Banking Sector Reforms and the Manufacturing Sector: The Manufacturers' Association of Nigeria Perspective

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I. Introduction: The Real Sector of the Economy

The Real Sector is the segment of the economy where high productive activities are carried out and comprise:

(i) Industry:
- Manufacturing
- Mining and Quarrying
- Electricity generation

(ii) Agriculture
(iii) Transport and Communication
(iv) Trade and Commerce
(v) Services
(vi) Building and Construction
(vii) Oil and Gas

However, the manufacturing sector is expected to dominate, shape and define the core path of industrialization all over the world. The sector is reputed to be an important engine of growth, an antidote for unemployment; a creator of wealth, and the threshold for sustainable development.

II. Historical Overview of Nigeria's Manufacturing Sector

II.1 Pre-Independence Era

Before independence in 1960, the Nigerian economy was characterized by:

- ➢ Agrarian activities both in production for domestic consumption and export.

- ➢ Near absence of industrial activities as industrialization was not part of the colonial economic agenda.

- ➢ Production of primary raw materials for foreign industries, and importation of manufactured goods.

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II.2 Post-Independence Economic Policies

Upon attainment of independence, the post-independence governments embraced the policy of transformation of the country into a modern industrial economy with emphasis on:

- High priority on rapid industrialization as Nigeria's development objectives in the First National Plan (1962-1968).

(i) Importation of finished products was discouraged to encourage locally manufactured products through import substitution strategy.

Unfortunately, our local industries are still heavily import-dependent in sourcing raw materials and capital goods. However, the emergence of the oil boom in the 1970's made huge foreign exchange available for further massive importation of industrial inputs. With the establishment of many industries, most industrial groups imported almost all of their raw materials and machinery/spare parts. The contribution of manufacturing to gross domestic product (GDP) rose significantly to about 9.5 per cent in 1975 from a paltry contribution of 3.2 per cent in 1960.

(ii) The Indigenization Policy (Decrees) of 1972 and 1977, as amended, were promulgated to address the obvious foreign domination of the Nigerian industrial landscape. However, the oil glut of the early 1980s spelt the doom for many of these high import-dependent industries. The then prevailing policies of import licensing as well as interest and exchange rates controls resulted in acute shortages of industrial inputs with adverse consequences on industrial production and capacity utilization. Many industries were closed down leading to massive retrenchments, with the resultant socio-security problems. Between 1982 and 1986, all macroeconomic indicators viz: oil revenues, naira exchange rate and foreign reserves posted negative trends in their movements. These led to the enthronement of a regime of rationing of foreign exchange among manufacturers and other users.

(iii) The Structural Adjustment Programme (SAP)
The SAP was adopted in 1986, as reform measures meant to:

- Reverse the downwards trends in the economy
- Widen our industrial base
- Promote stimuli for increased export

- Provide incentives for manufacturing to enhance its value-added and contributions to the GDP
- Provide greater employment opportunities
- Improve the technological skills and capacities available in the country
- Increase private sector participation in manufacturing through foreign direct investments (FDI) and local entrepreneurial activities

(iv) Trade liberalization as a major policy option of SAP was blindly applied by the government in order to make the sector competitive but without providing a conducive business environment with the following adverse consequences:

- ➢ High deterioration in the naira exchange rate leading to high costs of domestic production
- ➢ With high cost and scarcity of industrial raw materials, manufacturing capacity utilization and production fell drastically
- ➢ Manufacturing employment was not left out in the decline
- ➢ The small and medium enterprises that SAP was meant to encourage became victims of the reform agenda
- ➢ The much canvassed inflow of foreign investments that would accompany the SAP regime became a mirage
- ➢ The policy not only killed the manufacturing sector, but affected its contributions to the GDP. For instance, the sector's contribution to the GDP reduced from 9.5 per cent in 1975 to 6.65 per cent in 1995
- ➢ During the SAP period, the government completely divested itself of holdings of 67 companies and slated others for partial or full commercialization and for partial or full privatization depending how strategic they were considered to the economy

II.3 Post-Structural Adjustment Programme Era

Since the post-SAP period, the manufacturing sector has not experienced meaningful growth. The main feature of the Nigerian economic terrain is the steady de-industrialization as reflected in the high mortality rate of manufacturing outfits. The number of registered manufacturing firms with the Manufacturers'

Association of Nigeria (MAN) dropped from 4,850 in the early 1980s to 2,000 in 2010. Capacity utilization was 70.1 per cent in 1980 but declined rapidly to 29.3 per cent in 1995 before rising gradually (with fluctuating trends) to 52.8 per cent in 2005 and 48.0 per cent in 2009. The share of manufacturing in the aggregate GDP declined from 5.3 per cent in 1981 to 4.1 per cent in 1993, 3.4 per cent in 2005, and marginally increased to 4.1 per cent in 2009. Similarly, direct manufacturing employment declined over the years. A survey of about 300 manufacturing companies carried out by MAN showed that 2,752,832 people were engaged by the sector in 2001; 1,043,982 in 2005, and 1,026,305 in 2008. These trends are the consequential result of a number of problems confronting the sector, among which are:

- Near collapse of critical social and economic infrastructure
- High bank lending rates which are a great disincentive to new investment and mortal killer of existing ones particularly the SMEs
- Lack of long-term investible funds for manufacturing activities.
- Government policy inconsistency
- Deepening weak aggregate consumer demand
- Massive influx and dumping of all kinds of imported finished goods
- Multiplicity of taxes and levies
- Low government patronage of locally manufactured goods
- Insecurity of life and property, etc.

The problems highlighted above represent a significant deviation from the characteristics and requirements of a conducive business environment that the real sector needs to perform its role as the engine of growth and development.

II.4 Countries' Experiences on the Roles of Banks

A well-established and efficiently functioning banking system is the "brain" of the economy.

Banks offer institutional mechanism through which resources can be mobilized and directed from less essential uses to more productive investments. The role of banking institutions in the efficient allocation of available resources is for capital formation and accelerated growth. In America, Japan and Germany, the banking sector initiates and coordinates long-term industrial strategies by playing a more dynamic and active role in the industrialization and overall development of their economies – growth-inducing model. These countries have achieved a high level of economic development. South Korea, Malaysia, Taiwan and lately China, by adopting the growth-inducing model of banking are emerging as important world players in areas of industrialization. In these countries, the financial intermediaries act to stimulate entrepreneurial ability and encourage enterprises through extension of both financial and non-financial services to economic units as deemed necessary. The British banking system as well as those modelled on it adopted the passive or growth-induced model. This is a situation where banks look forward to the time when other non-financial problems in a country's development are removed and the investment atmosphere is now conducive for the financing of growth-inducing activities. The banks usually not only own large parts of industry, but also provide much of their financial advice, together with the share of their credit facilities.

III. Banking Sector Reforms: The Manufacturers' Association of Nigeria Perspective

III.1 Pre-Consolidation Experience

The Nigerian banking system, patterned after the British system, started off as a weak and passive financial system during the colonial era, directed mainly towards the needs of the expatriate administrators and merchants. The task of financing the development of the Nigerian economy was left to the post-independence era. Prior to the 1986 deregulated SAP regime, interest rates were fixed administratively by the CBN for socially optimum resource allocation, to promote orderly growth in the financial market and facilitate flow of credit to the preferred sectors like manufacturing, agriculture, and infrastructure. The motivating force was the compelling need to attract investments required to grow the economy, create employment opportunities, increase output and, generally, set the economy on the path of economic development.

The modest achievements recorded by the manufacturing sector in the 1970s and up to the early 1980s could partly be attributed to this generous monetary policy. The sector recorded 9.5 per cent contribution to GDP and over 70.0 per cent average capacity utilization in 1975. With the liberalization of interest rates in 1987, coupled with the abolition of the administrative sectoral allocation of bank credit, the field was now left to the market interplay of interest rate determination and credit allocation. The role of the CBN with regards to interest rates was confined to the fixing of the Minimum Rediscount Rate (MRR), now known as the Monetary Policy Rate (MPR). Experience has shown that since the post-SAP market reforms, lending rate has been on the upward trend.

Manufacturers and other real sector operators are of the view that the high lending rates in the country are not business-friendly and do not promote economic development. Lending rates at present vary between 15.0 per cent and 25.0 per cent (excluding other ancillary charges) and are too excessive for a developing economy like ours. This is contrary to what is obtainable in developed economies of the world where lending rates are single digit and even tilted towards zero per cent at the peak of the global financial crisis in those countries. Notwithstanding the fact that the Nigerian economy is currently experiencing high inflation rate to the tune of 13.8 per cent which in theory induces high lending rate because of the need to realign the real interest rate on deposits, the wide margin between deposit and lending rates appears uncomfortable and unacceptable to manufacturers.

Taking the average maximum lending rates of banks to the manufacturing sector (20.9 per cent) and the average rate on all categories of deposits (2.2 per cent), the wide disparity of 18.8per cent is not justifiable. Banks in Nigeria build in unnecessary and, sometimes, avoidable costs as a way of increasing lending rate thereby making it impossible to comply with the requirement of the Central Bank of Nigeria (CBN) which states that the banks should charge a maximum of 4per cent above the Monetary Policy Rate (MPR) as lending rate. This they do under the guise of liberalized interest rate regime. The analysis contained in the Nigerian Banks Financial Transparency Report 2010 which shows a total wage bill of ₦265 billion for staff strength of 59,807 of the 14 quoted banks in 2009 is food for thought. This amounted to an average of ₦4 million per staff. The CBN effort in getting the banks to publish their interest rates on deposits and lending has not moderated the high lending rates in Nigeria. The negative effects of high lending rates on economic development in Nigeria cannot be over-emphasized.

III.2. Post-Consolidation Experience

In 2004, the CBN directed the banks operating in Nigeria to recapitalize from a capital base of ₦5 billion to ₦25 billon. The recapitalization exercise led to a reduction in the number of operating banks from 89 to 24 well-capitalized banks. Expectations of a new dawn were high particularly in the real sector, given the new financial muscle of the recapitalized banks to finance both low and high ticket operations, thereby serving as a pivot of economic development. Lending rate was expected to fall with the obvious high liquidity of the banks. It is pertinent to note that our economy is yet to fully reap the benefits of the recapitalization in the banking industry. The agricultural sector and the SMEs that were supposed to enjoy the special consideration and sympathy of the post-consolidated banks were jettisoned on the excuse of high perceived risks and lack of realizable and adequate collateral.

These key sectors play fundamentally important roles in the economy of any nation. Most economies of the world are developed either through effective investments in real sector or trade liberalization; unfortunately Nigeria is not finding things easy in these two major areas. The forage of our banks with their huge capital into stock market speculative activities through unbridled margin loans left a lot of them in comatose when the bubble burst. The CBN had to come up with both financial and managerial rescue packages in order to avoid a total run on the economy. Those banks that still have the liquidity developed a high aversion for credit creation, thus, leading the economy into a credit squeeze situation.

IV. CBN Real Sector Intervention Fund

The ₦500 billion intervention fund was established in a bid to unlock the credit market. The sum of ₦300 billion was approved and earmarked for independent power projects for industrial clusters and the aviation industry while the remaining ₦200 billion was meant for the refinancing/restructuring of manufacturers' existing loans from the banks. The intervention fund was accompanied with a generous interest rate of 7.0 per cent per annum and long repayment tenor of between 10-15 years. The establishment of ₦200 billion Small and Medium Scale Enterprises Credit Guarantee Scheme is to encourage banks to lend to the financially-starved SMEs.

The risk exposure of banks under this scheme is guaranteed to the tune of 80.0 per cent, with lending banks granting credit at its prime rate of interest under a five-year tenor. This is a novel approach adopted by the CBN in redeeming the real sector. Manufacturers' Association of Nigeria has expressed gratitude to the CBN Management for this daring move, the first of its kind in any developing country. This bold initiative should set standards for monetary intervention in the real sector, and should ultimately define the relationship between the banking sector and the real sector. For a technologically-empowered manufacturing sector in Nigeria, long-term and cheap funds of this intervention nature is needed to finance the research into and production of capital goods and industrial plants. It is time to move our underdeveloped techno-economy from raw material enclave to capital goods production through appropriate financing and other macro-economic inducing policies. There is the need to enlarge the phases and scope of the CBN intervention fund. In view of the limited CBN intervention fund, many manufacturers are unable to access the refinancing scheme.

The scheme should not be limited to refinancing/restructuring alone, but should also embrace working capital and loans to resuscitate ailing industries. MAN enjoins CBN to exert her moral-suasion on the banks in order to make them responsive to the ₦200 billion SME Credit Guarantee Scheme operation as we have observed that they are at present apathetic to the scheme. MAN also believes that with diligent supervision of these laudable progammes, it is expected that the manufacturing sector will begin to experience positive turn around and be better placed to play its developmental roles of employment generation, poverty reduction, wealth creation and meaningful contribution to the nation's GDP.

V. Financing the Manufacturing Sector for the Attainment of Vision 20:2020

For a manufacturing sector that will contribute over 25.0 per cent to the envisaged US$900 billion GDP in year 2020, more pragmatic approach must be adopted by the coalition of the CBN, the Deposit Money Banks and other Development Finance Institutions.

(a) Sector Financing

- Appropriate measures should be put in place by the CBN to ensure the utilization of the vast resources in the pension, National Health Insurance, Insurance Fund and the National Housing Fund Schemes.

- Ensuring that all Deposit Money Banks are quoted on the stock exchange so that they can play active roles in the bond market for on-lending to the real sector.

(b) Infrastructural Financing

- The CBN noble example of IPP financing for industrial clusters needs to be emulated by banks.

- Bond issues can be explored for such funding needs for power infrastructure, roads, railways, port development, airports/airlines under a PPP arrangement.

- The availability of these vital infrastructures will go a long way to reducing the high cost of business operation and, ultimately, reduce banks' credit risk exposure.

- The banks should adjust to the reality of Vision 20:2020 by pushing for real sector financing as this has more ability to guarantee their continuous survival than putting their resources in bubble assets.

- Government should further devise a better way of administering subsidies to the agriculture and manufacturing sectors.

- The Executive and the legislative arms of government should curtail fiscal expansion in order to really moderate the high lending rate in the economy.

- Governments at all levels should continue to improve the enabling environment for competitive industrialization, rapid infrastructural development, good regulatory regimes, and other development indicators.