Banking in Nigeria and Chinese Economic Diplomacy in Africa

Abiodun Alao
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A ‘China–Africa Toolkit’ has been developed to serve African policymakers as an information database, a source of capacity building and a guide to policy formulation.

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ABSTRACT

While Sino–Nigerian relations have grown significantly since the 1970s, several aspects of the relationship have been controversial and difficult. However, the special attraction the two countries hold for each other has made the relationship persist, even amid difficulties and challenges. Although several aspects of the relations have received academic and policy attention, an area that remains as yet understudied is the relationship between the two countries in the banking sector. This is particularly important, as the banking sectors in both countries are undergoing significant changes. The objective of this study is to take a panoramic view of the changes going on in the Nigerian banking sector and to situate the discussion in terms of the broader Chinese economic interests in Nigeria. This paper argues that the current changes in the Nigerian banking sector are likely to set the sector on a path that can win it respectability and respect from across the world and that the inclusion of banking in China’s economic interests in Nigeria can be mutually beneficial to both countries. While China may have justifiable grounds to be unhappy with aspects of its relationship with Nigeria, the paper concludes that the future of the economic relationship between the two countries is bright and potentially beneficial to both nations.

ABOUT THE AUTHOR

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## ABBREVIATIONS AND ACRONYMS

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>CBN</td>
<td>Central Bank of Nigeria</td>
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<tr>
<td>CEO</td>
<td>chief executive officer</td>
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<tr>
<td>CNOOC</td>
<td>China National Overseas Oil Company</td>
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<tr>
<td>EDW</td>
<td>Expanded Discount Window</td>
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<tr>
<td>GDP</td>
<td>gross domestic product</td>
</tr>
<tr>
<td>ICBC</td>
<td>Industrial and Commercial Bank of China</td>
</tr>
<tr>
<td>MoU</td>
<td>memorandum of understanding</td>
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<tr>
<td>NGN</td>
<td>Nigerian niara</td>
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INTRODUCTION

China and Nigeria are currently undergoing significant changes that each hope will enable it to derive benefit from its enormous potential. With its massive population and superpower status, China has embarked on an aggressive pursuit of trade and investment across the world. Nigeria has been trying to bring about major domestic reforms in its political and economic life and thus remove the negative image the country seems to have acquired as an unstable and somewhat unreliable business partner. It is against this background of a mutual desire to ‘reach out’ that one may look at recent developments and future prospects of Sino–Nigerian economic relations. But while such economic relations cut across a very broad spectrum, an area that is yet to be fully explored is the nature and extent of the relationship that currently exists (or can exist) between the two countries in the banking sector. This is somewhat ironic, because the banking sectors in both countries are undergoing significant changes that have required them to go on ‘charm offensives’ for outside investments and engagements. The objective of this paper is to look at the current changes in the Nigerian banking sector and the role China has played or can play in the sector.

Any discussion of banking in Nigeria needs to be prefaced with a brief discussion of the country’s economy, since banks have to operate in national economic realities. As is well known, Nigeria’s economy is dependent on oil, sales of which account for more than 80% of the country’s annual budget. However, in terms of gross domestic product (GDP), agriculture contributes about 40–50%. The forecasts of the country’s economic growth as made by the International Monetary Fund in April 2010 were 7% and 7.3% for 2010 and 2011, respectively. On its part, year-on-year headline inflation rose from 12.0% in the last quarter of 2009 to 12.3% in January and February 2010. Similarly, core inflation was at 10.1% in January and February 2010, up from the 9.7% recorded in the last quarter of 2009. Provisional data indicates that real GDP grew by 6.8% in the first quarter of 2010 – down from 7.44% in the fourth quarter of 2009, but up from 4.5% in the first quarter of 2009. Quarterly GDP growth rates of 7.24%, 7.36% and 8.51%, respectively, were projected for the second, third and fourth quarters of 2010. This is the current situation that the banking sector has to address.

THE NIGERIAN BANKING SECTOR: REGULATORY AND LEGAL FRAMEWORKS

Currently, Nigeria has 24 commercial banks. There are also 98 mortgage banks, 84 finance houses and five development finance institutions, as well as five active discount houses. All these institutions are under the supervision of the Central Bank of Nigeria (CBN). There are also about 200 stock-broking firms, investment banks, asset management firms and issuing houses operating under the supervision of the Securities and Exchange Commission.

The Nigerian banking sector is controlled by the CBN, headed by a governor appointed for a period of five years. The governor is supported by four deputy governors, who head departments dealing with operations, corporate services, economic policy and financial system stability. Legal and regulatory frameworks for Nigerian banks come through two
sources: the Banking and Financial Institution Act and periodic policy documents issued by the CBN.

**RECENT DEVELOPMENTS IN THE NIGERIAN BANKING SECTOR**

In the last decade a number of major developments have taken place in the Nigerian banking sector. Perhaps the first was the $25 billion recapitalisation exercise undertaken by the former CBN governor, Charles Soludo, in 2006. This resulted in mergers and acquisitions and reduced the number of banks in Nigeria from 89 to 24. The objective was to strengthen the Nigerian banking sector and make it a credible global actor. The achievements of the recapitalisation could be seen from both quantitative and qualitative perspectives. Whereas the number of banks was reduced, the number of branches rose by 33% from 3,382 to 4,500, while the total asset base increased by 104% from Nigerian naira (NGN) 3.21 trillion to NGN 6.5 trillion. In the same vein, the ratio of non-performing loans to total loans improved by 51% from 19.5% to 9.5%.

Although largely successful, the recapitalisation brought challenges. The resultant growth in capital created a need for banks to return dividends to shareholders. This led to the aggressive expansion of credit in the system with very minimal consideration for good credit risk and management principles. The supervisory oversight by the CBN at this time was also weak. This regime of excessive credit expansion continued until the global economic meltdown in 2008. The recall of credit lines by the international financial houses threw the Nigerian banking sector into difficulties, as most Nigerian banks had granted credits that were non-performing.

There were other policy mistakes, including the relaxation of rules permitting banks to use the capital market to raise equity so soon after their recapitalisation; the frequency with which some of the banks raised fresh capital, raising doubts as to whether the NGN 25 billion recapitalisation had been successful in the first instance; and new liberal CBN ‘margin’ rules permitting banks to lend against the collateral of their own shares. All these combined to generate a questionable ‘boom’ in the stock market. Under the circumstance, it was inevitable that challenges would reappear in the country’s banking sector.

A second round of changes occurred after Lamido Sanusi became the CBN governor in June 2009. Sanusi believed that Soludo’s attempts at consolidation, although good, should have been seen as a ‘work in progress’ rather than an end in itself. He identified eight interdependent factors as being behind the fragile financial system in the banking sector:

- macroeconomic instability caused by large and sudden capital inflows;
- major failures in the corporate governance of banks;
- lack of protection for investors and consumers;
- inadequate disclosure and transparency about the financial position of banks;
- weakness in the regulatory framework;
- uneven supervision and enforcement;
- unstructured governance and management processes at the CBN; and
- general weakness in the country’s business environment.
These factors informed Sanusi’s decision to build his reform efforts around four pillars. The first is enhancing the quality of banks, which involves the CBN’s initiation of a five-part programme to enhance the operations and quality of banks. This consists of the introduction of industry remedial programmes to fix the key causes of the crisis; the implementation of risk-based supervision; reforms to regulations and the regulatory framework; enhanced provisions for consumer protection; and internal transformation of the CBN. The second pillar is the establishment of financial stability, built around strengthening the Financial Stability Committee within the CBN and establishing a hybrid monetary policy and macro-prudential rules. The third pillar is the enabling of healthy financial sector evolution, which entails the CBN reviewing the basic ‘one-size-fits-all’ banking model. The fourth pillar is ensuring that the financial sector contributes to the real economy. This allows the CBN to measure more accurately the relationship between the real economy and the financial sector.

One of the first things Sanusi did was to institute a special audit to ascertain the status of all 24 Nigerian banks. This audit came up with a damming report of monumental misdeeds. It was revealed that the total amount outstanding for banks in terms of the Expanded Discount Window (EDW) was NGN 256,571 billion, most of which was owed by five banks. Sanusi further said that a review of activities via the EDW showed that four banks had become almost permanently locked in as borrowers and were clearly unable to repay their obligations. A fifth bank had also been a very frequent borrower. These banks were Oceanic Bank, Intercontinental Bank, Finbank, Afribank and Union Bank. At the end of the final audit, four more banks – Bank PHB, Equatorial Trust Bank, Spring Bank and Wema Bank – were found to be in grave position. The CBN injected NGN 420 billion into the first set of five banks and NGN 200 billion into the second set of four banks. With the exception of Wema Bank, the heads of all these banks were removed.2

With the takeover of erring banks completed, Sanusi began focusing on other aspects of his reforms. Broadly, these can be discussed under four headings: the categorisation of banks; the creation of the Asset Management Company of Nigeria; the introduction of limitations of the terms in office for chief executive officers (CEOs); and the abolition of universal banking. These are briefly discussed below.

**The categorisation of banks**

Nigerian banks are now to be categorised as national, regional or international, with capitalisation levels depending on their type of operations. The minimum capital requirement for commercial banks is now NGN 25 billion, while banks intending to operate outside Nigeria have to raise a minimum amount of NGN 100 billion. Regional banks are to operate in a minimum of five and a maximum of 10 contiguous states and must have the word ‘regional’ in their names and a minimum capital of NGN 15 billion. The CBN also realised that there would be some specialised banking like non-interest banking, agricultural banking, etc., and a separate licence was established for this.

**Creation of the Asset Management Company of Nigeria**

This company was proposed to relieve banks of the burden of non-performing assets. It is expected to serve as a vehicle for resolving the huge non-performing assets of banks
accepting deposits. It will acquire the toxic assets of these banks in order to strengthen their balance sheet and bring about asset quality, improved liquidity and capital adequacy. The Ministry of Finance and the CBN each agreed to subscribe half of the NGN 10 billion initial share capital of this company.

Limitations of the terms in office of chief executive officers

Before Sanusi assumed office, the CEOs of Nigerian banks had a unlimited period of stay in office. This turned out to have serious implications for corporate governance. Under the reforms, the terms in office for bank CEOs is now limited to an initial period of five years, renewable for another five years. The same policy is extended to the CBN governor, his deputies, the managing director of the Nigeria Deposit Insurance Corporation and departmental directors. The governor of the CBN and his deputies are also prevented from taking up appointments in any bank until a period of five years after they had left the CBN, while for departmental directors this period is three years.

Abolition of universal banking and the introduction of specialised banking

Universal banking, the system of banking that allows banks to provide a variety of services to their customers, was abolished, as the CBN governor believes it opens the banking sector to abuse. However, because the CBN anticipates that some banks may wish to retain non-core banking business, it proposes that such banks must comply with CBN requirements for the establishment of holding companies, and such requirements include making a detailed business case for engaging in any non-core business operations. In short, in place of universal banking there will be two new classes of monocline banking licences: commercial banking, made up of national and regional banks; and specialised banking, including non-interest banks, microfinance banks and primary mortgage institutions.

As would be expected, Sanusis’s reforms have been controversial. They have, however, received domestic and international support. International support, for example, has come from the European Investment Bank, while the new Nigerian president, Dr Goodluck Jonathan, has given them his endorsement.

From June 2010, Nigerian banks can be grouped under three categories: (1) international banks; (2) profitable local banks; and (3) the rescued eight. The international banks are Stanbic IBTC, Standard Chartered and Citibank. These operate within international framework and are largely immune from the poor corporate management that has plagued some Nigerian banks. The profitable local banks include Access Bank, Diamond Bank, Eco-Bank, First City Monument Bank, Fidelity Bank, First Bank Plc, Guaranty Trust Bank, Skye Bank, United Bank for Africa, Sterling Bank, Unity Bank and Zenith Bank. These banks are largely in very good shape with credible governance structures. The rescued eight banks are still facing liquidity challenges, even though they are under the management of new boards established by the CBN.

Having gained a panoramic view of the current situation of banking in Nigeria, we need to look at the nature and extent of Chinese economic interests in Nigeria and how they relate to banking in the country.
Chinese economic interests in Nigeria are quite extensive, ranging from oil and gas to telecommunications and railways. In 2009 Nigeria came fourth among China’s top two-way trading partners in Africa and second among the top African importers from China. Indeed, the Nigeria–China Chamber of Commerce has been established to further develop trading relations between the two countries.

The first economic agreement between China and Nigeria was signed in 1972, but it was not until the mid-1970s that the relationship was strengthened. The development of the Nigerian Railways project was one of the earliest agreements between the two countries. This commenced in 1975, but stalled because of alleged corruption on the part of some Nigerian officials. It was later reactivated and an agreement for $528.6 million was signed in 1995. During the 1990s other economic relations included involvement in irrigated rice plantations in Lagos, in water resources in Borno State and in the Nigeria National Electricity Power Authority (now the Power Holding Company of Nigeria). China was also involved in Nigeria’s controversial steel projects in Ajaokuta and Aladja. An enabling agreement was signed between the two countries in May 1997, but this was later tainted by a serious corruption scandal. During the 1990s several economic agreements were signed between the two countries.

Although China is involved in many aspects of the Nigerian economy, the country’s main interest is oil, a resource that is also at the forefront of controversy in the West African nation. Several oil deals have been signed, one of the most significant being the one that allowed China to invest $4 billion in Nigeria’s infrastructure in return for first refusal rights on four oil blocks. In January 2006 China’s national offshore oil company acquired a 2.3 billion majority stake in a major oil field, and the last five years have witnessed some major Chinese investments. They include the 45% stake, worth $2.7 billion, of China National Overseas Oil Company (CNOOC) in an offshore deepwater oil field operated by Total. This is reported to be CNOOC’s largest foreign investment ever, and the company will pay $424 million for financing, operating and capital expenses. Profits will be shared with the Nigerian National Petroleum Corporation in a 70:30 ratio in favour of CNOOC. China has also recently agreed to spend $2 billion to build refineries and downstream infrastructure, while Sinopec paid $7.2 billion for Addax in 2009.

Chinese firms are pouring into the country to do business. In April 2005 ZTE Corporation entered into a deal with Nigeria Telecommunication to expand Nigeria’s network. The project is meant to provide local telecom components and other ancillary services. The Chinese Civil Engineering and Construction Company built the Nigerian Communications Commission building in Abuja, Nigeria’s capital. Most of the motorcycles on Nigerian roads are also from China. Shao Huixiang, deputy director-general of Shanghai municipality, where many of these motorcycles are made, confirmed the increase in transactions between China and Nigeria, noting that the trade between Nigeria and Shanghai alone amounts to about $172 million. There are also closed Chinese contacts with state governments. For example, the Borno State government awarded six major contracts to Chinese construction and engineering firms to stem the wave of flooding being experienced by the state. Also, a Chinese conglomerate, Zhuhai Minghong Group, is looking into reviving the moribund Awoomama Resort in Imo State.
A state-owned company, Genetic International Corporation of China, bought its first consignment of 100,000 metric tons of fresh cassava chips from Nigeria in July 2005. In the agricultural sector, Nigeria has shipped 80,000 tons of cassava chips to China and thereafter received an order to supply another 102,000 tons. China is also buying sesame seeds from Nigeria. Indeed, there are currently over 500 Chinese experts and technicians working in various aspects of agriculture in 20 Nigerian states. In short, the volume of trade between Nigeria and China has significantly increased, from $178 million in 1996 to $2.83 billion in 2007. China has also set up about 30 companies (some solely owned, some jointly owned with Nigerians) in Nigeria. These companies are involved in the construction, oil and gas, technology, services, and education sectors of the Nigerian economy.

But Chinese experiences with Nigeria have not always been pleasant ones, as there have been cases of corruption, non-payment of fees and reneging on agreements. Indeed, a number of agreements have had to be halted and renegotiated – with significant implications for the terms of loans and other financial agreements. While China is unhappy with these, the country also realises that the positive sides of the opportunities for business engagement with Nigeria far outweigh their negative aspects.

China seems to have appreciated that working in Nigeria has its own challenges. The country's involvement in Nigeria's oil industry also means that it has to take into consideration the security situation in the Niger Delta. China has tried to manage the situation as best as possible, despite cases of Chinese nationals being taken hostage. On the whole, there have not been specific complaints against China about the way that its companies relate to their Nigerian employees, even if there are complaints that the nature of the country's involvement in Nigeria adversely affects local markets.

**EXISTING BANKING LINKS BETWEEN CHINA AND NIGERIA**

Banking links between Nigeria and China already exist, even though this has been on a comparatively low scale. Broadly, Sino–Nigerian banking links can be discussed under two major headings: Chinese banks' sponsorship of development activities in Nigeria and the link between the two countries' commercial banks. In the first category, a number of Chinese banks have been involved in development activities in Nigeria. For example, in 2006 China Development Bank provided $20 million in financial support to Reliance Telecommunications to assist the company. Also, Export–Import Bank of China (China Exim Bank) is involved in the development of oil facilities and railways in Nigeria.

The banking links between China and Nigeria are not particularly extensive. Three Nigerian commercial banks are known to have established formal links with China. The first of these is First Bank, which has now been granted a licence to operate in China, thus providing it with a foothold in the Asian region. First Bank has other banking relationships with Chinese institutions, including a memorandum of understanding (MoU) with Yuemei Group, a textile-manufacturing firm with a value of $50 million; a partnership with Shenzhen Energy Group for the building of a 3,000 megawatt gas turbine power plant in Nigeria worth $2.4 billion; and an MoU with the Guangdong Xinguang Group for a $500 million investment in Ogun State. Guangdong Xinguang Group's collaboration with First Bank is in the areas of investment banking, project financing, business advisory services
and a correspondent banking relationship between the two organisations. First Bank also has an MoU with China Construction Bank to cover global banking collaboration.

Another Nigerian bank that has now established links with China is Standard IBTC Bank, which has links with the Industrial and Commercial Bank of China (ICBC). ICBC has now acquired a 20% stake in the South African Standard Bank Group – the banking group to which Standard IBTC Bank Nigeria belongs. ICBC’s involvement in Standard IBTC Bank has also made it possible for ICBC to become involved in a number of other economic interests in Nigeria.

A third bank that has now established links with a Chinese bank is Nigerian Export–Import Bank, which is positioned at the core of Nigeria’s trade-oriented activities. It provides short-term guarantees for loans granted by Nigerian banks to exporters and offers credit insurance against non-payment by foreign buyers. The bank has been holding high-level talks with Chinese financial institutions such as China Exim Bank. All these links further open China to other opportunities in the Nigerian banking sector.

**CHINA AND NIGERIAN BANKS: POSSIBLE ACQUISTIONS AND INVESTMENT OPPORTUNITIES**

There are grounds for China to play a significant role in acquiring and investing in Nigerian banks, and interviews held with very senior officials of the CBN and commercial banks indicate that China will be welcome to invest in the Nigerian banking sector. This can be done in two ways: investing in one of the rescued banks or involvement in one of the strong ones. Of the rescued banks, Wema Bank and Union Bank might be very good options, because they are still run like old and conservative banks and have fairly large networks of branches. Among the profitable banks, China may want to look for investment opportunities in banks like Skye and Sterling, which have strong financial bases and credible governance structures. There seems to be very little room for China to play any further role in the affairs of international banks in Nigeria.

In theory, there is no restriction on the extent of foreign ownership of Nigerian banks, provided it is approved by the CBN. According to Sanusi, the CBN is not likely to support foreign banks owning more than 10% of a Nigerian bank. But while not giving any exact figures, the governor confirmed in an interview that it is ‘something that needs to be looked at again’. He did not even rule out the possibility of outright ownership. Interestingly, he included China Construction Bank among those he would want to see acquiring ownership of Nigerian banks.

**CONCLUSION**

Nigeria is a country with enormous potential and a promising future. By 2015 it is expected that Lagos will be the third-largest city in the world and Nigeria, with an envisaged population of 287 million in 2050, will be the world’s sixth-largest country in terms of population size. This offers significant opportunities. The banking sector is now earning respect and confidence across the world. Consequently, with the growing nature of Sino–Nigerian economic relations, there is the need for China to be more involved in
the Nigerian banking sector; indeed, involvement in banking will further assist China’s investment in other sectors of the Nigerian economy. While China has reasons to be disappointed over some of its past experiences in Nigeria, especially those relating to corruption and scandals, the Nigerian banking sector is undergoing major reforms. More importantly, the sector now seems to be in need of a major external infusion of interest. There can also be no doubt that the inclusion of banking in the list of economic links between the two countries will, apart from being mutually beneficial, further deepen the relationship between the two countries.

ENDNOTES

1 For example, there is a general impression that corruption has percolated through all aspects of Nigerian economic and political life, and most global indexes on corruption rate Nigeria as one of the world’s most corrupt countries; e.g. the 2009 Transparency International Corruption Index ranked Nigeria 130th out of 180 countries surveyed.

2 Wema’s management was retained because there had only recently been a change in its directorship and its leadership at the time of the audit was not the one responsible for its financial situation. Also, the Equatorial Trust Bank was later returned to its management.


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