NATIONAL OPEN UNIVERSITY OF NIGERIA
FACULTY OF MANAGEMENT SCIENCES

COURSE CODE: BFN748

COURSE TITLE: FINANCIAL INSTITUTIONS AND MARKETS

COURSE GUIDE

COURSE WRITER: **Dr. Eleje, Edward Ogbonnia**
Department of Banking and Finance
Faculty of Humanities, Management & Social Sciences
Federal University, Wukari
Taraba State

COURSE EDITOR: **DR. AHMED ADO**
Associate Professor of Finance
Department of Banking and Finance
Abubakar Tafewa Balewa University, Bauchi

PROGRAMME COORDINATOR: DR OKOH, JOHNSON IFEANYI

HEAD OF DEPARTMENT **DR. OFE INUA**

Department of Financial Studies

Faculty of Management Sciences

CONTENTS **PAGE**

INTRODUCTION

BFN 748: Financial Institutions and Markets is a second semester course, two credit unit, 700 level core courses. It will be available for all students offering postgraduate Diploma in Banking and Finance programme in the Faculty of Management Sciences. The course will introduce students to the financial institutions and markets. In this course, students will be exposed to the history, regulatory and supervisory frameworks in the financial institutions and markets which will guide them in understanding the nitty gritty and workings of that market. Students will also be able to apply the knowledge in this course in financial institutions and markets setting.

COURSE GUIDE

The course guide tells students briefly what the course is about, what course material will be used, and how you can work your way through the study material. It suggests some general guidelines for the amount of time you are likely to spend on each unit of the course in order to complete it successfully.

The guide also gives you some guidance on your tutor-marked assignments, which will be made available to you in the Study Centre. There are regular tutorial classes that are linked to the course. You are advised to attend these sessions.

WHAT YOU WILL LEARN IN THIS COURSE

The BFN 748 course consists of 14 units. Specifically, the course discusses the following:

- Overview of Financial System
- Efficient Financial System and Economic Development
- The Financial Markets
- Financial Market Operations (Money Market)
- Financial Market Operations (Capital Market)
- Nigerian Financial Market Regulators
- Money Market Instruments
- Capital Market Instruments
- Banking Institution
- Bank Categorization
- Commercial Banking
- Development/Specialized Banking Institutions
- Bank Income and Investment Policy
- Insurance Institutions
- Pension Institutions and Administration
- Informal Financial Markets
- Informal Financial Institutions
- International Finance Institutions

COURSE AIMS

The aim of this course can be summarised as follows:
It aims to give you an understanding of the concept ‘regulation’, ‘supervision’ and legal framework as they affect the banking industry. It also aims at facilitating a good knowledge of the banking regulatory reforms which had taken place in the past as well as the structure and key players in Nigeria’s financial system.

Finally, you will have an insight into the ethics and best practices in the banking industry and related issues concerning governance in the banking industry.

COURSE OBJECTIVES

To achieve the aims set out, the course sets overall objectives. Each unit also has specific objectives. The unit objectives are always specified at the beginning of a unit, you should read them before you start working through the unit. You may want to refer to them during your study of the unit to check your progress.

You should always look at the unit objectives after completing a unit. When you do that, you will ensure that you have followed the instructions in the unit. Below are the overall objectives of the course. By meeting these objectives, you should have achieved the aims of the course as a whole. On successful completion of the course, you should be able to:

- Discuss an overview of the concept of the Financial System.
- Examine the Regulatory Framework of the Financial Market & Financial Market Instruments.
- State and explain the Financial Institutions (Banks) and non-bank financial institutions as well as the informal financial markets.
- Trace the history and evolution of the international financial institutions.

WORKING THROUGH THIS COURSE

To complete this course, you are required to read the study units, read set books and read other materials provided by the National Open University of Nigeria (NOUN). Each unit contains assignments which you are required to attempt and submit for assessment purposes. At the end of the course, there will be a final examination. The course should take you a total of 16 - 17 weeks to complete.

Below, you will find listed all the components of the course. What you have to do and how you should allocate your time to each unit in order to complete the course successfully on time. The list of all the components of the course is as presented.

COURSE MATERIALS

Major components of the course are:

- Course Guide
- Study Units
- Textbooks
- Assignment
- Presentation Schedule

Study units

The study units in this course are as follows:

Module 1:	**Concept of Financial System**
Unit 1	Overview of Financial System
Unit 2	Efficient Financial System and Economic Development
Unit 3	The Financial Markets
Unit 4	Financial Market Operations (Money Market)
Unit 5	Financial Market Operations (Capital Market)
Module 2:	**Regulatory Framework of the Financial Market & Financial Market Instruments**
Unit 1	Nigerian Financial Market Regulators
Unit 1	Money Market Instruments
Unit 2	Capital Market Instruments
Module 3:	**Financial Institutions (Banks)**
Unit 1	Banking Institution
Unit 2	Bank Categorization
Unit 3	Commercial Banking
Unit 4	Development/Specialized Banking Institutions
Unit 5	Bank Income and Investment Policy
Module 4:	**Non-Bank Financial Institutions & Informal Financial Market Institutions**
Unit 1	Insurance Institutions
Unit 2	Pension Institutions and Administration
Unit 3	Informal Financial Markets
Unit 4	Informal Financial Institutions
Module 5:	**International Finance Institutions-(IMF, IBRD)**
Unit 1	International Finance Institutions

Textbooks

At the end of each unit of the course, there are reference materials to which you can refer in order to increase the depth of your knowledge on the course. Please take this seriously.

Assignment Files

A number of assignments have been prepared to help you succeed in this course. They will guide you to have understanding and good grasp of the course.

Presentation Schedule

The presentation schedule included in your course materials also have important dates of the year for the completion of tutor-marked assignments (TMAs) and your attending to tutorials.

Remember, you are to submit all your assignments by the due date. You should guard against failing behind in your work.

Assessments

There are two aspects to the assessment of the course: first are the tutor-marked assignments and a written examination.

In tackling the assignments, you are expected to apply information, knowledge and techniques gathered during the course. The assignments must be submitted to your tutor for formal assessment in accordance with the deadlines stated in the ***Presentation Schedule*** and the ***Assignment File***. The work you submitted to your tutor will count for 30 percent of your total course mark.

At the end of the course, you will need to sit for a final written examination of 'three hours' duration. This examination will also count for 70 percent of your total coursework.

TUTOR-MARKED ASSIGNMENTS (TMAs)

Each of the units in the course material has a tutor-marked assignment (TMA) in this course. You only need to submit five of the eight assignments. You are to answer all the TMAs and compare your answers with those of your course mates. However, you should ensure that you collect four (TMAs) from the Study Centre. It is compulsory for you to answer four (4) TMAs from the Study Centre. Each TMA is allocated a total of 10 marks. However, the best three (3) of the four marks shall be used as your continuous assessment score.

You will be able to complete your assignment from the information and materials contained in your reading, references and study units. However, it is desirable in all degree level education to demonstrate that you have read and researched more widely than the required minimum. Using other references will give you a broader viewpoint and may provide a deeper understanding of the subject.

FINAL EXAMINATION AND GRADING

The final examination for BFN 748 will not be more than three hours' duration and has a value of 70 percent of the total course grade. The examination will consist of questions, which reflect the types of practice exercises and tutor-marked problems you have previously encountered. All areas of the course will be assessed.

Use the time between finishing the last unit and sitting for the examination to revise the entire course. You may find it useful to review your tutor-marked assignments and comments on them before the examination. The final examination covers information from all parts of the course.

COURSE MARKING SCHEME

Table showing the total course marking scheme is shown below:

ASSESSMENT	MARKS
Assignment 4 (TMAs)	Best three marks of the 4 TMAs @ 10 marks is 30 marks of the course = 40%
Final Examination	60% of overall course marks
Total	**100% of course marks**

COURSE OVERVIEW

This table brings together the units and the number of weeks you should spread to complete them and the assignments that follow them are taken into account.

Unit	Title of Work	Week Activity	Assessment (end of unit
	Module 1		
1	Overview of Financial System	1	Assignment 1
2	Efficient Financial System and Economic Development	1	Assignment 2
3	The Financial Markets		
4	Financial Market Operations (Money Market)	1	Assignment 3
5	Financial Market Operations (Capital Market)		
	Module 2		
5	Nigerian Financial Market Regulators	1	Assignment 4
6	Money Market Instruments		
7	Capital Market Instruments		
	Module 3		
8	Banking Institution	1	Assignment 5
9	Bank Categorization	1	Assignment 6
10	Commercial Banking		
11	Development/Specialized Banking Institutions	1	Assignment 7
12	Bank Income and Investment Policy		

	Module 4		
13	Insurance Institutions		
14	Pension Institutions and Administration		
15	Informal Financial Markets		
16	Informal Financial Institutions		
	Module 5:		
17	International Finance Institutions	1	Assignment 8
	Revision		
	Total	**17**	

HOW TO GET THE MOST FROM THIS COURSE

In distance learning, the study units replace the university lecturer. This is one of the great advantages of distance learning education. You can read and work through the specially designed study materials at your own pace, and at a time and place that suits you best. Think of it as you read the lecture notes and that a lecturer might set you some readings to do.

The study unit will tell you when to read your other materials. Jut as a lecturer might give you an in-class exercise, your study units also provide assignments for you to do at appropriate points.

Each of the study units follows a common format. The first item is an introduction to the subject matter of the unit, and how a particular unit is related with the other units and the course as a whole.

Next is a set of learning objectives. These objectives let you know what you should be able to do by the time you have completed the unit. You should use these objectives to guide your study. When you have finished the unit, you must go back and check whether you have achieved the objectives set. If you make a habit of doing this, you will significantly improve your chances of passing the course.

The main body of the unit guides you through the required reading from other sources. This will usually be either from **Reading Section** or some other sources.

Self-tests/assignments are interspersed throughout the end of units. Working through these tests will help you to achieve the objectives of the unit and prepare you for the examinations. You should do each of the assignments as you come to it in the study unit. There will also be numerous examples given in the study units, work through these when you come to them too.

The following is a practical strategy for working through the course. If you run into any trouble, telephone your tutor. When you need help, don’t hesitate to call and ask your tutor to provide it. In summary:

(1) Read this course guide.

(2) Organise a study schedule. Refer to the course overview for more details. Note the time you are expected to spend on each unit and how the assignments relate to the unit. Important information e.g. details of your tutorials and the date of the first day of the semester is available. You need to gather together all information in one place, such as your diary or a wall calendar. Whatever method you choose to use, you should decide on and write in your own dates for working on each unit.

(3) Once you have created your own study schedule, do everything you can to stick to it. The major reason that students fail is that they get behind with their coursework. If you get into difficulty with your schedule, please let your facilitator know before it is too late for help.

(4) Turn to unit 1 and read the introduction and the objectives for the unit.

(5) Assemble the study materials. Information about what you need for a unit is given in the 'Overview' at the beginning of each unit. You will always need both the study unit you are working on and one of your set books, on your desk at the same time.

(6) Work through the unit. The content of the unit itself has been arranged to provide a sequence for you to follow. As you work through this unit, you will be instructed to read sections from your set books or other articles. Use the unit to guide your reading.

(7) Well before the relevant due dates (about 4 weeks before the dates) access the Assignment file on the web and download your next required assignment. Keep in mind that you will learn a lot by doing the assignments carefully. They have been designed to help you meet the objectives of the course and, therefore, will help you pass the examination. Submit all assignments not later than the due dates.

(8) Review the objectives for each study unit to confirm that you have achieved them. If you feel unsure about any of the objectives, review the study material or consult your tutor.

(9) When you are confident that you have achieved a unit's objectives, you can then start on the next unit. Proceed unit by unit through the course and try to pace your study so that you keep yourself on schedule.

(10) When you have submitted an assignment to your tutor for marking, do not wait for its return before starting on the next unit. Keep to your schedule. When the assignment is returned, pay particular attention to your facilitator's comments. Consult your tutor as soon as possible if you have any questions or problems.

(11) After completing the last unit, review the course and prepare yourself for the final examination. Check that you have achieved the unit objectives and the course objectives.

TUTORS AND TUTORIALS

There are eight (8) hours of tutorials provided in support of this course. You will be notified of the dates, times and location of these tutorials, together with the names and phone numbers of your tutors, as soon as you are allocated a tutorial group.

Your tutor will mark and comment on your assignments, keep a close watch on your progress and on any difficulties you might encounter as they would provide assistance to you during the course. You must mail your tutor-marked assignments to your tutor well before the due date (at least two working days are required). They will be marked by your tutor and returned to you as soon as possible. Do not hesitate to contact your tutor by telephone, e-mail, or discussion board if you need help. The following might be circumstances in which you would find help necessary.
Contact your tutor if:

- you do not understand any part of the study units or the assigned readings;
- you have difficulty with the tutor-marked assignments;
- you have a question or problem with an assignment or with your tutor's comments on an assignment or with the grading of an assignment.

You should try your possible best to attend the tutorials. This is the only chance to have face-to-face contact with your tutor and to ask questions which are answered instantly. You can raise any problem encountered in the course of your study during such contact. To gain the maximum benefit from course tutorials, prepare a question list before attending them. You will learn a lot from participating in discussions actively.

SUMMARY

As earlier stated, the course BFN 748 is designed to introduce you to various techniques, guides, principles and practices relating to Financial Institutions and markets.

We hope you enjoy your acquaintances with the National Open University of Nigeria (NOUN) and wish you every success in the future.

COURSE CODE: BFN 748

COURSE TITLE: FINANCIAL INSTITUTIONS AND MARKETS

COURSE MATERIAL DEVELOPMENT

COURSE WRITER: **Dr. Eleje, Edward Ogbonnia**
Department of Banking and Finance
Faculty of Humanities, Management & Social Sciences
Federal University, Wukari
Taraba State

COURSE EDITOR: **DR. ADO AHMEDD**
Associate Professor of Finance
Department of Accounting and Finance
Abubakar Tafawa Balewa University, Bauchi

PROGRAMME COORDINATOR: DR OKOH, JOHNSON IFEANYI

Department of Financial Studies

Faculty of Management Sciences

HEAD OF DEPARTMENT **DR. OFE INUA**

Department of Financial Studies

Faculty of Management Sciences

TABLE OF CONTENTS

MODULE 1 CONCEPT OF FINANCIAL SYSTEM

Welcome to the first module of this course. The units under this module are as stated below:

UNIT 1 OVERVIEW OF FINANCIAL SYSTEM

CONTENTS

1.0 INTRODUCTION

You are welcome to the first unit of the first module in this course and we hope you will have a rewarding experience in your study. The basic objective of this unit is to acquaint students with proper conceptualization of the meaning, nature as well as structure of the financial system.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- define the concept financial system;
- state and explain the nature of financial system.
- enumerate and discuss the structure of financial system.

3.0 MAIN CONTENT

This afternoon, a typical NOUN student bought Fan Fresh Yogurt at a supermarket, paying for it with an ATM card. Then she jumped into her insured car, and drove to the university, which she attends thanks to her student loan. She may have left her parents' home, which is mortgaged, a few minutes early to avoid construction work on a new hostel, financed by bonds issued by the university. Or perhaps she needed to stop at the university computerized bookstore to purchase this Financial Institutions and Market textbook, using her credit card, before her class began.

Underneath the surface, each financial transaction in this story - even the seemingly simple ones - is quite complicated. If the supermarket owner and the student use different banks, paying for the yogurt will require an interbank funds transfer. The company that insures the student's car has to invest the premiums she pays until they are needed to pay off claims. The student's parents almost surely obtained their home mortgage through a mortgage broker, whose job was to find the cheapest mortgage available. And the bonds the university issued to finance construction of the new hostel were created with the aid of an investment bank.

This brief example hints at the complex web of interdependent institutions and markets which form the foundation for our daily financial transactions. The system is so large, so efficient, and generally speaking, so well run that most of us rarely take note of it. The system is called the financial system. A financial system is like air to an economy: If it disappears suddenly, everything would grind to a halt. So, what happens in the financial system - whether for good or for bad - matters greatly to all of us. To understand the system and how it works therefore, let's take a painstaking look into the proceeding sub-sections.

3.1 Meaning of Financial System

To expound properly the term 'financial system', it is highly imperative to explain the meaning and qualities of a system. These will in no small measure substantiate the conceptualization of the dynamic nature of financial system. Hornby (2000) defined a system as a set of ideas, theories, procedures, etc. according to which something is done. A system is also explained to mean an organized group of connected or interdependent components called subsystems which are linked together according to plan, to achieve specific objects (Jozee, 2015). A system is also a whole composed of parts in orderly arrangement according to some scheme or plan. From these above positions, a system can be summarized as an assemblage of objects arranged in regular subordination, or after some distinct method, usually logical or scientific; a complete whole of objects related by some common law, principle, or end; a complete exhibition of essential principles or facts, arranged in a rational dependence or connection; a regular union of principles or parts forming one entire thing; such as, a system of philosophy; a system of government; a system of divinity; a system of botany or chemistry; a military system; the solar system. Hence, every system has basic components which are in a functional relationship with each other and these have specific objectives. What then is a financial system?

A financial system of any economy is that system that bridges the gap between the deficit borrowers and the surplus Lenders in the economy. This type of system operates with institutional units and markets that interact, typically in a complex manner, for the purpose of mobilizing funds for investment and providing facilities, including payment systems, for the financing of commercial activities. According to the Central Bank of

Nigeria research series (1993) the Nigerian financial system refers to a set of rules and regulations and the aggregation of financial arrangements, institutions, agents, that interact with each other and the rest of the world to foster economic growth and development of a nation. A national financial system differs from the Global Financial System. The Global Financial System is a financial system consisting of institutions and regulations that act on the international level, as opposed to those that act on a national or regional level. The main players are the global Institutions, such as International Monetary Fund (IMF) and International Bank for Reconstruction and Development (IBRD). The financial system is a prime mover of economic development. It achieves this through the intermediation process, which entails providing a medium of exchange necessary for specialization and the mobilization of savings from surplus units to deficit units. Through this process, there is an enhanced productive activity which positively influences aggregate output and economic growth. It means the system ensures the efficient transfer of savings from those who generate them to those who ultimately use them for investment or consumption. Apparently, the financial system has been argued as the life wire of the contemporary economy without which no modern economy can thrive unperturbed (Eleje, 2009). A well-functioning financial system is thus a desideratum for a healthy economy due to its relevance to growth and development.

3/2 Nature of the Financial System

The financial system by its very nature is not just the institutions that expedites payments and extend credits. It incorporates all those activities and functions that direct real resources to their ultimate uses. In this sense, it is the central nervous system of a market economy. The financial system according to Crockett (2011) contains a number of separate, though interdependent components, all of which are essential to its effective working. First is the set of intermediaries such as banks, brokerage firms and insurance companies which act as principals in assuming liabilities and acquiring claims. The second component is the markets in which claims are exchanged. These include those for equity and fixed interest securities, as well as exchanges or over-the-counter markets for foreign currencies, commodities and derivative contracts. The third is the infrastructure necessary for the effective interaction of intermediaries and markets. Such infrastructure includes securities exchanges; payment and settlement systems; and the mechanisms that provide contractual certainty, and in addition generate and verify the information on which efficient financial intermediation rely upon. This would include credit ratings, accounting, auditing and financial analysis, as well as the supervisory and regulatory framework.

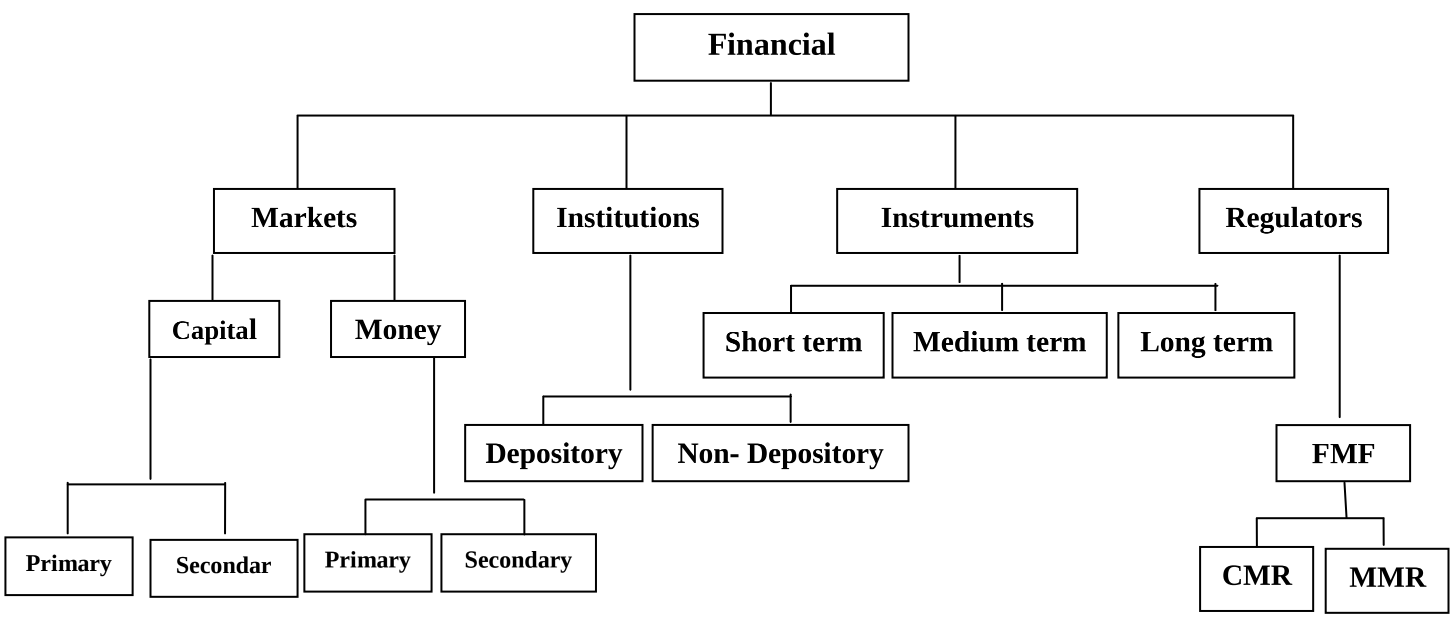
Meanwhile, the above components of the financial system, intermediaries, markets and infrastructure, are inextricably interconnected. Intermediaries require infrastructures to exchange and secure claims. They also need markets in which to hedge the risks arising from their intermediation activities. Markets only function efficiently when strong institutions are available to provide liquidity, and information providers support efficient price discovery. Hence, the various components of the financial system work together to improve available information to guide the effective and efficient allocation of resources and thus strengthening growth potential in the economy.

3.3 Structure of the Financial System

The financial system is composed of complex and dynamic structure. The structure provides avenue for organizing and managing the payments system, mechanisms for the collection and transfer of savings by banks and other depository institutions; arrangements covering the activities of capital markets with respect to the issue and trading of long term securities, arrangement covering the workings of the money market in respect of short-term financial instruments; and arrangements covering the activities of financial markets complementary to the money and capital markets for example the foreign exchange market, the arrangements for risk insurance; the futures market etc (Nzotta, 1999). In addition, the structure provides mechanism for stringent regulation and control of market operations to guarantee trust and confidence in the entire financial system.

A sound financial system is made up of four major interdependent pillars among which are the financial market, financial institutions, financial Instruments, and financial regulators (Okafor, 1983; Eleje, 2016). These pillars as detailed in subsequent modules could be structured diagrammatically:

Figure 1: Structure of the Financial System



Source: *Eleje, (2016)*

KEY:
FMF = Federal Ministry of Finance
CMRs = Capital Market Regulators
MMRs = Money Market Regulators

4.0 CONCLUSION

The financial system explains a complex and dynamic web of interdependent institutions, rules, instruments as well as markets which form the foundation for daily financial transactions. The system is so large, so efficient, and well run. It is like air to an economy; if it disappears suddenly, everything would grind to a halt. A financial system of any economy is that system that bridges the gap between the deficit borrowers and the surplus Lenders in the economy.

Financial system refers to a set of rules and regulations and the aggregation of financial arrangements, institutions, agents, that interact with each other and the rest of the world to foster economic growth and development of a nation. The financial system by its very nature is not just the institutions that expedites payments and extend credits. It incorporates all those activities and functions that direct real resources to their ultimate uses.

The system is made up of complex and dynamic structure. The structure provides avenue for organizing and managing the payments system, mechanisms for the collection and transfer of savings by banks and other depository institutions; arrangements covering the activities of capital markets with respect to the issue and trading of long term securities, arrangement encompassing the activities of the money market with respect to short-term financial instruments; and arrangements covering the activities of the aggregate financial markets complementary to the money and capital markets.

5.0 SUMMARY

In this unit, we defined the concept of financial system, explain the nature of financial system and discussed the structure of the financial system.

In the next unit, we shall examine the role of an efficient financial system to economic development.

6.0 TUTOR MARKED ASSIGNMENT

The financial system contains a number of separate but interdependent pillars very essential to its effectiveness. Identify and epitomize these major pillars.

7.0 REFERENCES/FURTHER READINGS

Crockett, A. What Financial System for the 21st Century? (Basel: Per Jacobson 2011)

UNIT 2: EFFICIENT FINANCIAL SYSTEM AND ECONOMIC DEVELOPMENT

CONTENTS

1.0 INTRODUCTION

In the preceding unit, we defined the concept of financial system, explain the nature of financial system and discussed the structure of the financial system.

In this unit, we shall examine the role of an efficient financial system to economic development.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- explain the nature of an efficient financial system;
- enumerate and discuss the role of efficient financial system to development;
- list and explain the contributions of efficient financial system to development.

3.0 MAIN CONTENT

The financial system remains sound and well placed to support expansion of the economy. However, the extent to which this can be achieved depends on the degree of efficiency or soundness of the system. Financial system efficiency explains the ability of the financial system to allocate financial resources to the most productive use. This means that an efficient financial system is fundamental to supporting growth and productivity in an economy. The objectives of this unit are to appraise the nature, roles and contributions of an efficient financial system to economic development of nations.

3.1 Nature of an Efficient Financial System

An efficient financial system is that system that allocates scarce financial and other resources for the greatest possible benefit to its economy, promoting a higher and more sustainable rate of productivity, and economic growth. It is that system that enables economic resources to be allocated to their best use across time and space without imposing unnecessary costs or rents on households and business (Box, 2014). An efficient financial system enables savers and borrowers to share risks in a way that enhances rather than hinders economic progress. Such a system must possess certain basic interconnected attributes which are germane to its efficient operation. First, a sound financial system must have a high level of confidence. That is to say, the participants must trust in the system. Integrity and trust should be the hallmarks of an efficient financial system.

Secondly, an efficient financial system must be able to sustain the intermediation process. To achieve this, it must have in place a large number of intermediaries and participants who must stand ready to engage in healthy competition amongst themselves and within confines and boundaries specified by law and code of professional ethics. Again, there should be a high degree of flexibility in the financial market. To this end, the instruments employed and the methods of operation should be market based, so that the market can respond and adapt to changes in economic and financial structure, no matter how small the change may be. Moreover, an efficient financial system must allow for balance in operations of the market. This means that there should be an optimal mix of various types of financial institutions with respect to both the transfer of current savings and the stock of past savings.

3.2 Roles of the Financial System to Economic Development

There exists a plethora of research findings which shows that the level of financial system development in any nation is the best indicator of general economic development potential. Classical studies for instance, Goldsmith (1969) documented that financial system development is of prime importance because the financial superstructure, in the form of both primary and secondary securities, accelerates economic growth and improves economic performance, to the extent that it facilitates the migration of funds to the best user i.e. to the place in the economic system where the funds will yield the highest social return. The implication here is that the financial system will discriminate against inefficient funds users. In helping as a vehicle to economic development, the financial system tries to achieve the basic function of resource intermediation. Here, through various institutional structures, they vigorously seek out and attract the reservoir of idle funds and allocate same to entrepreneurs, businesses, households and governments, for investments and use in various projects and purposes, with a view of returns. Alternatively, they may exploit their quasi-monopolistic position and fritter away investment possibilities with unproductive investments (CBN, 2004). It is therefore an axiom that without financial wherewithal, no business enterprise (small, medium, or big) or government can perform its productive functions effectively and efficiently. Consequently, financial resources affect business development.

The financial system plays the crucial role of improvement and sustains the efficient mobilization and allocation of financial resources in an economy. It also provides structures for the management of liquidity for financial assets and instruments. According to a report on the Nigeria system (1976), the financial system should perform the following functions:

- Facilitate effective management of the economy;
- Provide non-inflationary support to the economy;
- Achieve greater mobilization of savings and its efficient and effective channeling;
- Ensure that no viable project is frustrated simple for lack of funds;
- Insulate the economy as much as possible and as much as desirable from the vicissitudes of international economic scenes; effectively sustain the indigenization (ownership, control and management) of the economy; assist in achieving significant transformation of the rural sector; and assist in achieving a greater integration and linkages in agriculture, commerce and industry.

The functions above convey the enormous role the system plays in economic development. In addition to the above, the system provides adequate hedge to risk averse investors to hold a diversified portfolio of financial assets, as a protection against the premature liquidation of the firms in which they invested.

3.3 Contributions of the Financial System to Economic Development

The financial system guarantees that there is a sufficient stock of money to enhance the productive process in the economy. An adequate stock of money ensures that there is monetary balance and stability. The financial intermediation roles of the financial system manifest significant contributions to the process and magnitude of economic growth in several ways:

1. They improve efficiency in resource mobilization by pooling a myriad of individual savings of various persons;
2. They provide efficient allocation of savings into investment outlets,
3. They increase the fraction of societal resources devoted to interest yielding assets and long run investments, which in turn augments economic growth;
4. They reduce risk faced by firms in their production processes by providing liquidity to various financial assets.
5. They enable investors improve their portfolio diversification providing insurance and project monitoring information; and
6. They induce enterprises to operate more efficiently by monitoring loan projects by offering financial protection against premature liquidation of their capital.

In addition to the above issues, the financial system provides the necessary environment for the implementation of various economic policies of the government intended to achieve non-inflationary growth, high levels of employment, exchange rate stability, balance of payment equilibrium and foreign exchange management.

4.0 CONCLUSION

The central focus of the financial system is to support expansion of the economy as a whole. But the extent to which it can discharge this responsibility depends on the degree of its efficiency or soundness. A fully efficient financial system accomplishes the crucial role of improvement and sustains the efficient mobilization and allocation of financial resources in an economy. It also provides effective structure for the management of liquidity for financial assets and instruments.

An efficient financial system is that system that allocates scarce financial and other resources for the greatest possible benefit to its economy, promoting a higher and more sustainable rate of productivity, and economic growth. It is a system that enables savers and borrowers to share risks in a way that enhances rather than hinders economic progress. Such a system must possess certain basic interconnected attributes necessary to its efficient operation.

Efficient financial system contributes to economic development by improving and sustaining the mobilization and allocation of financial resources. It enables investors improve their portfolio diversification by providing insurance and project monitoring information. It also provides structures for the management of liquidity for financial assets and instruments. By so doing, it guarantees that there is a sufficient stock of money to enhance productivity. The financial intermediation roles of the system also manifest its significant contributions.

5.0 SUMMARY

In this unit, we have examined the role of an efficient financial system to economic development.

In the next unit, you will be introduced to the financial markets.

6.0 TUTOR MARKED ASSIGNMENT

Justify the contributions of an efficient financial system to economic development of a prototype economy such as Nigeria.

7.0 REFERENCES/FURTHER READINGS

Box C, Measuring Financial System Efficiency (New Zealand, Reserve Bank Financial Stability Report, 2014).

UNIT 3: THE FINANCIAL MARKETS

CONTENTS

1.0 INTRODUCTION

In the last unit, we examined the role of an efficient financial system to economic development.

In this unit, you will be introduced to the financial markets. This discussion will lead to explaining the nature of financial markets, classifying the financial markets and explaining how the developments of financial markets in Nigeria took place.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- conceptualise the nature of financial markets;
- classify the financial markets; and
- trace the developments of domestic financial markets in Nigeria.

3.0 MAIN CONTENT

Financial market explains an arrangement that contract entities to trade financial claims under some established rules of conduct. The structure of a country's financial markets is dictated by economic and financial development of its economy. As a country experiences growth in its wealth and income, its financial structure also becomes richer in financial assets, institutions and markets. There is therefore need for comprehensive appraisal of financial markets because current effort towards global monetary integration necessitates an examination of its likely impact on the economy.

3.1 Nature of Financial Markets

Financial market could be defined as a forum for the exchange of financial products denoted in some cases by a physical location, but in others by a common electronic information system sharing data on prices and volumes transacted and where a number of professionals take an active part in the market processes. Financial markets in general deals in financial assets and liabilities of various maturities and consist of institutions, instruments, rules and regulations which guides the mobilization of funds from the surplus units of the economy to the deficit units. The financial market in any country is one of the major pillars of growth and development. The market serves the function of enabling the efficient allocation of financial resources among the economic agents. It serves as the channel through which the surplus funds are transmitted between surplus units and the deficit units. In addition, the market serves a broad range of clientele, including different levels of government, corporate bodies, and private individual investors.

3.2 Classifications of Financial Markets

Conventionally, financial markets can be broadly divided into money and capital markets. These markets can further be categorized into primary and secondary markets, with the former concerned basically with raising new funds and the latter with trading on existing securities.

The Nigerian markets have informal elements which reflect the duality of the economy. These informal financial markets are where transactions in financial products are largely outside the ambit of government regulation. Although their existence pre-dates the formal financial markets, their continued relevance is ascribed primarily to the absence of elaborate documentation procedures and other regulations including collateral requirements for transactions in the formal financial markets. The most prominent forms of the informal financial markets in Nigeria include the Rotating Savings and Credit Associations (ROSCAs), pawn brokers and money changers (CBN, 2004). The Nigerian financial markets in terms of structure are unique and different from those of most other countries. This is due to several factors, including the dual nature of the economy, the agrarian nature of production, and communal restrictions and laws that guide savings mobilization. In addition, the rudimentary level of technological transformation as well as the prevalence of a strong cash economy has hindered the growth of the markets to meet global demands.

3.3 Developments of Financial Markets in Nigeria

Before the advent of the modern financial markets in Nigeria, the informal financial markets had been in operation in the form of money lending of varying maturities, ranging from short to long-term. But these traditional markets were predominantly featured by lack of established rules and guidelines and imposition of exorbitant interest rates by money lenders (Okafor, 2011). Financial market activities then were consummated devoid of the modern financial instruments but rather based on mutual agreement or pledge of physical assets as well as rendering of service by borrower to the lender to liquidated debt obligations. The modes of operation varied from culture to culture and still operational today some areas not adequately included by the modern financial markets.

The evolution of the formal financial markets in Nigeria arose from the necessity to root out the outflow of excess funds into investment outlets in the London money and capital markets. The second rationale was the need to develop markets that would stimulate effective and efficient monetary management by promoting portfolio management of the deposit money banks' (DMBs) and facilitating long-term capital mobilization through the capital market.

Consequently, the formal financial market in Nigeria evolved in the early 1960s. This follows the issuing of the first treasury bills of N8.0 million by the Central Bank of Nigeria (CBN) in April 1960 and the establishment of the Lagos Stock Exchange (LSE) which commenced operation in June 1961. Other subsequent financial market infrastructure and institutions were put in place to enhance the functioning of the markets. Such institutions include the establishment of the Securities and Exchange Commission (SEC) in 1979, as well as the incorporation of issuing houses and numerous stock broking firms.

4.0 CONCLUSION

The flow of financial resources in an economy is driven by the differences in the size of the fund, maturity and the risk content. Financial markets perform this role by transforming funds in the system in such a manner that the needs of both the ultimate providers and users of funds are met. The efficient mobilization and allocation of financial resources among economic agents in the economy stimulates economic activities and thus contributes significantly to economic development.

Financial market could be defined as a forum for the exchange of financial products denoted in some cases by a physical location, but in others by a common electronic information system sharing data on prices and volumes transacted and where a number of professionals take an active part in the market processes. The market is divided into money and capital markets. These markets can further be categorized into primary and secondary markets, with the former concerned basically with raising new funds and the latter with trading on existing securities.

Prior to the emergence of modern financial markets in Nigeria, the informal financial markets had been in operation in the form of money lending of varying maturities, ranging from short to long-term. The evolution of the formal financial markets in Nigeria arose from the necessity to root out the outflow of excess funds into investment outlets in the London money and capital markets.

5.0 SUMMARY

In this unit, we have conceptualised the nature of financial markets. We also classified the financial markets and traced the developments of the domestic financial markets in Nigeria.

In the next unit, we shall examine the financial market operations as it affects the money markets.

6.0 TUTOR MARKED ASSIGNMENT

Trace the evolution and development of the modern financial markets in Nigeria.

7.0 REFERENCES/FURTHER READINGS

CBN, Financial Markets in Nigeria (Abuja, Central Bank of Nigeria Publication, 2004)

Baye, M. R. & Jansen, D. W. Money, Banking & Financial Markets: An Economics Approach (India, A.I.T.B.S Publishers & Distributor, 2006)

UNIT 4 FINANCIAL MARKET OPERATIONS (MONEY MARKET)

CONTENTS

1.0 INTRODUCTION

In the preceding unit, we conceptualised the nature of financial markets. We classified the financial markets and traced the developments of the domestic financial markets in Nigeria.

In this unit, we shall examine the financial market operations as it affects the money markets. This unit focuses on enriching the knowledge of students with the money market concept, the evolution and growth in Nigeria, and the major motives for the establishment of the Nigerian money market respectively.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- define the money market as a concept;
- trace the evolution and growth of the Nigerian money market; and
- list and explain the objectives or motives for establishing the Nigerian money market.

3.0 MAIN CONTENT

The relevance of short tenured finance for growth and development of nations have been expressed in several socio-economic fora and found to be true. The money market is critical to ensuring the availability and sustainability of this category of funding.

This market plays crucial roles in the provision of short term funding for liquidity management and control of working capital of organization. In so doing, the money market stimulates routine economic activities which in turn trigger growth and development in the economy.

3.1 Concept of the Money Market

The money market is the short arm of the financial market. It is an arrangement whereby short-term financial services are provided. That is, the money market is where the short-term securities are bought and sold. It is the vehicle through which surplus fund units could convey their funds to the deficits units. The security traded in this market has maturity time of not more than one year. The major participants in the money market include individuals, companies, banks, discount houses and government. New issues (securities) and existing issues are initiated and traded in the money market respectively. Therefore, the market like the capital market has both primary and secondary segments. The primary market segment is the market for new issues. It is a market in which new issues/securities are bought and sold for the first time. The secondary market segment is the segment where already existing securities (financial instruments) are bought and sold.

3.2 Evolution and Growth of the Nigerian Money Market

Prior to the establishment of the Central Bank of Nigeria (CBN), there was no formal domestic money market in Nigeria. The Nigerian financial landscape was featured by short-term borrowing based on commercial papers linked to the London money market. Funds were moved from London market to Nigeria for financing export trade. The implication was that Nigerian businessmen and Government had no effective machinery for mobilizing short term funds for their business and development respectively.

With the establishment of the CBN in 1959, it became imperative to institute a formal local money market to provide avenues for investment in domestic liquid assets. Accordingly, the CBN Treasury Bills Ordinance of 1959 was enacted resulting in the release of the first indigenous Treasury bill in 1960. Hence, the first ever monetary instrument issued in Nigeria is the CBN Treasury bill. This was followed by Call Money Fund also initiated in the same year. The major Call Money Fund was issued by CBN in 1962. The issue of other money market instruments followed subsequently. Commercial Paper (CPs) and Treasury Certificates (TCs) were both introduced in 1968 while Certificate of Deposits (CDs), Bankers' Unit Fund (BUF) and Eligible Development Stock (EDS) were introduced in 1975 (CBN, 2000). TCs were introduced with an issue of N20.0 million as part of measure to prosecute the Nigerian civil war. Thereafter, TCs issuance followed the fortunes of the Federal Government finances, being suspended in times of buoyancy and reactivated during periods of financial pressures, until 1996 when it was finally discontinue.

Right from its inception, the Nigerian money market has witnessed phenomenal increase on its market instruments. This was made possible as more commercial and merchant banks were established in anticipation of meeting the need for domesticalising the Nigerian financial system, which was hitherto directly linked to the London financial market. Another feature of the money market is the overwhelming preponderance of government instruments in the market like TBs, TCs and EDS among others.

The corollary from the above shows that government has remained the most active participant in the money market right from its early stage. The federal government's development projects were mainly financed through the issuing of money market instruments. Example is the financing of the second development plan of 1962-1968. Also between 1967 and 70 in the midst of the civil war, the federal government use the money market to prosecute the emergence of rise in oil revenue. During the same period, TBs issued stagnated with new issues made mainly to replace maturing bills.

In terms of composition, the value of treasury instruments, especially treasury bills and certificates, dominated the Nigerian money market, accounting for 65.6 percent in 1965 and 98.4 percent in 1992. Since their introduction, both NTBs and TCs have witnessed tremendous growth. From N18.0 million in 1960 the value of NTBs increased to ₦221.8 billion in 1998, while TCs rose from a modest amount of ₦20.0 million in 1968 to ₦23.6 billion in 1995. The issuance of TCs was discontinued in 1996, while the existing ones were converted into NTBs, which in 2003 had a cumulative value of ₦825.1 billion and ₦2772.87 billion in 2015 respectively (CBN, 2015). CPs relative to NTBs was less popular and was over-shadowed by CDs between 1976 and 1991 before the issuance of CDs was discontinued in 1997. There were also significant growth in the level of CDs between 1978 and 1991 before the incidence of distress in the Nigerian financial system, predominantly the banking sector distress and failure in that era. In similar vein, bankers' acceptances (BAs) and CPs increased significantly between 1991 and 1998. Indeed, BAs, which debuted in 1991, assumed prominence especially from 1996 when it was second to NTBs for a greater part of the period up to 2003 (CBN, 2004). The prominence of CPs and bankers' acceptances in recent times is indicative of their attractiveness to private sector firms as a convenient way of raising short term finance.

3.3 Motives for the Establishment of the Nigerian Money Market

The following factors prompted the establishment of the money market in Nigeria:

- Localizing the credit base of the economy. This was meant to provide local investors the avenue for retention of funds in Nigeria and for the investment of fund repatriated from abroad.
- To provide the needed machinery for the provision of short term financing to the government.
- To establish monetary autonomy. This is a prerequisite for the working of a sovereign state.
- The need for the country to enjoy the functions of money market especially in the operating and executing of government monetary system effectively.

4.0 CONCLUSION

Money market operation was formally initiated in Nigeria in 1959 when the CBN Treasury Bill Ordinance was enacted. The Ordinance subsequently resulted in the release of the first indigenous Treasury bill in 1960. The Nigerian money market since that period has witnessed phenomenal increase on its market instruments. This was made possible as more commercial and merchant banks were established in anticipation of meeting the need for domesticalising the Nigerian financial system.

The money market is the short arm of the financial market. It is an arrangement whereby short-term financial services are provided. Prior to the establishment of the Central Bank of Nigeria (CBN), there was no formal domestic money market in Nigeria. The Nigerian financial landscape was featured by short-term borrowing based on commercial papers linked to the London money market. Several reasons prompted the establishment of the money market in Nigeria among which are:

- To localizing the credit base of the Nigerian economy.
- To provide the needed machinery for the provision of short tenured financing to the government.
- To establish monetary autonomy, and;
- To guarantee the need for the country to enjoy the functions of money market.

5.0 SUMMARY

In this unit, we focused on enriching the knowledge of students with the money market concept, the evolution and growth in Nigeria, and the major motives for the establishment of the Nigerian money market respectively.

In this next unit we shall consider the capital market arm of the Nigerian financial markets.

6.0 TUTOR MARKED ASSIGNMENT

Carefully examine the motives for the establishment of the Nigerian money market.

7.0 REFERENCES/FURTHER READINGS

Nzotta, M. S., Money, Banking and Finance: Theory and Practice, (Owerri, Continental Educational Books and Publishers, 1999)

Okafor, F. O., Micro Credit: An Instrument for Economic Growth and Balanced Development (African Banking and Finance Review, 1(1) 2000)

UNIT 5 FINANCIAL MARKET OPERATIONS (CAPITAL MARKET)

CONTENTS

1.0 INTRODUCTION

In the last unit, we focused on enriching the knowledge of students with the money market concept, the evolution and growth in Nigeria, and the major motives for the establishment of the Nigerian money market respectively.

In this unit we shall consider the capital market arm of the Nigerian financial markets.

2.0 OBJECTIVES

By the end of this unit, students should be able to understand the nature of the capital market; evolution of the Nigerian capital market; structure of the Nigerian capital market; operational mode of the Nigerian capital market; as well as capital market objectives, functions, challenges and prospects.

3.0 MAIN CONTENT

Long run high growth of an economy requires mobilization of huge amount of savings and then its allocation to the highest return assets/projects. For such efficiency, a well-developed capital has always been a requirement. Hence, the importance of a well-functioning capital market to facilitated long tenured financing for the stimulation and growth of an economy cannot be overstated. Capital market is pivotal to financial and economic development. They act as conduits through which funds from surplus sectors of the economy are channeled to the deficit sector for long term investment purposes. This fundamental role dictates the benchmark upon which the efficiency of the market is measured.

3.1 Nature of the Capital Market

Capital market is the long arm of the financial system. The market interactions facilitate the exchange of long-term funds between savings-surplus and savings-deficit economic units (Okafor, 1983). It is comprised of markets and institutions, which facilitate the issuance and trading of the long-term financial instruments. The market provides funds to industries and governments to meet their long-term capital requirements such as financing of fixed investment like building, plants, machinery, bridges, etc. Capital market therefore plays a pivotal role in stimulating industrial activities which invariably induce economic growth and development. Capital market has both primary and secondary markets. The major participants in the capital market include stock exchange, commercial banks, merchant banks, government, corporate organizations, insurance companies and individuals. There are four major instruments used in the capital market. They include: debt instruments, preferred stock, common stock and risk asset instruments. Details about these instruments would be discussed later in the subsequent section. The most common nature of the capital market is that it is the market for long term securities and provides services that are essential to a modern economy. It provides access to a variety of financial instruments that enable economic agents to pool price and exchange rate risks.

3.2 Evolution of the Nigerian Capital Market

At independence in 1960, Nigeria had no capital market. The predominance of the foreign owned commercial and merchant banks did not encourage the provision of capital market in Nigeria. It meant that those who had surplus funds to their immediate requirements had no market for them in the country. The only option opened to them was to repatriate those funds for investment overseas. This resulted in a negative net capital flow at a time when the country needed all the funds it could lay hands on for developmental purposes. Both Nigerian businessmen and the government had no effective means of financing their capital investment during the period. The effect of this brought about the establishment of capital market in Nigeria. The operationalization of the Nigeria capital market has its roots from the establishment of Lagos Stock Exchange (LSE) in 1960. It commenced business on 15th September 1961. The Nigeria Stock Exchange Act transformed the Lagos Stock Exchange to the Nigeria Stock Exchange (NSE) in 1977. Another key capital market institution, the Nigeria Securities and Exchange Commission (NSEC) was also established in 1977 to oversee the securities and ensure orderly market operations.

3.3 Structure of the Nigerian Capital Market

Nigeria has a formal and active capital market. The market presently comprises three (3) basic components - market for negotiated capital fund; risk asset market (COMEX), and market for long term securities (Nzotta, 1999; Eleje, 2009):

3.3.1 Negotiated Capital Fund Market:

The market comprises the operations of the informal sector like ESUSU, Adashi, and other forms of thrift savings. It includes market for institutionalized capital fund which encompasses institutionalized schemes that takes the form of consortium lending by associated financial intermediaries. In developing countries like Nigeria, these schemes are mainly government sponsored, otherwise; are joint venture between government and private enterprise. Such schemes in Nigeria include government Industrial Credit Scheme, development finance institutions etc. in brief, market for negotiated capital fund is descriptive of all transactions in capital funds that are not covered by negotiable instruments (Okafor, 1983).

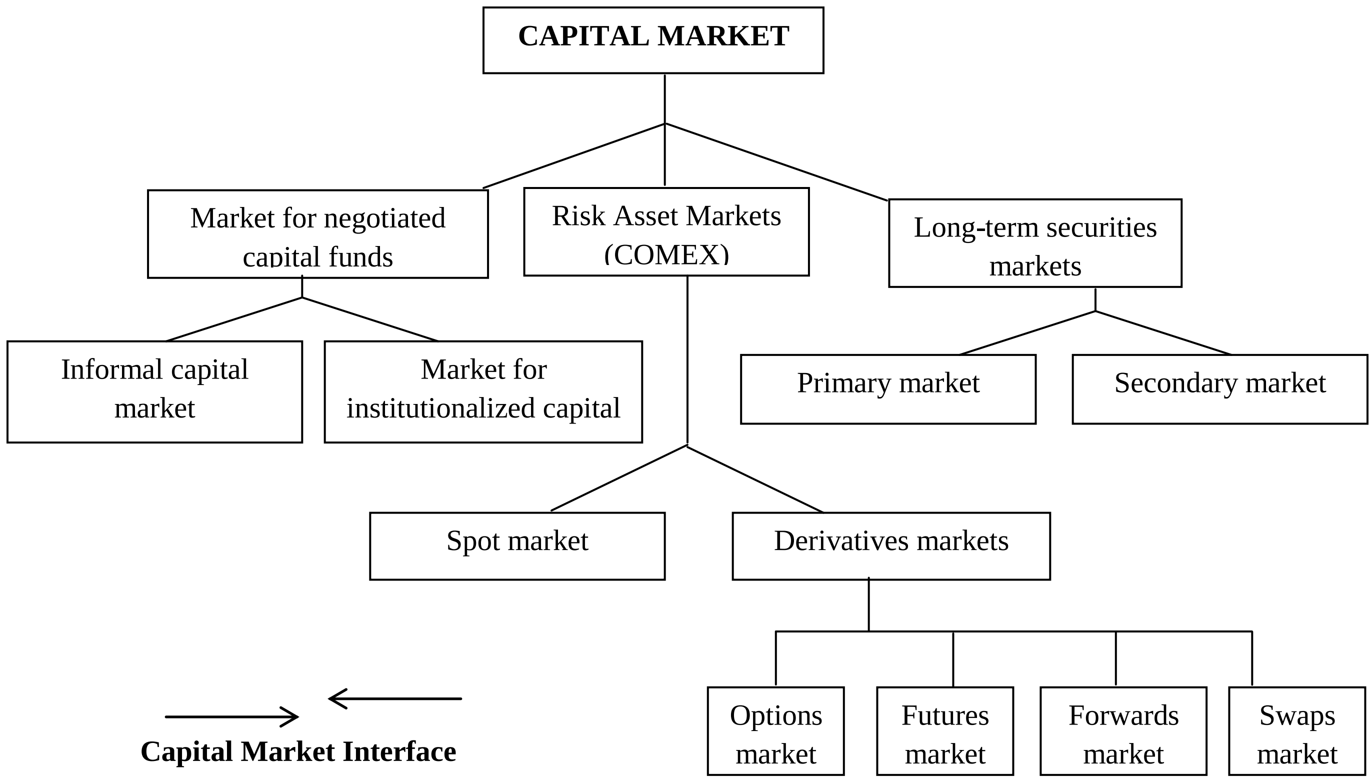
3.3.2 Long-term securities markets:

This is the market for long term securities like bond, rights, equity, preference shares etc. Securities market is classified into "Primary Market' where new securities are quoted, and "Secondary Market" where already existing securities are traded. Example is the stock exchange.

3.3.3 Risk Asset markets:

This arm of the capital market is where both physical assets and market-based risk management instruments are traded. Commodity producers make use of this market to raise long term funds for investment purpose. The market equally offers price insurance to both commodities and securities dealers. It should however be clarified that the relative importance of each of the highlighted segment depends on the stage of development of the economy, as well as the sophistication of its financial system. There is no doubt, for instance that securities market accounts for a higher proportion of capital market transactions in developed than in the developing countries. The diagram below represents the structure of the Nigerian capital market following the incorporation of the Abuja Securities and Commodity Exchange in 2006:

Figure 2: Structure of the Nigerian Capital Market



Source: Eleje (2009:64)

3.4 Operational Mode of the Nigerian capital market

If the government or company wants to raise long-term funds via the capital market, it must consult an issuing house or stockbroker. These specialists provide the government/company with financial advisory services. It is their duty to study the company's performance over the year in order to determine its financial needs. More so, they do not only advice on the best option, they undertake total financial restructuring of the company before introducing the facility to the company.

The stockbrokers and the issuing house liaise with the other parties- Registrars, Trustees, Auditors, Reporting Accountant, and solicitors, etc, to produce a marketing document known as a "**Prospectus**". A prospectus is a document which the public can rely on for making investment decision. For it to be produced, necessary approval from SEC and other bodies are obtained. If the financial option involves listing on the stock exchange, the brokers to the issues ensures that all necessary approval with the exchange are also obtained since only stock-brokers can introduce issues to the exchange. On the completion of the offer, the proceeds of the issue are handed over to the company for executing the proposed business programme on long term investment. Similarly, the securities are then listed on the Daily Official list of the Exchange. Private individuals wishing to invest and trade in the capital market need not go directly as such is not legally permitted. What they should do is to consult a stock broking firm and register with them. The stockbrokers acting as agent then do the trading on their behalf for a stipulated commission (NSE; 2004).

3.5 Objectives and Functions of the Nigeria Capital Market

The primary objective of the Nigerian capital market is to mobilize long term funds for investment to boost the nation's economic growth and development. This objective is embedded in her mission statement which states inter-alia: "promoting the Nigerian capital market to respond to the socio-economic development need of the nation" (NigBiz, 2003). The market functions are consistent with the objectives and missions and include the following:

- Provision of an additional channel for engaging and mobilizing domestic savings for productive investment and representing an alternative to bank deposits, real estate investment and the financing of consumption loans.
- Fostering the development of the domestic financial services sector and the various forms of institutional savings such as life insurance and pension funds.
- Improving the gearing of the domestic sector as well as helping in reducing dependence on borrowing.
- Improving the efficiency of capital by providing market measure of returns on capital and a market mechanism for management changes as compared with the administrative or political mechanism of public sector corporations.
- Capital market facilitates the transfer of enterprises from the public sector to the private sector.
- The market encourages privatization by increasing the marketability of new issues.
- It provides access to finance for new and smaller companies and encourage institutional development in facilitating the setting up of Nigeria's domestic funds, foreign funds, and venture capital funds.
- In summary, the Nigerian capital market helps to stimulate industrial as well as economic growth and development of the Nigerian economy.

3.6 Challenges of the Nigerian Capital Market

The Nigeria capital market faces enormous challenges in providing development capital for an economy that has just taken–off. The recent robust economic growth, spurred by extensive reforms, will require increased long-term funds for its sustenance. The capital market is expected to provide the much needed capital. In particular, the on-going reforms in the various sectors will require more support from the market for funding. Also, the commercial farmers, continuing explosion of the telecom sector and massive rebuilding of economic infrastructure through the PPP, will require huge funding which will exert enormous pressure on the capital market. There is also the need to promote the listing of the small and medium enterprises on the market, to make them grow and acquire best practices in corporate governance. The last and not the least of the challenges is the need to further internationalize capital market to promote the inflow of foreign capital and encourage the listing of Nigerian firms on foreign stock exchanges.

The future of the Nigerian Capital Market is still pregnant with the present money market mind-set of Nigerians to investment in the capital market segment of the financial system. This paper strongly calls for proper orientation to investors in the market must flourish and compete favorably with its foreign counterparts. Besides, the global financial crisis that affected the market needs to be thoroughly explained to the uninformed investors least, the stock market run will persist and this will of course adversely affect the growth of the capital market.

4.0 CONCLUSION

Every economy requires a sophisticated and an efficient capital market to progress because a healthy capital market is sine qua non for the sound fundamentals of an economy. Capital market utilizes the available productive resources to promote capital formation. Ensuring optimal allocation of attained funds to appropriate investment projects is the major agenda for the capital market of any nation. Mobilization and pooling of long term savings, easing the exchange of goods and services are the key features of a well-developed capital market. The more developed the capital market is, the more proper will be the allocation of accumulated funds. Nigerian Capital market is still growing and should be supported. This is because a well-developed capital market for Nigeria can channelize the resources of the nation to the most appropriate and productive projects.

Capital market is the long arm of the financial system. Its interactions facilitate the exchange of long-term funds between savings-surplus and savings-deficit economic agents. It is comprised of markets and institutions, which facilitate the issuance and trading of the long-term financial instruments. Capital market has both primary and secondary markets. The major participants in the capital market include stock exchange, commercial banks, merchant banks, government, corporate organizations, insurance companies and individuals.

At independence in 1960, Nigeria had no capital market. The operationalization of the Nigeria capital market has its roots from the establishment of Lagos Stock Exchange (LSE) in 1960. The market presently comprises three (3) basic components - market for negotiated capital fund; risk asset market (COMEX), and market for long term securities.
If the government or company wants to raise long-term funds via the capital market, it must consult an issuing house or stockbroker. These specialists provide the government/company with financial advisory services. The stockbrokers and the issuing house liaise with the other parties- Registrars, Trustees, Auditors, Reporting Accountant, and solicitors, etc, to produce a marketing document known as a "**Prospectus**" which the public can rely on for making investment decision.

The primary objective of the Nigerian capital market is to mobilize long term funds for investment to boost the nation's economic growth and development. This objective is embedded in her mission statement which states inter-alia: "promoting the Nigerian capital market to respond to the socio-economic development need of the nation". The market however faces enormous challenges in providing development capital for its economy. The recent robust economic growth, spurred by extensive reforms, will require increased long-term funds for its sustenance.

5.0 SUMMARY

In this unit, you were introduced to the nature of the capital market; evolution of the Nigerian capital market; structure of the Nigerian capital market; operational mode of the Nigerian capital market; as well as capital market objectives, functions, challenges and prospects.

We have by this development come to the end of the first module of this course.

6.0 TUTOR MARKED ASSIGNMENTS

a. Critically evaluate the structure and operational modalities of the Nigerian capital market.
b. The Nigeria capital market faces enormous challenges in the provision of development capital for its economy. Do you agree? Justify.

7.0 REFERENCES/FURTHER READINGS

Okafor, F. O. Investment Decisions (London, Cassel, 1983)

Nzotta, M. S. Money, Banking and Finance: Theory and Practice (Owerri, Continental Educational Books and Publishers, 1999).

MODULE 2 REGULATORY FRAMEWORK OF THE NIGERIAN FINANCIAL MARKET AND FINANCIAL MARKET INSTRUMENTS

You are welcome to the second module of this course. The module has three units under it, namely:

Unit 1 Regulatory Framework of the Nigerian Financial Market Regulators
Unit 1 Money Market Instruments
Unit 2 Capital Market Instruments

UNIT 1 NIGERIAN FINANCIAL MARKET REGULATORS

CONTENTS

1.0 INTRODUCTION

You are welcome to the first unit of the second module in this course.

In this unit, you will learn about the financial market regulators. They include: Federal Ministry of Finance; Central Bank of Nigeria (CBN); Bankers Committee; Nigerian Deposit Insurance Corporation (NDIC); National Insurance Commission; Nigerian Pension Commission; Securities and Exchange Commission (SEC); Nigerian Stock Exchange and Abuja Securities and Commodities Exchange.

2.0 OBJECTIVES

By the end of this section, students will properly conceptualize the regulatory roles and operational modes of the Federal Ministry of Finance, the Central Bank of Nigeria, the

Securities and Exchange Commission; the Nigeria Stock Exchange; and the Abuja Securities and Commodity Exchange, among other regulators.

3.0 MAIN CONTENT

3.1 The Federal Ministry of Finance

The Federal Ministry of Finance is the apex regulator of the financial system. It advises the Federal Government on its fiscal operations including operations of both the money and the capital market. It collaborates with the CBN on monetary matters. Before 1991, the responsibility for the supervision and licensing of banks was shared between the Federal Ministry of Finance and the CBN. This was reversed in 1991 when the CBN was allowed to discharge the duty solely. However, in 1997, the CBN enabling laws was amended making the CBN report to the presidency through the Federal Ministry of Finance on issues affecting both the money and capital market. This was also short leaved as the ministry ceased to exercise such control over the financial system in 1998. Nevertheless, it still formulates fiscal policies on the Board of the CBN and the NDIC as well as the monetary policy committee (MPC) of the CBN.

3.2 Central Bank of Nigeria (CBN)

The CBN is the apex regulatory authority for both banking and non-banking financial institutions. While it operates significantly at the money market segment of the financial system, the CBN also plays crucial role in the capital market. Besides, it is the underwriter to the federal government debt issues which it does by absorbing all unsubscribed portions (Nnanna, 1998). The process involves laying down terms and conditions for the issuance of federal government stocks thereby imparting resilience and stability in the market. Moreover, as part of its regulatory role to the capital market, the CBN took active part in setting up the Developmental Finance Institutions by subscribing to their capital (Okafor, 2011).

3.3 Bankers Committee

The Nigeria's bankers committee is a body established to provide and enforce sound banking ethic and global standard best practice to banking institutions in Nigeria. The committee is comprised of Chief Executives of Nigerian Banks, top Management of the CBN and other financial institutions. It has two major sub-committees that work on two broad areas of the banking industry, namely: Monetary and Fiscal matters as well as Ethics and professionalism in banking. The Bankers' Committee, since its inception has deliberated on such varied issues as foreign exchange rules, funding of small and medium scale industries, the reform of the Nigerian payments system as well as the Credit Risk Management System (CRMS) in Nigeria.

3.4 Nigerian Deposit Insurance Corporation (NDIC)

The NDIC was incorporated by Decree No. 22 of 1988 but commenced operations in February 1989. The basic rationale for its establishment is to work in collaboration with the CBN to protect Nigerian deposited funds with banks operational in Nigeria. The NDIC functions as provided by the Act, include;

- To insure all deposit liabilities of licensed banks operating in Nigeria so as to instill confidence in the Nigerian banking system.
- To render assistance in the interest of depositors in situations of imminent or actual financial difficulty of banks, particularly where suspension of payments is threatened, and avoiding damage to public confidence in the banking system.
- To assist the monetary authorities in the formulation and implementation of banking policy so as to ensure good banking practice and fair competition among banks in the country; and,
- To guarantee payments to depositors by insured banks or financial institutions up to a maximum. This is fixed at N50, 000 of assessable deposits of an insured bank in the event of failure.

At the instance of the CBN, the NDIC has executed the role of Receiver/Liquidator of some terminally distressed banks. The NDIC in jointly with the CBN exercises supervisory and regulatory functions in the financial system. On-site examination of banks and discount houses is frequently administered by CBN and the NDIC. Meanwhile, a joint CBN/NDIC Committee on problem banks was set up in the early 90's to review the supervisory processes on distressed banks. However, given the supervisory challenges and the need to attain internationally accepted best practices, the name of this committee was changed in 2000 to CBN/NDIC Committee on supervision. This Committee played crucial role in the organization of the 2002 workshop on the new Basel Capital Accord. It was also instrumental to the development of the contingency planning framework for banking systemic distress and crises resolution.

3.5 National Insurance Commission (NAICOM)

Prior to the creation of the Nigerian Insurance Supervisory Board (NISB) by the federal government in 1992, the Federal Ministry of Finance (FMF) had the sole responsibility of licensing and supervising insurance companies in Nigeria. In 1997, the National Insurance Commission Act No 1 established the National Insurance Commission (NAICOM) to replace the NISB as the regulatory organ in the industry.

The Commission was incorporated to ensure the effective administration, supervision and regulation of insurance business in Nigeria as well as regulate transactions between insurers and reinsurers within and outside Nigeria. It is charged with inspectorate powers by establishing the standards for the conduct of insurance business in Nigeria. It approves rates for premiums and commissions in the insurance industry and protects policy holders and other beneficiaries of insurance contracts. It protects government assets and advises the Federal Government on insurance issues. It also contributes to insurance education programmes of the Chartered Insurance Institute of Nigeria and the West African Insurance Institute.

3.6 Nigerian Pension Commission (PenCom)

Pension Commission was established to regulate, supervise and ensure an effective administration of pension matters. In this regard, the commission is mandated under the Act to inter alia, establish standard rules for the management of pension funds, approve, license and regulate PFAs, PFCs and CPFAs, manage national data bank on pension, impose sanctions or fines on erring employers, PFAs, PFCs and CPFAs and ensure that payment and remittance of contributions are made and beneficiaries of retirement savings accounts (RSAs) are paid as and when due. In order to avoid the illiquidity and un-sustainability that plagued the erstwhile defined benefit (PAYG) system, the Act and subject to enforcement by Pension Commission specifically spelt out the investment of pension assets (Pension Commission, 2010).

3.7 Securities and Exchange Commission (SEC)

The Securities and Exchange Commission is the apex regulatory body of the Nigerian capital market. As the highest regulator, it is legally mandated to regulate the market to achieve the double objectives of investors' protection and the market growth which is predicated on transparency and integrity. The SEC as popularly called is empowered by the Securities and Exchange Commission Decree, 1999 amongst other things to:

- Register and approve all securities for subscription or sale to the public, while ensuring that full disclosure is given in the prospectus and other issue documentation in the case of a public offer;
- Ensure orderly, fair, and equitable dealings in securities.
- Perform market oversight functions through surveillance, monitoring, as well as on/off site inspection to ensure fair play and equitable dealings on the exchange.
- Register commodity and stock exchanges, investment advisers and all market operators with a view to maintaining an enviable standard of conduct and professionalism in the stock market;
- Review, approve, and regulates mergers and acquisitions; and,
- Promote investors education and all categories of intermediaries in the securities market (SEC, 1999).

The major tools employed by SEC to carry out the above regulatory functions include, rules, regulation, registration, investigation, enforcement and market development functions viz; publications and public enlightenment programmes (CBN, 2006).

3.8 Nigerian Stock Exchange (NSE)

The Nigerian Stock Exchange metamorphosed from the Lagos Stock Exchange (Eleje, 2002). It is a self-regulatory organization and supervises the operations of the formal capital market. As a market supervisor or regulator, it provides a mechanism for mobilizing private and public savings and making them available for productive purposes (Ndi-Okereke, 2008). The NSC has since 1977 increased its trading floor to nine (9) as at December, 2006. They include Lagos (1961); Kaduna (1978); Port-Harcourt (1980); Kano (1989); Onitsha (1990); Ibadan (1990); Abuja (1999); Yola (2002), and Benin (2005).

The Exchange has 309 listed securities and 212 listed companies with a total market capitalization of N13.295 trillion as at end-December 2006 (NSE, 2007). The listed securities comprise of government stocks, industrial loans/stocks and equity/ordinary shares of companies. At present, the exchange trade via the Automated Trading System (ATS) which replaced the call over system in April, 1999. Clearing, settlement and delivery of transactions on the NSE are done electronically through the Central Securities Clearing System (CSCS), a subsidiary of the Exchange. The CSCS Limited also known as the "Clearing House" was incorporated in 1997 as part of the effort to make the Nigerian stock market more efficient and investor friendly. The Exchange is a membership institution, with 296 dealing and non-dealing members as at end 2002 (CBN, 2004). The dealing members are the stock brokerage firms, while the non-dealing members are the issuing houses, registrars, etc, as well as individuals who are distinguished in capital market functions operations.

3.9 Abuja Securities Commodities and Exchange (ASCE)

Early attempts to formalize commodity marketing in Nigeria is often traced to the 1930s when the European companies prominent amongst whom include the United African Company (UAC), John Holt, Societe Commerciale Occidentale Agency (SCOA) and Peterson Zochonis (PZ) were directly involved in purchases and exports of Nigeria's major agricultural commodities considered as essential raw materials for overseas industries (Onwumere and Eleje, 2009). This period marked the Commodity Marketing Board era which transcended beyond independence until the introduction of the Structural Adjustment Programme (SAP) in 1986.

With the report of the Odife Committee in 1997, reforms of the capital market were embarked upon again, including further deregulation, which allowed for the establishment of the Abuja Stock Exchange to stimulate competition in the sub-sector. The Exchange was incorporated in 1998, as Abuja Stock Exchange Plc (ASE), with authorized capital of N1.0 billion and paid-up capital of N500 million subscribed to by the shareholders as follows: CBN, 51 percent; National Insurance Corporation of Nigeria (NICON), 30 percent, Nigerian Industrial Bank (NIDB), 9 percent, Nigeria Re-Insurance Corporation, 8 percent; and Nigerian Bank for Commerce and Industry (NBCI), 2 percent. However, the Abuja Stock Exchange was short-lived as it was converted to a Securities and Commodities Exchange. The new Exchange is expected to assist the country in its drive to expand the horizon and contribution of Nigeria's non-oil exports to the gross domestic product (GDP). This is to be achieved through the internationalization and standardization of Nigeria's tradable commodities such as cocoa, sugar, cereals, cotton, rubber and even non-ferrous metals. The direct implication of this is further integration of Nigeria into the global commodities market.

4.0 CONCLUSION

Financial market regulation is an important element of ensuring that properly functioning financial markets exist. An effective regulatory regime fosters financial market development by encouraging the participation of investors and issuers in both money and capital market transactions (Kiyingi and Uwaifo, 2015). The regulatory regime must be robust enough to protect investors without acting as a disincentive to the participation of issuers. Sound regulatory framework has positive impact on the growth of the financial markets by encouraging the participation of investors or issuers. Similarly, speed and efficiency of the regulatory process make the market more attractive to expected users.
Nigerian financial market regulatory framework is getting more robust. Almost every segment of the market operates a regulatory regime. Nonetheless, the market regulatory system must achieve a balance between ensuring investors' protection and enabling efficient capital formation. In addition, the regulatory process must take a reasonable timeframe so as not to discourage potential participants from using the financial markets for their resource mobilization.

The regulatory bodies of the Nigerian financial markets are multi-dimensional. They are those the regulate activities in the money market segment only, those that regulates the capital market only, and those whose regulation interconnect the two segments of the market. Major regulators in the financial market include the Federal Ministry of Finance, Central Bank of Nigeria, Securities and Exchange Commission; the Nigeria Stock Exchange; and the Abuja Securities and Commodity Exchange.

Federal Ministry of Finance is the apex regulator of the financial system. It advises the Federal Government on its fiscal operations including operations of both the money and the capital market. The CBN is the apex regulatory authority for both banking and non-banking financial institutions. While it operates significantly at the money market segment of the financial system, the CBN also plays crucial role in the capital market. The Securities and Exchange Commission is the apex regulatory body of the Nigerian capital market. The Nigerian Stock Exchange is a self-regulatory organization and supervises the operations of the formal capital market in area of provision of stock market mechanism for mobilizing private and public savings and making them available for productive purposes. The Abuja Securities Commodities and Exchange regulate operations in the commodities and commodity risk assets market. They provide the mechanism for internationalization of the Nigerian commodities and securities market.

5.0 SUMMARY

In this unit, you learnt about the regulatory roles and operational modes of the Federal Ministry of Finance, the Central Bank of Nigeria, the Securities and Exchange Commission; the Nigeria Stock Exchange; and the Abuja Securities and Commodity Exchange, among other regulators.

In the next unit, you will be introduced to the instruments employed in trading in the money market.

6.0 TUTOR MARKED ASSIGNMENTS

- Examine the basic rationales for the establishment of NAICOM and SEC in Nigeria
- What are the similarities and dissimilarities between the CBN and the NDIC?

7.0 REFERENCES/FURTHER READINGS

Kiyingi, S. and Uwaifo, E. Nigerian Capital Markets: Legal and regulatory review and recommendations – The Nigeria-UK Capital Markets Project (A collaborative report of: the Nigerian Capital Markets Solicitors Association, and Law Society of England & Wales, 2015)

Okafor, F.O. 50 Years of Banking Sector Reforms in Nigeria (1960-2010): Past Lessons and Future Imperatives (Enugu, Ezu Books Nig. Ltd, 2011),

UNIT 2 MONEY MARKET INSTRUMENTS

CONTENTS

1.0 INTRODUCTION

In the previous unit, you learnt about the regulatory roles and operational modes of the Federal Ministry of Finance, the Central Bank of Nigeria, the Securities and Exchange Commission; the Nigeria Stock Exchange; and the Abuja Securities and Commodity Exchange, among other regulators.

In this unit, you will be study the various instruments employed to trade in the money market.

2.0 OBJECTIVES

By the end of this unit, students should be able to properly understand major money market instruments including treasury bills (TB), treasury certificates (TC), certificate of deposit (CD), bankers acceptances (BA), commercial paper (CP), eligible development stocks (EDS), and banker's unit funds (BUF).

3.0 MAIN CONTENT

Money market instruments are fixed income assets of high liquidity, very low risk, and short maturity. The maturity is mostly less than 12 months. There are several instruments available through which funds can be raised and traded in the money market. The proceeding subunits shall focus on these instruments.

3.1 Treasury Bills (TB)

These are the most popular marketable government securities. They are issued at discount and have 91-day maturity. Once they are issued, Treasury Bills can be bought and sold in the secondary market through government securities dealer. The return of the bill is the difference between the face value and the purchase value of the instrument. The first issue of treasury bills was made in Nigeria in 1960. The advantages of treasury bills include short maturity, vertically default-free status, and ready marketability. Their primary disadvantages lie in the fact that yields are normally the lowest of any marketable security.

3.2 Treasury Certificate (TC)

The Federal Government Treasury certificates are public issues with short maturities ranging between 3 months and one year and consequently higher returns. They are also issued at discount once or twice every month with odd interest rates (such as 5.471% and 6.053%) and sold at par. The first TC in Nigeria was issued in 1968 to bridge the maturity gap between the short tenured bills (TB) and the long tenured Development Stocks (DS).

3.3 Commercial Paper (CP)

Commercial paper consists of short term unsecured promissory notes that are issued by large, well-known corporations and finance companies. It is a form of direct finance by large credit worthy corporations. The investors in the paper are normally high networth and credit worthy individuals and institutional investors. If a company, say Nestle or Cadbury or Total Oil need immediate funds, it can sell commercial paper to another corporation or financial institution. By definition, commercial paper is simply a promise to payback a higher specified amount at a designated time in the immediate future. CP is also issued at discount and has maturities ranging between 2 or 3 days to 270 days. The advantage of CP is that by issuing it, a company avoids/circumvents the process of applying for loan. The disadvantages include possibility of risk of default in repayment, illiquidity, and unsecured or non-collaterized nature of the instrument. The secondary market for commercial papers in Nigeria is yet to be recorded. Therefore, their marketability is weak and there is high tendency for default risk, although they attract higher return than TBs and TCs.

3.4 Eligible Development Stocks (EDS)

The eligible development stock is another government used instrument for securing medium term funds for financing medium term government finance needs. EDS are stocks issued for development purposes and are project tied. They are gilt-edged stocks with fixed interest rates and maturity dates between 7 years and 25 years (CBN, 2004). They are usually issued in tranches and the interest paid bi-annually. EDS was first issued in Nigeria by Federal Government in 1975. A secondary market exists for EDS and its marketability is higher than that of commercial papers.

3.5 Certificated of Deposit (CDs)

A Certificate of Deposit is a receipt from a bank for deposit of funds with a stated maturity and specified interest rate. They are used to transfer surplus funds from one bank to another. There are two types of certificate of deposits Negotiable and Non-

Negotiable Certificate of Deposits. CDs are short term debt instruments sold by banks and other depository institutions. It pays the depositor at maturity a specified amount of interest agreed upon during the term of the certificate plus the purchase price of the CD. For example, N2000, 10% CD will pay the depositor N2000 + (10% of N2000) at maturity.

The Non-Negotiable Certificate of Deposit (NNCD) has a feature of time deposit receipt, which cannot be negotiated before its maturity.

3.6 Bankers Acceptance (BAs)

This is a letter of credit that has been stamped "Accepted" by a drawee bank. A bankers' acceptance is a short-term instrument issued by a firm as part of commercial transaction. Payment is guaranteed by a commercial bank (drawee bank) that accepts and acknowledges its obligation to honour a draft on the due date to the beneficiary of the letter. The draft face must have been signed across due at maturity. The BAs attract lower rate of discount than CPs. The major difference between bankers' acceptance and cheque is that if the party issuing the BA has insufficient fund in the account to cover the draft at maturity (when it is payable), the bank that stamped the draft is obliged to pay the amount of the draft to the party who holds it. For this reason, it is argued that BA is more valuable as a medium of exchange than a cheque due to the bank guarantee. BAs are particularly valuable in international trade.

4.0 CONCLUSION

Money market instruments describe short term financing instruments traded in the money market. They are fixed income assets of high liquidity, very low risk, and short maturity. The Nigerian Treasury bill remains the most popular marketable government securities. They are issued at discount and have 91 day maturity. Once Treasury bills are issued, they can be bought and sold in the secondary market through government securities dealer.

Money market instruments are fixed income assets of high liquidity, very low risk, and short maturity. The maturity is mostly less than 12 months. There are several instruments available through which funds can be raised and traded in the Nigerian money market. They include treasury bills (TB), treasury certificates (TC), certificate of deposit (CD), banker's acceptances (BA), commercial paper (CP), eligible development stocks (EDS), and banker's unit funds (BUF).

5.0 SUMMARY

In this unit, you were introduced to the various instruments employed to trade in the money market.

In the next unit, you will study the different instruments used by the capital market operators to trade in that market.

6.0 TUTOR MARKED ASSIGNMENT

Explain how a banker's acceptance differs from an ordinary bank cheque.

7.0 REFERENCES/FURTHER READINGS

Baye, M. R. & Jansen, D. W. Money, Banking & Financial Markets: An Economics Approach (India, A.I.T.B.S Publishers & Distributor, 2006)

CBN, Financial Markets in Nigeria (Abuja, Central Bank of Nigeria Publication, 2004)

UNIT 3 CAPITAL MARKET INSTRUMENTS

CONTENTS

1.0 INTRODUCTION

In the last unit, you were introduced to the various instruments employed to trade in the money market.

In this unit, we shall consider the different instruments used by the capital market operators to trade in that market.

2.0 Objectives

By the end of this unit, students should be able to properly understand the 3 major types of instruments in the capital market. They include debt instrument, preferred stock and common or ordinary stock.

3.0 MAIN CONTENT

In contrast to money market instruments, which have maturities of one year or less, capital market instruments have maturities of more than one year. Besides, they are those with perpetuity and those that confer ownership on holders. The principal capital market instruments will be discussed in the proceeding subunits.

3.1 Debt Instruments

Debt instruments in the capital market are those for securing long-term loans or borrowing. That is, they are bought and sold on the market for funding huge and long term investment. Debt instruments may be classified into two: those secured by specific assets e.g. mortgage bonds; and those not secured by specific physical assets e.g. debentures.

Debt instruments are long-term issues raised by organization or government parastatals. They attract fixed rate of interest, which are paid at a start coupon rate on their nominal value. Suppose the nominal value of bond is N200, 000 and the coupon rate is 10% the bond will receive #20,000 interest. One peculiarity of Debt instruments is that their obligations are met before payment, due to long term capital market instruments. In Nigeria, the federal government debt stock (bond) remains the most popular marketable government security in its capital market.

3.2 Preferred Stock

The preferred stock occupies an intermediate position between long-term debts, e.g. bonds. Preferred stock is considered a fixed income security, like common stock, it is part of the stockholder equity. The preferred stock holders receive dividend while the debt holders receive fixed interest payment. On the part of investors, debt securities attract low risk than the preferred stocks and common stock. Although the expected returns from preferred stock has a nominal value and dividend is paid at a fixed percentage of the nominal amount.

3.3 Common Stock

Company stock holders (Ordinary Shareholders) are its true owners. The common stock holder of a company have residual claim in the company. Their claims are paid after the debt holder and preferred stock holder have been paid in full. Common stock is considered a permanent form of long term financing, since, unlike the debt and preferred stock, common security. The expected return on the common stock investment is high as well as its risk.

4.0 CONCLUSION

Capital market instruments define long term financing instruments traded in the capital market. They are financial market instruments which have maturities of more than one year. Capital market instrument could be classified into debt or equity as well as hybrid products (preferred stock). The federal government of Nigerian bond remains the most popular marketable government security in the Nigerian capital market.

5.0 SUMMARY

Capital market instruments long tenured financing products traded in the capital market. There are several instruments available through which funds can be raised and traded in the Nigerian capital market. They debt instruments like bonds, preferred stocks, and shares or common stocks respectively.

With this, we have come to the end of module two of this course.

6.0 TUTOR MARKED ASSIGNMENT

Explain how a banker’s acceptance differs from an ordinary bank cheque.

7.0 REFERENCES/FURTHER READINGS

Baye, M. R. & Jansen, D. W. Money, Banking & Financial Markets: An Economics Approach (India, A.I.T.B.S Publishers & Distributor, 2006)

CBN, Financial Markets in Nigeria (Abuja, Central Bank of Nigeria Publication, 2004)

MODULE 3 FINANCIAL INSTITUTIONS

Welcome to module three of this course. The units in this module are:

UNIT 1 BANKING INSTITUTION

CONTENTS

1.0 INTRODUCTION

This is the first unit of module three. In this unit, you will consider the rationale for the emergence of banking institutions, trace the brief origin of the banking institutions, distinguish between a bank and a banker as well as a bank and a money lender. Finally, you will learn about the roles of banking institutions in aiding economic development.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- understand the rationale for the emergence of the banking institutions;
- trace the origin of banking institutions;
- differentiate between a bank and a banker;
- determine the difference between a bank and a money lender; and
- list and discuss the role of banking institutions in aiding economic development.

3.0 MAIN CONTENT

While walking in the streets of any town or city you might have seen some signboards on buildings with names such as First Bank, GTB Bank, Union Bank, Enterprise Bank, Bank of Agriculture, etc. What do these names stand for? Did you ever try to know about them? If you enter any such building you will find some kind of a business office. You will see some employees sitting behind counters dealing with visitors standing in front of them. You will find that some are depositing money at one counter while some are receiving money at another counter. Behind the counters in the office you will see tables and chairs occupied by officers. On one side of the office you will also see a small partitioned room where the manager is sitting with papers on his table. This is the office of a 'Bank'.

3.1 Rationale for the Emergence of the Banking Institution

People earn money to meet their day-to-day expenses on food, clothing, education of children, housing, etc. They also need money to meet future expenses on marriage, higher education of children, house building and other social functions. These are heavy expenses, which can be met if some money is saved out of the present income. Saving of money is also necessary for old age and ill health when it may not be possible for people to work and earn their living. The necessity of saving money was felt by people even in olden days. They used to hoard money in their homes. With this practice, savings were available for use whenever needed, but it also involved the risk of loss by theft, robbery and other accidents. Thus, people were in need of a place where money could be kept safely and would be available when required. This need thus informed the origin of bank.

3.2 Brief Origin of the Bank

The term '**bank**' is generic. Etymologically, the meaning generates from '*bench*' or '*counter*' as borrowed from middle French '*banque*' or Old Italian '*banca*'. In those days, benches were used as desks or exchange counters during the renaissance by Florentine bankers who used to make their transactions on top of desks covered by green tablecloths. Today, the term has grown from a mere counter or a bench transaction to a big legal organization. The definition has also broadened from persons to organizations as well as groups.

3.3 Meaning of a Bank and a Banker

Accordingly, a bank in modern time could be defined as a financial institution or a financial intermediary that accepts deposits of all categories and channels those deposits into lending activities either directly through loan provision or indirectly, through the capital markets. Buttressing the foregoing definition, a bank is a place where people can deposit their savings with the assurance that they will be able to withdraw them whenever required. It is also a place where people who wish to borrow money for business and other purposes can get loans from at a reasonable rate of interest. From the above legal perspective, a bank is a lawful organization, which accepts deposits that can be withdrawn on demand or a fixed determinable time and can also lend money to individuals and business houses that need it. Going by these activities, a bank is said to bridge the gap between those who have money (surplus) units and those who do not (deficit units).

3.3.1 Who is a Banker?

The English Common Law defined a banker as a person who carries on the business of banking specified as: conducting current account for his customer; paying cheques drawn on him or her; and collecting cheques for his/her customer. But the Bill of Exchange Act contains a more elaborate definition. The Act defined a banker as "a body of persons whether incorporated or not, who carry on the business of banking". The Act went further to define the business of banking as: *"The business of receiving money on current or deposit account, paying and collecting cheques drawn by or paid in by customers, and include other business as the authority may prescribe for the purpose of this Act"*

3.4 Banks and Moneylenders

Many a times, people think that a bank is like a moneylender who provides funds to borrowers and charges interest on the loan. But it is not so. A bank is quite different from a moneylender. A bank performs two main functions. Firstly, it accepts deposits, and on that basis it lends money. The moneylenders, on the other hand, advance money out of their own private wealth and usually do not accept deposits from others. The following table shows the distinction between a bank and moneylender:

Table 1: Distinction between Banks and Moneylenders

Basis	Banks	Moneylenders
Entity	Bank are organized institutions	Moneylenders are individuals
Activity	Banking activities include acceptance of deposits as well as lending of money.	Activities of moneylender may not include acceptance of deposits.
Clients	Banks meet the needs of people in general and the business community in particular.	Moneylenders meet the needs of agriculturists and poor people.
Security	Banks accept tangible and personal security against loans	Moneylenders generally accept gold, jewelry, or land as security for given loan
Loan recovery	The process is flexible for banks	The process is rigid and strict for moneylenders
Interest rate	Interest charged by banks is governed by MPR	Rate of Interest is decided by lenders and it is normally very high

3.5 Banks' Roles in Economic Development

Banks accept deposits from the general public as well as from the business community. Anyone who saves money for future can deposit his savings in a bank. Businessmen have income from sales out of which they have to make payment for expenses. They can keep their earnings from sales safely deposited in banks to meet their expenses from time to time. Banks give two assurances to the depositors: safety of deposit, and withdrawal of deposit, whenever needed.

On deposits, banks give interest, which adds to the original amount of deposit. It is a great incentive to the depositor. It promotes saving habits among the public. On the basis of deposits, banks also grant loans and advances to farmers, traders and businessmen for productive purposes. Thereby banks contribute to the economic development of the country and wellbeing of the people in general. Banks also charge interest on loans. The rate of interest is generally higher than the rate of interest allowed on deposits. Banks also charge fees for the various other services, which they render to the business community. Interest received on loans and fees charged for services which exceed the interest allowed on deposits are the main sources of income for banks from where they meet their administrative expenses.

4.0 CONCLUSION

The activities carried on by banks are called banking activity. This involves the acceptance of deposits and lending or investment of money. It facilitates business activities by providing money and certain services that help in exchange of goods and services. Therefore, banking is an important auxiliary to trade. It not only provides money for the production of goods and services but also facilitates their exchange between the buyer and seller. You may be aware that there are laws which regulate the banking activities in our country. Depositing money in banks and borrowing from banks are legal transactions. Banks are also under the control of government. Hence they enjoy the trust and confidence of the people. Also banks depend a great deal on public confidence. Without public confidence banks cannot survive.

Banking institutions are financial institutions or financial intermediaries that accept deposits of all categories and channel those deposits into lending activities either directly through loan provision or indirectly, through the capital markets. They contribute to economic development of the country and wellbeing of the people in several ways:

- Banking encourages savings habit amongst people and thereby makes funds available for productive use.
- It acts as an intermediary between people having surplus money and those requiring money for various business activities.
- It facilitates business transactions through receipts and payments by cheques instead of currency.
- It provides credits and advances to businessmen for short term and long-term purposes.
- It also facilitates import export transactions.
- It helps in national development by providing credit to farmers, small-scale industries and self-employed people as well as to large business houses which lead to balanced economic development in the country.
- It helps in raising the standard of living of people in general by providing credits for purchase of consumer durable goods, houses, automobiles, etc.

5.0 SUMMARY

By the end of this unit, students should be able to explain the rationale for the emergence of the banking institution; distinguish between a bank and a banker; distinguish between a bank and a money Lender; and, define the basic roles of banks in economic development.

In this next unit, we shall examine the categorization of banks according to their roles, mandates, functions and operations.

6.0 TUTOR MARKED ASSIGNMENT

- Distinguish between the banking institution and the money lender.
- Carefully epitomize the roles of the banking institutions to economic development

7.0 REFERENCES/FURTHER READINGS

Baye, M. R. & Jansen, D. W. Money, Banking & Financial Markets: An Economics Approach (India, A.I.T.B.S Publishers & Distributor, 2006)

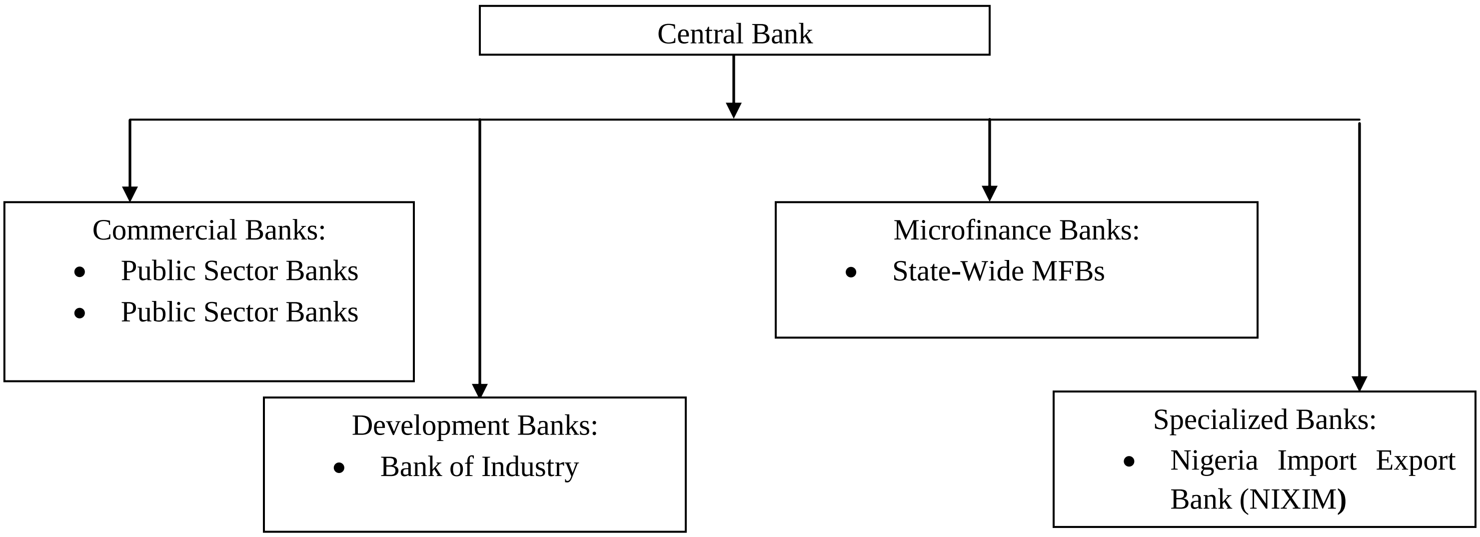
UNIT 2 BANK CATEGORIZATION

1.0 INTRODUCTION

In the previous unit, we studied the rationale behind the emergence of banking institutions.

In this unit, we shall consider the categorization of banks according to their roles, functions and operations.

Figure 3: Types of Banks



Source: *Author's Design*

2.0 OBJECTIVES

By the end of this unit, students should be able to know the types of banks operational globally and in Nigeria; explain the key roles/functions of the Central Bank (CB); Identify major advantages of each of the CB's roles; and, Know about the Central Bank of Nigeria (CBN) and its Organogram.

3.0 MAIN CONTENT

There are various types of banks which operate in any given economy to meet the financial requirements of different categories of people engaged in agriculture, business, profession, etc. On the basis of functions, the banking institutions in most economies and in Nigeria may be divided into the following types:

3.1 Central Bank - The Global Perspective

Generally, the Central Bank is the apex regulator of the monetary system of any economy. A bank is a central bank when it is entrusted to it the major functions of guiding and regulating the banking system of a country. Such a bank does not deal with the general public. It acts essentially as Government's banker; maintain deposit accounts of all other banks and advances money to other banks, when needed. The Central Bank provides guidance to other banks whenever they face any problem. It is therefore known as the banker's bank. The Central Bank of Nigeria (CBN) is the central bank of our country. The Central Bank maintains record of Government revenue and expenditure under various heads. It also advises the Government on monetary and credit policies and decides on the interest rates for bank deposits and bank loans. In addition, foreign exchange rates are also determined by the central bank. Another important function of the

Central Bank is the issuance of currency notes and regulating their circulation in the country by different methods. No other bank than the Central Bank can issue currency.

3.2 Functions of the Central Bank

A. Bank of Note Issue: - In almost all the economies of the world, the Central Bank has the sole monopoly of currency/note issue. The currency notes printed and issued by the Central Bank become an unlimited legal tender throughout the country of domicile. However, the monopoly of Central Bank to issue currency note could be partial in some countries. Example, in India, one Rupee notes are issued by the finance ministry while the rest are issued by the Reserve Bank of India.

Advantages of Central Bank's Monopoly of Note Issue

i. Ensures uniformity in the monetary system on issue and circulation of notes.
ii. Guarantees better control over money supply in the country
iii. Boost public confidence in the monetary system of the country
iv. Ease monetary management of the paper currency (Being the supreme bank, the Central Bank has full information about the monetary requirement of the economy and therefore can alter the quantity of the currency accordingly).
v. It permits the Central Bank to have effective control of Credit creation by commercial banks.
vi. Central Banks also earn profit from the issue of paper currency.
vii. Granting of monopoly right of Note Issue to the Central Bank avoids the political interference in the matter of Note Issue.

B. Banker, Agent, and Adviser to the Government: - Generally, the Central Bank of any economy is the Banker to that government. That is to say, it handles all local and international finances of the government on its behalf thereby acting as its agent on monetary matters. Being an expert in financial matters, the Central Bank is also saddled with the responsibility of advising the government on all monetary activities as detailed below:-

As a Banker to the government precisely, the Central Bank performs similar functions for the government as commercial banks do for its customers. Such include:

- It maintains the accounts of the governments at all levels.
- It receives deposits from governments but not private individuals.
- It grants short-term loans and advances to the government.
- It collects cheques and drafts deposited in the government accounts.
- It provides foreign exchange resources to the government for repaying external debts or purchasing foreign goods or other payments.

As an Agent to the Government, the Central Bank does the following:

- It collects taxes and other payments on behalf of the government.
- It raises loans for government from the public and thus manages public debts
- It also represents the government in the International Financial Institutions and Conferences.

As a Financial Adviser to the government, the Central Bank advises the government on all economic, financial and fiscal matters. Such matters include but not limited to deficit financing, devaluation, Trade policy, foreign exchange policy, etc.

C. **Bankers Bank: -** The Central Bank acts as Banker to other banks in the economy in three major capacities:

1. As the Custodian of Cash Reserve of other banks
2. As the lender of the last resort, and;
3. As Clearing Agent.

It is in this three major capacities, that the Central Bank act as a friend, philosopher, and guide to other banks in the economy especially, the commercial banks. We shall further discuss how the Central bank performs each of these roles and the accompanying advantages.

- ✓ As a Custodian of Cash Reserves of Banks, the Central Bank maintains the cash reserves of the other banks in the economy. It is of course legally mandatory for all commercial banks to keep a certain percentage of its cash balances as deposits with the Central Bank. These cash reserves can be utilized by the owner banks in time of emergencies.

Advantages of Central Bank's Custodianship of Cash Reserves of other Banks

i. Centralized cash reserves instill public confidence in the banking system.
ii. It provides the basis for a larger and more elastic credit structure.
iii. It can be effectively employed during periods of seasonal strains and financial emergencies.
iv. It also enables Central Banks provide financial accommodation to commercial banks which are in temporary difficulties.
v. Centralized cash reserves enables Central Bank have control or influence over commercial banks credit creation abilities. This is achievable through the instrumentality of variable cash reserve ratio.
vi. Above all, centralized cash reserves can be used to promote national welfare.

- ✓ As a Lender of Last Resort to banks, the Central Bank injects financial vitality to ailing banks in the economy. That is, they provide financial assistance to banks that are illiquid, distressed or at the verge of collapse. In doing this, the Central Bank guarantees safety of the bank and repose depositors more confidence in banking.

Advantages of Central Bank's Function as Lender of Last Resort to other Banks

- **i.** It increases the elasticity and liquidity of the whole credit structure of the economy.
- **ii.** It enables banks to carry out their routine financial activities even with limited cash reserves.
- **iii.** It provides financial help to banks in time of emergencies.
- **iv.** It enables Central Bank exercise its control over the banking system.

- ✓ As Clearing Agent, the Central Bank acts as a Clearing house for to other banks in all chequing transactions.

Advantages of Central Bank's Function as a Clearing Agent to other Banks

- i. It economizes the use of cash by banks while settling their claims and counter claims.
- ii. It reduces cash withdrawals and this enables commercial banks to create credit on a large scale.
- iii. The role of Cheque clearing keeps the Central Bank fully informed about the liquidity position of commercial banks.

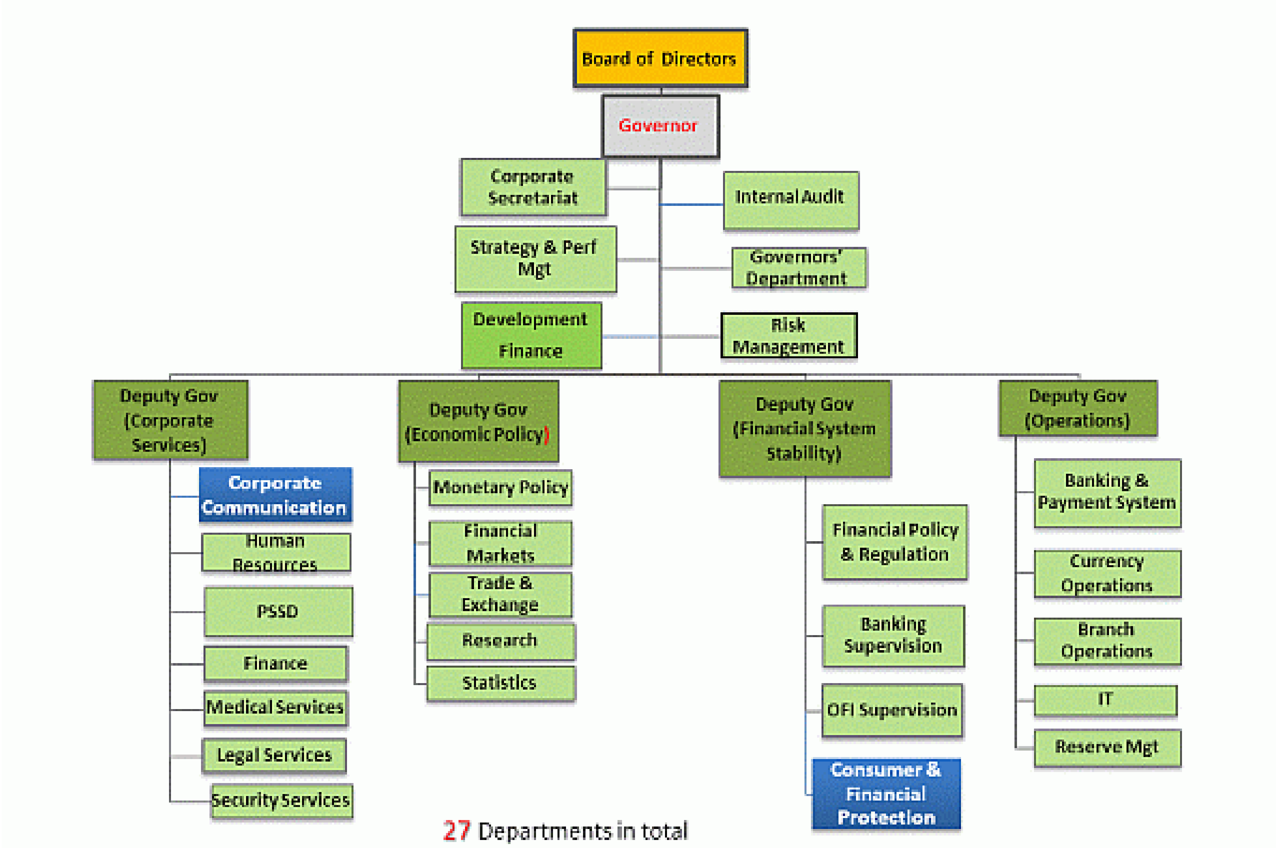
3.3 The Central Bank of Nigeria (CBN)

The Central Bank of Nigeria (CBN) is the apex regulator of the Nigerian money market. The Bank came into full existence and operation on 1st July, 1959 when the CBN Act of 1958 that established it was fully implemented. The Central Bank Act 1958 (as amended) and the Banking Decree 1969 (as amended) constitute the initial legal framework within which the CBN operated and regulated banks. However, these Act and Decree have received several amendments over the years.

At present, the legal framework within which the CBN operates is the CBN Act of 2007 which repealed the CBN Act of 1991 and all its amendments. The Act provides that the CBN shall be a fully autonomous body in the discharge of its functions of currency note issue, banker and agent to the government, as well as banker to other banks. The CBN according to the Act is charged with the objective of promoting stability and continuity in economic management. In line with this, the Act widened the objectives of the CBN to include ensuring monetary and price stability as well as rendering economic advice to the Federal Government of Nigeria.

The CBN is currently under the supervision of the Federal Ministry of Finance and directly responsible to the Minister of Finance with respect to the control and supervision of banks and other financial institutions. It is at the moment made up of 27 departments as structured in the organogram below.

Figure 4: **Organizational Structure of the CBN**
Source: CBN Website, 2014



4.0 CONCLUSION

Central Bank of any economy is the apex regulator of its monetary system. Such is entrusted with the responsibility of guiding and regulating the banking system of a country. The bank does not deal with the general public but acts essentially as government's banker and also maintain deposit accounts of all other banks.

The Central Bank of Nigeria (CBN) is the apex regulator of the Nigerian money market. The bank is fully autonomous in the discharge of its functions of currency note issue; banker and agent to the government; as well as banker to other banks. The bank is charged with the objective of promoting stability and continuity in economic management. In line with the CBN Act 2007, its objectives is widened to include ensuring monetary and price stability as well as rendering economic advice to the federal government of Nigeria.

There are various types of banks which operate in any given economy to meet the financial requirements of different categories of people engaged in agriculture, business, profession, etc. On the basis of functions, the banking institutions in most economies and in Nigeria may be divided into Central bank, commercial banks, microfinance banks, development banks, and other specialized banks.

The Central Bank is the apex regulator of the monetary system of any economy. A bank is a central bank when it is entrusted to it the major functions of guiding and regulating the banking system of a country. Its primary functions are tripartite and include currency note issue; banker, agent, and adviser to the government; and bankers bank.

Nigeria has a functional Central banking institution which came into full existence and operation on 1st July, 1959 when the CBN Act of 1958 that established it was fully implemented. The bank is charged with the objectives of promoting stability and continuity in economic management, ensuring monetary and price stability and rendering economic advice to the federal government of Nigeria. The CBN is currently under the supervision of the Federal Ministry of Finance and directly responsible to the Minister of Finance with respect to the control and supervision of banks and other financial institutions. It is at the moment made up of 27 departments.

5.0 SUMMARY

In this unit, we examine and discuss the categorization of banks according to their roles, functions and operations. We start with Central Bank and then others in that order.

We shall continue with the categorization of banks in the next unit by describing the mandate, functions and role of commercial banks in economic development.

6.0 TUTOR MARKED ASSIGNMENT

Carefully evaluate the tripartite functions of central banking institution in any economy.

7.0 REFERENCES/FURTHER READINGS

Bryan, L. Restoring Health and Profitability of our Banking System (New York, Harper Business, 1991)

Okafor, F.O. 50 Years of Banking Sector Reforms in Nigeria (1960-2010): Past Lessons and Future Imperatives (Enugu, Ezu Books Nig. Ltd, 2011)

UNIT 3 COMMERCIAL BANKING

1.0 INTRODUCTION

In the last unit, we examine and discuss the categorization of banks according to their roles, functions and operations. We start with Central Bank and then others in that order.

We continue with the categorization of banks in this unit by describing the mandate, functions and role of commercial banks in economic development.

2.0 OBJECTIVES

By the end of this unit, students will appreciate better the various forms of commercial banks; know the category of functions performed by commercial banks; and explain the key roles of commercial banks in economic development.

3.0 MAIN CONTENT

3.1 Commercial Bank

A commercial bank is a profit-seeking business firm, dealing in money and credit. It is a financial institution dealing in money in the sense that it accepts deposits of money from the public to keep them in its custody for safety.

Also, it deals in credit, i.e., it creates credit by granting short-term loans and other advances out of the funds received as deposits to needy people. It thus, functions as a mobiliser of saving in the economy.

A commercial bank is therefore like a reservoir into which, flows the savings represented by the idle surplus money of households and from which loans are given on interest to businessmen and others who need them for investment or productive uses. In addition to giving short-term loans, commercial banks also give medium-term and long-term loan to business enterprises.

Now-a-days some of the commercial banks are also providing housing loan on a long-term basis to individuals. We shall discuss the functions of commercial banks in details.

3.2 Forms of Commercial banks

Commercial banks in Nigeria and some other economies could operate in three forms based on ownership compositions:

3.2.1 Public Sector Banks:

These are banks where majority of the ownership stake is held by the Government of Nigeria. Examples of public sector banks are today are the Bridge Banks comprising of Enterprise Bank, Main Street Bank, and Keystone Bank. A Bridge bank is a temporary bank organized by the regulators (CBN & NDIC) to administer the deposits and liabilities of failed bank. Under this arrangement, the Nigerian Deposit Insurance Company (NDIC) is authorized to operate a failed bank for a period until a buyer can be found for its operation. The Bridge Bank option is a veritable tool of enhancing depositors' protection and promoting confidence by ensuring seamless continuity of banking operation.

In the Nigeria scenario, the CBN on August 5th 2011 revoked the operating licenses of three banks including Afribank, Spring Bank and Bank PHB which according to it did not show enough capacity and ability for recapitalization. In their place, the CBN through the NDIC establish Bridge Banks and transferred the assets and liabilities of the three banks to the Bridge Banks as follows: Main Street Bank Ltd (Afribank); Keystone Bank Ltd (Bank PHB); and Enterprise Bank Ltd (Spring Bank) respectively.

3.2.2 Private Sectors Banks:

In case of private sector banks majority of share capital of the bank is held by private individuals. These banks are registered as companies with limited liability. Examples of these banks in Nigeria include First Bank Plc, Union Bank Plc; GT Bank; UBA Bank Plc etc.

3.2.3 Foreign Banks:

These banks are registered and have their headquarters in a foreign country but operate their branches in our country. Some of the foreign banks operating in our country are Ecobank plc; Sterling Bank, etc. The number of foreign banks operating in our country has increased since the financial sector reforms of 2004.

3.3 Functions of Commercial Banks

Commercial banks perform a variety of functions which are common to both developed and developing countries. These are known as 'General Banking' functions of the commercial banks. The modern banks perform a variety of functions. These can be broadly divided into three categories: (a) Primary functions (b) Secondary functions, and (c) Ancillary Functions.

3.3.1 Primary Functions of Commercial Banks

The primary functions of the commercial banks include:

- Acceptance of deposits
- Advancing loans
- Creation of credit
- Clearing of cheques
- Financing foreign trade
- Remittance of funds

(a) **Acceptance of Deposits:** Accepting deposits is the primary function of a commercial bank. Banks generally accept three types of deposits viz., (a) Current Deposits (b) Savings Deposits, and (c) Fixed Deposits.

(1) *Current Deposits:* These deposits are also known as demand deposits. Demand deposits can be withdrawn at any time. Generally, no interest is allowed on current deposits, and in cases, the customer is required to leave a minimum balance undrawn with the bank. Cheques are used to withdraw the amount. These deposits are kept by businessmen and industrialists who receive and make large payments through banks. The bank levies certain incidental charges on the customer for the services rendered by it.

(2) *Savings Deposits:* This is meant mainly for professional men and middle class people to help them deposit their small savings. It can be opened without any introduction. Money can be deposited at any time but the maximum cannot go beyond a certain limit. There is a restriction on the amount that can be withdrawn at a particular time or during a week. If the customer wishes to withdraw more than the specified amount at any one time, he has to give prior notice. Interest is allowed on the credit balance of this account. The rate of interest is greater than the rate of interest on the current deposits and less than that on fixed deposit. This system greatly encourages the habit of thrift or savings.

(3) *Fixed Deposits:* These deposits are also known as time deposits. These deposits cannot be withdrawn before the expiration of the period for which they are deposited or without giving a prior notice for withdrawal. If the depositor is in need of money, he has to borrow on the security of this account and pay a slightly higher rate of interest to the bank. They are attracted by the payment of interest which is usually higher for longer period. Fixed deposits are liked by depositors both for their safety and for their interest..

(b) **Advancing Loans:** The second primary function of a commercial bank is to make loans and advances to all types of persons, particularly to businessmen and entrepreneurs. Loans are made against personal security, gold and silver, stocks of goods and other assets. The most common way of lending is by the following:

(1) *Overdraft Facilities:* In this case, the depositor in a current account is allowed to draw over and above his account up to a previously agreed limit. Suppose a businessman has only ₦ 30,000 in his current account in a bank but requires ₦ 60,000 to meet his expenses. He may approach his bank and borrow the additional amount of ₦ 30,000. The bank allows the customer to overdraw his account through cheques. The bank, however, charges interest only on the amount overdrawn from the account. This type of loan is very popular with Nigerian businessmen.

(2) *Cash Credit:* Under this account, the bank gives loans to the borrowers against certain security. But the entire loan is not given at one particular time, instead the amount is credited into his account in the bank; but under emergency, cash will be given. The borrower is required to pay interest only on the amount of credit availed to him. He will be allowed to withdraw small sums of money according to his requirements through cheques, but he cannot exceed the credit limit allowed to him. Besides, the bank can also give specified loan to a person, for a firm against some collateral security. The bank can recall such loans at its option.

(3) *Discounting Bills of Exchange:* This is another type of lending which is very popular with the modern banks. The holder of a bill can get it discounted by the bank, when he is in need of money. After deducting its commission, the bank pays the present price of the bill to the holder. Such bills form good investment for a bank. They provide a very liquid asset which can be quickly turned into cash. The commercial banks can rediscount the discounted bills with the central bank when they are in need of money. These bills are safe and secured bills. When the bill matures the bank can secure its payment from the party which had accepted the bill.

(4) *Money at Call:* Bank also grant loans for a very short period, generally not exceeding 7 days to the borrowers, usually dealers or brokers in stock exchange markets against collateral securities like stock or equity shares, debentures, etc., offered by them. Such advances are repayable immediately at short notice hence; they are described as money at call or call money.

(5) *Term Loans:* Banks give term loans to traders, industrialists and now to agriculturists also against some collateral securities. Term loans are so-called because their maturity period varies between 1 to 10 years. Term loans; as such provide intermediate or working capital funds to the borrowers. Sometimes, two or more banks may jointly provide large term

loans to the borrower against a common security. Such loans are called participation loans or consortium finance.

(6) *Consumer Credit:* Banks also grant credit to households in a limited amount to buy some durable consumer goods such as television sets, refrigerators, etc., or to meet some personal needs like payment of hospital bills etc. Such consumer credit is made in a lump sum and is repayable in installments in a short time. In some economies such as India, under the 20-point programme, the scope of consumer credit has been extended to cover expenses on marriage, funeral etc., as well.

(7) *Miscellaneous Advances:* Among other forms of bank advances there are packing credits given to exporters for a short duration, export bills purchased/discounted, import finance-advances against import bills, finance to the self-employed, credit to the public sector, credit to the cooperative sector and above all, credit to the weaker sections of the community at concessional rates.

(c) **Creation of Credit Function:** A unique function of the bank is to create credit. Banks supply money to traders and manufacturers. They also create or manufacture money. Bank deposits are regarded as money. They are as good as cash. The reason is they can be used for the purchase of goods and services and also in payment of debts. When a bank grants a loan to its customer, it does not pay cash. It simply credits the account of the borrower. He can withdraw the amount whenever he wants by a cheque. In this case, bank has created a deposit without receiving cash. That is, banks are said to have created credit. Sayers says "banks are not merely purveyors of money, but also in an important sense, manufacturers of money."

(d) **Promote the Use of Cheques:** The commercial banks render an important service by providing to their customers a cheap medium of exchange like cheques. It is found much more convenient to settle debts through cheques rather than through the use of cash. The cheque is the most developed type of credit instrument in the money market.

(e) **Financing Internal and Foreign Trade:** The bank finances internal and foreign trade through discounting of exchange bills. Sometimes, the bank gives short-term loans to traders on the security of commercial papers. This discounting business greatly facilitates the movement of internal and external trade.

(f) **Remittance of Funds:** Commercial banks, on account of their network of branches throughout the country, also provide facilities to remit funds from one place to another for their customers by issuing bank drafts, mail transfers or telegraphic transfers on nominal commission charges. As compared to the postal money orders or other instruments, bank drafts have proved to be a much cheaper mode of transferring money and have helped the business community considerably.

3.3.2 Secondary Functions of Commercial Banks

Commercial banks also play secondary banking roles which are often anchored on two specific areas namely: Agency Services and General Utility Services respectively.

1. **Agency Services:** Banks also perform certain agency functions for and on behalf of their customers. The agency services are of immense value to the people at large. The various agency services rendered by banks are as follows:

   (a) *Collection and Payment of Credit Instruments:* Banks collect and pay various credit instruments like cheques, bills of exchange, promissory notes etc., on behalf of their customers.

   (b) *Purchase and Sale of Securities:* Banks purchase and sell various securities like shares, stocks, bonds, debentures on behalf of their customers.

   (c) *Collection of Dividends on Shares:* Banks collect dividends and interest on shares and debentures of their customers and credit them to their accounts.

   (d) *Acts as Correspondent:* Sometimes banks act as representative and correspondents of their customers.
   They get passports, traveler's tickets and even secure air and sea passages for their customers.

   (e) *Income-tax Consultancy:* Banks may also employ income tax experts to prepare income tax returns for their customers and to help them to get refund of income tax.

   (f) *Execution of Standing Orders:* Banks execute the standing instructions of their customers for making various periodic payments. They pay subscriptions, rents, insurance premium etc., on behalf of their customers.

   (g) *Acts as Trustee and Executor:* Banks preserve the 'Wills' of their customers and execute them after their death.

2. **General Utility Services:** In addition to agency services, the modern banks provide many general utility services for the community such as:

   (a) *Locker Facility:* Bank provides locker facility to their customers. The customers can keep their valuables, such as gold and silver ornaments, important documents; shares and debentures in these lockers for safe custody.

(b) *Traveler's Cheques and Credit Cards:* Banks issue traveler's cheques to help their customers to travel without the fear of theft or loss of money. With this facility, the customers need not take the risk of carrying cash with them during their travels.

(c) *Letter of Credit:* Letters of credit are issued by the banks to their customers certifying their credit worthiness. Letters of credit are very useful in foreign trade.

(d) *Collection of Statistics:* Banks collect statistics giving important information relating to trade, commerce, industries, money and banking. They also publish valuable journals and bulletins containing articles on economic and financial matters.

(e) *Acting Referee:* Banks may act as referees with respect to the financial standing, business reputation and respectability of customers.

(f) *Underwriting Securities:* Banks underwrite the shares and debentures issued by the Government, public or private companies.

(g) *Gift Cheques:* Some banks issue cheques of various denominations to be used on auspicious occasions.

(h) *Accepting Bills of Exchange on Behalf of Customers:* Sometimes, banks accept bills of exchange, internal as well as foreign, on behalf of their customers. It enables customers to import goods.

(i) *Merchant Banking:* Some commercial banks have opened merchant banking divisions to provide merchant banking services.

3.3.3 Ancillary Functions of Commercial Banks

In recent years, commercial banks, particularly in developing countries, have been called upon to help achieve certain socio-economic goals laid down by the state such as rural development, employment generation, wealth creation, poverty eradication, etc. In response to this call, most commercial banks in Nigeria have framed special innovative schemes of credit to help small and medium scale businesses, agriculturists, village and cottage industries, retailers, artisans, the self-employed persons, etc through loans and advances at concessional rates of interest. In Nigeria precisely, commercial banks under the Small and Medium Scale Equity Investment Scheme (SMEIS) are mandated to advance 10% of their profit after tax (PAT) to small and medium scale enterprises per annum. In this scenario, banking is, thus, being used to sub serve the national policy objectives of reducing inequalities of income and wealth, removal of poverty and elimination of unemployment in the country.

It is clear from the above that banks help development of trade and industry in the country. They encourage habits of thrift and saving. They help capital formation in the country. They lend money to traders and manufacturers. In the modern world, banks are to be considered not merely as dealers in money but also the leaders in economic development.

3.4 Commercial Banks and Economic Development

Commercial banks are considered not merely as dealers in money but also the leaders in economic development. They are not only the store houses of the country's wealth but also the reservoirs of resources necessary for economic development. They play an important role in the economic development of a country.

A well-developed banking system is essential for the economic development of a country. The "Industrial Revolution" in Europe in the 19th century would not have been possible without a sound system of commercial banking. In case of developing countries like Nigeria, the commercial banks are considered to be the backbone of the economy. Commercial banks can contribute to a country's economic development in the following ways:

3.4.1 Acceleration of the Rate of Capital Formation:

Capital formation is the most important determinant of economic development. The basic problem of a developing economy is slow rate of capital formation. Banks promote capital formation. They encourage the habit of saving among people. They mobilize idle resources for production purposes. Economic development depends upon the diversion of economic resources from consumption to capital formation. Banks help in this direction by encouraging saving and mobilizing them for productive uses.

3.4.2 Provision of Finance and Credit:

Commercial banks are a very important source of finance and credit for industry and trade. Credit is a pillar of development. Credit lubricates all commerce and trade. Banks become the nerve centre of all commerce and trade. Banks are instruments for developing internal as well as external trade.

3.4.3 Monetization of Economy:

An underdeveloped economy is characterized by the existence of a large non-monetized sector. The existence of this non-monetized sector is a hindrance in the economic development of the country. The banks, by opening branches in rural and backward areas can promote the process of monetization (conversion of debt into money) in the economy.

3.4.4 Innovations:

Innovations are an essential prerequisite for economic development. These innovations are mostly financed by bank credit in the developed countries. But in underdeveloped countries, entrepreneurs hesitate to invest in new ventures and undertake innovations largely due to lack of funds. Facilities of bank loans enable the entrepreneurs to step up their investment on innovational activities, adopt new methods of production and increase productive capacity of the economy.

3.4.5 Implementation of Monetary Policy:

Economic development needs an appropriate monetary policy. But a well-developed banking is a necessary pre-condition for the effective implementation of the monetary policy. Control and regulation of credit by the monetary authority is not possible without the active co-operation of the banking system in the country.

3.4.6 Encouragement to Right Type of Industries:

Banks generally provide financial resources to the right type of industries to secure the necessary material, machines and other inputs. In this way they influence the nature and volume of industrial production.

3.4.7 Development of Agriculture:

Underdeveloped economies are primarily agricultural economies. Majority of the population in these economies live in rural areas. Therefore, economic development in these economies requires the development of agriculture and small scale industries in rural areas.

So far banks in underdeveloped countries have been paying more attention to trade and commerce and have almost neglected agriculture and industry. Banks must provide loans to agriculture for development and modernization of agriculture. In recent years, the State Bank of India and other commercial banks are granting short term, medium-term and long-term loans to agriculture and small-scale industries.

3.4.8 Regional Development:

Banks can also play an important role in achieving balanced development in different regions of the country. They transfer surplus capital from the developed regions to the less developed regions, where it is scarce and most needed. This reallocation of funds between regions will promote economic development in underdeveloped areas of the country.

3.4.9 Promote Industrial Development:

Industrial development needs finance. In some countries, commercial banks encouraged industrial development by granting long-term loans also. Loan or credit is a pillar to development. In underdeveloped countries like India, commercial banks are granting short-term and medium-term loans to industries. They are also underwriting the issue of shares and debentures by industrial concerns.

This helps industrial concerns to secure adequate capital for their establishment, expansion and modernization. Commercial banks are also helping manufacturers to secure machinery and equipment from foreign countries under installment system by guaranteeing deferred payments. Thus, banks promote or encourage industrial development.

3.4.10 Promote Commercial Virtues:

The businessmen are more afraid of a banker than a preacher. The businessmen should have certain business qualities like industry, forethought, honesty and punctuality. These qualities are called "commercial virtues" which are essential for rapid economic progress. The banker is in a better position to promote commercial virtues. Banks are called "public conservators of commercial virtues."

3.4.11 Fulfillment of Socio-economic Objectives:

In recent years, commercial banks, particularly in developing countries, have been called upon to help achieve certain socio-economic objectives laid down by the state. For example, nationalized bank in India have framed special innovative schemes of credit to help small agriculturists, self-employed persons and retailers through loans and advances at concessional rates of interest. Banking is thus used to achieve the national policy objectives of reducing inequalities of income and wealth, removal of poverty and elimination of unemployment in the country.

Thus, banks in a developing country have to play a dynamic role. Economic development places heavy demand on the resources and ingenuity of the banking system. It has to respond to the multifarious economic needs of a developing country.

Traditional views and methods may have to be discarded. "An Institution, such as the banking system, which touches and should touch the lives of millions, has necessarily to be inspired by a larger social purpose and has to sub serve national priorities and objectives." A well-developed banking system provides a firm and durable foundation for the economic development of the country.

From the above discussion, undoubtedly, we can say that, commercial banks form the most important part of financial intermediaries. It accepts deposits from the general public and extends loans to the households, firms and the government. Banks form a significant part of the infrastructure essential for breaking vicious circle of poverty and promoting economic growth.

4.0 CONCLUSION

Commercial bank is like a reservoir into which, flows in idle surplus resources of households and from which loans are given on interest to businessmen and others who need them for investment or productive uses. They form the most important part of financial intermediaries and a significant part of the infrastructure essential for breaking vicious circle of poverty and promoting economic growth. A well-developed banking system provides a firm and durable foundation for the economic development of the country.

A commercial bank is a profit-seeking business firm, dealing in money and credit. It is a financial institution dealing in money in the sense that it accepts deposits of money from the public to keep them in its custody for safety. Also, it deals in credit, i.e., it creates credit by granting short-term loans and other advances out of the funds received as deposits to needy people. Commercial banks in Nigeria and some other economies could operate in three forms based on ownership compositions as public sector owned commercial banks; private sector owned commercial banks; and foreign ownership based commercial banks. However, mixed ownership could also exist.

The modern commercial banks perform a variety of functions broadly divided into three categories viz; Primary functions, Secondary functions, and Ancillary Functions. The primary functions include deposit acceptance, advancing of loans, creation of credit, clearing of cheques, financing foreign trade, and, remittance of funds. The secondary commercial banking roles anchors on two specific areas namely; agency services and general utility services respectively. Ancillary functions reside on their roles towards rural development, employment generation, wealth creation and poverty eradication.

5.0 SUMMARY

In this unit, we continued with the categorization of banks by delving into the roles of commercial banks in economic development.

In the next unit, we shall yet consider the role of development or specialised banks.

6.0 TUTOR MARKED ASSIGNMENTS

- Succinctly appraise the Primary, Secondary, and Ancillary Functions of commercial banks in any economy.
- Commercial banks are considered not merely as dealers in money but also the leaders in economic development. Discuss.

7.0 REFERENCES/FURTHER READINGS

Baye, M. R. & Jansen, D. W. Money, Banking & Financial Markets: An Economics Approach (India, A.I.T.B.S Publishers & Distributor, 2006)

Eleje, E. O. & Olopade, D. O., Corporate Governance and Equity Ownership Clause for Banks in Nigeria: An Empirical Performance Assessment (Nigerian Journal of Management Sciences Vol. 4 No. 2, 2015)

UNIT 4 DEVELOPMENT/SPECIALIZED BANKING INSTITUTIONS

CONTENTS

1.0 INTRODUCTION

In the previous unit, we examined and discussed the categorization of banks according to their roles, functions and operations. We continued with this categorization by stating the functions, roles, and operations of the Commercial Banks.

In this unit, our focus will be on development/specialised banking institutions.

2.0 OBJECTIVES

By the end of this unit, students will be able to explain the meaning and purpose of development as well as specialized banks; discuss what necessitated the emergence of the Bank of Industry and Bank of Agriculture; evaluate the structure and pattern of operation of the Bank of Industry; and appraise the difference between microfinance banks and other development/specialized banks.

3.0 MAIN CONTENT

National economic progress often requires medium and long-term capital for purchase of machinery and equipment, for using latest technology, or for expansion and modernization. Financial assistance is provided by development banks such as the Bank of Industry,

Bank of Agriculture and microfinance banks to help achieve these vital national goals. They are also some specialized development banks such as Import-Export banks, Mortgage banks and urban development banks who undertake other specialized developmental functions like boosting of international trade, housing issues and urban development.

3.1 The Bank of Industry Limited

The Bank of Industry (BOI) limited emerged in 2001 from the reconstruction of the erstwhile Nigeria Industrial Development Bank (NIDB) and the Nigeria Bank for Commerce and Industry (NBCI). NIDB was established in 1964 under the guidance of the World Bank. The bank's 75% of initial equity was held by IFC, while the federal government held 25% (Oputu, 2008). NIDB was established to help in boosting industrialization in Nigeria at the eve of Independence. The Nigerian Bank for Commerce and Industry (NBCI) was established for the provision of financial services, such as equity investment and granting of loans and guarantees to indigenous enterprises in commercial and manufacturing activities. NBCI was owned 60% by the federal government and 40% by the Central Bank of Nigeria (BOI, 2012). NBCI did not take deposit from the general public in any form. Funding was traditionally relied on government subventions, concessional loans from multilateral financial institutions and inter-bank borrowing. The Bank's clientele base increased by 212% within ten years from 259 clients in 1984 to 809 clients in 1994.

NBCI served corporate organizations and small-scale manufacturers and not individuals. The 212% growth in NBCI clientele also represented the growth in the number of loans granted during 1985 to 1994. Also, the number of outstanding loans increased from 208% to 798 during the same period. However, since 1995, there became a sharp drop in the population served by NBCI. This was perhaps a result of competition from the new generation commercial banks, dwindling funding resources and recession that hit the nation's small-scale manufacturers which constituted NBCI's clientele base in the 1990s. Furthermore, the establishment of the National Economic Reconstruction Fund (NERFUND) for providing finance to medium and small scale manufacturing enterprises appeared to have duplicated the functions of NBCI in recent years and made NBCI had less impact among existing small manufacturers or new entrants into the manufacturing sector. Following the dismal performance of NBCI in late 1990s, NBCI was merged with NIDB to form the new "Bank of Industry" (BOI) in 2000 with a recapitalization of N50 billion. The Bank of Industry officially began operation in 2001(Iganiga, 2008).

3.1.1 BOI's Structure, Pattern of Operation and Major Clientele

Currently, the ownership of the BOI is composed of three major groups namely: Ministry of Finance Incorporated (MOFI), 58.86%; Central Bank of Nigeria (CBN), 41.12%; & Equity held by 43 private shareholders 00.02% respectively (Oputu, 2008). According to Okoye (Undated), the pattern of the funding of the microfinance sector by BOI has been in the form of loans, debentures and equity. With interest rates ranging from 10 to 20 percent per annum payable monthly, BOI loans tenors range from three to seven years with 6 months moratorium (BOI, Undated). However, its loan disbursement at the early days of its operation showed an undeniable discrimination against small businesses. For instance, out of a total of N1.72 billion given out as loans from 2001–31 March, 2004, only about N0.46 billion went to smaller enterprises while an astonishing N1.26 billion went to big enterprises. This goes to show a great level of unwillingness on the part of microfinance administrators to finance small businesses, which for the most part touches on the poverty level in the country.

Meanwhile, the vision of BOI is to be the leading self-sustaining Development Finance Institution, operating under sound management and banking principles that would promote the emergence and development of a virile competitive industrial sector in Nigeria. Consistently, the mission of the bank is to transform Nigeria's industrial sector and integrate it into the global economy by providing financial and business support services to existing and new industries to attain modern capabilities to produce goods that are competitive in both domestic and external markets. BOI core mandate is to provide financial assistance for the establishment of large, medium and small projects; as well as expansion, diversification and modernization of existing enterprises; and rehabilitation of ailing industries (BOI, 2012). Towards achieving these objectives, the bank has committed itself to some reasonable efforts so far. The current management has made a point of devoting 85% of the Bank's resources to SMEs. In fact, it can be argued that 100% of the Bank's resources are devoted to SMEs because the balance of 15% which is reserved for large enterprises finds its way to small enterprise as well because the Bank insists that large enterprises that get it must have linkages with small or medium enterprises (Oputu, 2008). BOI is under the supervision of Central Bank of Nigeria and the Federal Ministry of Commerce and Industry.

The BOI has certain core activities of which it seeks to pursue. The activities include project identification and selection, resource mobilization, equity financing, industrial policy formulation, business development support, encouragement of effective resource utilization via formation of coherent Public-Private-Partnership (PPP), advocacy towards improving the effectiveness and efficiency of the local entrepreneurs through: Reduction of initial set-up costs, taxation, timing and cost of obtaining consent to mortgage as well as obtaining C of O and, improving their enabling business environment (BOI, 2012; Udo, 2013).

In line with the mission of the bank anchored on the transformation of Nigeria's industrial sector and integrating it into the global economy via provision of financial and business support services, BOI is by law permitted to assist the following: (1) Small, medium and large enterprises, excluding cottage industries, (2) New or existing companies, seeking expansion, modernization or diversification, (3) Credit worthy promoters who will be required to prove their commitment to the project by contributing at least 25% of the project cost excluding land, (4) Borrowers whose management capability, financial situation, character and reputation are incontrovertible, (5) Clients with demonstrable ability to meet loan repayments, and (6) Borrowers with no record of unpaid loans to erstwhile development finance institutions and other banks.

3.2 Bank of Agriculture

The Bank of Agriculture (BOA) was formed in the late 2000 from the amalgamation of Nigeria Agricultural Cooperative Bank (NACB), Peoples Bank of Nigeria (PBN) and Family Economic Advancement Programme (FEAP) respectively. Previously known as the Nigeria Agricultural Cooperative & Rural Development Bank (NACRDB) after its merger, BOA is jointly owned by the government and the Central Bank of Nigeria. The bank was set up primarily to finance agriculture. It plays the bulk role of providing agricultural finance in the rural landscape. However, its deposit mobilization and credit services are also extended to urban clients.

The BOA is structured to accept deposits and offer loans/advances with interest rates stratified according to the purpose for the loan. It is required to lend 70% of its loan portfolio at single digit interest rates through loans of ₦250, 000 ($1,666) or less (David, 2011). The bank also offers a number of micro finance services, including target savings, start-up as well as small holder schemes. The authorized share capital was initially ₦1 billion, with an additional ₦9.1 billion in deposit for share account.

The sources of NACRBD funding are mainly equity as well as interest on loans and investments. However, the very low repayment rates and the interest rate cap have both been found to undermine the viability of the institution as well as restricting its ability to satisfy the demand for loans from its target clientele.

3.3 Community Banks cum Microfinance Banks (MFBs)

Community banking was initiated into the Nigerian banking landscape precisely in 1990 although the enabling Act, that is, the Community Banks Act 46 was formally enacted in 1992 with retrospective effect to 1990. Apart from spelling out modalities for the licensing and operations of Community Banks, the CB Act established major objectives paramount amongst which is the promotion of rural development by providing financial and banking services to agrarian rural communities inadequately supplied with such facilities by commercial banks and government owned banks. Government's imposition of ceiling on interest rates led to an inability of many CBs to recover their costs and eventually many became distressed.

The inauguration of the National Microfinance Policy and consequent introduction of microfinance banks (MFBs) in 2004 by the Central Bank of Nigeria (CBN) was a measure to address the poor performance of community banking in Nigeria. With the new initiative, all community banks operating in Nigeria were given twenty four (24) months to convert to microfinance banks. Two categories of MFBs were introduced namely, **State-Wide MFBs** with minimum capitalization of ₦1bn and **Local Government Area MFBs** with minimum capitalization of ₦20m respectively (Okafor, 2011). While the former category of MFBs is permitted to open branches anywhere within the chosen state of operation, the operation of the later is confined to the domiciled local government area. The two categories were instituted with the core objective of making financial services accessible to a larger segment of the potentially productive Nigerians predominant in the rural areas that otherwise have no access to such services thereby permitting them to contribute to rural transformation, promote synergy, and graduate the informal subsector into the formal financial system. Meanwhile, some modest success has been recorded especially through the MFIs that are supported by NGOs. They have been important financial provision for the rural poor in states such as Benue, Nasarawa and Bauchi, although their overall impact remains small.

3.4 Other Specialized Banking Institutions

There are some banks which cater for the requirements and provision of overall support for setting up businesses in specific areas of activity. They engage in some specific area or activity and thus called specialized banks. These banks include Federal Mortgage Bank of Nigeria (FMBN), Urban Development Bank (UDB) and Nigeria Import and Export Bank (NIXIM).

3.4.1 Federal Mortgage Bank of Nigeria (FMBN)

The FMBN provides loans to individuals, corporate bodies, sub-national governments and the Federal Housing Authority to execute housing projects. The FMBN mobilizes savings from individuals and corporate organizations.

The activities of the FMBN were boosted by that housing policy of the Federal Government under the mandatory savings of 2.5% of salary of all public workers in the country. Thus, based on the individual savings, a proportion of the savings is extended to these organizations/individuals to acquire housing assets. The loans often attract long repayment terms between 5 to 30 years and are at lower interest rates. Repayment of both capital and interest is periodical.

3.4.2 Primary Mortgage Institutions (PMIs)

Primary mortgage institutions were established to assist in housing development by mobilizing savings and deposits, granting loans and advances for the purpose of constructing residential places, promoting of housing fund through payment of interest rates which are in accordance with the guidelines of the operators and also granting loans and advances for the repairs of existing houses. The dearth of supply of housing finance and the deregulation of the financial services sector necessitated their emergence. PMIs were licensed to commence operation in 1989 under the framework of Decree No.53. The Federal Mortgage Bank of Nigeria (FMBN) was entrusted with the responsibility of regulating and supervising the activities of PMIs. As a measure to address the continued distress in the sector, the FMBN revoked the licenses of 97 institutions in 1997, thus reducing the number of PMIs in the country to 115. Another measure taken by FMBN to strengthen and restructure their operations was the upward adjustment of the minimum paid up capital from N5.0 million to N20 million beginning from June 1994 for new primary mortgage institutions, while the existing ones were given up to two-year grace period to recapitalize and improve their operations.

3.4.3 Urban Development Bank (UDB)

Urban Development Bank came into existence under Decree 51 of 1992 by the federal government. The rationale was to provide capital for combating the problems of urban housing, transportation, electricity, water supply and other urban infrastructure. With an authorized share capital ofN800 million, the paid up share of all the three tiers of government and Nigerian Labour Congress stood at N543.6 million. The bank was designed as a profit making institution to provide funds to both the public and the private sector of the economy for the development of urban infrastructure and mass transportation. However, UDB may with the approval of the Minister of Finance raise funds in foreign currency. Less than a decade after, the banks total assets declined from ₦445.l million in 1998 to N325.7 million in 1991. In the same year, it reported a modest operating surplus of N48.4 million as against a loss of N223.0 million the previous year.

3.4.4 Nigerian Export and Import Bank (NEXIM)

NEXIM is traced to the First National Development Plan. It was during this period that the federal government of Nigeria conceived of the idea to establishment an export credit agency that would provide export credit insurance for the country's largest agricultural exports. Consequently, in 1988, two years after the Structural Adjustment Program (SAP) was launched, the government finally set-up and export credit agency in the country initially as the Nigerian Export and Import Bank. In January 1991, NEXIM commenced full operation as an Export Credit Agency. The specified roles of the bank are; the provision of information on trade; offering advisory services in large areas like exchange rate, prices, markets, tariffs and non-tariffs issues; quality of products; trade practices and contract forms; finance and credit and all the issues involving freighting over land and sea; warehousing and storage; the provision of relatively large variety of risk bearing facilities to allow exporters or their banks cope with the risks in the export scene; export credit insurance and related facilities for handling credit risks; and the provision of local and foreign currency finance to exporters either directly or indirectly through deposit money banks to sustain exports.

In fact, if you want to set up a business for exporting products abroad or importing products from foreign countries for sale in Nigeria, NIXIM bank can provide you the required support and assistance. The bank grants loans to exporters and importers and also provides information about the international market. It gives guidance about the opportunities for export or import, the risks involved in it and the competition to be faced.

4.0 CONCLUSION

Real economic growth and development of any economy could be directly correlated with availability of medium and long-term capital for the purchase of machinery and equipment, for using latest technology, or for expansion and modernization. These funds are most times limited thus affecting development. Consequently, different governments have utilized the machinery of development specialized banking institutions to bridge the development financing gap. To a significant extent, Nigeria have fared well in this direction going by the establishment of the BOI, BOA, UDB, NEXIM among other specialized banking institution.

Specialized banking institutions provide medium and long term capital for stimulation of economic activities in the economy. Some notable industrial based specialized banks and other financial institutions which have operated in Nigeria include the Nigerian Industrial Development Bank Limited (NIDB) established in 1964; Nigerian Agricultural and Cooperative Bank Limited (NACB) established in 1973; Nigerian Bank for Commerce and Industry (NBCI) in 1973; National Economic Reconstruction Fund (NERFUND) in 1989; Peoples Bank of Nigeria (PBN) in 1989; Family Economic Advancement Programme (FEAP) in 1997; and the National Poverty Eradication Programme (NAPEP) in 2003 respectively.

In late 2000, NACB, PBN and FEAP were merged to form the Nigerian Agricultural Cooperative and Rural Development Bank Limited (NACRDB) whose name was changed again to what is today known as the Bank of Agriculture. Similarly, NBCI was merged with NIDB to form the Bank of Industry which commenced operation in 2001 with a recapitalization of ₦50 billion.

Community banking was initiated into the Nigerian banking landscape precisely in 1990 to promote rural development by providing financial and banking services to agrarian rural communities inadequately supplied with such facilities by commercial banks and government owned banks. The inauguration of the National Microfinance Policy and consequent introduction of microfinance banks (MFBs) in 2004 by the CBN was a measure to address the poor performance of community banking in Nigeria.

Some other specialized banks were set up by the federal government to cater for the requirements and provision of overall support to foreign trade, urban development and housing. These banks include Federal Mortgage Bank of Nigeria (FMBN), Urban Development Bank (UDB) and Nigeria Import and Export Bank (NIXIM).

5.0 SUMMARY

By the end of this unit, students will be able to explain the meaning and purpose of development as well as specialized banks; discuss what necessitated the emergence of the Bank of Industry and Bank of Agriculture; evaluate the structure and pattern of operation of the Bank of Industry; and appraise the difference between microfinance banks and other development/specialized banks.

In the next unit, we shall consider another important topic: Bank Income and Investment Policy.

6.0 TUTOR MARKED ASSIGNMENT

- Carefully discuss the factors that necessitated the emergence of the Bank of Industry and Bank of Agriculture.
- Appraise the difference between microfinance banks and other development and specialized banks.

7.0 REFERENCES/FURTHER READINGS

Okafor, F.O. 50 Years of Banking Sector Reforms in Nigeria (1960-2010): Past Lessons and Future Imperatives (Enugu, Ezu Books Nig. Ltd, 2011)

UNIT 5 BANK INCOME AND INVESTMENT POLICY

CONTENTS

1.0 INTRODUCTION

In the previous unit, we discussed the categorization of banks based on the role of development/specialised banking institutions to economic development.

In this unit, we shall look into bank income and investment policy.

2.0 OBJECTIVES

After studying this unit, students will understand the nature and sources of bank income; explain the key factors that influence bank investment policy; and be able to appreciate the liquidity versus profitability controversy.

3.0 MAIN CONTENT

A bank is a business organization engaged in the business of borrowing and lending money. A bank can earn income only if it borrows at a lower rate and lends at a higher rate. The difference between the two rates will represent the costs incurred by the bank and the profit. Bank also provides a number of services to its customers for which it charges commission. This is also an important source of income.

3.1 Sources of Bank Income

The followings are the various sources of a bank's income:

(1) **Interest on Loans:** The main function of a commercial bank is to borrow money for the purpose of lending at a higher rate of interest. Bank grants various types of loans to the industrialists and traders. The yields from loans constitute the major portion of the income of a bank. The banks grant loans generally for short periods. But now the banks also advance call loans which can be called at a very short notice. Such loans are granted to share brokers and other banks. These assets are highly liquid because they can be called at any time. Moreover, they are source of income to the bank.

(2) **Interest on Investments:** Banks also invest an important portion of their resources in government and other first class industrial securities. The interest and dividend received from time to time on these investments is a source of income for the banks. Banks also earn some income when the market prices of these securities rise.

(3) **Discounts:** Commercial banks invest a part of their funds in bills of exchange by discounting them. Banks discount both foreign and inland bills of exchange, or in other words, they purchase the bills at discount and receive the full amount at the date of maturity. For instance, if a bill of ₦1000 is discounted for ₦975, the bank earns a discount of ₦25 because bank pays ₦975 today, but will get ₦1000 on the due date. Discount, as a matter of fact, is the interest on the amount paid for the remaining period of the bill. The rate of discount on bills of exchange is slightly lower than the interest rate charged on loans and advances because bills are considered to be highly liquid assets.

(4) **Commission, Brokerage, etc:** Banks perform numerous services to their customers and charge commission, etc., for such services. Banks collect cheques, rents, dividends, etc., accept bills of exchange, issue drafts and letters of credit and collect pensions and salaries on behalf of their customers. They pay insurance premiums, rents, taxes etc., on behalf of their customers. For all these services banks charge their commission. They also earn locker rents for providing safety vaults to their customers. Recently the banks have also started underwriting the shares and debentures issued by the joint stock companies for which they receive underwriting commission.

(5) **Foreign Exchange Dealings:** Commercial banks also deal in foreign exchange. They sell demand drafts, issue letters of credit and help remittance of funds in foreign countries. They also act as brokers in foreign exchange. Banks earn income out of these operations.

3.2 Banks Investment Policy

The financial position of a commercial bank is reflected in its balance sheet. The balance sheet is a statement of the assets and liabilities of the bank. The assets of the bank are distributed in accordance with certain guiding principles. These principles underline the investment policy of the bank. They are discussed below:

(1) **Liquidity:** In the context of the balance sheet of a bank the term liquidity has two interpretations. First, it refers to the ability of the bank to honor the claims of the depositors. Second, it connotes the ability of the bank to convert its non-cash assets into cash easily and without loss.

It is a well-known fact that a bank deals in funds belonging to the public. Hence, the bank should always be on its guard in handling these funds. The bank should always have enough cash to meet the demands of the depositors. In fact, the success of a bank depends to a considerable extent upon the degree of confidence it can instill in the minds of its depositors. If the depositors lose confidence in the integrity of their bank, the very existence of the bank will be at stake. So, the bank should always be prepared to meet the claims of the depositors by having enough cash. Among the various items on the assets side of the balance sheet, cash on hand represents the most liquid asset. After cash on hand comes cash with other banks and the central bank. The order of liquidity goes on descending.

Liquidity also means the ability of the bank to convert its non-cash assets into cash easily and without loss. The bank cannot have all its assets in the form of cash because each is an idle asset which does not fetch any return to the bank. So some of the assets of the bank, money at call and short notice, bills discounted, etc. could be made liquid easily and without loss.

(2) **Profitability:** A commercial bank by definition is a profit hunting institution. The bank has to earn profit to earn income to pay salaries to the staff, interest to the depositors, dividend to the shareholders and to meet the day-to-day expenditure. Since cash is the least profitable asset to the bank, there is no point in keeping all the assets in the form of cash on hand. The bank has got to earn income. Hence, some of the items on the assets side are profit yielding assets. They include money at call and short notice, bills discounted, investments, loans and advances, etc. Loans and advances, though the least liquid asset, constitute the most profitable asset to the bank. Much of the income of the bank accrues by way of interest charged on loans and advances. But, the bank has to be highly discreet while advancing loans.

(3) **Safety or Security:** Apart from liquidity and profitability, the bank should look to the principle of safety of its funds also for its smooth working. While advancing loans, it is necessary that the bank should consider the three ‘C’s of credit viz; character, capacity and the collateral of the borrower. The bank cannot afford to invest its funds recklessly without considering the principle of safety. The loans and investments made by the bank should be adequately secured. For this purpose, the bank should always insist on security of the borrower.

(4) **Diversity:** The bank should invest its funds in such a way as to secure for itself an adequate and permanent return. And while investing its funds, the bank should not keep all its eggs in the same basket. Diversification of investment is necessary to avoid the dangerous consequences of investing in one or two channels. If the bank invest its funds in different types of securities or makes loans and advances to different objectives and enterprises, it shall ensure for itself a regular flow of income.

(5) **Saleability of Securities:** Further, the bank should invest its funds in such types of securities as can be easily marketed at a time of emergency. The bank cannot afford to invest its funds in very long term securities or those securities which are unsaleable. It is necessary for the bank to invest its funds in government or in first class securities or in debentures of reputed firms. It should also advance loans against stocks which can be easily sold.

(6) **Stability in the Value of Investments:** The bank should invest its funds in those stocks and securities the prices of which are more or less stable. The bank cannot afford to invest its funds in securities, the prices of which are subject to frequent fluctuations.

(7) **Principles of Tax-Exemption of Investments:** Finally, the investment policy of a bank should be based on the principle of tax exemption of investments. The bank should invest in those government securities which are exempted from income and other taxes. This will help the bank to increase its profits.

Of late, there has been a controversy regarding the relative importance of the various principles influencing the investment policy of a bank particularly between liquidity and profitability. It is interesting to examine this conflict.

Let us appraise what happens if the bank sticks to the principle of liquidity only. It is true that if the bank pays importance to liquidity, it can easily meet the demands of the depositors. The bank should have adequate cash to meet the claims of the depositors. It is true that a successful banking business calls for installing confidence in the minds of the depositors. But, it should be noted that accepting deposits is not the only function of a bank. Moreover, the bank cannot afford to forget the fact that it has to earn income to pay salaries to the staff, interest to the depositors, dividend to the shareholders and meet the day-to-day expenditure. If the bank keeps all its resources in liquid form, it will not be able to earn even a kobo. But profitability is a must for the bank. Though cash on hand is the most liquid asset, it is the least profitable asset. Cash is an idle asset. Hence, the banker cannot concentrate on liquidity only.

If the bank attaches importance to profitability only, it would be equally disastrous to the very survival of a bank. It is true that a bank needs income to meet its expenditure and pay returns to the depositors and shareholders. The bank cannot undermine the interests of the depositors. If the bank lends out all its funds, it will be left with no cash at all to meet the claims of the depositors. It should be noted that the bank should have cash to honor the obligations of the depositors. Otherwise, there will be a 'run' on the bank. A run on the bank would be suicidal to the very existence of the bank. Loans and advances, though the most profitable asset, constitute the least liquid asset. It follows from the above that the choice is between liquidity and profitability. The constant tug of war between liquidity and profitability is the feature of the assets side. According to Crowther, liquidity and profitability are opposing or conflicting considerations. The secret of successful banking lies in striking a balance between the two extremities.

5.0 CONCLUSION

The sources of banks income comprise interest on loans, interest on investments, discounts, commission, brokerage and foreign exchange dealings. Their assets are distributed in accordance with certain guiding principles underlining their investment policy. The principles include those of liquidity, profitability, safety, diversity, Saleability of security, investment stability, and the principles of tax-exemption of investments. Of all these principles, liquidity and profitability are opposing or conflicting considerations. The secret of successful banking lies in striking a balance between the two extremities.

A bank is a business organization engaged in the business of borrowing and lending money. A bank can earn income only if it borrows at a lower rate and lends at a higher rate. The difference between the two rates will represent the costs incurred by the bank and the profit.
The sources of banks income comprise interest on loans, interest on investments, discounts, commission, brokerage and foreign exchange dealings. The financial position of a commercial bank is reflected in its balance sheet. The balance sheet is a statement of the assets and liabilities of the bank. The assets of the bank are distributed in accordance with certain guiding principles. These principles underline the investment policy of the bank.

5.0 SUMMARY

We have considered in this unit, the various sources of income available to banking institutions and the investment policy instituted by them.

By this development, we come to the end of module three of this course.

6.0 TUTOR MARKED ASSIGNMENT

- Explain the key factors that influence bank investment policy.
- Liquidity and profitability are opposing or conflicting considerations. To what extent is this submission true?

7.0 REFERENCES/FURTHER READINGS

Bryan, L. Restoring Health and Profitability of our Banking System (New York, Harper Business, 1991)

Okafor, F.O. 50 Years of Banking Sector Reforms in Nigeria (1960-2010): Past Lessons and Future Imperatives (Enugu, Ezu Books Nig. Ltd, 2011)

MODULE 4 NON-BANK FINANCIAL INSTITUTIONS

Welcome to module four of this course. There are four units in this module. They are:

Unit 1 Insurance Institutions
Unit 2 Pension Institutions and Administration
Unit 3 Informal Financial Markets
Unit 4 Informal Financial Institutions

UNIT 1 INSURANCE INSTITUTIONS

CONTENTS

1.0 INTRODUCTION

In this unit, we shall consider the role of insurance institutions in aiding socioeconomic development of a nation.

2.0 OBJECTIVES

The objective of this module is to acquaint students with the concept of insurance, the evolution and growth of insurance in Nigeria as well as the nature and mode of operation of insurance business in Nigeria.

3.0 MAIN CONTENT

Insurance practice dates back to the beginning of the 14th century by Italian merchants who in attempt to protect their investments entered into agreement to bear the risk inherent in movement of goods. The risks associated with shipping of goods subsequently facilitated the evolution of risk insurance policy. Overtime, the popularity of the practice increased. The practice spread to London which was the then hub of maritime business. Modern day insurance practice was introduced to Nigeria by foreign merchants trading in goods from European countries. Insurance companies in Europe extended the risk cover provided for such merchants to their trading activities in Nigeria. These insurance companies subsequently appointed agents in Nigeria to transact business on their behalf locally. So far, a lot of transformations have taken place in the Nigerian insurance landscape from its inception to date. The practice has gradually expanded and flourished. In fact, after the banking industry and the stock market, the insurance industry controls more resources than any other financial service industry in Nigeria.

3.1 Concept of Insurance Business

The concept "insurance" cannot specifically be defined. In the case of *Department of Trade and Industry Vs. St Christopher Motorist Association Ltd* (1974), Templeman J opined that it was undesirable that there should be an all-embracing definition because of the tendency to obscure and occasionally exclude that which ought to be included (NOUN-Law 432). In relative terms however, insurance connotes an arrangement by which a person or an institution offers financial protection against loss or harm such as theft or illness in return for payment of premium. In a more technical term, it is a transaction in which the insurer (the insurance company) for a certain consideration (premium) promises to reimburse (indemnify) the insured or render services in the case of certain accidental losses suffered during the subsistence of the agreement. Section 102 of the insurance Act, 2003 provides that insurance also includes "Assurance" which is and insurance against certainty. That is, insurance against something that is certain to happen such as death, rather than something that might happen such as loss of or damage to property. Insurance therefore is a specie of business that specifically deals with risk management. It is concerned with appraising and controlling risk. It is an intricate legal, economic and social device for the handling of risks to life and property.

Insurance is also a contract. As a contract, the insured receives a cover called insurance policy which stipulates the conditions and circumstances under which the insured will be financially compensated. In most cases, the policy holder pays part of the losses referred to as the deductible while the insurer pays the rest e.g. car insurance, health insurance, disability insurance, life insurance and business insurance.

3.2 Nature and Structure of Insurance Business

Insurance companies accumulate vast sums of money by selling Insurance policies and collecting premiums to generate reserve funds that are invested to earn interest. The reserves are recognized in the insurance policy as cash surrender value. Under the terms of contract, the cash surrender value is the amount available in cash upon voluntary termination of a policy by it owner before it becomes payable at death or maturity.

A policy holder is entitled to the cash value if he or she cancels the policy. More so, the policy holder may borrow from the insurance company against the cash value of the policy. Thus, policy reserves may be viewed equally as a legal liability of the insurance company and as an investment of the policy holder.

Insurance firms mobilize relatively long term financial resources and act as financial intermediaries. Whereas general funds are invested in short tenured assets with high liquidity to make it easy to meet and settle claims timely, life funds can be committed to long term high yielding assets to complement the investment. Their investments are mainly in government securities and the mortgage industry.

Insurance business in Nigeria consists of life and non-life as well as those that engage in both activities and reinsurance operations.

32.1 Life Insurance

Life insurance business is a contractual obligation between the policy holder and the life assurance company by which the assured pays money (premium) in advance either as a lump sum or by installment over the life of the contract and in return for this the life assurance company assumes a specified liability. This liability may be in form of a whole life contract, i.e. term insurance where the sum assured is payable only if death occurs within the period or it may be an endowment assurance in which case the sum is paid on the death of the policy holder or at the end of the contractual period whichever comes first.

The premiums paid by the policy holders are invested in government securities, shares, and loans to corporations against the contingency claims of policy holders. Claims force the insurer to either liquidate some of its assets, draw on current cash flow, or both to settle the claim. Because most life insurance claims are clearly predictable, life insurance companies have a leeway to commit a good portion of their funds to the capital market thereby intermediating household savings with real capital investments of firms and the government.

Life Insurance companies rank among the leading institutions in the international financial system. As a saving vehicle, the products of life insurance companies are functionally similar to those of pension funds. Life insurance premiums are broadly based on age of the insured, average life expectancy of the insured, anticipated investment returns on the insurance fund, operating expenses and a reasonable profit margin.

3.2.2 Non-Life Insurance

The non-life insurance is basically categorized into property and liability insurance. Property insurance is a general term and covers the following specific types of insurance: fire, theft, ocean and inland marine, fidelity and surety, water damage, glass breakage, data processing, domestic/foreign credits and crop insurance. On the other hand, liability insurance is a broad term referring to insurance against losses arising from negligence, assault, libel and trespass.

Fire insurance indemnifies the insured person or business for loses and damage to buildings and personal property caused by fire, windstorm, explosion and other similar perils. Coverage may extend beyond the actual asset to accommodate loss of income and extra expense resulting from the loss of use of the destroyed asset. For instance, fire insurance may indemnify a homeowner against the loss of his house due to fire and the resulting hotel bills incurred until he or she purchases another house.

For theft insurance cover, the protection is against the criminal acts of others such as burglary, robbery and theft by persons other than employees of the insured. Hence, theft insurance is generally referred to as non-employee crime coverage. Criminal acts by employees are protected separately under fidelity bonds. Fidelity bonds protect a business against dishonest employees. When bonded employees embezzle funds or steal money, the bonding company pays for the loss. Most financial institutions in the United States are required by law to bond their employees, because it reduces the risk of failure due to internal embezzlement and fraud. Surety bonds are different from fidelity bonds because they ensure that a specific obligation of one party to another party will be met, rather than indemnifying against criminal acts. Marine insurance covers maritime trade and perils of the sea. Marine insurance insures the actual vessel and its equipment while cargo policies insure the cargo being carried by the vessel. Aviation insurance provides cover against damage to aircraft, legal liabilities and personal accidents.

3.3 Evolution and Growth of Insurance in Nigeria

Insurance business in Nigeria is traceable to the colonial era when the foreign companies which dominated commerce along the Western Coast of Africa wanted local protection of their marine operations in the region. The demand culminated in the setting up of the Royal Exchange Assurance by the British Authority in 1919, with its status upgraded to a branch office in 1920. In 1921, Royal Exchange Assurance Company was incorporated as a Nigerian company to do insurance business, thus becoming the first legitimate insurance company to be registered for insurance business in Nigeria. Three other foreign insurance companies were registered in 1949, but it was not until 1958 that the first indigenous insurance company, the African Insurance Company Ltd commenced insurance business in Nigeria. By 1960, the number of companies conducting insurance business in the country had risen to twenty-five, largely dominated by foreign companies. Government intervention with the establishment of the National Insurance Corporation of Nigeria (NICON) in 1969 and the indigenization Decrees of 1972 and 1977 respectively provided impetus for the establishment of indigenous as well as more foreign owned insurance business in Nigeria. However, the Structural Adjustment Programme of 1986 and the accompanying deregulation of the economy provided a leeway and new impetus for the insurance industry as the number of insurance companies rose from 83 in 1984 to 118 in 2001. However, following recapitalization mandate by the federal government in 2007 occasioned by poor performance in the sector, the number of insurance companies in Nigeria dropped to 49 insurance and 2 reinsurance companies (NAICOM, 2007) respectively.

3.4 Reinsurance Business in Nigeria

Just as individuals insure with insurance companies, the insurance companies themselves also insure either with fellow insurance companies or with insurance companies specialized in a particular area of business. These specialized companies are called

Reinsurance Companies. The Nigeria Reinsurance Corporation was established in 1977 to provide insurance cover for insurance companies. In addition, the Corporation is expected to assist the government in achieving its economic and social objectives in the field of insurance and re-insurance business. Accordingly, all registered insurance companies in Nigeria are statutorily required to reinsure 20 per cent of their total premium collections with Nigeria Reinsurance Corporation for the continent. The reinsurance companies have higher capacity for accumulation of funds faster than general and life insurance companies.

3.5 Nigerian Agricultural Insurance Agency (NAIA)

Agricultural insurance is concerned with the business of insuring agricultural property, crops/livestock and farmers against natural hazards such as fire, windstorm, flood, drought, pest invasion, crop failure, outcomes of war, and other natural and human causative elements that create an unforeseen risk to the farmer. The necessity for an agricultural insurance scheme became obvious in 1976 when moves made to that effect at the highest level of government. That year, government set up a committee to examine the desirability of such a scheme and to formulate proposal for its establishment. Following the recommendations of the committee to examine the desirability, a task force on agricultural on agricultural insurance scheme was set up on 1985 with mandate to work ou the final the final modalities for the operation of the scheme. Subsequently, The Nigerian Agricultural Scheme Agency (NAIA) was established on 15th December 1987 under the auspices National Insurance Cooperation of Nigeria (NICON). NAIA's broad objectives were among others to protect farmers against the effects of natural disaster such as fir, flood, drought, pest, crop failure and to pay commensurate compensation sufficient to keep the farmer in business even after suffering a loss. A reserve fund was established to which the federal government contributed an initial takeoff sum of 41 million. The 5th National Development Plan made provision for federal government's funding of 40 million while the states were to contribute their quota of N60 million. The initial scheme covered only rice and livestock such as such as poultry and cattle. The scheme was later expanded to cover all crops.

4.0 CONCLUSION

Insurance business cannot specifically be defined due to its complexities both by scope and operations. It is by nature an indemnity transaction distinct from other contractual transactions. Performance of obligations by parties to an insurance contract is at the core of its trust and efficiency. Modern insurance practices thrive in Nigeria and the institution is still growing and expanding. Regulation of the sector via recapitalization by the federal government has gone a long way to sanitize the sector and reduced incidence of sharp practices relating to insurance contracts. The reform has also positioned the sector for positive contribution to growth and development of the Nigerian nation.

An insurance policy is a contract that provides equal protection against financial loss associated with unforeseen contingencies or specified and identifiable risk in return for the payment of periodic or lump-sum premium payments to an insurer. By purchasing an insurance policy, the policyholder or his beneficiary reduces his risk exposure to the outcomes of the undesirable event. If the undesirable event fails to occur, the insurer earns profits based on the total sum of premiums collected, incomes accruing from investing the premium less operating expenses. The two main classes of insurance include life and non- life insurance. Life insurance companies are financial intermediaries, which offer policyholders protection against the risk of financial loss associated with death, disability or old age upon the payment of periodic premium.

When undesirable events are not associated with loss or livelihood, the insurance contract is referred to as property and casualty insurance. While life insurance policies are largely long term contracts, non-life insurance policies are essentially short tenured contracts, subjects to frequent renewal. These contracts do not have a saving components associated with them and if the insured unforeseen events fails to occur, the insured cannot be indemnified against a non-accident events. Thus distinction between an assurance and a property/casualty insurance policy is that whereas the former does not rely on risk evaluation in fixing premiums, risk evaluation is a desideratum to the latter.

5.0 SUMMARY

In this unit, we acquainted students with the concept of insurance, the evolution and growth of insurance in Nigeria as well as the nature and mode of operation of insurance business in Nigeria.

In the next unit, our focus will be on pension institutions and administration in Nigeria.

6.0 TUTOR MARKED ASSIGNMENT

- The concept of insurance cannot be specifically defined. Do you agree? Justify.
- Trace the evolution and growth of insurance business in Nigeria.
- What is reinsurance?
- Evaluate the nature and mode of operation of insurance business in Nigeria.

7.0 REFERENCES/FURTHER READINGS

Denise, D.M, Denis, G. & Donna, S. Towards inclusive insurance in Nigeria: An analysis of the Market and Regulations – Publication of the National Insurance Commission (Eschborn, June 2013)

Irukwu, T. O. Insurance Law and Practice in Nigeria (Lagos: Amfitop, 1999)

UNIT 2 PENSION INSTITUTIONS AND ADMINISTRATION

CONTENTS

1.0 INTRODUCTION

In the previous unit, we acquainted students with the concept of insurance, the evolution and growth of insurance in Nigeria as well as the nature and mode of operation of insurance business in Nigeria.

In this unit, our focus will be on pension institutions and administration in Nigeria.

2.0 OBJECTIVES

By the end of this unit, students will be able to conceptualize the history and development of pension institutions in Nigeria. They will also understand the nature and roles of the Nigerian Social Insurance Trust Fund; the basic rationales for the contributory pension reform of 2004 in Nigeria; the nature and operations of the contributory pension scheme (CPS); their achievements so far and their possible challenges in Nigeria.

3.0 MAIN CONTENT

Pension is a regular payment made during a person's retirement from an investment fund to which that person and/or his employer have contributed during his working life. Pension institutions are financial administrators legally licensed to manage pension funds of retired individuals of an organization.

In Nigeria, over the past years, the nation has been grappling with numerous challenges on multiple fronts, among which is pension and gratuity payment system of her ex-workers. Both the private and public sector workers have been confronted with this challenge.

3.1 History and Development of Pension Systems in Nigeria

Generally, pension worldwide is traced to Germany. The credit is given to the former German Chancellor Otto Von Bismarck for enacting a compulsory savings programme for workers in large firms who were exposed to the socialist ideologies in 1889 (Njuguna, 2010). The history of pension scheme in Nigeria dates back to the year 1951 when the first pension scheme was inaugurated in the country. Nigeria's first ever legislative instrument on pension matters was the Pension Ordinance of 1951 which had a retroactive effect from 1st January, 1946. The law provided public servants with both pension and gratuity.

The first legislation to address pension matters of private organizations in Nigeria was in 1961. The legislation gave birth to the National Provident Fund (NPF) scheme. Pensions Act No. 102 and Armed Forces Act No. 103 of 1979 were enacted with retroactive effect from April, 1974 (Ekpulu & Bingilar, 2016). The police and other Government Agencies' Pension Scheme were enacted under Pension Act No. 75 of 1987. This was followed by the Local Government Pension Edict which culminated in the establishment of the Local Government Staff Pension Board of 1987. Three decades after, the National Social Insurance Trust Fund (NSITF) scheme was established in 1993, by decree No. 73 of 1993 to replace the former NPF scheme with effect from 1st July, 1994 to cater for employees in the private sector of the economy against loss of employment, income, old age, invalidity or death.

3.2 Nigerian Social Insurance Trust Fund (NSITF)

Nigerian Social Insurance Trust Fund (NSTIF) came into existence by decree No. 73 of 1993. The major objectives of the fund were to employ a more comprehensive pension security scheme for Nigerian private sector employees. The scheme was established to supplant the National Providence Fund (NPF), which came into being in 1961 as a compulsory pension scheme for non-pensionable public servants and employees in the private sector. The NSITF inherited the NPF's assets and liabilities. The scheme was expected to enhance the benefits payable to contributors. The rate of contribution was ten percent of registered employee's salary/wages subject to a maximum salary of ₦528, 000 per annum. Out of the ten percent, the employee was expected to contribute 3.5 percent. As at December 1999, the total contribution collected by NSITF from employees stood at N5.228 billion with 9,988 and 558,985 registered employers and employees, respectively (CBN, 2004).

In terms of Product offering and processes, NSITF offered a wide range of medium and long term Infrastructure facilities to investors. The loans were used to finance companies expansion and often project tied. Their activities were targeted mainly at manufacturing, agriculture, cooperatives, small and medium scale enterprises and stat owned enterprises. NSITF provided equity and loanable funds to industries, indigenous persons and organizations by providing a wide range of allied financial services, including loan syndication guarantee, letter of credit and bills for collection, feasibility studies and management consultancy. It was perceived that the institution will contribute to industrial capital formation, foreign exchange conservation through import substitution and employment generation.

3.3 Rationales for Contributory Pension Reform in Nigeria

The evolution and development of pension scheme in Nigeria have not been without challenges. So many things happened in the old pension scheme thus necessitating the need for the reform of the sector by the federal government in July 2004 to position the sector better for development and general welfare of the citizenry. Prior to the reform period, most public organizations operated a Pay-As-You-Go defined benefit pension scheme and final entitlements were based on length of service and terminal emoluments. The defined benefit pension scheme in Nigeria was afflicted by many problems among which was poor funding due to inadequate budgetary allocations, weak as well as inefficient and non-transparent pension administration, unsustainable outstanding pension liabilities; demographic shifts and aging of the scheme; non-courage of workers in the private sector by any form of compulsory retirement benefit arrangement; and poor regulation of the hitherto scheme.

Besides, there was paucity of authenticated data for living pensioners and about 14 documents were required to be filed for pension claims. Moreover, sharp practices in the investment and management of pension funds aggravated the problems of pension liabilities and over 300 government ministries, agencies and parastatals were bankrupt. The above deficiencies predicated the need for proper and adequate reformation of the existing pension scheme in Nigeria in order to properly cater and provide for retirees benefit, hence, the emergence of the Contributory Pension Scheme (CPS) in 2004.

3.4 Contributory Pension Scheme (CPS) 2004 in Nigeria

The pension reform Act 2004 ushered in the contributory pension scheme in Nigeria. The scheme was established for all employees of the federal public service, Federal Capital Territory (FCT) and the private sectors including the informal sector employees in Nigeria. Being a contributory scheme, employees are to contribute minimum of 7.5 percent of basic salary, housing and transport allowances and employers are to also contribute a matching fund. So the total minimum monthly contribution of a typical employee contributor under the scheme is 15 percent of basic salary, housing and transport allowances. The major operators under the scheme are the National Pension Commission (PenCom), Pension Fund Administrators (PFAs), Closed Pension Fund Administrators (CPFAs) and Pension Fund Custodians (PFCs).

PenCom was established to regulate, supervise and ensure effective administration of pension matters in the new scheme. Prior to the new pension scheme, Nigeria operated a Pay As You Go defined Benefit Scheme burdened with lots of problems. According to Ahmed (2006), the CPS is premised on the following objectives:

- Ensure that every worker receives his retirement benefits as and when due.

- Empower and assist workers to save in order to cater for their livelihood during old age.
- Stem the growth of pension liabilities.
- Establish uniform rules, regulation and standards for the administration of pension matters.
- Secure compliance and promote wider coverage.

3.5 Achievements of the CPS in Nigeria

Since its commencement in 2004 to date, the CPS has recorded tremendous achievement as highlighted:

(i) The pension industry has grown from zero position to having a subscriber base of over N5.28 billion (PWHC, 2012).
(ii) The industry has also been able to create an atmosphere of transparency, and trust in dealing with stakeholders. The credit is attributed to the management style of the pioneer executive management of PenCom.
(iii) Again, the consultancy approach of PenCom in interaction with industry players as well as effective collaboration with other regulators in the financial industry has generated a robust regulatory framework which has successfully guided the affairs of the pension industry to date.
(iv) Furthermore, separation of the function of the Pension Fund Administrator (PFAs) from those of the Pension Fund Custodian (PFCs) has enhanced the security of the Pension fund assets. Unlike the previous pension scheme retirees have received their benefits within six month.

3.6 Challenges of the CPS in Nigeria

The ongoing contributory pension scheme in Nigeria is not without challenges. Few of the key challenges include:

- Paucity of investment instruments for Pension Fund Asset.
- Unhealthy activities of some regulatory agencies within the Nigerian financial system such as Securities and Exchange Commission (SEC), National Insurance Commission (NAICOM)
- Dearth of skilled manpower within the industry to enable it effectively carryout its mandate.

4.0 CONCLUSION

The legitimate right of every employee who has worked or is currently working for an organization, public or private, for a reasonable number of years is to be entitled to some benefits. The benefits could be in form of gratuity and pension payable to such employee by its employer at the time of retirement. Pension is a regular payment made during a person's retirement from an investment fund to which that person or their employer has contributed during their working life. It is a sum of money paid regularly to a person who no longer work because of old age, disability or retirement or to his widowed or dependent children by the state, former employers or from provident fund to which he and his employer both contributed. Pension companies are financial administrators legally licensed to manage pension funds of retired individuals of an organization. Nigeria has witnessed significant pension reform from the inception of pension in the country to date. Presently, the contributory pension scheme (CPS) is currently being experimented. While numerous achievements have been recorded, the scheme is still confronted with many challenges.

Pension is a sum of money paid regularly to a person who no longer work because of old age, disability or retirement or to his widowed or dependent children by the state, former employers or from provident fund to which he and his employer both contributed. In Nigeria, over the past years, the nation has been grappling with numerous challenges on multiple fronts, among which is pension and gratuity payment system of her ex-workers. Both the private and public sector workers have been severely affected. The public sector workers have suffered a lot under the Defined Benefit Scheme (DBS) and their private sector counterparts have been pained owing to different pension plans by their respective employers. Retirement benefit paid to retired employees prior to 2004 Reform Act was gratuity and pension.

The emergence of contributory pension scheme in 2004 brought huge relief to retiring employees as the scheme is designed to confront the problems inherent in the old Pay-As-You-Go scheme. The effective regulations of the scheme by PenCom have brought significant achievement including the growth of the industry from zero position to having a subscriber base of over N5.28 billion. The ongoing contributory pension scheme is however not without challenges. Among other major challenges, the scheme is seriously affected by dearth of skilled manpower within the industry to enable it effectively carryout its mandate.

5.0 SUMMARY

In this unit, students were able to conceptualize the history and development of pension institutions in Nigeria. They will also understand the nature and roles of the Nigerian Social Insurance Trust Fund; the basic rationales for the contributory pension reform of 2004 in Nigeria; the nature and operations of the contributory pension scheme (CPS); their achievements so far and their possible challenges in Nigeria.

In the next unit, we shall consider the informl financial markets and institutions in Nigeria.

6.0 TUTOR MARKED ASSIGNMENT

- Examine the products and offering processes of the Nigerian Social Insurance Trust Fund.
- What are the basic rationales for the contributory pension reform of 2004 in Nigeria?

- Appraise the achievements and challenges of the contributory pension scheme in Nigeria.

7.0 REFERENCES/FURTHER READINGS

Afolabi, A. A. An Evaluation of Pension Industry in Nigeria (International Journal of Banking, Finance, Management & Development Studies Vol. 3, No. 1, 2015)

Ekpulu, G. A. & & Bingilar, P. F. Pension Fund in Nigeria: An Appraisal (Quarterly Journal of Contemporary Research, Volume l 1&2, 2016)

UNIT 3 INFORMAL FINANCIAL MARKETS

CONTENTS

1.0 INTRODUCTION

In the last unit, students were able to conceptualize the history and development of pension institutions in Nigeria. They will also understand the nature and roles of the Nigerian Social Insurance Trust Fund; the basic rationales for the contributory pension reform of 2004 in Nigeria; the nature and operations of the contributory pension scheme (CPS); their achievements so far and their possible challenges in Nigeria.

In this unit, we shall consider the informal financial markets in Nigeria.

2.0 OBJECTIVES

This unit examines the evolution and nature of informal financial markets in Nigeria as well as their objectives and mode of operations.

3.0 MAIN CONTENT

Informal financial markets are financial arrangements that exist outside the framework of formal financial regulations. These markets however also contribute immensely to economic development of nations. Predominantly, informal financial groupings are more visible in rural societies but their presence is also recorded in the urban centres. As many as five or more informal financial groupings can be found in a village of less than 500 people and as many as 20 in a Nigerian rural town. Despite the proliferation of banks and other formal financial intermediaries, informal financial markets have continued to show strong presence in the cities to date.

3.1 Evolution of Informal Financial Markets in Nigeria

While anecdotal submissions have argued that the history of the evolution of informal financial markets in Nigeria is lost in antiquity, recent empirical studies have traced it to the evolutionary forces of the barter economies (Otu, Egbuna, Essien, and Tule, 2003) in which accumulated surpluses were initially exchanged in kind for labour, and later, for higher technology. The barter system of exchange served Nigerian communities relatively well and performed some of the vital roles of modern banking though in a limited and unsophisticated fashion. Owing to their largely unregulated environment, the informal financial markets have poor record keeping and unconventional auditing process. In terms of coverage and number, the informal financial markets are much larger than the formal financial institutions but not necessarily in the volume of activities.

3.2 Nature of Informal Financial Markets

The informal financial markets operate mostly on the principle of Rotating Savings and Credit Associations (ROSCAS) which have a long history in developing countries and they continue to be a major source of credit in African countries. Typically, a small group is formed from a village or family group where enforcement costs are low because of powerful social sanctions. Each member agrees to contribute periodically a certain amount, into a common pool, so that each, in rotation, can receive one large sum. It is built on trust and membership is often drawn from homogeneous groups e.g. from the same ethnic background, same work place or same neighborhood. If a member defaults in repaying a loan, the community bans him and if a member is banned from one group he is rejected by the community. The multiplicity and spread of membership among different forms of institutions is equally common both amongst the rural and urban clients. Sanctions and loan recovery methods are broadly similar, between urban and rural dwellers, across peoples, societies, communities, and countries. In almost all forms of informal financial institutions, peer group pressure and cohesion provide the most potent tool for loan recovery, an attribute that is conspicuously missing in formal financial institution.

Informal financial markets are also featured by regularity of contributions at periodic intervals. The frequency of contributions ranges from daily contribution associated with the highly informal itinerant traders-type contribution to the monthly contributions of the more organized semi-formal and cooperative-type Adashi and Bam groups. In-between these two extremities, there is an admixture of arrangements that suit particular groups but which depend to a large extent on needs and exigencies. However, variations are often dictated more by the nature of trade of the clients than other considerations

Another observable trait of informal financial markets is the high interest rates associated with transactions in the market. The interest rates which are often higher than the formal market interest rates, do not serve as a disincentive to clients in the informal credit market because, the market is flexible enough to accommodate the credit needs of every group. This is evidenced b' the unusually high patronage observed in the market and the increasing profile of its clientele. Although membership is optional, in co-membership associated with some groups, it could be involuntary. In some cases, there is co-membership because a member registers as many family members as possible under his family name, and makes periodic contributions under their names. However, such involuntary members are not entitled to credit facility, in which case, they are technically not members. Operationally however, they are members because the sponsor can arrogate all benefits accruing under their membership to himself.

The membership of informal financial markets is usually widespread, but largely adjoining. Thus, people who do not reside within a contiguous geographical location are not admitted. Besides, a prominent member, with a good financial stand in a group, must introduce an intending member not known within the society. In the event of such a member request for a credit facility, the pattern of his contributions must be closely studied with a view to ascertaining his credit profile. The surety, who must also be a prominent member with a good financial standing, must also have an impressive moral record. He must also exhibit impressive track record in previous transactions involving suretyship and loan procurement and repayment.

3.3 Informal Foreign Exchange Market

With the financial market reforms adopted in Nigeria since 1986, four segments of the foreign exchange market emerged: official market, bureau de change, the free funds market and the parallel market. Our focus shall be on the parallel market. In Nigeria, the concept of parallel market is most often wrongly associated with the foreign exchange market transaction. Government interventions introduce distortions in the foreign exchange market and so the price that emerges does not clear the market, hence the parallel market evolved to absorb the excess demand. Thus, the parallel market as it relates to foreign exchange transactions is linked to the inability of the foreign exchange market to efficiently meet certain foreign exchange needs of the end-users. The funds are sourced from the formal institutions and are patronized largely by merchants. The attraction of this market is the absence of documentation thereby making transactions faster. Customers do not need to disclose the source and/or intended use of the foreign exchange to the dealer. Participants in this market are not accorded legal recognition. Therefore, anyone who buys or sells foreign exchange may become an operator in the market. The market, though not legally recognized, has the advantage of smooth information flow and quick service delivery compared with the other segments of the informal financial market.

4.0 CONCLUSION

Informal financial markets have been recognized as a highly diverse grouping, integrating all financial activities consummated outside the functional scope of formal financial regulations. Participants in these markets include moneylenders, mobile savings collectors, rotating savings and credit associations, mutual assistance groups, landlords, neighbors, friends, and family members, who are active in financial intermediation through savings mobilization and credit creation amongst low income earners.

The supply of loanable funds from these sources is largely limited; however, evidence shows that the quantum of credit to the low income group is traced to the financial intermediation activities of informal credit markets.

Informal financial markets explain financial arrangements consummated outside the framework of formal financial regulations. While anecdotal evidence submits that the history of the evolution of informal financial markets in Nigeria is lost in antiquity, recent empirical studies have traced it to the evolutionary forces of the barter economies in which accumulated surpluses were initially exchanged in kind for labour, and later, for higher technology.

Often, the informal financial markets operate on the principle of Rotating Savings and Credit Associations which have a long history in developing countries and they continue to be a major source of credit in African countries.

Membership of informal financial markets is usually widespread, but largely adjoining. Thus, people who do not reside within a contiguous geographical location are not admitted.

5.0 SUMMARY

This unit examined the evolution and nature of informal financial markets in Nigeria as well as their objectives and mode of operations.

In the next unit, we shall consider the informal financial institutions in Nigeria.

6.0 TUTOR MARKED ASSIGNMENT

- Operationalize the evolution and nature of informal financial markets in Nigeria.
- What constitute the markets objectives and mode of operations?

7.0 REFERENCES/FURTHER READINGS

Okafor, F. O., Micro-Credit: An Instrument for Economic Growth and Balanced Development (African Banking and Finance Review Vol. 1 No.1, 2000)

Otu, M.F., Egbuna, E.N., Essien, E.A., Tule, M.K. Informal Credit Market and Monetary Management in Nigeria (Central Bank of Nigeria Occasional Paper Series, 2003)

UNIT 4 INFORMAL FINANCIAL INSTITUTIONS

CONTENTS

1.0 INTRODUCTION

In the last unit, you learn the informal financial markets in Nigeria. The study considered the evolution and nature of informal financial markets as well as informal foreign exchange market.

In this unit, we shall discuss informal financial institutions.

2.0 OBJECTIVES

This unit examines the different forms of informal financial institutions and their sustainability in Nigeria.

3.0 MAIN CONTENT

Informal financial institutions play leading roles of financial intermediation in the informal financial markets. They are those financial institutions or associations not integrated into the formal financial institutions framework of the formal financial system but whose activities bridge the financing gap between the surplus spending and deficit spending economic units.

Their activities are therefore very pivotal in stimulating effective economic performance. Informal financial institutions operating in the Nigerian informal markets include moneylenders, mobile savings collectors, rotating savings and credit associations, mutual assistance groups, landlords, neighbors, friends, and family members, who are active in financial intermediation through savings mobilization and credit creation amongst low income earners.

3.1 Nature of Informal Financial Institutions

Ordinarily, informal financial institutions are easily identifiable in Nigeria because of the permanence of shared forms and characteristics.

There is however, no identifiable distinction between informal financial institutions operating in urban and those in rural areas. Also the volume of resources mobilized does not exhibit any meaningful difference based on location.

3.2 Forms of Informal Financial Institutions

The most common forms of informal credit institutions, involving the transfer of cash in Nigeria are the Esusu, Bam, and Adashi. In the southern part of the country, the several heterogeneous communities have different variants of this informal financial association, often reflecting the peculiarities of their communities. For instance, amongst the Ibos of the southeast, it is commonly known as Isusu whilst the Yorubas call it Ajo. The Ibibios call it Efe while the Kalahari Ijaws call it Oku. In the north central zone, these informal financial associations are severally known as Adashi, Adashe, and Bam.

3.2.1 Esusu/Isusu & Adashi

Esusu or Isusu or Adashi is a contribution-based-savings-scheme that is principally interest-free. Esusu is very common especially amongst the rural communities of Nigeria. The main factor for the arrangement or membership is shared or common interest. Adashi meeting are periodic i.e, weekly, fortnightly, or monthly depending on what members agreed upon. The schedule of the Adashi is drawn up indicating when a member will take his turn as a beneficiary whose turn it is to collect the Adashi. The binding principle is that once the Adashi has commenced and other beneficiaries have taken their turn, members cannot voluntarily withdraw their membership without disrupting the schedule. Thus, group pressure makes continuity possible. Also a member who had been a beneficiary cannot withdraw his membership until all members who contributed have taken their turns. Often, all members contribute the same amount.

3.2.2 Bam

Bam is a periodic savings scheme mostly found in the north central part of Nigeria. Essentially, it involves the meeting of like minds with the intention to provide a pool of savings to be withdrawn at the end of the year. All intending members are required to pay a stipulated registration fee. A member can register himself and some members of his family and there is no limit as to the number of his family members he can register. What is essential however is that once registered and periodic contributions are made, members are obliged to continue to contribute the same amount they started with. Default attracts a penalty. The benefit of multi-membership is that the accrued interest from loans granted by the bam is shared at the close of every season to members according to contributions. The more members a person has under his name in addition to his total savings, the larger his interest.

Bam loans normally carry a predetermined interest element, which is paid up-front on receipt of the loan. The loans are highly collaterised and fully repayable before the close of the bam season. The collateral is often the savings of the beneficiary and those of his guarantor. However, if these sources were unable to extinguish the loan, the personal property of the beneficiary is attached. To this end, Bam loans have an exceptionally high repayment rate with no default, as group pressure compels a high repayment rate.

3.2.3 Daily cum Periodic Contributions

This is like a savings scheme amongst traders and artisans in which an agreed amount of money is paid daily, to a convener, agreeable to the traders. The convener or his agent goes about with a register and membership cards which he issues to new members and in which the amounts contributed on a daily basis are recorded. A member pays an agreed amount on a daily basis which must be recorded promptly in both the register and the membership card. The savings are paid back to the contributors at the end of an agreed period, usually, a month. The contributors forfeit a day or two days savings to the collector to cover his cost of operations. The advantage of this system is that traders who would not have been able to save because of the vagaries of the particular trade are able to save and provide working capital at the end of every month. In addition, it affords traders the opportunity to make savings without the trouble of abandoning their businesses to go to a bank which may be far away from their place of work. Hence, this system has a major attraction for traders. The major difference between this scheme and "Esusu" is that members need not know themselves apart from the collector and there is no loan facility to members.

3.2.4 Money Lenders

Money lenders are direct offshoot of post-barter and pre-colonial money economy. The practice is therefore as old as the origin of money. It exemplifies a typical economic model in which surplus-spending-units lend their surpluses to deficit-spending-units for investment. Anyone in need of urgent funds but could not find it elsewhere, end up at the money lenders shop. Since the money lender operates single-handedly, and is consulted only in periods of crisis, he is at liberty to charge interest rates that are most often, very high and not related to the economy-wide interest rates. Though he may replenish his money stock from the formal financial markets, nevertheless, the interest plus margin, which he charges, compensates for the vagaries of loan repayment.

3.2.5 Cooperative and Thrift Societies

Cooperative and thrift societies provide a veritable source of funds mobilization and participatory credit administration in Nigeria. They are organized to mobilize savings and to channel financial resources to individual needs, largely for consumption. Cooperative societies are associations of persons, employees, usually of limited means, who voluntarily come together on the basis of equality and equity for the enhancement of member's corporate and individual welfare. A member has the privilege of borrowing from the society at highly reduced interest rate. Each member is entitled to borrow about 100 percent of the amount deposited with repayment period not exceeding one year. For employees in the same organization, default risk is minimized through arrangements with the employer to deduct loan repayment from salary at source, thereby confining possible cases of default to indebted members that are dismissed or suddenly compelled to leave the service.

The society derives substantial income through the investment of surplus contribution in formal financial institutions. Sources of income of the society include interest on loans to members and investments. Cooperatives are very popular in Nigeria, particularly in the south-western Nigeria where they have existed for over a century, and have achieved remarkable feats. Although, cooperative societies mobilize savings and grant credits, the extent of financial intermediation undertaken is extremely limited in the sense that they do not maintain reserves and do not engage in fractional reserve banking or money creation. Like other informal financial institutions, the value of credits granted is relatively small. More importantly, the credit extended is not usually included in the aggregate domestic credit on which macroeconomic policy is based.

3.2.5 Savings and Credit Associations

This type of association operates in a more formalized way than the "Esusu" kind of association, and is therefore much closer to the variants of the formal financial system. Savings and credit associations may or may not be registered under legislation but they are always registered under the Cooperative Association Act. This type of semi-formal financial institution has a significant presence in rural Nigeria.

These associations function in a similar fashion as the credit and thrift societies. Their modus operandi is not too different from the Bam, Adashi, or other credit associations. They are mainly organized by traders or persons in the same trade or even by people whose professions cut across; savings are periodic; the level of savings largely depend on the ability of the members; and benefits may be in kind or financial. For instance, a member would be given some bonus shares, or loans to expand his trade or start a new business. Also, deposits are recorded in the passbooks. A member could borrow twice or more of the amount contributed. Loans are repayable over a period of time which does not exclude members from periodic contributions. Another attraction of savings and credit association is that loan defaulters are subjected to unorthodox methods for the recovery of outstanding loans, including realization of outstanding balance from pledged security and the sale of the personal property of the borrower.

3.3 Other forms of Informal Financial Institutions

A wide variety of informal financial institutions exist, such as the highly informal credit in kind associations that are morally motivated, but not necessarily financially induced. Within this spectrum, can be identified three principal classes: those whose credit is cash based, those who extend credit facilities in kind, and a hybrid of the two. The in-kind type of informal finance involves pooling of labour, extension of goods/articles of trade to other traders who sell and make returns. It is also popular in farming projects such as: land clearing, planting, and harvesting or for building a new house. This type of labour-pooling approach varies among different ethnic groups. Amongst the Yorubas of the south west, it is known as *aaro*; amongst the Hausa, *gayya*; and *Ihyumbe* amongst the Tiv of the north central. This type of association pools together the labour of two or more people, to work often on a farm for a given period. This has to be ‘repaid to other members of the pool on rotational basis and for the same period. Gayya, another variation of this association involves working on members’ farms, using simple farming implements like ox-drawn carts

4.0 CONCLUSION

Informal financial institutions bridge the financing gap between the surplus spending and deficit spending economic units. They perform the crucial role of financial intermediation through savings mobilization and credit creation amongst low income earners. Their activities are very germane in stimulating effective economic performance in the aggregate economy. Informal financial institutions have existed since the origin of the barter economy. Their distinctive modus operandi inform the sustainability of their operation till date. Informal financial institutions operating in the Nigerian informal markets include moneylenders, mobile savings collectors, rotating savings and credit associations, mutual assistance groups, landlords, neighbors, friends, and family members.

Informal financial institutions are those financial institutions or associations not integrated into the formal financial institutions framework but whose activities bridge the financing gap between the surplus spending and deficit spending economic agents. They play leading roles of financial intermediation in the informal financial markets. Informal financial institutions are easily identifiable in Nigeria because of the permanence of shared forms and characteristics. The most common forms of informal credit institutions, involving the transfer of cash in Nigeria are the Esusu, Bam, and Adashi. Esusu is a contribution-based-savings-scheme that is principally interest-free. It is very common especially amongst the Ibo rural communities of Nigeria. Bam is a periodic savings scheme mostly found in the north central part of Nigeria.

Money lenders are direct offshoot of post-barter and pre-colonial money economy. The practice is therefore as old as the origin of money. Money lender operates single-handedly, and is consulted only in periods of crisis. For this reason, he is at liberty to charge interest rates that are most often, very high and not related to the economy-wide interest rates. Cooperative societies are associations of persons, employees, usually of limited means, who voluntarily come together on the basis of equality and equity for the enhancement of member’s corporate and individual welfare. Savings and credit associations operate in a more formalized way than the “Esusu” kind of association, and are therefore much closer to the variants of the formal financial system. They may or may not be registered under legislation but they are always registered under the Cooperative Association Act.

5.0 SUMMARY

This unit examines the different forms of informal financial institutions and their sustainability in Nigeria.

By this development, we have come to the end of module four.

6.0 TUTOR MARKED ASSIGNMENT

Examine the different forms of informal financial institutions and their sustainability in Nigeria.

7.0 SUGGESTED FURTHER READINGS

Okafor, F. O., Micro-Credit: An Instrument for Economic Growth and Balanced Development (African Banking and Finance Review Vol. 1 No.1, 2000)

Otu, M.F., Egbuna, E.N., Essien, E.A., Tule, M.K. Informal Credit Market and Monetary Management in Nigeria (Central Bank of Nigeria Occasional Paper Series, 2003)

MODULE 3: INTERNATIONAL FINANCIAL INSTITUTIONS

Welcome to the fourth and final module for this course. The module contains four units which are listed below.

UNIT 1 INTERNATIONAL FINANCIAL MARKET DIFFICULTIES

CONTENTS

1.0 INTRODUCTION

The globalization of financial markets constitutes a major challenge to the regulation of financial activities and institutions which continues to be carried out by national governments. It creates several problems for which solutions are not easy to implement.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- discuss the difficulties encountered in International financial market; and
- proffer possible remedial actions for the identified issues.

3.0 MAIN CONTENT

3.1 International financial market difficulties

The difficulties encountered in the operation of the international financial markets are as stated below:

- First, due to the growing interdependence in international financial markets financial difficulties experienced in one country can easily spill over to other countries. A systemic crisis in one country and the failure of its authorities to deal with it appropriately may lead to a global banking crisis.

- Second, regulation can be considered as a tax and can have an impact on the international competitiveness of financial institutions. Different regulatory regimes may also create barriers for firms in cross-border trade in financial services. For instance, different capital requirements create an unlevel playing field between financial institutions of different countries.

- Third, financial institutions may attempt to avoid more stringent domestic regulation by locating abroad. Regulatory arbitrage impairs the effectiveness of regulation and the ability of different countries to maintain their own regulatory framework. Regulatory competition may eventually lead to a downward regulatory spiral. As is demonstrated in a game-theoretic framework by taking into account the special informational characteristics of financial products and the role of reputation in the banking industry there may, however, be limits to this process. In particular in retail markets where financial integration is far less complete there remain upward regulatory pressures. Countries will be able to maintain regulatory measures as a signal of quality differentiation provided that they are valued by customers.

3.2 Possible remedies

The concern for the distortion of international competition certainly has been a major driving force behind attempts towards worldwide solutions for financial regulation. Recent international financial crises are increasing the urge for an international approach. International market integration also helps to explain the recent shift of emphasis from structural towards prudential regulation.

Through efforts of international coordination an answer is sought for the questions of what should be the right of access to foreign markets, and whose rules should apply in international financial services. In this respect a tendency is observed to give branches and subsidiaries of foreign banks the same treatment as domestic banks. For cross-border transactions of financial intermediaries it is proposed that they should be monitored by the home country. Regulation and coordination can be limited as banks should be allowed to develop their own risk-assessment procedures which should only be subject to regulatory review.

Taking into account the concern for the threat of complete deregulation, however, stronger forms of international harmonization are also being envisaged. The European Union has linked policies of mutual recognition and home country control rules with agreements on minimum standards of conduct. The Basel Committee on Banking Supervision has laid down common bank capital rules. These minimum standards, continue to be enforced by individual countries. They are, however, being criticized for their arbitrariness and potential inflexibility. Finally, faced with the increasing need for worldwide regulation, an agreement that extends beyond the Basle countries on a set of minimum capital standards, as Goldstein (1997) has argued for may be eventually attained. But international cooperation beyond these minimal standards remains a difficult issue. In particular, faced with the fragmented supervision by many agencies to be multiplied by the number of countries, the prospects for international cooperation to reinforce supervision remain bleak. These difficulties to agree on the international dimension of financial regulation and supervision are enhancing the overall trend towards greater emphasis on discipline by the market rather than by regulators.

4.0 CONCLUSION

In the face of the possibility of a worldwide systemic crisis the lender of last resort function still remains largely the endeavor of national central banks. Whether emergency liquidity assistance should be provided not only for banks but also for other financial intermediaries, and whether the lender of last resort function should be provided at the international level, remain heavily debated issues.

5.0 SUMMARY

You have learnt in this unit that the major International financial market difficulties as well Possible remedial actions for the identified issues

In this next unit, you will consider the international monetary fund (IMF).

6.0 TUTOR-MARKED ASSIGNMENT

Discuss briefly three international financial difficulties

7.0 REFERENCES/FURTHER READINGS

Afifia-Oru, B. (2009). *Dynamics of credit economic system in Africa*, Lagos : Byolah concepts ltd

Central Bank of Nigeria (2011). Understanding Monetary Policy series no 3, CBN Monetary Policy Framework.

Chand, S. (Undated). Economic stabilization: Monetary policy and direct controls, retrieved from www.yourarticlelibrary.com/eco

Dirk, H. (1999). Regulations of banking and financial market, Encyclopedia of Law & Economics

Osaze, E.B. (2007). *Capital markets,* Lagos : The Bookhouse Company

UNIT 2 INTERNATIONAL MONETARY FUND (IMF)

CONTENTS

1.0 INTRODUCTION

You have learnt in the last unit that the major International financial market difficulties as well Possible remedial actions for the identified issues

In this unit, you will consider the international monetary fund (IMF). This study will include defining the concept, enumerating the functions and the role in undertaking surveillance of the global economy.

2.0 OBJECTIVES

At the end of this unit you should be able to define the concept IMF, enumerate and discuss the functions performed by this multilateral financial institutions and the role undertaken by them to ensure surveillance of the global economy.

3.0 MAIN CONTENT

3.1 Meaning of International Monetary Fund (IMF)

The International Monetary Fund (IMF) is an international organization that was initiated in 1944 at the Bretton Woods Conference and formally created in 1945 by 29 member countries. The IMF's stated goal was to assist in the reconstruction of the world's international payment system post-World War II. Countries contribute money to a pool through a quota system from which countries with payment imbalances can borrow funds temporarily. Through this activity and others such as surveillance of its members' economies and the demand for self-correcting policies, the IMF works to improve the economies of its member countries (Escobar, 1980). The IMF describes itself as "an organization of 188 countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world." (IMF, 2012). The organization's stated objectives are to promote international economic co-operation, international trade, employment, and exchange rate stability, including by making financial resources available to member countries to meet balance of payments needs. Its headquarters are in Washington, D.C., United States.

3.2 Functions of International Monetary Fund (IMF)

The IMF works to foster global growth and economic stability. It provides policy advice and financing to members in economic difficulties and also works with developing nations to help them achieve macroeconomic stability and reduce poverty. The rationale for this is that private international capital markets function imperfectly and many countries have limited access to financial markets. Such market imperfections, together with balance of payments financing, provide the justification for official financing, without which many countries could only correct large external payment imbalances through measures with adverse effects on both national and international economic prosperity (Isard, 2005).The IMF can provide other sources of financing to countries in need that would not be available in the absence of an economic stabilization program supported by the fund. Upon initial IMF formation, its two primary functions were: to oversee the fixed exchange rate arrangements between countries, thus helping national governments manage their exchange rates and allowing these governments to prioritize economic growth, and to provide short-term capital to aid balance of payments. This assistance was meant to prevent the spread of international economic crises. The Fund was also intended to help mend the pieces of the international economy post the great depression and World War II.

The IMF's role was fundamentally altered after the floating exchange rates post 1971. It shifted to examining the economic policies of countries with IMF loan agreements to determine if a shortage of capital was due to economic fluctuations or economic policy. The IMF also researched what types of government policy would ensure economic recovery (Jensen, April 2004). The new challenge is to promote and implement policy that reduces the frequency of crises among the emerging market countries, especially the middle income countries that are open to massive capital outflows. Rather than maintaining a positive of oversight of only exchange rates, their function became one of "surveillance" of the overall macroeconomic performance of its member countries. Their role became a lot more active because the IMF now manages economic policy instead of just exchange rates.

In addition, the IMF negotiates conditions on lending and loans under their policy of conditionality, which was established in the 1950s. Low-income countries can borrow on concessional terms, which mean there is a period of time with no interest rates, through the Extended Credit Facility (ECF), the Standby Credit Facility (SCF) and the Rapid Credit Facility (RCF). Non-concessional loans, which include interest rates, are provided mainly through Stand-By Arrangements (SBA), the Flexible Credit Line (FCL), the Precautionary and Liquidity Line (PLL), and the Extended Fund Facility. The IMF provides emergency assistance via the newly introduced Rapid Financing instrument (RFI) to all its members facing urgent balance of payments needs.

3.3 Surveillance of the global economy

The IMF is mandated to oversee the international monetary and financial system and monitor the economic and financial policies of its 188 member countries. This activity is known as surveillance and facilitates international co-operation. Since the demise of the Bretton Woods system of fixed exchange rates in the early 1970s, surveillance has evolved largely by way of changes in procedures rather than through the adoption of new obligations. The responsibilities of the Fund changed from those of guardian to those of overseer of members' policies. The Fund typically analyses the appropriateness of each member country's economic and financial policies for achieving orderly economic growth, and assesses consequences of these policies for other countries and for the global economy.

3.4 Conditionality of Loans

IMF conditionality is a set of policies or conditions that the IMF requires in exchange for financial resources. The IMF does not require collateral from collateral economic but rather requires the government seeking assistance to correct its macroeconomic imbalances in the in the form of policy reform. If the conditions are not met, the funds are withheld. Conditionality is perhaps the most controversial aspect of IMF policies. The concept of conditionality was introduced in an Executive Board decision in 1952 and later incorporated in the Articles of Agreement. Conditionality is associated with economic theory as well as an enforcement mechanism for repayment; Stemming primarily from the Work of Jacques Polak in the Fund's research department, the theoretical underpinning of conditionality was the “monetary approach to the balance of payments." (Chorev and Babb, June 2009)

3.5 Structural Adjustment

Some of the conditions for structural adjustment can include:

- Cutting expenditures, also known as austerity.
- Focusing economic output on direct export and resource extraction.
- Devaluation of currencies.
- Trade liberalization, or lifting import and export restrictions.
- Increasing the stability of investment (by supplementing foreign direct investment with the opening of domestic stock markets).
- Balancing budgets and not overspending.
- Removing price controls and state subsidies.

- Privatization or divestiture of all or part of state-owned enterprises.
- Enhancing the rights of foreign investor's vis-a-vis national laws.
- Improving governance and fighting corruption.

These conditions have also been sometimes labeled as the Washington Consensus.

3.6 Benefits of MF Loan conditions

These loan conditions ensure that the borrowing country will be able to repay the Fund and that the country won't attempt to solve their balance of payment problems in a way that would negatively impact the international economy. The incentive problem of moral hazard which is the actions of economic agents maximizing their own utility to the detriment of others when they do not bear the full consequences of their actions, is mitigated through conditions rather than providing collateral; countries in need of IMF loans do not generally possess internationally valuable collateral anyway. Conditionality also reassures the IMF that the funds lent to them will be used for the purposes defined by the Articles of Agreement and provides safeguards that country will be able to rectify its macroeconomic and structural imbalances. In the judgment of the Fund, the adoption by the member of certain corrective measures or policies will allow it to repay the Fund, thereby ensuring that the same resources will be available to support other members.

Why did Nigeria opt for structural adjustment instead of IMF loan during regime?

3.7 Criticisms of IMF Conditionalities

In some quarters, the IMF has been criticized for being 'out of touch' with local economic conditions, cultures, and environments in the countries they are requiring policy reform. The Fund knows very little about what public spending on programs like public health and education actually me." especially in African countries; they have no feel for the impact that their proposed national budget will have on people. The economic advice the IMF gives might not always take into consideration the difference between what spending means on paper and how it is felt by citizens. It has been said that the IMF's role as a generalist institution specializing in macroeconomic issues needs reform. Conditionality has also been criticized because a country can pledge collateral of "acceptable assets" to obtain waivers on certain conditions. However, that assumes that all countries have the capability and choice to provide acceptable collateral.

One view is that conditionality undermines domestic political institutions. The recipient governments are sacrificing policy autonomy in exchange for funds, which can lead to public resentment of the local leadership for accepting and enforcing the IMF conditions. Political instability can result from more leadership turnover as political leaders are replaced in electoral backlashes. IMF conditions are often criticized for their bias against economic growth and reduce government services, thus increasing unemployment.

Another criticism is that IMF programs are only designed to address poor governance, excessive government spending, excessive government intervention in markets, and too much state ownership. This assumes that this narrow range of issues represents the only possible problems; everything is standardized and differing contexts are ignored A country may also be compelled to accept conditions it would not normally accept had they not been in a financial crisis in need of assistance.

It is claimed that conditionalities retard social retard social and hence inhabit the stated goals of the IMF, while Structural Adjustment Programs lead to an increase in poverty in recipient countries. The IMF sometimes advocates “austerity Programmers”, cutting public spending and taxes even when the economy is weak, to bring budgets closer to a balance, thus reducing budget deficits. Countries are often advised to lower their corporate tax rate. In Globalization and its Discontents, Joseph E. Stiglitz, former chief economist and senior Vice president at the World Bank, criticizes approach, the purpose of the fund is no longer valid, as it was designed to provide funds for countries to carry out Keynesian reflections, and that the IMF “was not participating in a conspiracy, but it was reflecting the interests and ideology of the western financial community. “ (Friedman 2002).

3.8 Qualifications for Membership

Any country may apply to be a part of the lMF. Post-IMF formation, in the early postwar period, rules for IMF membership were left relatively loose, Members needed to make periodic membership payments towards their quota, to refrain from currency restrictions unless granted IMF permission, to abide by the Code of Conduct in the IMF Articles of Agreement, and to provide national economic information. However, stricter rules were imposed on governments that applied to the IMF for funding. The countries that joined the IMF between 1945 and 1971 agreed to keep their exchange rates secured at rates that could be adjusted only to correct a fundamental disequilibrium in the balance of payments, and only with the IMF's agreement. Some members have a very difficult relationship with the IMF and even when they are still members they do not allow themselves to be monitored, Argentina for example refuses to participate in an Article IV Consultation with the IMF.

In terms of benefit, member countries of the IMF have access to information on the economic policies of all member countries, the opportunity to influence other members' economic policies, technical assistance in banking, fiscal affairs, and exchange matters, financial support in times of payment difficulties, and increased opportunities for trade and investment.

3.9 Leadership of IMF

IMF organs consist of Board of Directors, Executive Board and the Managing director.

3.9.1 Board of Governors

The Board of Governors consists of one governor and one alternate governor for each member country. Each member country appoints its two governors. The Board normally meets once a year and is responsible for electing or appointing executive directors to the

Executive Board. While the Board of Governors is officially responsible for approving quota increases, Special drawing right allocations, the admittance of new members, compulsory withdrawal of members, and amendments to the Articles of Agreement and By-Laws, in practice it has delegated most of its powers to the IMF's Executive Board. The Board of Governors is advised by the International Monetary and Financial Committee and the Development Committee. The International Monetary and Financial Committee have 24 members and monitors developments in global liquidity and the transfer of resources to developing countries. The Development Committee has 25 members and advises on critical development issues and on financial resources required to promote economic development in developing countries, They also advise on trade and global environmental issues.

3.9.2 Executive Directors

24 Executive Directors make up Executive Board. The Executive Directors represent all 188 member-countries. Countries with large economies have their own Executive Director, but most countries are grouped in constituencies representing four or more countries. Following the 2008 Amendment on Voice and Participation, eight countries each appoint an Executive Director: the United States, Japan, Germany, France, the United Kingdom, China, the Russian Federation, and Saudi Arabia. The remaining 16 Directors represent constituencies consisting of 4 to 22 countries. The Executive Director representing the largest constituency of 22 countries accounts for 1.55% of the vote.

3.9.3 Managing Director

The IMF is led by a managing director, who is head of the staff and serves as Chairman of the Executive Board. The managing director is assisted by a First Deputy managing director and three other Deputy Managing Directors. Historically the IMF's managing director has been European and the president of the World Bank has been from the United States. However, this standard is increasingly being questioned and competition for these two posts may soon open up to include other qualified candidates from any part of the world. In 2011 the world's largest developing countries, the BRIC nations, issued a Statement declaring that the tradition of appointing a European as managing director undermined the legitimacy of the IMF and called for the appointment to be merit-based. The head of the IMF's European department is António Borges of Portugal, former deputy governor of the Bank of Portugal. He was elected in October 2010.

3.9 Voting Power

You should note that voting power in the IMF is based on a quota system. Each member has a number of "basic votes" (each member's number of basic votes equals 5.502% of the total votes), plus one additional vote for each Special Drawing Right (SDR) of 100,000 of a member country's quota. The Special Drawing Right is the unit of account of the IMF and represents a claim to currency. It is based on a basket of key international currencies. The basic votes generate a slight bias in favor of small countries, but the additional votes determined by SDR outweigh this bias.

3.9.1 Effects of the quota system

The IMF's quota system was created to raise funds for loans. Each IMF member country is assigned a quota, or contribution, that reflects the country's relative size in the global economy. Each member's quota also determines its relative voting power. Thus, financial contributions from member governments are linked to voting power in the organization. This system follows the logic of a shareholder controlled organization: wealthy countries have more say in the making and revision of rules. Since decision making at the IMF reflects each member's relative economic position in the world, wealthier countries that provide more money to the fund have more influence in the IMF than poorer members that contribute less; nonetheless, the IMF focuses on redistribution.

4.0 CONCLUSION

The IMF is only one of many international organizations and it is a generalist institution for macroeconomic issues only; its core areas of concern in developing countries are very narrow. One proposed reform is a movement towards close partnership with other specialist agencies to better productivity. The IMF has little to no communication with other international organizations such as UN specialist agencies like UNICEF, the Food and Agriculture Organization (FAO), and the United Nations Development Program (UNDP).

International institutions like the International Monetary Fund (IMF) and the World Bank have the brightest economists and the lead in advising poor countries on how to break out of poverty, but the problem is development economics. Development economics needs the reform, not the IMF. It should also be noted that IMF loan conditions need to be partnered with other reforms such as trade reform in developed nations, debt cancellation, and increased financial assistance for investments in basic infrastructure to be effective. IMF loan conditions cannot stand alone and produce change; they need to be partnered with other reforms or other conditions as applicable.

5.0 SUMMARY

In this unit, you learnt the meaning of international monetary fund (IMF), its functions and its surveillance of the global economy. You also studied the structural adjustment, the benefits of IMF loan conditions, a critique of IMF conditionalities and the qualifications for IMF membership. Other sub-topics covered by you in this unit were the leadership of IMF, its Board of Governors, and the voting power of IMF members and effects of the quota system;

With the discussion of IMF in this unit, the study of the African Development Bank will be the focus of the next unit.

6.0 TUTOR MARKED ASSIGNMENT

1. Why does IMF provides policy advice and financing to members in economic difficulties and also works with developing nations to help them achieve macroeconomic stability and reduce poverty?
2. IMF conditions are often criticized for their bias against economic growth and reduce government services. Discuss.

7.0 REFERENCES AND FURTHER READING

Chorev, N. & Babb, S. (2009).The crisis of neoliberalism and the future of international institutions: a comparison of the IMF and the WTO". Springer Science and Business Media.

Escobar, A. (1980).Power and visibility: Development and the invention and management of the third world. *Cultural Anthropology* 3 (4), 428-443.

Friedman, B. M. (15 August 2002). "Globalization: Stiglitz's Case". Nybooks.com. Retrieved 30 May 2010.

IMF (2012). About the IMF". International Monetary Fund Home Page. Retrieved on 14 October 2012 from https://www.imf.org/external/about.htm.

lsard, P. (2005). Globalization and the International Financial System: What's Wrong and What Can be Done. New York: Cambridge University Press

Jensen, N. (April 2004). "Crisis, Conditions, and Capital: The Effect of the IMF on Foreign Direct Foreign Investment". Journal of Conflict Resolution 48 (48): 194.

Osaze, E.B. (2007). *Capital markets,* Lagos : The Bookhouse Company

Stiglitz, J. (2002). Globalization and its Discontents. New York: WW Norton & Company.

UNIT 3 THE AFRICAN DEVELOPMENT BANK (ADB)

CONTENT

1.0 INTRODUCTION

In the preceding unit, we learnt the meaning of international monetary fund (IMF), its functions and its surveillance of the global economy. We also studied the structural adjustment, the benefits of IMF loan conditions, a critique of IMF conditionalities and the qualifications for IMF membership. Other sub-topics covered by us were the leadership of IMF, its Board of Governors, and the voting power of IMF members and effects of the quota system;

In the present Unit, we shall discuss the African Development Bank. This discussion will lead to tracing its history, describing the group entities, explaining the African Development Fund and Nigeria Trust Fund and analyzing the management and control of the ADB.

2.0 OBJECTIVES

At the end of this unit, you should be able to:

- Discuss the African Development Bank Group (ADB);
- Trace the history of the African Development Bank (ADB);
- Describe the group entities of the African Development Bank Group (ADB);
- Explain the African Development Fund;
- Explain the Nigeria Trust Fund;

- Analyze management and control of the African Development Bank (ADB);
- Analyze functions of the African Development Bank (ADB);
- Examine the status of the African Development Bank (ADB);
- Trace the recent trends and directions of the African Development Bank (ADB);
- Discuss the ADB's support of RMCs through the fight against HIV/ AIDS and
- List the membership of ADB.

3.0 MAIN CONTENT

3.1 The African Development Bank (ADB)

The African Development Bank (ADB) Group is a regional multilateral development finance institution established to contribute to the economic development and social progress of African countries that are the institution's Regional Member Countries (RMCs). The ADB was founded following an agreement signed by member states on August 14, 1963, in Khartoum, Sudan, which became effective on September 10, 1964. The ADB comprises three entities: the African Development Bank (ADB), the African Development Fund (ADF) and the Nigeria Trust Fund (NTF).

As the premier development finance institution on the continent, the ADB's mission is to help reduce poverty, improve living conditions for Africans and mobilize resources for the continent's economic and social development. The ADB headquarters is officially in Abidjan, Côte d'Ivoire. However, due to recent events in Côte d'Ivoire, the institution's activities have temporarily been relocated to Tunis, Tunisia (AfDB, 2014).

3.2 History of the African Development Bank (ADB)

At the end of the colonial period in Africa, growing desire for more unity within the continent led to the establishment of two draft charters, one for the establishment of the Organization of African Unity (OAU) established in 1963, later replaced by the African Union, and for a regional development bank. A draft agreement was submitted to top African officials, then to African Ministers, before being cosigned by twenty-three African governments on August 4, 1963, in the form of an agreement establishing the African Development Bank. The agreement came into force on 10 September 1964. Although established officially in under the auspices of the Economic Commission for Africa, the ADB began operation in 1966. Although originally only African countries were able to join the bank, since 1982 it has allowed the entry of non-African countries as well. During its forty years of operations, ADB has financed 2,885 operations, for a total of $47.5 billion. In 2003, it received an AAA rating from the major financial rating agencies and had a capital of $32.043 billion.

A development bank's mission is to promote the investment of public and private capital in projects and programmes that are likely to contribute to the economic development of its stakeholders. The bank therefore finances projects run either by the government or the private sector. The ADB is one of the five major multilateral development banks in the world that provides assistance to its regional member countries with a view to helping them achieve their development goals. The ADB's primary objective is to assist African countries – individually and collectively - in their efforts to achieve economic development and social progress. To this end, the institution's main challenge is to reduce poverty on the continent.

Combating poverty is at the heart of the continent's efforts to attain sustainable economic growth. The Bank therefore seeks to stimulate and mobilize internal and external resources to promote investments as well as provide RMCs with technical and practical assistance. In partnership with various international and development organizations, including the United Nations, the World Bank, and the International Monetary Fund, the ADB has, since 2000, undertaken to support RMCs in their efforts to attain the Millennium Development Goals (MDGs).

3.3 Group entities the African Development Bank Group (ADB)

The African Development Bank Group has two other entities: the African Development Fund (ADF) and the Nigeria Trust Fund (NTF).

3.3.1 The African Development Fund

Established in 1972, the African Development Fund started operations in 1974. It provides development finance on concessional terms to low-income RMCs which are unable to borrow on the non-concessional terms of the ADB. In harmony with its lending strategy, Povery reduction is the main aim of ADF activities. Twenty-four non-African countries along with the ADB constitute its current membership. The largest ADF shareholder is the United States with approximately 6.5 percent of the total voting shares, followed by Japan with approximately 5.4 percent. The Federal Reserve Bank of New york was designated as the depositor bank for the fund according to telegraphs sent from the U.S. Embassy in Abidjan in 1976.

The ADF's general operations are decided by a Board of Directors, six of which are appointed by the non-African member states and six designated by the AfDB from among the bank's regional Executive Directors. The ADF's sources are mainly contributions and periodic replacements by non-African member states. The fund is usually replenished every three years, unless member states decide otherwise. The total donations, at the end of 1996, amounted to $12.58 billion. The ADF lends at no interest rate, with an annual service charge of 0.75%, a commitment fee of 0.5%, and a 50-year repayment period including a 10-yeargrace period. The tenth United Kingdom replenishment of the ADF was in 2006.

3.3.2 The Nigeria Trust Fund (NTF)

The Nigeria Trust Fund (NTF) was established in 1976 by the Nigerian Government with an initial capital of $80 million. The NTF is aimed at assisting in the development efforts of the poorest ADB members. The NTF uses its resources to provide financing for projects of national or regional importance which further the economic and social development of the low-income RMCs whose economic and social conditions require financing on non-conventional terms. In 1996, the NTF had a total resource base of $432 million. It lends at a 4% interest rate with a 25-year repayment period, including a five-year grace period.

3.4 Management and Control of the African Development Bank (ADB)

The ADB is controlled by a Board of Executive Directors, made up of representatives of its member countries. The voting power on the Board is split according to the size of each member's share, currently 60%-40% between African (or "regional") countries and “non-regional” member countries (“donors”). The largest African Development Bank shareholder is Nigeria with nearly 9 percent of the vote. All member countries of the ADB are represented on the ADB Board of Executive Directors.

Member governments are officially represented at the ADB by their Minister of Finance, Planning or Cooperation who sits on the ADB Board of Governors. The ADB Governors meet once a year (at the Annual Meetings of the ADB each May) to take major decisions about the institution’s leadership, strategic directions and governing bodies. The Governors typically appoint a representative from their country to serve in the offices of the ADB’s Board of Executive Directors.

Day-to-day decisions about which loans and grants should be approved and what policies should guide the ADB’s work are taken by the Board of Executive Directors. Each member country is represented on the Board, but their voting power and influence differs depending on the amount of money they contribute to the ADB.

3.5 Functions of the African Development Bank (ADB)

The primary function of ADB is making loans and equity investments for the socio-economic advancement of the RMC. Second, the bank provides technical assistance for development projects and programs. Third, it promotes investment of public and private capital for development. Fourth, the bank assists in organizing the development policies of RMCs. The ADB is also required to give special attention to national and multinational projects which are needed to promote regional integration.

3.6 Status of the African Development Bank (ADB)

The ADB promotes economic development and social progress of its RMCs in Africa and the bank commits approximately 3 billion dollars annually to African countries. Its relatively small lending and tendency to follow in the footsteps of more prominent public institutions like the world bank implies that the African Development Bank has been receiving little interest from civil society organizations as well as academia. ADB emphasizes the role of women along with education reforms, and lent its support to key initiatives such as debt alleviation for Heavily Indebted poor Countries and the New partnership for African’s Development (NEPAD).

The Bank is currently based in Tunis, Tunisia after relocating from its headquarters in Abidjan, Cote d' lvoire because of instability there. It employs approximately 1,020 employees as of 2007, and has 78 members: 53 countries in Africa and 25 American, European, and Asian countries.

3.7 Recent Trends and Directions of the African Development Bank (ADB)

One of emerging views, repeatedly cited by the ADB's Board of Directors and management, is that the ADB should be more "selective" and "country-focused" in its operations. Though this policy has still to be clearly defined, it appears to be driving certain lending priorities.

The infrastructure sector, including Power supply, water and sanitation, transport and communications has traditionally received the largest share of ADB lending. This focus was re-affirmed in the ADB's 2003-2007 Strategic Plan, which identified infrastructure as a priority area for ADB lending. In 2005, the ADB approved 23 infrastructure projects for approximately $982 million, which totaled 40 percent of ADB approvals that year. Given the increased attention to infrastructure development in Africa from donors and borrowers, it is likely that ADB's infrastructure lending will increase significantly in the coming years. In 2007, infrastructure operations accounted for approximately 60 percent of the bank's portfolio.

Regional integration infrastructure projects will also be a key part of the ADB's future business. According to the ADB's 2005 Annual Report, regional economic blocs will make Africa "more competitive in the global market", while transport and power interconnections between smaller African economies will help create larger markets within the continent. The ADB's member countries claim that ADB, as a multilateral institution, is particularly suited to support regional integration projects.

The ADB has also been designated the lead agency to facilitate "NEPAD infrastructure initiatives", which are regional integration projects led by African Regional Economic Communities (RECs). Additionally, the ADB hosts the Infrastructure Consortium for Africa (ICA). The ICA was established by G8 countries to coordinate and encourage infrastructure development in Africa, focusing on regional infrastructure development in particular. The ADB also helps to prepare projects so they may obtain financing from others sources through an initiative called the Infrastructure Project Preparation Facility (IPPF). So even if the ADB is not directly involved in financing a particular infrastructure project, it may have helped to make that project possible.

3.7.1 The ADB's Support of RMCs through the Fight against HIV/AIDS.

Another key area of concentration of the ADB's support of RMCs is the fight against HIV/AIDS. The ADB has five policies towards securing Africa's future through health funding:

- Institutional capacity building through assistance of policy/strategy formulation and implementation

- Human capital development to create an environment for the operation of national AIDS strategies through training and technical assistance support
- HIV/AIDS multi-sectoral responses with emphasis on prevention and control interventions that include IEC (Information, Education and Communication), STI,(sexually Transmitted Infection) VCT (Voluntary Counseling and Testing), infrastructure support for the establishment of laboratories and blood transfusion facilities, and provision of equipment and supplies, including antiretroviral drugs
- Advocacy through participation in international and regional forums to raise political commitment and leadership towards a collaborative effort in the fight against the pandemic among RMCs and development partners
- Partnership development with a view of forging new alliances and revitalizing existing collaboration to cover critical development concerns such as HIV/AIDS and to bringing partnership activities within the framework of the bank's vision.

To date, the bank's contribution in the fight against HIV/AIDS is estimated at over 500 million Dollar. The bank is also among the initiating partners of AIDS in Africa – Scenarios for the future, a project whose outcome will enable governments and development partners alike to make strategic choices of current and future development paths and define their activities accordingly in order to face the challenges posed by HIV/AIDS.

Energy projects are likely to become a more important area of the AFDB's infrastructure work, given the lack of access to energy services across Africa and continued high oil prices affecting oil-importing countries. It is not clear if the ADB's role in the energy sector will prioritize energy projects for domestic consumption or for export, although the ADB has supported both in the past. The ADB is currently drafting an energy policy and developing its contribution to the G8-mandated Clean Energy Investment Framework.
Although there is no official statement or consensus to this effect, ADB lending for agriculture, (non-infrastructure) rural development and social sectors, such as health and education, is reportedly likely to decrease over the coming years.

4.0 CONCLUSION

The ADB's financial standing has been restored from the near collapse of 1995, but its operational credibility remains a work-in-progress. ADB is still a relatively small source of development finance for Africa. The ADB management and shareholders should address the urgent task of reforming Africa's development bank to enable it deliver on its mandate especially a strong focus on infrastructure.

5.0 SUMMARY

In this unit**,** you learnt the African Development Bank Group (ADB), its history, entities, functions, management and control, status, and membership. You also learnt the recent trends and directions of the African Development Bank (ADB) and its support of Regional Member Countries (RMCs) through the fight against HIV/AIDS

In the next unit, we shall discuss the International Bank for Reconstruction and Development otherwise called the World Bank.

6.0 TUTOR MARKED ASSIGNMENT

1. Trace the history of the African Development Bank (ADB)
2. State the functions of the African Development Bank (ADB)

7.0 REFERENCES AND FURTHER READING

AfDB (2014). about-us/frequently-asked-questions. African Development Bank (ADB) Home Page. Retrieved on 05/03/2017 from http://www.afdb.org/en/about-us/frequently-asked-questions/

Osaze, E.B. (2007). *Capital markets,* Lagos : The Bookhouse Company

Wathne, C. & Hedger, E. (2010). What does an effective multilateral donor look like? London: Overseas Development Institute

UNIT 4 THE INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT (IBRD) OR THE WORLD BANK

CONTENT

1.0 INTRODUCTION

In the preceding unit**,** we learnt the African Development Bank Group (AfDB), its history, entities, functions, management and control, status, and membership. You also learnt the recent trends and directions of the African Development Bank (AFDB) and its support of Regional Member Countries (RMCs) through the fight against HIV/AIDS.

In the present unit, we shall discuss the International Bank for Reconstruction and Development otherwise called the World Bank. You should note that the World Bank is different from the World Bank Group which we shall discuss in the last unit of this course, that is, Unit 5.

2.0 OBJECTIVES

At the end of this unit, you should be able to

- Discuss the formation of the World Bank or the IBRD;
- Analyze the functions of the World Bank;
- State the purposes of the World Bank;
- Describe the resources of the World Bank;
- Describe the lending procedure of the World Bank;
- Give a general provisions regarding. World Bank loans and guarantees;
- Describe the World Bank structural adjustment loans; and
- Undertake a critique against the World Bank policies.

3.0 MAIN CONTENT

3.1 The Formation of the World Bank or the IBRD

Like the International Monetary fund (IMF), the International Bank for Reconstruction and Development (IBRD) or simply the World Bank was also formed at the United Nations Monetary and Financial Conference held at Bretton Woods, New Hampshire, U.S.A. 1-22 July 1944. The Bank was meant to take care of the long-term economic problems of member-nations. Such aims for its creations are:- to help the war-torn nations in the reconstruction of their economies, and to help the vast underdeveloped world in accelerating the pace of economic growth. By 1988, the Bank's membership stood at 151 countries. Its headquarters is in Washington D.C. and maintains 40 offices throughout the world.

The five institutions of the World Bank are the International Bank for Reconstruction and Development (IBRD), International Development Association (IDA), International Finance Corporation (IFC), Multilateral Guarantee Agency (MIGA), and International Centre for the Settlement of Investment Disputes (ICSID). The World Bank's projects and operations are designed to support low-income and middle-income countries' poverty reduction strategies. The Bank provides low-interest loans, interest-free credits and grants to developing countries for a wide array of purposes that include investments in disaster recovery and risk mitigation, education, health, infrastructure, financial and private sector development, and environmental and natural resource management. Although the World Bank has traditionally played a key role in post-disaster recovery and reconstruction, it has been increasing its involvement in longer term disaster risk reduction. The overarching objective is to mainstream disaster risk reduction and climate change adaptation in country development strategies.

The World Bank supports country development strategies, such as Poverty Reduction Strategies (PRSP), Country Assistance Strategies (CAS), United Nations Development Assistance Frameworks (UNDAFs), and National Adaptation Programmes of Action (NAPAs), to reduce vulnerabilities to natural hazards. This is done through providing analytical, technical and operational support to countries for disaster risk reduction.

3.2 The Functions of the World Bank

The functions of the World Bank are:

(a Reconstruction of the war-devastated economies and development of economically backward countries through investment and capital accumulation and through use of productive capacity for production of civilian goods and services.

(b) To achieve the above objective through promotion of foreign private investment by means of guarantees or participation in loans and other investments made by private investors; and in case of non-availability of private capital at reasonable terms, to supplement private investment by providing, on suitable conditions, finance for productive purposes out of its own resources.

(c) To promote long-term balanced growth of international trade and maintenance of equilibrium in balance of payments by encouraging international investment for the development of productive resources of the members, thereby assisting in raising the standard of living.

(d) To assist in bringing about a smooth transition from a war-time to a peace-time economy.

(e) To encourage that the more useful and urgent projects are dealt with first.

(f) To underwrite loans to developing nations.

(g) Renders technical assistance to LDCs.

(h) To comment on the financial buoyancy and credit-worthiness of a borrowing nations through its expertise and understanding of financial matters. It issues certificates of credit-worthiness and these are acceptable and respectable the world-over.

(i) It can also borrow money from member nations (advanced, rich nations) to finance its own loans.

3.3 The Purposes of the World Bank

It is important to note that the Bank has certain regional offices to serve the following purposes:

(a) To help the Bank in maintaining and improving the effectiveness of its development assistance.

(b) To bring the ‘sectors experts’ and ‘country experts’ closer to each other thus helping the Bank in better understanding of the needs, opportunities and problems of the member countries.

(c) To permit an optimum utilization of the Bank staff in preparing, appraising and implementing projects. Its loans are medium- and long-term in nature.

3.4 Resources of the World Bank

The World Bank has three main sources of funds viz:

(a) Its own capital (i.e authorized capital):- This is made up of subscribed capital, paid-in capital, and amounts subject to call. Thus, it is divided into three parts:

(b) 2 per cent of the subscribed capital is payable by the subscriber in the form of U.S. dollars or gold and is available to the Bank for lending other uses.

(c) 18 per cent of subscription is payable in member's own currency and is available to the Bank for lending with the consent of the member whose currency is involved.

(d) The remainder (80 per cent) is not payable for lending, rather it can be called only for meeting the obligations of the Bank arising out of its borrowing or guaranteeing of loans.

(e) Retained Earnings:- A proportion of the Bank's retained earnings (net) is transferred in the form of grants to one of its affiliates, IDA, and the balance transferred to the General and Special Resources.

(f) Borrowings:- This forms the largest sources of the Bank's funds for lending and the major sources of borrowing are the international capital markets of the capital-rich members (through the issue of AAA rating bonds)

3.5 Lending Procedure of the World Bank

Loans rather than grants are given to needy member-nations at rates close to the market interest rates. Such loans come in the following forms:

(1) The IBRD may give loans out of its own paid-in capital and retained earnings.

(2) The Bank can guarantee in whole or in part loans made by private investors through the usual investment channels. Such guarantees attract a guarantee commission to the Bank.

(3) The Bank may borrow from the capital markets of the world on the strength of its own credit-worthiness and in turn give loans to its borrowers. In this way, it acts as a bridge between the capital-surplus and capital-deficit areas of the world.

3.6 General Provisions Regarding. Loans and Guarantees

The Bank can make loans or can guarantee them subject to the following conditions:

(a) With the exception of loans given to the IFC, every loan must be made to or guaranteed by the member-government (or other competent authority) on its behalf acceptable to the World Bank, in whose territory the project to be financed is located.

(b) The World Bank ensures that the borrower and the guarantor have the paying capacity.

(c) It lends only for productive purposes and in non-military projects.

(d) It must ensure that the project to be financed will be able to provide a return commensurate with the amount of investment, i.e, its return must be enough to service its debt obligations and show a surplus thereafter.

(e) Except in special circumstances, the World Bank loans are for specific projects.

(f) A loan made for a project cannot be diverted to any other use.

(g) Only economic considerations inform the Bank's decision to give loans.

(h) The World Bank satisfies itself that in the prevailing market conditions the borrower would be unable otherwise to obtain loans under conditions which in the opinion of the Bank are reasonable for the borrower.

(i) There must be a written report, prepared by a competent committee after careful study of the merits of the proposal, recommending the project.

(j) The World Bank normally gives a loan only to cover the foreign exchange component of the project, though in special circumstances a part of the local cost may also be financed by the Bank's loan.

(k) The World Bank deals only with member governments, their Central Banks or some other competent agency.

(l) The loan must be spent in the economies of member-nations.

(m) A project slated for financing must be able to contribute to the economic development of the borrowing member- nation.

(n) The Bank has the right to determine the loan amount and conditions though it has to satisfy itself that the interest rate and other charges are reasonable and appropriate to the project.

(o) The loan amount or guarantee is not limited by the member's subscribed capital.

(p) Amortization and interest must be paid in currencies in which the loan was made.

3.7 The World Bank Structural Adjustment Loans

The World Bank began a policy of structural adjustment lending in 1979-80 in response to the markedly deteriorating prospects that were then foreseen for developing nations in the 1980s. Such structural adjustment lending was designed within the staff and financing levels available to the Bank and within its mandate, to those governments that had requested such support and that had recognized the need to formulate and introduce, as a matter of urgency, a set of comprehensive measures designed to adjust the structure of productive activities of their economies to the markedly deteriorating external situation (World Bank, 1982). The objective here is to provide quick disbursing finance to support measures, specifically designed to strengthen country balance of payments within 5-10 years without restricting imports in a manner that would adversely affect its economic and social development. Such loans which are generally medium-term in nature are in the Bank’s view directed to achieve the following:

(a) To support a programme to specific policy changes and and institutional reforms so that the productive resources of the economy can be put to a better use in the sense of improving the balance of payments in medium and long-run, and to simultaneously help in the maintenance of economic growth.

(b) To act as a catalyst for the inflow of other external capital to ease the balance of payments situation.

To extend such loans, the Bank insists on a high degree of conditionality, imposed upon LDCs only, leading to their bearing the cost resource-reallocation and consequent hardships.

Such conditionality imposed includes:

(a) A set of pricing policies including tariff reforms, fiscal incentives, budget subsidies, and interest rate charges;

(b) Revised public investment priorities;

(c) Improved budget and debt management and

(d) A policy for strengthening institutions particularly public enterprises.

Nigeria has benefited from this scheme in her SAP which began in July 1986. The World Bank has long been criticized by non-governmental organizations, such as the indigenous rights group survival international, and academics, including its former Chief Economist Joseph Stiglitz, Henry Hazlitt and Ludwig Von Mises (Stigliz, 2003, 2007). Henry Hazlitt argued that the World Bank along with the monetary system it was designed within, would promote world inflation and “a world in which international trade is state dominated” when they were being advocated (Hazlitt, 1984). Stiglitz argued that the so called free market reform policies which the Bank advocates are often harmful to economic development if implemented badly, too quickly (“shock therapy”), in the wrong sequence or in weak, uncompetitive economies (Stiglitz, 2003; Schneider, 2002).

One of the strongest criticisms of the World Bank has been the way in which it is governed. While the World Bank represents 188 countries, it is run by a small number of economically powerful countries. These countries (which also provide most of the institution's funding) choose the leadership and senior management of the World Bank, and so their interests dominate the bank. Titus Alexander argues that the unequal voting power of western countries and the World Bank's role in developing countries makes it similar to the South African Development Bank under apartheid, and therefore a pillar of global apartheid (Alexander, 1996). In the 1990s, the World Bank and the IMF forged the Washington Consensus, policies which included deregulation and liberalization of markets, privatization and the downscaling of government. Though the Washington Consensus was conceived as a policy that would best promote development, it was criticized for ignoring equity, employment and how reforms like privatization were carried out. Joseph Stiglitz argued that the Washington Consensus placed too much emphasis on the growth of GDP, and not enough on the permanence of growth or on whether growth contributed to better living standards (Stiglitz, 2007).

The United States Senate Committee on Foreign Relations report criticized the World Bank and other international financial institutions for focusing too much "on issuing loans rather than on achieving concrete development results within a finite period of time" and called on the institution to "strengthen anti-corruption efforts".

Criticism of the World Bank often takes the form of protesting as seen in recent events such as the World Bank Oslo 2002 Protests, the October Rebellion, and the Battle of Seattle. Such demonstrations have occurred all over the world, even amongst the Brazilian Kayapo people. Another source of criticism has been the tradition of having an American head the bank, implemented because the United States provides the majority of World Bank funding. "When economists from the World Bank visit poor countries to dispense cash and advice," observed The Economist in 2012, "they routinely tell governments to reject cronyism and fill each important job with the best candidate available. It is good advice. The World Bank should take it." (The Economist, Mar 31st 2012). You should note that Jim Yong Kim was the most recently appointed president of the World Bank.

4.0 CONCLUSION

The World Bank is a United Nations international financial institution that provides the loans to developing countries for capital programs. The World Bank's official goal is the reduction of poverty. According to its Articles to its Articles of Agreement, all its decisions must be guided by a commitment to the promotion of foreign investment and international trade and to the facilitation of capital investment. The World Bank is the world's premier development institution. For almost 70 years, the leader of the IMF and World Bank has been subject to an indefensible carve-up. The head of the IMF is European; the World Bank, American. This shabby tradition has persisted because it has not been worth picking a fight over. It is long overdue for the headship of the World Bank and the IMF is opened to candidates from the rest of the world.

5.0 SUMMARY

In this unit, you learnt how the World Bank or the IBRD was formed as well as its functions, purposes, resources and lending procedure. You also learnt the general provisions regarding the World Bank loans and guarantees, the Bank's structural adjustment loans and a critique of its operation.

By this development, we have come to the end of the course. Please endeavour to read your materials, study extensively by referring to other reference materials. Attempt your tutor marked assignments and submit them to your tutor ensuring to take note of the comments for your guide.

We wish you a very successful examination.

6.0 TUTOR-MARKED ASSIGNMENT

1. Analyze the functions of the World Bank.
2. Undertake a critique of the policies of IBRD

7.0 REFERENCES/FURTHER READINGS

Alexander, T. (1996). Unravelling Global Apartheid. An Overview of World Politics. Cambridge, UK: Polity

Hazlitt, H. (1984). From Bretton Woods to World Inflation: A Study of the Causes and Consequences. Washington, D.C.: Regnery Publishing.

Schneider, J. (2002). "World Markets: Anthropological Perspectives". In MacClancy, Jeremy. Exotic No More: Anthropology on the Front Lines. Chicago, IL: University of Chicago Press.

Stiglitz, J. E. (2003). The Roaring Nineties: A New History of the World's Most Prosperous Decade, New York, NY: W. W. Norton & Company.

Stiglitz J.E. (2003). Globalization and Its Discontents. New York, NY: W. W. Norton & Company.

Stiglitz, J. E. (2007). Making Globalization Work. New York, NY: W. W. Norton

The Economist, (Mar 31st 2012). Hats off to Ngozi. The Economist 2012-03-31. Retrieved on 2012-04-02 from http://www.economist.com/node/21551490