Internationales Afrikaforum 2/1994 Vol. 30 No. 2:191-196

By Hans Dieter Seibel

Underdeveloping Nigeria through reregulation -will community banks survive?

Regulating the financial system through restrictions on foreign exchange, interest rate controls and constraints imposed on financial institutions have been among the principal instruments of financial repression in low-income countries. In recent years, many have taken to deregulation, but mostly in response to donor persuasion and pressure rather than conviction. Unpopular political regimes have found it difficult to get over their initial hardship period which the restructuring of a whole economy and its financial system entails. The Nigerian Government, in a populist gesture, has just succumbed to the temptations of re-regulation. Commercial banks are hard hit. Small farmers and microentrepreneurs are among the first victims

Community banks are an institutional innovation of the deregulation period. Within a three-year period, around 900 of them have come into existence. These are local financial institutions the share capital of which is owned approximately half by self-help groups and half by individuals of the respective communities. Bank ownership by self-help groups is the ultimate form of linkage banking. These community banks provide convenient deposit facilities and access to credit to the self-help groups who are their co-owners. They were also found to be highly innovative and responsive to local needs and demands. They form part of a network, which is under their own secondary-tier regulatory authority. Will they escape from the fetters of the new financial repression?

Regulation

Until 1986, the financial system of Nigeria was tightly regulated, with exchange and interest rates fixed by the Government. Through quotas, tariffs, licences and subsidies, the government intervened in virtually all spheres of the economy. Entrepreneurial activity which exists in abundance in Nigeria, flowed more into the struggle for import licences, contracts and subsidies than productive activities. Cheap imports substantially reduced the profitability and thus the scale of national food production. The economy, and government revenue, of OPEC country Nigeria largely depended on petroleum exports, with minimal diversification. In the context of political instability, massive market distortions and gross factor misallocations, Nigeria's external debt rose to unprecedented hights.

Deregulation

In 1986, the government deregulated tile financial system and introduced, in collaboration with IMF and World Bank, a structural adjustment program (SAP). Deregulation altered the financial System:
interest rates rose, and so did monetary and credit aggregates which expanded at unprecedented rates (CBN *1993:1).* In particular, domestic resource (including savings) mobilization grew rapidly; the financial infrastructure changed and expanded substantially (including the number of banks and bank branches, vast numbers of Bureaux de Change and about 900 community banks) exceeding by far the supervisory capacity of the Central Bank; and financial innovations in the banking sector became prominent (Oyewole 1993). As imports were cut, food prices rose, and so did national food production, accompanied by a large scale back-to the land movement. The percentage of food imports to total imports

declined from a peak of 6.2 % in l980 to under 1 % in l988 and then rose to 2.3 % in 1989. Agriculture and the agro-industrial sector enhanced their competitiveness substantially. ,,Nigeria previously a huge importer of rice and maize is now almost sell-sufficient in these grains. The share of the agricultural sector in GDP has stabilised at over 30 % in both 1986 and 1990, a big improvement on the 20 % level of 1980." (ECPER 1993:10). During 1986-90, the average annual growth rate of GDP was 3.66 %, while during the pre-SAR period of 1979-85 it was a mere 0,4% p.a. (ECPER 1993:10). In a speech in November 1993, the Governor of the Central Bank stated that,

> ,,the positive impact of financial liberalization on financial savings, competition and quality of financial services is manifest." (Ogwuma 1993:3)

Yet, the government failed to keep its budget under control, with internal public debt outstanding continuing its upward trend throughout and external debt outstanding climbing from $13 billion in 1985 to over $33 billion by l990 (or from l5% to 110%, respectively, of GNP) (ECPER 1993:11). Various forms of subsidies, misallocations and misappropriations continued unabated; and structural reforms were only hall-heartedly carried out. During the pre-SAP period 1980-86, Federal Government deficits averaged N 3.9 billion a year, increasing to an annual average of N 23.4 billion during the SAP years 1987-90, with a pronounced upward trend (ECPER 1993:9; cf. Ndekwu 1990,1991; Philips 1990).

As a result, alter a - perhaps doubtful – all-time low of 5.5% in both 1985 and 1986, inflation skyrocketed, and the combination of political and economic instability proved lethal to deregulation. In 1993, the results of democratic elections were cancelled and a military regime was reinstated, bringing the country to the verge of chaos.

Re-regulation

In January 1994, the government cancelled deregulation, adding policy instability to political and economic instability. Exchange controls were tightened by fixing the exchange rate (causing an immediate drop of the market value of the Naira by 50%) and reverting the sale of foreign exchange to the monopoly of the Central Bank. All interest rates ware fixed, with savings and deposit rates pegged at 12-15 %, while the lending rate ceiling was set at 21 % (at a time of 100% inflation p.a.!), rendering real returns on savings extremely negative and leaving a margin to the banks mostly inadequate to cover costs of funds, administrative costs and risks. Re-regulation was also extended to other sectors (including the fixing of hotel rates for non residents at arbitrary and oftentimes astronomical heights).

Nigeria's re-regulation policy reads as if inspired by the author's paper on, *How to Undermine Financial Systems and Development,* though in 1/1994 this was only in press and not yet available to policymakers in Nigeria (Seibel 1994).

A consensus is building up among academics in Nigeria that while deregulation was a good thing it failed in its implementation: ,,The bold corrective measures embodied in SAP were appropriate and represented the best way out of the quagmire. Faulty implementation has, however, robbed the country of much of the fruits...' (ECPER 1993:18). Or in the words of the new Head of State, General Sani Abacha: ,,Deregulation requires discipline among the key operators in the vital sectors, which absence has resulted in the near collapse of the economy today", at the same time adding that, ,,no country anywhere in the world freely surrenders its economy to the absolute interplay of market forces" (15/2/1994; cf. *Daily Times* 16/2/94:1). As "deregulation was dogged by innumerable distortions, resulting in low economic input, rising interest rates, currency depreciation, and unemployment" (General Abache, cf. *The Guardian* 16/2/94:1), re-regulation is being considered as an effort to restore that discipline. This decision however appears without scholarly foundation; to the

contrary, ,,... a reversion to the era of administrative controls in the economy will not solve underlying problems and will not put us in a durable path of self-sustaining growth... implementation should now be much more consistent... there seems to exist no other viable alternative." (ECPER 1993:18, 23), adding strong warnings against exchange and interest rate controls and equally strong recommendations in favour of budgetary restraint and effective fiscal measures (ECPER 1993:18-20).

Impact

The results of re-regulation evident in February 1994 ware disastrous. The loss of confidence in politics is now followed by a loss of confidence in the economy and the policymakers behind it. The Central Bank, hitherto an adamant advocate of deregulation, now appears as an instrument of the government.

Hundreds of Bureaux de Change ware wiped out overnight, banks lost their hitherto highly profitable foreign exchange business, and resource mobilization dropped. The number of banks in distress -many of them weakened by hazardous experimentation unsupervised by the Central Bank during deregulation goes up almost by the day, causing bank runs and further aggravating the Situation of the already shaky banking industry. According to press reports, financial institutions are now turning to non legal forms of transactions to survive (e.g., lending charges hidden in the principal, bringing effective rates up to pre-reregulation levels around 38% -still far below the rising inflation rates).Only the community banks, which were excluded from foreign exchange transactions, with their strong resource base, their prudential lending and their own internal bank supervision System, seem to be winners, attracting local customers who lost confidence in their commercial bank. So far they have adhered to the Bankers Tariff, thought hey do not fall under the banking law; hence they may also have to struggle to survive on the margins between the fixed interest rates on savings and credit. No community bank failures have so far been reported, and no licences have been revoked.

An ECPER journal article concludes that Nigeria, similar to other resource-rich countries like Zaire or Zambia, has ,,wasted the opportunities created in the form of inherited natural wealth... Successful countries and firms are those that create, rather than inherit, competitive advantage; those that exploit opportunity, that relish challenge and thrive in the face of adversity." (Hawkins 1993:32). To this one should add that the latter would be an adequate description of Nigerian microentrepreneurs in the thriving informal sector (including the informal financial sector), while the former is the legacy of a state-interventionist stance.

The implications of the new monetary policy may be summarized in one sentence: *,,underdeveloping Nigeria through re-regulation."*

Community Banks:
Local Financial Institutions Owned by Self-help Groups and Individuals

Community banks are an institutional innovation which evolved during the deregulation period, representing the highest stage in linkage banking: self-help groups linked to banks through ownership - a case of informal financial institutions turned into formal intermediaries (cf. Seibel 1985,1989,1992).

The latter is of great relevancy in a country that as a whole has perhaps the strongest System of informal financial institutions in Africa, among which the indigenous rotating and non-rotating savings and credit associations are most prominent, such as *esusu* and *ajo* among the Yoruba, *dashi* among the Hausa, *isusu* among the Igbo, Oja and *aterugba*

among the Igala, *bam* among the Tiv, etc., and a vast array of derivatives (Seibel & Damachi 1982; Seibel 1984; Seibel 1989; Seibel & Marx 1987).
Community banks are local financial institutions registered under Decree No. 46 (28/4/1990) and owned directly by the people and their self-help groups. They abide by the Bankers Tariff and other Central Bank regulations. Their interest rates are similar to those of commercial banks (CBN 1993:46). After a provisional period they might eventually come under Central Bank supervision.

Equity capital requirements are N 250,000 [US $ 11,364 at the official rate or US $ 5,208 at current market rates] (compared to N 50 million for commercial banks). They fully depend on locally mobilized resources, comprising mainly equity capital, deposits and accumulated profits. Ownership is dispersed over a wide range, comprising three categories of owners with roughly the following shares:

The Community Development Association, which is a communitybased self-help group:	30 %
Member-based self-help groups (unions of craftsmen, traders associations, farmers groups, cooperatives, etc.):	22 %
Individuals:	50 %

Their main purpose is the provision of convenient and safe savings deposit facilities and the granting of credit to the local population, including loans to the Community Development Associations, the various self-help groups in a community and individuals.

The decree vests overall responsibility for the policy and operational performance of community banks in the NBCB (National Board of Community Banks), headed by a Governing Board, with its seat in Abuja, the new capital city. NBCB is a second-tier regulatory authority which has supervisory powers over the community banks (comparable to the Central Bank, which is a first-tier regulatory authority supervising commercial and merchant banks). NBCB reports to the Central Bank on a quarterly basis. At the same time; NBCB is an interest association, comparable to DGRV and DSGV in Germany, and offers central banking functions to its members.

During the period of inception, its administrative costs are borne by the government. As subsidies (for institution-building, not credit!) are withdrawn, NBCB expects to eventually become self-reliant on the basis of mandatory contributions from community banks and fees for services.

During the first three years, the operations of the board were organized in four zones, covering the whole country, with their seats in Bauchi for the NE, Kaduna for the NW, Enugu for the SE and Lagos for the SW. Each zonal office has a staff of about 300, providing promotion & appraisal, training, and supervisory services through Appraisal, Inspection and Training Sections under the NBCB Operations Department. With the steady increase in banks, the number of zonal offices is presently being doubled. The additional zonal offices are located in Makurdi, Minna, Benin City and Uyo.

For a period of two years the banks are under the guidance of their zonal offices and the National Board, NBCB. A provisional license is granted by the NBCB. After 15 months of satisfactory operation, an operating license is to be granted by the Central Bank.

Having mobilized up to N 10 million and more per bank (one has mobilized N 23 million), the community banks have proven beyond doubt that local savings exist.

The first community bank opened up in 12/1991. Within the first three years of existence, their number grew to 879, and the total amount of savings has passed the N 2 billion mark. By 12/1993 a total of N 941 million had been disbursed in loans.

The Central Bank routinely reports on community banks. In its Annual Report for 1992 (OBN,1993:46) states that,

> ,,Agriculture and petty trading were relatively large recipients of the banks' loan facilities while significant amounts also went to petty restaurant businesses and cottage industries. A substantial amount was also lent to small-scale enterprises engaged in manufacturing and transportation." (Cf. Adejumobi 1991; NBCB 1992a, b)

BCB Community Bank, Ltd.; A Case Study (2/1994)

BGB (a fictious name for a real community bank) was established in 9/1991 upon the initiative of local leaders organized in a Community Development Association (CDA). It has 269 shareholders who established the bank without any equity or other lending support from outside, including NBGB, with the following proportions of share capital:

Community Development Association	30 %
Societies and corporate bodies	22 %
Individuals	48 %

The bank does not serve as a conduit for government loans.

Total assets are N 13.2 million, including N 1.7 million in fixed assets. The deposit base grew as follows (in Naira):

12/1991	1.76 million
12/1992	6.62 million
12/1993	10.58 million

The bank provides deposit, •credit (including overdraft) and checking services, the latter through a corresponding bank.

Deposits as of 12/1993 were comprised of the following:

Time deposits	3.12 million
Demand deposits	1.23 million
General saving accounts	6.03 million
Daily deposit collection and mobile banking	0.20 million

The loan portfolio (loans and advances) amounts to N 2.39 million (12/1993). Among others the portfolio includes a three-year loan to the GDA for the purchase of three income-generating 30-seater buses and a lending scheme to groups of market vendors in cooperation with their respective market associations: up to N 180,000 p.a. to the livestock section, N 300,000 to the wood section, N 250,000 to the foodstuff section, and N 300,000 to the remaining sections.

14.15 % of the loan portfolio are overdue (but not necessarily bad debts). Portfolio quality is shown by the structure of bad debt provisions in 1993, which follows the Prudential Guidelines (effective as of 1993) as issued by the Central Bank:

Payments overdue 3 months	N 102,242
Payments overdue 6 months	N 23,510
Payments overdue 12 months	N 151,731.

The bank is required to hold a cash balance of N 3 million at any time. Excess liquidity is placed in a call account with the corresponding commercial bank (at 19% interest).

Interest rates are 12 % on passbook savings, 12.5 % on 7-day call deposits, 13 % on 3-months time deposits, 14 % on 6-months time deposits and 15 % on 12-months time deposits. Depending on maturity (maximum mostly 1 year) and risk, the interest rate on loans varies from 19 % to 21 %. There is no interest rate differentiation between individuals and groups.

Among the most interesting financial innovations of BCB is a daily deposit collection scheme operated through a staff of 10 organized in 5 teams of two each on the nearby market. These doorstep services are modelled after the *alajo* scheme (Yoruba word for daily deposit collector) which originated among the Yoruba in Southwestern Nigeria and spread from there among the coast to neighbouring countries (Ghana: *anago susu;* Ivory Coast: *nago* - cf. Seibel & Marx 1937). Each bank team reaches about 100 customers per day and collects between N 20-35,000. Instalments due at the end of the month may be deducted from a client's savings account If so arranged.

In 1992 the bank made a loss (after provision for bad debts); in 1993 it broke even, with a small net profit of N 70,000.

A Case for Development Assistance?

German technical assistance might greatly contribute to the further evolution of community banks in Nigeria, particularly if provided by the Savings Banks Foundation for International Cooperation or by Deutscher Raiffeisen- und Genossenschaftsverband (German Confederation of Cooperatives) representing together perhaps the world's broadest network of local financial institutions (mobilizing 77.2% of all savings and delivering 50.9 % of all credit in Germany in 1993). But this might pose a dilemma to German development assistance:

On the one hand, the German Government requires as a conditionality that partner governments provide the right policy environment. On the other hand, it wants to promote viable institutions serving the poor in sustainable ways. As usual in the developing world, there is no optimal solution.

References

Adejumobi, A.: Processes and Problems of Community 0rganization for Self-Reliance. NISER Monograph Series No. 111991. Ibadan 1991: NISER

Central Bank of Nigeria (GBN): Annual Report and Statement of Accounts for the Year Ended 31st December, 1992. Lagos 5/1993: CBN

ECPER (Emwai Centre for Political and Economic Research): Structural Adjustment Programme – Any Way Out. ECPER Journal for Political and Economic Studies, Vol. 1 No. 1,1993: 2-26.

Hawkins, A.M.: Options for Long-Term Economic Growth in Nigeria. ECPER Journal for Political and Economic Studies, Vol. 1 No. 1,1993: 27-37

NBCB (National Board for Community Banks): The Community Banking System in Nigeria: An Introduction. Abuja 1992a: NBCB

NBCB: Community Banks Decree. Abuja 1992b: NBCB.

Ndekwu, Eddy C.: Monetary Development and Management in Nigeria. Ibadan 1990: NISER

Ogwuma, P.A. (Governor, CBN): Recent Developments in the Nigerian Financial Services Industry: Problems and Challenges. An Address at the Annual Dinner of the Chartered Institute of Bankers of Nigeria, 12 Nov. 1993. Lagos

Oyewole, O.B.: Empirical Analysis of the Effect of Financial Policy Reforms on Innovations in Nigeria`s Banking Sector. Savings and Development Vol. 17 No. 2, 1993: 153-167

Philips, Adedotun O.:; Economic Impact of Nigeria`s Structural Adjustment Programme, NISER Monograph Series No. 1/1990. Ibadan 1990: NISER

Seibel, H.D.: Ansatzmöglichkeiten für die Mobilisierung von Sparkapital zur Entwicklungsfinanzierung: Genossenschaften und autochthone Spar- und Kreditvereine in Nigeria (Savings mobilization for development: cooperatives and indigenous savings and credit associations in Nigeria). Forschungsberichte des BMZ Vol. 63. Köln 1984: Weltforum Verlag

Seibel, H.D.: Das Entwicklungspotential autochthoner Selbsthilfeorganisationen im ländlichen Bereich. Ein Fallbeispiel aus Nigeria. Internationales Afrikaforum 20/1, 1984: 66-74

H.D. Seibel: Savings and Development: A Linkage Model for Informal and Formal Financial Markets. Quarterly Journal of International Agriculture (Berlin) 24/4, 1985: 290-298

H.D. Seibel: Linkage Informal and Formal Financial Institutions in Africa and Asia Pp. 97-118 in J. Levitsky, ed., Microenterprises in Developing Countries. Intermediate Technology Publications, London 1989

H.D. Seibel: Developing the Financial System through Deregulation. Asia Pasific Rural Finance, July-Sept. 1991: 30-37

H.D. Seibel: Self-Help Groups as Financial Intermediaries: A Training Manual for Self-Help Groups, Banks and NGOs. Saarbrücken 1992: Breitenbach

H.D. Seibel: Easy Money: How to Undermine Financial Systems and Development. Quarterly Journal of International Agriculture (Berlin), Vol. 33 No. 1, 1994: 60-77.

H.D. Seibel & M.T. Marx: Dual Financial Markets in Africa: Case Studies of Linkages between Formal and Informal Financial Institutions. Saarbrücken 1987: Breitenbach

H.D. Seibel & U.G. Damachi: Self-Help Organizations: Guidelindes and Case Studies for Development Planners and Field Workers – A Participative Approach. Bonn 1982 (2nd ed. 1983): Friedrich-Ebert-Stiftung

Exchange rates on 18/2/1994:
Office rate: US-$1.- = Naira 22 *Market rate: US-$1.- = Naira 48*