EFInA Quarterly Review

(January to March 2011)

1 Nigerian Economy

1.1 2011 Budget

In March, the two chambers of the National Assembly approved an aggregate expenditure of N4.97 trillion for the 2011 fiscal year. The figure represents an increase of about N433 billion over the amount presented to the National Assembly in December 2010 by President Goodluck Jonathan. The budget breakdown is as follows:

- N2.47 trillion - recurrent expenditure
- N1.56 trillion - capital expenditure
- N0.50 trillion - statutory transfers
- N0.44 trillion - debt service

The Minister of Finance, Segun Aganga, said that the N4.97 trillion budget will spur job creation in the country. Aganga said: “President Goodluck Jonathan has declared that we are cutting down costs in the 2011 budget, but more importantly it is a budget of job creation. We have N50 billion in the budget to kick-start a public work programme, in addition to that we are focusing on labour intensive projects in agriculture, IT-outsourcing, construction, housing and entertainment sectors”. Aganga said that the government was also looking at providing “safety nets” for the inactive poor, the unskilled and uneducated.

1.2 National Minimum Wage

In March, President Goodluck Jonathan signed into law the new national minimum wage bill for the implementation of the N18,000 monthly pay for Nigerian workers. In May 2009, in a bid to forestall a labour crisis, the Federal Government set up a tripartite Committee to look into the national minimum wage issue. The Committee had initially proposed a minimum wage of N22,500 per month. However, the Committee observed that the economy could not support this amount and after extensive deliberations, it was agreed that the new wage should be pegged at N18,000. The last time the minimum wage was reviewed in Nigeria was in 2000 when the Obasanjo administration increased it to N7,500.

1.3 Foreign Reserves

Nigeria’s foreign exchange reserves increased from $33.25 billion at the end of February to $36.38 billion by 8 March. The increase was primarily due to the rise in world oil prices. However, the foreign reserves are still significantly less than a year ago, when it was $41.55 billion.

1.4 Sovereign Debt

According to the Director-General, Debt Management Office (DMO), Dr. Abraham Nwankwo, as at the end of December 2010, Nigeria’s total debt was $34.6bn (N5.19tn), of which

86.71% (N4.5tn) was domestic. He said that most of the domestic debt was incurred through the Federal Government of Nigeria's bonds with maturity dates ranging from three to twenty years which are issued by the DMO on monthly basis. Justifying the level of the nation's debt, Nwankwo said it was still within a safe range, adding that by international standards, a country like Nigeria could afford to have an outstanding debt of up to 40 percent of its Gross Domestic Product.

The DMO boss said the Federal Government preferred domestic to foreign debt as a measure to deepen the country's bond market, adding that the strategy for 2011 and 2012 was to help the private sector, especially the small and medium-scale enterprises to access the bond market. The DMO reintroduced the issuance of sovereign bonds in 2003, but started regular bond issuance in 2005 based on a monthly issuance calendar. With external borrowing limited to concessional windows, borrowing from the domestic market has become the main source of raising capital by the Federal Government for funding its activities. The policy shift towards the development of the domestic market was anchored on the desire to finance government budget deficits as well as to provide a platform for raising long-term capital for funding public and private sector projects; develop the domestic capital market; and provide a benchmark for pricing other financial instruments in line with global best practices.

On January 21, 2011, Nigeria successfully launched its first sovereign bond of $500 million bond on the London Stock Exchange's main market. The bond has an annual interest rate of 6.75 percent and matures in January 2021. The bond offering has created a benchmark US dollar bond yield curve that should lead to lower borrowing rates for Nigerian companies issuing corporate bonds in the domestic and international markets. The bond attracted investors from 18 countries spanning Europe, US, Asia and Africa who were said to have booked $1.3 billion as against $500 million on offer. Going forward, it is expected that the nations' corporate entities will be able to more easily access well-priced long term financing from the International Capital Markets, to fund economic opportunities such as infrastructure development. The Minister of Finance, Segun Aganga said "This transaction clearly puts Nigeria on the global map. We now have a transparent and internationally observable benchmark against which international investors can accurately price risk".

1.5 Inflation

The National Bureau of Statistics stated that the country's inflation rate increased to 12.8 percent in March from 11.1 percent in February. The rise in inflation was attributed to the rise in the general price level for consumer items such as yam, beverages, fruits, vegetables, fish and cereals at both urban and rural areas.

The inflation rate in March of 12.8 percent is the highest recorded this year, which validates the fears of finance experts and monetary authorities that it will be difficult to achieve a single digit inflation rate that the government is proposing this year. To curtail the threat of inflation as well as stabilise the economy by ensuring too much money was not allowed in circulation, the apex bank during the last Monetary Policy Committee meeting voted to increase the lending rate (the Monetary Policy Rate) by 100 basis points from 6.5 percent to 7.5 percent effective from February.

1.6 Unemployment

Statistics shows that forty nine percent of Nigerians between the ages of 15 to 24 in urban areas are unemployed. The Finance Minister, Segun Aganga said that "While the growth of the Nigerian economy remains robust, we face a challenge in making sure that the growth is all-inclusive, as the unemployment rate remains fairly high". According to the National Bureau of Statistics, the national unemployment rate for 2009 was estimated at 19.7 percent. Unemployment for the 15 to 24 age group was estimated at 41.6 percent (49.9 percent in urban areas and 39.6 percent in the rural areas) in 2009.

Nigeria, Egypt and Tunisia typify a widespread African problem of high unemployment rates amongst youths. According to the 2010 Africa Economic Outlook, more than 60 percent of Africa's population is under the age of 25 and is expected to increase to 75 percent by 2015. The International Labour Organization (ILO) reports that 7.2 percent of Africa's youths are unemployed and an additional 46.9 percent are underemployed or inactive. In Nigeria and many other African countries, there is too much emphasis on certificates to the detriment of skill acquisition. Teaching methods and curricula have not been adjusted to address new requirements for trained manpower, especially in the private sector, which demands graduates with different and higher skill levels and knowledge. So with governments no longer automatically hiring university graduates, millions of unemployed youths have to find their own jobs. The private sector, especially small and medium-scale companies, which could have engaged some of these youths, have been victims of economic decline.

The World Bank Country Director for Nigeria, Onno Ruhl, recently stated that Nigeria must create efficient vehicles for job creation to curb rising youth unemployment and to avoid upheavals by the growing number of frustrated youths in the near future. Ruhl's statement was prompted by the current youth (15 to 24 years) unemployment rate in the country which he put at 46 percent, 4.4 percent higher than the 41.6 percent being quoted by the National Bureau of Statistics. Ruhl noted that Nigeria has 100 million people under 30, which is roughly the equivalent of the combined population of Egypt, Tunisia and Libya. "Most shockingly, every year about 1 million aspiring students pass Nigeria's Joint Admission Board's entrance exam, but only 200,000 of them actually gain admission to Universities in the same year. This means that each year the equivalent of the population of greater

Amsterdam, my home town, qualifies for university but do not get in." Ruhl said. According to Ruhl "No government in the world could employ the number of youths waiting for jobs in Nigeria. Nigeria will need an ambitious private sector-led growth strategy and also have to focus every policy on making it easy for the private sector to create jobs. This would be a big shift for most policy makers".

2 Financial Sector

A report issued by the US-based group, Global Financial Integrity (GFI), stated that Nigeria might have lost $130 billion between 2000 and 2008 to illicit financial flows. The report entitled: Illicit Financial Flows from Developing Countries: 2000 to 2008 stated that Nigeria has the 10th highest illicit outflows in the developing world, with an average of $15 billion per year. Illicit outflows include trade mispricing, kick-backs, bribes, embezzlement and other forms of official corruption. According to the report, China is ranked the highest country of illicit outflows in the developing world with $2.18 trillion, followed by Russia with $427 billion and Mexico with $416 billon. Others in the top 10 are Saudi Arabia with $302 billion; Malaysia with $291 billion; United Arab Emirates with $276 billion; Kuwait with $242 billion; Venezuela with $157 billion; and Qatar with $138 billion. According to the report, over the 2000 to 2008 period measured, the average yearly illicit outflows from developing countries were estimated at $725 billion to $810 billion. Over the period reviewed, the report puts real growth of illicit flows in the African region at 21.9 percent, compared with 24.3 percent in the Middle East and North Africa; 21.3 percent in developing Europe; 7.85 percent in Asia; and 51.8 percent in the Western Hemisphere. GFI Director, Raymond Baker said that every year developing countries were losing ten times the amount of Official Development Assistance remitted for poverty alleviation and economic development.

2.1 Banking Industry

The Governor, Central Bank of Nigeria, Mallam Lamido Sanusi, has said that the banking sector crisis will be over by the end of the second quarter of this year. He based his optimism on the result of the various reforms introduced by the apex bank, especially the recapitalisation of the Deposit Money Banks and the activities of the Asset Management Corporation of Nigeria. Commenting on the economic situation in the country, he said that "No economy in the world had grown as a result of proceeds from the sales of primary products, adding that the development of the real sector was the only guarantee for economic advancement in Nigeria". He said the CBN, through its deliberate economic policies, was making sure that the real sector was supported, and that the bank was aware that the sector remained a huge catalyst for economic growth.

The Central Bank of Nigeria has said that the number of banks in the country may be reduced from 24 to 20 by middle of this year, when the industry is expected to have completed all the recapitalisation deals. Foreign and local investors including Standard Chartered Group, FirstRand, Capital Alliance Group, Habib Bank Pakistan, First City Monument Bank, Access Bank, Fidelity Bank and First Bank had indicated interest in one or two of the banks namely: Bank PHB, Union Bank, Afribank, Oceanic Bank, Spring Bank, Intercontinental Bank and FinBank.

According to figures released in March by the Ministry of Finance (based on CBN and World Bank data) only 1 percent of financing for formal businesses in Nigeria comes from the banks and other financial institutions; in spite of several efforts by the Central Bank and government stimulus to encourage the banks to expand lending, especially to the real sector. So rather than depend on the banks, these businesses source a huge chunk of their financing, up to 70 percent internally from their retained earnings, about 25 percent from suppliers' credit and advances from customers, while the remaining 5 percent is sourced from family and friends. The CBN noted that the growth in credit to the three tiers of government, against the backdrop of the decline in private sector credit is a reflection of the fact that government borrowing has to some extent crowded out private sector credit.

2.1.1 Savings Mobilization

The low deposit rates paid by banks may be a disincentive to mobilization of deposits. The feeling in the market is that banks need to provide reasonable incentives for the mobilization of savings. Failure to do this may constrain the flow of funds into the key sectors of the economy like manufacturing and agriculture. Analysts say the existing low rates of about 1% per annum paid on savings deposits could have far reaching implications for financial intermediation and the mobilization of long-term funds which is critical for enhancing investments in the real sector and economic growth.

2.1.2 Human Resources

After decades of losing its brightest employees to New York and London, Africa's fast-growing and expanding financial markets are helping it lure back highly skilled, local-born bankers. While Africa's shortage of skilled financial professionals remains a chronic problem and a major concern – it may be the continent has finally turned the tide, thanks to a returning Diaspora. According to Naveed Riaz, CEO, Citigroup Africa, a lot of Africans who have developed skills in more developed markets believe that the biggest opportunities for growth are back in their home markets. Africa's growth prospects are particularly impressive when compared to that of many developed economies. A Bain & Company study released in February stated that the continent's $107 billion financial services industry is expected to grow at a compound annual rate of 15 percent to 2020, outpacing its economic expansion.

2.1.3 Bank/ATM Fraud

Bank Fraud

The Nigerian Deposit Insurance Corporation (NDIC) stated that the volume of reported cases of attempted or successful frauds and forgeries in the nation's banking sector was N41.2 billion in 2009, which represents a drop from N53.5 billion in 2008. According to the NDIC, the drop was achieved because of the rapid improvement in accountability and transparency in conducting banking transactions in the country. The NDIC Chairman, Hassan Adamu, stated that 1,764 cases of fraud were recorded in 2009, as against 2,007 in 2008. However 10 out of the 24 banks accounted for over 90 percent of the fraud cases in 2009 as against over 64 percent in 2008. In absolute terms, the total amount involved in those 10 banks was N37.2 billion in 2009, as against N34.3 billion in 2008. The Chairman further stated that one of the major challenges the NDIC faced in 2009 was that many of the licensed microfinance banks and primary mortgage institutions did not pay their insurance premiums.

ATM Fraud

The Central Bank of Nigeria has recovered N2bn from Deposit Money Banks (which has been returned to the banks' customers), which was money wrongly deducted from customers using their ATM cards within the last year. According to the CBN governor, there is an urgent need to build and sustain consumer confidence in the use of ATM cards. He stressed that the move would go a long way in strengthening the nation's banking sector. As part of efforts aimed at tackling the problem of ATM card fraud within the banking sector, Sanusi said that the apex bank have established the Card Fraud Arbitration Committee to ensure speedy resolution of complaints by customers. He said, "We should recognise the fact that financial institutions are in business because they have customers who patronise their products; but when consumers' confidence begins to wane due to inefficient service delivery, it means that something needs to be done to restore their confidence". The Central Bank intends to introduce biometric ATMs to check the spate of illegal deductions from the accounts of bank customers using ATM cards.

2.1.4 Banking Reforms

For breaching guidelines on the operations of ATMs, the Central Bank will impose various sanctions on banks and e-payment companies in the country. In February, the apex bank imposed a sanction of N50,000 per day for infringing certain aspects of the ATM guidelines, such as failure to establish help desks; putting in place non-functional help desks; lack of online monitoring mechanisms and back-up power (inverters) for ATMs; late submission of returns and data on ATM fraud; and failure to respond to a customer or to the CBN within 72 hours. The banks will be fined N50,000 per week for disobeying certain rules, including failing to provide audit trails and journals for ATM transactions, failure to have 2 percent of ATM deployed with tactile graphic symbol for use by the visually impaired, as well as failure to comply with new policy of offsite ATM deployment. Non compliance with migration to EMV after September 30, 2010 will attract a fine of N50,000 and the issuer will bear full liability for any fraud perpetrated with the magstripe card. The Central Bank further stated that failure to resolve any ATM dispute with evidence of resolution within 14 days requires the deployer to refund the total amount involved in the fraud. In addition, an ATM deployer will be made to refund the full amount involved in any fraud perpetrated on its ATM for failure to provide footage on the disputed transaction when required. An ATM without a camera installed will attract a fine of N50,000 and deactivation of the ATM until the camera is installed.

2.1.5 Deposit Money Banks (DMBs)

Cash Management

In a bid to reduce the cost of doing business in the financial sector, the Central Bank, Deposit Money Banks and cash processing companies have concluded plans on how to reduce the cost of moving cash by at least 15 percent. The three parties agreed on the separation of wholesale cash management and retail cash management functions. The Central Bank will continue to be responsible for the production and issuance of currency notes, storage of mint notes, destruction of unfit notes and is also expected to outsource or lease out its existing processing facilities to service providers. Cash in transit and cash processing will be carried out by private companies, leading to a reduction in cash held in bank vaults. The DMBs are to select bulk cash centres across clusters within their branch network for cash lodgements and withdrawals above the limit, while banks without bulk cash centres are to deal through correspondence banks.

On limiting cash deposits and withdrawals - Razia Khan, Regional Head of Research, Africa, Standard Chartered Bank said the move will create less of an inflation risk, by putting in place curbs on withdrawals. She said it will also encourage the adoption of other means of payments other than cash for the purchase of large items – cheques, credit cards, etc.

2.1.6 E-Payments

With N80 billion monthly transactions being carried out on 8,500 ATMs deployed across the country using 28 million debit cards, the CBN is estimating a 200% growth in electronic payment cards usage by 2015. In the next five years, the Central Bank will concentrate on strengthening regulatory and institutional frameworks against card fraud in order to drive card usage towards meeting the nation's Vision 2020. The CBN is confident that the estimate would be achievable, through the various card-related electronic payment schemes being put in place by the apex bank.

However, a recently released report titled "Debit Card Customer Usage Pattern 2010" revealed that over 74 percent of the respondents said they only used their debit cards for cash withdrawals at ATMs. 14 percent of the respondents used their debit cards to make purchases on the web, POS or ATM. 7 percent also used their cards for funds transfer from one bank account to another, while only 4 percent of the respondents used their cards to make bill payments. According to the report, ATM downtime and fear of fraudulent activities emerged as major factors inhibiting the frequent use of debit cards for payment transactions. To deepen the culture of card usage, the report recommended that banks and card schemes operators should focus on marketing strategies that will encourage card holders to activate and use their cards as frequently as the need arises for all relevant transactions, stressing that most bank customers are unaware that they can use their cards for payment transactions on other channels other than ATM withdrawals.

2.1.7 Microfinance

Worried by the massive withdrawal of funds by the micro depositors, which has created a serious liquidity problem in the microfinance sub-sector, operators are set to pursue the government and donors for funds. Many customers of microfinance banks withdrew their money after the CBN announced the revocation of operating licenses of 224 microfinance banks in September 2010. The negative impact of these withdrawals has pushed practitioners into looking for various ways of accessing funds to remain in business.

In February, in a bid to tackle the challenges faced by microfinance banks, the Central Bank came up with a '4-pillar' reform agenda to strengthen the sub-sector:

i. sanitization of the sector
ii. capacity building
iii. restructuring
iv. restoring public confidence

These reforms aim to deal with some of the challenges faced by microfinance banks, which include 'mission drift'; MFBs operating like 'micro-commercial banks' – with a fleet of branded cars and high expenditure profile; weak capacity; poor understanding of the microfinance concept and methodology for delivering microfinance services; poor corporate governance and susceptibility to insider abuse; incompetence and ineffective oversight of the board; poor risk management and weak internal controls; dearth of external funding; impact of the global financial turbulence of 2008/2009; and weak capitalisation. In its restructuring agenda, the CBN plans to revise its regulatory and supervisory framework and guidelines. The key message from the apex bank is that microfinance banking is a regulated activity and only well-capitalised institutions that are ready to comply with the rules and regulations will be allowed to operate in that space going forward.

2.2 Non-interest (Islamic) Banking

According to the Central Bank governor, Nigeria would like to establish itself as the African Hub for Islamic banking and is working on a regulatory framework to try to emulate the success of the industry in Malaysia. Nigeria has one of Africa's fastest growing consumer and corporate banking sectors. Islamic finance is estimated to be a $1 trillion global industry, but ratings agency, Moody, forecasts that the industry could hit $5 trillion over time. Asian economies including Malaysia and Indonesia have seen rapid growth in Islamic banking. However, growth in the Gulf Arab region has steadied, partly due to inconsistent regulations and wrangling over the interpretation of Sharia principles. Sanusi said Nigeria was looking at the example of Malaysia where a national Sharia Council sets the rules for Islamic financial institutions, which are standardised under the Central Bank. Sanusi said Nigeria was looking at Islamic finance not just for the opportunities it would offer to banks and investors, but also as a way of diversifying the country's financial system in order to mitigate risk. "Islamic banking products are tied to the real economy, so they are part of our reform programme of getting banks to lend to the real economy. They also discourage excessive speculation and risk taking, which is consistent with some of the new guidelines the Central Bank is putting in place. So from a financial stability perspective and from a financial deepening perspective, Islamic banking is an important part of the apex bank's agenda'', Sanusi said.

2.2.1 Non-interest Banking Regulations in Nigeria

The operational structure of Non-interest Financial Institutions (NIFIs) as defined by the Central Bank is grouped into seven categories:

i. Full-fledged non-interest deposit money bank or subsidiary
ii. Full-fledged non-interest microfinance bank or subsidiary
iii. Non-interest branch of a conventional bank or financial institution
iv. Non-interest window of a conventional bank or financial institution
v. A development financial institution registered with the CBN to offer non-interest financial services either full-fledged or as a subsidiary
vi. A primary mortgage institution registered with the CBN to offer non-interest financial services either full-fledged or as a subsidiary
vii. A finance company registered with the CBN to provide non-interest financial services, either full-fledged or as a subsidiary

Conventional banking and non-interest banking are basically different in their financial intermediation roles. Hence, the nature of their underlying assets and liabilities, products and services, financial reporting, risk management practices and capital requirements are completely different. However it is impractical to prevent co-mingling of conventional banks' interest-based assets and liabilities with those of their non-interest based branches or windows.

3 Telecoms Sector

Nigeria's GSM subscriber base continues to rise in a strong and growing telecoms market. Figures released by the Nigerian Communications Commission (NCC) stated that as at the end of February, there were 83 million active GSM lines. Of this figure, MTN had 38,683,520 subscribers; Globacom had 19,627,415 subscribers; Airtel had 15,834,243 subscribers, Etisalat had 6,791,986 subscribers and Mtel had 258,520 subscribers. Within the CDMA market, Visafone is the market leader with 2,558,867 active lines, followed by Multilinks with 1,454,704 active lines, then Starcomms with 1,149,380 active lines and then Reltel with active 939,145 lines. In March, Visafone announced that it will further strengthen its market position by acquiring Multilinks CDMA mobile assets.

The table below provides a summary of telephone subscribers in Nigeria as at February 2011:

	Number of connected lines	Number of active lines
Mobile GSM	**108,564,834**	**83,453,999**
Mobile CDMA	**12,404,906**	**6,114,669**
Fixed Wired/Wireless	**1,619,907**	**1,014,638**
Total	**122,589,647**	**90,583,306**

Source: NCC

3.1 SIM Registration

The NCC directed that from 14 February that all new SIM cards should be on receive only mode for a period of 30 days. In March, the NCC said it will impose a fine of N5 million on any telecommunications operator that failed to put new SIM cards on 'receive only' mode.

4 Mobile Money

The global mobile money industry, according to a report by Pyramid Research, will generate over $200bn by 2015, which is about eight percent of Africa's nominal Gross Domestic Product. Similarly, Ovum, a global research company, in its 2011 forecasts, states that there will be between 925 million and 1.54 billion registered mobile money users in emerging markets by 2015. Ovum also predicted that Nigeria will witness a revolutionary growth in mobile money transfer in 2011 and the years ahead. With over 140 million people, about 22 million bank accounts and less than 10,000 bank branches, experts say that un-banked and under-banked Nigerians estimated to be about 80 million would benefit from this mobile money revolution. The challenge that the providers will face is that of signing up quality agents before competition gets to them. The major role of an agent is cash in and cash out.

Agents will act like mini bank outlets, where different services like bill payments, remittances, P2P payments, banking services can be conducted. An agent needs to balance risk, provide space, hire literate staff and manage additional security issues that might arise from this new relationship with a bank or mobile money provider in their community. The agent will also need to commit to some level of branding from the provider; maintain a certain level of float in the form of a pre-deposit; and hire one or two employees that will facilitate transactions.