The Global Financial Crisis, its Impact on the Nigerian Banking System and Future Safeguards

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Introduction

The hurricane came with all speed, clearing anything on its path – that is what the recent global financial crisis (that got intensified 2009) did to nations and their economies especially in the developed countries and on the banking sub-sector. The banking sector of Nigeria was no exception. Nine banks were rescued in 2009 with an initial amount of over 620 billion naira (About 4 billion dollars) and much more after, nationalised and later sold out to new investors.

The root of the global financial crisis which started in the United States of America began with the collapse of American mortgage market when for several reasons the value of properties went down drastically, leading to inability to refinance individual home mortgage because the banks were reluctant to lend (Friedman and Friedman 2010, P.31). Banks that had a lot of money tied up in loans to house owners who were no longer able to pay went bankrupt or near bankrupt, with that came the credit crunch.

The extent and severity of the crisis that began with the bursting of the housing bubble in the United States of America in August 2007 reflects the confluence of myriad of factors some of which are familiar from previous crises, while others are new (Sanusi 2010, p. 2).

The crisis manifested itself globally in the form of liquidity and credit crunch, breakdown of confidence in the banking system, de-leveraging and banks inability to improve capital adequacy, weak consumer demand, and fall in global output affected Nigeria through both the financial and real (trade, remittances and aid) channels (Ogunleye 2010, p. 253).

The cumulative effects of the crisis lead to distress in the banking sector.

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Objective

The main purpose of this study is to find out how the recent global financial crisis affected the banking sector in Nigeria. In addition, it will find what has been done to curtail it, and what should be done to stop future recurrence.

Methodology

Secondary data was used for this research, sourced from Central Bank of Nigeria publications. The method of analysis used for this research was descriptive and used simple percentages when necessary. The period covered in this study was between 2005 and 2012, which encompasses the phase of the major reform of consolidation of the banking systems in Nigeria and the period when the global financial crisis got intensified (beginning 2007).

Results

We found out that Nigeria was not insulated from the crisis, especially the second round effect. This was a result of the undiversified nature of the Nigerian economy and its high dependence on export of crude oil. The foreign capital inflows so generated compounded the impact of the external shocks arising from the crisis. In specific terms, Nigeria experienced low demand for its oil exports due to the recession in the economies of her major trading partners especially the United States of America. Hitherto, between 2004 and 2008 Nigeria experienced exceptional increase in oil price which resulted in huge inflow of foreign exchange and robust economic growth. This coupled with appreciable level of foreign direct investment flows resulted in excess liquidity in the banking industry which the real sector of the economy could not absorb. The result was that the excess liquidity in the banks found its way into stock market as shown in the extraordinary rally in the stock prices on the Nigerian stock exchange between 2006 and 2008, and the oil industry sector of Nigeria's economy. The bursting of the bubble resulted in these sectors to be affected the most and the banking sector got engulfed in the mess.

The Nigerian stock market was bullish between December 2005 and March 2008, it suddenly became bearish such that between 2007 and 2008 All Share Index at the Nigerian Stock Exchange declined by 43.5 percent, the market capitalisation for the corresponding period was 27.5 percent down (Sanusi 2010,p.9). The market downturn had negative impacts on bank balance sheets due to increased provisioning for bad debts and lower profitability. In the petroleum sector, Nigeria's Bonny Light Crude Oil Spot Price FOB which was $95.16 per barrel in January 2008 rose to $146.15 in July2008

before declining to $76.24 per barrel by October 17, 2008 (Sanusi 2010, p.8).Within six months it has lost 50% of its peak price. This, coupled with the collapse in the International price of oil, led to severe decline in foreign exchange receipts and consequently, government revenue contracted. Similarly, the exchange rate of the naira had witnessed consistent depreciation since the adverse effect of the crisis on the price of crude oil became manifested in the country. The implication of the falling oil prices and dwindling revenue for government plus naira depreciation were: less deposits for banks which depend on public sector for bulk of their deposit liabilities, declining capital inflows into the economy (this has the effect of worsening the problem of relatively high operating costs occasioned by decaying infrastructure like power because of the dearth of funds), loss of income from strategic business units in banks due to restrictive foreign exchange policies, capital market downturn leading to loss of investor confidence, loss of business income for key financial institutions that are directly dependent on the stock market and its implications to banks that are exposed to such institutions etc. The cumulative result was sharp deterioration in the quality of bank assets which immediately led to concerns over banks' liquidity.

Within a short period the Central Bank of Nigeria found out that nine banks have inadequacies in capital asset ratios and liquidity ratios as well as weaknesses in corporate governance and as well risk management practices. All the nine banks were discovered to be exposed to oil and gas transactions as well as capital markets which were experiencing turbulence as a result of the global financial crisis. The Central Bank took over the banks and injected N620 billion (about 4 billion dollars).

Conclusion and Recommendations

In conclusion it could be seen from the results that weaknesses of the banking sector coupled with macroeconomic instability lead to distress in the banking sector. This is because there were regulatory and supervisory failures on the part of the Central Bank of Nigeria and other agencies of government.

This study recommends that the Central Bank of Nigeria and other agencies of government should sit up and ensure proper, coordinated and proactive regulation and supervision of the banking industry in Nigeria, such that under-capitalisation, poor corporate governance, inadequacies in capital and other unwholesome practices are done away with. The issue of liberalization especially in the area of capital account opening should be revisited, because of the way funds are siphoned out of the country. Lastly, the economy needs to be re-engineered and diversified to reduce over-reliance on oil as the main foreign exchange earner for the country, as fluctuations in its price could result in macroeconomic instability, which inturn could result in a distressed banking sector.

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