THE ORIGIN, GROWTH AND DEVELOPMENT OF BANKING IN NIGERIA

The banking system in Nigeria has since independence undergone radical changes. Banking in Nigeria developed from an industry, which at the time of independence in 1960 was essentially dominated by a small number of foreign banks into one in which the public sector ownership of banks predominated in the 1970s and 1980s; and in which the Nigerian private investors have played an increasingly important role since the mid-1980s. The banking industry also went through phases of regulation and deregulation. In the 1960s, extensive government intervention characterized the financial sector. This was intensified in the 1970s. The objective was to influence the efficiency of resource allocation and promote indigenization. Since the adoption of the Structural Adjustment Program (SAP) in 1986, the financial sector has been liberalized and measures have been put in place to enhance prudential guidelines and tackle bank distress.

The different licensed banks in Nigeria fall into different generations. These “generations” of banks fall into the five phases of bank licensing.

(i) **First generation**: These were banks that were licensed before Nigeria's independence in 1960.

(ii) **Second generation**: These were banks licensed between 1960 and 1980.

(iii) **Third generation**: Banks licensed between 1980 and 1991 fall into this category

(iv) **Fourth generation**: These were banks licensed from 1998 to 2005.

(v) **Fifth generation**: These were banks licensed from 2005 till date (post-consolidation era).

This lecture traces the history of the development of commercial banking activities in Nigeria from the 19th century to the present period. The lecture is divided into four main sections. The first section deals with the historical development of banking in Nigeria, the second section deals the structure of banking, and the third section discusses banking legislation. The fourth section deals with consolidation of the banking sector.

**Historical Development of Commercial Banking**

Commercial banking activities started in Nigeria in 1872 with the establishment of the African Banking Corporation (ABC), which was saddled with the responsibility of distributing Bank of England notes for the British Treasury. Three amongst the largest banks currently operating in Nigeria had their origin in the colonial period. The Bank of British West Africa (later called Standard Bank, and now called First Bank Nigeria, plc) was set up in 1894. The next commercial bank to appear was Barclays Bank DCO,
(now known as Union Bank Nigeria, plc) in 1917. The British and French Bank, the precursor of the United Bank for Africa plc started operations in 1949. These banks were set up to provide banking services for the British commercial interest and colonial administration in West Africa. Indeed when the West African Currency Board was formed in 1912, the then Bank of British West Africa became the agent of the Currency Board. The Bank of British West Africa had until then been the principal importer of currency from the British Treasury.

For a considerable length of time, the foreign banks dominated the financial sector of the Nigerian economy. Nigerians criticized this domination, as anecdotal evidences existed that the banks not only favoured expatriates but also openly discriminated against Nigerians in the processes of carrying out their banking duties especially in the allocation of loans and financing the development needs of the country. They were alleged to favour their foreign owners rather than caring for Nigerians and the Nigerian economy. The domination provoked resentment which after independence led to the government's securing greater local control over the financial system and ensuring improved access to credit for the priority areas of the economy and for indigenous businesses.

A second generation of banks came into existence around the time of independence. These banks were also mainly foreign owned. They included the Banque Internationale Pour L'Afrique Occidental (BIAO) now known Afribank Nigeria pic, which is currently the fourth largest bank in Nigeria.

This was followed in subsequent years in the 1970s by the establishment of commercial banks by the state governments and the entry of merchant banks mostly as joint ventures between foreign investors and the Federal Government and/or private investors.

**Indigenous Banking: growth and development**

One of the special features of early banking in Nigeria was the dichotomization of banking into expatriate (foreign) and indigenous banking systems. Expatriate banks were those that were foreign-owned and incorporated outside Nigeria. Banks in this category had access to overseas liquidity from their head offices. On the other hand, indigenous banks were those owned and operated by Nigerians, with their head offices in Nigeria. The National Bank of Nigeria came into existence in 1933, as the first indigenous bank that was to survive. Other banks that were established before that time included the Industrial and Commercial Bank and the Nigerian Mercantile Bank. These two banks failed as a result of inadequate capital, fraudulent practices and bad management. In most cases indigenous banks originated from state support and assistance. The National Bank of Nigeria had an authorized paid-up capital of ₦500, 000, of which only ₦1,152 was paid up initially. The second indigenous bank was the African Continental Bank(ACB) Ltd, which started as a private company under the name of Tinubu Properties Ltd in 1937. In January 1947, it became Tinubu Bank Ltd. Towards the end of the same year (in November) the Tinubu Bank Ltd was registered as the African Continental Bank Ltd with an authorized capital of ₦20, 000.

As a result of the postwar conditions of increased economic activity and high export prices, numerous banks grew up in the Nigerian economy. In the period May 1945 to January 1947, four indigenous banks were established. Only two of these banks- the African Continental Bank and the Agbonmagbe bank
(now Wema bank) managed to survive. In the period 1950-51 which is often referred to as the period of "banking boom" in Nigeria, about eighteen banks were hurriedly established. By the end of 1954, all of them had either gone into voluntary liquidation or were closed down by the police. The only survivor was the Merchant Bank, which finally collapsed in the early part of 1960.

The development of indigenous banks within the Nigerian economy was indeed a very turbulent one. The collapse of many indigenous banks weakened public confidence in them. A host of factors was responsible for the failure of these banks. First, many of the banks had insufficient capital. Fourteen of the eighteen banks had a paid-up capital of less than ₦12,000 (equivalent of six hundred pounds), and this was often used to pay off the losses incurred in the first year. Second, many of the banks were poorly managed and lacked foresight. Third, records were either badly kept or not kept at all. Fourth, many of the banks expanded their offices too rapidly. For example, the Nigerian Farmers and Commercial Bank with a paid-up capital of about ₦26,000 had twenty-eight offices within a short time. Finally, there were no banking regulations to specify banking code of conduct. It was a period of free for all in banking industry. If there had been regulations regarding the amount of paid up capital, many of the banks that failed would not have qualified to receive a licence in the first instance.

With the attainment of regional autonomy in 1954 came the direct policy of the then Eastern and Western Regions. In the case of the Western Region, the debate started in the House of Assembly by the then Premier, Chief Obafemi Awolowo, on 21 December 1956 as follows:

I believe that it is generally known that one of the cardinal policies of this Government is the studied encouragement of indigenous banking institution ... The Government intends to pursue vigorously its policy of giving financial assistance to indigenous banks so that they may be better able to provide credit facilities for Nigerian businessmen and women and others who have profitable projects in which to invest the funds thus provided them.

Further on the basis of laid down principles, he continued, "Three indigenous banks have passed the tests in different degrees and have been given one form of assistance or another...The three banks in question are the National Bank of Nigeria, The Merchant Bank and the Agbonmagbe Bank.

The policy of the then government of the Eastern Region was also one of promoting the growth of indigenous banks and was formulated as follows:

- To discourage the monopoly of monetary transactions by any one bank;
- To liberalise credit facilities to Nigerian entrepreneurs;
- To encourage the development of indigenous Nigerian banking; and
- To plan for the eventual establishment of a state bank.

While the original aim of the regional governments were good, the relationship between the banks and individuals at the helm of government affairs became issues of serious debate later. The methods of injecting public funds into the indigenous banks, as well as the use made of the money, became points of bitter criticism. The banks were used to foster party political interests. Consequently, tribunals were set up to probe particularly into the affairs of the African Continental Bank and the National Bank of Nigeria. In the case of the African Continental Bank, the Forster-Sutton Tribunal (1962) found that “the
manner in which the agreement (i.e. to inject public funds) came into being is shrouded in mystery, since no witness who could have elucidated on the matter chose to tell us the truth”. The report also concluded:

We believe that Dr. Azikiwe's primary motive was to make available an indigenous bank with the object of liberalizing credit for the people of this country, but we are satisfied that he was attracted by the financial power his interest in the bank gave him.

Reporting on another indigenous bank - the National Bank of Nigeria - the Coker commission (1962) stated:

The order of the day is that unless you are a member of the Action Group (the then ruling party in Western Region), you do not come within the contemplation of their schemes, projects and other activities. We are reliably informed that it is the laid down policy of the Government that these bodies should give employment to only approved members of the Action Group.

The report further went on:

The finances of the National Bank of Nigeria Limited did not present very happy picture, the principal causes of that being:

- The huge loans outstanding in the names of erstwhile directors of the bank and/or persons, or companies in which they are interested; and

- The loans to the Action Group which are operated in various names and which are not secured in any shape or form.

**Banking Regulations/ Legislations**

In many countries of the world, the banking industry is put under serious scrutiny through regulations because of the nature of its activities. The role of banks in the mobilization of resources is considered important to the direction and pace of economic growth and development. There is, perhaps, no other industry that is as regulated as the banking industry if only for this simple reason. The soundness of the banking system is a concern for public policy. Banks that failed are potential sources of all kinds of instability in the system. The reasons for its tight control are in many cases obvious. First, the product of the activities of banks is money, which if left uncontrolled can cause irreparable damage to the economy. The power of banks as an intermediary to create money is enormous. If unchecked, banks can create excessive money and cause inflation. Inflation of the excessive type is known to be inhibitive of growth. Second, banks deal with other people's money and it is important to keep a tab on them to see that these amounts of money are utilized in an efficient way and where they are most needed. More importantly, they need to be protected from total collapse or distress. Third, there may be need to direct resources to certain sectors of the economy and without regulation, banks may not direct resources to such sectors. There are a number of examples that can be drawn. Banks have been directed to provide funds to the most productive areas of the economy from time to time. Similarly
banks have also been directed to support agricultural development from time to time as in the case of the agricultural loan guarantee scheme. Fourth, banks are controlled in order to break monopoly tendencies which may-hinder competition and hence efficiency of the financial sector. If unchecked, banks can form cartels and in the process be less innovative in a way that can benefit the economy. Fifth, public confidence in the banking system is maintained through regulation. It is necessary that depositors be protected in such a way that their deposits are convertible to cash when needed without loss to the customer.

The banking sector in Nigeria has been subject to extensive regulation by the Central Bank of Nigeria; and has had direct participation by both the Federal and State governments since the attainment of independence. In the earlier years, economic nationalism and developmental aspirations were the important considerations behind the interventionist policies. It must be stressed that in earlier years, however, the resultant effects of the intervention was financial repression as the controls while making the resources available to government at cheap rate channeled resources away from where rates of returns could have been maximized.

In general, economic regulation embraces all types of control, which is imposed on economic activities by government. Regulation in banking can be classified into preventive regulation and protective regulation. In the category of preventive regulation are such measures to restrict entry into banking business by licensing; restriction on the types of business that banks may be involved. Other preventive regulations include capital adequacy requirements, control of liquidity and statutory reserves, imposition of restrictions on the amount of credit that banks can give and bank examination.

The protective regulations include such measures as deposit insurance schemes and the central bank's assumption of controls on banks. In Nigeria three categories of banking regulations are in existence. These are statutory regulations, Central Bank's guidelines and other regulations incidental to the Central bank performing its functions'. With regards to banking regulation, three periods are discernible and these are discussed in turn below.

(a) Era of Free Banking or laissez-faire banking

The period 1892 to 1951 was basically a period generally referred to as the era of free banking or laissez-faire banking because there were no rules or guidelines controlling the activities of banks. There were no rules, regulation and or laws that regulated the business of banking until 1952 when the first ordinance was enacted. During this period a number of indigenous banks grew up but many failed as a result of the reasons given previously. Only the expatriate banks (or foreign banks) survived. As seen above also, a number of the indigenous banks that survived owed their survival to the acquisition of regional governments. It was during this period that the three biggest foreign banks, the former Bank of British West Africa, Ltd, the Barclays Bank and the British and French banks were established.

Similarly, the two indigenous banks that survived were established during this period.

(b) The Era of Banking Regulation
In general, banking regulations are expected to reflect changes in the economic situation. From the beginning of banking in Nigeria till 1952, there was no regulation of banks. The collapse of one bank after the other during the various crises periods of banking in the depression period of the 1930s and after resulted in a significant loss to the depositors. The loss caused considerable concern within government circles. A commission was set up to inquire into banking business in Nigeria and made recommendations to the government on the extent as well as the form of control that was required in the country. The Committee (Paton, 1948) that was set up in September 1948 reported in October of the same year.

There are two discernible periods in this era of banking regulation. The first was the era of limited regulation from 1952-1958, and the era of intensive regulation from 1958-1986. With the enactment of the 1952 Banking Ordinance came the initial attempt at regulating the banking industry. The Ordinance stipulated the provisions for the licensing of banks. A valid banking license was required before a banking business can be embarked upon. It stipulates the procedures for banking business by prescribing the mandatory minimum capital requirements for banks. It also did put in place regulations for checking bank failures. The 1952 Banking Ordinance defined banking business as "the business of receiving from the public on current account money which is to be repayable on demand by cheque and on making advances to customers" (Paton, 1948).

The Ordinance stipulated the amount of paid-up capital required if a licence was to be granted by the Financial Secretary. This was Twelve Thousand Five hundred pounds, an equivalent of Twenty Five thousand Naira (₦25,000) for indigenous banks, and One hundred Thousand pounds (₦200,000) for expatriate banks. Banks also had to maintain a reserve fund into which at least 20 percent of their profits had to be paid annually. This allocation had to be made until the total fund was equal to the paid-up capital. Banks were also required to provide an adequate degree of liquidity satisfactory to the Financial Secretary. The Ordinance became effective immediately for new banks, while the existing banks were given a three-month grace period within which they were required to obtain a license and three years to comply with the provisions of the Ordinance. The Financial Secretary was given the power to refuse to refuse or to withdraw a license if, in his considered opinion, he was satisfied that there was some defined deficiency in the operations of a bank. Finally, another important provision of the Ordinance was the periodic examination and supervision to which the banks were subjected. This was to ensure that banks did comply with the provisions of the ordinance.

While the 1952 Banking Ordinance was seen as a great advancement in the attempt to develop a sound financial structure, it nevertheless had inherent defects. In the first place, no provision was made for assisting banks in need. Secondly, many banks kept cash idle in order to maintain the required level of liquidity. Since there was no avenue for them in which to invest these funds, it was indeed an economic waste. The expatriate banks on the other hand were in an advantageous position. Not only could they get funds from their overseas headquarters in times of need, they also had access to the money and capital markets in London. Furthermore, the use of a bank-examiner was not as successful as envisaged because of the dubious window-dressing techniques that banks used to deceive the bank-examiners. Finally, the laws were capable of preventing undercapitalized banks from being established, but they were incapable of preventing malpractices and abuses in banking.
The period of intensive regulation began with the CBN Ordinance of 1958. The CBN Act of 1958 gave legal backing to the establishment of the Central Bank of Nigeria. With this the CBN was armed with the power to stipulate measures to curb bank failures of the type that occurred during the banking boom in Nigeria. The Act gave the Central Bank the power to promote and integrate the Nigerian financial system. The essential provisions of the 1958 Banking Ordinance, which established the Central Bank of Nigeria and determined its powers and responsibilities, included the raising of the authorized capital of expatriate banks to ₦400,000 from the original amount of ₦200,000. The indigenous banks authorized capital was retained at its original level of ₦25,000. Other important changes included the following:

1. The raising of the proportion of profits to be transferred to the reserve fund from 20 percent to 25 percent;
2. The prohibition of banks from trading or owning real estate except where absolutely necessary;
3. The fixing of a limit of loans to anyone person or client at 25 percent of paid-up capital; and
4. The provision for a reserve requirement, the amount and composition of which could be changed by the Central Bank.

The 1962 Amendment was more far-reaching than the 1961 Amendment, which mainly dealt with the liquidation of banks. In the 1962 Amendment the following important provisions were made:

1. The paid-up capital of indigenous banks was raised from ₦25,000 to ₦500,000; existing banks were given seven years to comply with this new regulation.
2. Expatriate banks were required to give a satisfactory undertaking to the Minister of Finance to keep assets of at least ₦500,000 within Nigeria.
3. The definition of liquid assets was changed.
4. Banks were allowed to own real estate for the purpose of future development.

In 1969, a government Decree repealed the earlier banking legislation. The objective was to strengthen the banking system and increase the power of the Central Bank over the economy. Perhaps it is fair to say that the 1969 amendments were more comprehensive than the previous ones. It is appropriate to say that the 1969 Banking Decree excelled other legislation in the range of additions to the Central Bank's armory of control techniques, and in broadening the sphere of monetary control to embrace most banking institutions other than commercial banks.

The 1969 Banking Decree can be broken into two broad areas: that dealing with the amendments to the Central Bank of Nigeria Ordinance 1958, and the other dealing with the 1952 Banking Ordinance. In the first category were regulations intended to improve the Central Bank's grip on the economy and those intended to make the Central Bank participate positively in the development of the economy. The control of bank liquidity, for example, is an indirect method of controlling bank credit. Apart from a redefinition of the possible range of liquid assets, the power of the Central Bank to require banks to hold any given ratio between specified liquid assets and demand and time deposit was further strengthened. The Central Bank was also given the power to vary both the composition of any specified liquid assets and the proportion of the different categories of assets that banks may hold from time to time. For the first time, the Central Bank was also empowered to require commercial banks to
maintain a given ratio between their cash reserves and specified classes of deposit liabilities. The required cash reserves were to be held by the bank at its head office.

Most of the new provisions in the 1969 Banking Decree that referred to commercial banking were designed not only to improve the efficiency of the operations of the commercial-banking system but also to promote a sound financial structure. Some of the provisions are stated below;

1. The minimum paid-up capital requirement was increased to ₦600,000 for indigenous banks, while that of expatriate banks was fixed at ₦1.5 million.
2. The Central Bank was given the power to monitor as well as approve banks' advertisement and also to authorize the opening and the closure of bank branches.
3. All banks were required to be incorporated locally, and only the balance sheet of their Nigerian operations was required to be published.
4. In addition to the 1962 Amendment, which required commercial banks to transfer 25 percent of their net profit into a reserve fund until the total sum was equal to paid-up capital, the 1969 Banking Decree additionally required that a transfer of $1\frac{1}{2}$ percent of net profit be made where the amount of reserve funds was equal to, or in excess of, paid-up share capital.

Other laws enacted included the 1968 Companies Act which made it mandatory for foreign owned banks operating in Nigeria to be incorporated in the country. As a result of the more conducive atmosphere, more commercial banks sprang up in the country. Between 1959 and 1960, eight new commercial banks were established bringing the total number of commercial banks to 12. This number increased to 17 by 1962. From 1969 onwards, the controls over the banking system were set out in monetary policy circulars issued by the Central Bank of Nigeria.

During the 1970s, government acquired controlling shares in a number of foreign banks including the "big three" commercial banks which had had the monopoly of the Nigerian banking sector. The three were the Standard Bank (now First Bank), the current Union Bank and the United Bank for Africa. The motivation for the Federal Government equity participation in banking was the urgent need to control strategic industries (or what is popularly referred to as the commanding heights of the economy) and to further the indigenization policy that it was pursuing. The policy of Government in banks in which it held equity was to appoint board members, including the chairman and to set out broad policy guidelines for their operations, while the day-to-day running was left in the hands of bank's management. As part of the privatization programme, the Federal Government sold most of its equity shares to Nigerian private investors in 1992/93.

Two other important banking legislations were the Banking Act of 1969 and the Exchange Control Act of 1962. The Banking Act of 1969 provided for the regulation as well as the control of the monetary and financial system. The Act made provision for the granting of licenses to banks while at the same time imposing restrictions on the activities of licensed banks. Provision was also made in the Act for the CBN to exercise its powers in maintaining monetary and financial stability of the economy, the stipulation of
liquidity and capital adequacy requirements, certain categories of investments that the banks cannot undertake. It also stipulates limits on interest rates and bank lending to the private sector. While the Exchange control Act did not deal with the banks directly, they were however affected as the transactions are carried out through the banking system. The existing foreign exchange restrictions would necessarily affect the actions of the banks.

A rural banking programme was initiated in 1977. Under the scheme, commercial banks were directed to establish a given number of branches in the rural areas over the following decade. The sole aim was to mobilize the financial resources of the rural areas, promote banking habit, attract cash held in the rural areas to the banking system in order to enhance the effectiveness of monetary policy and extend credit to the rural areas. In the second phase of the scheme (1980-84), 266 branches were distributed among 20 banks. Of this number only 18 were outstanding at the end of the period. Less success was however achieved in the third allocation (1985-89) as banks realized the non-profitability of the rural banking scheme its social value notwithstanding. Of the 300 allocations made to 28 banks, only 3 were opened at the end of December 1985.

It has not been possible to reproduce here all the clauses of the Banking Ordinances and decrees and Acts. It must be emphasized that one striking reason for the laws was the necessity of evolving a sound financial system. Apart from strengthening the banking system as a whole to prevent a recurrence of earlier banking misfortunes, the Central Bank's control span and opportunities for effective monetary policy have been widened. One must never lose sight of the fact that the 1967-9 Amendments were motivated not only by public criticisms aimed at closing loopholes and ambiguities of the existing institutional framework but also by the need to face the stark realities of a war situation.

(c) The Era of Financial System Deregulation

The introduction of the Structural Adjustment Program (SAP) brought into being a new phase of banking in Nigeria. The underlying philosophy was to institute a more efficient system for the allocation of resources. The period from 1986 saw a systematic removal of controls that were deemed injurious to the operations of the financial system. Thus, the objective of liberalization was to make the system more market-oriented. The major policy thrust during the period of de-regulation includes:

- Relaxation of the conditions for the licensing of banks. This inevitably led to a phenomenal growth in the number of banks.
- De-regulation of interest rate regime.
- Promulgation of new CBN and other financial institutions Decree numbers 24 and 25 of 1991, respectively.
- Establishment of the Nigerian Deposit Insurance Corporation.
- Introduction of Open Market operation.

As early as the beginning of the Structural Adjustment Programme, the deregulation of the interest rate was accepted as an important element of the reform process. Early in 1987, the interest rate structure was adjusted upwards. This policy was taken as a means of improving the efficiency of the banking
system and improving resource allocation. The principles of maintaining a minimum level of interest rate on savings and time deposits and a maximum lending rate was retained. The controls on interest rates were removed in 1987 and the CBN adopted the policy of fixing only its minimum rediscount rate. This was to signal the CBN's desired direction of interest rate changes. Another major interest rate policy that was taken was in 1989 when the CBN announced that banks could pay interest on current accounts deposits while the rate to be paid would be subject to negotiation between banks and their customers. Subsequently the payment of interest on demand deposits was made mandatory for banks in January 1990. The purpose of this was to enhance greater competition in the mobilization of savings.

Two major changes to the interest rate occurred before 1992. The first was the issuance of guidelines by the CBN on the spread of banks' interest rates. This affected the spreads between savings deposit and prime lending rates, the prime and the highest lending rates and the margin between inter-bank interest rates and the prime lending rates. The second modification was in January 1991 when the government, as a temporary measure had to prescribe a maximum margin between the banks' average cost of funds and their maximum lending rates as well as a minimum level of savings deposit rates.

The resultant high interest rates were suspected to inhibit investment and hence growth which was the opposite of the effects expected by government. In 1992, the policy of interest rate deregulation was reinstated as a result of the orderliness that has been restored to the interest rate regime. The reforms in the financial sector were designed to increase competition, and strengthen the supervisory role of the regulatory authorities.

Since the commencement of the reform programme, more banks have been licensed than any other period in the history of the nation. Thus by 1990, the total number of banks was 106 while the number of bank branches/offices increased from 1,655 in 1985 to 2,025. Later years saw more growth both in number of banks as well as branches. The growth was not limited to commercial banks as there were dramatic increases in the number of merchant banks and increases in the variety of financial institutions. The proliferation of banks and other financial institutions brought about mixed blessings.

While the increased number of banks brought about keen competition with all the different innovations, it also overstretched the limited number of qualified people in the industry. Some banks resorted to poaching in an attempt to get the necessary manpower for the management of their banks. As a result of the increasing demand for high-level manpower, given the limited supply, standards were compromised. As a result of the compromise of standards together with other defects such as rampant internal mismanagement, insider abuse, massive loan repayment defaults and macroeconomic instability there was systemic distress in the banking sector between 1995 and 2000. Indeed a total of 33 terminally distressed banks had their licenses revoked between 1994 and 2000 - 2 in 1994, 2 in 1995, 26 in 1998 and 3 in 2000.

In a way the liberalization of the financial sector (which has permitted the easy entry of banks and the removal of allocative controls), has had significant and important effects on the financial market. One of these is an increase in the number of banks. The growth of private banks and the influence of the
Federal government in banks have no doubt injected a reasonable degree of commercial orientation and increased competition into banking. In spite of the financial liberalization, however, there has been limited impact in terms of improvement in the efficiency of the allocation of resources. The reasons for this included the inconsistency and the partial nature of the deregulation exercise, the high rates of inflation that has impeded the attainment of positive real rates of interest, large government deficits that absorbed a substantial part of bank credit and the mismanagement as well as fraud in both public and private sector banks. These have led to extensive waste of resources. As indicated earlier, the inconsistency in interest rate policy was an impediment to the attainment of allocative efficiency.

Interest rates were decontrolled in 1987 but the CBN stipulated a maximum spread between deposit and lending rates since 1989, ceiling on bank lending rates were imposed during 1991, removed the following year and re-imposed at the beginning of 1994.

The period of deregulation witnessed a number of institutional changes, which were strategic to the banking industry. Among these were first, the establishment and the take-off of the Nigeria Deposit Insurance Corporation (NDIC) in 1989. The NDIC is charged with the responsibility of insuring bank deposits against bank failures. It is also charged with ensuring safe and sound banking practices through effective monitoring and supervision of banks in collaboration with the Central Bank of Nigeria. With the increasing growth of the banks, fears were rampant that failure could occur again. The establishment of NDIC was therefore to instill greater confidence in the banking system. The second was the series of actions taken by the CBN and NDIC to assist distressed banks which were beset by a number of serious problems including illiquidity, poor asset quality, capital erosion, poor management and general technical insolvency", After special examination between 1990 and 1991, eight technically insolvent banks were identified. Some holding actions were imposed on them in order to safeguard their assets; and the management of one of the banks which failed to respond positively to official action was taken over by the Central Bank of Nigeria in January 1992. In June 1993, another set of five banks were taken over by the CBN for similar reasons.

The third significant change was the promulgation of two banking laws in 1991 - the CBN Decree No 24 of 1991 and the Banks and Other Financial Institutions Decree (BOFID) No 25 of 1991 which repealed the CBN Act of 1958 (as amended) and the Banking Decree 1969 (as amended). The CBN Act significantly enlarged the powers of the CBN with respect to the maintenance of monetary stability and a sound financial system. The Decree also had provisions for the use of market-based instruments of monetary control. The Banks and Other Financial Institutions Decree (BOFID), also called Banks and Other Financial Institutions Act (BOFIA) on the other hand introduced changes in regulation that can promote the development of the banking sector in a deregulated economy. The decree contains the following important elements:

- The centralization of bank licensing, regulation and Supervision in the CBN.
- Strengthening the regulatory powers of the CBN with regards to the keeping of proper records of accounts by financial institutions, the control of distressed banks and the winding-up of failed institutions.
- Enlargement of the duties and responsibilities of directors and external auditors of banks.
• Bringing under regulation all financial sector operators in the informal sector whose activities influence the economy in a significant way.

There are so many other interesting aspects of the BOFIA. Suffice to mention a few. The Decrees spells out punishment against acts of Directors and officers of a bank, which are considered inhibitive of the efficient operations of the bank. BOFIA restricts some activities of banks except prior approval is obtained from the central bank. Such activities include, for example, the total amount of loan or financial guarantee that may be granted to any person. A bank is also prohibited from permitting outstanding unsecured credit in excess of N50,000. For the early detection of fraud or any financial mismanagement, the Act makes it mandatory for all banks to keep proper books of account in respect of all transactions relating to the operations of the bank.

Consequent to the promulgation of the CBN Act and BOFIA in 1991, the need to regulate this rapidly growing sub-sector led to the creation of a department in the CBN known as the "Other Financial Institutions Department (OFID)". This department has the responsibility for supervising other financial institutions. The department has responsibility for the off-site and on-site supervision of community banks, primary mortgage institutions, finance companies, bureaux de change and development finance institutions. The supervisory role of the department was assumed in April 2001. The vision of the department is not only to be proactive but efficient in the regulation and supervision of the specialized banks and other financial institutions by "ensuring a sound, safe, effective and efficient other finance institutions sub-sector in Nigeria. The mission of the department is to develop an appropriate regulatory/supervisory framework and strategy that would guarantee the desired growth and efficient performance of the other financial institutions sub-sector, through adequate and effective surveillance and monitoring".

It is necessary to mention the BOFI (Amendment) Decree No. 38 of 1998, which further gives a lot of discretion and authority to the central bank to regulate and supervise some categories of institutions in the financial sector.

The CBN can license new banks without recourse to either the President or the Ministry of Finance. The CBN has the authority to vary or revoke the conditions for granting new licenses including the power to determine the paid-up capital of each bank. The CBN can apply any actions it deems fit to resolve distress in the banking sector.

A very important action that has placed banks at greater alert in the period of deregulation was the withdrawal of public sector deposits from the banking system. The idea behind the withdrawal was to make banks more proactive in their orientation and move away from armchair banking which has hitherto been the practice.

The Structure of Banking in Nigeria

The structure of banks in Nigeria has to centre on a number of aspects. It is this aspect of banking that
would be discussed in this section. These include the structure of ownership of banks in Nigeria, the size of banking and the distribution of bank branches in Nigeria. With regards to the ownership of banks in Nigeria, this has also gone through changes over time. At the beginning of banking in Nigeria, it was strictly a dichotomy between expatriate banks and the indigenous banks. Even though there were problems with indigenous banking at the beginning, some of them eventually managed to survive with regional government support. In the evolution of banking in Nigeria, different interests developed. These interests included the participation of the Federal Government, state government and private individuals in banking. It is to this aspect of banking that we would now discuss.

(a) The Federal Government participation in banking.

With the promulgation of Nigeria's indigenization decree in 1972 came the subsequent need to interfere in the field of banking. The Federal Government in 1973 acquired a 40 percent interest in the three biggest banks. This was the Federal Government's first incursion into commercial banking. This participation was upgraded to 60 percent in 1976, when the same level of indigenous participation was extended to cover all foreign commercial and merchant banking in Nigeria.

When the Federal Military Government announced the government's participation in commercial banking in the 1973-4 budget, the aim was expressed thus:

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

It was, however, quite obvious after 1973-4 that the problems besetting the financial system could not be solved by the Federal Government's 40 percent participation in the major expatriate banks. It was as a result of this that the extent of participation in commercial banks was increased.

It seems the aim of government is to challenge the monopoly and domination of the expatriate banks, apart from the necessity of controlling an important aspect of the national economy and twisting commercial banking lending policy towards the medium or long-term needs.

The importance of the Federal Government ownership declined since the mid 1980s and the sale of the Federal Government equity to the private sector in 1992/93. The financial performance of the Federal Government banks during the 1970s and 1980s does not really appear to have been very good while the quality and efficiency of their services were poor. Although the four largest commercial banks recorded profits during this period, their returns on assets were low and returns to equity not impressive when account is taken of inflationary trends. Indeed as a result of the absence of prudential guidelines till the 1990s, most of the published accounts are likely to have overstated earnings. Consequent to the introduction of the prudential guidelines in 1990 where loans were to be classified according to their quality and provisions made for non-performing loans, the First Bank recorded losses as a result of the need to make provision for bad debts, while profits in the other three major banks were drastically reduced.
Relative to the other banks - the state and private banks- the four major Federal Government banks" remained solvent and avoided the distress that plagued other banks. They were able to avoid serious trouble for four main reasons. First, they have benefited from their long experience in banking and the influence of their foreign shareholders in employing experienced bankers who practiced conservative management style. In addition to this, the Federal government has ensured that those appointed to executive positions were seasoned and highly experienced bankers. Second, these banks practiced strict portfolio management: loan, as a share of total assets was restricted to below 40 percent in most years. The impact of this policy has been to reduce the adverse impact of non-performing loans on their balance sheets. Given the size of these banks, their loan portfolio was well diversified. Third, competition among the banks has been limited as a result of the barrier to entry before 1986. These banks had access to government and government parastatals' deposits. This access plus interest rate controls ensured that their average cost of funds was low, and this helped to offset their high overhead costs. Given their international links as well as their historical position in the economy, these federal-owned banks have a high degree of resilience to economic vicissitudes. Indeed they had become important to all the multinational companies operating in Nigeria.

b) State Ownership of banks and Participation in banking

Regional or State participation in banking as discussed earlier started with the establishment of the National Bank of Nigeria owned by the Western Region of Nigeria and the African Continental Bank owned by the Eastern Region. The regional governments acquired equity shares in these banks and when these banks got into financial difficulties, the regional governments subsequently became the majority shareholders. The Bank of the North owned by the Northern Regional Government in collaboration with Lebanese investors was established in 1959. Another bank, the Agbonmagbe Bank since renamed Wema Bank was taken over a year before independence in 1959.

The Military government abandoned regional governments during the Nigerian civil war and State governments were created in May 1967. After the civil war in 1970, the newly created governments found out that there were no infrastructures - mainly roads, buildings etc. Additionally they had no institutions to finance the much-needed facilities. Each State then felt the need to set up its own financial institutions to take care of these basic needs. The primary aim of the State governments in setting up the banks was to access funds for the purposes of development as well expanding credit facilities to indigenous businesses, in particular, citizens of the State. Between 1970 and 1976, a number of State banks were established. These included the New Nigeria Bank by the Midwest Government in 1970; the Pan African bank in 1970 by the River State Government, and the Mercantile Bank in 1971 by the South Eastern Government. The six Northern Governments acquired the Bank of the North which was previously a partnership with a Lebanese group of banks. With the creation of more States (increase of States from 12 to 19) in 1976, the tempo of State banking increased. Commenting on the phenomenon of State banking, the Federal Commissioner of Finance in addressing the Financial System Review Committee on April 5 1976 said as follows:

"just as in the 1950s, we saw the mushrooming of indigenous private banking companies, so in the 1970s we are witnessing the expansion of state banks; we should
soon have nineteen such banks! Again state banks are the off-springs of inevitable reaction: the sad experience of businessmen and consumers from areas of the country that were not specifically identified particular banking interests. In essence therefore, the motivation for establishing state banks has been parochial”.

By 1980, there were ten banks in which State governments held majority equity shares. In 1995, State governments had 17 banks listed”. This is after leaving out those banks that got distressed between the early 1990s and 1994- about ten distressed banks were taken over by the CBN during the 1992-95 periods. In 1985, the management and accounting systems of State-owned banks were adjudged to be unsatisfactory. The poor financial position of the State owned banks became more obvious in the 1990s when the imposition of prudential was made involving stricter loan classification, capital adequacy and tightening of liquidity position.

In general, the performance of the State banks has been very poor. The financial problems afflicting them can be attributed to a host of factors. First, the quality of their management has been very poor because of political interference of their State governments and the attitudes of politically powerful and influential borrowers who do not pay back their indebtedness.

Those at the helm of affairs at the State banks were often not the most competent but those with political weight who got their positions because of political patronage. Second, there was a lot of inside-abuse in the State banks. Third, the precarious state of the finances of many various governments made it not only difficult for some of them to service their loans, but the poor financial positions have undermined their ability to recapitalize their own banks. Fourth, frequent changes of the leadership of the State government as new military governors were deployed to states created its own problems for the State banks as incoming leaders have most times accorded priority to the servicing of loans contracted by a previous government.

(c) Private Ownership of Banks

The history of private ownership of banking in Nigeria dates back to the 1920s and 1930s when banking business was unregulated. These banks were set up in order to compete with the expatriate banks with a view to assisting indigenous businesses. Between 1942 and 1952, an indigenous banking boom occurred in Nigeria. About 185 so-called "mushroom banks" were registered even though most of them did not start operation. Most of the banks that did start operation collapsed within a few years because of a combination of factors including mismanagement, insider lending and inadequate capitalization. For quite some time there was a lull in private involvement in banking. In the mid 1970s, some private individuals participated in banking by collaborating with State governments.

With the advent of SAP and the liberalization of the financial sector and in particular the easy licensing of banks before the CBN suspended issuing new licenses in response to emerging signs of distress in the industry in 1991, many private banks were established. During the periods 1987-92, the private Nigerian investor established about 27 commercial banks and 42 merchant banks.

In general, the privately owned banks have been mainly urban based and have small branch networks.
Many have concentrated on foreign exchange dealing, financing local businesses and foreign trade. A number of factors were responsible for the growth of privately owned banks.

First, there were lots of opportunities to be tapped and gaps to be filled in the banking sector. The private banks were able to develop their own clientele and offered their own services. A few of them were able to carve a niche for themselves in banking; and some offered higher interests to their customers when interest rates were deregulated in 1987. Second, many of the banks were set up to take advantage of the opportunities available in the foreign exchange market. The foreign exchange market was liberalized in 1986 with the introduction of the exchange auction system. Bankers were allowed to buy foreign exchange that they sold to their customers. The possibility existed for these banks to resell the foreign exchange at the parallel markets and make profits that a lot of them did. With the existence of the bureaux de change in 1989, another avenue was opened for banks to resell their foreign exchange from the auctions and make profit. The fact that only banks could participate in the auction system and the fact that no matter how small a bank was, it could still obtain foreign exchange, provided powerful incentives for investors to establish banks even though the intention is not to conduct conventional banking business the way it is generally conceived. The third factor in the growth of privately owned banks was the political nature of granting banking licenses in the second half of the 1980s. During the Military regime, the Federal Ministry of Finance had the authority to grant license with the involvement of the Presidency and the Federal Executive council involved in reviewing applications. Those who had political influence and links to the Military were able to obtain licenses even though they had no cognate experience in banking.

The conducive environment notwithstanding, many of the banks ran into problems in the 1990s. Four of the banks were liquidated by the CBN in 1994 and a further 13 distressed banks were taken over by the CBN in 1995. Two other banks had their licenses suspended for persistent infractions of the banking laws in 1994.

Table 1 below shows the number of banks, their branches and location - urban, rural and abroad for the periods 1970-2002. In the 1970s the number of banks was less than 20. It was in 1980 that Nigeria had twenty banks with a total of 740 branches. The number of banks steadily grew to about 80 banks in 2002 with about 2193 branches. Of these branches, only about 22 percent branches of the total branches are held abroad. The earlier years showed the urban bias in the location of bank branches. In the late 1970s, the preponderant of the bank branches were located in urban areas, more than 70 percent in the period 1971-1981. While the urban bias in the location of bank branches is still evident today, the share of bank branches in the urban areas as a proportion of total bank branches have somewhat declined from its high value of 72 percent in 1981.

Table 1: Number of Commercial Banks and their Branches: Distribution by Location (1970-2002)
<table>
<thead>
<tr>
<th>Years</th>
<th>No of Bank</th>
<th>Urban Branches</th>
<th>Urban % of Total</th>
<th>Rural Branches</th>
<th>Rural; % of Total</th>
<th>Branches Abroad</th>
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**Banking Consolidation: The New Era of Banking in Nigeria**
It has been noticed by analysts that the capital base of Nigerian banks is low and this may hamper their effectiveness. On July 6th 2004, the new Governor of the CBN announced at a special meeting of the Bankers Committee in Abuja, Nigeria, the first phase of the reform of the banking sector in Nigeria. Key in the new reform, banks in Nigeria are expected to build up their capital base to N25 billion from the existing N2 billion. This is expected to be achieved by December 2005. He further announced a phased withdrawal of public sector funds from banks starting from July 2004 and the consolidation of banking institutions through mergers and acquisitions. The Governor further noticed that Nigerian banks are not really engaged in the strict banking business of savings intermediation but have turned themselves into traders. They are involved in trading in foreign exchange, in government treasury bills and are sometimes involved in the direct importation of goods through companies of doubtful credibility. The need for capitalization was also anchored on examples drawn from Malaysia and South Africa.

In order to facilitate the realization of the Reform Agenda, the Central Bank of Nigeria released a set of incentives on consolidation in the Nigerian banking industry to assist banks in meeting the approved capital base. Some of the incentives include authorization to deal in foreign exchange; permission to take public sector deposits, recommendation to the fiscal authorities for the collection of public sector revenue and tax incentive in the areas of capital allowance, company income tax, stamp duties etc.

It has been claimed by the Central Bank of Nigeria that the current recapitalization is aimed at repositioning the industry to achieve a more stable and efficient banking industry that is capable of meeting the needs of the people better, and in the process facilitate economic growth. It was hoped that the new directive will spur a consolidation of what is often described as Nigeria's fragile financial structure. The seemingly overcrowded sector can end up merging in order to give a new flavor to banking business in Nigeria.

Specifically, as mentioned by the Deputy Governor of the CBN, the re-capitalization will reposition banks to:

(a) Improve the capacity of banks to finance large transactions.

(b) Raise confidence in the banking sector through the resolution of the distress syndrome.

(c) Enhance healthy competition by providing level-playing field and reducing regulatory abuses and other malpractices that were rampant with the marginal players.

(d) Achieve a greater level of transparency in the bank's operations.

(e) Become a global player.

At the launching of the re-capitalization idea, a lot of criticisms grew mainly from the operators of the system who believed the new capitalization was aimed at eliminating the small banks and reducing the
number of banks in the country. The point of disagreement between the junior and senior workers of the banks was anchored on whether to back the policy of the CBN or work for its reversal. While the junior workers worried about the possible loss of jobs that it might entail, the senior staff believed that the recapitalization will deepen the economy in the long run. Bankers under the auspices of the Chartered Institute of Bankers (CIBN) set up a 10-man committee that recommended the stratification of banks into categories. The National Assembly also at one time urged the stratification of banks into different categories with the bigger ones having a bigger recapitalization rate.

As time wore on, it now seems the various criticisms have died down as banks scramble for funds in the capital market in order to meet the capital base requirement. It is difficult to know in some cases the genuineness of the reports of the statements of accounts of many of the banks. A number of banks have been selling shares in order to meet the capital base requirement or to boost up their bargaining power just in case they have to go into merger with other banks.

Various attempts are being made by various banks to merge into one bank in order to meet the order of the Central Bank of Nigeria. Of course for all of the merging banks there would be need to have the general annual meeting for the bank's shareholders to endorse the merger. The 19 northern state governors for example have recently paid money to boost the shareholders' fund of the bank as part of their agreement on the recapitalization of the bank. The First North Bank plc comprising Bank of the North, NUB International Bank Limited and New Africa Bank plc has formally applied to the Central Bank of Nigeria for its approval in principle. The CBN has however in a circular in June 2005 limited the Federal and state's investment in any bank either directly or indirectly to 10 percent. The CBN has noted that the resurgence of government interest in bank investment, particularly state government was capable of scuttling the gains of the on-going consolidation in the banking industry. There are reported moves by Fidelity Bank plc and FSB International bank plc to merge. It is reported that the proposed bank would retain the name Fidelity Bank but would adapt the FSB logo and its green/purple colour scheme. It is expected that the merged bank would have a combined asset base of about ₦75 billion, gross income of ₦13 billion, shareholders funds in excess of ₦26 billion and a combined branch network of about 60 branches.

In some cases, these are likely to be marriages of odd couples or marriages to satisfy the requirements of the Central Bank. Whether the forced marriage would last would depend on a number of factors including coincidence of interests of the parties, the state of the economy that would influence viability.

One cannot know presently what the outcome of the recapitalization of banks will yield in terms of the growth of the banking sector itself and the ensuing competition that would develop. What is obvious however, is that the only banks in the first generation, the First Bank of Nigeria, Union Bank and the United Bank for Africa are likely to retain their identity even if they were to merge with other banks. At present, the Union Bank of Nigeria is poised in acquisition/ takeover of some banks and has signed the memorandum of understanding (MOU). The banks involved are six. These are Broad Bank, Gulf Bank, Universal Trust Bank, Union Merchant Bank, Midas Bank and Triumph Bank. Preliminary consent has been given for the merger of two large banks: United Bank for Africa and the Standard Trust Bank. Many other banks are not likely to be that lucky as they are likely to be swallowed in the merger process.
by the bigger and powerful ones. There are many banks that are in various stages of merger approval stages. The possibility also exists that some very weak banks may have no one to associate with and go into oblivion. The "banking water" is presently troubled as many possibilities exist for merging permutation. Some banks are involved in merging processes with more than one bank. What the final situation would be is unknown till December 2005. At the time of writing this book, it is expected that there would be about 22 banks when all the dusts have settled down.

When banks merge, there are lots of implications for positions at the top management level in terms of who evolves at the chief executive. There are also implications for those who would remain as members of the board because when two to three banks merge, it would be unwieldy to retain all the previous members.

What the re-capitalisation and the possible merger portray for the future of the financial sector and the Nigerian economy is not concretely known at this time. There is a lot of uncertainty. What is clear from the proponents of the re-capitalisation, however, is that it would lead to the evolution of bigger banks that would not only be more efficient but can finance bigger size transactions for the economy. The ability to succeed in such financing also depends very crucially on the growth of the real sector of the economy, a point that is often ignored. While we draw inferences from the performances of the banks in Asia, Malaysia and South Africa, it is often not realized that the basic infrastructures (water, constant power supply) are important ingredients in their performance. In Nigeria, the erratic nature of power supply is not only a hindrance to operational efficiency of banks and great nuisance to customers in particular. It seems very clear therefore that the growth of the real sector is very primary in all the reforms that are being envisaged. If the real sector refuses to grow, banks may have no transactions to finance. If the economy does not grow, mergers and big size banks may not rid the industry of its presently alleged poor reputation.

**In a more generalized summary:**

**Background**

In 1892, the African Banking Corporation and British West Africa, now First Bank of Nigeria, were established in Nigeria. In 1925, the Anglo-Egyptian Bank and National Bank of South Africa gave birth to Barclays Bank in Nigeria. In 1948, the British and French Bank for Commerce and Industry started operations in Nigeria, which metamorphosed into the United Bank for Africa.[2] The first domestic bank in Nigeria was established in 1929 and called Industrial and Commercial Bank. The bank liquidated in 1930 and was replaced by Mercantile Bank in 1931. The African Continental Bank was created in 1949 as the only sustainable indigenous bank after the liquidation of the Industrial and Commercial Bank. The year 1947 shows the emergence of an agricultural bank called the Nigerian Farmers and Commercial Bank.

**The modified universal banking model**

In 2010, the Central Bank of Nigeria re-modified the existing universal banking model that permits the holder of a commercial banking license to operate in other non-core banking, either directly or indirectly
through designated subsidiaries. The introduction of this scheme classifies banking licenses into commercial, Merchant and Specialised/Development Licenses.

**Nigeria banking reform**

Nigeria banking reform can be divided into two main phases, 2004 and 2009. Each phase had significant economic effects:

**Banking Reform of 2004 and its effect**

This reform focused on bank consolidation through the mechanism of merger and acquisition. This resulted in rebasing of commercial banks from ₦2 billion to ₦25 billion, while the 89 existing commercial banks in the country became 25.

The apex bank apart from capitalization also invested in banking automation which enhances banking returns. The reform established a reporting portal for bank customers for the purpose of information sharing. Under this reform, deposits from public sectors and government-owned agencies can be collected by the commercial banks in order to enhance their level of liquidity.

**Banking Reform of 2009 and its effect**

The Asset Management Corporation of Nigeria (AMCON) was established in 2009 by the National Assembly. The institution acquires non-performing loans of commercial banks. The financing of AMCON is composed of a ₦50 billion CBN fund and 0.3% of total assets of participating commercial banks. It also supports the implementation of International Financial Reporting Standards (IFRS) for global reporting compliance in terms of reporting. This reform reviewed the universal banking model by restricting commercial banks to banking activities only. The reform also addresses excessive banking interest by the creation of a non-interest bank.

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