critically analyzed. Such measures are those that started with the advent of SAP and those that have been passed over the years to the present day.

To fully appreciate the scope of liquidity management, the work delves into the essence of liquidity, the measure of liquidity and the monetary instruments that are available for the management of liquidity.

Furthermore, the various measures which have been adopted by the banks to manage the crisis are also covered by the study.

1.5 SIGNIFICANCE OF THE STUDY

A study of this nature has tremendous significance to the banks, the government, the public and the academia.

The banks stand to derive a lot of benefits since the findings and recommendation are of great importance in terms of planning inputs for their operations. Some banks that have been in need of some survival strategies can borrow a leaf from the other banks by adopting their time-tested strategies towards coping with the liquidity crisis.

The government and the CBN are bound to find the analysis and the subsequent suggestions very useful in terms of dealing with the banks. This, in view of the fact that the suggestions are very useful in terms of monetary policy

formulation. The CBN and the government are by implication going to adopt such suggestions so as to make the banks enjoy conducive atmosphere within which to operate.

The study is of tremendous importance to the academic since it offers more literature on the subject of liquidity squeeze on treasury management. It is useful to the academia since it stands to contribute to source of knowledge particularly in treasury management.

1.6 LIMITATION OF THE STUDY

The main limitation lies in the assumptions made in the research, which made the researcher to restrict contact to only four states of the federation. One of the implication of costs because of the economic situation in the country, which makes travelling around very expensive, the work has been based on the data as made available by the respondents in the four states.

The researcher restricted the coverage of the research work to Kano, Kaduna, Abuja and Lagos, where the headquarters of almost all banks are situated. Moreso, the only banks contacted are the branches of commercial banks, merchant banks, development banks, community banks, people's banks that have branches in these areas. Their headquarters were only contacted in most cases.

The other source of limitation is the fact that the main focus of the study has been the banks to the neglect,

to some extent, of public entities.

1.7 ORGANISATION OF THE STUDY

The research report has been divided into five main chapters.

The initial chapter takes a look at the background to the study with briefs on the related issues which are normally contained in chapter one. These are the significance, statement of problem, scope of the work, and limitation.

The second chapter takes on the analysis of the literature review. The various concepts in treasury management were analyzed in the chapter. The third chapter discusses the various methods of collecting data for the study.

The fourth chapter presents the data generated and takes on the analysis of such data. The last chapter summarises and concludes the work. The last segment of this chapter is the area of recommendation.

1.8 DEFINITION OF RELEVANT TERMS

Some terms which are relevant to the study have been defined based on the context of this research report. Such terms are as explained below:

1. BANK DEPOSIT:- refers to the surplus funds kept by the depositors with the bank.

2. CAPITAL ADEQUACY:- refers to the amount of the capital funds which are termed enough or sufficient to cover the liabilities of the bank.

   The liabilities here refer to the total deposits with the bank.

3. FINANCIAL MARKET:- refers to the type of arrangement which facilitates trading in monetary instrument or securities.

4. INTER-BANK DEALING:- refers to the money market in which banks secure short-tenored funds for overnight funding of the clearing account with the CBN.

5. LIQUIDITY:- simply refers to the availability of or maintaining adequate funds to meet all obligations or commitments as and when they fall due.

6. MARKETABLE SECURITIES:- refer to the monetary instrument which can easily be converted into cash. These are short-term securities such as treasury bills and certificates.

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7. MONETARY INSTRUMENTS:- refer to the monetary securities such as the marketable securities which can be used to raise funds.

8. MONEY MARKET:- refers to the financial market that deals in very short-term securities.

9. ORGANISATION:- refers to entities, institutions, enterprises, and corporate bodies such as the banks, ministries, parastatals, military setups, finance houses, firms, etc.

10. STABILISATION SECURITIES:- refers to non-marketable, low-interest instruments normally issued by the CBN to banks with which to mop up excess liquidity.

CHAPTER TWO

LITERATURE REVIEW

This chapter takes on the analysis of the concept of treasury management. And in order to have a proper grasp of the meaning, length and depth of the topic, we consider it appropirate to review the related literature. The analysis covers the management of funds both the private sector and the public sector. The emphasis is focused on the sourcing and utilization of funds particularly in the banking subsector of the private sector. On a comparative basis, the analysis also touches on the sourcing, allocation and utilization of funds at the government levels; Federal, State and Local governmental set ups.

Generally, the chapter analyzes the organisation of the treasury function, sources and uses of funds, besides the various views on the management of the treasury and the related issues. All these issues are discussed in relation to the situation which obtains in the financial institutions (especially the banks) and the government subsector of the economy.

2.1 CONCEPTUAL FRAMEWORK OF TREASURY MANAGEMENT

Treasury management can be viewed as the management of funds in organisations be they banks, finance companies, the government departments and agencies, corporate

entities and institutions. In another terms, treasury management concerns the management of the available financial resources. This centres on sourcing or receiving, disbursing and investing funds in banks, finance houses, government establishments, institutions and corporate entities.

Fundamentally, treasury management revolves around planning for and controlling of funds towards ensuring that the funds are readily available when required besides the judicious and efficient utilization and allocation of such funds. This boils down to connote that in treasury management, sourcing for and utilization of funds have to be planned for, controlled during allocation (or disbursement) and utilization with a view to ensuring prudent management of the available funds.

As it were, the conerstones of treasury management are essentially planning, controlling and monitoring of the sourcing, disbursing and investing the available financial resources. Above all, the significant objective of treasury management harps on the need to guide against running out of funds, holding excessive cash and keeping tab on the strategic objectives of the organization. These strategic objectives are survival, growth, meeting financial obligations and honouring customers' (the depositors) demands as it is the case with the financial institutions.

In the financial institutions, particularly the banks and the finance companies, managing the treasury involves hedging against financial embarrassment, which can arise out of illiquidity, minimisation of borrowing costs and maximisation of investment income within the overall liquidity needs of these organisations. Essentially, therefore, treasury management in financial institutions involves a system of efficient planning, effective monitoring and efficient allocation and control of funds.

In the government circle, management of the treasury involves sourcing for funds, collection of the approved rates and charges (in the area of taxes) and disbursement of the funds based on the appropriate expenditure sub-heads and necessarily on the strength of the approved authority to incur expenditure for the various government establishments; government departments, the agencies and institutions. Above all, it involves the control and monitoring of government expenditure and management of the approved fiscal and monetary policies. In essence, the treasury is a government department which is responsible for controlling and monitoring the government (public) expenditure and managing the laid-down and existing fiscal policies.[1]

2.1.1 SOURCING FOR FUNDS

In banks, generally, sourcing for funds comes through the deposits of the customers. In general

terms, the main sources of funds for the banks are the borrowings (loans) from the Central Bank and other banks - inter-bank borrowings and deposits of the customers in the form of savings, time deposits, current accounts, and inter-bank placements.

Dposits from the customers are a major source of financing the banks operations. In the words of Adewumi (1985),

> "sources of these deposit funds include corporate depositors - institutions in both the public and private sectors of the economy who account for over sixty per cent of all types of deposits. Others are institutional investors such as pension funds, insurance companies that account for ten per cent of the deposits"[2]

This view merely confirms the fact that the major source of banks funds come in form of deposits from the customers. And the bulk of the deposits come from the organisations in both the private and public sectors. In addition, there are the individuals who have enough surplus funds from business transactions, which they do deposit with the banks for various periods of times.

Generally, the banks strive to increase their deposits from the customers through attractive offers. These offers include insurance covers for accidents and deaths, upfront payments for the interest, the issurance of credit cards to large depositors, payment of interest on current account balances and other benefits associated with jumbo sums of money in deposits.

Other sources include inter-bank placements for varied periods of time. There is the money at call and at short notice, which indicate funds with the bank arising out of inter-bank borrowing that must be repaid on demand. The money at short notice may be money borrowed for, say, twenty-four hours but at a very low interest rate.

The loans from the Central Bank are normally taken in circumstances beyond the control of the banks. Such borrowing are recoursed to only as the last resort. The loans attract some interest which is based on the minimum rediscount rate or the bank rate. Such rate is used as a basis upon which the interest rates chargeable on loans to the public - institutions and individuals - are based by the banks. The funds which come through the borrowings from the Central Bank are used to meet demands by the customers at peak periods such as Sallah festivities, Easter, Christmas and New year celebrations. Such peak period can arise from the payments of salaries to the workers around month ends.

In the government circle, the sourcing for funds include sale of crude oil and other petroleum products, royalties, tariff, income tax, excise duties as well as other direct and indirect taxes such as the value added tax (VAT) recently introduced on some goods

and services. Other sources include tolls, rates and surcharges. In addition, government normally goes aborrowing.

For the short-term loans, the government uses instruments such as the Treasury Bills and Treasury Certificates. The former instruments are issued by the government to raise funds which are payable in three months. Their majority does not exceed ninety-one days. The latter instruments are medium-term government securities which mature in one to two years.[3]

There are other instruments which are being used by the government to raise funds. These are long-term instruments such as the development loan stock or government bond. These instruments are redeemable by the government after a very long period of time, say, ninety-nine years. Such instruments can be used by the state or local authorities.

2.1.2 MANAGEMENT OF CASH

In general terms, cash is needed by the organisations for use in settling financial obligations such as payment of salaries, and allowances, execution of projects, working capital and meeting the demands of the customers as it is the case with banks.

According to Fisher (1902), firms (and other organisations) need cash as a result of their need to transact with one another.[4] In the view of Marshall and Pigon (1919), the amount of money held at any particular time is directly influenced by the frequency of transaction, individual's level of wealth and the opportunity cost of holding money.[5] Accordingly, as the velocity of transaction increase, the amount of funds or money held will also increase.

According to Keynes (1936), there are mainly three reasons for holding cash, which he designated as transactionary motive, precautionary motive and speculative motive. The transactionary motive holds that cash balance is held to meet cash transactions in the course of normal business operation; that money is held to meet irregular cash outflows and the planned acquisition of fixed assets and inventories.[6] For the precautionary motive, cash is held for meeting unenvisaged needs. The funds are balances kept to meet unanticipated cash needs occasioned by such factors as sharp increases in the prices of raw materials, strikes and unexpected delays in the collection of accounts receivable.[7]

For the precautionary purpose, the amount of funds held depends on predictability of cash inflows and outflows. By implication, if the predictability is high less cash must be held against an emergency or other contingency. It also depends on the firm's ability to raise fund within a shortest possible time.
In the view of Keynes (1936), balance held for precautionary purpose is a function of the rate of interest.[8]

For the speculative motive, the funds held are to enable organisations to take advantage of opportunities which avail themselves at unexpected moments. The amount of funds held for this purpose is a function of the prevailing interest rate. According to Keynes (1936), where interest rate is expected to fall, the demand for money is relatively low, since firms hold bonds in anticipation of capital gain.[9]

There are other reasons as advanced by Hartley (1976) such as: cash is necessary due to existence of float between when company pay cost of securing resources and when conversion process is completed, and inventories turn into receivables and actual receipt of the cash made.[10] In the interim, firm need cash to finance its operation, which arises from the non-synchronization of cash payments and receipts. The other reason is attributed to the inability of the management to accurately forecast the cash flows.

Some receivables could remain uncollected when due. And as a result of this kind of situation, organisations have to keep cash balance to forestall eventuality.

Bechler (1983) posits that organisations' rationale for holding cash is the desire to promote good relationship with their bankers.[11] This view is hinged on the fact that with a large cash balance above the banks' compensation balance requirement, the organisations can easily secure a short-term credit line on a short notice.

OBJECTIVE OF CASH MANAGEMENT

Cash management revolves around the management of: cash flows into and cash flows out of the organisation; cash flows within the organisation; and cash balance held by the organization at any point in time. The basic objectives of cash management are: to meet the cash disbursement needs, which involves the payment schedule; and to minimise the funds committed to transactions.[12]

The overall rationale in line with the above objectives is to maintain a high level of liquidity with minimum risk. And similarly, there is the desire to generate additional income by investing idle funds when they become available or reduce outstanding loans.

Ideally, the first step towards realising the twin objective is the establishment of a minimum of cash balance above which excess will be invested in marketable securities.

According to Bechler (1983)[13], the main goal or objective of cash management is reducing to the barest minimum the amount of cash that is being used within the firm so as to increase organisational profitability without jeopardising its liquidity need. This, in essence, indicates that cash management aims at a fair risk-return trade off. He holds the view that organisations should pursue a cash management practice that will minimize its risk of insolvency. This presupposes carrying sufficient cash balance to meet financial obligations when due. On the strength of this, Bechler recommends that: enough cash must be on hand to dispense effectively with the disbursal needs that arise in the course of doing business; and the firm's investment of idle cash balances must be reduced to a minimum.[14] There is the need to strike a balance between safety, liquidity and yield.

It is pertinent at this **juncture** to delve into the analysis of the practice of cash management.

According to Pandy (1987), there are four phases of cash management which are as follows:[15]

1. Cash Planning: This concerns projecting future cash inflows and outflows at the present time;

2. Managing the Cash Flow: This has to do with a decisive aim at quickening receipt and showing down disbursal (or usage) of cash;

3. Optimum Cash Level: This provides the benchmark (or basis) that guides towards investment in marketable securities;

4. Investing Idle Cash: This has to do with selection of securities to buy that will satisfy the firm's objectives.

Cash Planning provides a device with which to plan for and control the use of cash. The cash inflows are needed for the operations of the organisation while the cash outflows are necessary for the smooth running of the organisation. Both the inflows and the outflows have to be syncronized in order to eliminate or minimise idle cash or liquidity crisis. The plan calls for cash statement based on forecast of cash inflows and outflows for a given period in line with the present operations or the anticipated future operations. The most popular device for planning and control of cash receipts and payments is the cash budget.

The budget gives information on the timing and magnitude of expected cash flows of the organisation and cash balances over the projected period. It is useful in determining the future case needs, plan for the financing of such needs and exercising control over the cash and liquidity.

Managing the cash flows involving accelerating cash collections and slowing disbursement. Acceleration of cash collection can be achieved by reducing perceived delays, which are associated with mail float, processing, float, transit float and disbursing float. The procedures that may be used to accelerate the collection and slowing disbursement of cash depend on the prevailing conditions. Expenses should be incurred in managing cash inflows and outflows as long as the marginal returns exceed the marginal costs.

The optimum cash balance which should be maintained has to take cognisance of both transactionary balance and the precautionary balances. The major considerations which are paramount in deciding the ideal cash balance to maintain are the issues of profitability and liquidity. The level of cash balance to be maintained should be such that it does not jeopardise the liquidity position of the organisation. On the same token, it should enhance the profitability position of the organisation.

The idle cash has to be invested in assets that can stand a substitute for cash and satisfy a temporary investment requirement of the firm.[16] In the view of Toy (1976), the investments should be made with the certainty of availability at the due date as the overriding consideration because today's investment may represent the payment of next week.[17] Essentially, therefore, liquidity and safety of the principal should constitute the prime importance in selecting short-term marketable securities. Other considerations include yield, which is the return on the investment, taxability of the interest income and capital gain and the value to be obtained if the securities are to be disposed off.

2.1.3 MANAGEMENT OF DISBURSEMENT

Disbursement of funds is based on the laid-down procedures and authorisation of the officers in charge of such responsibility.

In the financial institutions, especially the banks, the disbursement of funds is strictly controlled. The banks do not just release money without due regard to the existing procedures and controls. The funds are released on the strength of approval by the designated officers. The authorisation is based on the merit of the needs which warrant the release of funds. This has to do with the funds to be used for the commitments of the organisations.

Considering the scenerio in the banking institutions, there are laid-down procedures for the release of funds. To meet customers' demands, they have to present the necessary documents in the form of cheques (for the current account holders) and the pass books (for the savings). The cheques are passed by the paying Cashiers to the supervisors and accountants who are to authorize the payment to the customers. In some cases, the managers have to approve payment when the amounts of the cheques are beyond the limits of the junior officers. The same procedure applies to the payments on the presentation of savings pass book.
The rationale behind such practice is to prevent fraudulent practices.

The investment of funds has to be approved by the superior officer to the treasury officer. The usual procedure is for the treasury officers to discuss the investment proposals with their superior officers who will have to sanction the release of funds for the commitments on behalf of the banks. Such procedure is ideal since disbursement of funds should be authorised and controlled. The treasury officers or the financial officers as the case may be, in any case, are just in charge of investment or release of funds but the authorisation is a prerogative of their superiors.
It is a question of ensuring some checks and balances.

Within the public sector,[18] the release of funds is based strictly on the laid-down legal provisions; a derivative of the constitutional provisions. Funds are normally released for various needs in the areas of capital and recurrent expenditure besides investment purpose.

The release of funds in the government circle is based on the approved functional heads and subheads for the purposes of accountability and control. In addition, the authority to incur expenditure (AIE) must be issued after the release of the budget before spendings from the heads and the subheads can commence. During the civilian rule, the heads of expenditure as contained in the estimates is usually included in a bill called the Appropriation Bill which the appropriation by heads of expenditure expresses the Assembly's allocation of funds to different uses.

The total amount allocated to a head may not be exceeded nor may new heads be created without the knowledge and consent of the Assembly. Each head is divided into a series of numbered subheads. These are smaller divisions of the estimates showing within a head how funds are to be allocated between various uses. The division by subhead is approved by the Assembly

when it considers the estimates but does not appear in the Appropriation Act.

Expenditure or spending, which involves the release or commitment of funds, is monitored by the Ministry of Finance. Virement, which indicates provision to transfer funds between subheads, is also controlled by the Ministry of Finance with the issue of virement warrants. The Financial Regulation 502[19] imposes the duty of vote - watching on the officers responsible for controlling votes. These are the accounting officers who are required to keep a vote book for each subhead showing: the amount sanctioned in the estimates or provided by supplementary appropriation, adjusted by any transfer by virement to another subhead with the relevant warrant members at the top of the book; and in the columns provided, the expenditure incurred, any further known liabilities and the balance available. It is the duty of the officers in charge of votes, as expected, to ensure that excess expenditure is not incurred on the subheads controlled by them.[20]

2.1.4 MANAGEMENT OF INVESTMENT

As earlier stated in this section of the chapter, investment of funds or the idle cash should be in the assets that can stand a substitute for cash, satisfy a temporary investment requirement of the firm, ensure reasonable returns and the safety of the principal

amount of funds. Above all, investment has to be made with the certainty of availability of the funds at the due date since today's investment may represent the pay roll or payment of next week.

Some other factors which are of paramount - consideration are: liquidity which relates to the degree with which a security can be converted into cash for use in meeting commitment; yield which is the gain from the investment, which is to be as high as possible, given safety and liquidity constraints; and taxability of the interest income and capital gain of a security in the portfolio of investment.

There is a variety of marketable securities which are available for investment purpose. These securities are normally issued by the government, its agencies and corporate bodies. These securities are Treasury Bills, Treasury Certificates, Commercial Papers, Federal Agency Securities, Certificates of Deposit, Bankers Acceptance, and Repurchase Agreement, among others. These are discussed in detailed analysis in another section of this chapter.

2.2 ORGANISATION OF THE TREASURY FUNCTION

This section considers how the treasury function is being run or organized in the various organisation. Every bank has a treasury department which has to be organized in an appropriate manner in order to ensure

efficiency, effective management and control. The analysis below takes critical look at both financial institutions and the government establishments.

2.2.1 TREASURY FUNCTION IN FINANCIAL INSTITUTIONS

In practice, the organisation of treasury function vary from one bank to the other. But the principles behind such organisation are similar if not the same. Most of the commercial banks in the country have their treasury departments centralised in their head offices; in order to reduce losses, guide against fraudulent practices and ensure desired performance of such sections of the banks.

The merchant banks carry out treasury operations in all their branches at full scale. But the commercial banks which are small allow only their big branches to carry out treasury investments. All bank's branches engage in treasury activities in one form or the other as regards sourcing of funds or investments.

There are rules and procedures which are laid down by the bank management for compliance in their treasury operations. Some reviews are done on regular basis as the need arises. Such procedures include: the settlement and recording procedures for all transactions; the level of authority required for all transactions; the limits for investments and placements of funds;

the officers or dealers authorised to deal in specified products or securities; serial pre-numbering of recording forms and confirmation slips for transactions monitoring; and maintenance of daily rate transaction sheets to reduce off-market and related party transactions.

It is instructive to state that merchant banks appear to have the most efficient treasury departments among the banks in the country. Of particular interest is the treasury department of the International Merchant Bank (IMB) PLC. The bank consults for other banks in terms of treasury organization and management. Such banks are the African Continental Bank Limited (ACB), Lion Bank PLC and Intercity Bank PLC. The organisation of the treasury function at the IMB PLC is analyzed below.

The treasury department of the IMB PLC is termed as the Treasury and Money Market which has four units: Asset and Liability Management; Domestic Group which deals with branches and inter-bank market; Foreign Exchange Group in charge of foreign exchange dealings, placements of foreign currencies overseas, domicillary accounts and exports proceeds; and Intermediation Issuing House which deals with discountable instruments such as commercial papers and bankers acceptances.

Still on the treasury of the IMB PLC, three units reports to a Senior Manager who in turn reports to a General Manager. The Deputy Manager in charge of

intermediation issuing house reports directly to the General Manager. The General Manager has full responsibility for the bank's treasury management and dealings with financial institutions in the country and abroad. He has to report to the Executive Director in charge of Investment Banking. The Director ensures that the funding strategies formulated are strictly followed. Directly, the Executive Director is responsible to the Managing Director. The whole treasury set up is under the supervision of the Asset and Liability Committee, which reviews and guides treasury activities periodically.

The overall funds management of IMB PLC is co-ordinated by the Committee, which consists of the General Manager, Senior Manager and the Officers in charge of all the units under the treasury and money market department. The committee has high powered representation of all top management staff.
This committee is in charge of interest rates, which reviews them periodically for deposits in the light of the situation which obtains in the money market.

2.2.2 TREASURY FUNCTION IN GOVERNMENT ESTABLISHMENTS

The focus here is on the Federal, State and Local government setups in terms of the organisation and management of their treasury departments. The analysis

has been considered necessary since the public sector revolves around these important variables in our national economy.

The Treasury at the Federal level operates the Consolidated Revenue Fund in accordance with the Appropriation Act and expenditure warrants issued by the Minister of Finance. The Treasury is headed by the Accountant - General of the Federation. The Auditor - General audits the transactions of the Consolidated Revenue Fund. The Ministries draw on the Consolidated Revenue Fund via warrants to incur expenditure and they account for such expenditure to the Accountant-General. The Accountant-General finalizes the accounts of the Federation and passes them to the Auditor-General who audits the accounts and then reports to the Government (in the case of the military rule and the Public Account Committee of the National Assembly-in the case of civilian rule. This is supposed to be done annually.[21]

Based on constitutional arrangement, the State Governor is responsible for the finances of the state. He causes estimates to be prepared and authorizes the withdrawal of funds through the Commissioner of Finance from the Consolidated Revenue Fund of the State. All revenues and other funds received are paid into the Fund except money due for the other specified public fund.

Normally, no money can be withdrawn for use without authorization by the Governor (under the military) or the House of Assembly in the case of civilian rule. Each state has a Director of Audit whose tenure of office, access to records and right of reporting are similar to those applicable to the Auditor-General at the Federal level.[22]

The treasury at the local government level in terms of its organisation defers from state to state. But in most cases, the treasury is normally headed by a treasurer who is the senior member among the permanent staff of the council. He relations with conducted through a Finance Committee.

The duties of the treasurer at the local government level include: receiving and disbursing money; keeping proper accounting records of money received and spent; seeing that financial instructions are observed in making out of vouchers, payments and disbursement of funds generally; informing the council regularly of the state of its finances; making necessary returns to the state government; giving financial advice to the council; making sure that all revenues belonging to the council are collected; seeing that policies and expenditures are carried out with due regard to economy and value for money; and maintaining efficiently run and staffed financial operations.[23]

2.3 SOURCES AND USES OF FUNDS IN GOVERNMENT ORGANISATIONS

This section of the chapter attempts to analyze the various sources through which government organisations (the federal, state and the local council) generate their funds as well as spending of such funds.

2.3.1 SOURCES OF FUNDS IN GOVERNMENT ORGANISATIONS

The Federal Government generates its funds from the following sources:

i. Foreign Exchange Earnings (from exports,etc)
ii. Personal Income Tax (from salaries of workers).
iii. Petroleum Profit Tax (from oil companies)
iv. Company Income Tax (from annual profits)
v. Property Income from Rents
vi. Dividends and Interests from Investments
vii. Mining Rents and Royalties
viii. Capital Gains, Casino and Airport Taxes
ix. Import and Export Duties
x. Purchase Tax - Value-Added Tax
xi. Internal Loans
xii. External Loans.

The loans are obtained by the government through the use of Treasury Bills, Treasury Certificates, Bankers Unit Fund, Development Stocks, Certificate of Deposits,

and commercial papers, among others. The bulk of the government revenue comes through the foreign exchange earnings which are followed by royalties and rents, petroleum tax and duties or tariffs. The loans are taken to augment the revenue which are generated from various sources enumerated above.

The state government obtains its funds through allocations, revenues and loans. These sources are analyzed below:

i. Statutory Allocation and Grants
ii. Sales or Purchase Tax
iii. Football Pools and Betting Taxes
iv. Motor Vehicle Tax
v. Drivers' Licence Fees
vi. Entertainment Tax
vii. Cattle Tax
viii. Personal Income Tax on Salaries.
ix. Capital Gains Tax
x. Stamp Duties, Estate Duties and Gift Tax.
xi. Property Income from Rents
xii. Dividends and Interests from Investments.
xiii. Loans-on-Lent (internal and external loans).
xiv. Miscellaneous - fees from markets, business premises, land allocation, contract tax, development levy, and PAYE deductions.

The state depends mainly on the allocations and grants from the federal government for the large chunk of its funds. Generating funds or revenue from the other sources enumerated above have not been anything to count on as they are very difficult to collect or realised as a result of tax evasion, falsification of records and fraudulent practices and outright embezzlement by the officials in charge of revenue generation.

The local government generates its funds from allocations, grants, revenue and possibly loans. The various are as enumerated below:

i. Statutory Allocation and Grants
ii. Rates on property, education levy, and street lighting.
iii. Taxes-community tax, flat rate, and poll tax.
iv. Fines and Fees: court fees and fines; motor park fees; forest fees; public advertisement fees; market fees; regulated premises fees; registration of births and deaths fees and licence fees.
v. Miscellaneous - rents on council estates, royalties, interests on investments and proceeds from commercial activities.

Just like the state, the local council depends mainly on the statutory allocations and grants for survival Over the years the local councils have not been generating any appreciable amount of revenue (or funds) from taxes and fees. Some local councils, without exaggeration, could end up spending almost the equivalent of amount realisable from these taxes and levies on their collection. Unless these councils contract out the collection of taxes and fees as well as levies to finance companies, nothing appreciable might be forthcoming from such sources of revenue.

2.3.2 USES OF FUNDS IN GOVERNMENT ORGANISATIONS

It is only pertinent at this juncture to consider the various commitments to which the government at various levels put their funds. In most cases the funds are spent on the maintenance of the government structures such as payment of salaries and allowances, renovation of buildings and maintenance of vehicles, machinery and equipment, especially at the local level. Generally, the funds are expended on the various commitments which are largely dictated by the provisions of the constitution.

At the federal level, the government makes use of its funds on both capital and recurrent expenditure. Such expenditure is purely for developmental purpose.

The various uses to which funds are committed are as follows:

i. Defence and National Security.
ii. Education and Health Care Delivery
iii. Maintenance of Law and Order
iv. Agricultural Development
v. Development of Mineral Resources
vi. Construction of Roads, Dams and Bridges.
vii. Social and Recreational Activities - Arts, culture, sports, competitions, etc.
viii. Provision of Water and Electricity
ix. Establishment of Industries and Industrial Layouts.
x. Ecological Disasters - floods, Draught, Famine, Oil Spillage, etc.
xi. Provision of Communication Facilities.
xii. Provision of Transportation Facilities.

The above list is by no means exhaustive. There are miscellaneous commitments on which the Federal government spends money which may be dictated by exigencies.

At the state level, the government spends money on capital and recurrent expenditure. There are areas which are reserved exclusively for the federal government. The other areas on which the state government expends money or funds on are as follows:

i. Education and Health Care Delivery.

ii. Maintenance of Law and Orders.

iii. Agricultural Development

iv. Industrial Development - in the areas of ownership and layouts.

v. Development of Markets, Shopping Centres, etc.

vi. Construction of Roads, Dams, Bridges, etc.

vii. Social and Recreational Facilities and Activities - Arts and Culture, Sports and Competitions, Amusement Parks, etc.

viii. Provision of Water and Electricity

ix. Provision of Transportation Facilities

x. Miscellaneous Commitments.

The list as at above is not exhaustive. There are other areas of commitments which could crop up and call for the attention of the state government financially. Such could be imposed by the federal government on the state or arise out of exigencies. It is instructive or pertinent to note here that payment of salaries and allowances (expenditure on emolument), which borders on recurrent expenditure has dominated the state government over the years. The amount of funds available in some states might only be enough to meet the annual bills on staff emoluments. Some states are not hicky enough to have sufficient funds to cover the outlay on the salaries and allowances. Hence they have to resort to borrowing to cover the deficits.

On a sad note, some state governments have resorted to retrenchment of workers in the recent times.

The local government councils too have to expend funds on both the capital and recurrent expenditure. At this level, the funds are mainly used for the emoluments of the staff members. Besides, there are other functions performed by the local councils which are conferred on them constitutionally. Such functions which involve the use of funds include the followings:

i. Establishment and maintenance of markets, car parks and public conveniencies.

ii. Establishment and maintenance of cementeries, burial grounds and homes for the destitute or infirm.

iii. Construction and Maintenance of roads, streets, drains, parks and other public facilities prescribed by the state legislature.

iv. Provision and maintenance of public conveniencies and facilities for refuse disposal;

v. Participation in the funding of education, development of agriculture and natural resources (other than exploitation of minerals, health services and other matters to be determined by the state legislation.

There are other areas in which the local communities feel the presence of the local councils. Instances are the provision of transport facilities, electricity and water supply. Furthermore, there are other areas which normally involves the attention of the local councils financially. And these, in most cases, are imposed by the Federal government. These are the provision of basic health centres, contribution for the funding of immunisation and road construction. The local councils are normally required to contribute the so-called matching grants to supplement the federal and state government allocation towards the execution of some projects which are in most imposed.

In some cases, the federal and state governments normally impose unplanned expenditure on local councils without being accompanied by adequate grants.

2.3.3 CONTROL ON THE USES OF FUNDS

There are some measures of control which have been instituted to check fraudulent practices, embezzlement, excess expenditure and misappropriation of funds in the government establishments.

The Account-General may not allow an issue from the Consolidated Revenue Fund or Development Fund unless it is supported by a relevant warrant for expenditure.

These warrants are issued by the Minister of Finance or the Commissioner of Finance. The warrant authorizes the Account-General to issue money and officers controlling votes to incur expenditures.

A Provisional General Warrant is a means of providing funds before an Appropriation Act is passed. It allows money to be provided for the first few months of the financial year until an Appropriation Act is passed. Constitutionally, it is recognized that if by the beginning of a financial year an Appropriation Act has not been passed, the President is empowered to authorize the withdrawal of money from the Consolidated Revenue Fund in order to meet expenditure necessary to carry on the services of the Government. This is for a period not exceeding six months or until the coming into operation of the Appropriation Act, whichever is earlier. The amount so authorized must not exceed the sum withdrawn from the Consolidated Revenue Fund for the corresponding period of the previous year.[24]

There are fourteen different types of expenditure warrant as specified by the Financial Regulations. Seven of these are for recurrent expenditure and the other seven ones for capital expenditure. Prominent forms among all of them are the Annual General Warrant of Recurrent Expenditure and the Annual General

Warrant of Capital Expenditure. These authorize the Account-General to issue funds arising from the main Appropriation Act. Certain items of expenditure that need special control are excluded from the Annual General Warrant. And by implication, the sums granted by the Appropriation Act are greater than those contained in the expenditure warrant. An issue of a Reserved Expenditure Warrant is necessary for the items which are not covered by a warrant before such can be funded.

The system of warrants, it has been noted, allows the executive a more sensitive form of control over the issue of funds than would be offered by a system relying entirely on the provisions of Appropriation Acts.[25] Another form of control over expenditure (or use of funds) is the provision of the monthly reporting procedure for ministries' accounts. Besides, the accounts have to be audited regularly. In the past, there was a system of control on the use of funds in which ministries used clearance or suspense accounts (below the line accounts) to avoid making entries in their vote books which, if entered, would have revealed excess expenditure. This was, in 1979, cancelled when the use of clearance accounts was outlawed.

It has to be recognised that it is not always possible to envisage all commitments at the time of preparation of budget. And the system is made flexible as a result of singular reason.

This calls for the supplementary estimates for expenditure which was not previously foreseen. The supplementary provision must be approved by the Ministry of Finance. The alternative lies in the use of virement, but it is strictly controlled. Virement is not possible between the heads of the budget but only between one subhead and another subhead of the same head. A restriction on the amount to be vired can be placed on the accounting officer, and he may not create a new subhead by virement. And it becomes the prerogative of the Ministry of Finance where large sums are involved.

2.4 SOURCES AND USES OF FUNDS IN BANKING INSTITUTIONS

This section considers the analysis of the various ways through which the banks source their funds for their operational activities. On the same token, the analysis also delves into the ways and manners through which the banks commits the available funds.

2.4.1 SOURCES OF FUNDS IN BANING SECTOR

Basically, the sources of funds available to all banks (commercial, merchants, development, among others), are generally the same. But the degree of usage and the amount of funds generated from the various sources vary from one to another.

The sources through which the banks generate their funds can be classified into internal and external. The internal sources include corporate savings, disposal of assets, leasing, provision for depreciation, debt factoring, among others. The external sources include share capital (equity), loans, deposits, among others. These sources are analyzed below.

1. CORPORATE SAVINGS

This source constitutes the main means through banks generate funds on yearly basis. The outstanding aspect of corporate savings is the cash generated from operations. This is obtained from funds which are not paid out as dividends from the profits generated. Such portion of earnings which has been realised from operations constitute a common pool of future funds out of which dividend will be paid and new investments financed. In essence, this refers to the reserves in form of statutory reserve, general reserve and revenue reserve from the profit and loss account. These reserves can be converted into share capital through capitalisation, and the amount spread into shares through banks, right or script issues to the existing shareholders.

2. SALE OF ASSETS

The stock of an existing asset can be disposed or sold to outsiders (or the workers) and the cash realised

ploughed back into the operations of the corporation. The sale is effected as opportunities avail themselves. Such assets are disposed of or sold when their foregone earnings would in future produce a rate of return as their disposal value lower than the corporation's combined cost of capital. The amount of funds from this source can be very negligible but it has to be reckoned with as a source of funds.

3. LEASING OF EQUIPMENT

This can be done as against outright sale of assets or equipment. This is commonly used for plant, machinery, land, building, vehicles, and office equipment. The corporation leases out the asset in return for periodic rents. The rents being generated from the lease agreement periodically constitute some viable source of funds for the corporation. These rents are charged to the profit and loss account as revenue generated from the assets so released on leasehold agreement.

4. DEBT FACTORING

This applies to the debts which are being owed to the banks. The banks sell the book debts - at a discount to allow profit to a buyer, the factoring company - in order to obliterate tying up capital in the advnaces it allows to its customers. Another form of it is that the factoring company advances a proportion (about eighty percent) of the amount of advance (or

credit) as it is made, without the company actually acquiring the debts. This is then recouped out of the cash being paid by the customers as it is received. The remaining twenty percent (the discount) is the profit to the factoring company.

5. PROVISION FOR DEPRECIATION

Depreciation is a charge against the profits realised in the course of the operational activities of the banks. This reduces the amount of profit and it is an operating cost. But the cash from it is available for the use of the corporation. The funds which may have accumulated over the years constitute provision for depreciation. The obvious rationale is to provide funds for the eventual replacement of the asset at a time it becomes a mere scrap.

6. ACCOUNTS PAYABLE

This refers to the funds meant for the creditors, accrued charges, taxation and dividends. Some of this are items which are in transit (between branches) and some others are yet to be claimed. The dividends have be declared for the shareholders but not yet claimed, which can amount to reasonable amount of money; can run into millions of naira. The total amount of funds from this source can be of much premium to the banks.

7. SHARE (EQUITY) CAPITAL

This source generates funds from the owners of the banks who are the shareholders of the corporations. The source can be categorized into preferred stock and common stock.

The Preferred Stock which is in form of preference shares is a kind of preferential but limited status. There are different types of preference shares such as cumulative and participating preference shares. These shares have features such as dividends being paid ahead of common shares; not deductable as expenses for corporate tax; and the par value have to be paid ahead of common stock but behind all debt obligations.

The Common Stock connotes full partnership in the corporation. It is regarded as the economic equivalent of full partnership in the earnings and assets of the corporation. The dividends for the common shares are discretinary and the stock holders only get the residual value of the profits after other payments. The common stockholders only receive what is left in terms of the value of the corporation necessarily after payment to all creditors, suppliers and the preferred stockholders in liquidation.

8. DEPOSITS FROM CUSTOMERS

Deposits from the customers (individuals, groups, and organisations) constitute an essential component of

money which is available for the banks operational activities.[26] In terms of the types of deposits, there are the demand deposit, savings deposit,and time deposit.

Demand Deposit provides some substantial (or large chunk) of the overall deposits available to the banks. It is an appropriate form of deposit for those individuals and organisations who place value on liquidity and the availability of funds at any time. Withdrawal of money is with cheque at any time without prior notice to the bank. It is, in essence, an economical and safe means of transferring a sizeable amount of money from one point to the other. Transfers are usually made through the banking clearing system.

Savings Deposit is a form of regular or pass-book entry account in which banks pay interest monthly at compound interest rate basis. The conventional attitude of banks is to pay savings withdrawals on demand. But the account holder can be restricted as to the amount and the number of times that withdrawal can be made within a period of time. The interest accruable to the holders of this account can be forfeited if withdrawals are made frequently than required in a period, say, a week or a month.

Time Deposit, unlike other types of deposit, has time status. Such deposit is kept with the bank for a specified period of time as agreed upon by both the depositors and the banks. The deposit is normally

evidenced by a non-negotiable receipt issued by the banks. Interest payable by the bank on this deposit is agreed upon at inception and the rate depends on how long the deposit stays with the bank. The bank repays both the principal and interest accrued at the date of maturity necessarily at the instance of surrendering of the receipt on the deposit properly endorsed. The depositor can forfeit some amount called penalty interest if withdrawal is to be made before maturity of the deposit.

9. CERTIFICATE OF DEPOSIT

This is a form of time deposit but it is mostly used where there is a competition for deposits. There are two categories of certificate of deposit; negotiable and non-negotiable. The non-negotiable type has the same status with time deposit. The negotiable type can be transferred by the holder of such an account. It is normally issued in large denominations with maturity of one year or less. They are issued in bearer forms and may be traded on the secondary market before maturity. The banks use this instrument to attract large investors with funds that could otherwise be placed in other money market instruments.

10. INTER-BANK BORROWING

According to Reed and Cotter (1980),[27] inter-bank borrowing is an alternative source of deposit that may be obtained at a price to meet the liquidity need of a

bank. Dealings on inter-bank placements are mainly on overnight basis, but it is possible to obtain funds for longer periods. Funds can also be obtained on this basis from the Central Bank (CBN). The terms for the transaction are mostly negotiated between the banks concerned with the funds purchased used largely to meet liquidity requirements.

11. BORROWING FROM THE CENTRAL BANK

The banks do engage in borrowings from the central bank. As has earlier been stated in this chapter, the banks do borrow some funds from the central bank only as a last resort. Such funds are normally utilized to meet the liquidity needs of the banks as regards meeting customers demand for their funds (deposits) through withdrawals.

The size of the banks' borrowing from the central bank is a barometer of the degree of the borrower-lender relationship which exists between the banks and the central bank and consequently of the dependence of the former upon the latter in the economy. Such relationship is very crucial to the power of the central bank towards exercising an effective control on the credit creation activities of the other banks in the country.

The degree to which the other banks depend for financial succour on the central bank is a measure of the degree of effectiveness of the latter in influencing

the lending or credit creating activities of these banks and consequently of the effectiveness of central bank's monetary and credit policy.[28]

The borrowings from the central bank by the other banks serve as a safety valve for these banks in the periods of urgent need of funds to meet the demands of the depositors. The central bank charges some interest on such loans, which is the rediscount rate. This influences the rate of interest which the other banks charge on loans and advances to their customers. This method of borrowing creates a healthy operational relationship between the central bank and the other banks. It is, in essence, part of the reciprocal relationship between the central bank and the other banks, especially the commercial banks.

Such borrowings are mostly used by the commercial banks in the sense that they do engage in the retailing banking activities. This necessitates constant payments of funds (liquid cash) to the customers; in fact on a daily basis. And more often than not, these banks do run short of funds. And they have to resort to the lending facilities of the central bank towards meeting such illiquid situation.

The merchant banks are presently operating on a wholesale basis in the country. And they do not need cash for payments to the customers all the time, except occasionally. But the operators of such banks have been

pressurizing the central banks to grant them the opportunity of operating on a retail banking status so as they be on the same pedestal with the commercial banks as well as the community banks and the peoples bank.

12. UNIT TRUSTS AND INVESTMENT TRUSTS

The unit trust initiative represents an important source whereby the savings of small investors can be channelled into investment. Based on its operation an investor with small amount of fund can invest an interest in several corporations where a direct investment would have to be limited to one or at most two.

Very small transactions are relatively expensive to process and this is reflected in the high dealing costs charged on them. A unit trust is managed by a management company for which its services receives fees and commissions. It is often owned by a merchant bank or commercial bank.

Investment trust is a limited company with its own conventional financial structure whose business is to invest in the shares of other companies. By buying shares in investment trusts, investors obtain an interest in a relatively widespread of instruments as they would with a unit trust. Unlike in the case of the unit trust however, an investment trust is closed and a potential investor must find someone willing to sell shares for him.

13. PENSION FUNDS AND ASSURANCE FUNDS

A sizeable amount of funds are made available from pension funds and from life assurance companies in endowment business. For both, the members make regular payments over a long period of time in order to obtain a **benefit** either as a lump sum or as an annuity upon the arrival of a specific date.

2.4.2 SOURCING FOR FUNDS BY THE BANKS

This pre-occupation involves the identification and development of a proper deposit and funding base which can support the particular situation of the bank and its operations. It is instructive to note that the overriding objective in the sourcing for funds is to provide liquidity for the banks at all times.

Liquidity, it should be understood, means that a diversified deposit base (savings, call deposits, time deposit and demand deposit) is to be maintained in order to finance unexpected rise in the need for funds (investments, borrowing, placements) or recall of funds by depositors.

Sourcing of investable and loanable funds have increasingly become problematic in view of the fact that there is multiplicity of financial institutions which are all competing among themselves for the investing public funds. Banks, therefore, have resorted

to various strategies in the recent times, to attract funds. These strategies include improvement of operations, ensuring prompt and efficient services to customers, agressive advertising and promotion, upfront payment of interests on deposits, payment of brokerage (or commission) for sourcing of depositors; payment of attractive interest rates on deposits, introduction of cards (e.g., UNICARD, UBACARD) for depositors' use, attract offers on deposits (e.g., insurance cover, health care-hospital bill payment, scholarships for the children of deposits, accident benefits) and other new products. Banks attempt to become innovative by introducing such products among the services being rendered to their customers.

The banks normally seek to minimize cost of sourcing of funds so as to maximize returns. This, they do by bringing some professional skills to bear on sourcing for optimum mix of deposit funds. This is ensured by offering attractive schemes to the depositors. These include deposit for foreign exchange, and special saving schemes in areas of school fees schemes, share purchase schemes and traders deposit schemes.

The greater percentage of a bank's investible funds are accounted for by deposits. This is so much important to the banks as the single source of their liquidity that they often engage in keen competition

for deposit mobilisation. This, in view of the fact that the capacity of banks to grant credit depends upon their capacity to mobilise deposits. The investment and lending activities of the banks would have been on a considerably smaller scale but for the large funds which they receive as deposits.[29]

2.4.3 USES OF FUNDS IN BANKING SECTOR

Generally, the uses to which the banks put their funds are basically the same. It is only the use of nomenclature and the areas of financing (agriculture, industries and manufacturing) that may differ. Such areas in which the banks commit their funds include investment, loans and advances, acquisition of assets, cash and short-term funds placements, bills discounting, placements in stabilisation securities, among others. These various uses are analyzed below.

1. INVESTMENT OF FUNDS

Some banks do invest part of their funds in equity holdings in other corporate entities. Some other ones are known to have set up other entities which invariably become their subsidiaries. Most merchant banks and development banks have their own subsidiaries which they set up with part of the funds available to them.

The commercial banks too are left out in this area of funds commitment. They do use part of their own funds for acquiring equity shares in some industrial and manufacturing companies. In addition, they do have funds committed into unit trusts and investment trusts. Besides, these banks do allocate part of their funds for the administration of pension funds trusts and estates.

2. EQUIPMENT LEASING

The acquisition and leasing of equipment has been the traditional preserve of the merchant banks as well as the development banks in the country. There is a development in the financial institution circle of recent in which the government came out with a policy that the commercial banks should feel free to go into leasing business.

Equipment leasing has provided a viable avenue or channel through which the banks do commit part of their funds. Leasing involves acquiring some items of equipment which are offered to the desired and prospective users in return for period rentals. These capital assets may be insured, installed for the lessees' use and maintained by the banks as the lessors, which indicate operating leasing agreement.

On the other hand, the lessees may have to insure and maintain the equipment on lease on the basis of the agreement; financial lease.

3. PURCHASE AND DISCOUNTING OF BILLS

Banks normally use part of their funds to purchase some securities in form of treasury bills and treasury certificates. It is usually compulsory for the merchant and commercial banks especially to take up some of these securities whenever they floated by the central bank on behalf of the government. In terms of the size of the funds committed on these securities, the commercial banks invest more on them than the merchant banks. In the area of discounting of bills (commercial papers) the merchant banks are the dominant holders of these instruments. The reason for this is not far-fetched. The merchant banks have the financing of foreign trade as one of major areas of operation. The commercial banks too do discount bills for their customers but to a limited scale.

The funds which have been committed on the discounting of bills (or lent to the discount market) represent the money at call and short notice. And such funds can be taken back on either demand or at short notice. The bank's make some earnings on these funds, and such funds constitute the banks' second line of defence and are highly liquid being recoverable at call.

Bills discounted is also a highly liquid earning asset and is included in the money market asset. These bills are regarded as self-liquidating automatically out of the sale of goods covered by such bills. This means, therefore, that first class bills are self-liquidating papers and are readily transferable to the central bank by way of rediscount without much loss because of the very short maturity duration of these bills.[30]

4. LOANS AND ADVANCES

The banks are always anxious to utilise their funds in such a manner as to optimise their net income from the use of these funds. Consequent upon this desire, every bank strives to maximize its net profit earnings or returns by employing its surplus funds by lending it to trade and industry but against tangible and or personal security. The earnings from the loans and advances come in form of interest chargeable on these funds. The lending portfolio differs from bank to bank depending on the policy of the bank and its areas of interest or that of the shareholders and directors. These funds can be mean to finance projects, agriculture, and housing scheme, besides industrial and commercial financing.

The banks also give out part of their funds to the government in form of taking up the government development loan stock whenever they are issued out

by the central bank on behalf of the federal government. Just like the subscription to securities such as treasury bills and treasury certificates, the banks are under a statutory obligation to commit part of their funds into the development loan stock. There is the statutory provision regarding the minimum percentage of bank deposits that must be invested in government securities.

5. STATUTORY CASH RESERVES

The banks are required by the statutory provisions that certain percentage of their liquid cash or total deposits with the central bank in the form of minimum legal cash reserves. And an increase or decrease in this minimum legal reserves ratio has the effect of increasing or depleting the total cash reserves of the banks, and consequently affect their optimum credit - creating capacity; an important function of the banks in the economy.

The issue of the minimum legal cash reserves ratio for the commercial banks was first introduced in America in 1933 at a time when the Board of Governors of the Federal Reserve System (the equivalent of the central bank) was empowered by a legislation to alter the member banks' requirements by regulation "in order to prevent injurious credit expansion or contraction."[31]

This power as conferred on the Reserve System to vary the minimum legal reserves to be maintained by the member banks with the Reserve Board was aimed at securing an additional device in enabling the Board to control the money market by contracting of expanding the credit - creating capacity of the member banks.

6. MISCELLANEOUS USES OF FUNDS

The banks, especially the commercial banks must maintain cash reserves with which to meet the daily demands on withdrawals of funds by the customers. Such cash reserves are funded from the money available to the banks.

The banks also expend part of their funds in acquiring some fixed assets. Lands have to be purchased or acquired for the purpose of putting up structures for the banks' headquarters and branch offices. In addition, plants and equipment have to be procured for use. Other assets are motor vehicles, motor cycles, furniture and fittings. In the recent times, banks started to invest heavily on the acquisition and installation of computers and their accessories. The move to computerize the services of the banks has been informed by the need to improve as their services to the customers.

Lastly, other uses of funds include the retirement, of liabilities, payment of dividends with cash out of the available funds and meeting commitments which are incidental to the day-to-day operations of the banks.

2.5 LIQUIDITY MANAGEMENT AND LIQUIDITY CRISIS

It is pertinent to take on the management of liquidity and the analysis on the liquidity crisis. The analyses in the various sections which precede this section constitute some prelude to the analysis of the twin issues of liquidity management and liquidity crisis.

2.5.1 LIQUIDITY MANAGEMENT

The essence of liquidity to the banks has two considerations; primarily as a basic purpose of maintaining liquidity is to enable a bank to pay back its depositors; and cash reserve has to be maintained to meet withdrawals as a result of loans made by a bank to the customers which leak out in the form of cash withdrawals. Banks are expected to maintain appropriate liquidity ratio against customers' deposits since the deposit mix of banks can be very volatile. Liquidity is not supposed to be tied only to the banks total deposits. But a consideration for the liquidity should incorporate the composition of the credit portfolio of the banks.[32]

In discussing the management of liquidity of the banks, it is pertinent to consider the impact of the major source of banks' liquidity; the deposits.

Such impact is normally precipitated by the volatility inherent in the deposits of the banks' customers. The volatility exhibited by deposits is very critical to the availability of funds since banks have to assess and decide on the proportion or percentage of total deposits that is available for investment diversification. In a situation whereby very large proportion of deposits are withdrawn at very short intervals, the bank has to keep a greater percentage of deposits in cash and the near cash assets or liquid assets than would been needed in a situation of less turbulent withdrawals.[33]

Still on the role played by the volatility of deposits, time deposits present less problems in terms of adjustment because such deposits are only accepted by the banks against retention tenures. In the case of demand deposits, it is very difficult to make adjustments in liquidity since they are proned to unanticipated withdrawals. Nonetheless, these deposits provide the banks with a relatively cheap investment base since they command low interest. They only call for careful provisions for withdrawals. In the country, another cheap source of funds is the deposit for the foreign exchange. The banks do require their customers to make some deposits for foreign exchange allocation in their current account before being allocated with the foreign exchange. The practice is that the allocation is normally released piece meal.[34]

the characteristics of their customers in relation to the banks' operations. Consideration is normally given to the average size of the deposit account so as to understand and appreciate the elements of risk associated with the various types of deposits. In the case of large deposit account, the element of risk involved is high since an unanticipated withdrawal of large amount can bring about adjustment difficulties. Nevertheless, the fluctuations associated with the average large deposit, as has ascertained from study, pose less risk than the small type and it becomes desirable for the banks to invest the surplus funds for the sake of profitability.[36]

In case of deposits which are mainly savings and time tenure, those types with large sums of funds tend to be unstable. It has been discovered that such funds do come from the excess of large demand deposits and can only remain in their accounts as long as they represent surplus funds to the immediate needs of the depositors. In comparative terms, the small institutional and individual deposits are known to be relatively stable but the demand deposits coming from such group of investors do fluctuate.[37]

Another important factor that influences the variability of deposits, as has been pointed out, is the size of the bank. Large banks are said to enjoy more stability in their demand deposits as a result of their wide operational network coupled with the

2.5.2 CHANGING PATTERNS OF DEPOSITS

The deposits brought to the banks by the customers (or investors) are very susciptible to fluctuations. The patterns of fluctuation in deposits must be watched and analyzed in order to determine the ideal proportion of the total demand deposits that has to be invested by the banks.

The variability or fluctuations in deposit levels are associated mainly with the behaviour of the depositors. The banks have no control over the inflow of deposits and their outflows in form of withdrawals. The increase and decrease in the levels of deposits are functions of some variables. In the case of demand deposits, such factors are the volume of sales, the income of customers, the size of the bank, and the tempo of business and economic activities.[35] In the recent times, the desire of the customers has become a potent influence on the inflows and outflows of the deposits kept with the banks. The interest of the customers have become dampered as a result of the incessant closures of banks in the country; this arises out of frequent strikes being embarked by the bank workers. Moreso, the customers do rush to withdraw their funds from the affected banks at the slightest hint of the crisis of distress.

The volatility of the deposits of the customers is largely outside the whims or control of the banks but they do make conscious efforts to understand

diversification of their activities. The wide representation of the depositors ensures some off-set in terms of inflows and outflows of funds from their deposits. The same scenario applies to interbank deposits. Banks by a conscious choice of the geographical spread and economic activities to serve, can influence the impact of the frequent deposit variability on their operations.[38]

2.5.3 THE ESSENCE OF LIQUIDITY MANAGEMENT

According to Stignum (1983),[39] liquidity is the ability to ensure availability of funds to meet commitments at reasonable price at all times. In the view of Fraser (1978),[40] a bank is considered to have adequate liquidity when it is in a position to meet normal withdrawals and requests for loans without having to sell - or liquidate medium or long term assets.

As explained by the banking practitioners, the essence of liquidity management can be likened to the concept of a reservoir. Vividly, it has been described as follows:

> "A bank's liquidity can be likened to a reservoir. If all receipts of funds are viewed as inflows and disbursement of funds are outflows from a reservoir of available funds, then sound liquidity management requires that the reservoir never runs dry. Inflow of funds into the reservoir are generated from new

> deposits, repayment of loans, sale or maturity of instruments, money borrowings, interest and other income and market additions to capital. Outflow from the reservoir results from cash required for deposit withdrawals, new and renewed loans, new instruments, repayment of borrowings, interest, dividends and other expenses."[41]

From this view, it means that funds flow into the bank's reservoir from all sources which have been analyzed within the earlier part of this section. The bank has to channel the available funds to where they are needed if it has to perform its role as a financial intermediary.

Liquidity management, according to the practitioners, necessitates controlling the level of the funds (the reservior as has been described at above) on a daily basis and the anticipation of funds movement in the long run. The control is ensured by regulating the flow into and out of the reservoir by managing both the need for and the availability of funds. This, in order to maintain the ability to ensure a delicate balance between inflow and outflow of cash.[42]

The essence of bank's liquidity is precipitated by the fact that financial intermediation involves a maturity transformation; the use of proceeds of short-term investments such as term loans and advances. Luckett (1976) posits that the dangers of liquidity inadequacy inherent in maturity transformation has to be recognised in the commercial loan theory.

According to the theory, banks should lend on short-term self liquidating commercial papers. The theory is hinged on the fact that the liabilities of a bank are repayable on demand, and the bank may not be able to meet its obligations if it commits the funds raised from the commercial papers, which is short-term liabilities, into long-term lending.[43]

Based on the study of many banks that have failed, the lesson to learn is that liquidity is supposed to be marginalized in the quest for the banks survival and profitability. As it were, liquidity is to be regarded as the central issue that ensures depositors confidence and "keeps the door open in the short-run"[44] In order to hedge against liquidity crisis, the banks are expected to structure their short and long-term investments portfolio to take care of unexpected short-term financial commitments and obligations.

2.5.4 LIQUIDITY IN RELATION TO ASSETS AND LIABILITIES

There are theories which have been evolved by some writers on the management of liquidity in relation to the assets and liabilities of the banks. These theories are as analyzed below.

THE SHIFTABILITY THEORY

The theory in respect of the asset liquidity management maintains that a bank's liquidity is a function of its ability to shift its assets to someone else at a predictable price. On this basis, a bank could obtain liquidity by disposing some of its assets through rediscounting of treasury bills towards raising cash or funds.

The other sources of liquidity as regards asset liability management include: Pledging of assets to raise cash; restructuring the asset portfolio such that the investment in long-term maturing assets is increased; and reducing the demand for loans or the curtailing of drawdown of existing commitments through the adjustment of principally the interest rate of the maturity and other structure of the credit.

A bank must be prepared to contend with losses if it seeks access to liquidity through asset liquidity management. The inherent losses in this approach relate to the penalty for terminating the contractual relationship (under - borrower) with the bank at a time before maturity date. In another way, they may relate to reduction in income resulting from sacrificing or forfeiting the opportunity to investment in higher income earning assets.[45]

THE ANTICIPATED INCOME THEORY

This theory still concerns the asset side liquidity management.

It asserts that a banks liquidity can be planned for provided scheduled loan repayments are based on the future income of the borrower.

The theory goes further to presuppose that bank's liquidity can be influenced by the maturity pattern of the loan and investment portfolios. Moreso, the theory advocates that lending should be based on the ability of the borrower (or beneficiary) to garner cash to meet repayment rather than relying much on the collateral pledged for the loans.[46]

THE LIABILITY MANAGEMENT THEORY

According to Reed et al (1984),[47] the theory holds the view that banks can meet liquidity requirements by bidding in the money market for additional funds. By implication, the bank can gain access to liquidity from the liability side of the balance sheet.

On the above premise, a bank that has run short of funds could dispense with the wholesale deposits or raise funds through money market instruments - in form of certificate of deposit - with which to beef up its liquidity.

In the management of liquidity, Riehl et al (1983)[48] posit that liquidity management has changed from the traditional asset side. These days, banks and non-banks change their liquidity to the liability side of the balance.

That the banks now structure their liabilities in such a way so as to be able to roll-over maturing liabilities with great ease and garner new liabilities by borrowing fresh funds, without difficulties. The banks, therefore, rely mainly as sufficient liquidity in the money market for tapping new funds whenever they wish to do so.

THE LOANABLE FUNDS THEORY

This theory maintains that the supply of loanable funds which affects the bank's liquidity is a function of the schedule of interest rate. According to Onyido (1986), the price which the banks pay for loanable funds is the interest rate which represents an income for the depositors and cost to the bank.[49] As expected, the higher the inducement for parting with funds, the more the depositors purchase the banks deposits. To lay credence to this assertion, Riehl et al (1983) maintain that there is always a price at which funds can be raised by the credit worthy customer or the borrower.[50]

Access by the banks to depositors funds depend on the size of the bank and the public perception of the image of the bank. This affects the depositors' confidence, which in turn affects the banks' liability access to liquidity. Other considerations are the interest payable on deposits and the government policies which affect the supply of money in the economy. These factors tend to determine the availability of deposits in the economy.

2.5.5 MEASURING BANK'S LIQUIDITY POSITION

Some devices have been evolved for determing the liquidity position of a bank. Such methods relate mainly to some standard ratios as they affect loans, advances, deposits, liquid assets, and current liabilities.

There is the loan to deposit ratio. As a commonly used ratio, it determines the percentage of deposits which has been committed to loans. The ratio is expressed as the total loans and advances divided by total deposits and multiplied by one hundred. In calculating the ratio, a distinction is made between stable deposits (term deposits) and volatile deposits (call and demand) since different implications would be arrived at in their calculations.

The calculation which indicate short - term assets implies a high level of liquidity but the ratio can be quite high. Conversely, a ratio with asset structure including a large proportion of long term assets may indicate liquidity problems. This, in view of the fact that the assets may have to be sold at a loss in the event of an urgent need for liquidity. According to Fraser (1978), therefore, the loan to deposit ratio only serves as a guide; that it becomes meaningful when the structure of the assets in relation to maturity is brought into focus.[51]

The other measure is the liquidity ratio, which is calculated as the total specified liquid assets divided by total current liabilities. For the specified liquid

assets, the items included are: cash; balance held with the CBN less any shortfall for agricultural and residential buildings; balance held with internal banks (excluding uncleared effects) less any balance held for internal banks; the treasury bills; the treasury certificates; money at call held with other banks less money at call held for other banks; certificates of deposit held if not less than eighteen months to maturity; eligible stocks (the state securities) of not more than three years to maturity; and bankers unit fund.

The items of current liabilities include: current savings and time deposit accounts; certificate of deposit issued if not more than eighteen months to maturity; excess balances held for internal banks; money at call held for other banks; and balances held for external office less any balance held with external offices, ignoring net minus.

This is, as can be observed, being practised in the country. The monetary authorities (the CBN) usually stipulate a minimum level of liquidity ratio to be maintained by the banks given the premium which is attached to the liquidity of banks in relation to their stability. The usual practice is that the ratio expected is normally contained in the CBN monetary policy and credit guidelines. Besides the requirement on the liquidity ratio, the commercial banks are under obligation to maintain a cash ratio as stipulated for

a specified bank of total deposit liabilities.

The cash ratio shows the amount of cash held in a bank's till or as a balance at the CBN expressed as a percentage of the total of customers' balances in the current or deposit account. But the liquidity ratio indicates the relationship between those assets of the bank which are in money - or the assets which can quickly be turned into money - and the total balances that the customers of the bank have in their bank account.[52]

2.5.6 INSTRUMENTS OF LIQUIDITY MANAGEMENT

There are a variety of marketable instruments or securities which are available for the management of liquidity. These instruments can be invested in and rediscounted whenever funds are needed by the banks. They are termed as marketable securities because they can easily be converted into cash within a very short notice of their placement. These securities are analyzed below.

1. TREASURY BILLS

The bill is issued by the government for the purpose of raising funds for its operation. It is sold on a regular basis by the government treasury.
The bills are now issued with a maturity period ranging from ninety one days to one year. The bills are sold at a discount in denominations.

The treasury bills are virtually riskless and have secondary market where they can be sold before the maturity date. The bills offer the highest form of liquidity and a complete absence of default. Accordingly, their yields are not comparable to other securities since they are discount instruments.

2. TREASURY CERTIFICATES

The instruments are medium-term government securities maturing in one or two years. Their issue by the government treasury is meant to bridge the gap between the treasury bills and long-term government securities - the development or eligible stocks.

The instruments have higher rate of interest than that of treasury bills. They are rediscountable at the central bank before their maturity date. They offer a good medium for the merchant banks' short-term investment and they are included in the eligible assets for meeting banks legal liquidity requirements.

3. COMMERCIAL PAPERS

These are securities which are of short-term in nature. They are termed as short-term insecured promissory notes, which are issued by finance companies and large industrial firms. Their maturity ranges from three to six months and they are sold directly or through the dealers.

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As they are bearer papers, the instruments are readily negotiable in the secondary market. Interest on them are normally the same as those on certificate of deposits. The degree of their risk is related to the credit standing of the issuers.

Dealing in commercial papers is being dominated by the merchant banks in the country since they act as the agents of the companies requiring finance or funds through the use of these securities. The rates of yield on these instruments are normally higher than those of other treasury obligations.

4. BANKERS ACCEPTANCE

The acceptance is a draft - which is drawn on a specific bank by an exporter in order to obtain payment for goods he has shipped to a customer (the importer) who maintains an account with that specific bank. The importer normally instructs the bank to honour the draft at a specific future date. At the instance of this, the exporter has the option of either waiting for the maturity or sell it at a discount.

The acceptance is a short-term debt instruments with a little risk as a result of the endorsement they command from the importer and accepting bank. The interest on this instrument is the same as the yield on the certificate of deposit. They are like treasury bill sold on a discount basis.

They command less liquidity and therefore, attract yield advantage over the treasury bills.

5. REPURCHASE AGREEMENT

The agreement involves actual sale of securities by a borrower to the lender with commitment on the part of the borrower to repurchase the securities at contract prices plus stated interest rate. These agreements are usually executed in large amount of money. Returns are taxable, and the yield from the instruments is reached through negotiation between the lender and borrower.

Other instruments of liquidity management such as the inter-bank placement, certificate of deposit and unit trusts as well as the investment trusts have been discussed earlier in this chapter.

2.5.7 MANAGING LIQUIDITY CRISIS

Some options are available for the management of liquidity crisis in the banks. One of such options is the variation in the maturity of its assets, which can take various avenues. It is usually desirable to for a bank to increase the proportions of its short-term loan or short-term securities in order to minimize its liquidity risks since the shorter the maturity of these assets, the more liquidity they assume.

The other option is for the bank to improve its liquidity position by lengthening the maturity of its liabilities. This can be ensured or achieved by increasing the rate of interest offered for purchased funds. It is normally desirable to go for the short maturity funds than the long maturity funds. But there is a limit to its use.

The crisis can be managed by embarking on aggressive marketing to obtain deposits from the prospective investors. Some securities and other instruments can be issued to enlarge the base of funds generation. This results into increase in the level of purchased funds. Volatile deposits call for the liquidity management which ensures a build up of liability cushion or safety valve. This is achieved with recourse to discretionary source of funds such as the inter-bank placements.

A very painful option is the sale of assets at liquidation prices, which involves some substantial losses. This is used in an acute situation of inadequate liquidity. To guide against a run on the bank - a situation which makes depositors to rush for the withdrawal of their deposits in order to avoid the loss of the funds - banks shun the purchase of funds on the money market but resort to the sale of its assets. The other source of funds is the lender of last resort, which involves borrowing from the apex bank with which to take care of illiquid situation. This involves

some costs and problems but the banks must patronize it in order to avoid embarrassing situation of not being able to meet their obligations.[53]

2.6 INTEREST RATE REGIME AND LIQUIDITY MANAGEMENT

According to Pyle (1971)[54] posits that there are certain basic ingredients which are necessary in financial intermediation. Thus financial intermediation can only thrive: the smaller the risk premium on deposits and the longer the risk premium; the greater the positive dependence between loan and deposit yields; and the larger the standard deviation of deposit yields and the smaller the standard deviation of loan yield.

Fundamentally, therefore, financial intermediation can only become attractive to the banks if the spread between interest paid on deposit and interest charged on loans is wide or reasonable. Nonetheless, caution is normally observed in area of not mismatching assets and liabilities maturities. There is the problem of the interest rate exposure arising out of changes in the interest rate regime, which affects the earnings of the banks.

The appropriate hedge against such exposure or risk is the preparation of the cash flow statement and maturity balance sheet. The former statement is

precisely a kind of projection whilst the latter shows the present situation in terms of the cash flows position. The cash flow statement is prepared with the use of the figures of the expected cash inflows and outflows for a definite period of time. The net effect between the inflows and the outflows is the most important aspect of the statement. Such balance between the cash flows is used for planning on financial intermediation.

The maturity balance sheet portrays the maturity period of the assets and liabilities of the bank. The preparation calls for the grouping of the assets and liabilities on the basis of maturity or repricing within the period involved. The statement is termed Asset Reproced Before Liability Statement, and this mirrors appropriately the mismatch position of the bank's assets and liabilities.

It is normally desirable for the bank to determine the magnitude of the interest rate risk or exposure so as to device some control measures. The measurement takes the form of relating the percentage increase or decrease in interest rate in the economy to the difference between the total assets and total liabilities for a particular period of time. This is related to the number of days in the perceived gap between assets and liabilities.

The control involves pegging the upper limits for the positive and negative gaps for each maturity period. Based on this, the bank can plunge into the market for funds and investment within the boundaries which are deemed desirable.

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CHAPTER THREE

RESEARCH METHODOLOGY

This chapter explains the methods of data collection. In addition, it attempts to explain the various sources of data which have been used for the study. In essence, the chapter explains how the data for the study have been obtained from both the primary source and secondary source.

3.1 METHODS OF DATA COLLECTION

The study relies heavily on the survey method of data collection. The method makes use of an area selected for generalization since it is difficult to cover the whole population under study. It is conducted in such a manner as to collect the necessary data which are essential for arriving at meaningful conclusions in treasury management.

The study is based on the use of questionnaire and personal interview. The questionnaire is meant for those operators of the institutions who could not be reached or have the time to grant personal interview to the researcher. The personal observation or interview is directed at those areas of operations in terms of the normally activities involved in treasury management. The interview is directed mainly at those operators of the government treasury at various levels of government; the federal, state and local councils.

Both the questionnaire and personal interview are used for the collection of data for the primary source of information. And the secondary source of data is explained at the latter part of this chapter.

It is pertinent to stay here at the onset that the research methodology used for this study is descriptive. By implication, an attempt is made to analyze the data collected on treasury management and the impact of liquidity squeeze, which has come mainly from the external environment.

3.2 SAMPLE SELECTION

The population for this study comprises the financial institution, especially the banks and the government establishments particularly the federal, state and the local government departments and organisations. The obvious constraints in the areas of finance, number of finance institutions and the spread of the government organisations, have precipitated the use of sample.

Towards making the findings of this research work to be true generalization of the population under study, a random sample is used in selecting the banks and government organisations for the study. The type of sampling method which has been is the stratified random sampling.

The branches of the banks which are accessible to the researcher in terms of their locational advantage. Therefore, the researcher relied heavily on the data which

could be generated from these banks which are located in areas such as Kaduna, Zaria and Kano.

For the government organisations, the Federal Secretariats at Kano, and Kaduna have been selected for the purpose of generating data for the treasury management in the public sector. On the same token, some local councils in Kano, Zaria, and Kaduna have been selected with a view to generating data on the treasury management at the local council level. The two states of Kano and Kaduna have been used to gather information on the management of the treasury at the state level.

Some basic assumptions have been made as a result of the sample selection. These assumptions are that:

1. What obtains in one commercial bank is applicable to other commercial banks;

2. What obtains in one merchant bank is the same with other merchant banks;

3. What obtains in one development bank is relevant to other development banks;

4. What obtains in one state is applicable to other states of the federation; and

5. What obtains in one local council in one state is applicable to other local councils in other parts of the federation.

3.3 PROCEDURE FOR DATA COLLECTION

The data from the primary source have been collected through the use of questionnaire and personal interview.

3.3.1 QUESTIONNAIRE

The questionnaire was administered to the sample selected in the sample survey under study. The questionnaire was prepared and circulated to the officers of the banks which have been selected for the study. The officials of the state, federal and local government offices were also given the questionnaire. In fact there were two types of questionnaire; one was for the banks and the other for government organisations.

For the questionnaire design, emphasis was on the functions, organisation and the instruments of treasury management. Moreso, the questionnaire also contained areas for the sources of funds, uses of funds and the situations that could lead to liquid squeeze or crisis. Other areas in the questionnaire are the management of liquid risk, working relationship between the apex bank and the other banks, the impact of liquid squeeze, government action, the apex bank's measures on crisis of liquidity and the survival strategies of the organisations towards coping with liquidity squeeze.

The questionnaire consisted of both closed and open-ended questions. The former type of questions was meant to guide the respondents in expressing their opinions.

And the latter type was meant to allow the respondents to enjoy some modicum of freedom in answering questions without reservations. Moreso, the respondents were allowed to express their opinions freely and supplying some pieces of information which are beyond the comprehension of the researcher. The questions are not unnecessarily many in order not to discourage the prospective respondents from answering them and returning the questionnaire in good time.

3.3.2 INTERVIEW

Some respondents are normally inclined towards giving oral response instead of filling questionnaire. They find it very difficult to attend to questionnaire due to lack of interest, time, and official protocol may forbid such since it could be termed as divulging official secret.

Personal interview were conducted on some officials of the organisations under study. The interview was conducted essentially towards complementing the use of questionnaire. The researcher used the non-directive type of interview so as to encourage the respondents to talk freely on the subject under study.

The researcher interviewed the branch managers and accountants of the banks that were contacted for the study.

For the government organisations, the officials of the Federal pay offices, the branch of the Federal Ministry of Finance, the State Finance Ministry, the officials of the State Treasury and the Treasurers of the local councils were interviewed. The researcher conducted the interview personally without involving any field assistants for the study.

3.4 THE SECONDARY DATA

For any academic study, the secondary source of data is very essential especially for the review of the related literature besides providing some viable basis for the analysis of the conceptual framework of the subject matter under study.

The secondary data were obtained by using the available literature as regards the relevant texts, journals, newspapers, publications of the apex bank (CBN), annual reports and statement of accounts of the various banks which the researcher was able to lay his hands on.

3.5 SUMMARY

The data which have been used for the study were generated from both the primary and secondary sources. The primary data were obtained through the use of personal interview and questionnaire. For the secondary data, sources include texts, journal, newspapers and publications of CBN, among others.

Some difficulties were encountered in the course of generating data for the study. Out of the numerous questionnaires distributed only very few ones were filled and returned or made available to the researcher. Official policy especially within the government circle preclude some officials from responding to the researcher. The usual excuse is that they are forbidden by the general order to grant interview or even fill questionnaire of any sort.

Some officials of the banks refused bluntly to either grant the researcher interview or even attend to questionnairs. Some questionnaires were picked unfilled as the selected respondents refused to answer the questions on the questionnaire. The usual excuse from such respondents was that of lack of time and chance.

On ground of the fear of industrial espionage, some officials of the banks refused to divulge pieces of information on the management of liquidity in their organisations. The reason is simply that such information might be used against them. This, in view of the fact that the present economic situation in the country entails the spirit of the survival of the fittest; as a result of fierce competition in the banking industry.

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CHAPTER FOUR

PRESENTATION AND ANALYSIS OF DATA

This chapter of the study attempts to present the pieces of information which have been obtained from the research. As expected, the other important aspect of the chapter is the analysis of the data generated from the study. It has already been stated in the preceding chapter that the analysis is purely the descriptive; devoid of statistical methods, models and formulations.

From the data generated, the researcher attempts to analyze the reasons which have precipitated liquidity squeeze in the banking sector to the extent that some banks have been liquidated while some other ones have become distressed. A brief analysis is devoted to the factors responsible for liquidity squeeze in the government organisations.

The governmental factor is not left out in the analysis of the liquidity squeeze overtime in the country. The policy measures of the government which led to the squeeze are considered. Closely related to this consideration is the role of the apex bank (the CBN) in the treasury management as it affects liquidity squeeze and interest rate exposure.

The other aspects of the chapter have to do with the analysis of the impact of liquidity squeeze on the treasury and the survival strategies adopted by the banks to manage the squeeze.

4.1 REASONS FOR LIQUIDITY SQUEEZE

There are varied and numerous reasons which can precipitate liquidity squeeze and liquidity crisis. These factors are embedded in the external environment of the organisations (the banks), and as such they have little or no control over them.

4.1.1. LIQUIDITY SQUEEZE IN BANKING SECTOR

The reasons or factors responsible for liquidity squeeze and subsequently liquidity crisis in the banks are analyzed below.

1. INTRODUCTION OF STABILIZATION SECURITIES

According to the practitioners of the banking operations, the mopping up of excess liquidity started from April 1989. The use of stabilization securities started from August 1990 when the Central Bank of Nigeria embarked on mop up exercise by issuing out stabilization securities which saw the withdrawal of the sum of one billion naira (₦1 billion) from the banks' vaults to the stabilisation account. The explanation by the CBN was that the banks were having excess cash and short-term money market instruments which can be converted into cash at short notice.[1]

The stabilisation securities are a kind of IOU instruments issued by the CBN to banks whose liquidity position are higher than the prescribed by the monetary authorities.

The value of the security which is issued to each bank is equal to the perceived excess cash and such amount is automatically withdrawn from the account of the bank concerned; its account with the CBN.

The issue of it has becoming without prior notice. Therefore, it has the effect of distabilising the liquidity position and the operations of the banks. Traditionally, the securities are issued out as measure to penalise banks that have exceeded their liquidity ratio but they are now being issued on a regular basis on all banks.

2. WITHDRAWAL OF GOVERNMENT FUNDS FROM BANKS

The government gave a directive in April 1989 to the CBN through the money circular that all the government and parastatal funds should be withdrawn from all commercial and merchant banks to the CBN. A sum of four billion naira (₦4 billion) was withdrawn from the banking system in the exercise. The amount was estimated to be almost thirteen percent (13%) of the aggregate deposits in the banking system.[2]

The policy drastically reduced the amount of funds available to the banks in the business of financial intermediation besides having to meet the customers' demand through withdrawals of their deposits. As a result of the grave consequences on the liquidity position of the banks, they have to device several strategies towards coping with the squeeze.

3. RAISE IN THE PAID-UP SHARE CAPITAL

In the month of October 1991, the apex bank (CBN) had directed that banks should raise up their paid-up capital. The directive was that the capital base of twelve million naira (₦12 million) for the merchan banks should be raised to the sum of forty million naira (₦40 million) while that of the commercial banks from twenty five million naira (₦25 million) to fifty million naira (₦50 million[3]).

The banks were given a dealine within which to implement this directive. The fallout from this measure was the suspension of the inter-bank lendings by the big and well established banks. The suspension put most illiquid, cash strapped banks in jeopardy as the bouyant ones adopted discriminatory attitude against them. The suspension,as a chain reaction, led to the increase in the inter-bank lending rates. And moreso, the measure led to the disappearance of shor and medium term funds, usually recalled by the creditors after thirty, ninety or one hundred (30, 60, 120) days.[4]

4. INCREASE IN MINIMUM LIQUIDITY RATIO

The minimum liquidity ratio for the banks was thirty percent (30%) for the commercial banks and twenty two point five percent (22.5%) for the merchant banks in 1990. But in 1994, the CBN monetary guidelines changed the ratio to thirty percent (30%) for both the merchant banks and commercial banks.[5]

The cash reserve requirement prescribed for the commercial banks in 1990 was based on certain class in which the banks belong. These banks were classified into four classes using the volume of the total deposit liabilities. The merchant banks before 1990 were only required to comply with the liquidity ratio, but in 1990 they were also required to maintain a cash ratio of five percent (5%)[6]

5. ABOLITION OF GRANTING OF LOANS AGAINST FOREIGN GUARANTEE

The government decided to abolish foreign guarantee and currency deposits as collateral for naira loans in 1989. The implementation of the abolition order led to a reduction of about three billion naira in credit to the private sector by the banking system.[7]

The order made granting of loans and advances against foreign guarantees and foreign backed by letters of credit to become illigal. These instruments are internationally accepted as a means of raising funds but the government still went ahead to abolish it. As it were, the short time within which the banks were required to comply could not be observed by some banks and their accounts were debited as a punishment. This act of the CBN plunged many banks into financial quagmire. The fallout is the abnormal rise in the inter-bank lending rates.

6. INTRODUCTION OF PRUDENTIAL GUIDELINES

The apex bank introduced the prudential guidelines in (1990) on lending portfolio of the banks.

The implementation requires the maintenance of adequate provision for the bad debts affected the fortunes of the banks.

The combined effects of this measure and other various regulatory instructions such as the payment of interest on demand deposit accounts have been responsible for the scarcity and high cost of funds for the banks. The economic situation coupled with the competitive nature of the banking industry has heightened the competition for funds.

7. OPERATION OF FOREIGN EXCHANGE MARKET

The advent of the Structural Adjustment Programme (SAP) in 1986 was accompanied by various monetary policy measures aimed at revamping the economy of the country.

One of such monetary policy measures is the introduction of the Second-Tier Foreign Exchange Market (SFEM). Consequent upon this development, the apex bank (CBN) requested banks to back up their foreign exchange demands at the market with naira equivalent. Moreso, there was the abolition of the special foreign exchange deposit account from the banks. The combined effect was the worsening of the banks financial predicament and denied them access to foreign exchange at CBN.

8. INCREASE IN NUMBER OF FINANCIAL INSTITUTIONS

In the wake of the advent of the Structural Adjustment Programme, the CBN introduced the Second-Tier

Foreign Market. In addition, there was the deregulation of the financial system.

The situation gave birth to many finance houses and banks such as the commercial banks and the merchant banks. Besides, the government midwived the birth of the People's Bank with so many branches all over the country. As if the number of banks was not overwhelming, the government allowed coming on board a number of Community Banks, which are purely unit banking but their likes are found everywhere in the country.

The whole scenario brought about fierce and cut throat competition within the industry. According to CBN report, there were 58 commercial and 48 merchant banks in the country as at the end of the year 1990. These banks have 2013 branches. All these banks compete for loanable funds with 80 stock brokers and 92 bureaux de change. The number of commercial banks rose to 67 while that of merchant banks became 55 in the year 1993.[8]

The number of the financial institutions continued to rise over the years. In the year 1994, there were 874 community banks, 275 branches of People's Bank, 3 discount houses, 279 primary mortgage institutions, 290 finance companies and 103 insurance companies in the country.[9]

The abnormal rise in these financial institutions resulted into scarcity of loanable funds. Moreso, the interest rates on funds became unimaginable as the unofficial rates reign supreme. The situation gave rise

to financial distress of some banks while some others have since been liquidated by the apex bank.

MISCELLANEOUS FACTORS

There are other factors which led to the situation of illiquidity or liquidity squeeze and crisis in the banking industry.

One of them is the call by the apex bank for the lodgement of deposits in respect of external payment arrears outstanding. The other factor is the deregulation of the interest rate regime in the country. This has the effect of making the interest rates to become so sky-rocketted that it was very difficult for some banks to secure funds from investors. Moreso, the inflationary trend has been assuming dangerous dimension to the extent that the business of financial intermediation - the prime of banking activities - became very discouraging, if not a nightmare.

There is the problem associated with the cash reserve requirement. The apex bank made such ratio to be related to the cash deposits out of the total deposit of the investors and depositors alike. The other point is the inconsistency in the monetary policy guidelines of the government. Today, it is guided deregulation, yesterday it was regulation and deregulation, but who knows what the government will come out with in the next year monetary policy guidelines? The scenario has left the banks more confused as regards their primary of financial intermediation; especially sourcing for and investing the funds.

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4.1.2 LIQUIDITY SQUEEZE IN PUBLIC ORGANISATION

A brief analysis is dwelt with under this section in terms of the consideration of the probable factors that normally lead to liquidity squeeze and liquidity crisis. The analysis is brief since it is only the factors that are enumerated hereunder.

First and foremost, liquidity sequeeze can arise out of a shortfall in the expected revenue of the government. In the case of the revenue being generated from petroleum, the slide in the prices of crude oil of various grades can distort the expected revenue of the government. The pricing of crude oil is susceptible to the situation which obtains in the international market with little or no influence of the petroleum producing countries, of which Nigeria happens to be one.

The other factor is the shortfall in the expected revenue from taxation. There are the reasons of tax evasion, tax default, falsification of records and non-remittance of the amount of income tax on salaries of the workers. In the recent times, the Kaduna State Government has been reorganising the machinery of revenue generation as a result of the huge amount of tax revenue which has been outstanding against individuals and organisations in the state. The latest figure declared by the State Government to be outstanding on such source of revenue is about one billion naira - ₦1 billion.

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At the state level of government, the factors which normally give rise to liquidity problem, as discovered

from the study, are as follows:

1. A great deal of revenue is being generated from one main source (the petroleum), which happens to fall under the control of the federal government.

2. The flow of funds may be impeded or redirected since money trickles from the level of the federal government to the parastatals and then to the states. The funds do not normally flow in a predictable manner.

3. Unexpected changes in the availability of funds, which cause disruptions, losses, and cash strap.

4. Funds dry up as a result of limited sources of revenue being exploited by the states.

5. The release of funds in form of grants is characterised by unvertainty, irregularity, vagaries in timing and frequency as well as abruptness in the priorities of the federal government.

6. Incessant increase in the salaries and allowances of the workers without matching grants with which to take care of the increase in terms of the extra cost to the state government.

7. The imposition of unecessary projects on the state government without any funds coming from the federal government to execute them.

8. Engagement in white elephant projects by the state government which might arise out of sheer political expediency.

At this level of government, the combined effects of the factors have led to the non-payment of salaries and allowances and in some other cases, the retrenchment of a large number of workers out of the existing workforce. In the past, the state governments have been made to suffer some financial embarrassment to the extent that their workers went to the extent of engaging in work to rule and outright strikes, which paralyzed the governmental activities.

At the local government level, there are varied factors which have been responsible for liquidity squeeze and crisis. These factors are as enumerated below.

1. Irregular and untimely release of statutory allocation to local governments.

2. Unnecessary delay and cuts and alterations in the local government estimates by the state governments.

3. Non-payment of the state contribution of internally generated revenue to the local governments.

4. Spending limit imposed on the councils.

5. Encroachment of state governments on local government sources of revenue.

6. Imposition of unplanned expenditure on local governments by federal or state governments without being accompanied by adequate grants.

7. Untimely approval of the annual estimates of local government by the state governments.

8. Meagre amount of funds from the statutory allocations to local governments.

From the study, it was discovered that the local councils usually encounter financial difficulties in the face of untimely release of their statutory allocations coupled with the non-payment of the state contribution of internally generated revenue.

4.2 GOVERNMENT POLICY MEASURES

The government has been playing a crucial role in the events that led to the situation of liquidity sequeeze in the banking industry. The government exerts strong influence on the operations of banks in the economy. From time to time, the government comes out with varied policy measures in the area of monetary guidelines which tend to regulate the operations of the banks.

The usual policy measures are contained in the annual budgets and various monetary circulars which are published and subsequently passed to the banks through the apex bank.

The introduction of the Structural Adjustment Programme (SAP) as introduced in 1986 brought some measures that have worked against the fortunes of the banks. The aspect of the foreign exchange market (SFEM) brought with it unhealthy competition for loanable funds with which to bid for foreign exchange. It also led to the birth of numerous financial institutions, which has affected or revolutionalised the operations of the banking industry.

Another aspect of SAP is the deregulation of the financial operations. Of interest is the deregulation of the interest rate regime which caused abnormal rise in the interest rates on loanable funds. Moreso, the banks were charging different interest rates on loanable funds, which made it very difficult to mobilise funds for effective and efficient banking operations. The consequential effect is the crash of some financial institutions including banks.

The singular policy measure which has the most devastating effect on the operations of the banks is the withdrawal of the public accounts and their funds from the banks in April 1989. As has earlier been stated in this chapter, the policy made so many banks to become financially crippled to the extent that they could not meet their financial obligations. Some of the banks that could not refund the outstanding deposits of the government and parastatals accounts were punished by the apex bank. The policy caused the banks (both

commercial and merchant banks) to lose a staggering amount of four billion naira (₦4b), almost thirteen percent (13%) of their aggregate deposits.

Subsequently, the government went ahead to direct that certain existing practices in the banking industry should be discontinued with. These measures include abolition of granting of loans against foreign guarantee and letters of credit, introduction of prudential guidelines, directive for the lodgement of deposits in respect of external payment arrears outstanding, and increase in the minimum cash reserves ratio of the banks with the apex bank.

Another important policy measure which has grave implications for the banks is the directive that banks should increase their capital base - the share capital - with a deadline that could not afford the adequate time within which to mobilise funds. The directive led to the suspension of inter-bank lendings by the big banks, discrimination in the inter-bank lending, increase in the rates of inter-bank lending, and the sudden disappearance of short and medium term funds from the money market.

In discussing the policy measures of government that led to the liquidity crisis, mention must be made of the **stabilisation** securities. The securities are administered largely by the apex bank to mop up excess liquidity in the banks' vaults.

4.3 THE INFLUENCE OF CBN ON TREASURY MANAGEMENT

The Central Bank of Nigeria (CBN) is the apex bank in the country. It occupies the position of the regulatory body for the financial institutions in the economy. The influence of this bank on the other banks, therefore, is not contestable.

Over the years, the apex bank has involved itself with measures which considered necessary in regulating the operations of the financial institutions in order to ensure the health of the economy. These measures have gone a long way in influencing and in effect regulating the management of the treasury in the various banks.

Treasury management should be seen as an operation which centres on liquidity management. The liquidity management takes care of sourcing and investing loanable funds. And this is the prime operation of the various banks, which revolves around financial intermediation in the economy. For the liquidity management to be considered in the first instance, there must be funds which have to be mobilized through deposits, inter-bank placement or lending and money at call and short notice. The other aspect is the use to which the funds are put. There is in the areas of loans and advances, equipment leasing, investment, purchase of marketable securities, rediscounting of bills, meeting demands of customers through withdrawals, repayment of borrowed funds, and placements with other banks. All these operations in treasury management cannot be carried out without due

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consideration to the policy measures on monetary guidelines which are normally issued by the apex bank.

Fundamentally, therefore, the operations of the treasury management in the banks come under the directives of the Central Bank. All the directives or monetary guidelines which the CBN does issue are meant to guide are direct the course of operation in treasury management. Such directives or guides of CBN indicate how funds should be sourced, and the way commitments of such funds are dictated by such policies. Largely the issues of liquidity, interest rates and monetary guidelines generally fall under the ambit of the apex bank's monetary regulations and controls.

The actions and reactionary functions of the CBN constitute a major variable in the external environment of the banks. These regulations are normally double-edged swords; carrying both threats and opportunities for the banks. Considering the liquidity mop-up of 1989 as far as liquidity management was concerned, it had a lot of threat for some banks and for others, it was a viable opportunity to garner more fortunes. The deregulation of the interest rate regime made some banks to scoop much fortunes while to the others especially the position of the less viable ones had to be put in jeopardy.

The apex bank adjusted its minimum rediscount rate towards indicating the direction of the interest rate regime in 1987 as a result of the government's intention

to allow the cost of capital to be determined by the market forces of the demand for and supply of loanable funds. Within the same year, the apex bank abolished all direct controls on interest rates and adjusted the minimum rediscount rate upwards. This resulted into cut-throat bidding by banks at the foreign exchange market. The CBN had earlier on (in 1986) engaged in direct control of the domestic money supply, which led to the withdrawal of about four billion naira (₦4b) from circulation; such amount was reserved by the banks to fund imports. This action of the CBN had the effect of depleting the quantum of funds as available to the banks in liquidity management.[10]

The influence of the CBN on treasury management was also felt when it carried out the directive of the government that all the funds of the government ministries and parastatals be withdrawn from the banks. The policy was largely blamed on the CBN as it was regarded as the culprit in terms of the advice given to the government that resulted in such policy measure. It was on record, as has been pointed out earlier in this chapter that the sum withdrawn from the banks on the strength of such directive was almost one fifth of the total deposits with both the commercial and merchant banks. This tight monetary control was believed to be the handiwork of CBN.

There are times when the CBN evolved some policies which are not inimical to the fortunes of the banks. Nonetheless, such actions still influence the treasury management of the banks. In December, 1987, for instance, the CBN reduced the minimum rediscount rate with the sole

intention of encouraging investment through obtaining loans from the banks. This also affects the operations of the treasury of the banks. It encouraged the banks to favour the small and medium scale industries in their disbursement of funds for loans and advances. Predictably, the CBN made an upward revision of the rediscount rate in 1987. This also affected the operations of the treasury management in the banks.

In most cases, the apex bank does not pass any policy measures that are meant to favour the banks. The CBN, without taken the interest of the banks into consideration, came up with a number of measures which have devastating effect on the liquidity of the banks; all in 1989. The apex bank raised the liquidity ratio above the existing level. In addition, the CBN decided to include Commercial Papers and Bankers Acceptances in lending as part of the indices used in computing the credit ceiling of banks. These measures took some toll on the banks' liquidity. Another measure is the pegging of dividend declaration, making it conditional on a bank's proven capital funds adequacy in terms of the maintenance of a one to twelve ratio between the bank's adjusted capital funds and the total loans and advances.

There is the use of stabilisation securities for the regulation of the money supply in the economy. The securities are being used regular to mop up the so-called liquidity of the banks. By using it as a mop-up strategy on excess liquidity, the banks' liquidity position is being subjected to some vicissitudes and vagaries as

as the management of their treasury has become very difficult.

4.4 THE IMPACT OF THE SQUEEZE ON TREASURY MANAGEMENT

The impact of liquidity squeeze on the banks' vault has been very devastating to the extent that there were no funds in their treasury or vaults to manage any longer. Consequently, the banks were subjected to all manners of problems, which range from distress, total failure, liquidation, changes in the system of operations to the outright takeover by the apex bank.

The crisis as experienced by the banks in terms of the scarcity of loanable funds revolutionalized the operations of their activities. The crisis led to the demise of the traditional arm-chair banking. And the operators of the banks started engaging in aggressive marketing of their products, cut-throat competition and aggressive mobilisation of loanable funds to meet their obligations to the depositors.

Some innovation was introduced into the business of bank operations. In order to attract customers and depositors alike, the banks introduced the computerisation of their operations. The aim is to offer quick service to their customers by shortening the span of time of cashing cheques, checking for balances in the accounts of customers, processing of cheques, retrieval of records (or data) as well as calculation of interest on deposits.

The use of stabilisation securities, which started from the 1989 and continued to date, has contributed in no small measure towards making some banks to become financial distressed. According to the operators of the banks, stabilisation securities are now being classified as risk assets, which consist of net loans, fixed assets and other assets which carry the risk of default since banks cannot get them to meet urgent cash requirement. Moreso, funds cannot even be assessed as and when due as a result of the continuous rollover of the stabilisation issues by the apex bank.

The deregulation of the financial system paved way to the phenomenal growth of banks as all types of investors who have surplus funds to throw about entered into the banking system. The behaviour of these new generation banks made the apex bank to engage in stringent monetary control, which subsequently led to financial distress of some banks. The unpredictable monetary policy environment of the apex bank led to the erosion of the assets base and capital inadequacy of the banks, management incompetency - since the operators were left more confused than ever - and the loss of confidence by the public on the banking system.

The apex bank engaged in cleaning up exercise that led to the imposition of some sanctions on the so-called erring banks. These banks are termed erring because they were assumed to have behaved in such manner that contributed in pushing other banks into distress. The reasoning is that such erring banks were indebted to some other banks

thus causing them to become financially distressed whereas they (the debtor banks) were adjudged healthy.

The issues of stabilisation securities led to the banks' funds being held with the apex bank which is about three times or more than the total shareholders funds. As revealed by the bank operators, the CBN holds not less than twenty eight billion naira (₦28 billion) in stabilisation securities. This results into making only banks with large deposit base to survive the erosion on their resources, and the valnerable ones have crashed out of business. The permanent nature of the stabilisation securities issues poses grave consequences for the bank's since the issues normally exceed a bank's free capital; a measure of the bank's shareholders funds not covered by the fixed assets. The use of these securities has been blamed by the bank operators as largely responsible to the failure of some banks.

Some of the distressed banks have been liquidated by the apex bank. The banks so liquidated were not just from either the commercial sub-sector and the merchant sub-sector of the banking system. Some of the liquidated banks were commercial banks while others were merchant banks. The issue of failure led to the loss of deposits by the customers and the shareholders funds. The customers of other banks became panic - striken since their believe was their own banks could be liquidated just like the other ones that have failed. Some customers went to the extent of withdrawing their deposits from the banks while leaving only some small amount in their accounts.

The regulating authorities are not helping matters either. This, in view of the fact that each depositor is only entitled to a paltry fifty thousand naira (₦50,000) regardless of the amount of deposit or the credit balance in the account. This is the case since at the instance of a bank's failure or liquidation, the CBN appoints the Nigerian Deposit Insurance Corporation (NDIC) as liquidators whose main duty is to see to the orderly winding up of the bank. But the NDIC is in the circumstance both a liquidator and an underwriter and has liability of up to fifty thousand naira (₦50,000) on each depositor. This can only make those having surplus funds to seek other avenues of investments instead of depositing such funds with the banks of whose returns and the repayment of the equivalent sums are uncertain. And at best, the recovery of the main deposits and the accrued margins can be forfeited in the event of bank failure. Moreso, the other implication is the run on the banks; a panic measure whereby the customers are to rush to withdraw their funds from the banks because of the spate of distress and outright failure of some banks.

The reaction of the public and the depositors alike as a result of the liquid crisis in the banking industry brought some serious impact on the banks. Such reaction can be measured in terms of the confidence cost in the banks, the withdrawal of deposits, degeneration of the banking habits of the people and the clamour by some segment of the enlightened public for the merger of some banks. It is instructive to note that some banks have

been taken over by the apex bank. As a result of such move, the management of such banks has been sacked besides the dissolution of their boards. All these measures have made nonsense the management of the treasury of such banks.

4.5 SURVIVAL STRATEGIES OF ORGANISATIONS

The analysis in this section is restricted to the banks. The survival strategies refer to the measures adopted by the banks towards coping with the liquidity squeeze and crisis as regards treasury management.

As we have stated in the preceding section, the banks could not just maintain lucklustre attitudes towards the crisis situation in which they found themselves as a result of the incessant bombardment by the apex bank. One strategy as adopted by these banks is the introduction of computers in their operations. And as a result, the accounts of the customers have become computerised, thus paving way for quick services, shortening of the length of time for paying customers through cheques, easy retrieval of records of accounts and prompt attention to customers generally. The rationale behind this innovation is to attract and retain customers so as to have access to their surplus funds.

Over the year, the banks realised the benefits which can accrue from the business of unit trust and investment trusts. Therefore, to attract customers with funds to invest, some banks established their own subsidiaries to

handle such business on their behalf. The innovator that blazed the trail is the ICON Merchant Bank, who has successfully managed until trust to the admiration of other banks. A usual feature is the annual general meeting of the unit trust holders during which the results will be declared to the benefits of the existing investors as well as the prospecttive ones. Other banks have joined in the business of unit trusts and investment trusts as means of mobilising funds for their treasury.

The banks engage in the introduction of all sorts of products towards mobilising funds for their treasury. These products include upfront payment of interests on deposits, payment of brokerage on fund mobilisation even to bank staff, payment of attractive and competitive interest rates on deposits, introduction of deposit cards (UNICARD, UBACARD, among others) for the use of the depositors, offers on deposits in the areas of insurance cover, health or hospital bills payment, scholarships for the children of depositors, and accident benefits, and other attractive products which the banks have considered necessary in the bid to mobilise and compete for deposits from the investors.

The other strategy adopted by the banks is the payment of unofficial rate of interest on deposits. Some operators of the banks contended that some banks have no choice than to engage in such an unhealthy practice. The practice is known in some banks as "under the table interest or premium" on deposits. This is being practised by those

banks in dire need of funds; being compelled to engage in such unethical practice by paying higher interest or premium on deposits in outright negation of the ruling rate or prevailing interest rate. By implication, such banks do source for their funds through the offer of under the table charges to those who are ready to borrow. In order to recoup their cost of funds, they have no choice other than resorting to such practices.

Some banks adopted the strategy of the diversification of deposit base. In some cases, the emphasis was shifted from government and parastatal funds to wealthy individuals and institutional investors. Moreso, some banks concentrated on the oil companies with some attractive offers with which to get their funds for their treasury. The other device is the investment of high proportion of the bank's funds into short-term securities such as treasury bills, treasury certificates, money at call and at short notice as well as inter-bank placements. This conforms with the asset side liquidity management. Moreso, some banks put much of their funds in liquid assets since other liabilities which formed a decent percentage of the funds available for operations are very volatile.

Another strategy is the cautious watch over granting of loans and advances. There was outright reduction in the amount granted as loans and advances to customers. The ideal is to maintain a reasonable ratio of loan to deposit so as to guarantee the availability of funds with which to meet the customers' demands through the withdrawals of their deposits. Loans and advances can

command high income but there are risks associated with them. It is usually desirable, as contended by the operators of the banks, to sacrifice income for liquidity given the current situation in the country.

All the above measures as combatant strategies for survival have contributed towards ensuring that some banks survive liquidity crisis and stay in business.

FOOTNOTES TO CHAPTER FOUR

1. Okafor, K. (1991); "CBN Withdraws ₦500 million from Banks," Business Times, Lagos, May 27.

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7. Abdulwahab, op. cit.

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9. CBN Annual Report for the year ended 31st Dec. 1994, PP. 35, 36, & 50.

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CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATION

This chapter summarises the work and takes care of the concluding remarks. Besides, it contains the suggestions of the researcher in the area of recommendation as regards the management of the treasury in the period of liquidity squeeze and crisis.

5.1 SUMMARY

The study has the main focus on the management of the treasury both in the financial institutions and the government organisations. Moreso, it attempted to analyze the impact of liquidity squeeze on treasury management most especially in the banking industry. The emphasis has been laid on the sourcing and uses of funds, situational variables that can lead to liquidity squeeze and the survival strategies adopted by the banks with which to withstand the crisis and stay in business.

The management of the treasury concerns the sourcing, disbursing and investing of funds in banks, finance houses, government establishments, institutions and corporate entities generally. The hallmark of treasury management revolves around planning for and controlling of funds towards ensuring that the funds are readily available when required, besides the judicious and efficient utilization and allocation of such funds. Hence, efficient management of the treasury planning for the sourcing and utilization of

funds, controlling the allocation and disbursement and ensuring prudent management of the available funds.

The fundamental objective of treasury management harps on the need to guide against running out of funds, holding excessive cash and keeping watch on the disbursement and utilization of the available financial resources. Such is very necessary towards ensuring the survival, growth, taking care of financial obligations and investing cash in both short and medium ventures. Particularly in the banks, managing the treasury involves hedging against financial embarrassment which can arise out of cash strap situation. Moreso, it is necessary to ensure the minimisation of costs and maximisation of investment income within the overall liquidity needs of the banks.

Management of the treasury in government circle centres on the sourcing for funds, collection of the approved rates and charges and disbursement of the available funds based on the appropriate heads and sub-heads, and necessarily on the strength of the approved authority or warrant to incur expenditure. It also takes care of the control and monitoring of government expenditure and management of the approved fiscal and monetary policies.

As we have discovered from the study, the major source of funds for the banks is the depositors from the investors. Other sources include loans, inter-bank borrowings and loans from the apex bank, which is normally the last resort.

The deposits come in the form of current accounts, savings, time deposits, and inter-bank placements, among others. The banks strive to increase their deposits through all sorts of attractive offers to the investors and competitive and aggressive advertising.

The various uses to which the banks commit their fund, as we have discovered from the study, include investment in viable ventures, equipment leasing, purchase of treasury bills and certificates, discounting of bills, loans and advances, statutory reserves, cash reserves, purchase of fixed assets, putting up structures to house their headquarters and some branches, procurement of plants and equipment, and retirement of liabilities. Other uses include payment of dividends and meeting other commitments incidental to their operations.

The government organisations source their funds through revenues generated through the instruments of: taxation, rents, investments, royalties, gains, fees, fines, duties, loans, allocations, and proceeds from commercial activities. The various use for the funds include the capital and revenue expenditure. The items for such expenditure include education, health care delivery, defense, maintenance of law and order, agricultural development, construction and maintenance of roads, water and electricity, communications, transportation, establishment of industries and development of motor parks, shopping centres, among others.

Liquidity management is the core of treasury management. The essence of liquidity is to enable an organisation take care of its commitments and invest in instruments that are readily marketable or those that can mature in a short time. The management of liquidity is normally influenced by the policy measures of the government and those of the apex bank (CBN).
The interest rate regime also affects liquidity.

5.2 CONCLUSION

Since the advent of the Structural Adjustment programme (SAP) in 1986, the banks have been made to be grappling with incessant bomboardment from both the government and the apex bank. One major feature of SAP is the deregulation of the financial system. Such action of the government has resulted into untold hardship for the banks as regards liquidity management.

The banks have been subjected to all manners of monetary policy measures which have affected their liquidity and treasury management. These policy measures include the use of stabilisation securities for mopping up excess liquidity, frequent changes in the liquidity ratios, the raise in the capital base of the banks, withdrawal of government and parastatal funds from the banks, introduction of the foreign exchange market and increase in the minimum cash reserves ratio. Others are the introduction of the prudential guidelines and the

registration of more banks, finance houses, insurance companies, mortgage institutions and discount houses. All these measures have been responsible for the liquidity squeeze and crisis as experienced by the banks.

The apex bank and the government have never played less role in the liquidity crisis. The government formulated the various monetary measures for the interest of the overall growth and development of the economy. The apex bank (CBN) being the regulatory authority in the banking sector has been implementing such monetary policy measures faithfully, but to the detriment of the banks' fortunes.

The impact of such policy measures has come in the areas of: the absence of funds in the banks' vaults; financial distress, total failure or collapse of some banks, and outright liquid tion of some of the banks. The banks have come constant placement of funds in form of stabilisation securities which are risky assets since the banks cannot get the funds to meet urgent cash requirements. The other form of impact is the erosion of the asset base of the banks and capital inadequacy, management incompetency, and loss of confidence in the banks by the public and the investors.

For the banks, they have to engage in all sorts of strategies, some healthy while some are very unethical and inimical to the economic growth and development of the country. Such strategies include: the introduction of computers into their operations; venturing into the

business of units trusts and investment trust; the use of attractive offers to lure the depositors; the payment of the so-called "under the table interest or premium on deposits; and the abnormal interest rate on loans and advances.

Furthermore, some banks adopted the system of deposit diversification by shifting from government funds to the deposits of oil companies, wealthy individuals and institutional investors. Some other banks maintained cautions watch over their loans and advances by maintaining a reasonable ratio of loan to deposit so as to guarantee the availability of funds to take care of urgent needs.

5.3 RECOMMENDATION

There are numerous variables that normally affect the management of the treasury in both the public and private sectors. Such variables which come through the policy measures of the government and the apex bank are outside the influence or control of the banks. But they can still evolve healthy strategies to hedge against the adverse effects of liquidity crisis. Hence we offer some suggestions which are considered ideal for managing and hedging against cash strap situation.

1. Cash balance can be invested in securities whose maturity correspond with some anticipated payments in future. This involves investing in a portfolio of liquid assets; the marketable securities.

2. The banks should make it as a matter of policy to be reviewing its liquidity position on a weekly basis. This can be practised without problem since the branches of the banks can be compelled to be remitting returns on a weekly basis.

3. The banks have to ensure the maintenance of adequate ratio of loans to deposits, with a minimum amount of funds committed to loans and advances. The remaining amount out of the total deposits should be used for the treasury bills and certificates and bill discounting so as to have the funds readily available for urgent needs.

4. There is the need for the banks to be maintaining a reasonable amount of overhead costs in their operation. This can be effected through rationalisation of operations, cutback in the number of branches, rationalisation of staff strength and cutting down the expenditure on utilities.

5. Both the government and the apex bank have to maintain some degree of consistency in their bid to regulate the activities of the financial institutions. It is not healthy to engage in regulation, deregulation and the so-called guided deregulation. All these are subject to abuses by the apex bank and as such the government to be making use of technocrats (of great repute and integrity) in formulating monetary policies.

6. The CBN has to chart a stable course for the excess liquidity mop up instead of moving from one policy measure to another one which at best would confuse the operators of the financial institutions. Afterall the core of the staff of the bank is supposed to be made up of seasoned bankers and reputable technocrats.

7. The banks should all engage in appropriate strategies that encourage people to keep their funds with them instead of engaging in advertisement and publicity which only appeal to the wealthy segment of the society. The confidence of the public in the banking sector has been eroded over the years. And it is left for the operators to come up with the appropriate strategies which can help towards redeeming such bad dent.

8. The government should borrow leaf from the other countries as regards the practice whereby the government fund its public sector programme by the establishment of an auction system for its debt instruments so that banks and other participants are allowed to bid competitively for such instrument.

9. The government should ensure that the idea of just granting licence to influential individuals without considering their professional background, which might not be relevant in the business of banking.

10. There is the need for the government and the CBN to review the practice of allowing the depositors to collect only ₦50,000 regardless of their individual amount of deposits. The ideal practice is for the authorities to fix a certain percentage which will be related to the amount of deposit in terms of payment to the depositors in the event of bank liquidation.

11. The authorities should empower the NDIC to be arresting and prosecuting the loan beneficiary who has defaulted in repayments so that the innocent depositors will not suffer unjustly. The practice of allowing the loan defaulters to go scot free while the innocent depositors suffer losses should be discouraged.

12. The amount of the stabilisation securities on a bank should not be allowed to be more than the bank's capital. This is the shareholders funds which might not pose problems for the banks.

13. The various levels of government should enlarge the revenue base so that they can generate more funds to cater for their needs.

14. The federal government should be releasing the funds for the statutory allocation to other levels of government so as to help ease their liquidity problems.

15. There is the need for the state governments to stop the practice of not releasing their contribution out of the internally generated revenue to the local councils so as to ease their liquidity problems.

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QUESTIONNAIRE

(FOR BANKING INSTITUTIONS)

1. Type of Bank (please tick)

   (a) Commercial Bank
   (b) Merchant Bank
   (c) Development Bank
   (d) People's Bank
   (e) Community Bank.

2. Describe briefly the organization of the Treasury Function in your Banks:-

   _____

   _____

   _____

   _____

3. Mention the various sources of funds to your Bank:-

   i. _____

   ii. _____

   iii. _____

   iv. _____

   v. _____

4. What are the various monetary policy measures which the government has used since the advent of SAP?

   i. _____

   ii. _____

   iii. _____

../2

iv. _____

v. _____

5. Mention the various uses of funds in your Bank:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

6. What are the various sources of liquidity squeeze on the Banks over the years?

i. _____

ii. _____

iii. _____

iv. _____

v. _____

7. Mention the various strategies adopted by your Bank to cope with liquidity squeeze:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

8. Describe briefly the main impact of the liquidity squeeze on Treasury Management in your Bank:-

_____

_____

_____

_____

../3

9. What are the various types of deposits which the customers have with your Bank?

i. _____

ii. _____

iii. _____

iv. _____

v. _____

10. Name the various types of customers that patronize your Bank:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

11. List the main sources of large deposits from the customers of your Bank:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

12. Describe the role of the CBN in the liquidity squeeze

_____

_____

_____

13. Describe the role of the Government in the liquidity squeeze:-

_____

_____

_____

_____

QUESTIONNAIRE

(FOR GOVERNMENT ORGANISATIONS)

1. State of the Local Government: _____

_____

2. Mention the various sources of revenue to your State/ Local Government being generated locally:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

3. What are the sources of Federal Government Subvention to the State/Local Government?

i. _____

ii. _____

iii. _____

iv. _____

v. _____

4. Mention the Sources of Control over Expenditure:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

5. What are the sources of joint revenue with the State?

i. _____

ii. _____

iii. _____

../2

iv. _____

v. _____

6. List the sources of joint revenue with the Federal Government:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

7. What are the sources of the Expenditure for the Government in your area?

i. _____

ii. _____

iii. _____

iv. _____

v. _____

8. List the existing constitutional Provisions over Expenditure:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

9. List the existing Constitutional Provisions over sources of Revenue:-

i. _____

ii. _____

iii. _____

../3

iv. _____

v. _____

10. Mention the sources of liquidity Problems which have confronted the Government in your area:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

11. What are the sources of liquidity problems which the Government can experience?

i. _____

ii. _____

iii. _____

iv. _____

v. _____

12. Mention the Problems arising from the liquidity Problems:-

i. _____

ii. _____

iii. _____

iv. _____

v. _____

13. What are the measures adopted to cope with the liquidity problems?

i. _____

ii. _____

iii. _____

iv. _____

v. _____

../4

14. Describe briefly the organisation of your Treasury Department:-