BULLION

PUBLICATION OF THE CENTRAL BANK OF NIGERIA

Volume 31, Number 4

October - December 2007

ISSUES IN FINANCIAL REMITTANCES, ECONOMIC INTEGRATION, BANK CONSOLIDATION AND DEVELOPMENT FINANCING

BEHIND THE SCENE

BULLION is published every three months by Central Bank of Nigeria. Views expressed therein do not necessarily reflect the thinking of the Bank's Management. Copies of the journal are available without charge through formal request to the Editor. Articles appearing in the journal may be reproduced only with the expressed permission of the Editor or the article's author.

BULLION ISSN - 0331-7919

CONTENTS PAGE

The Impact Of Remittance On Economic Development

By Dr. A. Englama*

Introduction

Worker's remittances consist of goods or financial instruments transferred by migrants living and working abroad to residents of the home economies of the migrants. It is limited to transfers made by workers who have stayed in foreign economies for at least one year while transfers from migrants that are self employed are excluded (IMF, 1999). The phenomenal growth of remittances in recent times has caught the attention of governments particularly in the developing countries, international organizations, Non-Governmental Organizations (NGOs) and the private sector, due to its importance as a viable source of external financing. It has out performed some traditional capital inflows such as foreign direct and portfolio investments in several countries while it had become a major source of foreign exchange for others. By its nature remittances is counter-cyclic in nature, voluntary and targeted at improving the welfare of family members in home countries. The inflow of remittances during period of economic downturn when compared with other flows further highlight its potential as an economic development tool.

Studies have shown that several factors influence the decision to remit money from abroad. One of such factors is the prevailing economic circumstance in the country of origin. Other factors include wage rates, exchange rates and inflation rate (Russell 1986). Furthermore, socio-demographic characteristics of migrants, political, economic and legal environment of home country of remitters are part of the factors worthy of consideration. Strong cultural behavior and emotional links to the migrants' home of origin are also critical. Although several developing countries such as Mexico, India, the Philippines, etc, had long taken advantage of remittance to boost their economic growth, others such as Nigeria are beginning to recognize the

* **Dr. Englama** is a Deputy Director in the External Sector Division of Research Department, Central Bank of Nigeria, Abuja. The views expressed in the paper are those of the Author and do not in any way represent the views or thinking of the Central Bank of Nigeria

need to enhance the inflow of remittances.

Researchers however, have not agreed on its role as an economic development tool as some have expressed concern that continued currency appreciation due to high inflows could lead to a Dutch disease phenomenon. On the other hand, there are examples of countries that made deliberate efforts to attract remittances as a source of external financing. It is against this background that this paper examines the impact of remittances on economic development on recipient countries. The rest of the paper is structured as follows: Following this introduction section II discusses conceptual issues, Section III focus on the overview of the global remittance environment. The impact of remittances on economics development is highlighted in section IV. The paper is summarized and concluded in Section V.

Section II
Concepts of Remittances

Remittance is the inflow that results from migration. Migration is the voluntary movement of person / persons from a home country to seek a more prosperous environment and or to ensure the safety of life. When migration is documented it is termed regular, the reverse is termed irregular migration. Human trafficking is not migration because people were forced to move against their will. Fundamentally, the theory of migration takes into cognizance the various labor market opportunities available to labour in developing countries. The theoretical underpinnings are those individuals who choose employments that maximize their expected gains from migration. The labour-force, both actual and potential, compare expected incomes for a given horizon in the labor receiving country with the domestic incomes; and migrate if the former exceeds the latter (Todaro 1969). The most favourable outcome of migration is remittances. Remittances has been defined severally as Tewolde (2005) describes remittance as monetary and non-monetary items that migrants earn while working abroad and later send back to their families living in their homeland (country). Shivani and Tineke (1999) and the International Labour Organization (ILO 2001) defined remittances as the portion of international migrant workers' earnings sent back from the country of employment to the country of origin. Harrison (2003) and Department for International Development (DFID) (2003) in their analytical studies defined remittances as the sum of workers' earnings and compensation of employees and migrants' transfer.

A deviation form the above definitions is Levitt's (1996) which stated that it is ideas, practices, identities and social capital that flow as social remittances. Ahlburg (1991) discusses remittances in a broader perspective as a reflection of monetary dimension in the complex web of linkages that exists between migrant Diasporas and their home countries.

To avoid the ambiguity surrounding the specific meaning of remittances countries adopt the definition in the Balance of Payments Statistics Manual of the International Monetary Fund (IMF),where remittances is defined as the sum of three components: workers' remittances, compensation to employees and migrant transfers. Workers' remittances are recorded under the current transfers in the current account of the balance of payments. It includes goods and financial instruments transferred by migrants, who reside and work abroad in a given country for more than one year. It could be in cash or in kind from migrant to resident households in the country of origin. Migrant transfers are treated as capital transfers of financial assets as they move from one country to another and stay for more than one year. The assets or liabilities that migrants take with them when they move from one country to another and are regarded as workers remittances as well. They are reported under capital transfers in the capital account of the IMFs Balance of Payments. The manual simply view workers' remittances and migrants' transfers as transfers, while compensation of employees is records of remuneration for work done. They are part of the unilateral transfers account in the current account section of the balance of payments. In other words, they are credit item in the current account; hence they help to partially offset the deficit in trade on merchandise and services.

Remittances can be sub-classified into financial remittances, social remittances, and remittances-in-kind. Financial remittances are the inflow of cash and financial products. Cash are sent formally through the banks and network of the international Money Transfer Organizations (MTOs) and also conveyed through informal channels. Financial remittances could also be in the form of Diaspora bond receipts that are designed by the home countries to attract funds from the diaspora. The Diaspora provide social remittances to their local communities in the area of health, education as well as the building of infrastructure through donations of funds. Social remittances also include the values and norms on which social capital is based for example social and political leaders can sometimes harness the status they acquire in the host country to advance their cause in the homeland. They also include values about how organizations should work, incorporating ideas about good government, good churches and about how politicians and clergy should behave. These include again how individuals delegate household tasks, the kinds of religious rituals they engage in, and how much they participate in political and civic groups. Social remittances are passed systematically and intentionally. A social remittance occurs when migrants speak directly to a family member about a different kind of politics and encourage them to pursue reforms. In cases such as these, ideas are communicated intentionally to a specific recipient or group. People know when and why they changed their mind about something or began to act in a different way.

Remittance-in-Kind are goods that are sent from abroad to home countries.

This can take the form of clothing items, medicines, toiletries, books, electronic equipments and in certain cases automobiles.

Section III
An Overview of Global Remittance Environment

The remittances environment describes the physical entities, players and the process that are involved in the chain of remittance delivery. The major players are the international Money Transfer Organizations (MTOs), their agents, the machineries such as the ATM and mobile phones, the deployment of Information and Communication Technology (ICT) and the rules and regulations. Western Union Money Transfer is the dominant of all the MTOs. It has the largest worldwide presence in the industry with almost one-quarter of the global market. **Based on its 2006 report, the company has approximately 270,000 agent locations in over 200 countries and territories. Another major player is the** MoneyGram which provides worldwide money transfer services, working closely with chosen agents in 125,000 locations across 170 countries and territories. Other MTOs such as Thomas Cook and Vigo operate in tandem, though with a lesser presence than Western Union. The institutions that are involved in remittance delivery vary from country to country so also their market shares in each region and among the sending countries. In some regions/countries, such as Southern Europe, Nigeria and Philippines, banks and postal agencies are the leading service providers. The remittance market however represents the total funds sent by migrants through both formal (i.e. banking system) and informal (i.e. Alternative Remittance System) channels. The attractiveness of either system is predicated on a number of factors which include among others: the cost of transactions, speed, security of funds, geographic proximity/accessibility, convenience in terms of familiarity and language.

The formal channel of money transfer provides data on the amount transferred in contrast to the informal channels which pose a particular risk of being used for money laundering and possibly financing of terrorism. The predominance of informal cash transfers are based on personal relationships through business people, courier companies, friends, relatives or oneself. The choice of use of the informal channel of remitting funds can be attributed to constrain caused by banking and foreign exchange regulations, low outreach, and insufficient protections to recipients, among others.

The rapid development in ICT had made it possible to reach a wider range of communities that would have been isolated. In particular the use of mobile phone with a unit cost that is affordable for an average family and the advent of the internet facilitate real time delivery services thus promoting the growth in international money transfer. Despite the advancement in ICT, the charges on remittance to developing countries remain relatively high. It averages about 10 per cent of the total amount remitted.

Formal remittance flow worldwide in 2007 was estimated at US$318 billion up from US$268 billion in 2006 of which US$199 billion was remitted to developing countries, $47 billion to low income countries. The volume of remittances reported officially soared, in part due to increased migrants' interests in sending more money home and in part due to improved reporting system. Of the regions in the world, Latin America and the Caribbean remained the highest recipient, while remittances to Europe (accounted for by France) and Central Asia registered the highest growth rate in 2007 (World Bank 2007). In reality, the official reports of remittances are always underestimated, because migrants also use unofficial channels to send money home, and these sums are not recorded.

India remained the highest recipient of remittance inflow in 2007 with US$27 billion; in the second place is China (US$25 billion) and the Philippines fourth with (US$17 billion). The developed countries are the major sources of remittances with the United States accounting for US$42 billion in 2006.

Table 1: World Remittance Inflow of Top Countries

	2005	2006	2007
India	21.3	25.4	27
China	20.3	23.3	25.7
Mexico	21.9	24.7	25
The Philippines	13.6	15.3	17
France	12.3	12.5	12.5

Chart 1: **Inflow of Remittances by Region**

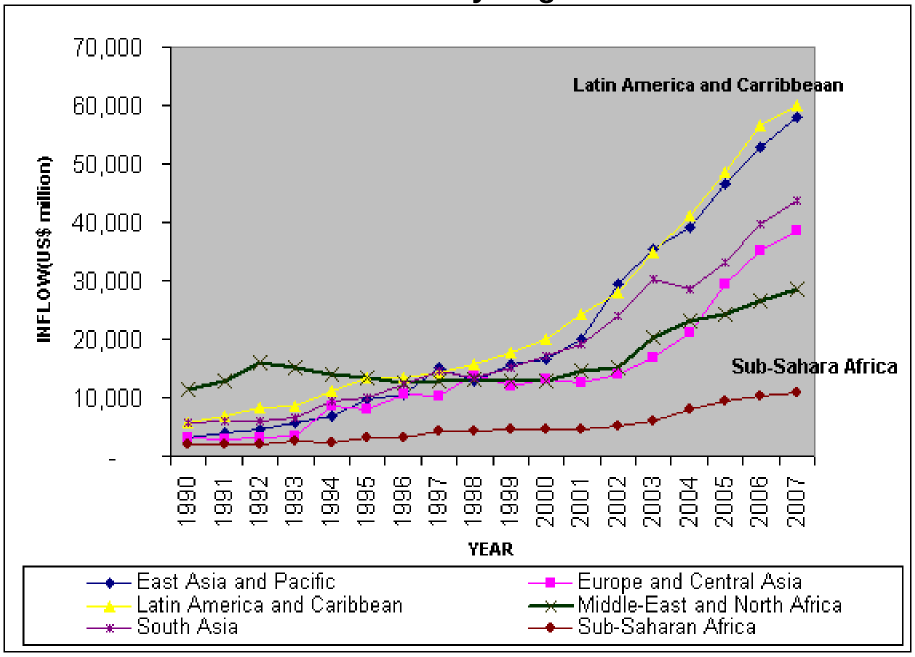
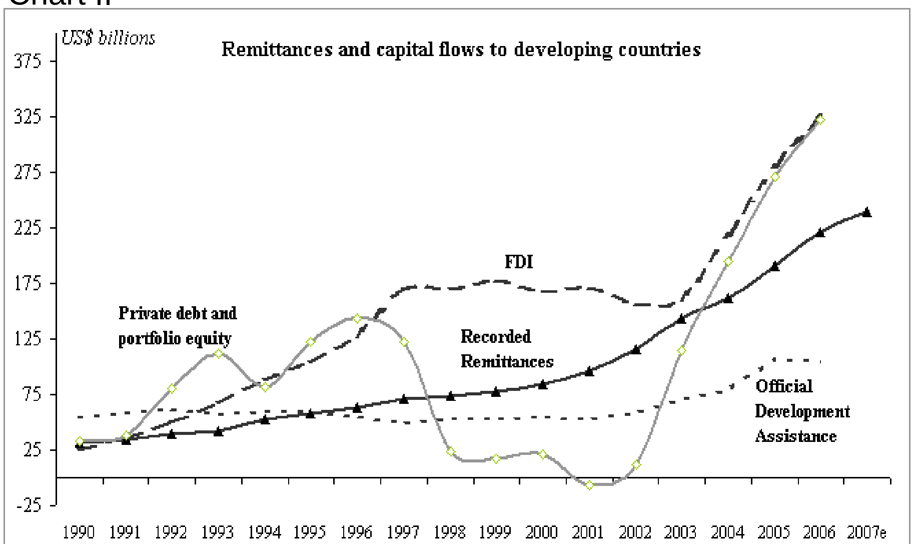


Chart II



Sources: *Global Economic Prospects 2006: Economic Implications of Remittances and Migration* (World Bank), *World Development Indicators 2007*, and *Global Development Finance 2007*.

A trend analysis of capital flows into developing countries by the World Bank (2007) showed that private debt capital, portfolio equity, FDI, remittances and official development assistance (ODA) were each below US$75.0 billion in 1990. The inflow of FDI grew gradually to about US$175 billion by the late 1990's where it peaked until 2002, when it rose above US$350.0 billion in 2006. Private debt and portfolio equity on the other hand had been unstable with wide fluctuations between 1990 and 2007. It however, rose above all the other capital flows in 1992 to US$120.0 billion but dropped below the FDI flows in 1993 to about US$80.0 billion. Although it increased to about US$125.0 billion in 1995, it became negative in 2005 before it dramatically rose to equate FDI by 2005. ODA had been steady but the growth has been lower than most other capital inflows. Remittances on the other hand rose constituently from less than about US$25.0 billion in 1990 to over US$240.0 billion in 2007.

Even though the official figure on remittance inflow world wide is staggering, the informal remittances could contribute an additional 50 per cent to inflows in some cases. The continued existence of the informal channel can also be attributed to the existence of irregular migrants that seek new livelihood to alleviate economic hardship in addition to the cheaper and quicker services provided.

Available data indicated that large pool of the Nigerian Diaspora are found in different parts of Europe, North America, the Middle East and high income and developing Asian countries. According to the World Bank, Nigeria is the largest recipient of remittances in sub-Sahara Africa (SSA) countries. The country receives about 65.0 per cent of officially recorded remittance flows to the region and about 2.0 per cent of global remittance flows, with a total of 54 per cent from the United States.

Data from the Central Bank of Nigeria (CBN) indicated that remittances through the banking system stood at US$2.26 billion in 2004, while figures for 2005 and 2006 were $3.3 billion and US$7.7 billion, respectively. In 2006 the official statistics was at US$10.6 billion while estimates for 2007 was US$18.0 billion. A recent study on the remittance environment in Nigeria concluded that the official inflow could be increased by 25.0 per cent, through the formalization of the informal channels.

Remittance inflows into Nigeria had surpassed Overseas Development Aid (ODA) since 2002, (approximately five times the ODA valued at US$271 million). Under reporting of remittance flows to Nigeria is still common because of data collection deficiencies and the prevalence of informal transfer mechanism.

Section IV
The Impact of Remittances on Economic Development

Different definitions of economic development are widely used but the most notable and universally accepted definitions are the ones that consider the enhancement of productive capacity of a country. Its impact on economic development however can be viewed at the macro and micro level and had varied over the years.

The consensus view on the impact of remittance on economic development had been subject to cycles of pessimism and optimism (Harrison 2003;Carrasco and Jane Ro; 2007). In recent times, governments have embraced and promoted the inflow due to greater understanding and the magnitude of inflow (Roberts 2004). The potential benefits identified over the years are: It serves a stable source of external finance, a potential source of capital formation through savings and investments, promotes human capital development and; reduces inequality and poverty etc. There are evidences that showed that remittances are increasingly used for investment purposes in developing countries, especially in low income countries. Migrants are more likely to continue to invest in their home countries despite economic adversity than foreign investors, an effect that is similar to the home-bias in investment (World Bank 2001; Carrasco and Ro 2007).

At the macro level remittance is incorporated into the national accounts of the receiving countries as transfers from abroad. Hence they go directly into the expenditure pattern of the economy, saving or investments. Long-run output growth could be accelerated as a result of the additional investments in physical and human capital especially where well developed financial system and institutions allow remittances to be well intermediated and used.

Adelman and Taylor (1990), found from their studies that every dollar received from migrant working abroad leads to an increase in Gross National Product (GNP), though this depends on whether it was received by urban or rural households.

Large remittances flows improve a country's creditworthiness for external borrowing this is because the inflow would effectively reduce the country's debt/exports ratio, thereby, improving the country's credit ratings and access to international capital markets. Moreover, some financial institutions in developing countries have been able to tap into international market under relatively favourable conditions through securitization of the future flows.

Remittances increase the resources at the disposal of recipients resulting in increased demand for goods and services. The growth in the consumption of social amenities such as health, education and shelter produces a positive impact on human development. Remittances if invested or consumed, contribute to output growth and generate positive multiplier effects, where there are sound economic policies and flexible foreign exchange in place.

Remittance contributes to National Savings which in turn increases investment, in the economy. Remittances as a source of external financing also helps to smooth fluctuations in economic growth in migrants' countries of origin as remittances flow continue at a normal rate or even increase during period of economic hardship (WEO, 2005). Examples of countries that experience economic development through remittance inflows abound in the literature. A high percentage of such developments are in the areas of infrastructural development. For example, Malians living in France have helped build 60 per cent of the infrastructure in Mali. Other examples are: The Central Mexican state of Zacatecas had maintained a programme called “Tres Por Uno” which means three-for-one since 1992. This programme matches each dollar sent by migrants or hometown associations with three additional dollars from the federal, state and local governments for community projects. The programme raised more than US$4.5 million dollars for about 400 community projects. It support road construction and projects that create employment. There are other states in Mexico that uses similar funding to promote economic development programmes.

Israel is one of the countries that had taken advantage of remittances to promote economic development early. Since 1951, the Development Corporation of Israel (DCI) raised over US$25 billion as external finance through the issuance of bonds to the Diaspora. The proceeds were used to finance major public projects such as desalination, construction of housing and communication infrastructure.

The government of India through the State Bank of India (SBI) had raised well above US$11.0 billion from 1991 from Diaspora bonds. The bank issued the India Development Bonds (IDBs) to soften the effects of the Balance of Payments crises in 1991 and raised US$1.6 billion. In 1998 Resurgent India Bonds (RIBs) issued to mitigate the effects of sanctions following the nuclear test fetched US$4.5 billion while US$5.5 billion was realized in 2000 through the issuance of the India Millennium Deposits (IMDs).

In Philippines, the government embarked on the creation of structured employment overseas for its citizens in the 1970s. The country had continued to reap massive remittance inflow from part of the worker's earnings remitted home. By 1989 the Commission of Filipinos Overseas launched (LINPAL) a programme that facilitated the contribution of the Diaspora to economic development through supporting education, health and welfare, livelihood and small infrastructure projects. The programme had yielded in excess of US$1.0 billion, (Sander 2003).

Looking ahead, remittance flows could also be used to accelerate financial development in recipient countries depending on the extent to which financial products and institutions can be developed to persuade recipients to turn their remittances into deposits with financial institutions. In turn, financial development generates positive effects on growth and development.

On the micro level, remittance studies by Newland and Patrick (2004) showed that millions of poor people in countries that have access to technology benefit from the multiplier effect of Diaspora investment. This is inspite of the fact that their countries are not positioned for international investments. Furthermore, remittances have a direct impact on poverty reduction since it flows to the household directly. Remittances help to loosen budget constraints on recipients allowing them to increase the consumption of durables and non-durable goods. Hence, a sizeable amount of remittance flows are utilized to maintain family and provide social security as there is no national welfare system operating in most of the developing countries. Various studies have shown that remittance receiving households tend to be better than non-receiving household in terms of higher average incomes and assets bases. (Sander 2003; Rajan and Subramanian 2005). Economic impact studies in Mexico showed that remittances mostly or sometimes completely cover general consumption and or housing. One estimate indicates that 80 per cent of the money goes for food, clothings, health care, transportation, education and housing expenses. Remittances are also for financing new business venture or used to sustain an existing business which in turn contributes to the development of the economy. The Federal Reserve Bank of Dallas (2004) noted that in Mexico, remittances accounts for about 27 per cent of the capital invested in micro enterprises throughout urban Mexico with estimates going up as high as 40 percent in states that have high migrant population in the United Sates. In India and Pakistan remittances have contributed to sharp increase in agricultural production as it enhances the ability of local farmers to purchase tractors and machineries. The influence of remittances on small and medium industry and microfinance are basic ingredients of strengthening the institution, which is a cornerstone for economic development.

Countries that have promoted the use of formal sector for remittances have increased banking population, an indication of economic development. Thus, highly stable and predictable remittance inflows can be used as collateral and leveraged to provide access to commercial credit and the capital markets by individuals which if judiciously disbursed will impact positively on the economy of the recipient country.

On the pessimistic side, views were expressed that remittances sent by an individual migrant directly to his or her family do not contribute to development because the greatest portion of such income is spent on consumption and very little is directed towards 'productive investment.' Others noted that it decreases home production which consequently reduces income which could create negative multiplier. This may further resulted in a downward spiral in local economic activity. In this perspective, migrants' income has a limited potential to alleviate poverty. Remittances has also been said to create dependency of migrants' households as well as the economy as a whole, especially if they constitute a main source of foreign currency.

Assuming remittances are characterized by high volatility, countries might suddenly find it difficult to generate sufficient financial assets needed to grow the economy. Therefore, a dramatic fall in remittances does not only affect national economies but also the individuals who depend on money transfer from abroad. It is also possible that remittance flows may generate similar problems at a national level by supporting the overall balance of payments position, thereby reducing incentives to implement economic reforms.

In addition, it could lead to a Dutch disease, when the increased inflow leads to currency appreciation, making the tradable sector of the economy to suffer as it losses competitiveness relative to the outside world. The “Ghost Town Effect” is another negative phenomenon caused by the belief of residents of a town that they can only meet their financial need through migration. The local economy in this case becomes dependent on inflow of remittances and where it stops abruptly there is a ghost town effect as the local economy disappears and more people move out. This effect can also be attributed to the family joining the migrant. Mexico in particular had been hit with this phenomenon over the past ten years (Carrasco and Ro 2007).

Section V Policy Recommendations

The impact of remittances on economic development hinges on the sustainability of the inflow as well as the development of the appropriate structures to channel the inflows into areas that would be beneficial to the economy as a whole. The following policy measures are therefore recommended if remittance will impact on economic development:

- § The involvement of larger numbers of banks and other financial institutions in the inward transfer of remittance. Some countries such as Senegal have opened domestic bank branches in countries in areas of high migrant population. This had increased flows as migrants prefer to deal with domestic institutions and staff. At the home front, there should be increased access to banking service points to increase the number of recipients that would have easy access to receiving their funds. Both recommendations would reduce the cost and increase efficiency of remittance delivery.
- § Remittance distribution should be supported by a sound, predictable, non-discriminatory and proportionate legal and regulatory framework to encourage the participation of international financial institutions through good governance and risk management practices
- § Domestic banks that act as agent to the international MTOs should be encouraged to shift business from purelymoney transfer operators,and offer financial instruments that can encourage savings.Such as opening of a bank account by recipients and credit services that are securitized by future remittance inflow to recipients. These would encourage recipients to

save part of their funds that can be channeled into economic activities.

§ The informal flow of remittance can be formalized through the expansion of the financial systems infrastructure to channel the large amount of informal remittances flow to the formal channel. This could be achieved by permitting post offices and micro finance institutions to operate in money transfer business, as they have many branches in rural areas

§ The payment system infrastructures and network should be improved to promote wide and efficient delivery of remittance services. This involves interlinking the various money transfer operators with other ICT facilities such as the use of cellular phones and Point of Sales (POS) terminals.

§ Offering bonds to the Diaspora to raise money for investments in their home countries with an attractive premium. It is pertinent however to ensure that the legal and registration rules to issue bond abroad do not create future legal and administrative encumbrances.

§ Facilitate government advocacy through effective policies and bilateral initiatives. Such initiatives include partnership with the host countries to reduce the cost of remittances and provision of consular permits to facilitate use of formal remittance channels by all categories of migrants.

§ Government should reach out to Home Town Associations (HTAs) by supporting their efforts through incentives and cooperation with matching funds and credit programme. These associations could be encouraged to contribute towards the provision of social projects and local infrastructure.

§ An entrepreneurship development programme should be institutionalized. Recipient countries could come up with micro-finance institutions to capture remittances, which will be channeled to investment ventures for returnees.

§ The Public Private Partnership model for the development of infrastructure as done in Mexico should be adopted. The Federal, State and local government must be willing to match the inflow of funds from the Diaspora for economic development. It serves as an incentive and increase the voice of the Diaspora in promoting economic development.

§ The Central Bank or any other relevant government organization should develop a web-site that can be assessed anywhere in the world as done in the Philippines to provide information on institutions that provide remittances services into the country. This would ease and increase the channels of sending remittances back home by the Diaspora. The remittances environment should be transparent and offer customer's protection. Loss of money through internet fraud should be tackled through safe online transfer mechanism to ensure the safety of information and identities of the recipients/senders.

§ Lastly, a strong and stable macroeconomic environment to assure migrant of the safety of their inflow should be enthroned.

Section VI

Summary and Conclusion

Remittances are being regarded as one of the stable and predictable source of external finance for economic development especially if properly invested. The effect of remittances varies from country to country, in relation to their efficiency in channeling remittances to productive uses. Although remittance affects economic behavior, it is not the omnibus solution to the problems of underdevelopment given the associated negative effects when not adequately managed. It is pertinent therefore that productive and sustainable avenue for the investments of remittances must be identified at the same time, policies to enhance the contribution of migrant associations to country of origin.

This paper has focused on funds remitted as contributing to economic development, other benefits accruable from the Diaspora should not be over looked. Apart from foreign exchange, the Diaspora has more to offer their countries of origin in the long run, their skills, investments, and social networks may have more important effects. Governments and other public and private institutions may help to create a framework in which the Diaspora could make their intellectual capital available to their home countries through visits, consultancy or internet contacts.

In conclusion, the use of remittance as a resource for development remains highly debatable even-though examples abound, further empirical studies however may bring to light more information on its role as an economic development tool. The recipient countries therefore require better data management on its inflow, usage pattern, transfer mechanism, and good practices to channel savings into investment schemes for economic development.

REFERENCES

Adelman and Taylor (1990):" Workers'Remittances to Former Soviet States" www.ier.hitu.ac.jp/ Common/ publication/DP/DP476.pdf

Ahlburg (1991): Remittances and Their Impact: A Study of Tonga and Western Samoa. Pacific Policy Papers No. 7. Canberra: National Centre for Development Studies, Australia www.adb.org/Documents/Reports/ Remittances-Pacific/references. PDF

Alessandra and Ivo (2006): "Remittances and Movement of Persons," Working paper 8 13 November 2006 www.unece.org/stats/documents/ece/ces/ge.10/2006/wp.8.e.doc

Carrasco and Jane Ro (2007): "Remittances and Development" The University of IOWA Centre for International Finance and Development" http://www.uiowa.edu/ifdebook2/contentc/part4-II.shtml

Department For International Development (DFID) (2003) : "Conference on Migrant Remittances: Development Impact, Opportunities for the financial sector"www.livelihoods.org/hot_topics/docs/RemitConf.doc

*Canas J et all(2004): "*Explaining the Increase in Remittances to Mexico" Issue 4, July/August 2007Federal Reserve Bank of Dallas, Federal Reserve Bank of Dallas (2004),

Harrison A.T. (2003): "Working Abroad-The benefits of Nationals Working in Other Economies" OECD Round table on Sustainable Development

International Labour Organization (ILO), (2000): "Migration and Development in Central Maghreb" www.ilo.org/public/english/protection/migrant/publ/imp-

International Monetary Fund (IMF) (1999): "Are Immigrant Remittance Flows a Source of Capital forDevelopment" www.imf.org/external/pubs/cat/longres.cfm?sk=16801.0

Ketkar and Ratha (2007): "Development Finance via Diaspora Bonds", being a paper presented at the Migration and Development Conference at the World Bank Washington D.C. May 23, 2007.

Levitt P.(1996): "Social Remittances: A Conceptual Tool for Understanding Migration and Development." Working Paper Series. No. 96.04. Cambridge, Massachusetts:www.unfpa.org/swp/2006/english/notes/notes_for_indicators1.html

Newland and Patrick (2004): "Beyond Remittances: The Role of Diaspora in Poverty Reduction in their Countries of Origin": Being a study by the Migration Policy Institute for the Department of International Development, Migration Policy Institute.

Rajan and Subramanian 2005, "Impact of Remittances on Poverty and Financial Development in Sub ideas.repec.org/p/imf/imfwpa/07-38.html

Roberts (2004): "Remittances, Institutions and Economic Growth1 in Armenia" www.kent.ac.uk/economics/staff/mep/Remittances.pdf

Russell S. (1986):"Remittances from International Migration: A Review in Perspective" World Development, 14(6),pp.677-696.

Sander C. (2003): "Migrant Remittances to Developing Countries" A SCOPING STUDY: Overview and Introduction to Issues for Pro-Poor Financial Services Development (DFID), Bannock Consulting

Shivani and Tineke (1999): "Microfinance and Migrant Remittances" Being the Paper commissioned by the Multilateral Investment Fund, Inter-American Development Bank, www.gdrc.org/icm/remittance/more-remittance.html

Tewolde (2005): "Remittances as a tool for development and reconstruction in Eritrea. An economic analysis" Journal of Middle Eastern Geopolitics,Vol 1, No 2 (2005)

Todaro (1969): "Industrial Economics and Economic Development aiu.edu/publications/student/english/industrial%20economics.html

World Economic Outlook (WEO) (2005): " Two Current Issues Facing Developing Countries" Chapter II, WEO 2005

Woodruff C. and Zenteno R. (2001): "Remittances and Micro-enterprises in Mexico." www.worldbank.org/afr/diaspora/200802hlseminar/G8-Berlin-Increasing%20Macroeffects%20of%20

World Bank (2001): "Remittance and Development"

World Bank (2008): "India Top Receiver of Migrant Remittances in 2007, Followed by China and Mexico" being a World Bank press release number 2008/243/DEC,http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,CONTENTmdk:21692926

Remittances Inflow: A Potential Source Of Economic Development For Nigeria

By Sanni. H. Taiwo*

Abstract

The relevance of remittances worldwide prompted the need to examine the possibility of leveraging remittances for rapid attainment of economic growth in the country. Available literatures revealed that the deployment of remittances could have both positive and negative consequences. It thus has a long term prospects if utilized efficiently especially where it is employed to finance education, health and investments. In a developing financial system such as Nigeria, remittances could be used to alleviate credit constraints and act as a substitute for financial development. Even where it is employed to increase consumption, it thus enhances production, boosts per capita income and consequently reduces poverty and inequality. Conversely, where remittances are excessively dependent upon by a country, it could dampen the morale of recipients in contributing to economic expansion. The paper however noted that a lot of resources accrued to the country through remittances are yet to be fully maximized. It therefore stressed the need to develop appropriate macroeconomic policies to respond to large remittances inflow for economic development of this country.

1.0) Introduction

The pace of globalization over the past decades has contributed significantly to the increasing spate of integration of the world economy. It has in turn culminated in a countless number of financial flows, trade in goods and services, movement of persons and various forms of technology transfer across the world. As globalization deepens, so does the movement of people across the shoreline of other countries. Although, the global movement is attributed to the quest for improved condition of living through higher earnings on similar occupations in the low-income countries, the growing issues of trade, transportation, telecommunications, transfer of remittances and tourism, thus constitute other critical factors contributing to the nexus between migration and remittances. However, the issue of migration remains controversial from the point

* **Mr. Sanni** is a Principal Economist in the Fiscal Analysis Division of Research Department, Central Bank of Nigeria, Abuja. The views expressed in the paper are those of the Author and do not in any way represent the views or thinking of the Central Bank of Nigeria.

of view of scholars. While some people see it as a threat to societies at home and host countries, other scholars in developing countries view it as loss of human capacity trained from public funds, with little consideration for remittances and its attendant impact on economies of these countries. However, the majority of the policy debates on migration in recent times centers on the loss of skills and labor from poor to rich nations, particularly in vital areas of the economy such as agriculture.

Remittances constitute a portion of international migrant workers' earnings sent back from the country of employment to the country of origin. It makes up a significant portion of the income of the recipients, which could be in the form of cash or goods to support families. It's being recognized as one of the migration phenomena in the economies of many labor-sending countries. Its occurrence has grown rapidly in the past few years and now represents the largest source of foreign income for many developing countries. However, the issue of estimating the exact volume of remittance flows remains very difficult simply because of the unprecedented volume of transfers that take place through unofficial channels. Available statistics showed that the size of official remittance flows to developing countries was about $251 billion in 2007, which double the amount of development assistance received by emerging economies. Informal and unreported remittances were estimated at $86 billion totaling about $337 billion worldwide. Nigeria has since the past few years recorded significant growth in remittance flow. Between 2002 and 2006, the country recorded a quantum leap in remittances from $1.35 billion to $15.0 billion in 2007.

Prior to this scenario, the impact of remittances on economic development was rather ignored based on the argument that remittances were mainly used for consumption and not for productive investments. Not until recently that the government of most countries began to realize the prominence of remittances as a critical source of external funding, the second largest after Foreign Direct Investment (FDI) for many developing countries. Again, there is little or no attention devoted to research studies, sponsoring of seminars, developing core principles, financing project to help raise awareness of the importance of remittance flows, and leveraging development impact by providing increase financial options to remittances' families and their communities. It is therefore necessary that developing countries should begin to show greater interest towards enhancing inflow of remittances to their economies. Nigeria, in particular should intensify efforts at using remittances to grow its economy as it is increasingly becoming a potential tool for achieving economic development in the world of today.

It is against this background that the paper aims at probing into the use of remittances as a vehicle for achieving sustainable economic growth. The rest of the paper is structured into sections, thereby focusing on the following topics: review of selected literature, overview of remittance industry, remittances and economic development, policy measures designed to enhance remittance flows for economic growth, and summary and conclusion.

2.0) Review of Selected Literature

There has been a plethora of literatures on all aspects of financial flows to developing countries with few references on remittances. This is because official remittances which are the financial counterpart of the migration flows have received less attention by mainstream academics and policy makers. In recent times, there has been increasing changes following the growing recognition of workers' remittances as an important and stable source of financing economies of most countries. As a result, the issue of remittances cannot be treated in isolation of migration as both concepts are commonly linked. The theory of migration, therefore, takes into cognisance the various labor market opportunities available to labor force in developing countries. Thus, the theoretical underpinning states that every individual chooses the job that maximizes their expected gains from migration as the labor force, both actual and potential, compares their expected incomes for a given horizon in the labor receiving country (the difference between returns and costs of migration) with prevailing average countries' of origin incomes; and migrate, if the former exceeds the latter (Todaro 1969).

Available studies further showed that the size of remittance flows depend partly on the number of emigrants' resident in other countries, and in part relates to their salary levels and cost of living. Therefore the migrant's propensity to remit from the available resources determines the volume of remittances sent, which is in turn a function of a combination of factors: the available incentive programmes, the removal of black market premium on exchange rates and the presence of stable or unstable economic and political conditions. Macroeconomic studies by El-Sakka and McNabb (1999); Russell (1986) identified determinants such as the level of economic activity in the host and the home countries, the wage rate, inflation, exchange rate, interest rate differentials or the efficiency of the banking system as contributory factors to remittance flows in countries.

Also stressed in one of the studies conducted by Wahba 1991 that the prevailing economic circumstance in the country of origin coupled with political stability and consistency in government policies and financial intermediation significantly affect the flow of remittances. Faini (1994) finds evidence that the real exchange rate is also a significant determinant of remittances. Real earnings of workers as well as total number of migrants in the host country were consistently found to have a significant and positive effect on the flow of remittances (Swamy 1981; Straubhaar 1986; Elbadawi and Rocha 1992; Chami, Fullenkamp and Jahjah 2005). Socio-demographic characteristics of migrants, where female migrants are more likely to have families with them in the host country, impact on her capability to remit money home. Social factor by way of strong cultural behavior and emotional links to the migrants' home of origin is also critical in remittances decision-making process.

Rapoport and Docquier (2005) provide an excellent overview of theoretical reasons for remitting money home. Accordingly, remittances are sent home due to a combination of altruistic and self interest motives. It has been widely acknowledged that altruism towards family members at home has become an important motivation for remitting (Lucas and Stark 1985). This implies that remittances are simply utility function in which the migrant cares about the consumption of the other members of the households. On the other hand, self interest motives for remitting may evolve, if the family aims at entering into mutually beneficial agreements thereby making the family to be eligible for inheritance, esteem or other resources in the community of origin. In this respect, migrants send remittances in order to reimburse the household for past expenditures such as schooling or cost directly related to migration or invests for the future either out of concern for inheritance or as a way of maintaining status or return home in dignity. Lucas and Stark (1985) view remittances as a result of an inter-generational contract between migrants and their parent in the home country.

The international migration has the potential to contribute to sustainable development through remittances, skill transfer, investment, brain circulation and Diaspora networks. The most notable positive economic effect of migration is in remittances. This refers to monetary and other cash transfers sent from migrants to their families and communities at country of origin. It has great potential to generate a positive impact in migrants' home countries. Maimbo (2003) reports that remittances to developing countries have doubled Official Development Assistance (ODA) from developed countries. Ratha (2003) also observes that remittances have proved to be the most stable flow compared to ODA and private capital flows. Remittances, thus remain the third largest source of foreign exchange for Mexico after oil and tourism, such that a remittance of a dollar to Mexico produces an increase of about $2.90 in the Gross Domestic Product (GDP) and an increase of about $3.20 in economic output. Meyer (1998).

Unequivocally, remittances are not only used as a mechanism for the survival of the poor in developing countries, but also in a risk sharing mechanism, a stable source of investment and for future consumption smoothing (Ratha 2003). Taylor (2004) observes that the United States (US) always wants to make remittance flows to developing countries for developmental purposes, being a stable source of funding economies of these countries. In addition, remittance flows could be planned for consumption (by recipient households) as they are less volatile than those for investment. He, however implore migrants to strive to increase remittances during the time of economic problems especially in low-income countries where their families depend significantly on remittances as a source of income and living close to subsistence levels. Even when the purpose behind remittance is investment, remittances are less likely to suffer the sharp withdrawal that characterizes portfolio flows to other countries. There are numerous evidences to prove that remittances are increasingly used for investment purposes in developing countries, especially in low income countries. Several studies estimate that remittances from the United States are responsible for almost one-fifth of the capital invested in micro-enterprises in urban Mexico (Woodruff, Christopher and Zenteno, 2001). Similarly, in the Arab Republic of Egypt, a large proportion of returning migrants in the late eighties set up own enterprises using funds brought back from abroad, (McCormick, Barry and Wahba, 2002). Fayissa (2008) observes that remittances do positively impact on the economic growth of African countries. The impression from the study reveals that the conventional sources of growth through investment in physical and human capital and the ability of household to have the wherewithal of spending on health, housing, and other household items is not sufficient but also by strategically harnessing the contributions of remittances.

Remittances do respond to dramatic changes in economic adversity in recipient countries as well as clement economic climate. As low income countries lifted exchange rate restrictions and liberalized their current and capital accounts in the 1990s, remittance receipts rose sharply, and the volatility of remittances was used for investment purposes. The cross-country comparison reveals that remittances are affected by the investment climate in recipient countries in the same manner as capital flows. Countries that are more open than those that practice autarchy, trade/GDP or more financially deepened (M_2/GDP), often received larger remittances. Aside from the fact that remittances provide a significant source of foreign exchange, it could be used to finance imports, thereby contributing to a healthy balance of payments position.

It has also been noted that some emerging market economies prefer to use remittances as collateral against borrowing. (Nayyar, Deepak 1994). However, the study of remittances and their impact on household income, individual and household measures of poverty, their contributions to micro-enterprises, and their importance for the acquisition of economic and human capital has suffered some drawbacks. It has therefore been established through most research studies that "individual" or "family" remittances, or those remittances sent by an individual migrant directly to his or her family do not contribute to development because the greatest portion of such income is spent on consumption and very little is directed towards 'productive investment.' Developmental economists view remittances as a partial compensation for loss of labor and capital through migration which indirectly decreases home production and consequently reduces income through negative multiplier effect. The combined effect of this development could be a downward spiral in local economic activity.

3.0) Overview of Remittances Market in Nigeria

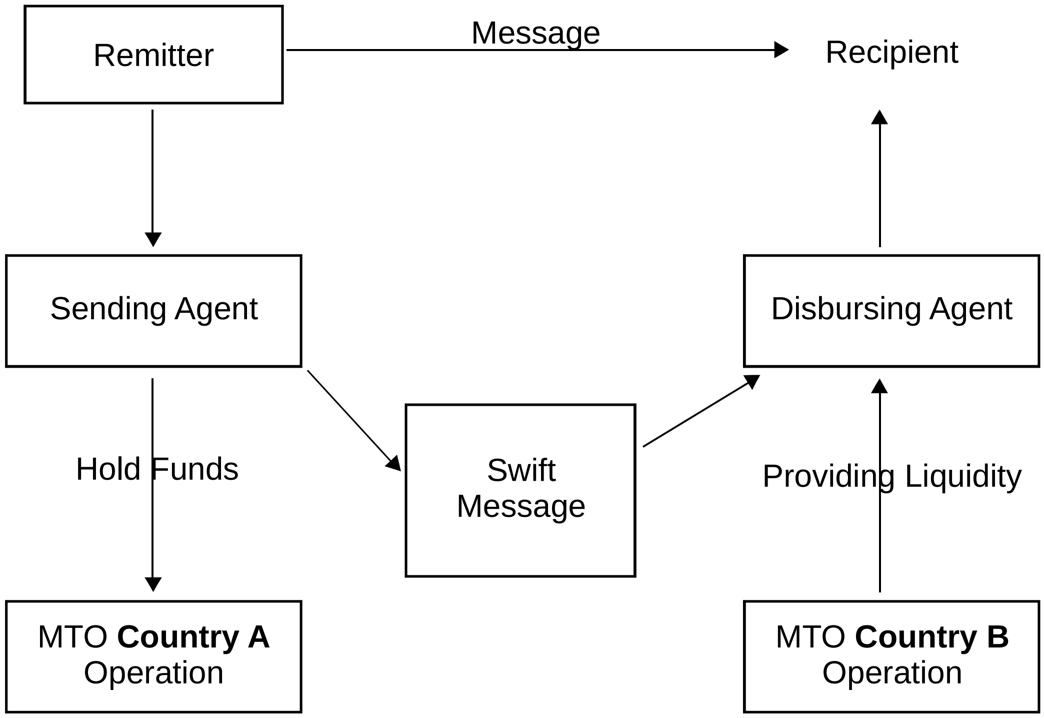
The global market place for remittance is scattered all over with different market shares in each region and among the sending countries. In some regions, such as Southern Europe, the most important players are banking institutions, while in other places like Nigeria and the Philippines, and some other developing countries, the main competitors are banks and postal agencies operating as money service providers. It is increasingly becoming competitive considering the incentives offer to recipients, though there is substantial scope for improvement. From indication, the sheer size of the market continues to attract new entrants into the market and nearly all the banks have hooked up with the remittance service providers.

Despite the

competitiveness, non-banks and informal channels remain robust as evidence has shown that they may be expanding their share of the market if government fails to take decisive step in redeeming the situation. However, the remittance market represents the total funds sent by individuals resident in abroad through both formal (i.e banking system) and informal (i.e Alternative Remittance System) channels. The attractiveness of either system is predicated on a number of factors which include among others: the cost of transactions, speed, security of funds, geographic proximity/accessibility, convenience in terms of familiarity and language. A formal remittance operation has been initiated by remittance service providers collecting funds from remitters through the use of different instruments. The common instrument is cash while other instruments in use include direct debits, cheques, money orders, and credit card. Certain communication is expected to take place between the agent and the remittance service through a dedicated computer system, e-mail, fax or telephone. The message is pass-through a special device known as Society Worldwide Inter-bank Financial Transaction (SWIFT), a proprietary database, fax, e-mail or phone. The time it takes to move funds from one point to another is instant.

Of all the money transfer mechanisms, the Western Union money transfer (WU) appears to have the largest worldwide presence in the industry. Other companies like Thomas Cook and Money Gram operate in tandem, though with a lesser presence than Western Union. While Western Union conducts almost three-quarter of all transactions through financial institutions in most of the corridors, Money Gram serves as second largest remittance company in the world after Western Union. Other formal intermediaries such as banks and the postal office play a small role in these corridors. However, the presence of formal channel of money transmission is making it feasible to determine the volume of funds transferred from the sending country to the recipient country at a given point in time. This is in contrast to informal channels which pose a particular risk of misuse of remittances for money laundering and possible financing of terrorism. It has been established that the predominance of informal cash transfers is largely dependent on personal relationships between the remitter and the fund provider. This could be through business people, courier companies, friends, relatives or oneself. Various studies have shown that the growing propensity to remit through undocumented or informal channel remain higher than formal channel in developing countries. This could be as a result of the stringent banking and foreign exchange regulations, low outreach, and insufficient protections to recipients, among others. Unlike the formal system, customers are not required to have a banking account or any knowledge of operating one. In fact, most of the illegal migrants prefer to send money informally. There is, therefore, the increasing need for service providers to correct the weaknesses in the formal sector and strive to raise competitiveness towards attracting larger share of remittance flows.

Fig 1: **ELEMENT OF REMITTANCES OPERATION**



In Nigeria, the demographic remittances environment showed a population of about 145 million as at 2007, the same level as in the preceding year. It is however projected to grow at an average rate of 2.6 per cent. Thus the population density of the country remains at 159 persons per square kilometer and its labor force remains steady at 53 million or 36.6 per cent. About 49 per cent represents urban population with age dependency ratio of 0.89. The country's poverty headcount ratio to national poverty line is 71.2 per cent, while the Gross National Income (GNI) per capita as at the same period is put at $103 and a record of 6.1 per cent GDP growth rate. Total number of emigrants is about 836,832 or 0.6 per cent of total population (table 1). However, the number of emigrants has ballooned in size as a result of the rising rate of unemployment in the country. This scenario has caught the attention of high level policy makers in the country as it has both positive and negative implications for the economy.

From the preliminary survey conducted by Research Department of the Bank in 2007, the Western Union (WU) money transfer commenced operation in Nigeria in 1996. It has since dominated the international MTOS as its market share stood at 55.5 percent, followed by Money Gram with 22.2 per cent. The third in the series is Travelex at 11.1 per cent, while other MTOs such as Vigo Remittance Corp, Coin-star and Money Exchange SA had a market share of 3.7 per cent each. Other formal intermediaries such as non-banks and the postal office play a small role in these corridors.

Remittance flows to the world were estimated at $337 billion in 2007, of which $251 billion was remitted to developing countries, $33 billion to low income countries, $218 billion to Middle Income

Countries (MICs), $140 billion to Lower MICs, and $78 billion to Upper MICs. The amount remains higher than the level of the Official Development Assistance (ODA). Others namely High Income Organization of Economic Cooperation and Development (OECD) and non-OECD reported $81 and $5 billion, respectively in 2007 compared to $72 and $4 billion in 2006. This could be attributed, in part, to the growing interests of migrants in sending more money home and, in part, due to improvement in the reporting system. Overall, Nigeria is among the top recipient countries after India, China and Mexico, and the Philippines. The share of remittances in total GDP rose throughout the period under review except for 2003 when it declined sharply from 2.1 to 1.4 per cent (table 3). It could be inferred that the depreciation of the dollar helped to raise the value of remittances from the Europe to developing countries. In addition, the growth in migrant stocks due to increased globalization and an increase in migrant incomes contributed to higher share of remittances. However, the official reports of remittances appears to have been underestimated because migrants still make increasing use of unofficial channels to send money home, and are not in anyway accounted for in the computation of remittances.

Recent studies further showed that a large number of Nigerians serve in different parts of Europe resulting in a very wide range of income and remittance potential. Most Nigerians are also present in significant numbers in North America, the Middle East and both high income and developing Asian countries. Evidence also revealed that the chunk of remittances to Nigeria were from the United States (US), representing about 54.0 per cent, followed by the United Kingdom (UK) and Canada. It has also been established that Nigeria is the leading recipient of remittances in sub-Sahara Africa (SSA) countries. They receive about 45.5 per cent of officially recorded remittance flows to the low income region and about 4.5 per cent of global remittance flows. Available data from the Central Bank of Nigeria (CBN) also indicates that remittances through the banking system was US$1.62 billion in 2000 but later increased to $10.7, thereafter estimated at $15 billion in 2007. Given this outlook, Nigeria's remittance to GDP was higher than other financial flows particularly, Foreign Direct Investment (FDI) and portfolio investment as well as non-oil exports. Just as is the case for “other countries” in the region; underreporting of remittance flows to Nigeria is still very observable because of data collection deficiencies and the prevalence of informal transfer mechanism, which accounts for about 50.0 per cent of total flows to the country.

Overall, remittances are by far the largest source of foreign exchange earnings and make up a significant share of gross domestic product (GDP). Considering the evolution of remittances and its measure in terms of GDP, remittances to Nigeria is bound to rise significantly if economic potentials is backed by sound socio-economic condition, stable political environment, a strong integrated financial system, efficient financial infrastructure, and reliable financial providers.

4.0) How Do Remittances Contribute to Economic Development in Nigeria?

In an attempt to discuss the impact of remittances on economic development in Nigeria, one is tempted to first of all provide an answer to the question of how remittances can be encouraged to achieving positive effects in the economy. It is simply to try to prevent, or at least, limit the possible negative consequences of remittances. And in the process of taking such step, concerted efforts should be made to enhance the ratio of officially transferred financial resources and at the same time ponder on how to increase the development efficiency of remittances. This is because the larger the resources of the Diaspora saved or invested for economic expansion, the better for the country particularly, if official remittances derived from the recipient countries are properly harnessed. This is expected to enhance the chances of moving the economy on the path of sustainable growth.

Aside from the critical role of remittances in countries' economic development, they also serve as a potential for increasing externally generated fund through economic diversification, allowing migrants and their families to invest in social activities such as education, building houses and creating avenue for reducing poverty levels. Analysts have noted that there is hardly any causal relationship between inflows of remittances and economic performance, but they tend to correlate. This is because the issue of developmental impacts of remittances is dependent not only on the continued flow and the ease with which money can be remitted to recipients, but also on market conditions, in particular the transaction costs. Ceteris paribus, if market conditions are stable, inflow of remittances is not only going to increase, but also spur economic growth. On the other hand, a weak market condition thus explains reasons why the remittance-induced growth impulses are not always transmitted to the national economy.

Another positive effect of remittances is its potential to augment individuals' incomes and increase the recipient country's foreign exchange reserves. An access to foreign exchange earnings provides valuable support to balance of payments accounts and help development through importation of essential goods. Whether or not the foreign exchange will actually be spent on imports essential for development is, of course, a key issue. This is because the additional foreign exchange earnings through this source could be squandered away by superfluous spending of the government on luxury projects or on ostentatious private consumption. If this happens, it may have high withdrawal or negative multiplier effects on the economy and consequently worsened balance of payments difficulties. It could also lead to an appreciation of the external value of the country's currency, a variant of Dutch disease. The appreciation of the currency makes exports more expensive in foreign markets and shift resources from tradable to non-tradable goods, thereby slowing down growth in employment and pressure emigration further. However, with regard to the on-going trade policy reforms in the international scene, remittances may help in improving foreign exchange difficulties in countries, particularly if it is used to propel output growth. In the same vein, if these resources are used for consumption, it could in turn generate positive multiplier effects, (Stahl and Arnold 1986).

Adelman and Taylor, (1990) found out in their studies that every dollar received from migrants working abroad leads to increase in Gross National Product (GNP). Similarly, the household survey conducted in Pakistan in the late 1980s and early 1990s showed that the marginal propensity to save generates higher income multiplier effect from international remittances than from domestic urban-rural remittances. Data available showed that Nigeria has indirectly used remittances to generate sufficient growth in the economy when one considers the contribution of remittances to economic growth. However, the country needs to intensify efforts at harnessing remittances for improved economic development. In terms of the proportion of remittances in total GDP, the country recorded a mere growth of 0.4 per cent in 1996 but later soared to 8.5 per cent in 2007. The analysis of the growing trend in remittances is better appreciated when compared with other financial flows. In comparison with other flows particularly FDI and portfolio investment to GDP, it thus fluctuates between 0.8 per cent in 1996 to 3.3 per cent in 2007, and 0.1 per cent and 2.5 per cent during the comparable period. On the other hand, the share of non-oil exports receipts to GDP was relatively low as it only accounted for less than 1.3 per cent throughout the period. However, the ratio of oil exports to GDP was quite substantial reflecting higher contributions than remittances. This justifies the argument that inflow of remittances could surpass oil export earnings, if improved incentives are made to encourage its flow to the country.

Nigeria could use the flow of remittances to raise additional funds in the world capital market as was experienced in countries such as Brazil, El Salvador, Mexico, and Turkey. In these countries, remittances were used as collateral to raise funds in the international capital market. Studies have shown that remittance flows are highly stable and predictable resource and a such they can be used as collateral and leveraged to provide alternative development finance institutions access to commercial credit and the capital markets, which if judiciously disbursed will impact positively on the economy of the recipient country. On the contrary, remittances could have an adverse effect on the economy, if not motivated by altruism and where increased remittance income undermines the recipients' zeal to work. Where remittances are characterized by high volatility, the country might find it difficult to generate sufficient financial assets needed to grow the economy. Therefore, a dramatic fall in remittances does not only affect national economies but also the individuals who depend on money transfer from abroad.

Remittances could play a major role in economic development, if the financial industry provides the majority of household access to simple deposit account opening for recipients of remittances from abroad. With such technical innovation, radical shift from informal to more formal channels will be highly experienced. The available funds can then be deployed to develop the grass root institutions that serve the poor in the country. The influence of remittances on Small and Medium Industry and Microfinance cannot be exaggerated because they are basic ingredients of strengthening the institutions as bedrock for economic development. This will further help in reducing poverty and improving the investment climate of recipient countries.

Several arguments have

been put forward on the implications of excess reliance on remittances. While some analysts felt that remittances, unlike other type of financial flows, do not have a negative effect on a country's competitiveness, (Rajan and Subramanian, 2005), but carry the potential risks of encouraging corruption or wasteful spending. Others view that remittance flows do support the overall balance of payments position but tend to reduce incentives to implement economic reforms. However, the overall argument here is that excessive reliance on remittances has its own associated peril. Its sudden changes in receipts could make the economy unduly vulnerable, hence not often advisable. Thus, the positive effects of remittances hitherto identified could be disenchanted if they are used mainly for ostentatious consumption in remittance-receiving country and importation of luxury goods, thereby worsening the country's balance of payments difficulties. Similarly, remittances could dampen the country's export, if they lead to an appreciation of the external value of the country's currency, a variant of Dutch disease. The appreciation of the currency can make exports more expensive in foreign markets and shift resources from tradable to non-tradable goods, thereby slowdown growth in employment and pressure emigration further.

5.0) Policy Recommendations

One of the key challenges that Nigeria is currently facing with the substantial inflow of remittances is how to manage this resource for veritable programmes that will be of benefit to the Nation. Effective implementation of such programmes is expected to contribute to poverty reduction and spur economic growth. It therefore calls for appropriate policies that would influence migrants' decision to remit money back home for economic use. Such policy should aim at encouraging migrants to increase their flows to their countries for developmental benefits. For remittances to serve as a veritable instrument for economic development in Nigeria, government may have to adopt the following measures:

- To implement a practical agenda that would reflect the needs of senders and recipients in the country. And for any development agenda for remittances to be realistic, it is imperative to encourage Development Banks to play a major catalytic role in optimizing the remittance markets. Optimization of remittance flows should go beyond merely inducing the sending countries to reduce the cost of transaction, but involve the enhancement of factors such as convenience, safety, regulatory compliance and positive development impact to attract larger flows of financial resources than would otherwise be the case. Optimization should focus more on improving “formal” channels to both senders and receivers so that the market share of “informal” or “ alternative remittance system” is brought down through market forces. Since informal systems are opened to fraud and abuse, financial service providers should collaborate to address it aggressively so as to bring to an end the issue of image tarnishing.
- The need to accelerate the use of non-cash payment mechanism

so as to make remittance flows unattractive to criminals, and more economically efficient. The conversion of remittances into deposit money or money purpose card accounts will go a long way in helping to accelerate the use of formal channels in developing countries and possibly lessen the attraction of informal use. The use of official transfer channels cannot be overemphasized but achievable, if appropriate incentives are offered to recipients to save more within the formal banking sector. To make formal transfer increasingly attractive, the government should continue to offer favorable exchange rates, call for reduced transmitter costs, improved institutional framework and establish efficient banking systems

- Intensive research and education programmes, as well as outreach and consumer protection are active ways of preventing fraudster from taking undue advantage over the recipients. Nigeria government should mount pressure at ensuring effective security against loss of property and valuables
- The need to leverage remittances for Small and Medium Enterprises (SMEs) development and Microfinance is important. The grass root institutions that serve the poor in providing efficient remittances services linked to tailored financial products (deposit, savings investment and insurance) should be adequately empowered. Therefore, creating an enabling environment is central to remittance institutional strengthening program. An efficient service company to run technology and treasury for thrift, rural and micro finance banks should be given a boost. The recent conversion of the Microfinance Institutions (MFIs) into regulated financial institutions is a credible and plausible policy. Since the microfinance institutions are set up to create opportunities for the poor, they could be allowed to access remittance funds. The authority could then use remittance float to create a zero cost pool of funds for lending to MFIs. A dedicated and customized remittance platform and a marketing channel should be provided. Government should also provide subsidized credit facility to these institutions so as to enable them contribute significantly to the development of the SMEs and consequently, the economy. There is therefore the need for the government to improve small microfinance loan eligibility by increasing depository and client base through remittance offering
- Since the existing regulatory framework has failed to guarantee increased market participation in the remittances environment, there is need for an enabling regulatory environment for remittance service to strive. Having observed a relatively fewer number of international banks showing interest in developing specialized remittance products in Nigeria, there is the need to initiate more stringent regulations for money transfer operations from the regulators. Good regulations and administrative guidelines are required

for effective financial operations, which will in turn encourage people to make more use of formal channel. Enhanced transparency that will result from good regulations will help to deter any abuse of the systems and in turn assist policy makers to gather accurate data required for economic planning.

- The government should create increased access to financial infrastructure by making it easier to obtain licenses from the monetary authorities. In addition, they should provide identification facility that would help to minimize the rate of fraud. The payment system infrastructure that has the potential to increase the efficiency of remittance services should be improved upon. Therefore, competitive market conditions, including appropriate access to domestic payment infrastructure should be fostered in the remittance industry. The remittance services should be supported by appropriate governance and risk management practices. It should be given a sound, predictable, non-discriminatory and proportionate legal and regulatory framework.
- The current initiative by the Department for International Development (DFID) to partner with the government in the country of origin should be pursued with vigor. This will go a long way in reducing the cost of remittances and enhancing the impact of the flows in the lives of recipients. This collaboration will help to facilitate the introduction of more remittance products, increase competition, improve transparency, influence policy by addressing legal constraints to remittance flows between major developed countries and developing countries, and build the capacity of the remittance-receiving institutions in the recipient countries. However, the success of these initiatives depends on the commitment of both governments towards developing effective policies framework for improving remittance landscape
- Government should reach out to Home/Village Town Associations (HTAs) including rural areas by supporting their efforts with adequate incentives and create opportunity for matching funds with credit programme. Experiences of countries have provided insight into the ways in which resources of migrants can be mobilized for local development in the home country. Migrant associations in host country should be established and backed by law. With this approach, they will be able to play an active role in financing projects that will improve the living conditions of the communities and provide development in the home country. In addition, it will enable the society to leverage the collectively pooled funds to support development projects especially on local infrastructure
- An entrepreneurship development scheme for return-migrants should be fostered. The guiding of return-migrants on how to set up their businesses is a critical area that should be looked into by the authority. This is because the ability to identify and develop a project, as well as the

managerial skills required to execute the business need to be guided with practical demonstrations and physical support. In other words, rather than focusing on "migrant-specific" investment programme, recipient countries could tailor its micro-finance institutions to capture remittances, which will in turn be channeled to investment ventures for economic development

! Given that remittances are private flows, it is imperative that any initiatives from the government should focus more on the private sector. Therefore, planned incentives should be targeted at facilitating the development of transfer mechanisms for remittances and promoting investments and new economic activities by the Nigeria's Diaspora. Though the framework might include actions towards strengthening the institutions for remittance transfers, promoting access to finance and implementing financial literacy program for migrants, it should be tailored to private sector needs, and

! Increased collaboration between the various financial operators and the monetary authority is necessary. This could be instituted by way of creating an Association of Remittance Operators (ARO) with appropriate legal backing. This will further increase the driving force for remittance mobilization into the country and consequently help in deploying the resources into economically viable projects.

6.0) Summary and Conclusion

There is no doubt that the global financial imbalance among countries is discernible and reversible through mobilization of external funding for economic development. Of the international financial flows to developing countries, remittances constitute one of the stable and predictable sources used for realizing developmental needs of most recipient countries. In spite of the growing importance of remittances in global capital flows and economic development, the place of remittances is still being underestimated as little attention is being given by less developed countries. Even where remittances are glaring, basic information on them are not fully available to enable countries plan ahead for economic growth. Most devastating is the inaccurate data on remittances which are doubtful because of the problems of maintaining records of transactions that pass through official channels. Consequently, the lack of data availability on number of migrants in relations to remittances make planning difficult and impracticable to factor remittances into policy consideration. It has also been one of the causes of inconclusive empirical results in most remittance studies.

Country experiences have clearly shown the increasing role of remittances in achieving Millennium Development Goals (MDGs) and as such remittances are viewed as developmental strategy. In fact, the failure of development strategy is being viewed as the driving force for remittances because it has made intending migrants to seek for succor. In the recent past, the flow of remittances has generated a strong impact on the communities of many countries in particular India. The development has created a major difference between countries with a high rate of remittances as opposed those with meager remittances. For remittances to serve as a tool for development, it is critical to consider among others: the regulatory environment, develop entrepreneurship scheme for return-migrants, create incentives to encourage private sector flows, apply appropriate technology provide efficient remittance services linked to tailored financial products, strengthen infrastructure technology to support remittance services and increase focus on possible means of reducing transaction costs as well as exchange rate losses. Another promising ways are to link both banks and postal agencies including microfinance institutions together so as to facilitate remittance services and its utilization. Other recommendations include the need to promote fair competition and pricing, and seek partnerships and alliances including linkages between money transfer companies and other financial institutions thereby expand financial services. Governments and other public and private institutions may help to design a framework through which the positive aspects of the remittances and development can be strengthened and the negative ones reduce in impact.

Contrarily, remittances do have indirect impact on development especially where the dependency level is high. One of the disturbing effects of such development is that it dampens the morale of the remitter to work harder for survive. Not only having this effect, it could also lead to a Dutch Disease phenomenon of overvalued real exchange rates, loss of export competitiveness, over consumption, under investment thereby delay much needed policy reforms for economic development.

In conclusion, the paper seeks to examine how and to what extent remittances can be harnessed to promote economic development of the migrant sending country, it fails in its entirety to discuss effects of outflows of remittance on the country. However, one specific question that cannot be avoided even within the limited scope and in the context of the present study is: Do outflows of remittances hurt the economy of the host country? The question is quite important considering a series of argument put forward by some analysts stating that outflow of remittances is indeed a drain on the country's economy with an adverse effect on external balance of payments position. Since the view is seemingly valid, it could be a strong argument against remittance outflows. It, thus, has a long run effects on the country's balance of payments positions. However, this concern is not unexpected but need to be discussed extensively using macro econometrics techniques.

APPENDIX 1: Definitions of the Remittance

Unless otherwise indicated, total remittances are computed as the sum of three items in the IMF's Balance of Payments Statistics Yearbook (BOPSY): “Workers' Remittances”, “Compensation of Employees” and “Migrant Transfers”.

Workers' Remittances (part of current transfer in the current account) are current transfers made by migrants who are employed and resident in another economy. This typically includes those workers who move to an economy and stay, or expected to stay, a year or longer.

Compensations of

Employees (part of the income component of the current account) instead comprises wages, salaries and other benefits (cash in kind) earned by non-resident workers for work performed for residents of other countries. Such workers typically include border and seasonal workers, together with some other categories e.g. local embassy staff.

Migrants' Capital Transfer (part of the capital account) includes financial items that arise from the migration (change of residence) of individuals from one economy to another.

Table 1 Appendix II
SELECTED DATA ON DEVELOPING COUNTRIES (2006)

	Developing Countries	Sub-Saharan Africa	Low Income	Nigeria
Population	5,489	770	2,403	145
Population Growth avg. (1997/2006)	1.4	2.5	1.9	2.6
Labor Force (million)	2,569	317	991	53
Urban Population (%)	43.9	35.9	30.4	49
Age Dependency Ratio	0.57	0.88	0.69	0.89
GDP Growth rate	6.1	4.9	6.8	6.1
GNI per capita ($)	2,000	668	1,580	103
Poverty Line (% of pop)	na	41.1	na	71.2
Stock of Emigration(million)*	145	15.9	43.5	836,832

* 2005
Source: World Development Prospects Group, World Bank

Table 2 Appendix III
REMITTANCE INFLOWS TO DEVELOPING COUNTRIES

(US$ billion)	2002	2003	2004	2005	2006	2007	Change Btw 2006-2007	Change Btw 2002-2007
Developing Countries	116	143	163	194	226	251	11%	118%
East Asia & Pacific	29	35	39	47	53	59	11%	100%
Europe & Central Asia	14	16	23	32	39	47	22%	246%
Latin America & Caribbean	28	35	42	48	57	61	6%	117%
Middle East & North Africa	15	20	23	24	27	29	8%	89%
South Asia	24	30	29	33	40	44	11%	82%
Sub-Saharan Africa (SSA)	5	6	8	10	11	12	7%	132%
Low Income Countries	15	17	20	24	29	33	15%	118%
Middle Income Countries	100	127	143	170	197	218	11%	118%
Lower MICs	70	89	95	110	127	140	10%	99%
Upper MICs	30	38	48	60	70	78	11%	162%
High Income OECD	53	61	67	68	72	81	12%	54%
High Income non-OECD	1	2	3	4	4	5	7%	304%
World	170	206	234	266	303	337	11%	99%

Source: Based on Data from IMF Balance of Payments Statistics Yearbook 2007

Table 3
Appendix IV
CONTRIBUTIONS OF REMITTANCE FLOWS TO NIGERIAN ECONOMY

	2002	2003	2004	2005	2006	2007e
Remittances ($ billion)	1,349.8	1,061.7	2,262.3	6,475.8	10,577.1	15,000.0
Remittances per person	11.3	8.9	18.9	54	73	103.5
Population (million)	120	120	120	120	145	145
GDP current basic prices						
(N billion)	7,795.8	9,913.5	11,411.1	14,572.2	18,067.8	22,638.8
GDP current basic prices						
($ billion)	6,442.8	7,661.1	8,547.6	11,022.8	14,038.7	17,755.9
Exchange Rate (N/$)	121	129.4	133.5	132.2	128.7	127.5
GDP growth rate	4.6	9.6	6.6	6.5	5.6	6.2
Annual growth rate of Remittances	9.1	-21.3	113.1	186.2	63.3	41.8
Total remittances as a % of GDP	2.1	1.4	2.6	5.9	7.5	8.5

E: estimates
Source: Author's Calculation

Table 4 Appendix V
Ratios of Selected Financial Flows to GDP in Nigeria

Year	PERSONAL HOME REMITTANCES	FOREIGN DIRECT INVESTMENT INVESTMENT	PORTFOLIO EXPORTS RECEIPTS	OIL EXPORTS RECEIPTS	NON-OIL
1996	0.4	0.8	0.1	8.4	0.2
1997	0.9	0.8	0.0	7.6	0.2
1998	0.8	0.6	0.0	4.6	0.2
1999	2.3	1.9	0.0	24.5	0.4
2000	2.4	1.7	0.7	28.2	0.4
2001	2.0	1.9	1.3	28.0	0.4
2002	2.1	2.8	0.3	20.7	1.2
2003	1.4	2.6	0.2	29.6	0.9
2004	2.6	2.1	0.2	38.6	1.0
2005	5.9	2.0	2.5	42.3	0.7
2006	7.5	3.2	0.6	31.1	0.7
2007e	8.5	3.3	0.8	33.3	0.9

E:estimate
Source: Central Bank of Nigeria.

Appendix VI

Top ten remittance recipients in developing countries in 2007 are India ($27.0 billion), China ($25.7 billion), Mexico ($25.0 billion), Philippines ($17.0 billion), Romania ($6.8 billion), Bangladesh ($6.4 billion), Pakistan ($6.1 billion), Indonesia ($6.0 billion), Egypt, Arab Republic ($5.9 billion) and Morocco ($5.7 billion).

Top ten remittance recipients in low income countries in 2007 are: India ($27.0 billion), Nigeria ($15.0 billion), Bangladesh ($6.4 billion), Pakistan ($6.1 billion), Vietnam ($5.0 billion), Nepal ($1.6 billion), Kenya ($1.3 billion), Yemen Republic ($1.3 billion), Tajikista ($1.3 billion), Haiti ($1.2 billion).

REFERENCES

Adams, Richard H. Jr. (1993). "The Economic and Demographic Determinants of International Migration in Rural Egypt". *Journal of Development Studies* Vol 30 (1) pp. 146-67.

Adelman, Irma, and J. Edward Taylor. (1990). "Is Structural Adjustment with a Human Face Possible? *The Case of Mexico." Journal of Development Studies*. Vol 26, pp. 387-407.

Chami, R. Fullenkamp, C. and Jahjah, S. (2005). Are Immigrant Remittance Flows a Source of Capital for Development?, IMF Staff Papers, Vol. 52, No. 1

Elbadawi, I. A. and Rocha, R. (1992). Determinants of Expatriate Workers' Remittances in North Africa and Europe, Working Paper WPS 1038, Country Economics Department, The World Bank, Washington, DC.

El-Sakka, M. I. T. and Mcnabb, R. (1999). The Macroeconomic Determinants of Emigrant Remittances, World Development 27 (8), pp. 1493-1502.

Faini, R. (1994), WorkersMeyers, D. S. et. al. (1998). "Migrant Remittances to Latin America: Reviewing the Literature", in Inter-American Dialogue, The Thomas Riviera Policy Institute.

Fayissa, B. and C. Nisiah (2008). "The Impact of Remittances on Economic Growth and Development in Africa", Unpublished paper, Middle Tennessee State University.

Lucas, R. E. B. and Stark, O. (1985). Motivations to remit: Evidence from Botswana. Journal of Political Economy 93(5): 901-917.

Maimbo, S. and D Ratha (2003). Remittances: Development Impact and Future Prospects Washington, D.C , World Bank.

McCormick, Barry, and Jackline Wahba. (2000). "Return Migration and Geographical Inequality: The Case of Egypt." Unpublished paper, University of Southampton.

Nayyar, Deepak. (1994). Migration, Remittances and Capital Flows: The Indian Experience. Delhi: Oxford University Press.

Rajan, R. and Subramanian. (2005). "What Prevents Aid from Enhancing Growth", (Unpublished), Washington, D. C., IMF.

Rapoport, H. and F. Docquier. (2005). "The Economics of Migrants' Remittances", Handbook on the Economics of Reciprocity, Giving and Altruism, forthcoming.

Ratha, Dilio. (2003). "Workers' Remittances: An Important and Stable Source of External Development Finance," in a Global Development Finance: Striving for Stability in Development Finance Ch 7: pp. 157-175 (Washington D.C. World Bank).

Russel, S. (1986). "Remittances from International Migration: A Review in Perspective" World Development, Vol. 14, No. 6, pp. 677-696.

Stahl, Charles W., and Fred. Arnold. (1986). "Overseas Workers' Remittances in Asian Development". International Migration Review 20(4): pp 899-925.

Swamy, G. (1981). "International Migrant Workers' Remittances: Issues and Prospects" World Bank Staff Working Paper, No 481. Washington, D. C. World Bank.

Straubhaar, T. (1986) "The Determinant of Workers' Remittances: The Case of Turkey", weltwirtschaftliches Archiv, 122(4): 724-740.

Taylor 2003 J (2003). Migration and Incomes in Source Communities: A new economics of migrateon perspectives from China: Economic Development and Cultural Change, 52(1): 75-101

Todaro, M. P. (1969). "A Model of Migration and Urban Unemployment in Less Developed Countries", The American Economic Review, Vol. 59, pp. 138-48.

Wahba, S. (1991) "What Determines Workers' Remittances?" Finance and Development, 28: 59 88, December.

World Bank. (2001) Global Economic Prospects 2002. Washington, D.C.

World Bank, (2006) "Global Economic Prospects 2006: Economic Implications of Remittances and Migration".

Woodruff, Christopher, and Rene. Zenteno. (2001). "Remittances and Microenterprises in Mexico". Unpublished paper University of California, San Diego.

Bank Post- Consolidation Issues And Challenges In Malaysia And India: Lessons Of Experience For Nigeria

By U. Kama*

1.0 Introduction

The financial services industry is restructuring and consolidating at an unprecedented pace around the globe, particularly in the developed and the emerging market economies, owing mainly to the increasing wave of globalization, structural and technological changes, as well as the integration of financial markets. For instance, in the USA, since 1979, there has been well over 3,500 mergers in which two or more banks were consolidated under a single bank charter and more than 5,800 acquisitions in which banks retained their charter but were bought by a different bank holding company. In 1998, a merger in France resulted in a new bank with a capital base of US$688 billion, while the merger of two banks in Germany in the same year created the second largest bank in Germany with a capital base of US$541 billion. In Japan, a merger had produced the new Tokyo-Mitsubishi bank with over $700 billion in assets.

In most of the emerging market economies, including India, Malaysia, Argentina, Brazil and Korea, consolidation has also become prominent, as banks strive to become more competitive and resilient to shocks as well as reposition their operations to cope with the challenges of the increasingly globalized banking systems. In these economies, the banking systems were before the reforms characterized with vulnerability to systemic distress and macroeconomic volatility, making policy fine-tuning inevitable. As McKinnon and Shaw (1973) observed in their seminar work on the key roles of banks as propellants of growth and development in developing economies, "a feeble banking system is repressive, distortionary and dis-connects the intermediation process thereby precipitating macroeconomic instability" . This requires that policy makers, as Nnanna (2005) opines, articulate robust policies that will deepen the financial system to enable banks play their roles most efficiently.

Consequently, the banking system reforms in these economies were focused on liberalization of banking business through mergers and acquisitions (consolidation) in most

* **Mr. Kama** is a Principal Economist in the Financial Analysis Division of Research Department of the Central Bank of Nigeria, Abuja.
The views expressed in the paper are those of the Author and do not in any way represent the views or thinking of the Central Bank of Nigeria.

cases which threw up a lot of challenges for the industry and the economies at large.

This paper critically reviews the issues and challenges that faced the post-consolidation exercise in both India and Malaysia as well as the lessons of experience Nigeria could draw from them.

The paper has six main sections. Following this introduction is section two which gives an overview of the bank consolidation exercises in both Malaysia and India, while section three discusses the post-consolidation issues and challenges in the two countries. Section four examines the lessons of experience for the Nigeria's post-consolidation banking industry. Section five presents the concluding remarks.

2.0 Overview of Bank Consolidation in Malaysia and India

2.1 Bank Consolidation in Malaysia

The Malaysian financial sector consolidation can be traced back to the 1997-1998 East Asian financial crisis that left many Malaysian banking institutions with high levels of non-performing loans (NPL) (BNM Annual Report, 1999). The Bank of Negara Malaysia (BNM) resorted to capital injection and removal of problem loans from banks' books to special-purpose government vehicles to stem bank failures. It was later realized that a longer-term solution lay in the consolidation of the banks. Initially, only 2 severely weakened banking groups were merged towards the end of 1998 to stem systemic risks in the financial system. The financial sector gradually removed barriers to entry for foreign entities under the ASEAN Framework Agreement on Services and the General Agreement on Tariff (GAT) on Trade and Services (BNM Annual Report, 1999). The foreign banks stood ready to capture significant market shares as domestic banks were engrossed in managing loan losses. In 1999, the BNM extended the bank consolidation program to include the entire domestic financial sector. Banking institutions were given the liberty to form their own merger groups and to elect their own leaders to lead the merger process. Approval was granted for the formation of 10 equity of RM 2 billion and an asset base of RM 25 billion (BNM Annual Report, 1999). Over a period of only two years, BNM facilitated the merger of 58 financial institutions comprising commercial banks, merchant banks and finance companies into 10 domestic anchor bank groups with 13 foreign banks.

As a result, extensive nationalization of common functions was carried out (Aziz, 2002). Credit growth rose strongly, largely due to demand side factors owing to strong credit demand in response to the low interest rate environment (BNM, Annual Report 2000). Significant amounts of distressed assets were removed from balance sheets in addition to Tier 1 capital injections conducted by the central bank.

2.2 Bank Consolidation in India

India embarked on a strategy of economic reforms in the wake of a balance-of payments crisis in 1991. The central plank of the reforms was in the financial sector. Reforms were simultaneously undertaken in all the segments of the financial markets to enable the banking sector to perform its intermediation role in an efficient manner. The thrust of these reforms was to promote an efficient and competitive financial system with the ultimate objective of improving the allocative efficiency of resources through operational flexibility, improved financial viability and institutional strengthening. The reform measures in the financial sector were envisaged along the following lines:

First, reform measures were initiated and sequenced to create an enabling environment for banks to overcome the external constraints. These were related to administered structure of interest rates, high levels of pre-emption in the form of reserve requirements, and credit allocation to certain sectors. Sequencing of interest rate deregulation was an important component of the reform process which impacted greater efficiency to resource allocation. The process was gradual and was predicated upon the institution of prudential regulation for the banking system, market behaviour, financial opening and, above all, the underlying macroeconomic conditions. The interest rates in the banking system were largely deregulated, except for certain specific classes such as savings deposit accounts, non-resident India (NRI) deposits small loans up to Rs.2 lakh and export credit. The needs for continuance of these prescriptions as well as those relating to priority sector lending were flagged for wider debate in the latest annual policy of the RBI. However, administered interest rates still prevailed in small savings schemes of the Government.

Second, as regards to the policy environment of public ownership, the lion's share of financial intermediation was accounted for by the public sector during the pre-reform period. As part of the reforms programme, initially, there was infusion of capital by the Government in public sector banks, which was followed by expanding the capital base with equity participation by the private investors. The share of the public sector banks in the aggregate assets of the banking sector came down from 90 per cent in 1991 to around 75 per cent in 2004. The share of wholly Government-owned public sector banks (i.e., where no diversification of ownership had taken place) sharply declined from about 90 per cent to 10 per cent of aggregate assets of all scheduled commercial banks during the same period. Diversification of ownership led to greater market accountability and improved efficiency. Following the reforms, infusion of funds by the Government into the public sector banks for the purpose of recapitalization amounted, on a cumulative basis, to less than one per cent of India's GDP, a figure that was much lower than that for many other countries. Even after accounting for the reduction in the Government's shareholding on account of losses set off, the current market value of the share capital of the Government in public sector banks had increased manifold and as such what was perceived to be a bail-out of public sector banks by Government turned out to be a profitable investment for the Government.

Third, one of the major objectives of banking sector reforms was to enhance efficiency and productivity through competition. Guidelines were laid down for the establishment of new banks in the private sector and foreign banks were allowed more liberal entry. By 1993, twelve new private sector banks had been set up. As already mentioned, an element of private shareholding in public sector banks was injected by enabling a reduction in the Government shareholding in public sector banks to 51 per cent. As a major step towards enhancing competition in the banking sector, foreign direct investment in the private sector banks was allowed up to 74 per cent, subject to conformity with the guidelines issued from time to time.

Fourth, consolidation in the banking sector was another feature of the reform process. This also encompassed the Development Financial Institutions (DFIs), which provided long-term finance, while the distinction between short-term and longterm finance provider increasingly become blurred over time. The complexities involved in harmonizing the role and operations of the DFIs were examined and the RBI enabled the reverse-merger of a large DFI with its commercial banking subsidiary which was a major initiative towards universal banking. Guidelines for mergers between non-banking financial companies and banks were issued, while those between private sector banks were also issued. The principles underlying these guidelines were applicable, as appropriate, to the public sector banks also, subject to the provisions of the relevant legislation

The unique features of the financial sector reforms were as follows:
First, financial sector reforms were undertaken early in the reform cycle. Second, the reforms process was not driven by any banking crisis, nor was it the outcome of any external support package. Third, the design of the reforms was crafted through domestic expertise, taking on board the international experiences in this respect. Fourth, the reforms were carefully sequenced in respect to instruments and objectives. Thus, prudential norms and supervisory strengthening were introduced early in the reform cycle, followed by interest rate deregulation and gradual lowering of statutory pre-emption. The more complex aspects of legal and accounting measures were ushered in subsequently when the basic tenets of the reforms were already in place.

Another unique feature was the reform of the public sector banks which dominated the Indian banking sector. These banks were recapitalized by government to meet prudential norms through issuance of bonds. The mechanism of hiving off bad loans to a separate government asset management company was not considered appropriate in view of the moral hazard. The subsequent divestment of equity and offer to private shareholders was undertaken through a public offer and not by sale to strategic investors. Consequently, all the public sector banks which issued shares to private shareholders were listed on the exchanges and were subjected to the same disclosure and market discipline standards as other listed entities. To address the problem of distressed assets, a mechanism was developed to allow sale of these assets to Asset Reconstruction Companies which were in private sector and operated as independent commercial entities.

In terms of the processes, certain interesting features of the reforms were in evidence. The first was its gradualism, wherein reforms were undertaken only after a process of closer and continuous consultation with all stakeholders. This participative process with wider involvement not only encouraged a more informed evaluation of underlying content of policies but also enhanced the credibility of policies and generated expectations among economic agents about the process being enduring in nature. The second was a constant rebalancing of reform priorities predicated upon the domestic and global business environment, institution of prudential practices, up-grading of the regulatory and supervisory framework, institution of appropriate institutional and legal reforms and the state of openness of the economy. The third important feature of the reforms was its harmonization with other policies dictated, among others, by the state of preparedness of the financial sector and above all, the underlying macroeconomic environment. Fourth, the reforms progressed with emphasis on the development of a system that was responsive to the needs of all sections of the society.

3.0 Post-Consolidation Issues and Challenges in Malaysia and India

3.1 Malaysia

Following the successful consolidation of the banking sector, efforts were shifted to building the domestic financial infrastructures. Ten (10) banking groups emerged from seventy-one (71) banks that existed in the pre-consolidation period in Malaysia. The consolidation exercise was a major structural enhancement of the financial system. Banking institutions attained a minimum capital size that was able to benefit from economies of scale and undertake the necessary investment in technology important to the industry.

A major transformation of the structure of financial intermediation was in terms of the deepening and broadening of the private debt securities market. In this regard, efforts were directed at promoting a robust domestic bond market that provided a competitive source of long-term debt funding and viable investment alternative for investors. The trading and information infrastructure was enhanced with the introduction of the fully automated system for tendering, bond information and dissemination system and real-time gross settlement system.

Another development in the financial landscape was the growing significance of Islamic Banking and Finance in the financial system. Islamic Banking strongly emerged as an efficient and effective financial intermediation channel, and formed an integral part of the overall Malaysian financial system. A comprehensive Islamic financial system covering banking, Islamic insurance, the money market and capital market, that operated in parallel with the conventional system existed in Malaysia. Islamic banking accounted for about 10 per cent of the market share of the total banking system.

Despite these positive outcomes of the consolidation exercise, a number of issues and challenges emerged in the Malaysian banking industry. Some of the issues and challenges were:

The Need for Microfinance Institutions to Reinforce Growth and Development:
As mega banks emerged in the economy following the consolidation exercise, there was need for the development of venture capital industry, a better framework for SME financing and the provision of micro-financing. This was to ensure that credit was made available to all the segments of the economy, as well as support the growth of new areas and industries.

Huge Investment required in ICT to Integrate and Upgrade Systems:
With the completion of the consolidation exercise, domestic banking institutions actively embarked on up-grading their systems, adopting new technologies, including product delivery, risk management and information systems. The adoption of new technologies in the Malaysian banking system was primarily to automate business processes and also to harmonise the different systems and solutions arising from mergers of many banks..

Competition Pressures:
The new financial landscape that emerged created the need for the banks to move towards strategic business differentiation among themselves in order to serve the relevant market segments as well as position themselves to face the emerging competition. Business delivery channels and processes were then reviewed to enhance efficiency levels and service quality to the customers. Many banks formed strategic alliances with partners to enrich their value proposition to their customers through cross-selling of products and services. Indeed, the Malaysian banking industry became more consumer-centric as several banking institutions embarked on customer relationship management systems to better understand the need of their customers in order to provide better levels of service and to gain a better understanding of their drivers of profitability.

Corporate Governance and Institutional Issues:
The new banking environment required greater levels of transparency and standards of disclosure, especially with the greater volume of transactions coming in the post-consolidation exercise. To address this problem, a hybrid approach was adopted by Malaysia which included Legal reforms, self-regulation as well as measures to encourage market-based regulation. New measures were introduced to further improve the level of governance among banking institutions. This includes limiting the number of directorships of chief executive officers, reviewing the responsibility and accountability of the board and management as well as requiring for the setting up of various board committees.

Enhancing Capacity in the Industry:
Arising from the experience of the Asian financial crisis, placing greater emphasis on enhancing the credit skills and the creation of a more robust credit culture in the industry became imperative in the new financial landscape. To that end, an accreditation process was introduced by the regulatory and supervisory authorities, aimed at better equipping credit officers with the required skills.

Consumer Awareness and Protection:
Another issue was how to raise the awareness of the public on their rights and responsibilities in relation to the new financial landscape in Malaysia. In this regard, a comprehensive 10-year consumer education programme was introduced. This was to raise consumer awareness and understanding on banking products and services and to educate the public on their rights and responsibilities in their relationship with a financial institution.

Reform of the Payments Systems:
A deliberate reform of the payments system was undertaken to ensure that the payment system was

stable and efficient. Bank Negara Malaysia implemented a real time gross settlement system known as RENTALS for inter-bank funds transfer to reduce the credit and settlement risk in the financial system. In addition, a range of retail payment systems was also implemented to further increase payments system efficiency through electronic channels, which included the introduction of inter-bank Giro, internet banking, mobile banking and electronic purse.

3.2 India

Post-Consolidation in India resulted in impressive institutional and legal reforms. A Board for Financial Supervision (BFS) was constituted comprising selected members of the RBI Board with a variety of professional expertise to exercise 'undivided attention to supervision'. The BFS, which generally met once a month, provided direction on a continuing basis on regulatory policies, including governance issues and supervisory practices. It also provided direction on supervisory actions in specifics cases. The BFS also ensured an integrated approach to supervision of commercial banks, development finance institutions, non-banking finance companies, urban cooperative banks and primary dealers. A Board for Regulation and Supervision of Payment and Settlement Systems (BPSS) was also constituted to prescribe policies relating to the regulation and supervision of all types of payment and settlement systems and also determined criteria for membership to these systems. The credits information companies (Regulation) Bill, 2004 was passed by both Houses of the Parliament, while the Government Securities Bills, 2004 was also passed. Certain amendments were considered by the Parliament to enhance Reserve Bank's regulatory and supervisory powers. Major amendments related to the requirement of prior approval of RBI for acquisition of five per cent or more of shares of a banking company with a view to ensuring 'fit and proper' status of the significant shareholders, aligning the voting rights with the economic holding and empowering the RBI to supersede the Board of a banking company. In addition, the efficiency and productivity of the system was improved through enhanced competition in the industry.

However, some issues arose from the post-consolidation exercise that needed to be addressed.

Corporate Governance and Institutional Issues: The first issue pertained to greater transparency and disclosure requirements in the post-consolidation industry. To address this problem, a number of measures for enhancing the transparency and disclosures standards were later introduced in the industry. For instance, with a view to enhancing further transparency, all cases of penalty imposed by the RBI on the banks as well as directives issued on specific matters, including those arising out of inspection were placed in the public domain.

As part of its efforts to improve corporate governance, the RBI focused on ensuring “fit and proper” owners, directors and senior managers of the banks. Transfer of share holding of 5 per cent and above required acknowledgement from RBI and such significant shareholders were put through a “fit and proper” test. Banks were also asked to ensure that the nominated and elected directors were screened by a nomination committee to satisfy the “fit and proper” criteria. Directors were also required to sign a covenant indicating their roles and responsibilities. The RBI issued detailed guidelines on ownership and governance in private sector banks emphasizing diversified ownership.

Ensuring a Safe and Sound Financial System:
The issue of ensuring the safety and soundness of the industry became prominent in the post-consolidation era in India. In order to address this problem, a set of micro-prudential measures were instituted by RBI to strengthen the banking system and also to ensure their safety and soundness with the objective of benchmarking against international best practices such as risk-based capital standard, income recognition, assets classification and provisioning requirement for non-performing loans as well as provisioning for "standard" loans, exposure limits for single and group borrowers, accounting rules, investment valuation norms, among others.

Robust Supervisory Framework:
As part of the efforts to ensure healthy and sound banking industry, there was the need to give greater attention to issues relating to the regulation and supervision of the industry. The RBI's process of regulation and supervision was strengthened. The strategy of on-site inspection and off-site surveillance mechanism together with greater accountability of external audit was instituted.

In tandem with the need to improve the prudential practices as well as the institutional arrangement to improve supervision, there was need to ensure that integrity of payments and settlement system was put in place. The legal environment for conducting banking business was also strengthened. Debt recovery tribunals were introduced exclusively for adjudication of delinquent loans. To combat the menace of crime-related money, a money laundering Act was enacted in 2003 to provide the enabling legal framework. The Credit Information Companies (Regulation) Act, 2004 was also enacted by the Parliament to enhance the quality of credit decision making.

4.0 Lessons of Experience for Nigeria
The question then is what lessons can Nigeria learn from the bank post-consolidation era in both Malaysia and India that would help in improving and strengthening the functioning of our banking industry? It should be realized that banking institutions, being the main providers of financing in the economy, need to assume a much greater role in contributing towards the long-term development, especially the small and medium-sized enterprises (SMEs). In an emerging economy like Nigeria, the traditional relationship between creditor and debtor has to evolve into business partnership whereby banking institutions are expected to play a more participative role in identifying gaps in processes, skills and expertise as well as usage of technology and assist in filling such gaps by providing funds to investors.

Arising from the experience of both India and Malaysia was issues of strong management teams in the banking industry. In Nigeria, Banks will require strong management teams that are committed to bringing about overall performance improvements and capacity enhancements. Paradigm shifts would mean that new strategies would have to be conceptualised and articulated to address the increasingly complex issues arising from the consolidation exercise.

In both countries, at the post-consolidation era, customers' expectations took quantum leap. In the same manner, Banking in Nigeria will no longer involve providing standard products to customers. In order to remain competitive as financial intermediaries, banking institutions would need to be sensitive to customer needs for greater efficiency and convenience. There would be need for financial products to be personalized and customized to the individual needs of corporate and retail clients. Banking institutions would therefore need to be more proactive and innovative in packaging and marketing their products. While customers will expect wider range of products to be offered, of greater importance is the banking institutions' ability to provide these products at competitive pricing.

Taking a queue from both Malaysia and India, the new financial landscape requires bank managements in Nigeria to re-examine their existing business models to see where their strengths lie, and to what opportunities these strengths can be applied to enhance returns. Specifically, there is need for the re-engineering of business processes and reassessment of business models by banks so as to fit in the new financial landscape as well as the need to move towards strategic differentiation among the banks in order to better serve the relevant market segment. This may involve market or functional specialization as banks decide which functional areas or combinations of risk management, customer services, product innovations, to exploit and maximize to their advantage.

Hitherto, training was viewed as costly and unnecessary expenditure by banks. The reforms in the banking industry has evolved a competitive process that only well motivated and trained employees would effectively contribute to value creation within the banks. The lesson here therefore is that only competence and commitment from the organization's workforce, and their continuing training and development, will real strategic change take place in the work processes.

Furthermore, with the completion of the consolidation exercise in Malaysia, domestic banking institutions actively embarked on up-grading their systems, adopting new technologies, including product delivery, risk management and information systems. The adoption of new technologies in the Malaysian banking system was primarily to automate business processes. In the same manner, the evolving financial landscape in Nigeria following the consolidation exercise would require the adoption of high technology systems that would facilitate the achievement of new levels of operations in order to meet the needs of customers. This will translate into new products and innovations in order to harvest economies due to convenience, increased access to information, speed of transactions, and enhanced control.

In the wake of the growth in the volume and complexity of financial transactions and world-wide integration of financial markets, risk management has increasingly become a key concern. Therefore adoption of a sound risk management practices will minimize adverse consequences that may be faced by financial institutions during periods of uncertainty. An effective risk management system facilitates the measurement and management of risk exposures, thus minimizing potential future losses. In addition, adoption of robust internal controls by Nigerian banks designed to provide qualitative standards are also necessary to complement the quantitative analysis of risk and would provide a check and balance in the overall risk management practices in the industry.

To address the problem of corporate governance issues, a hybrid approach was adopted at the post consolidation era by Malaysia, which included legal reforms, self-regulation as well as measures to encourage market-based regulation. New measures were introduced to further improve the level of governance among banking institutions. This included, limiting the number of directorships of chief executive officers, reviewing the responsibility and accountability of the board and management as well as requiring for the setting up of various board committees. In Nigeria, the corporate governance issue is a critical one that needs to be improved substantially in this post consolidation era. The consolidation exercise really revealed the cankerworm in the sector, comprising misreporting and mis-representation of facts, abuse of insider-related credit and poor management of assets. To this end, the CBN in March 2006 had issued a new code of corporate governance for the post consolidation banks in Nigeria and advised them to adopt and implement accordingly. Salient in the code are the issues of ensuring 'fit and proper" owners and directors of the banks and laying stress on diversified ownership.

As part of the efforts to ensure healthy and sound banking industry, the regulatory authorities in both Malaysia and India at the post consolidation era, gave greater attention to issues relating to the regulation and supervision of the industry by strengthening their process of regulation and supervision. In the same vein, the regulatory authorities in Nigeria, on their part, would be required to further streamline their regulatory framework as well as strengthen their supervisory capacity to ensure a sustainable growth and development in the industry. In this regard, there would be need to properly monitor the activities and performance of emerging mega banks to prevent distress and failures in the post-consolidation era. Other areas for effective regulatory action would be in the following areas:

- Full implementation of the risk-based supervision framework;
- Implementation of Consolidated Supervision
- Need for greater capacity for supervisors; and
- Provision of necessary supervisory tools/software

Arising from the bank consolidation exercise in Malaysia was the issue of how to raise the awareness of the public on their rights and responsibilities in relation to the new financial landscape. In this regard, a comprehensive 10-year consumer education programme was introduced. This was to raise consumer awareness and understanding on banking products and services and to educate the public on their rights and responsibilities in their relationship with a financial institution. The lesson for us here is how to ensure adequate and effective consumer education and protection as well as prevent any disruption in the level or reliability of services to bank customers, including their protection from potential unfair practices.

Moreover, in India, the legal environment for conducting banking business was strengthened after the consolidation exercise and debt recovery tribunals were introduced exclusively for adjudication of delinquent loans. Also, a Credit Information Companies (Regulation) Act, 2004 was enacted by the Parliament to enhance the quality of credit decision making. The main lesson here for Nigeria is the need for a review of our bank resolution and loan recovery system. In Nigeria, the liquidation of failed banks constitutes a great challenge for the CBN as failed banks normally go to court to challenge the revocation of their operating licences. Even after final court order might have been gotten for their liquidation, the issue of the disposal of their assets for the settlement of the depositors is another problem that may take sometime. This brings to the fore the need to establish special courts in the country exclusively meant for the liquidation of failed banks and adjudication of delinquent loans. In the wake of growth in the volume and complexity of financial transactions, involving both local and foreign investors in the post-consolidation era, there is need for both the law enforcement agencies and the judiciary to cooperate as well as work closely in the enforcement of the existing law on dud cheque in order to engender some confidence in the new financial landscape. Also, there is need to expedite action on the establishment of the Assets Management Company (AMC) as well as the revision of the necessary laws that will make it possible for both the CBN and NDIC to liquidate failed bank (s) without litigation by the bank (s) involved.

As mega banks emerged in Malaysia, following the consolidation exercise, efforts were made in the development of venture capital industry, which is a better framework for SME financing and the provision of micro-financing. This was to ensure that credit was made available to all the segments of the economy, as well as to support the growth of new areas and industries. Although the CBN is addressing this issue through the establishment of microfinance banks (MFBs) which basically are to offer appropriate microfinance services such as savings, credit, micro-leasing, domestic fund transfer and other financial services that are needed by the economically active poor and low income households, the challenge therefore is to adequately educate the operators of these institutions so that they will not derail in the management and provision of required services to the targeted group.

Another key lesson of experience for Nigeria is the role of government of both Malaysia and India played in the provision of social and economic infrastructure and enabling environment for banking business in order to boost the confidence of foreign investors in the sector. The current trend in economic growth is that capital flies to where capital already exists. Although there have been recent efforts by the government to improve our infrastructural base, notably in power, roads, and railways, much is needed generally in the medium term to long term. This will provide reduced cost of operations for the banks and which will be translated to lower cost of funds for users of funds in the economy.

5.0 Concluding Remarks

To conclude, we say that the experience from both Malaysia and India bank post consolidation era shows that a more diversified and sound financial sector, a more efficient and competitive financial services industry and all the structural enhancements made, had evolved a more effective and resilient financial system. The overall economic and financial transformation that occurred had resulted in economies that were mutually reinforcing the regional growth; and economies that had increasing role in the creation of wealth in the Asian region.

For us in Nigeria, the big lesson to learn is that sustaining growth in the post consolidation era requires stability to be preserved in the macroeconomic environment, the financial system and markets as well as the social environment through corporate social responsibility which refers to operating business in a manner that will also contribute to economic development, while improving the quality of life of the workforce and the local community and the society at large.

REFERENCES

Central Bank of Nigeria., "Facts File on Bank Recapitalization" A publication of the Central Bank of Nigeria, 2004.

Central Bank of Nigeria. Annual Reports, various issues and other internal publications.

Emenuga, C. ''The Outcome of Financial Sector Reforms in West Africa'' World Bank. Adjustment in Africa: Reforms, Results and the Road Ahead, World Bank Policy Research Report, Oxford University Press, New York, 1994.

Gyorgy, S. (2001) - "Banking Sector Reform in Hungary: Lessons Learned, Current Trends and Prospects" in Current Issues in Emerging Market Economies Organised by the Croatian National Bank June, 28 30.

Ikhide, S. and Alawode, A. 'Financial Reforms, Macroeconomic Stability and the Order of Economic Liberalization: The Evidence from Nigeria," Research Report presented at the African Economic Consortium Workshop, Nairobi, Kenya, December 4-9, 1994.

Nnanna, O.J - "Beyond Bank Consolidation: The Impact on Society" in CBN 4th Monetary Policy Conference, forthcoming 2005.

Soludo, C. - "Briefing on Current Reforms in the Nigerian Banking Sector". Being a brief held with foreign diplomats and other nationals in the country at the wake of the recent banking industry reforms in 2004.

Soludo, C. - "Consolidating the Nigerian Banking Industry to meet the Development Challenges of the 21st Century" Being an address delivered to the Special Meeting of the Bankers' Committee, held on July 6, 2004 at the CBN Headquarters, Abuja

Siems, T., - "Quantifying Management's Role in Bank Survival." Federal Bank of Dallas Economic Review, First Quarter, 1987, 1992.

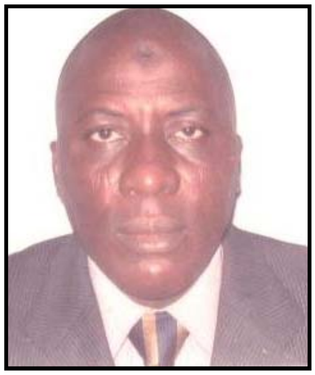
Tan Sri Dato' S. "Post Asian Financial Crises: Securing Financial Stability" Keynote Address at the Asian Banker Summit 2003.

Udoma , U.U. - "Banking: Post Consolidation Challenges" Being a text of paper presented at the 4th annual monetary policy conference of the Central Bank of Nigeria, 18 19th November, 2004 at Abuja.

Reddy Y V. "Banking Sector Reform in India- an Overview" Keynote Address at the Institute of Bankers of Pakistan Karachi, 2005.

Reddy Y V. "Reforming India's Financial Sector: Changing Dimensions and Emerging Issues" Public for the International Center for Monetary and Banking Studies IUHEI, Geneva, Switzerland, 2006.

The Role Of Central Bank Of Nigeria In Economic And Financial Integration In The West African Sub-region



By ABWAKU ENGLAMA* Ph. D and GANIYU KAYODE SANNI*

Introduction

Regional economic and financial integrations have long been accepted as strategies to promote growth and development. Conceptually, economic integration is the unification of different economic activities by members in the same union. These include custom, market, trade and laws regulating these activities. Thus, as economic integration increases, the barriers to trade between markets diminish. Balassa (1961) identifies six different stages of economic integration (i) preferential trading area (ii) free trade (iii) custom union (iv) common market (v) economic and monetary union; and (vi) complete economic integration. Put simply, regional economic integration is an agreement among contiguous nations to allow for the free flow of ideas, investment funds, technology, goods and services, and free movement of persons within the region in which a single large market subsists with the benefits of comparative advantage and economies of scale. The inherent benefits in economic integration explained why regional economic cooperation has gained momentum partly as a strategy to cope with global economic problems. As many countries are not strong enough on their own to cope with the rapid changes in the global economy, groups of countries use regional integration to achieve the necessary conditions for sustainable growth and development.

Financial integration on the other hand, is simply a process whereby a group of countries form a monetary union for the purpose of having a single monetary authority with a common currency or convertible currencies linked through an exchange rate arrangement; the

Dr. Englama and Mr. Sanni are Deputy Director and Principal Economist in the External Sector Division of Research Department, Central Bank of Nigeria, Abuja.
The views expressed in the paper are those of the Authors and do not in any way represent the views or thinking of the Central Bank of Nigeria.

determination and conduct of a unified monetary policy and a unified exchange rate policy. It involves the unification and joint management of both monetary and exchange rate policies of the union. It requires two major conditions: exchange rate unification, which requires that the exchange rate in the area bear permanently fixed relationship among the currencies of integrating members, while currency convertibility implies the absence of all forms of exchange controls for both current and capital transactions within the group (Max Corden, 1972).

The monetary integration is an important aspect of economic integration and as such, it is now being pursued with vigor in the sub-region with a view to forging a larger economic space to enhance economic growth and development. The decisions and commitment to have a monetary union are as a result of the gains and opportunities that await integrating countries which indeed outweigh the perceived costs. The formation of a monetary union facilitates macroeconomic stability as it strengthens macroeconomic management, and ensures the effective performance of money as a medium of exchange and store of value. The use of single currency helps to conserve scarce foreign exchange resources and enhances efficiency in domestic and regional resource allocations. Other associated benefits included the possibility of hastening the process of fiscal integration, reducing speculative capital flows, as well as enhancing the coordination of macroeconomic policies among others. However, there are costs involved in the membership of monetary union. The major potential cost of economic and financial integration is the uneven sharing of gains from the integration process. The moment the policy determination becomes centralized in a union, it becomes arduous for individual members to pursue independent stabilization policies. It thus engenders a considerable loss of autonomy in the use of fiscal policy to influence domestic economic activity. Also the use of monetary and exchange rate policies to tackle problems of internal and external imbalances may be totally constrained, and could possibly lead to importation of inflation from high inflation infected union member countries. Other costs include loss of discretionary use of macroeconomic policy instruments for stabilization purposes by individual members of the union and a partial loss of sovereignty.

The central banks of integrating member countries play a leading role in the realization of the objectives of economic and financial integration. Therefore, this paper intends to highlight the role of Central Bank of Nigeria in the economic and monetary integration in the West African sub-region. The paper is therefore, divided into five sections, following the introduction, section II presents a brief analysis of economic and financial integration in the sub-region, while section III discusses the role of Central Bank of Nigeria in the economic and financial integration in the West African sub-region. Section IV examines the achievements, problems and challenges of economic and financial integration in the sub region. The last section contains a summary of the paper, its key policy recommendations and some concluding remarks.

2.0 A Brief Analysis of Economic and Financial Integration Efforts in West African Sub-Region.

The Economic Community of West African States (ECOWAS) was founded in 1975 including both the francophone (WAEMU) countries, and the anglophone countries (the Gambia, Ghana, Guinea, Liberia, Nigeria and Sierra Leone) as well as Portuguese-speaking Cape Verde, for the purpose of integrating and accelerating economic development of the sub-region. Consequently, several schemes/programmes were established to actualize this objective. Among them were ECOWAS Trade Liberalisation Scheme (ETLS), West African Clearing House (WACH now WAMA), Inter State Road Transport (ISRT), ECOWAS Monetary Cooperation Programme (EMCP), West African Monetary Zone (WAMZ), West African Monetary Institute (WAMI). Highlights of important aspects of some of these schemes are provided below:

2.1 West African Monetary Agency (WAMA).

In 1996, the West African Clearing House (WACH) which was established in 1975 as a multilateral payment facility to improve sub-regional trade in West Africa, was transformed into a broad based autonomous agency called the West African Monetary Agency (WAMA). WAMA's Headquarters was officially inaugurated on the 28th November 1996. Following the transformation of WACH into WAMA, WAMA took over the assets and liabilities of the West African Clearing House. WAMA is comprised of the eight central banks of the West African sub-region. These include: BCEAO (Banque Centrale des Etats de l'Afrique de l'Ouest), Bank of Cape Verde, Central Bank of the Gambia, Bank of Ghana, Central Bank of Liberia, Central Bank of Nigeria and Bank of Sierra Leone. These central banks serve fifteen out of the sixteen countries of the West African sub-region with Mauritania being the only one out of the union.

WAMA was empowered to monitor, coordinate and implement ECOWAS' Monetary Cooperation Programme, encourage and promote the application of market determined exchange rates for intra-regional trade, initiate policies and programmes on monetary and economic integration and ensure the establishment of a single monetary zone in West Africa. The Agency's financial resources are derived from annual contributions from member central banks and other sources as may be approved by the Committee of Governors. Resources for the WAMA budget are derived 40% from equal contributions of member central banks, and 60% on the basis of the ratio used by ECOWAS in fixing each Member State's contribution to the ECOWAS budget.

Objectives

The Agency is concerned with monetary co-operations and payment issues within the context of economic and monetary integration process of the region and therefore has the following objectives:

! Promotion and use of national currencies for regional trade and transactions

! Bringing about savings in the use of foreign reserves for member states

! Encouraging and promoting trade and exchange liberalization

! Enhancing monetary cooperation and consultation among member states

! Facilitating the harmonization and coordination of monetary and fiscal policies and structural adjustment programmes

! Ensuring the monitoring, coordination & implementation of ECOWAS monetary cooperation programme

! Encouraging & promoting the application of market determined exchange & interest rates for intra-regional trade

! Initiating policies and programmes on monetary integration and cross border investments that will lead to a single monetary zone in West Africa.

In order to achieve these objectives, the Agency has to define policies and programmes to promote monetary and fiscal harmonization and cooperation in the sub-region, operate the Credit Guarantee Fund mechanism & Traveller's Cheque scheme; prepare periodic reports on exchange rates, fiscal & monetary harmonization, trade and exchange control liberalization, balance of payments, and other monetary cooperation issues; and collect, store and disseminate statistical information for member central banks and related institutions in West Africa as well as undertake relevant studies on matters relating to sub-regional economic integration.

Achievements

WAMA has contributed to sustaining the West African Unit of Account (WAUA), which is an Integral part of the sub-regional payment system adopted by member countries to settle financial transactions between them without involving their scarce foreign reserves.

WAMA has contributed to the creation and circulation of the ECOWAS Travellers' Cheque.

WAMA has maintained a good Clearing and

Payment System among member Central Banks in West Africa.ÊIn this respect, WAMA has been working with the West African Bankers Association (WABA) to harmonize payment systems in the private sector of the sub-regional economies.

WAMA has contributed to the realization of the Second Monetary Zone which is shortly to launch a Common Currency for the non-UEMOA (*Union économique et monétaire ouest-africaine)* member countries of ECOWAS. WAMA is also spearheading a monetary integration programme that will lead to a single monetary zone for West Africa in the near future.

WAMA operates a Credit Guarantee Fund Scheme for ECOWAS member Central Banks.

WAMA is also coordinating the Harmonization of Policies on Exchange Rates, Banking Laws, Statistics and Payment Systems in the sub-region.

2.2 ECOWAS Monetary Cooperation Programme (EMCP)

In order to facilitate trade and investment in the sub-region, member countries resolved to put in place some form of monetary cooperation, which is the first step in the establishment of monetary union. By monetary union, all member countries adopt or evolve a common currency under a unified exchange rate arrangement and apply a common authority. The Heads of State and Government of ECOWAS adopted an ECOWAS Monetary Cooperation Programme (EMCP) in 1987, that would lead to the establishment of single currency zone in the sub-region (Ashinze 2004). The EMCP is the most prominent scheme for monetary integration in the West African sub-region.

The specific objectives of the EMCP were to be implemented in three phases. In the short term, the aim was to strengthen the existing payment mechanism of the West African Clearing House through the settlement of outstanding payment arrears in the clearing mechanism; introducing new payment instruments such as the travelers cheque; introducing a credit guarantee fund facility to support the clearing mechanism; and removing all non-tariff barriers that tend to restrict the use of national currencies to effect payments for some current transactions such as hotel bills and air tickets. In the medium term, the EMCP was expected to achieve limited regional convertibility of national currencies by removing existing restrictions on their use. In the long run however, the ultimate goal of the EMCP is the establishment of a single ECOWAS monetary area involving the use of a common convertible currency, the establishment of a common central bank, the pooling of foreign exchange reserves and the negotiation of an external convertibility guarantee with an appropriate international agency. To facilitate these objectives, member states were to embark on an economic policy reform programme to achieve macroeconomic convergence. The policy reform programme was to adopt the policies of realignment of exchange rates and the adoption of a market-based exchange rate; removal of exchange control regimes; and minimize fiscal deficits and their financing through the rationalisation of government expenditure and tax reform. The short-term objectives of the EMCP have not been fully achieved, as exemplified by the failure to clear the arrears in the clearing house mechanism, the delay in introducing new payment instruments, the problems with the newly introduced ECOWAS traveller's cheques and the unwillingness of members to remove non-tariff barriers to intra-regional trade and other transactions. The medium- to long-term objectives of the EMCP have also not been fully attained, leading to the deferral of the establishment of the single monetary zone. The slow pace of the implementation of the ECOWAS Monetary Cooperation Programme (EMCP), especially the establishment of the single monetary zone, was attributed to the lack of commitment of member countries, absence of policy coordination and harmonization between UEMOA and non-UEMOA countries, and lack of political will and strong leadership to implement the policies and actions required in moving the programme forward.

2.3 West African Monetary Zone (WAMZ)

The failure of the EMCP inspired the Authority of Heads of State and Government of ECOWAS in December, 1999 at its 22nd Summit held in Lome, Togo to adopt a strategy of a Two-Track (Fast-Track) approach. This was initiated by Nigeria and Ghana aimed at reviving and accelerating the integration process in the sub-region. Following the initiative of Nigeria and Ghana, consultations were held with the Governments of The Gambia, Guinea, Liberia and Sierra-Leone, and at a mini-Summit of the Heads of State of the six countries, held in Accra, Ghana on April 20, 2000, the “Accra Declaration” on the creation of the *Second Monetary Zone* was signed. At that summit, Cape Verde and Liberia served as observers. The West African Monetary Institute (WAMI), domiciled in Accra, Ghana, was set up as an institutional vehicle to establish the WAMZ and make necessary preparations for the emergence of the common central bank and the introduction of a single currency as planned. It became operational in January 2001.The objective of the WAMZ was to fast-track the integration of the Anglophone economies through the creation of appropriate macroeconomic conditions that will facilitate and ensure the unification of the WAMZ and UEMOA and thus achieve the ECOWAS monetary union (Nnanna 2006).

At the meeting of the Convergence Council of Ministers and central bank Governors of the WAMZ in Accra, Ghana, on June 20, 2002, the following decisions/recommendations were made to move the WAMZ project forward (Ebi 2003):

- A strong West African central bank system should be established with authority to undertake monetary policy for the Zone.
- The foreign exchange reserves and liabilities of the member countries of the WAMZ should be fully pooled to back the common currency of the WAMZ when it is introduced.
- Member countries should take steps to accede to the IMF General Data Dissemination Standard (GDDS) to harmonize statistical data and methodologies.
- WAMI should conclude its study on the central bank financing of government budget deficits.
- WAMI should undertake a study on the exchange rate parities existing among the member countries' currencies, to determine if they could guarantee competitiveness of the component economies of the WAMZ.
- When a review of the WAMZ exchange rate mechanism band is undertaken (after it has been operating for six months), a narrower band should be prescribed to provide the required discipline..
- Member countries that have not paid their contributions to the Stabilisation and Cooperation Fund should do so by the end of June 2002.
- All member countries should redouble their efforts in sensitising the various interest groups to the WAMZ programme, as this is critical to the success of the WAMZ project.
- The earlier decision on ECO as the name of WAMZ common currency was reiterated. This is without prejudice to the ongoing efforts on the name of a common currency for ECOWAS.
- The Governors should closely study the draft amendment to the Statute of the WACB for discussion at its following meeting.
- The country that would be eventually selected to host the headquarters of the WACB (Ghana, Nigeria and Guinea have applied) was required to be committed to implementing open sky policy as defined in the Yamoussoukro Agreement.

Convergence Criteria

In order to realize the objectives of the WAMZ, two convergence criteria were set for member countries. These were:

Primary Convergence Criteria

The primary convergence consist of four variables namely exchange rate, inflation, budget deficit and central bank financing of fiscal deficits with prescribed target and are as follows:

- Under the Budget Deficit, all member countries are expected to reduce the ratio of their budget deficit to Gross Domestic Product (GDP) to 4.0 per cent or less by end 2003. This was later extended to 2008;
- The maintenance of single digit inflation by end of 1998 for all countries except Liberia and Sierra-Leone that were to achieve the single digit target by 2000. It was later set at not less than or equal to 5.0 per cent to be achieved by 2003 but later extended to 2008;
- The government of all member countries are to reduce progressively their borrowings from the central bank to a ceiling of 10.0 per cent of a previous years fiscal revenue by 1998 but was also extended to 2008;
- Countries' reserves were initially billed to cover 3 months of imports by end-2000, but was later reviewed to at least 6 months of import to be achieved by end 2003 and now extended to 2008.

The Secondary Criteria are:

- Domestic Debt Arrears: there was prohibition of new domestic debt arrears and liquidation of all existing arrears;
- Tax revenue /GDP ratio: Member countries were to employ appropriate measures to expand their tax bases and ensure that fiscal receipts are not less than 20.0 per cent of GDP;
- Wage bill: Member countries were to incur wage bills of not more than 35.0 per cent of total fiscal receipts;
- Domestically Financed Public Investment: They were to ensure that not less than 20.0 per cent of tax revenue is used to finance public investment. This is intended to reduce the debt servicing cost of public investment;
- Real Exchange Rate: Member countries were require to maintain real exchange rate stability in the context of an exchange rate mechanism. This was intended to maintain price stability; and
- Positive Real Interest Rate: Countries should maintain positive real interest rate in order to stem possible occurrence of financial disintermediation, sustain confidence of both local and foreign investors in the economies and reduce the possibility of financial arbitrage and capital flight and

consequently achieve price stability.

! Originally, monetary integration was planned to be achieved in 1990 but could not be realized up till now due to the failure and the delay in implementation of necessary policies such as currency convertibility and resolution of internal economic and financial imbalances especially as regards price stability. Other notable factors that hamper progress towards convergence in the Zone included the failure of countries to incorporate WAMZ convergence criteria in their budget programmes, unsatisfactory implementation of policy recommendations to achieve convergence and the absence of sanctions in cases where countries derogate.

2.4 West African Monetary Institute (WAMI)

The Head of States of six countries in West Africa, as part of the fast-track approach to integration, decided in Accra, Ghana, April 20, 2000 to establish a second monetary zone to be known as the West African Monetary Zone (WAMZ) by the year 2003. These countries namely The Gambia, Ghana, Guinea, Liberia, Nigeria and Sierra Leone signed the 'Accra Declaration' which defined the objectives of the zone as well as, an action plan and institutional arrangements to ensure the speedy implementation of their decision. It is envisaged that this zone will be merged with the CFA Franc Zone to form a single monetary zone in West Africa. In order to facilitate the creation of the common Central Bank and the introduction of a common currency, an interim institution, the West African Monetary Institute was set up in Accra, Ghana in January 2001.Ê The Institute which would undertake technical preparations for the establishment of a common West African Central Bank started operations in March 2001.

Functions of WAMI

In accordance with its statute, the Institute is mandated to perform the following functions:

i. Monitor state of convergence

The WAMI would monitor the state of macroeconomic convergence of the member countries vis-à-vis the prescribed benchmarks (the primary and secondary convergence criteria and submit an analysis of developments in the member countries to the decision making body of the zone, the Convergence Council. The convergence reports which would be submitted to the Council on quarterly basis would contain recommendations on policy measures needed to achieve the required convergence in the participating economies.

ii. Harmonise Regulations and Design Policy Framework

The Institute would ensure that regulations on financial markets in all member countries including laws relating to both bank and non-bank financial institutions, are harmonised in order to create a level playing field for all economic operators within the Zone. The WAMI would also ensure the harmonization of monetary policy, banking regulations and accounting practices of all the participating countries of the WAMZ. This would allow comparability and formulation of a common monetary policy for all the six countries. In order to ensure effective banking supervision in the zone, WAMI would make proposals on an institutional framework for a centralized supervisory authority.

Iii Promote Regional Payment System

The WAMI would also promote the development of the payments system in the second monetary zone to facilitate the implementation of a common monetary policy. This would require close collaboration with member central banks and the West African Bankers Association (WABA) to implement a payments system infrastructure that would allow the interlinking of all participating countries. This would facilitate the smooth execution of monetary policy operations and efficient transfers within the zone.

iv Exchange Rate Mechanism and Conversion Rate

The WAMI would study the issue of exchange rate parities within the WAMZ and recommend the appropriate exchange rate mechanism and parities for the existing currencies in the zone. It would also provide basis for setting up an exchange rate mechanism and the appropriate bands of fluctuation for currencies in the zone. It would be responsible for determining the value of the common currency and the conversion rates of national currencies into the common currency.

v Organisation of Scheme

It would embark on a programme of sensitization of citizens of the member countries in order to create wide public support for the introduction of the new currency. This would involve organisation of seminars/workshops etc. to educate the public on the new currency, the ECO. This activity would be undertaken in collaboration with member states which have set up National Sensitisation Committees (NSCs) in this regard.

vi Design and Technical Preparation of the New Currency

The WAMI will be responsible for the preparation of background work on the new currency to be issued by the common Central Bank. This would include the name, determination of par value, denominations, that would facilitate the printing of the new bank notes and coins by the WACB.

vii Modalities for Setting up a Common Central Bank

The Institute would also be responsible for the setting up of the common Central Bank, including drawing up the legal framework of the central bank and related institutions, proposals for selecting the Headquarters, the modalities for contributing to the capital, the physical infrastructure and drawing up guidelines for the hiring of key officers.

viii Foster Cooperation among countries

The West African Monetary Institute will fulfill a role similar to that played by the European Monetary Institute (EMI). In this regard, the West African Monetary Institute (WAMI) would provide a platform for intense cooperation between the central banks in the WAMZ, and foster in the countries of the Zone the feeling of ownership of the future common Central Bank.

ix Create Enabling Environment

The Institute would create the conditions for a smooth transition to the new common currency by ensuring that regulations in all countries are consistent with the introduction of a new currency; prices are quoted in the new currency as well as any other practical issues that would facilitate the smooth introduction of the new currency, and withdrawal of old currencies.

2.5 West African Institute for Financial and Economic Management (WAIFEM)

The West African Institute for Financial and Economic Management (WAIFEM) was established on July 22, 1996 by the constituent central banks : The Gambia, Ghana, Liberia, Nigeria and Sierra Leone and became operational in January, 1997. The principal objective of the Institute is to build capacity for macroeconomic and financial management in the countries of its member central banks. The functions of the Institute are to:

· Sponsor or conduct seminars, training courses and consultative fora on central banking and macroeconomic issues;

! Support, design and implement programmes for the training of suitably qualified staff from the region;

! Publish and disseminate information on central banking and macroeconomic policies in the region;

! Identify, design and promote networks of researchers, analysts, managers and professional associations;

! Collaborate with national, bilateral and multilateral training or other institutions consistent with the objectives of WAIFEM;

! Carry out such activities which may advance the purposes of WAIFEM

2.6 ECOWAS Trade Liberalisation Scheme (ETLS).

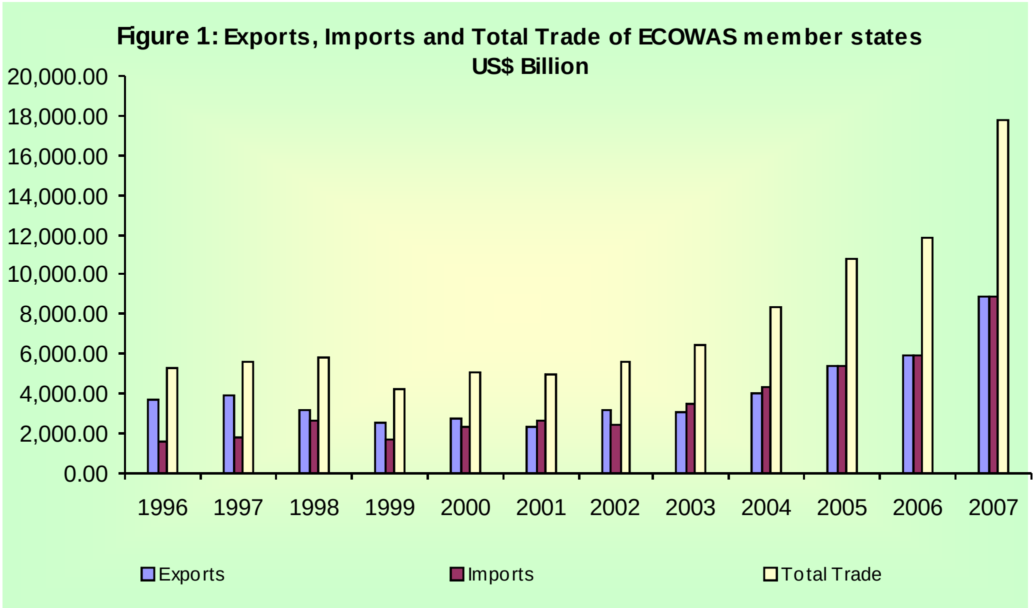
The ETLS was adopted in January 1990 by member countries to encourage intra-regional trade development and promotion. The core focus of the scheme is the removal of tariff barriers to intra community trade. Specifically, the objectives of the ETLS are: establishment of a Custom Union; elimination of Custom duties and taxes of equivalent effects; removal of non-tariff barriers; and establishment of Common External tariff. The ETLS is expected to result in the creation of integrated market for trade in goods and service as well as increase in the region's competitive advantage in the global market. Consequently, the integrated and enlarged market would attract investment. Furthermore, the economies of scale made possible by the larger regional market would pave way for more efficient production and distribution systems.

Analysis of available data on Intra-ECOWAS trade from 1996-2007 indicate that the value and volume of intra-ECOWAS has continued to increase since the adoption of the ECOWAS Trade Liberalisation Scheme which has led to unhindered movement of goods in the sub-region. Total trade increased from US$5.3 billon in 1996 to US$5.6 billion, US$5.8 billion, US$6.5 billion and US$10.8 billion in 1997, 1998, 2003, and 2005 respectively. It is estimated to increase by 50.0 percent to US$17.8 billion in 2007 from the level in 2006. Exports from ECOWAS countries amounted to US$3.1 and US$4.0 billion in 2002 and 2004. It further rose to US$5.7 billion and US$5.9 billion in 2005 and

Table 1 - ECOWAS Visible Trade (1996-2007)
US$ billion

	Exports	Imports	Total Trade
1996	3,667.01	1,629.68	5,296.69
1997	3,863.52	1,766.87	5,630.38
1998	3,165.36	2,639.65	5,805.01
1999	2,584.06	1,684.02	4,268.08
2000	2,788.28	2,324.41	5,112.69
2001	2,306.19	2,631.93	4,938.12
2002	3,148.21	2,415.76	5,563.97
2003	3,037.80	3,458.73	6,496.52
2004	3,986.12	4,327.85	8,313.97
2005	5,389.90	5,361.39	10,751.29
2006x	5,928.89	5,897.53	11,826.42
2007x	8,893.33	8,846.30	17,739.63

Source:
ECOWAS
Statistical tablex: Estimated



3.0 The Role of Central Bank of Nigeria (CBN) in the Economic and Financial Integration in the West African Sub-Region

The role of CBN towards integration efforts in the sub-region is linked to the statutory functions assigned to it by the CBN Act of 1958 as subsequently amended. According to the CBN Act No 7 of 2007, the objects of CBN shall be to:

! Ensure monetary and price stability;
! Issue legal tender currency in Nigeria;
! Maintain external reserves to safeguard the international value of the legal tender currency;
! Promote a sound financial system; and
! Act as banker and provide economic and financial advice to the federal government.
! The performance of these functions by the Bank has direct linkage to the goals of ECOWAS to achieve economic and financial integration in the sub-region. In most cases the CBN represents Nigeria in most of the agencies of ECOWAS. Of all the functions expected of the Bank, an important one is the formulation of sound economic policy that will position the Nigerian economy to achieve greater benefits from the integration process in the sub-region. Below are some of the roles that have been performed by the CBN towards the integration in the sub-region:
! The CBN facilitated the establishment of WAMA and WAMI
! The CBN on behalf of the government of the Federation ensures regular payments of Nigeria's subscription to ECOWAS, WAMI, and WAMA. Apart from financial support, the Bank has provided both technical and human capital supports to the key institutions driving the integration efforts in the sub-region.
! Promote and facilitate sub-regional payments system such as ECOWAS travelers cheque
! The CBN ensure the formulation of sound monetary policy whose primary target is the achievement of single digit inflation. To achieve the objectives of its monetary policy, the Central Bank of Nigeria has continued to rely on market-based techniques in

the management of the Bank's balance sheet. The primary instrument of policy has continued to be open market operations, supported by reserve requirements and discount window operations for enhanced effectiveness. Other policy instruments include the cash reserve requirement, the liquidity ratio, the discount window and the use of the Bank's securities to mop up excess liquidity in the system.

- To fulfill the convergence criteria of the WAMZ, macroeconomic policy is formulated to increase the rate of growth of real GDP, reduce unemployment, maintain price and exchange rate stability, promote a healthy balance of payments, reduce the lending rate and mobilise more savings. Specifically, in order to reduce inflation to a single digit figure (as low as 5%), the central focus is on effective control of anticipated liquidity injections that may arise from excessive government spending. Periodically, the central bank determines target growth rates of money supply, which are compatible with overall policy goals. It relies mainly on open market operations and other policy instruments for liquidity management, primarily to control banks' reserves.
- The CBN played a leading role in the formulation of Nigeria's home grown economic reform programme - National Economic Empowerment and Development Strategy (NEEDS). The NEEDS which was launched in 2004 has repositioned the Nigerian economy to be the leading recipients of foreign capital flows in Africa. The successful implementation of the NEED programme has made Nigeria to continue to play leading role in the sub-region. Thus, it has helped to foster integration drive of the country.
- With regard to central bank financing of budget deficits, which has been limited to 10% of the previous year's tax revenue, the Bank has continued to insist that government borrowing from it should not exceed the statutory limit of 12.5% of the estimated current budget revenue and that should that occur, the market rate of interest should be applied. The policy of the Bank is against the inflationary financing of government deficits through the ways and means advances and, with the instrument autonomy granted to it, the Bank will continue to apply the traditional instruments to fine-tune the system to ensure compliance with this convergence criterion.
- On the need to ensure that gross external reserves cover at least six months of imports, the Bank's policy has been based on proactive reserves and risk management. These include: portfolio diversification; exchange rate policy; foreign exchange budgeting and balance of payments policies.
- The Bank has carried out a consolidation of the Banking system in order to enable the domestic money banks play their roles in the global market. The success of the consolidation exercise is manifested in the expansion of many Nigerian owned bank

branches in the sub-region.

- In order to ensure that Nigerian currency (Naira) is convertible and serve as reference currency in the sub-region the Bank recently launched the strategic agenda for the Naira. The policy is meant to shore up the value of Naira and get the country prepared for the smooth take-off of ECO currency;
- The Bank in 2007 launched Financial Sector Strategy 2020 (FSS 2020) whose principal objective is to make Nigeria the financial hub of Africa. The implementation of the strategy would help to solidify Nigeria's preparedness for integration in the sub-region.
- The Bank has been involved in the sensitization of key stakeholders on the need to buy-in the project through organization of seminars and conferences.

4.0 Achievements, Problems and Challenges of Economic and Financial Integration in the Sub-Region

Remarkable progress has been made since the inception of ECOWAS . In particular, intra-ECOWAS trade has continued to grow, member countries have succeeded in taming rising inflation to single digit, members have also imbibe the principle of fiscal prudence as many countries have met the target of fiscal deficit requirements under the WAMZ convergence criteria. Members have also adopted common external tariff. There is also free movement of goods and people in the sub-region. In spite of all these achievements in the integration process, the ECOWAS integration agenda continued to face a number of problems and challenges:

First, the major hurdles to African integration have been the lack of full commitment manifested in the failure to incorporate agreement reached by different integration scheme in national plans. This tendency has played down the value of collective agreements or protocols arrived at to expedite trade and harmonize policies at sub-regional levels. Nomvete (1997) views that the failure to integrate the cooperation programmes into the national administrations is due to lack of follow-up of decisions taken at the sub-regional meetings.

A second problem is that awareness on the issue of economic integration has not been promoted at the grassroots level or that the private sector which is the engine of economic growth has not been actively involved in the effort to advance integration by the various African states. Whatever may be the reasons, African leaders have also failed to explain fully to the people the reasons for their participating in integration arrangements and the advantages which accrue to the majority. To the extent that cooperation arrangements are (or were) forged without the full participation and knowledge of the population, their stability and success of implementation of programmes have been difficult to be guaranteed.

A third inhibiting factor to cooperation according to Nomvete (1997) is the dearth of local private entrepreneurs and technical and management skills. As a result, the operational management of the economy, including project formulation, project implementation and investment decisions, is left to the public sector (parastatals), which normally would not be as responsive to opportunities for cross-border investments and joint ventures with businessmen from neighbouring countries and/or from developed countries, and are guided not by profitability of projects in economic and financial terms but by political exigencies. It is the lack of home-grown private entrepreneurs and skills which accounts for the excessive dependence of African economies on imported products.

The financial constraint facing the realization of the WAMZ programme remains a serious problem as most member countries are yet to settle their financial obligations that have fallen due. The initial euphoria at the inception of the WAMZ programme and the Fast Track integration process led to a prompt settlement of financial obligations towards the setting up of WAMI. Subsequently, a Fund to support the adjustment efforts of member countries was thought to be critical for the convergence process of the Zone. Thus the Stabilisation and Cooperation Fund was designed and adopted for operationalisation in the first quarter of 2002. A total of $100 million was, considered modest for adoption, while the first installment of $50 million was to be paid in the first quarter of 2002 and the balance paid in September 2002. It is disheartening to remark that the payment of the first tranche is yet to be fully made as scheduled by member countries. This could be linked to the problem of political commitment of the government because if member countries consider the benefits associated with the monetary integration process, none of them would have been defaulting. Obviously, the financial aspect remains a critical challenge to the sub-regional member countries (Nnanna 2006).

Compliance with macroeconomic convergence criteria is also a serious problem confronting participating member countries. The attainment of economic convergence is critical to the integration process in ECOWAS and necessary for ensuring internal and external balance, a prerequisite for the take-off of the single monetary union. As already stated, the performance of the countries of UMEAO was comparatively better than that of the WAMZ as members of the former group made impressive feats in the maintenance of low inflation, sufficient external reserves and positive real interest rates, whilst the WAMZ countries were noted for relatively high budget deficit, high inflation and low external reserves with the exception of Nigeria. However, performances have been constrained by external shocks particularly the sharp declines in the prices of some of the major primary commodity exports of the zone. This has led to the deterioration in the revenue inflow to the countries. In addition, the persistence of fiscal dominance continued to weaken the effectiveness of the monetary policy leading to slippages in the criteria of budget deficit/GDP ratio and central bank financing of government budget deficit, while inflation rate exceeded the targets in some countries. It is incumbent on those countries affected by weak fiscal consolidation to institute measures to address the problem of fiscal imbalance.

Almost related to the aforementioned issue is the critical challenge of ensuring that the UEMOA countries which are already in monetary union continue to experience macroeconomic stability, while the rest of the region makes steady progress in the convergence process.

This will ensure overall macroeconomic stability in the region, characterized by highly stable prices and convertible exchange rates. The authorities of the UEMOA should continue to steer member countries on the path of macroeconomic stability, while the WAMZ countries must apply the right policy tools and undertake reform measures to address the obstacles to the integration process. It is hoped that the sustained performance by the UMEOA on macroeconomic stability will facilitate smooth merger with the WAMZ when the time comes. It is obvious that the preparedness of the UMEOA to merge with the WAMZ would determine the success of the ECOWAS single monetary zone project in the long run.

The economic dependency status of many African countries is another factor that works against the viability and strength of sub-regional economic cooperation groupings in Africa. Many African countries still depend excessively on supplies of manufactured products originating from developed countries, even when comparable products are available within a sub-regional preferential arrangement. This kills the rationale for creating bigger markets to facilitate the growth of viable production enterprises. The preference for imports from industrialized countries is attributable not only to habit but also to the trading advantages enjoyed by the suppliers from the developed countries.

Another factor is linked with the elitism which characterizes the implementation process of integration which lack grassroots support at the national level. This is due to the manner in which the cooperation arrangements were launched. In many countries the idea of forming or joining an economic cooperation arrangement was not derived from the wishes of the people or in response to the felt needs of the leadership but rather from ideas instigated by a donor country or countries (Abraham 2000).

A particular weakness of economic arrangements is that they tend to be based more on linguistic and cultural criteria. In such groupings, divisive elements are strong and their existence frustrates the development of cohesive and viable sub-regional grouping. For example, in West Africa, Ghana, Liberia and Sierra-Leone (English-speaking countries) are geographically surrounded by CEAO countries all of which are French speaking. Gambia is culturally and economically part of Senegal but not a member of French speaking bloc of the Senegal River Basin because it is English-speaking as opposed to Senegal which is French-speaking.

Another problem is the reluctance and inability of the members of economic blocs to create the facilities and the mechanisms necessary to expedite the movement of goods and services. A case in point is the clearing mechanism on which agreements were signed but not followed up.

The clearing and payments mechanism was established in some cooperation arrangements to promote the use of local currencies in intra-sub-regional trade to ease the foreign exchange constraint. A critical problem is that of the accumulation of payments arrears. In the West African and Central African clearing houses, for example debtor monetary authorities have on many occasions failed to settle their obligations in the clearing house at the end of the transaction period, and have accumulated payments obligations which remain unsettled.

Furthermore, there is no adequate transport infrastructure for intra-African trade. Even when tariffs have been reduced and intra-country transport links are open, the costs of transport between countries forming a cooperation bloc tend to be high. There are problems of operational and institutional nature which make intra-African cooperation difficult. These relate to information, banking, language, costs of promotion, prices of research, etc.

Finally, there is the problem of multiple membership The multiplicity of regional economic communities has several drawbacks:

i. Fragmented economic spaces and approaches to regional integration.
ii. Increased cost of membership in regional economic communities.
iii. Unhealthy rivalry for donor funds.
iv. Contradictory obligations and loyalties for member countries.
v. Inconsistent objectives and conflicting operational mandates.
vi. Duplicated efforts.
vii. Reduced ability for regional economic communities to pursue coherent and effective integration programmes

5.0 Summary, Conclusion and Recommendations

The paper has discussed the various integration efforts in the sub-region, the role of CBN as well as the achievements, problems and challenges of the economic and financial integration in the ECOWAS sub-region. Therefore, in order to surmount the identified challenges, the following policies are recommended for adoption:

- Collective efforts should also be made to improve the precondition for enhanced integration through joint efforts aimed at improved roads, telecommunication and large industries which are unaffordable for the small states. Coupled with this, measures should be taken to remove tariff barriers and encourage division of labour, stimulate specialization in production and spur economies of scale.
- There is the need for member countries to demonstrate in clear terms their financial commitment to the programme and embark on wide publicity in order to keep stakeholders abreast of the progress on monetary integration. Concerted efforts should be made at achieving compliance with the macroeconomic convergence.
- There is the need for improving the economic and political environment to ensure rapid technological and innovative developments.
- An effective institutional framework for managing the financial sector and strengthening international financial infrastructure, are necessary for sustainable liberalization.
- Careful study of the timing, sequencing and degree of market liberalization.
- Capital account convertibility needs to be in line with domestic capacity to implement financial reporting, regulation and supervision standards.
- Diversification of economies cannot occur without an active industrial and technological policy, which entails an

important role for the government, as markets are not perfect.

- Strengthening institutional and human skills capacity of regional economic cooperations (RECs) and their country-level focal points are critical to implementing agreed instruments of economic integration.

SELECTED REFERENCES

Adedeji Adebayo (2002): History and Prospects for Regional integration in Africa- an address at the Third Meting of the African Development Forum, Addis Ababa.

Asihinze J.O (2002): "West African Monetary Institute (WAMI) and the efforts towards Monetary Integration" paper presented at the workshop organized by International Economic Relations Department

Balassa B (1961): The Theory of Economic Integration

Bax Nomvete (1997): "Regional Integration in Africa: A path strewn with obstacles" published in the magazine The Eye on Ethiopia and The Horn of Africa Vol. 6, No. 39, April-May, 1997.Ê

Corden, W. M., (1972): Monetary Integration Essay in International Finance, No. 93, Princeton University, Princeton, 42 pages

Ernest Ebi (2002): Regional Currency Areas: Lessons from the West African Sub-Region and Nigeria's Policy Stance

Hogan, E. B., (2001): "ECOWAS Monetary Cooperation Programme: Issues, Progress and Prospects," CBN Bullion, Vol. 25, No 2, April/June, pp 23-32.

Kinfe Abraham (2000): The challenges and prospects of Pan-African Economic Integration-A Paper Presented at the Conference on Economic integration and Transboundary Resources Organized by the Ethiopian International Institute for Peace and Development (EIIPD)

Nnanna O. J (2006): The ECOWAS and the Challenges of Monetary Integration

Ukpong, G. E., (2002): "Second Monetary Zone in ECOWAS: Issues, Progress and Prospects," Central Bank of Nigeria, Economic and Financial Review, Vol. 41 No. 4, pp 10-22.

West African Monetary Agency, (2005): "Progress Report on Macroeconomic Convergence: WAMA," Freetown, pp1-43.

WAMI: Annual Report and Statement of Account of the West African Monetary Institute, Various Issues.

West African Monetary Institute, (2004): "Economic and Monetary Integration in West Africa: Evolution, Achievements and Prospects," Accra: WAMI, pp 1-120.

Http://www.ak-sophiabooks.org/researchworks.htm

Improving The Agricultural Sector Toward Economic Development And Poverty Reduction In Nigeria

By OBIECHINA, MICHAEL EMEKA*

1.0 Introduction

Since Nigeria became independent, most government policies have been directed towards accelerating economic development with the ultimate aim of transforming the economy into an industrialized one, as well as raising the welfare of the population. The foregoing has been the underpinning factor propelling most government policies.

One of the sectors expected to act as a catalyst towards the realization of this goal is agriculture[1]. The traditional role of agriculture in economic development provides the foundation for this position. The role includes product contribution, market contribution, factor contribution and foreign exchange contribution (Johnston and Mellor, 1961). No doubt, it has continued to play a very important role in the economic development of the country.

Notwithstanding, the enviable position of the oil sector in the Nigerian economy over the past three decades, the agricultural sector has remained the largest and arguably the most important sector of the economy. Agriculture's contribution to the Gross Domestic Product (GDP) has remained stable at between 30 and 42 per cent, and employs 65 per cent of the labour force in Nigeria (Aigbokhan, 2001). It is estimated to be the largest contributor to non-oil foreign exchange earnings. This means that agriculture holds abundant potentials for enhancing and sustaining the country's foreign exchange.

Most of the employment generated by the agricultural activities is in the rural area. Anyanwu, et al (1997) posited that more than 80 percent of the rural population of Nigeria is engaged in one type of agricultural activity or the other. Apart from those engaged in subsistence farming, the bulk of the agricultural export crop (Cocoa, Palm Kernel, Rubber, Cotton, Groundnut Palm Oil etc) producers are smallholder farmers. Furthermore, studies have shown that a

! Mr. Obiechina is an Economist in the Monetary Policy Department, Central Bank of Nigeria, Abuja. The views expressed in the paper are those of the Author and do not in any way represent the views or thinking of the Central Bank of Nigeria.

! My discussion of agriculture in this paper is focused on crops, livestock, fisheries and forestry.

large percentage of the rural farmers are among the poor (FOS, 1999). The level of poverty in the rural areas is high and has continued to be determined, largely by the fortunes of agriculture and the international market prices for the agricultural commodities, which constituted the major non-oil exports of the economy. Also, the level of poverty has been exacerbated by the decline in the sector's role and contribution to the economy, as well as increasing income inequality; with Gini coefficient of 0.49 in the rural areas and 0.54 in the urban areas (MDGs Report, 2005).

Government has embarked on various policies and programmes aimed at strengthening the sector in order to continue performing its roles, as well as measures for combating poverty. These have generated different scholarly reactions as to the efficacy of government policies and programmes in improving the agricultural sector. While CBN, 1992; Obadan, 1994; Jimaza, M. and Sani, E. I. 2003) maintained that agricultural export did respond positively to policy reforms, particularly in the 1980s, others suggest that there has been a general failure of the sector to respond appropriately to the policies (Olomola, 1998). However, literatures are abound on the role of agriculture in economic development and poverty reduction (Atoloye, 1997; DFID, 2005). With soaring increase in the level of poverty, especially in the rural areas, and the apparent decline in the role of agriculture, when compared to the 1960s, the current rate of poverty reduction may be too slow to meet the targets set for 2015. If this current rate of poverty reduction is maintained, poverty incidence would reduce to 43 per cent as opposed to 21.4 per cent by 2015 (Ibid, Pg. 6). There is an urgent need for the government to resuscitate the agricultural sector, perhaps restoring it back to its past glory.

This paper considers the role of agriculture in engendering economic development and poverty reduction in Nigeria. This is achieved by using trend analysis to review the various contributions of agriculture, and its policies and progrmmes toward the economic development of the country. It analyses the country's poverty profile, its inter-linkages with agriculture as a means of combating poverty in the country. It also, made recommendations that will boost agriculture development, as well as poverty reduction in the country. The paper is divided into 6 sections. Following the introduction is Section 2, which explains the conceptual framework for agriculture growth, poverty and poverty reduction - the inter-linkages of agriculture, poverty and poverty reduction in economic development. Section 3, analyses the role of agriculture as the mainstay of Nigeria economy. It takes into account agriculture's contribution to the Gross Domestic Product (GDP), employment generation and export earnings etc. Section 4, considers the various agricultural policies and its reform under the National Economic Empowerment and Development Strategy (NEEDS). Section 5, reviews the poverty profile in the country, x-raying the various dimensions and causes of poverty in Nigeria, as well as the major challenges of agricultural development in Nigeria. Finally, Section 6 dwelt on recommendations that will boast agriculture development, as well as poverty reduction in the economy.

2.0 Conceptual Framework for Agriculture Growth, Poverty and Poverty Reduction

Poverty is one of the greatest challenges of human development, and arguably the greatest obstacle to government policies and programmes, especially in the underdeveloped countries. Poverty in Sub-Saharan Africa has become a major preoccupation of academics, policy makers and the international development partners, including the United Nations Development Programme (UNDP), DFID and World Bank etc, especially since the 1990 (Ajakaiye,1998).

Historically, the dominant view, especially during the early stages of industrial revolution in Europe was that poverty arose out of the fickleness of character. This belief, which places the responsibility for poverty at the doorsteps of individuals, has since been jettisoned to the realization that the socio-economic framework is really at the roots of poverty. Sharing this view, R.H. Tawney in Titmus (1958) posited that "The problem of poverty… is not a problem of individual character, but a problem of economic and industrial organization. It has to be studied at its source and only secondary in its manifestation" Ozo-Eson, I. (1998).

The massive presence of poverty and hunger, and the apparent inability of most underdeveloped economies to address their associated problems prompted the development of an integrated world approach. The approach was anchored in the MDGs -"spare no effort to free our fellow men, women and children from the abject and dehumanizing conditions of extreme poverty, to which more than a billion of them are currently subjected-a commitment set in the Millennium Declaration (Sachs, 2005; Brown, 2005).

With about 70 percent of the MDGs' target groups living in rural areas, particularly in Asia and Africa, and for most of the rural poor, agriculture is a critical component in the successful attainment of the MDGs…" more immediate gains in poor households' welfare can be achieved through agriculture, which can help the poor overcome some of the critical constraints they now face in meeting their basic needs. (WDI, 2007)

There seemed not to be a conclusive opinion among scholars on the role of agriculture as a key source of growth and poverty reduction. Some suggests that agriculture's role as a key source of growth and poverty reduction is limited (Maxwell, 2004), others believed otherwise - while conditions for smaller and poorer farmers are undoubtedly challenging, the more optimistic (Lipton, 2004, and Hazell, 2005) believe that productivity gains are possible with the right policies and will have a major impact on growth and poverty.

Lipton (2005) argued that agricultural growth should reduce poverty through farming: agricultural growth results in increased demand for unskilled labour, thus creating jobs and tending to raise the rural wage rate; generates returns to land, an asset that some of the poor have when they have few other assets than their labour power; and tends to push down the price of produce, including food, to the immense benefit of the majority of the poor who have to buy in food staples. Wiggins (2006) submitted that historical record has shown that no country - city states such as Hong Kong and Singapore excepted - has ever seen rapid economic growth without substantial growth of its agriculture. In many cases the increases in agricultural output have preceded the major expansions of manufacturing. This would be the case for the UK in the 17th and 18th Century, as well as many of the recent East Asian growth stars, such as China, South Korea, Indonesia, and Taiwan.

Agriculture's importance to poverty reduction transcends its direct impact on farmers' incomes. Evidence has shown that agricultural growth has benefited millions through higher incomes, more plentiful and cheaper food, and by generating patterns of development that are employment-intensive and benefit both rural and urban areas**.** Gallup et al (1997) reported that for every 1 percent increase in per capita agricultural output led to a 1.61 percent increase in the incomes of the poorest 20 percent of the population. Thirtle et al (2001) concluded from a major cross-country analysis that, on average, every 1% increase in agricultural yields reduced the number of people living on less than US$1 a day by 0.83 percent.

The use of agriculture as a veritable instrument for wealth creation and poverty reduction could be explained within the framework of agricultural linkages or “multiplier” and the wider economy, though (Ellis, 2000) questioned whether these linkages have remained as strong today, particularly in Africa. The argument being that, in many situations, additional income is increasingly likely to be spent on imported consumer goods and agricultural inputs rather than locally produced goods. However, other studies have established the strength of the growth linkages. Estimates show that on average in Asia, every $1 of additional farm income created a further $0.80 in non-farm income (Bell et al 1982; Hazell and Ramaswamy, 1991). Also, in Africa, estimates show that every additional $1 of farm income leads to a further income of between $0.96 in Niger and $1.88 in Burkina Faso elsewhere in the economy (Delgado et al, 1998). Models of the Kenyan economy show these”multipliers“from agricultural growth which is three times as large as those for nonagricultural growth (Block and Timmer, 1994). In Zambia, estimates suggest that every $1 of additional farm income creates a further $1.50 of income outside agriculture (Hazell and Hojjati, 1995). Irz et al. (2001) estimate that for every 10 percent increase in farm yields, there is a 7 percent reduction in poverty in Africa, and a 5 percent reduction in Asia, while growth in manufacturing and services has no such effect. De Janvry & Sadoulet (2002) used stylized models to show how improved farm productivity can reduce poverty in different circumstances. In Africa, they argued that benefit comes from direct increases in production accruing to the poor as farmers; in Asia, the benefit to the poor comes from increased jobs and upward pressure on farm wage rates; while in Latin America, the poor gain from additional jobs created in the food chain. In Nigeria**,** Sudharshan, et al (1995) confirmed that the share of the population in poverty declined from 43 percent to 34 percent in Nigeria between 1985 and 1992 because of a 34 percent increase in average per capita expenditures.

Increases in agricultural output, brought about by increasing land and labour productivity, have made food cheaper, benefiting both the urban and rural poor, who spend much of their income on food. Bangladesh provides an excellent example, between 1980 and 2000; the real wholesale price of rice in Dhaka's markets fell from 20 to 11 Taka per kg, bringing major benefits to poor consumers (Smith and Haddad, 2002). Poor households typically spend 5080 percents of their income on food (Nugent, 2000), including many poor farmers.

There is no gainsaying in acknowledging the key role of agriculture in poverty reduction, especially within the underdeveloped countries with cases of labour-intensive, small-scale agriculture having strong links to growth in other areas**.** However**,** the “structural transformation” of poor countries' economies away from dependence on agriculture lies at the heart of sustained poverty reduction. The relationship between agricultural growth and poverty reduction is more when countries are least developed. At the early stages of development, agriculture typically accounts for a large share of total employment, and food represents a major part of poor people's spending. As the non-farm sector develops, and economies become progressively less dependent on agriculture, the relationship becomes less important overall, but remains significant in some parts of these economies where the non-farm sector is least developed (DFID, 2005).

3.0 Agriculture In Nigeria's Economic Development

The role of agriculture in the Nigeria's economic development was explained using trend analysis on the position agriculture has been the mainstay of Nigerian economy. Prior to the attainment of independent, agriculture was identified as a potential factor, capable of catapulting Nigeria's economic development. The colonial administration in realizing this set up marketing boards for the major cash crops. According to Helleiner (1966) export production accounted for about 57 percent of Nigeria's Gross Domestic Product (GDP) in 1929. Oil palm products alone accounted for between 85-90 percents of the total volume of exports during the period. The contributions of the sector to the GDP continued to increase, for example, agriculture became the leading sector of the economy in 1950s and 1960s. In the periods 1960-64 and 1965-69 agriculture output accounted for 63 and 54 percents of GDP (Aigbokhan; 2001). From Table 1, this declined significantly from the 1970s. From an annual average value of 58.8 percent for the period 1960-69, it dropped to 33.2 percent for the period 970 74, It marked an epoch in Nigeria's economic history through the 1973/74 (Crude oil price shocks). It further went down to 30.2 percent for the period 1975-79, on annual average, its contributions to GDP from 1997-2006 is 41 percent.

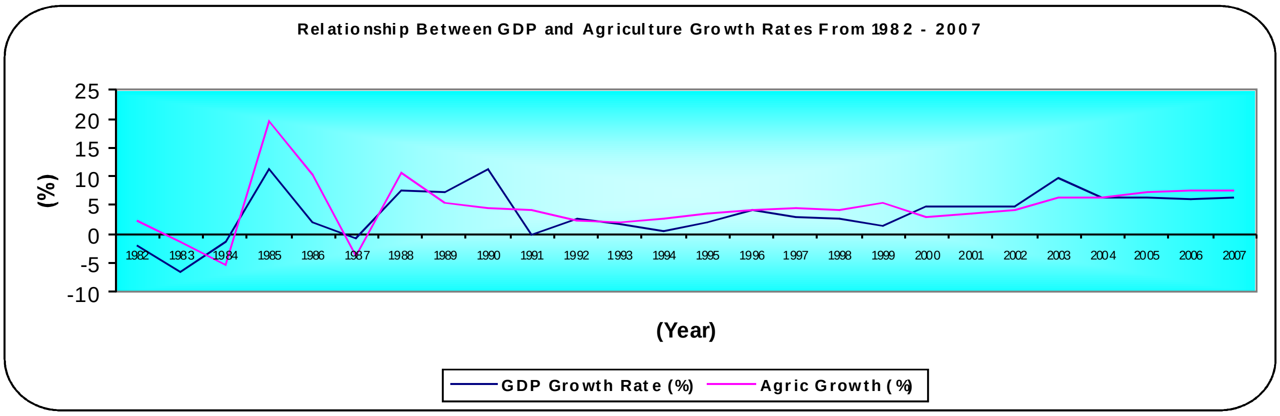
TABLE 1: Percentage of Distribution of Nigeria's GDP at 1984 Constant Factor Cost (%)

Period Year	GDP	Crude Oil Petrol	Manufa-cturing	Agriculture	Retail & Wholesale	Others
1960 - 69	26.8	1.6	6.1	58.8	N.A	33.60
1970 - 74	58.2	17.4	2.5	33.2	11.0	35.9
1975 - 79	73.7	24.3	5.0	30.2	12.1	28.40
1980 - 84	68.4	15.5	9.08	35.36	13.3	26.94
1985	68.90	15.1	8.6	40.3	13.00	23.0
1986	71.1	13.8	8.0	42.7	13.0	22.5
1987	70.7	12.5	8.4	41.5	13.9	23.7
1988	79.8	12.3	8.7	41.5	13.8	23.7
1989	83.5	13.2	8.2	40.6	13.4	24.6
1990	90.4	12.8	8.2	39.0	12.7	27.3
1991	94.5	12.4	8.3	39.0	12.5	27.8
1992	97.4	13.4	7.9	38.3	12.5	27.9
1993	100	13.1	7.3	37.8	12.6	29.2
1994	101	12.6	7.2	37.3	12.5	30.4
1995	103.3	12.6	6.7	34.0	12.2	34.5
1996	107	13.1	6.5	39.0	11.8	29.6
1997	110	12.8	6.3	39.4	11.7	29.8
1998	112	11.9	5.9	40.4	11.8	30.0
1999	116	10.7	5.9	41.0	11.7	30.0
2000	120	11.5	6.0	41.0	11.5	30.0
2001	126	12.0	6.0	40.3	11.2	30.5
2002	131	9.8	6.1	41.2	11.7	31.2
2003	136	8.9	6.4	40.3	11.3	33.1
2004	528	25.7	3.7	40.9	12.9	16.8
2005	562	24.3	3.8	41.1	13.6	17.2
2006	594	21.9	3.9	41.8	14.8	17.6

1 Source: Computed From CBN Statistical Bulletin, Vol. 16, Dec. 2005 and CBN Annual Report and Statement of Account, 31st December, 2006. Note: Figures from 1960-69; 1970-74, and 1975-79 are on annual averages, [1]Provisional

Figure 1, shows the movement of the GDP and agricultural growth rates with both moving in the same direction. The GDP growth rate of 2003 and beyond was driven mainly by development in the agricultural sector, which grew by 7 per cent and the oil sector by 27 per cent (NEEDS, 2004).

Figure 1



Note: 2007 is Provisional

During the periods 1962 - 65 and 1967 - 71, the share of food import in total import was low, being 9.6 and 8.6 percents respectively. Using food import to total import as a proxy for agriculture contribution to the food supply, it has been posited that agriculture was able to supply most of the food needs of the economy (Adubi, 2001). Its annual average was 9 and 16 percents respectively for the periods1971-77 and 197886. It declined to 13 percent from 1994 1999. Also, from 2000-2006, it dropped and has an average of 9 percent (Table 2).

TABLE 2: The Nigerian Imports and Food Imports (1970-2006) By S.I.T.C.

Year	GDP At Current Basic (N-m)	Total Imports (N m)	Food Imports (N m)	Food Imports As % of Total Imports
1970	5203.70	756.4	57.7	7.63
1971	6570.70	1078.9	88.3	8.18
1972	7208.30	990.1	95.8	9.68
1973	10990.70	1224.8	126.3	10.31
1974	18298.30	1737.3	154.8	8.91
1975	21558.80	3721.5	298.8	8.03
1976	27297.50	5148.5	441.7	8.58
1977	32747.30	7093.7	780.7	11.00
1978	36083.60	8211.7	1027.6	12.51
1979	43150.80	7472.5	1254.3	16.79
1980	50848.60	9095.6	1437.5	15.80
1981	47619.7	12839.6	1819.6	14.17
1982	49069.3	10770.5	1642.3	15.25
1983	53107.4	8903.7	1761.1	19.78
1984	59622.5	7178.3	1349.7	18.80
1985	67908.6	7062.6	1199.0	16.98
1986	69147.0	5983.6	801.9	13.40
1987	105222.9	17861.7	1873.3	10.49
1988	139085.3	21445.7	1891.6	8.82
1989	216797.5	30860.2	2108.9	6.83
1990	267550.0	45717.9	3474.5	7.60
1991	312139.8	87020.2	3045.7	3.50
1992	532613.8	145911.4	12840.2	8.80
1993	683869.8	166100.4	13953.4	8.40
1994	899893.2	162788.8	13837.0	8.50
1995	1933211.6	755127.7	88349.9	11.70
1996	2702719.1	562626.6	75392.0	23.40
1997	2801972.6	845716.6	100728.3	11.91
1998	2708430.9	837418.9	102165.1	12.20
1999	3194023.6	862515.7	103489.8	12.00
2000	4537640.0	985022.4	113630.5	11.54
2001	4685912.2	1371409.1	160209.1	11.68
2002	5403006.8	1512695.3	144297.6	9.54
2003	6947819.9	2080235.3	201648.3	9.70
2004	8264962.41	1987045.3	178747.4	9.00
2005	14553097.0	247932.3	171817.1	6.93
2006	18067830.0	2528086	174229.4	6.90

Source: Computed from CBN statistical Bulletin Vol. 10. No. 2, Dec. 1999, CBN statistical Bulletin Vol. 16. Dec. 2005, CBN Annual Reports and Statement of Account, for the year ended 31st Dec., 2006

[1] Provisional.

Compared to its 1994 1998 average value of 12 percent, the average value of 9.33 percent for the period, 2000-2006 showed a remarkable drop in the nation's food importation. This is a good development, if it is going to be sustained. Nigeria need not be spending a large chunk of her foreign exchange on food importation, considering agriculture potentials.

Agricultural contributes to the finances of government. The then regional governments derived much of their development finances from agriculture. Between 1954 and 1957, N144 million or 42 percent of the marketing boards surplus were disbursed as grants to regional governments, and another N24 million as loans to regional government. Furthermore, between 1962 and 1966, 13 and 34 percents of the regional government finances depended on Marketing Boards Surpluses (Adubi, 2001.). The role of Marketing Boards was very important especially in stabilizing farm incomes and generating funds for the execution of development projects in the economy. The Boards continued this role until in 1986, when the government introduced the Structural Adjustment Programme (SAP).

In terms of employment generation, more than 80 percent of the rural population of Nigeria is involved on one type of agricultural activity or the other. This indicates the extent to which agricultural sector absorbs the labour force in Nigeria. According to World Bank Report cited in (Anyanwu et al, 1997), the sector employs about 71 percent of Nigeria's total labour force in 1960, and by 1977, this dropped to 56 percent. It was 68 percent in 1980, falling to 55 percent in 1985, 53 percent in 1986, 55 percent in 1988 and 57 percent annually from 1989 to 1992 (Ibid.) and by 2005, it rose to 60.88 percent. Table 2, reveals the extent to which the agricultural sector has continued to be dominant in employment generation in the country when compared to other sectors.

TABLE 2: Sectoral Contribution to Employment Generation

Description	**2001**	**2002**	**2003**	**2004**	**2005**
Total Working Population	100	100	100	100	100
Agric. Hunting, Forestry & Fishing	54.75	59.50	59.49	59.26	60.88
Mining & Quarrying	0.16	0.15	0.14	0.14	0.14
Manufacturing Industries	1.78	1.52	1.75	1.74	1.9
Prod. & Dist. of Electric, Gas & Water	0.82	0.72	0.88	0.88	0.90
Building & Construction	0.66	0.56	0.56	0.56	0.57
Comm. Repairs of Auto & Domestic Art	0.28	0.20	0.20	0.2	0.22
Hotels & Restaurants	0.21	0.19	0.19	0.19	0.20
Transport, Storage & Communication	0.89	0.87	0.85	0.86	0.87
Finance & Intermediation	0.83	0.54	0.58	0.57	0.59
Real Estate, Renting & Bus. Activities	0.16	0.13	0.13	0.12	0.13
Public Admin & Defence, Comp. Soc. Sec	12.45	11.03	10.47	10.5	0.13
Education	20.18	18.56	18.01	18.25	19.88
Health & Social Work	0.63	0.41	0.60	0.61	0.62
Others	6.21	5.52	6.17	6.13	6.2

Source: National Bureau of Statistics; the Nigerian Statistical Fact Sheets On Economic and Social Development, June, 2005.

Agricultural sector has contributed largely to the nation's foreign exchange earnings. It was the largest contributor to the foreign exchange earning before the emergent and dominance by crude oil from the 1970s. Its contribution to the total export earnings accounted for 86 percent of total exports in 1955-59, 80 percent in 1960-64 and 57 percent in 1965-69 (Aigbokhan, 2001). From the 1970s (Table 3), agricultural contribution to total export has been declining, as a result of the Country's over reliance on crude oil. From 1970-74, agriculture accounted for 15.4 percent of total exports, by 1975-79, it declined to 5.0 percent, between 1985-89 and 1990-94, it accounted for 14.23 and 2.0 percents respectively, and by 2004-6, it went down to less 1 percent. In terms of foreign exchange from non-oil export, agricultural sector contribution is prominent. It accounted for 70 percent of non-oil export in 1970 and by 1982; it was 97.4 percent of the non-oil export. It dropped to 33 percent in 2004, and moved up to 38 percent in 2006.

TABLE 3: Nigeria's Total Exports; Oil and Non-Oil Exports, with Agriculture as Share of Non-Oil Exports (1970-2006)

Year	Total Export (N' million)	Oil Export (N' million)	Non-Oil Export (N' million)	Agric (N' million)	Agric (% Non-Oil Export)
1970	885.4	510	375.4	265.2	70.64
1971	1293.4	953	340.4	242.8	71.33
1972	1434.2	1176.2	258	172	66.67
1973	2278.4	1893.5	384.9	250.1	64.98
1974	5794.8	5365.7	429.1	276	64.32
1975	4988.4	4563.1	362.4	231	63.74
1976	6751.1	6321.6	429.5	274.1	63.82
1977	7630.7	7072.8	557.9	375.7	67.34
1978	6064.4	5401.6	662.8	412.8	62.28
1979	10836.8	10166.8	670	468	69.85
1980	14077	13632	554.4	340.1	61.35
1981	11033.8	10680.5	342.8	178.4	52.04
1982	9196.4	8003.2	203.2	198.6	97.74
1983	7502.5	7201.2	301.3	259	85.96
1984	9088	8840.6	247.4	208	84.07
1985	11720.8	11223.7	497.1	192.1	38.64
1986	8920.5	8368.5	552.1	407.4	73.8
1987	30360.6	28208.5	2152	1588.4	73.81
1988	31192.8	28435.4	2757.4	2558,2	92.78
1989	57971.2	55016.8	2954.4	2131	72.13
1990	109886.1	106626.5	3259.6	2429.3	74.53
1991	121533.7	116856.5	4677.3	3425	73.23
1992	205611.7	201383.9	4227.8	3054.9	72.26
1993	218801.1	200710.2	4991.3	3437.3	68.87
1994	206059.2	927565.3	5349	3818.8	71.39
1995	950661.4	1286215.9	23096.1	15512	67.16
1996	1309543.4	1212499.4	23327.5	17202.6	73.74
1997	1241662.7	717786.5	29163.3	19826.1	67.98
1998	751856.7	1169476.9	34070	16338.9	47.96
2004	4602781.54	4489472.19	113735.3	37532.6	33.00
2005	6372052.44	6266696.62	105955.82	44395.49	41.9
2006	5752747.74	5619152.88	133594.86	50498.86	37.8

Source: Computed from CBN statistical Bulletin Vol. 16. Dec. 2005, CBN 2005 and 2006 are Provisional.

4.0 Agricultural Policies and Reform Programmes

Nigeria's agricultural development policies had over the years been informed by the belief that the rapid development of the sector would no doubt lead to the overall growth and development of the economy (sectoral inter-linkages). This has been the underpinning factor behind most government agricultural policies to enhance and sustain the capacity of high level of food production for domestic consumption and exports; especially within the areas, we command comparative advantage, as well as developing the production and processing of exportable cash crops to boost the nation's non-oil foreign earning capacity.

In this paper, three periods may be identified, within which different government agricultural policies and programmes could be situated. These three periods are analyzed within the context of finance, pricing and marketing and institutional reforms. The periods are:

Minimal Intervention (1960-69), Strong Intervention (1970-1985); and Non-Intervention (1986-2007).

Minimum Intervention Period (1960-1969)

Agricultural production during this period was characterized by minimum government intervention with the then different regional and state governments pursuing their agricultural policies at their own pace. The role of the central government was more of supportive. There were very few financial and institutional reforms, when compared to the period thereafter. It was characterized by the presence of large small farmers producing the bulk for both domestic and export markets. These were mostly achieved through the activities of various marketing boards and cooperative societies.

Strong Intervention Period (1970-1985)

The period from 1970 to 1985 witnessed a strong government intervention in the agricultural production. With the emergent of crude oil price shock from 1973-74, and its subsequent dominance as the major source of foreign exchange earnings, coupled with the reduction in agricultural contributions to the GDP and increase in food import as a percentage of total import (See Tables 1 & 2), there was a remarkable presence of government in agricultural production with the aim of restoring its past glory. This presence made manifest in a lot of financial and institutional reforms, as well as international organizations assisted programmes designed to reconstruction or reform the whole structure of agricultural sector in order to strengthen the economic position of the farmer.

The desire of government to boost food production within the shortest possible time by encouraging masses of farmers led to the establishment in 1973 of the National Accelerated Food Production Project (NAFPP). The programme was based on the green revolution concepts and experiences of Mexico, India, Philippines and Pakistan. Its main objectives are to accelerate the production of six major food crops, namely, rice, millet, sorghum, maize, wheat and cassava. It was bedeviled by inadequate finance, inadequate commitment by some states, inadequate publicity and poor infrastructural facilities. In terms of finance of agricultural production, there was Nigerian Agricultural and Co-operative Bank (NACB) established in 1973. It was designed to foster growth in the quantity and quality of credit to all aspects of agricultural production including poultry, farming, fisheries, forestry and timber production, horticulture, etc. It was also aimed at improving storage facilities for agricultural products and the promotion of the marketing of agricultural products. The quantity of loans granted to smallholder farmers has proved grossly inadequate

(Anyanwu, et al, 1979).

Furthermore, there was the development of River Basin Authority. The idea for this development was nurtured in 1963 with the involvement in the Lake Chad Basin and River Niger Commission for countries bordering the lake and the Niger River. This was first tried in 1973 with the establishment of the Sokoto-Rima and the Chad Basin Development Authority respectively and subsequently, the creation of others through enabling Decrees. It was designed to cater for the development of land and water resources, which are considered potentials for Nigeria's agricultural purposes and general development. However, the activities of the River Basin Development Authorities (RBDAs) had been hampered by lack of land in the South, as well as funds for its operational activities.

The international organizations have not been left out of the pursuit for self reliant in food production. Since 1974, the World Bank had assisted Nigeria with a series of Agricultural Development Programmes (ADPs), which have gone through various phases. With its establishment in 1974, the programme, which started with three "enclave project" in the northern part of Nigeria (Funtua, Gusau and Gombe ADPs) brought an improvement for some of the major food crops, such as maize, sorghum and millet, combined with improvements in the extension services, the input supply system, the rural road network and village water supply. Through, the Multi-sector (MSADP-1 & 2), the programme later spread to all the states in the country. In addition, there was the Operation Feed the Nation (OFN), established in 1976 with the aim of increasing food production and eventual attainment of self sufficiency in food supply. Other reasons for the scheme include, encouraging the section of the population which relies on buying food to grow its own food. This did not stay long before it waned off.

In attempt to reduce the sufferings encountered by farmers in securing loans, another financial institution was created in 1977. The Agricultural Credit Guarantee Fund (ACGF) was created in order to encourage the flow of increased credit to the agricultural sector. The scheme became operation in 1978 with the objective of providing "guarantees in respect of loans granted for agricultural purposes by any bank in accordance with the provisions of the Act" and with the aim of increasing the level of bank credit to the agricultural sector.

There was also, the establishment of the Land Use Act in 1978. The Decree was aimed at reforming the traditional land tenure system, which was believed to be causing bottleneck to the development of agriculture. In the 4th National Development Plan, it was succinctly stated among others "The land tenure system has long been a bottleneck in the establishment of large-scale farms by private operators. With the implementation of the recent land use decree, private sector involvement in large-scale agricultural activities should receive a boost during the next plan period…. Availability of land should no longer be a constraint to agricultural undertakings. The reform should promote between securities of tenure and also encourage consolidation of holdings and large-scale operation. It should make it easier to attract foreign entrepreneurs and foreign capital agricultural projection" (Ibid.). The

Decree rests the control of all land in state government's hands to be in trust for the Federal Government. It however, does not disturb the rights of users of land already occupied or developed in rural areas but transfers allocation powers over undeveloped land from traditional authorities to local government.

The agricultural sector received yet another boost from government in its bid to achieve food sufficiency for the economy. The Green Revolution Programme was launched in 1980 by the then Alh. Shehu Shagari's administration, its principal objective was centered on self-reliance in food production and diversification of country's sources of foreign exchange earning. Input subsidies and crop pricing policies were streamlined while constructions of rural physical infrastructures were embarked upon through massive Federal government allocations. Though, there existed some measures of success, these were short-lived due to shortage of funds, mismanagement and fraud, inadequate data etc (Anyanwu, 1986).

Non Intervention Period (1986-2007)

This period of non-intervention or deregulation marked an epoch in Nigeria's history. The government's Structural Adjustment Programme became the driving force behind most government policies and programmes. The agricultural policy and programmes from 1986 were driven by non-government intervention. In fact, they were conceived and operated within a framework of deregulated economy. Arguably, it was seen as the required antidote necessary to kick-start the agricultural sector from its drop in the 1970s and early 1980s. As observed by the (Ministry of Agriculture, 2001) “the response of the sector to the various policy measures has been mixed. Between 1970 1982, agricultural growth rate stagnated at less than 1 percent with sharp decline in the production of export crop. Per capita calorific food supply declined from surpluses in the 1960s to a deficit of 38 percent in 1982, while Nigeria turned net import bills rising astronomically”

Trade liberalization was another important policy reform of the period under the SAP. The period witnessed the abolition of import and export licensing and exchange control. Under this new policy, export owners were expected to be entitled to 100 percent of their foreign exchange earnings provided they are kept in the domiciliary account. The marketing boards were abolished and the Export Incentive and Miscellaneous Provisions Decree of 1986 was enacted, through, which the Central Bank of Nigeria (CBN) could provide refinancing and discounting facilities to commercial and merchant banks to encourage them to provide credit and risk bearing facilities in support of exports. This later became the Nigerian Export Credit Guarantee and Insurance Corporation in 1988, which subsequently was renamed the Nigerian Export-Import Bank.

Some institutions were established and restructured to facilitate the availability of funds to the sector. The Agricultural Credit Guarantee Scheme Fund, established in 1977 to guarantee 75 percent of any default in bank loans granted to the agriculture, had its initial capital of ₦100 million recapitalized to ₦1.0 billion and ₦3.0 billion and 1999 and 2001 respectively. There was the establishment of the Nigerian Agricultural Insurance Company (NAIC) in 1987, which has among its mandate to protect farmers against losses arising from natural or man-made hazards beyond their control. There was the establishment of Directorate for Food, Roads and Rural Infrastructure (DFRRI), Peoples Bank of Nigeria (PBN) etc.

Also, there was the establishment of National Agricultural Land Development Authority (NALDA) in 1991 with the mandate of executing national agricultural land development programme in order to moderate the chronic problems of low utilization of abundant farm land. The main target of the programme was the development of 30,000-50,000 hectares of land in each state during the 1992-1994 National Rolling Plan period. Also, it was to see to the placement of at least 7,500-12,500 farmers within the area developed. There are indications that this may not have been fully accomplished

Agricultural Development Programmes (ADP), which was established in the 1970s as three pilot projects grew to 31 by 1993. Its services include covering four integrated components of agriculture; adaptive research, agricultural extension, input supply and rural infrastructure development. It underwent further restructuring with the Agricultural Project Monitoring and Evaluation Units (APMEU) to form the unified extension services to the farmers. In addition, the River Basin Development Authorities (RBDAs) functions became streamlined; it disposed all their non-water assets and withdrew from all activities involving direct production. There number was reduced from 21 to 11. Furthermore, the period saw the merger of Nigerian Agricultural and Cooperative Bank (NACB), which was established in 1973 with the Peoples Bank of Nigeria (PBN) and the Family Economic Advancement Programme (FEAP) to form the Nigerian Agricultural Cooperative and Rural Development Bank (NACRDB), with a swooping capital of N10.0 billion.

Agricultural Policy under the National Economic Empowerment and Development Strategy (NEEDS)

Agricultural policy under the NEEDS was informed by the sector's new policy framework under President Olusegun Obasanjo's Regime (1999-2007). Agricultural sector development received enormous presidential attention with so many Presidential Initiatives on Rice, Cassava and Cocoa etc. being set up. There was, the National Programme for Food Security (NPFS), launched in November, 2001 and designed to provide for food security for the country.

NEEDS is a poverty reduction strategy paper, expected to last from 2004-2007. It was predicated on the fact that Nigeria had experienced decades of low productivity and slow economic growth. The economy was characterized by weak macroeconomic policies, circumscribed by the high and inefficient but highly volatile and unsustainable public sector spending (Essien, 2005). Agricultural policy under NEEDS was designed to achieve overall agricultural growth and development; through the attainment of self sustaining growth in all the sub-sectors of agriculture and the structural transformation necessary for overall socio-economic development of the country as well as the improvement in the quality of life of all Nigerians.

The document set out some targets for the agricultural sector development and means of achieving them. For example: developing and implementing a scheme of land preparation services to increase cultivable arable land by 10 percent annually and fostering private sector participation through incentive schemes; achieving $3 billion in agricultural exports, a major component of which will be cassava by 2007; drastically reduce food imports from 14.5 percent of total imports to 5 percent by 2007; and achieving minimum agricultural growth rate of 6 percent per annum within the context of macroeconomic framework. It also, provides for the government annual capital spending on the sector, which are 3, 4, 4 and 4 percents for 2004-7 respectively.

5.0 Poverty Situation and Agricultural Challenges in Nigeria

Nigeria's economic development can aptly be captured by “Poverty In the Midst of Plenty”. It is a paradox as well as thought provoking to planners, policy makers and particularly to development partners both within and outside the country. Nigeria, which was one of the richest 50 countries in the early 1970s, has retrogressed to becoming one of the 25 poorest countries at the threshold of the twenty first century. It is ironic that Nigeria is the sixth largest exporter of crude oil and at the same time host the third largest number of poor people after China and India (Igbuzor, 2006). The Country is rich, but the people are poor. Nigeria is rich in land, people, oil and natural resources, but the people could hardly eat, or drink or clothe themselves not to talk of being largely unhealthy and uneducated (Okunmadewa, 1996). With about two-thirds of the Nigerian people being poor, despite increases in revenues from crude oil over the past decades, our people have been falling deeper into poverty. In 1980, an estimated 27 per cent of Nigerians lived in poverty. By 1999, about 70 per cent of the population had income of less than $1 a day the figure has risen since then (NEEDS, 2004).

Nigeria's per capita GDP was among the lowest in the world during the 1980s and 1990s, costing it decades of development. Annual per capita GDP remained stagnant in the 1990s, and it grew just 2.2 per cent between 1999 and 2003 far below than the 4.2 per cent per capita growth needed to significantly reduce poverty. With GDP of about $45 billion in 2001 and per capita income of $300 a year, Nigeria has become one of the poorest countries in the world. As of 2000, it had earned about $300 billion from oil exports since the mid 1970s, but its per capita income was 20 per cent lower than in 1975 (Ibid). Nigeria is among the 20 countries in the world with the widest gap between the rich and the poor. The Gini index measures the extent to which the distribution of income (or in some cases consumption expenditure) among individuals or households within an economy deviates from a perfectly equal distribution. A Gini index of zero represents perfect equality, while an index of 100 implies perfect inequality. Nigeria has one of the highest Gini index in the world. The Gini index for Nigeria is 50.6. This compares poorly with other countries such as India (37.8), Jamaica (37.9), Mauritania (37.3) and Rwanda (28.9) (Op cit.).

Nigeria provides a textbook example of an economy that requires development in the agricultural sector as vehicle for poverty reduction. Apart from agriculture being the mainstay of Nigeria's economy, it provides employment and linkages with the rest of the economy. With an average annual investment rate of barely 16 percent of GDP, which is far below the minimum investment of about 30 percent of GDP required to unleash a poverty reduction growth of at least 7-8 percent per year, increasing urbanization growth rate of 5.3 percent, among the highest in the world (NEEDS, 2004), stagnant manufacturing sector, operating at 25 percent industrial capacity utilization for 2006 (Okereke-Onyiuke, 2006), as well as 75 percent of arable land, and 40 percent under cultivation, there is no doubt that agriculture is the necessary catalyst required to drive the economy, hence the need for increased government effort at unlocking the agricultural potentials.

Poverty in Nigeria is deep and severe. It is caused by the interplay of social, economic, political, cultural and environment factors - lack of access to employment opportunities, minimal access to credit facilities (especially, the rural women), problems in productive sector, increasing income inequality, gender inequality, destruction of land natural resources caused by environmental degradation (Oil pollution in the Niger Delta) and leadership deficits etc. Sudharshan, et al (1995), stated that apart from poverty's overwhelmingly rural and regional characteristics, it is also strongly influenced by education, age, and the nature of employment. Those without education account for most of the poor and an overwhelmingly large fraction of the extreme poor. Looking at the poverty profile for Nigeria, it shows that by 1980, it was 28.1 percent and it rose to 46.3 percent in 1985. It moved from 42.7 percent in 1992 to 65.6 percent in 1996, and dropped to 54.4 percent by

TABLE 4: Poverty Profile for Nigeria
(Percentage of Poor People in Total Population)

Factor	**1980**	**1985**	**1992**	**1996**	2004
National	**28.1**	**46.3**	**42.7**	**65.6**	54.4
Geopolitical Zones					
North East	35.6	54.9	54.9	70.1	72.2
North West	37.7	52.1	36.5	77.2	71.2
North Central	32.2	50.8	46.0	64.3	67.0
South East	12.9	30.4	41.0	53.5	26.1
South West	13.4	38.6	43.1	60.9	43.0
South Central	13.2	45.7	40.8	58.2	35.1
Sector					
Urban	17.2	37.8	37.5	58.2	43.2
Rural	28.2	51.4	46.0	69.3	63.3
Gender of Head of Household					
Male	29.2	47.3	45.1	66.4	NA
Female	26.9	38.6	39.9	58.5	NA
Size of Household					
1 Person	2.0	70.0	29.0	13.1	12.6
2-4 People	8.8	19.3	19.3	59.3	39.3
5-9 People	30.0	50.5	51.5	74.8	57.9
10-20 People	51.0	71.3	66.1	88.5	73.3
More than 20 People	80.9	74.9	93.3	93.6	90.7
Education of Head of Household					
None	30.2	51.3	46.4	72.6	68.7
Primary	21.3	40.6	43.3	54.4	48.7
Secondary	7.6	27.2	30.3	52.0	44.3
Post Secondary	24.3	24.4	25.8	49.2	26.3

Source: Adapted From the National MDGs Report 2005, National Bureau of Statistics 1999, 2005 and NEEDS, 2004

Limited access to Finance

Limited or inadequate access to credit facility is one of the greatest challenges confronting the average Nigerian farmer. Farming activities in Nigeria are dominated by small farm-holders, who are frequently affected with the problems of raising funds especially, when there is need for the expansion of land under cultivation, introduction of new crops or seeds etc. Government has made some policies, which are expected to soften the hardship farmers incur in raising funds, but this noble programme has not been fully realized, partly due to lack of political will to fully implement the policy to its fullest. Again, the interest rate regime in the country might be a source of discouragement for the farmers. With a soaring interest rate of between 18-23%, it might be difficulty for an average Nigeria farmer to secure loans from the deposit money banks. Banks too, are not comfortable extending credit facilities to customers, whose ability to honour their debt obligations might be in doubt, as well as difficulty of projecting returns on investments.

Poorly Functioning Markets

The absence of an effective marketing system is a bane in agricultural development in Nigeria. Since the abolition of commodity marketing boards in the late 1980 (Structural Adjustment Programme), a vacuum was created, which is yet to be effectively filled in the marketing arrangements of agricultural produce. Despite, the introduction of the Abuja Securities and Commodity Exchange (ASCE) in 2001, farmers still suffer from marketing facility problem, and this predisposes them to seasonal price variations. It is even more challenging with the private sector, as it has not always responded as expected. The failure of government organizations is undeniable; however, in many instances the private sector is not providing a viable alternative because they are weak and still dependent on government's patronage.

Reduction of Public Expenditure on the sector

In many underdeveloped countries, public expenditure on agriculture as a percentage of total government expenditure has fallen short of the Food and Agricultural Organization (FAO) recommendation that 25 percent of government capital budget allocation be assigned to the agricultural development capital budget. This has not been achieved by the government, thereby affecting government's programmes and policies for the sector. In terms of capital allocation to agriculture, it was an average of 4.74 percent from 1970-1980. But, from 1980-2000, it rose to 7.00 percent and 10 percent from 2001-2007 though revealing an increase, but still falls short of FAO recommendation of 25 percent.

The ratio of agricultural budget expenditure to total government expenditure from 1970-1980 was on average of 2.66 percent. It rose to 8. 34 percent from 1981-1984, however, by 2000, it nosedived to a ridiculous value of approximately 2.00 percent and was 2.10 percent in 2007. This failed short of the Maputo resolution that governments of member state of African Union (AU) to allocate at least 10 percent of national budgetary resources for the implementation of the Comprehensive African Agricultural Development Programme (CAADP), which Nigeria is a signatory.

TABLE 6: Budget Estimates of Federal Government Total Expenditure And Agricultural Expenditure

Year	Total Govt. Expd (N' Million)	Total Govt. Capital Expd (N' million)	Total Agric Expd (N' million	Agric Capital Expd (N' million)	Agric Capital Expd(% of Total Capital Govt. (Expd.)	Total Agric Export(% of Total Govt. Expd.)
1970	903.90	187.8	10	5.6	2.98	1.11
1971	997.2	173.6	12.7	8.4	4.84	1.27
1972	1463.6	451.3	33.1	20.7	4.95	2.26
1973	1529.2	565.7	48.8	35.4	6.26	3.19
1974	2740.6	1223.5	112	87.4	7.14	4.09
1975	5942.6	3207.7	250	211.2	6.58	4.21
1976	7856.7	4041.3	147.7	129.2	3.2	1.88
1977	8823.8	5004.6	125	105.5	2.11	1.42
1978	8000	5200	148.1	128.4	2.47	1.85
1979	7406.7	4219.5	356.2	321.9	7.63	4.81
1980	14,968.5	10163.3	468.1	435.6	4.29	3.13
1981	11413.7	6567	809	775.1	11.8	7.09
1982	11923.2	6417.2	1069.2	1035.1	16.13	8.99
1983	9636.5	4885.7	1214.5	1185.2	24.25	12.6
1984	9927.6	4100.1	285.3	252.5	6.16	2.87
1985	10041.1	5464.7	1018.1	985.4	18.03	10.14
1986	16223.7	8526.8	925.4	892.5	10.47	5.7
1987	22018.7	6372.5	394.3	365.1	5.73	1.8
1988	27749.5	8340.1	650	595.7	7.14	2.34
1989	41028.3	15034.1	1062.6	981.5	6.53	2.59
1990	60268.2	24048.6	1966.6	1758.5	7.31	3.26
1991	66584.4	28340.9	672.3	551.2	1.94	1.01
1992	92797.4	39763.3	924.5	763	1.92	1.00
1993	191228.9	54501.8	2835.3	1820	3.34	1.48
1994	160893.2	70918.3	3719.1	2800.1	3.95	2.31
1995	248768.1	121138.3	6927.7	4691.7	3.87	2.78
1996	337217.6	212926.3	5574	3892.8	1.83	1.65
1997	428215.2	269651.7	7929.6	6247.4	2.32	1.85
1998	487113.4	309015.6	11840.4	8876.6	2.87	2.43
1999	358103.2	136984.2	10047.3	6912.6	5.05	2.81
2000	664457.3	311608.8	10596.4	5761.7	1.85	1.6
2001	1018025.6	438696.5	64943.9	57879	13.19	6.38
2002	1188734.6	321398.1	44803.8	32364.4	10.07	3.77
2003	1225956.7	241688.6	16045.2	8510.9	3.52	1.31
2004	1384001.3	351260	49926.4	38669.8	11.01	3.61
2005	1743240	519510	76636.7	60310.7	11.61	4.4
2006	1842587.7	552385.8	107463.9	89544.9	61.21	5.83
2007	1885923.9	830557.93	38833.6	22703.6	2.73	2.10

Note: 2007 is a provisional value and 2002-2007 excludes Statutory Transfers to NDDC, NJC AND UBE.

Policy Inconsistence

Government policies and programmes are critical to agricultural development. Apart from laying the foundation for policy thrust that drives the process, it provides the stakeholders with the necessary information that informs their investment decisions. Inconsistence of policies and programmes breed doubts among investors, and this affects investment, as well as the level of productivity. This has affected government policies and programmes in the country.

Adverse Environment

Environmental challenges are increasingly posing threats to agricultural productivity and aquatic lives in Nigeria. The cultural practice of bush burning and over-grazing has continued to contribute to soil degradation. The reported cases of frequent oil spillage and gas flaring in the Niger Delta also affect the aquatic environment, and farming activities in this region are heavily impeded.

Inequitable Access to Productive Resources

Increasing gender inequality will inhibit access to factors that will engender good and quality life. This include factors as access to credit, education, freedom of expression and freedom from certain cultural and religious impairments that have continued to constitute clogs in the wheels of human development.

Poorly Developed Infrastructure

Poor developed infrastructure is one of the characteristic features of underdeveloped economies. This is heavily manifest in the rural areas, where there is dearth of basic infrastructural facilities. The absence or near decay of basic infrastructural facilities in the rural areas could partly be held responsible for increasing rural-urban migration. A poor transport and communication infrastructures limit market and information access for many farmers in the underdeveloped countries, and consequently increases their cost of production. It is estimated that 60% of Africa's rural population lives in areas with good agricultural potential but poor access to markets (Kelley and Byerlee, 2003). In a third of African countries, transportation costs account for more than 25 percent of the total value of exports, and in Uganda they exceed 70 percent (von Braun et al, 2002), the Nigerian situation may not really be different.

International Agricultural Prices

International agricultural commodity price has continued to experience decline, and this has affected farmers' incomes, especially those in the underdeveloped countries where international agricultural prices volatility are rarely protected by any form of government assistant. Since the 1960s, world prices of most important agricultural commodities including food staples have steadily fallen and this trend is expected to continue (DFID, 2004). Between 1980 and 2003, the prices of agricultural raw materials and food and beverages fell by 60 percent and 73 percent, respectively (UNCTAD, 2003). In 2003, coffee and cotton prices were 17 percent and 33.5 percent of their 1980 real values. From 1997 to 2001 alone, the combined price index of all commodities fell by 53 percent in real terms (FAOSTAT, 2004). The continued drop in the international commodity prices of agricultural products is source of discouragement to farmers.

Ravaging Impact of HIV/AIDS

One of the greatest challenges of agricultural development is the increasing prevalence of HIV/AIDS within the rural and urban areas. This challenge is not restricted to agriculture development alone, but to the entirety of development. It is a cross-cutting issue with links to education, agriculture, labour and defence etc. For example, the HIV/AIDS prevalence in Nigeria has grown from 1.8 percent in 1992, 3.4 percent in 1994, 4.5 percent in 1996, 5.4 percent in 1999, 5.8 percent in 2001 and dropped to 5.0 percent in 2003 (MDG Report, 2005). Although, empirical evidence about its impact on agriculture is limited, it has serious adverse impacts on food security in Nigeria; affecting the availability of labour (which is a key asset of the poor); impeding the transfer of agricultural skills from one generation to the next; and diverting resources that could be used to boost productivity.

Technologies of Production

Development in the science and technology industry has made it increasingly difficult for those lagging behind to effectively compete in the international market. The agricultural production in Nigeria is still dominated by small scale farmers, whose access to the latest techniques of agriculture is very minimal. Technological innovation in the agricultural sector development will increase its productivity, thereby making food available to the people. Lack of availability of food is the most critical dimension of poverty, reflected in the popular saying that "when hunger is excised from poverty, the burden of poverty is light". Increased agricultural productivity will definitely lead to decline in costs and increasing returns to the farmers. However, this has not been achieved with the existing level of technology in the agricultural sector. The reason being that technological innovation in Nigeria is rudimentary and characterized by low agricultural production.

Increased food production will have impact on food prices when there are efficient storage facilities and marketing systems, including food processing. For example, processing technology, which plays key role in on-farm storage, pest control, and reduction of post-harvest losses, is also rudimentary in Nigeria.

Rehabilitation of Agricultural Research Institutions

Agricultural research institutions are encumbered with the aching problems of under funding and neglect from government, as well as the private sector patronage. Success in research requires commitment both from the funding agency and institution concerned. A lot of agricultural research innovations have been abandoned apparently due to inadequate funding and project utilization for commercial purposes.

6.0 Recommendations

This paper concludes by calling for government effort at tackling the constraints to increased agricultural productivity and poverty reduction. It achieves this, by making recommendations considered appropriate for the agricultural development and poverty reduction in Nigeria.

(i) Provision of Supportive Agricultural Policies.

Government should provide supportive agricultural policies that will help farmers in cushioning the reoccurring effects of international agricultural commodity prices, as well as those that hinder increased agricultural production. For example, during the Structural Adjustment Programme (SAP), the government's input price subsidies were steadily reduced, and the naira exchange rate devalued. The devaluation of the naira exchange rate was expected to boost export, but this was happening when the international agricultural commodity prices were going down. Though, it improves producer prices, it also raised the cost of farm inputs, thereby limiting there use by farmers, who constitute the bulk of agricultural producers in the country. Government should endeavour to provide supportive agricultural policies that will boost production.

(ii) *Increased and Efficient Public Spending*

Increased and efficient public spending on agriculture, particularly in the areas of roads, irrigation and agricultural research will be highly effective in increasing agricultural productivity and reducing poverty. This will be achieved through reduction in cost of production, increased supply of commodity that will improve income of rural farmers. Though, public spending in this sector had been grossly inadequate and poorly directed, weak governance has continued to hunt the available scare resource. Good governance and fiscal transparency should be embraced in order that resources channeled towards infrastructure and services development will achieve their targets.

(iii) Market Failure

Efficient and effective produce marketing mechanism is necessary in realizing agricultural potentials for poverty reduction. Providing efficient and effective markets, that are accessible to poor people, require policies and programmes, which will reduce the transaction costs and risks that inhibit the private sector participation. As said earlier, increasing infrastructural development will help in arresting the dwindling fortunes of agriculture. Furthermore, considering the place of agricultural in economic development, government should provide the necessary safety values which will cushion the impact of market failures.

(iv) Finance Gap.

High cost of capital (high interest rates) and existing anomalies in lending for investment in agricultural production should be addressed. While the cost of raising funds through the money market is high, there is, this existing anomaly, which relates to credit availability; disbursement of loans after the planting season, as well as the actual disbursement falling short of loan approval. Again, there is this complaint of increasing loan defaulting which hinders banks from providing loan facilities. Limited access to finance, particularly short-term seasonal credit, remains a major obstacle to poor farmers in Nigeria, who are investing in agricultural production. Government should provide stable macroeconomic environment, which will address the high interest regime and encourage credit facility to the sector.

(v) Improve Access to land and Water

The country is richly blessed with abundant land and water resource for the production of cash and food crops, livestock and forestry products. With 75 percent of arable land and less down 40 percent under cultivation, there is no doubt that the country still provides potential for agricultural growth and poverty reduction. What, it requires is the judicious management of its land and water resources. The introduction of the Land Use Decree of 1978, which vested greater ownership of land in the government, seems to have been grossly abused. This is, because there are strong allegations of large hectares of land being allocated to “would-be” farmers that till today were not put to cultivation. Yet, the bulk of export crop producers are smallholder farmers, who have little or no access to large land and irrigation services. Government policies and programmes should be directed at helping the farm smallholders to secure lands for cultivation. This may be achieved by reviewing legal and administrative procedures and strengthening the financial position of the poor.

(vi) Science and Technology

The place of science and technology in agricultural development cannot be overemphasized. One of the major problems confronting agricultural production in Nigeria is the continuing use of inefficient traditional practices and inappropriate technologies. Being conscious of the dynamic nature of technology, the adoption and management of modern agricultural technology-modern farming and husbandry depends on adequate knowledge about them. This could be realized through massive agricultural extension services, community broadcasting, rural exhibitions, etc.

(vii) Policies Consistency

Policy consistency and macroeconomic stability are necessary for predictable investment climate. Policy inconsistency discourages investment and this affects the output of goods and services. Government should be seen as a continuum, and its favourable polices and programmes sustained, whenever there is change in the leadership structure. The often change of policies sends wrong signal to the investment community, and perhaps discourages realization of prior policy targets.

Conclusion

Agriculture still remains at the core of economic activity in Nigeria in term of its employment and income generations as well as inter-linkages with other sectors of the economy. With roughly 75 per cent of her land being arable, of which about 40 per cent is under cultivation, the sector's prospect for growth and vehicle for poverty reduction is not in doubt. The Nigerian government's realization of this vintage position of agriculture as an instrument for fast-driving her economic growth will not be out of place if pursued with vigour and all seriousness.

REFERENCES

Adubi, A.A. (2001) "Agriculture in Nigerian Economy: An Overview" Paper presented at the Workshop on Planning and Management Of Agricultural Sector, August 14-25, 2000 (Ibadan: NCEMA)

Aigbokhan B.E. (2001) "Resuscitating Agricultural Production (Cocoa, Cotton, Groundnuts,
Palm Oil, Rubber, etc) for Exports". Cited in CBN Proceedings of the 10th Annual
Conference of the Zonal Research Units, 2001.

Ajakaiye, O. (1998) "Conceptualization of Poverty In Nigeria" Cited in CBN Proceedings of the 7th Annual Conference of the Zonal Research Units, 1998.

Anyanwu, J.C, Oaikhenan, H., Oyefusi, A. & Dimowo, F. A. (1997) The Structure of
Nigerian Economy (1960 1997). Anambra State Nigeria; Joanee Educational Publishers Ltd.

Atoloye, A. S. F (1997) "Strategy For Growth-Led Poverty Alleviation In Nigeria" Central Bank of Nigeria Economic and Financial Review, Vol. 35, No. 3

Beghin, J.C., D. Roland-Holst and D. van der Mensbrugghe (2002) " Global Agricultural Trade and the Doha Round: What are the Implications for the North and south?" Working Paper 02-WP 308. Center for Agricultural and Rural Development, Iowa State University Iowa-USA

Bell, C., P. Hazell and R. Slade (1982) Project Evaluation in Regional Perspective. Johns Hopkins University Press, Baltimore.

Block, S. and P. Timmer (1994) Agriculture and Economic Growth: Conceptual Issues and the Kenyan Experience. Harvard Institute for International Development, Cambridge, MA.

Brown, M. M. (2005) "Within Our Graps: Decisive Action On Poverty" Global future, a World Vision Journal of Human Development, Second Quarter.

Central Bank of Nigeria/NISER (1992) "The Impact of SAP on Nigerian Agriculture and Rural Life" Vol. 1, The National Report, January.

Delgado, C., J. Hopkins and V. Kelly (1998) "Agricultural Growth Linkages in Sub-Saharan Africa". IFPRI Research Report 107. International Food Policy Research Institute, Washington DC.

De Janvry, A.; Sadoulet, E. 2002. World poverty and the role of agricultural technology: direct and indirect effects. *Journal of Development Studies*, 38 (4), 126

DFID (2003) "Agriculture and Poverty Reduction: Unlocking the Potentials" . Policy Paper, December

DFID (2004) "Rethinking Tropical Agricultural Commodities". Agriculture and Poverty Reduction Working Paper 10, DFID, London. Available at http://dfid-agriculture-consultation.nri.org/process.htm

DFID (2005) "Growth and Poverty Reduction: The Role of Agriculture" Policy Paper, Dec.

Ellis, F. (2000b) Rural Livelihoods and Diversity in Developing Countries. Oxford University Press, Oxford.

Evbuomwan, G., Ukeje, E. U., Otu, F., Amoo, B. A., Essien, E. A., Odey, L.I., & Abba, M. A. (2003) "Agricultural Development: Issues of Sustainability" Published in Contemporary Economic Policy Issues In Nigeria. Nnanna, O. J., Alade, S. O., & Odoko, F. O (eds.), Central Bank of Nigeria

Essien, A. E. (2005) " A Consistent Macroeconomic Framework For The Agricultural Sector Under the National Economic Empowerment and Development Strategy (NEEDS)" CBN, Bullion Vol. 29, No. 4, Oct. /Dec.

FAOSTAT (2004) Available at http://www.faostat.fao.org

Federal Office of Statistics (1999) "Poverty And Agricultural Sector" , Abuja- Nigeria, October.

Gallup, J. S. Radelet and A.Warner (1997) "Economic Growth and the Income of the Poor". CAER II Discussion Paper No. 36. Harvard Institute for International Development, Boston MA.

Hazell, P. (2005) "The Role of Agriculture And Small Farms In Economic Development". Paper presented at "The Future of Small Farms" research workshop, June 26-29, 2005, Withersdane Conference Centre, Wye, UK.

Hazell, P. and B. Hojjati (1995) "Farm / Nonfarm Linkages in Zambia". Journal of African Economies, 4(3): 406-435.

Hazell, P. and C. Ramasamy (1991) "The Green Revolution Reconsidered: The Impact of High-Yielding Rice Varieties in South India". Johns Hopkins University Press, Baltimore and London.

Helleiner, G.K (1966) "Peasant Agriculture, Government Economic Development In Nigeria" Irwin Illinois, P.A.

Igbuzor, O. (2006) "Review of Nigerian Millennium Development Goals 2005 Report" Actionaid International Nigeria

Irz, X.; Lin, L.; Thirtle, C.; Wiggins, S. 2001. Agricultural Growth and Poverty Alleviation.
Development Policy Review, 19 (4), 449466.

Jimaza, M. and Sani, E. I. (2003) "Agricultural Production and the Economic Development of Nigeria" Journal of Development and Society, Vol. 1, No. 4

Johnston, B. F. and Mellor, J. W. (1961) "The Role of Agriculture In Economic Development" American Economic Review (September) Pp. 566-93

Kelley, T. and D. Byerlee (2003) " Surviving on the Margins: Agricultural research and Development Strategies for Poverty reduction in Marginal Areas". World Bank, Washington DC.

Lipton, M. (2004) New Directions for Agriculture in Reducing Poverty: The DFID Initiative. Available at: http://dfid-agriculture-consultation.nti.org/launchpapers/michaellipton.html

Lipton, M. (2005) "Can small farms survive, prosper, or be the key channel to cut mass poverty?" Presentation to FAO Symposium on Agricultural Commercialization and the Small Farmer, Rome, 4-5 May 2005

Maxwell, S. (2004) Launching the DFID consultation " New Directions for Agriculture in Reducing Poverty". Available at http://dfid-agriculture-Consultation.nri.org/launchpapers/simonmaxwell.html

Ministry of Agriculture (2001) "New Agricultural Policy Thrust" Federal Ministry of Agriculture and Rural Development, Abuja.

MDGs (2005) "Nigeria Millennium Development Goals Report" National Planning Commission, Abuja - Nigeria

National Economic Empowerment And Development Strategy (2004) Document produced by the National Planning Commission (NPC), Abuja

Nugent, (2000) "The impact of urban

agriculture on the household and local economies". In
N. Bakker, M. Dubbeling, S Gundel, U. Sabel-Koscella and H. de Zeeuw (eds.) Growing Cities, Growing Food, DSA, Eurasburg.

Obadan, M. I. (1994) "An Econometric Analysis of Rubber Export in Nigeria" NCEMA Occassional Paper

Okereke-Onyiuke, N. (2006) "A Review of the Performance of The Nigerian Stock Exchange in 2006" Nigerian Stock Exchange (NSE), 2006, Lagos-Nigeria.

Okunmadewa, F. (1996) "Nigeria: Poverty Reducing Growth Strategies and Options" CBN/World Bank Collaborative Study, Proceedings of the Workshop on Nigeria: Prospects For Development (Vision 2020) April, 1996

Olomola, A. S.(1998) "Analysis and Management of Agricultural Sector Performance and Inter-sectoral Linkages", paper presented at the Training Programme on Sectoral Policy Analysis and Management, NCEMA: Ibadan, June.

Op. Cit., Igbuzor, O. (2006) "Review of Nigerian Millennium Development Goals 2005 Report" Actionaid International Nigeria

Ozo-Eson, I (1998) "Income Inequality and Poverty In Nigeria" Cited in CBN Proceedings of the 7th Annual Conference of the Zonal Research Units, 1998

Sachs, J. (2005) "The Year of Development" World Vision Journal of Human Development, Second Quarter.

Smith, L. and L. Haddad (2002) " How potent is economic growth in reducing undernutrition? What are the pathways of impact? New cross-country evidence". Economic Development and Cultural Change 51(1): 5576.

Sudharshan, C. Nwafon, J. and Thomas, S. (1995) " The Evolution of Poverty and Welfare In Nigeria" World Bank Analytical/Working Papers, July.

Tangermann, S. (2003) "Cutting Support Can Help Farmers to Prosper". The Financial Times, 22 August.

Thirtle, C., X. Irz, L. Lin, V. McKenzie-Hill and S. Wiggins (2001) Relationship between Changes in Agricultural Productivity and the Incidence of Poverty in Developing Countries. Report commissioned by Department for International Development, London.

UNCTAD (2003) Economic Development in Africa: Trade Performance and Commodity Dependence. United Nations, New York.

Wiggins, S. (2006) "Agricultural Growth and Poverty Reduction: A Scoping Study" IDRC, Ottawa-Canada, Working Papers on Globalizations, Growth and Poverty, No. 2, March

von Braun, J., P. Wobst and U. Grote (2002) "'Development Box' and Special and Differential Treatment for Food Security of Developing Countries: Potentials, Limitations and Implementation Issues", ZEF Discussion Papers on Development Policy, Bonn.

World Development Indicator (2007) Annual World Bank Publication, USA.

Increasing Mortgage Finance Efficiency In Nigeria

By TIMOTHY OLUGBENGA NUBI* (Ph. D)

ABSTRACT:
Absence of a mortgage financing mechanism has been widely reported to be one of the most telling indices of underdevelopment. The huge capital outlay involved makes housing the largest form of investment decision by most family making credit inevitable for its procurement. Several efforts had been made in Nigeria to build a sustainable mortgage finance system but there are very few results to show for the efforts. This paper is a comprehensive appraisal of the primary mortgage banks in Nigeria. The survey covers the operating primary Mortgage Institutions (PMI) Lagos and Abuja. The result revealed that the PMIs are undercapitalized and unbundled. Absence of secondary mortgage and mortgage insurance together with poor operation that relies heavily on manual and not taking advantage of IT. It was recommended that PMI should be recapitalized, mortgage insurance introduced, and mortgage finance unbundled while the deposit money banks be encouraged to invest in mortgage.

INTRODUCTION

Home ownership, in most parts of the world, is usually the largest investment decision in the lifetime of an average family (Christian, 1990). The capital outlay involved often necessitates borrowing. Where credit is available, the house is purchased and the loan is later amortized over a period of about 20-30 years. Where there are no credit facilities, since home consumption cannot be deferred, construction is embarked upon on incremental (progressive housing) basis, creating new slum or urban sprawl and its attendant socio-economic problems.

According to Nevitt (2001), the invention of mortgage finance is of equal significance as the invention of steam engine in Britain in 18th century. Absence of a mortgage-financing mechanism according to Adams (1992) is one of the most telling indexes of underdevelopment (see Table 1). In countries with

* Dr Nubi is a Senior Lecturer & Sub Dean, Faculty of Environmental Sciences, University of Lagos, Lagos, Nigeria and President, Ideal Habitat Initiatives (a Non Governmental Organisation). The views expressed in the paper are those of the Author and do not in any way represent the views of the University of Lagos or Ideal Habitat Initiatives.

the highest per capita incomes, a middle-class breadwinner must still have twice his annual gross income to buy a modest house, but by the time he can accumulate it, he may be dead. Since urbanization has been universally accompanied by rising costs of homes, a shortage of capital for the purchase, and a gap between income and shelter cost, the only way of acquiring a home is by going into debt.

A good house should last at least a lifetime. In the more developed nations where a mortgage system exists, the house is built first and paid for in installments out of earnings. According to Christian (1990) if there is no financing mechanism, families have no alternative but to rent (if they can), build a cheap makeshift, crowd into small spaces squat, or sleep on the streets. Absence of a mortgage system can lead to stagnation of the building and materials industries, increased unemployment, social discontent, and in some instances even political upheaval. In underdeveloped nations effort had been made have sought to set up various mechanisms to finance home building. Most of the devices are crude and ineffectual.

The fact that a government mortgage fund exists does not always mean that it functions. The statement in the UN report is as relevant today for many countries as it was in 1954:

….*the mere passage of a law does not mean it will work; a loan program must be so drawn as to reach the greatest pool of possible borrowers; experienced personnel is indispensable; restrictions night express the desire for safety but simultaneously be too unpractical to allow the program to function; the whole business of mortgage lending is a highly technical operation, which calls for the best skills available in the business; the experience of one country in financing cannot be blindly copied by another and made to work.*

The modern method of housing finance emerged from the U.S. Apart from its great contribution to the wealth of America. Mortgage finance has resulted into 74% home ownership in 2003. This has since increased with about 43 million mortgage loan as at 2008. Table 1 shows the contribution of mortgage to GDP in various countries. It is pathetic that while mortgage constitute about 87% GDP in Denmark, it is less than 0.5% in Nigeria. The development of mortgage industry probably explains why some countries are rich while some are poor, developed and underdeveloped, advanced and in transition, emerged or emerging. The extent to which a nation is transiting from developing to developed depends on efforts put at building prerequisite housing finance infrastructure, legal, physical and economy. This paper is an attempt at examining the state of mortgage finance in Nigeria and presents a road map towards building a robust mortgage finance market as an engine for the nation's socio-economic transformation.

Table 1: Residential mortgages as percentage of GDP

Rank	Country	%
1	Denmark	87.5
2	USA	71.0
3	UK	70.4
4	Germany	54.3
5	Portugal	50.6
6	Sweden	50.0
7	Ireland	45.0
8	Spain	42.1
9	Finland	35.6
10	Hong Kong	31.0
11	Nigeria	0.38

Source: UN-HABITAT 2005 Report on “Financing Urban Shelter” p29

MORTGAGE FINANCE IN NIGERIA

The Federal Minister of Works and Housing, Chief Tony Anenih, in February 2000 expressed concern over the appalling state of housing finance in Nigeria. He saw no reason why mortgage banking that worked in other nations could not work in Nigeria. Previous studies by Abiodun (1999) and Okupe (2000) show that it succeeded in other countries. The modern housing finance model base on secondary market has become deeply rooted and South Africa, a nation that got liberation from apartheid region about a decade ago, has recorded considerable progress in housing finance.

The evolution of mortgage banking in Nigeria can be traced to the establishment of the Nigeria Building Society in 1956. The society collapsed in early seventies due to its inability to perform its statutory function. This led to government injecting N20m and changing its name to Federal Mortgage Bank of Nigeria (FMBN) in 1977.

At no time was the bank able to meet up with the pressure of demand. In 1979, outstanding application was N223.8 million and available funds equalled N127.0 million, meaning that demand and supply was in the ratio of 2:1. This degenerated to ratio 4:1 in 1986 when the outstanding application increased to N465.8 million and only N105.3 million was available (FOS) 1986. The failure of the FMBN over the years and acute shortage of housing led to the promulgation of the National Housing Policy of 1991. There is no doubt that both the Policy of National Housing Fund and the decree of 1992 was promulgated to strengthen the housing industry, especially its financial sector. The mandatory savings provision of the policies is meant to resolve this.

The banks are mandated to contribute 10% of their loanable fund to the Fund while insurance companies are to contribute 40% of their life insurance premium to the fund. The contribution, which was N19.9 million in 1992, only increased to N5.26 billion in 2000 and N24 billion in 2008 (FMBN 2007). This is mainly a deduction from the salaries of government workers and very few private companies and is less than 10% of the projected collection for the period (See Table 2).

TABLE 2: NHF COLLECTIONS BETWEEN 1999 and 2007

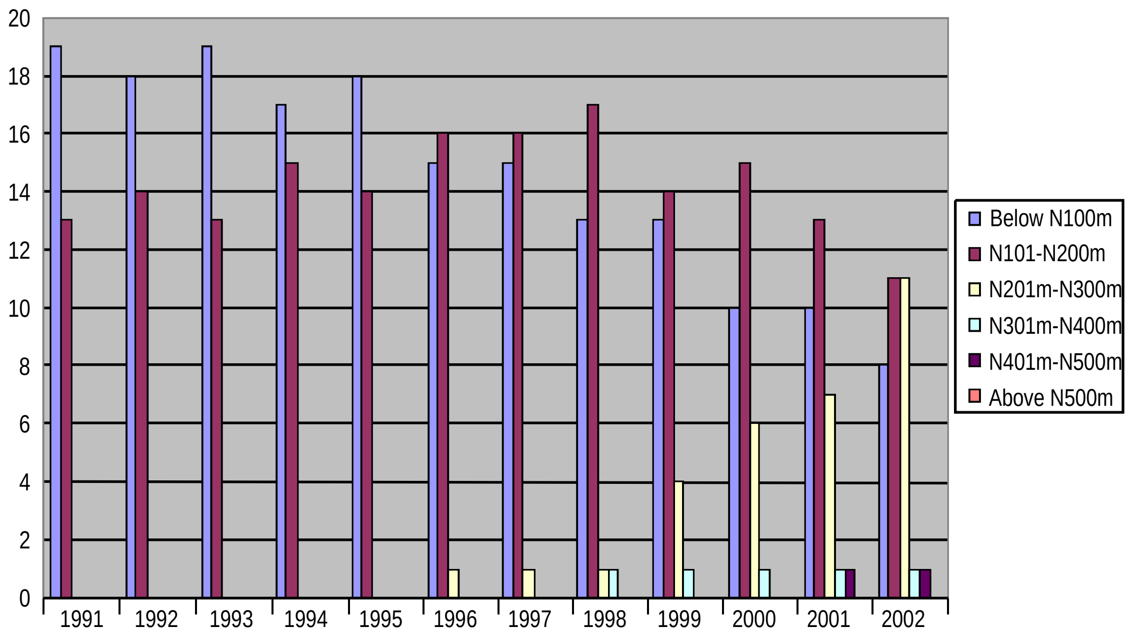
Year	Amount (N Billion)
1999	1,550,000,000.00
2000	1, 750,000,000.00
2001	2,000,000,000.00
2002	1,900,000,000.00
2003	1,800,000,000.00
2004	2,400,000,000.00
2005	4,100, 000,000.00
2006	5,000,000,000.00

Source: M.I. Atagher FMBN 2007

PRIMARY MORTGAGE INSTITUTIONS

The business of PMIs is primarily to advance loan to potential borrowers for house ownership. The amount of loan originated, therefore, depends on the capital base of the PMIs. The requirement for licensing was N5m in 1992. This was increased to N10m in 1996 and the N100m in 2001 (FMBN). It was not until 1996 that one PMI recorded N100 million capital base. As at 2002, 8 (25%) have not been able to meet up with the required N100 million capitalization. The research revealed that in 2002 only one (1) PMI has between N401m-N500m and none has more than half a billion naira (See Figure 4.3). CBN in November 2004 warned that PMIs that had not met up with the N100m should do so or have their license withdrawn (The Guardian 2004). With the N25billion capitalization base regime imposed on commercial banks other financial sectors like the PMIs and Insurance became. The PMIs' inability to meet up with the N100m capitalization calls for concerns. With the loan ceiling being pushed to N5m, it means PMIs with limited capital base can only grant an average of N2m loan to 50 applicants.

Figure 4.3.Organizational Share Capital



Source: Nubi Field Survey 2006

Operations

The operations of PMIs remain bundled; all their operations are done in-house. This has limited accessibility. If operations are unbundled, mortgage brokers, for instance, will be licensed to operate. Mortgage brokers by the level and size of the firms require little capital to start and operate. They usually act in most part of developed economies as originators and servicers of mortgage. Their operations often bring phenomenal increase in the volume of origination of loans. The insurance companies are very good examples of this model.

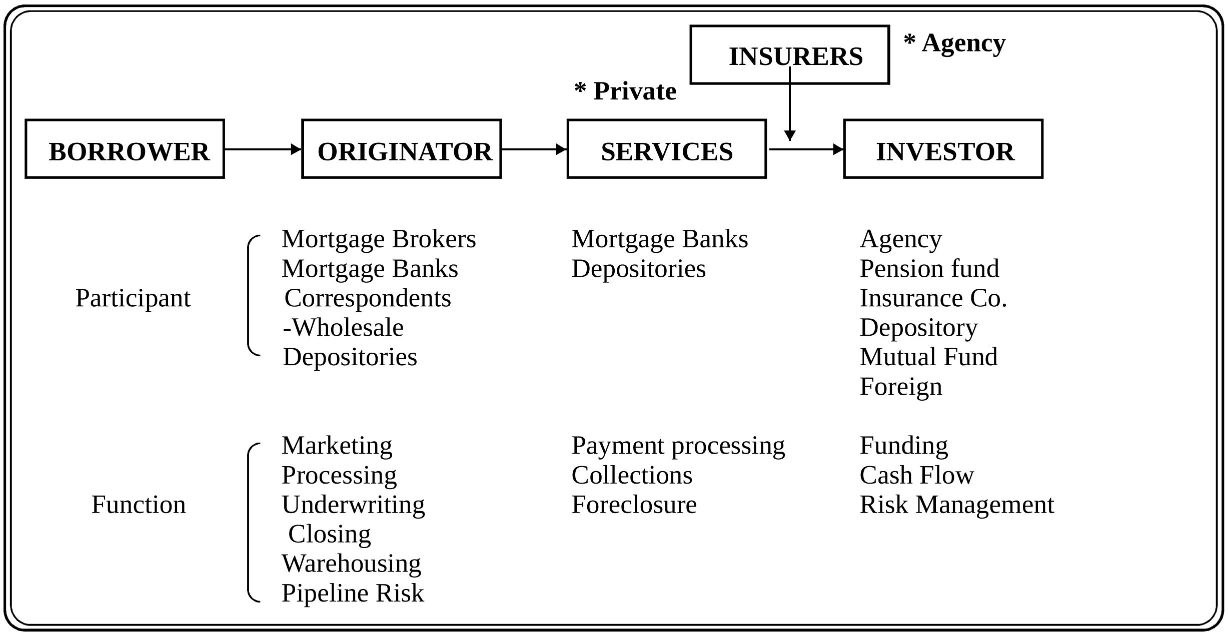


Figure 2: Unbundled mortgage system. Source: Lea (2000:7)

Many vehicle owners in remote settlements in Nigeria do insure their vehicles without coming to the cities.

Location

Location is believed to be an essential factor in determining the degree of physical accessibility, hence the overall effectiveness of mortgage finance. About 70% of the operating PMI(s) are in Lagos and Abuja. It was discovered that out of 58 PMIs in Lagos, 40 are in Victoria Island. By the virtue of their location, they are only accessible to the high worth bracket in the society. Mortgage operation in its ideal state, according to Vuyisani (2001) requires face-to-face transaction. The distance imposed by location is, therefore, an accessibility constraint. PMIs in Abuja are also at the central district. None in areas with great demand like Kuboi, Karu, Suleja, etc. In other states of the federation, the PMI(s) are located in the state capitals. Town and cities like Shagamu, Ijebu-Ode in Ogun State with population of about 500,000 each have no PMI. This confirmed Agbola (1997) claim that mortgagors do incur more than what they needed to amortize their loan on transportation from Shaki to Ibadan in Oyo State.

About 60% of the PMI(s) operate frmtheir main office without any branch. 28% have 1-3 branches, 6% operate between 4-6 branches while another 6% have more than 6 branches. Those that have more than 6 branches are subsidiaries of commercial bank. This category of PMIs, - like Union Homes, a subsidiary of Union Bank and Co-operative, Savings and Loan of Co-operative Bank, use that parent companies location advantage to run their mortgage business.

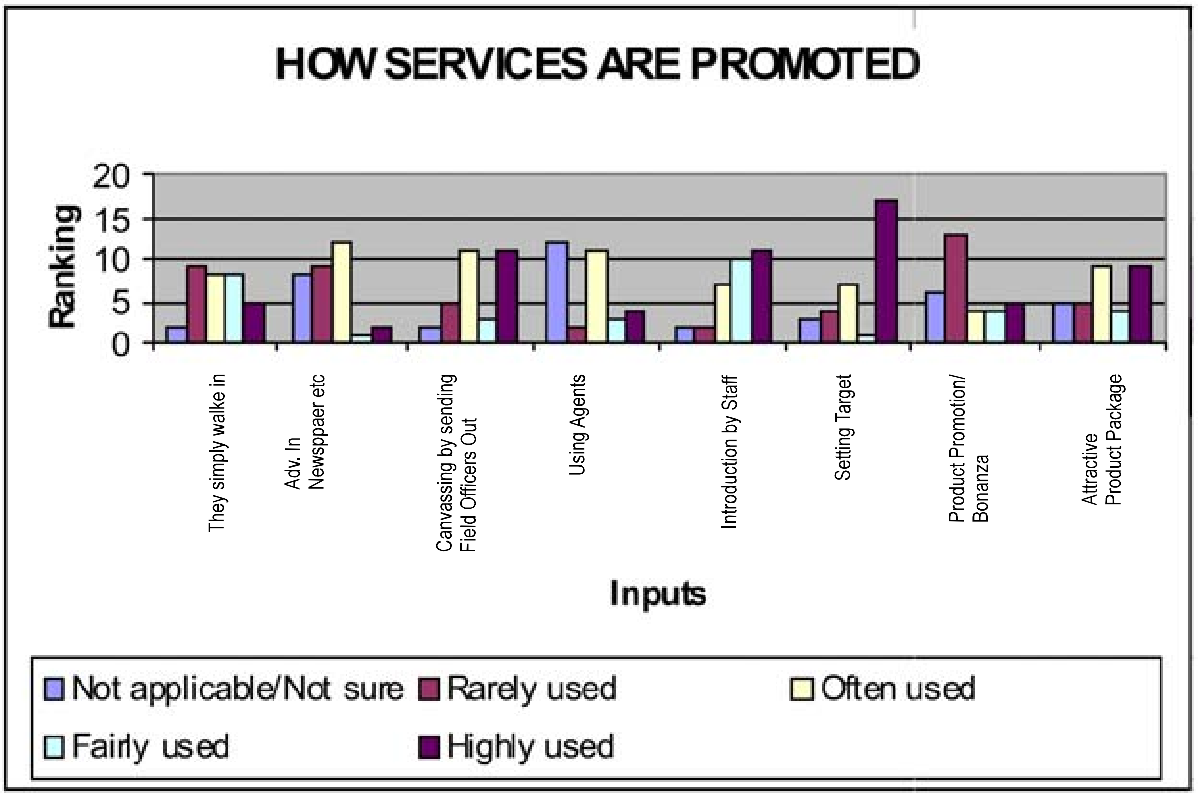
Use of Information Technology (IT) and Unbundling, Marketing variables

Information Technology (IT) plays a significant role in today's business. Apart from speed, it also helps to create broad access where most potential borrowers are connected to internet. According to Lee (2002), about 60% of mortgage origination and servicing in the United State are now done on line. It is shocking to discover that 46% of the PMIs do not have e-mail facilities and 46% do not have Internet services. Some 18% do not use computer at all for their operation, another 18% cannot check customers' balance on line. While 68% cannot link their branches, another 65% do not provide on line payment system.

Service Promotion

On how PMIs promote their services, 29% of all the PMIs never use brokers, while 8% of them rely on setting targets for staff. This is the highest mode, followed by introduction of customers by staff canvassing through field offers, which is common among 5% of staff. Some 15% and 13% use product promotion and attractive packages. Radio and newspapers are the popular methods of advertisement and are only being used by 20%. It is worthy of note that advertisement is not popular among PMIs.

Figure 3:Promotion of Services



Source: Nubi Field Survey 2006

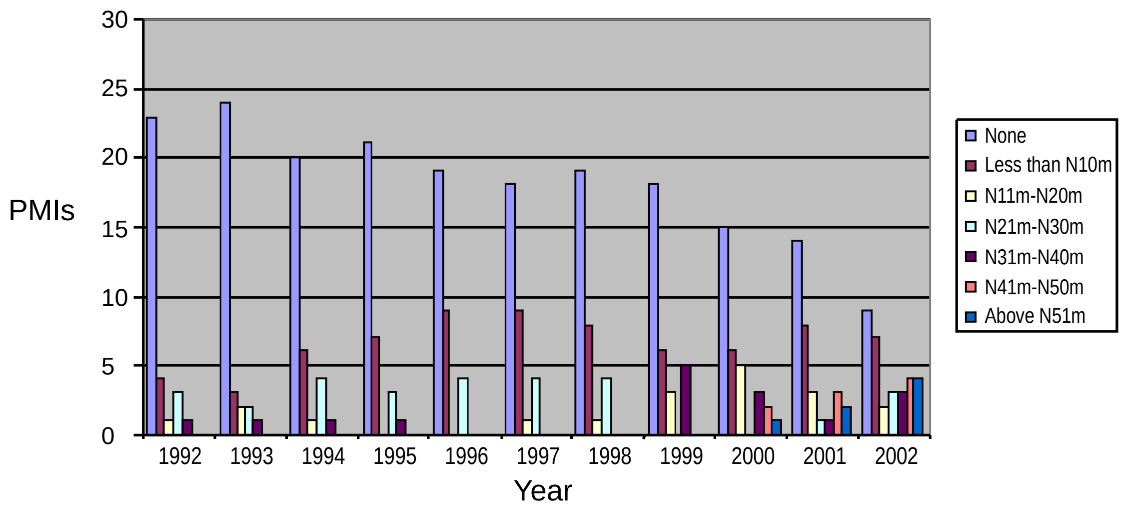
Access to Secondary Market

The importance of this cannot be over-emphasized in terms of liquidity. Once PMIs are not liquid, their operations cannot be sustained. The only means through which PMIs can sell their block loan is through the FMBN who, for now, operates as the secondary mortgage market (SMM) in Nigeria. The condition for accessing NHF has been described by PMI as too stringent especially the demand for block mortgage of securitization to be sold as well as other PMI assets as collateral a situation that the PMI described as over collaterization.

Crossing these hurdles had been very challenging to operating PMIs. This is responsible for their low patronage of the product, thus, creating a big distortion in the market. It is unfortunate that FMBN itself has limited fund but is trying hard to develop. The N100 billion bond floated in 2006 was a step in right direction but face challenges of been replicated because of several concession it enjoyed.

CUSTOMERS RELATED MATTERS

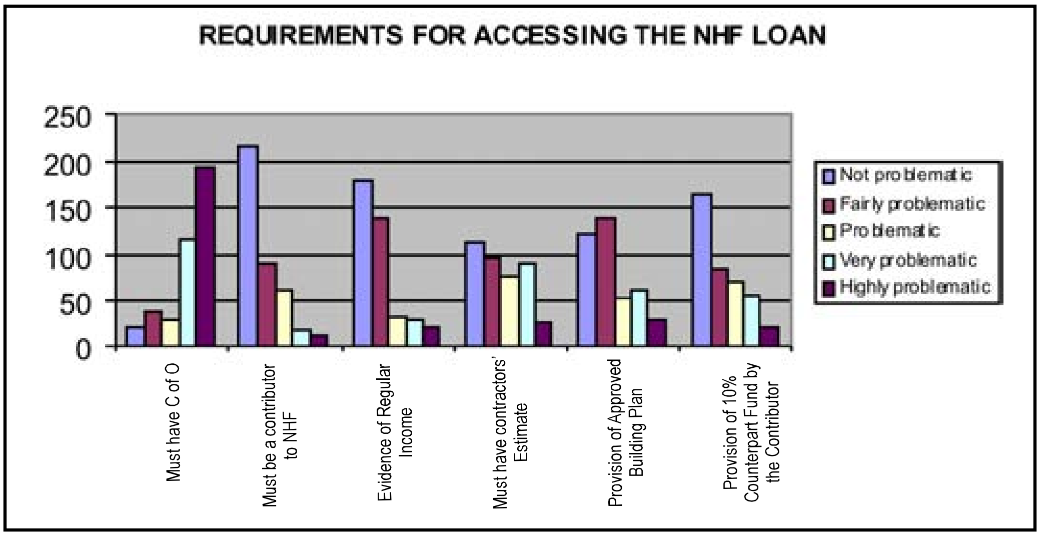
Figure 4.Savings Deposited by Customer



Source: Nubi Field survey 2006

From figure 4 above, it can be seen that the saving improved only in 1999. PMI started recording savings up to N50m in 2000. Saving, according to Christian (1986) is the bedrock of a sound mortgage finance system. Predominant among these is low income and high poverty level of most Nigerian (Okumadewa 1998). Profit after tax as shown in Figure 4.5 has remained equally very low. It is predominantly under N10miliion for most PMI. Only 3 PMIs made between N11 and N20m in 1997. Only one PMI (Union Homes) had consistently declared more than N50m profit since 1996.

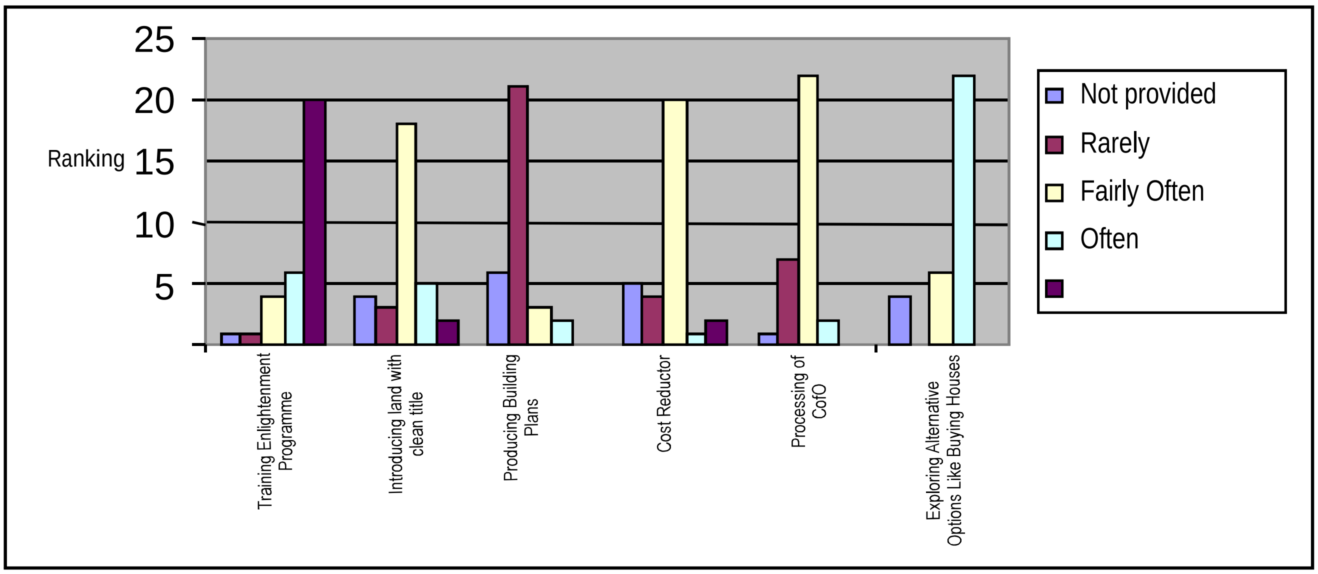
Figure 5. Stringent Requirements for Accessing the NHF Loan



Source: Nubi Field Survey 2006

Figure 5 shows that C of O was ranked as most highly problematic and very problematic among other requirements. Also ranked high, although fairly problematic, is the need to have regular income. This may not be unconnected with high rate of job losses in the last few years in Nigeria. Among the requirements viewed as non-problematic are mandatory savings of 2.5% to NHF and regular income, 10% counterpart funding. Term and condition of loans where equally assessed and found not to be problematic to fulfill.

Figure 6.Assistance Offers to Customers



Source: Nubi Field Survey 2006

On assistance offered to customers and the mode, 5% claimed to assist customers in accessing loan through training and enlightenment programmes on how they can meet banks requirements, only 19% help customers to acquire land with unencumbered or clean title and 24% on building cost reduction through project planning. As many as 28%, 5% and 19% of the PMIs help their customers to process approved building plan, C of O and how to embark upon purchase of housing units.

Interest Rate and Loan to Value (LTV) Ratio

Interests charged by PMIs ranged between 20-40%. This is quite high for mortgage considering the low yield and long-term nature of the underlying properties. According to Lea (2001), low interest rates as well as high LTV are two clear indicators of mortgage finance efficiency. In the United States and United Kingdom, interest rates are as low as 4%. The study revealed that only 25% of PMIs charge less than 10% as interest on home ownership loan, 62% charge 10-20% while 12% charge above 20%. For commercial property, which is the preferred type of loan by most PMIs, charges on interest rate are about 40% (The Guardian 2005). Most PMIs require as high as 40-60% down payment before loan could be granted and balance are usually expected within 12 months, making housing a 'cash and carry' commodity like any other commodity in the open market.

Table 2.1, 2.2 and 2.3 demonstrates the importance of long term interest on affordability of housing. The longer the term, the lower the repayment and the higher the affordability.

Table 2.1 Interest rate at 15% p.a. for N3million

Tenure	5yrs	10yrs	15yrs	20yrs	25yrs	30yrs
Monthly Rentals (Princ + Int)	71,369.79	48,150.49	41,654.28	39,128.69	38,024.92	37,516.65

Table 2.2 Interest rate at 10% p.a. for N3million

Tenure	5yrs	10yrs	15yrs	20yrs	25yrs	30yrs
Monthly Rentals (Princ + Int)	63,741.13	39,395.22	31,904.82	28,575.65	26,861.02	25,910.48

Table 2.2Interest rate at 10% p.a. for N3million

Tenure	5yrs	10yrs	15yrs	20yrs	25yrs	30yrs
Monthly Rentals (Princ + Int)	56,613.70	31,569.65	23,390.48	19,423.67	17,137.70	15,687.98

Housing stock created through PMI loans and time taken

Developments financed by PMIs show an increasing trend from 1999. No PMI granted more than 10 loans per annum before 1998. The result also shows that loans for owner-occupier type of houses lagged behind commercial properties.

About 71% of grantees reported that they have only completed less than 20 houses from loans approved in the last five years. Another 26% have 40-60 houses to their credit and only 3% of the PMIs have more than 100 houses financed till date. 50% of the PMIs claimed to have accessed NHF for their customers, 13% have not while 37.5% claimed to have their applications with FMBN under processing.

On time taken to get loan approved, 41%of the PMIs claimed that it takes over 13 months. This is in agreement with Ogunleye (2002), who claimed that long delay in granting approval which is often more than 13 months was a major factor that led to collapse of PMIs in the past.

Mortgage Insurance

In order to achieve robust mortgage finance, a transition economy like Nigeria according to Andrejus (2002) has to overcome certain specific issues that generally have been solved in most of the market economy countries. These issues, or risks to be more precise, could be divided into two groups: Political and Economic. The long term nature of mortgage finance exposed lenders to greater risks especially in volatile economies like Nigeria. Mortgage finance is like a tripod with PMI, secondary market and insurance as the three legs. For the tripod to stand, it therefore requires the three legs. Unfortunately until recent time, the insurance industry in Nigeria has nothing to write home about.

If housing finance risks can be reduced, one of the major controls on mortgages currently applied, which is the initial down-payment, may be decreased. In general practice, banks without additional guarantees may efficiently function only in the set risk scale (for example, a maximum loan-to-value ratio of 70%). Nations with economies in transition face the situation of higher instability, so property values may also fluctuate significantly. This means that banks striving to avoid the risk of loss on property disposition would request a higher initial down-payment from a potential mortgage recipient. Having the additional safeguard from these risks through insurance, the banks have an opportunity to decrease down-payment requirement.

The second important result achieved according to Andrejus (2002) is the decrease in the mortgage interest rate. In the situation when the mortgage issued is insured, the bank has less need of covering risks with the mortgage interest rate. Furthermore, the premium paid by the insurance company may also cover the costs related to losses not covered by properly recovery. Having the opportunity of insuring the mortgages issued, and in this way eliminating most risks, banks are interested in obtaining insurance on the majority of mortgages issued. In such situations, interest rate discounts may be applied for such mortgages.

ROAD MAP

To make the PMIs play significant roles in housing finance, urgent measures that emerged from this study should be taken. Among these are:

i. Publicity. The claim of most IPDs, not to be aware of operations and opportunities in Mortgage Finance is worrisome. PMIs should embark on massive mobilization of people using various media. This should include television, radio, internet, street awareness campaign and even carnival and lottery. This is crucial to the survival of the industry. Such awareness will lead to increase in savings and, subsequently, the number of loan originated.

ii. PMIs should embark on massive training of staff. This may require collaboration with universities and other research centres. Overseas training may be required to really get the PMIs to understand the complexity of contemporary finance system which involves use of IT for daytoday operation.

iii. PMIs should focus on organization for total package of their product. This involve working with the housing co-operatives which are on ground in many establishments like universities, ministries and parastatals like PHCN, NITEL etc. Informal sectors like Road Transport Union can also be mobilized. The PMIs should be involved in land acquisition for such projects. Membership of such organization must be sufficient for loan approval as the group will be held responsible for the default of any member.

iv. Accessing the Secondary Mortgage Market (SMM) is crucial for the expected increase in origination. This is the only way to solve the problem of illiquidity in the PMIs. This requires development of capital products like Mortgage Backed Security, Bond, Real Estate Investment Trust (REIT)

v. Another critical product that must be developed as a matter of urgency is the Mortgage Insurance Market to offer title insurance, construction Risk Insurance, Rent insurance etc. This is with thorough understanding that mortgage finance is like a tripod with origination and secondary as 1st and 2nd leg while insurance form the third leg.

vi. The 1989 Decree on PMIs should be revised to make it fully congruent with CBN's taking full control of the regulatory and supervisory framework, which should be transformed to largely parallel the existing framework applied to banks.

The list of authorized PMI activities should be extended at least in the housing sector, to include (non-exhaustive list):

- refinancing of existing mortgage loans
- residential second mortgages (provided that loan-to-value ratios limits are met)
- loans and equity funding for housing developers, with tight credit risk and concentration limits
- loans to housing cooperatives and housing rental investors (with prudential underwriting criteria)

The Mortgage Bank Association is requesting that PMIs have the right to mobilize foreign exchange resources, obtain direct access to treasury bills market (currently through banks), and open check accounts. The researcher does not have sufficient access to financial data to analyze these requests, but would note that foreign exchange mismatches may become a dangerous substitute to current term mismatches in *naira.*

The statutory reserves made by PMI to FMBN (currently 5% of their total savings remunerated at 8% since 1999) should be transferred to the CBN. If PMIs are then effectively supervised in accord with an improved prudential regulatory framework in line with that of commercial banks, the NDIC may consider extending deposit insurance to sound PMIs. While this would enable PMIs to better compete with banks in attracting savings, PMIs may always remain weak because of inadequate diversification and unattractive deposits. In the long run, PMIs will require this insurance (like in the U.S. or U.K) if they are to survive, because these specialized financial institutions always need some funding form deposits (even if their main funding source may then come from secondary mortgage markets). A move to rapidly de-license dormant PMIs as well as those not meeting the requirements of reporting, provisioning, concentration limits, and the N100 million minimum capital requirement is a high priority. This action is required to restore the reputation and ensure the stability of the overall PMI industry. Off-site and on-site supervision should be accelerated. The participation of ex-FMBN inspectors in this regard is recommended. CBN should make audit and inspection reports available to FMBN to support its NHF-refinancing activities. The accreditation of mortgage lenders for NHF refinancing should remain the responsibility of FMBN.

CONCLUSION

Even if these recommendations are implemented, it is unlikely that more than a handful of PMIs will survive and become active mortgage lenders. Their origination skills may be more usefully exploited in association with some commercial banks support (then acting practically as mortgage brokers) or by using secondary mortgage markets (so as not to keep balance sheet long-term mortgage portfolios).

The study revealed that the PMIs that are subsidiary of commercial banks perform better than others in terms of branching, capital base, loan origination etc. Developers have confidence in these PMIs also. If the above could be pushed through, it will go a long way in revolutionalizing mortgage finance business in the country. Therefore, broadened mortgage lending by commercial banks is the primary potential source for financing a successful housing finance programme in Nigeria as banks have most of the money, a more appropriate funding base and much of the country's relevant lending skills in this area. Re-structuring the PMI sector is an important and difficult challenge, but is unlikely to produce a comparable impact on the growth of the mortgage industry for reasons earlier enumerated in this study. Commercial banks in Nigeria over time have natural comparative advantages over smaller and fragile PMIs to make housing loans, given their much bigger size, cheaper funding through core deposits, a large distribution network, their servicing and marketing departments and tools, and capacities to cross-sell retail products.

REFERENCES

Abiodun, A. (1999) Housing finance under National Housing Fund: An
appraisal. Paper presented at the General Meeting of the Nigeria Institute of Town Planning.

Adams, O. (1992). Management Training Needs of Nigeria Indigenous Contractors and their preferred delivery system. Unpublished PhD Thesis, University College London, London.

Agbola, T.A. (1997). Institutional Constraints on Housing Development. The Journal of Habitat International. 6(2), 54 - 67.

Andrejus T. (2002, March). Mortgage Insurance in Housing Finance The way to go for Countries in Transition. The Journal of International Union of Housing Finance (IUHF), 16 (3)

Atagher M.I (2007): "Roles of Federal Mortgage Bank of Nigeria in Emerging Mortgage Market" being a paper presented at National workshop on Effective mortgage Creation and Origination as Panacea for Affordable Housing in Nigeria organized by AHCN, October 2007

Christian, J. (1980). Housing Finance for Developing Country. Prepared for International Union of Building Society and Saving Association, U.K.

Guardian (2005, Monday 18) How Mortgage-backed Securities can tackle Nigeria's Housing Woes. The Guardian. P. 37

Federal Mortgage Bank of Nigeria, (2000, March). Assessing National Housing Fund. Journal of Federal Mortgage Bank of Nigeria. Pp. 24.

Lea, M. (2001). The Applicability of Secondary Mortgage Markets to Developing Countries. International Union of Housing Finance Journal, 3 (3), 21-26.

Nevitt K. (2001). Mortgage Finance in a Changing World. University of Pennsylvania: Zerich Center of Real Estate Finance Wharton.

Ogunleye, K. (2002). Why the Mortgage Bank got Distressed. NDIC Quarterly. A publication of Nigeria Deposit Insurance Corporation, 10 (4), 25-30.

Okumadewa, F. (1998). Nigeria: Poverty Reducing Growth and Strategies and Options Collaborative study. Proceedings of the workshop of CBN/World Bank. Abuja.

Okupe, O. (2000). Problems of Real Estate Developers in Nigeria. A paper presented at a workshop organized by Nigerian Institute of Quantity Surveyors. Abuja.

Nubi T.G (2006): An Assessment of the Effectiveness of Housing Finance in selected Cities of Nigeria. A dissertation for the award of Doctor of Philosophy in Construction Management.

Vuyisani, M. (2001, December), The State of Housing Finance in South Africa In *IUHF Journal* 16 (2).

BOARD OF GOVERNORS

Prof. Chukwuma C. Soludo	-	Governor (Chairman)
Suleiman Barau	-	Deputy Governor (Operations)
Mr. Ernest C. Ebi	-	Deputy Governor (Corporate Service
Mr. Tunde Lemo	-	Deputy Governor (Financial Sector Surveillance)
Dr. (Mrs.) Sarah O. Alade	-	Deputy Governor (Economic Policy)

CENTRAL BANK OF NIGERIA

Printed by
MARKET LINK
0803 306 1476