Mallam Sanusi Lamido Sanusi: Developments in the banking system in Nigeria

Address by Mr Mallam Sanusi Lamido Sanusi, Governor of the Central Bank of Nigeria, Lagos, 14 August 2009.

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Distinguished Ladies and Gentlemen of the Press,

As we are all aware, the world economy has been hit by the repercussion of the financial meltdown that started with the sub-prime mortgage crisis in the United States of America and spread to Europe and other parts of the world. This crisis has led to the collapse of many banks and other financial institutions, and even rendered an entire nation bankrupt.

In Nigeria, the banking system appears to have weathered the storm due to a number of factors. Among these are the facts that our financial system is not strongly integrated into the international financial system, as well as the relatively simple nature of financial products and strong capitalization and liquidity of Nigerian banks.

However, there are many who have been aware for a while now that whereas the system in general is likely to absorb and survive the effects of crisis, the effects vary from bank to bank. A few Nigerian banks, mainly due to huge concentrations in their exposure to certain sectors (capital market and oil and gas being the prominent ones), but due to a general weakness in risk management and corporate governance, have continued to display signs of failure.

As far as October last year, some of the banks showed serious liquidity strain and had to be given financial support by the Central Bank in the form of an "Expanded Discount Window" (EDW) where the CBN extended credit facilities to these banks on the basis of collateral in the form of Commercial Paper and Bankers' acceptances, sometimes of doubtful value.

As at June 4, 2009 when I assumed office as Governor of the CBN, the total amount outstanding at the Expanded Discount Window was N256.571 billion most of which was owed by the 5 banks.

A review of the activity in the EDW showed that four banks had been almost permanently locked in as borrowers and were clearly unable to repay their obligations. A fifth bank had been a very frequent borrower when its profile ordinarily should have placed it among the net placers of funds in the market. Whereas the five banks were by no means the only ones to have benefited from the EDW, the persistence and frequency of their demand pointed to a deeper problem and the CBN identified them as probable source of financial instability, most likely suffering from deeper problems due to non-performing loans.

The impact of the situation of these banks was being felt by the market in different negative ways. Because of this strain in their balance sheets, the banks pushed up the interest rate paid to private sector deposits and their competitors had to follow suit. They also contributed to the destabilization of the inter-bank market as many of their competitors were unwilling to take an unsecured risk on them. If was primarily because of these banks, or at least some of them, that the CBN took the step of guaranteeing the inter-bank market when it stopped granting new lines under the EDW. Without that guarantee, almost four banks would not have been able to borrow in the inter-bank and would probably have collapsed.

As you are aware, we guaranteed the inter-bank market to give us the time to conduct a thorough diagnostic of the banks and ensure that appropriate remedial action is taken. At least four of the banks in question have since the guarantee came into force either remained heavy users of funds at the EDW or drawn heavily from other banks under cover of the CBN guarantee to wind-down at this window. In all events, it is clear that they do not have the ability to meet their obligations to depositors and creditors as they are in a grave situation.

In view of the aforementioned circumstances, I instructed the Director of Banking Supervision of the CBN to carry out a Special Examination of the following five banks:

1. Afribank Plc
2. Finbank Plc
3. Intercontinental Bank Plc
4. Oceanic Bank Plc and
5. Union Bank Plc.

The examination was conducted by a joint team of CBN and NDIC officials. The major findings on the 5 banks included:

1. Excessively high level of non-performing loans in the five banks which was attributable to poor corporate governance practices, lax credit administration processes and the absence or non-adherence to the bank's credit risk management practices. Thus the percentage of non-performing loans to total loans ranged from 19% to 48%. The 5 banks will therefore need to make additional provision of N539.09 billion.
2. The total loan portfolio of these five banks was N2,801.92 billion. Margin loans amounted to N456.28 billion and exposure to oil and gas was N487.02 billion. Aggregate non-performing loans stood at N1,143 billion representing 40.81%.
3. From 1 and 2 above, it is evident that the five banks accounted for a disproportionate component of the total exposure to capital market and oil and gas, thus reflecting heavy concentration to high risk areas relative to other banks in the industry.
4. The huge provisioning requirements have led to significant capital impairment. Consequently, all the banks are undercapitalized for their current levels of operations and are required to increase their provisions for loan losses, which impacted negatively on their capital. Indeed one is technically insolvent with a Capital Adequacy Ratio of (1.01%). Thus, a minimum capital injection of N204,94 billion will be required in the 5 banks to meet the minimum capital adequacy ratio of 10%.
5. The five banks were either perennial net-takers of funds in the inter-bank market or enjoyed liquidity support from the CBN for long periods of time, a clear evidence of illiquidity. In other words, these banks were unable to meet their maturing obligations as they fall due without resorting to the CBN or the inter-bank market. As a matter of fact, the outstanding balance on the EDW of the five banks amounted to N127.85 billion by end July 2009, representing 89.81% of the total industry exposure to the CBN on its discount window while their net guaranteed inter-bank takings stood at N253.30 billion as at August 02, 2009. Their liquidity ratios ranged from 17.65% to 24% as at May 31, 2009. (Regulatory minimum is 25%).

It is important to note that at least three of the banks are systemically important (accounting for more than 5% of assets and deposits in the banking system) and together the five banks account for 39.93% of loans, 29.99% of deposits, and 31.47% of total assets as at May 31, 2009.

Given the extent of the asset quality problem leading to liquidity stresses, and the variety of stress points on the banks' balance sheets, failure to act to secure the financial health of these banks will clearly place the system at risk. The Central Bank has a responsibility to act to protect all depositors and creditors and ensure that no one loses money due to bank failure. The Bank also needs to move decisively to remove this principal cause of financial instability and restore confidence in the banking system.

Consequently, having reviewed all the reports of the examiners and the comments of the Directors and Deputy Governors, I am satisfied that these 5 institutions are in a grave situation and that their Management have acted in a manner detrimental to the interest of their depositors and creditors, Therefore, in exercise of my powers as contained in Sections 33 and 35 of the Banks and Other Financial Institutions Act 1991, as amended, and after securing the consent of the Board of Directors of the CBN, I hereby remove the Managing Directors and the Executive Directors of the following banks from office with effect from Friday, August 14, 2009.

1. Afribank Plc
2. Intercontinental Bank Plc
3. Union Bank of Nigeria Plc
4. Oceanic international Bank Plc
5. Finbank Plc

These persons forthwith cease to be directors and officers of their respective banks.

The Board of the Central Bank of Nigeria has also appointed the following as the MD/CEOs of the affected banks:

1. Mr. John Aboh – MD/CEO Oceanic International Bank Plc
2. Mr. Mahmud L. AlabI – MD/CEO Intercontinental Bank Plc
3. Mr. Nebolisa Arah – MD/CEO Afribank Plc
4. Mrs. Suzanne Iroche – MD/CEO Finbank Plc
5. Mrs. Funke Osibodu – MD/CEO Union Ban Plc

Each of the above will head a management team that will include Executive Directors and Chief Financial Officers to be appointed by the CBN. This team is tasked with continuing the businesses of the banks as a going concern. I therefore appeal to the Boards of the affected banks, in their own interest, to co-operate with the newly appointed Executive Management.

We are conscious of the fact that changing management alone will not resolve this problem. Consequently, the CBN is injecting a total of about N400 billion into these five banks with immediate effect in form of Tier 2 Capital to be repaid from proceeds of capitalization in the near future. This injection is sufficient to resolve and stabilize all the institutions and enable them continue normal business. The injection of fresh capital by the CBN is a temporary measure as government does not intend to hold the shares for long and shall divest its holdings as soon as new investors recapitalize these banks.

Let me also advise all debtors of Nigerian banks, that the CBN and all government agencies are united in our commitment to support the recovery efforts of the banks. Debtors who do not pay shall have their names published in national newspapers in due course and we will solicit the support of law enforcement agencies in recovery.

Let me reassure especially the customers of the affected banks and all the banks in general that there is no cause for alarm They should continue to transact their normal business in the banks where their accounts are domiciled as this exercise is meant to further strengthen the banking industry and recapitalize the affected banks.

I should also state at this point that the scope of the Special Examination was widened to cover all 24 banks. So far, we have concluded the audit of 10 banks including these five, the others being Diamond Bank, First Bank, United Bank for Africa, Guaranty Trust Bank and Sterling Bank. We have also commenced the next batch of 11 banks and hope to conclude them by end of August, All in all, we expect to conclude the audit in mid-September. The Central Bank is requiring all banks to make appropriate provisioning for non-performing loans and disclose them. We hope that by the end of this quarter, all banks would have cleaned up their balance sheets. On the basis of the information available to us so far, we are confident that the banking system is safe and sound and we have dealt with the major sources of systemic risk.

I will conclude by restating that, going forward, the CBN will not waiver in its desire to ensure that public confidence in the Nigerian banking system is maintained through appropriate disclosures and the reinvigoration of its policy of zero tolerance on all professional and unethical conducts.

We will not allow any bank to fail. However, we will also ensure that officers of banks and debtors who contribute to bank failures are brought to book to the full extent of the law and that all proceeds of infraction are confiscated where legally feasible.

Thank you.