REDESIGNING NIGERIA'S FINANCIAL SYSTEM
BY S.B. FALEGAN
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Redesigning Nigeria's Financial System by Chief S. B. Falegan is organized into twelve chapters, and the time frame of the book is 1960-83. Analytically, the twelve chapters of the text can be grouped into four categories, namely:

(A) The Background;
(B) Analysis of the Structure, Performance and Problems of the Nigerian Financial System;
(C) Promotion of the Financial System; and
(D) The Prospects of Nigeria Becoming a Regional Financial Centre.

Group A contains chapters one and two and provides the historical background of the book. Chapter one surveys the economic environment of Nigeria and shows how oil replaced agriculture as the engine of growth and how the economy consequently became too dependent on oil. Consequently, when the oil glut set in at the beginning of the 1980's, Nigeria's economic hardship worsened with huge balance of payments deficit, rising foreign debt burden, budget deficits and inflation. In Chapter two, the concepts and terms used in the rest of the book are explained. I consider this approach useful in enhancing the reader's understanding of subsequent chapters.

In group B, the structure, performance and problems of the Nigerian Financial System are analysed. The author examined the structure of the system in chapter three, and identified a dual system in the economy — the formal (official) and the informal sectors. The formal sector contains commercial and merchant banks, including development banks, savings institutions and contractual institutions such as pension funds and insurance companies. Due to the inadequacy of this formal sector, the informal sector comprising traditional institutions like *esusu* and thrift societies abound, especially in the rural areas. The weaknesses of the formal financial institutions include inadequate coverage of rural areas, the preference of merchant banks for short-term lending and inadequate resource base for development finance institutions. Another important constraint of the system that was identified by the author is excessive Federal Government interventions in financial intermediation such as floating development stocks and sharing the proceeds among the State governments instead of allowing them to go to the capital market. While corroborating the view that excessive government intervention distorts the smooth operation of any financial system, it should be noted that the author's experience of this practice is based on his observations up to 1983. At present, the proceeds of the Federal Government stocks are no longer shared among the states. This has created more incentives for state goverments to borrow directly from the capital market.

The author examined the processes and problems of monetary policy in Nigeria in chapter four and blamed the fiscal operations of the government as the major factor undermining Central Bank's monetary management. This view is consistent with the Nigerian experience in which monetary policy is usually thrown out of gear whenever government fiscal requirement becomes unsustainable and inconsistent with other macro-economic objectives, such as inflation and balance of payments viability. The author also opined that the reliance on fiscal policy and direct control has relegated some monetary policy instruments to the background while monetary policy functions mainly through credit allocation and interest rate structure in which lower rates are set for the preferred sector. He further observed that little attention has been paid to interest rates as instruments for mobilizing savings and for the allocation of loanable funds. While this observation on interest rates could be tenable for the period (1960-83), in which the author based his writing, it is no longer true under the current deregulated interest rates regime with a positive Minimum Rediscount Rate.

In chapter five, the author summarized most of the patent structural weaknesses of the Nigerian financial system. These include inadequate financial institutions and financial instruments, lack of supervision over non-bank financial institutions which were chartered outside the Banking Decree and the absence of control of the informal sector (or traditional financial institutions) which fill the gap left by the formal sector. The author also observed that the underdevelopment of the financial markets constrains the use of open market operations while the non-functioning of open market operations in turn inhibits the growth of these markets. Although, one of the major impediments to active open market operations — low administered deposit and lending rates — has been removed since the publication of this book, the instrument is still not effective in monetary management because other prerequisites are yet to be met. For example, government securities which are the major money market instruments are still used mainly to raise fund for the government rather than as instrument of monetary management. Furthermore, the Central Bank is still the major holder of the securities, the recently improved yield on these securities notwithstanding.

Chapter six is an extension of chapter five. The author looked more critically at the structure and operations of commercial and merchant banks and argued that the spread between the rediscount rate and the prime lending rate should be narrowed so as to discourage banks from taking undue advantage of the gap to resort to borrowing from the Central Bank for on-lending to customers for profit. I consider this recommendation as a reasonable precaution against the abuse of Central Bank's discount window. The author also frowned at the ownership of banks by state governments because of the usual conflict between sound banking practices and the borrowing needs of state governments. Other weaknesses of the system include the adverse effect on intermediation by rigid insistence on collateral before loans are approved; congestion of banking halls due to inability of banks to meet the demand for their services which results in personalized services and favouritism; and the craze among newly established banks to concentrate their operations in Lagos even though they were incorporated outside Lagos. The author, therefore, recommended for the establishment and localisation of banks in specific geographical areas, and the increase in the number of banks that have specialised functions in order to supplement the existing set-up. These recommendations are capable of rein-

forcing the financial system, provided there is caution against over specialisation as the author also noted.

The focus of chapter seven is on the Nigerian Securities market. After explaining the meaning and mechanics of the securities market, the author endeavoured to advance reasons why the market is still far from ideal. Some of these reasons include the fact that many Nigerians are reluctant to lose control of their businesses to others outside their circles, hence they prefer debt to equity financing. This restricts the number of new shares that are supplied to the market. Secondly, many investors buy securities to hold and not for trading, thereby starving the secondary market of securities. The demand for securities is also low because of low savings and ignorance of prospective investors.

Chapters eight to eleven (Group C) focus on the solutions to the problems of the financial system. These chapters attempt to capture the title of the book which is *Redesigning the Nigerian Financial System.* Chapter eight examines further the state of savings and savings institutions and calls for increased drive to raise savings from both rural and urban areas by: (i) modernizing traditional financial institutions such as *esusu* and thrift societies; (ii) making interest rate attractive to depositors; (iii) emphasizing revenue generation by government parastatals; (iv) diversifying investment portfolios of insurance companies into unquoted securities; establishing new financial institutions and improving existing ones; and (v) encouraging both the government and the private sector to add more securities to the market. The author, however, recognized the possibility that increased elasticity between these instruments and money can complicate monetary management. Consequently, he called for the harmonization of the instruments by the monetary authorities. Some of these recommendations, however, have been overtaken by changes in the financial system since the book was published.

In chapter nine, the author gave a recipe for filling the management, regulatory and institutional gaps in the financial system. Specifically, the author recommended:

(i) a new approach in government companies and parastatals which will enable them to make positive contributions to development through cost effectiveness and efficiency;
(ii) credit rating system for all public-owned institutions;
(iii) modernization and mechanization of the country's financial operations;
(iv) clear, flexible and responsive legislation, administration and regulation of the sustem; and
(v) additional financial institutions to fill the gap left by the existing ones.

These recommendations are sound. What remains is the technical details for the practical implementation of some of them.

Still on solutions, chapter ten explores the measures for fostering active securities market. Apart from inducing private companies to go public, conflicts and irrelevances in the existing laws should be resolved while measures should be taken to make existing laws effective. Other strongly favoured measures include the modernization of the trading system in the market, the rating of securities in order to enlighten investors, encouraging the underwriting of securit-ˢs, and the development of unlisted securities market. ᵉpt for the rating of securities whose practical problems ˡlementation should be explored further, the other prescriptions are inevitable changes which must be made to enhance the securities market.

The author concluded his package of prescriptions for the financial system in chapter eleven. He sees the Central Bank as the hub around which the development of additional institutions and instruments will revolve, and re-emphasized the complimentarity of the discount rate and open market operations for effective credit and monetary control. The conditions given for effective use of these instruments include active and cautious use of the discount market by the CBN, elastic and variable interest rate structure and an asset management policy of the banks that is sufficiently sensitive to the actions of the Central Bank on the securities market. It is important to observe that except for the interest rate structure which has undergone major changes recently, other pre-requisites are still absent today as they were during the time frame of the book. In order to simplify the operations of the discount window, the author goes on to prescribe a variant of an instrument called the Lombard facility in which banks are allowed to pledge eligible securities instead of the straight discounting that sells securities in return for advances. This facility offers an option to the straight discounting and introduces some flexibility in discounting. The other important factor given for effective use of the open market operation is the market situation in which the existence of shortage or excess liquidity in the financial system (instead of the need to raise government revenue) determines the volume of securities issued. This will no doubt enhance monetary control but will depend on whether the government places its priority on monetary or fiscal measures. Finally, the author advised the government to de-emphasize direct credit control and above all to initiate reforms along with Securities and Exchange Commission in their regulatory functions. This is one of the areas in which this book could be enlarged in future.

The final chapter of the book analyses the conditions, advantages and problems of a regional financial centre and examines the prospects of Nigeria becoming such a centre for Africa. After analysing the situation in Nigeria, the author rightly observed that the necessary conditions for such a centre does not exist at present. However, the development of such a centre in Nigeria will depend on a number of factors which include the restructuring and the development of the financial system and the economy as a whole, the ability of the Nigerian economy to maintain investors' confidence, and the liberalization of trade and payments regime.

I consider the book a big contribution to knowledge. It has married experience with theory. The result is a highly qualitative and illustrative product. The problems identified and the solutions provided are food for thought. The book will be very useful to university students, researchers and managers of the public and private sectors. It should be noted, however, that some of the author's observations have been overtaken by developments in the financial system since the completion of the book. Some of these changes have been noted in his postscript. I expect these changes to be fully taken into account in the next edition of the book.

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