Access to Finance in Nigeria:

Microfinance, Branchless Banking, and SME Finance

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Executive Summary

Building on recent years of reform and growth, Nigeria has a historic opportunity to lay the foundations for a strong financial sector. At 5.6 percent average annual growth between 2000 and 2005, the Nigerian economy is experiencing its fastest growth in the past twenty years. The Nigerian Government aspires to build on this trajectory and make the country one of the world's twenty largest economies by 2020. A weak financial sector, particularly with respect to services for the non-petroleum producing sectors, has been an obstacle. Nigeria's financial system is still shallow and the majority of Nigerians lack access to formal financial service providers. While bank private sector lending has expanded significantly over recent years, it is still below average for Sub-Saharan Africa.

Nigeria has a long history of community finance, microfinance, and Small and Medium Enterprises (SME) finance initiatives to provide financial services to the unbanked population. However, performance has been mixed. A recent FinScope survey conducted by Enhancing Financial Innovation and Access (EFInA) concluded that 74 percent of adults (64 million) have never been banked, and only 15 percent of women currently have bank accounts. While 71 percent of salaried workers have a bank account, 86 percent of rural adults are unbanked.

The Government is cognizant of the need to strengthen the financial sector and has developed a comprehensive long-term strategic plan for its development: the Financial System Strategy 2020 ("FSS 2020"). The plan aims to build on the success of the recent banking sector reforms to promote greater stability, depth and diversity of the entire financial system. The draft FSS 2020 was presented at an international conference in June 2007 and approved in September 2007, where all key Government agencies and responsible Parliamentary Committees were represented.

Given significant financial sector reforms and private sector innovations, there are encouraging signs that access to finance is poised for growth in Nigeria. This report provides a diagnostic of access to finance and identifies key issues for microfinance, branchless banking and SME finance. The over-arching issues across all three sectors include the following:

- **Greater transparency of financial performance and market information**: There is little data on market demand for microfinance, SME finance or branchless banking. Likewise, data on financial performance or outreach is scarce for microfinance banks, SME finance providers, and branchless banking providers.
- **Strengthen capacity at all levels**: Providers of microfinance, SME finance and branchless banking all noted challenges to manage current levels of rapid growth, develop new products, expand in new geographic areas, and address other strategic and operational challenges. Likewise, the CBN would benefit from increased capacity to conduct both off-site and on-site supervision.
- **Promote financial infrastructure**: Considerable attention has been given to designing new laws, regulations and guidelines to upgrade the payments system, private credit registries, and collateral registries. Moving quickly and surely on these core components of the financial infrastructure could help Nigeria's financial sector modernize and significantly expand access to finance.

- **Promote consumer protection**: As more financial service providers enter the market, competition is starting to appear in some urban areas. Given the growing diversity and complexity of services across microfinance, SME finance and branchless banking, it may be time to introduce consumer protection for financial services.
- **Coordinate efforts**: Several programs have been launched by funders, the Federal Government and several State Governments to promote microfinance, SME finance and branchless banking. In particular, concessional funding to promote microcredit or SME lending can damage the long-term development of the sector. The FSS 2020 and national programs such as EFInA and the MSME program are excellent opportunities to coordinate efforts, share information across programs, ensure that good international practices are incorporated in programs, and improve aid effectiveness.

The report addresses microfinance, branchless banking, SME finance, and cross-cutting issues for access to finance. For each area of analysis, the key findings and recommendations are summarized.

Microfinance

The Microfinance Policy, Regulatory and Supervisory Framework for Nigeria developed by the CBN in 2005 initiated an important turning point in the industry with the creation of the Microfinance Bank (MFB) as an institutional vehicle for privately owned, deposit-taking microfinance institutions (MFIs). Prior to this, a few notable Non Governmental Organizations (NGOs) were established that have grown to provide microfinance in a sustainable manner according to international standards of good practice. However, until recently the majority of institutions have been smaller NGOs, community banks, cooperatives, and non-bank financial institutions with uneven management capacity, low outreach to clients, and challenges to becoming profitable.

The Framework is designed to unite the best of the NGO credit organizations, the privately-owned community banks, and new MFI initiatives under a common legal, regulatory and supervisory regime. The Microfinance Framework catalyzed two driving forces in the microfinance industry at an extraordinary pace and scale. First is the immediate investment of capital by a large number of Nigerian and international investors in newly created MFBs. The second force is the new regulation and supervision framework for this emerging industry. The rate of growth in the microfinance industry, measured by number of institutions, capitalization, or portfolio growth, is among the fastest of any microfinance industry globally at *similar early* stages of development.

As part of the Microfinance Policy Framework, the CBN in collaboration with the Bankers Committee has created the Micro Credit Fund (MCF) to partner with state governments to channel credit to the microenterprise sector. The CBN reports that the balance of funds available to the MCF at the end of 2007 was around NGN 20 billion (US$ 172 million). Specific lending policies for the MCF were not shared with the diagnostic team. Nevertheless, the intended scale of the operation is enough to warrant concern about the impact on the MFBs. Accounting for the state matching funds, the current balance of the MCF is already 80 percent of the total deposits in the MFBs at June 2008; the 2010 projections for the MCF are four times the amount of current deposits. There are at least two adverse effects that can result from an initiative of this size. The first is a general disincentive for the MFBs to develop capacity for mobilizing savings. In itself, the MCF reflects an emphasis on credit that is pervasive in Nigerian policy discussions around access to finance. If large volumes of wholesale funds are made available to the MFBs, they will have less interest in providing savings services, and may become dependent on wholesale borrowing to fund growth. The second adverse effect can already be observed in the various microfinance credit programs associated with the National Poverty Eradication Programme (NAPEP). NAPEP channels funds through the MFBs to local organizations and individuals. The MFB pays NAPEP 1 percent for the funds and is limited to a 400 basis point margin, charging the borrower 5 percent. The margin is insufficient to cover the MFB's operational costs. Repayment performance with loans associated with public funds in Nigeria is also very poor, which exposes the MFB to additional losses. Finally, the allocation of NAPEP funds, like most subsidized credit programs, is perceived to be politically motivated. To the extent that is the case, these transactions expose the MFB to political influences that can undermine independence and portfolio quality in the long run.

Key recommendations to improve microfinance are summarized here and explained further in Section 8.1:

- Publish historic financial statements, financial and outreach performance data and interest rates of all MFBs on the CBN website (immediate)
- Prioritize supervision efforts on the largest MFBs (immediate)
- Develop off and on-site supervision tools and training programs (immediate)
- Raise the minimum capital requirement for unit MFBs (short-term)
- Allow acquisitions and mergers without geographic restrictions (medium term)
- Ease geographic restrictions on MFB expansion (short-term)
- Promote capacity building initiatives aligned with MFB needs, CBN requirements, and funder programs (short- and medium-term)
- Align all MFB wholesale lending programs with a market-based model for pricing and eligibility requirements (immediate)

Branchless Banking

The main payment instruments available in Nigeria include large-value credit transfers, checks, retail electronic debit and credit transfers, and payment card systems, among others. Electronic purses (a form of stored value cards), internet-based banking along with mobile payment services have recently been introduced. For the first seven months of 2008, ATM transactions represented nearly 91 percent of the value of all electronic fund transfers in Nigeria. The Central Bank of Nigeria estimates that there are approximately 7,000 ATMs in the country, representing a low penetration rate of only one ATM per 20,000 individuals. For the first seven months of 2008, point of sale (POS) transactions represented over 4 percent of the value of all electronic fund transfers in Nigeria. The POS penetration rate represents a ratio of less than 50 POS terminals per 1 million inhabitants – an extremely low penetration rate compared to other countries in Africa. Nigeria has four licensed Global Standard for Mobile (GSM) network operators (MTN, Glo, Zain (formerly Celtel), and Mobile Telecommunications Limited) with approximately 50 million mobile telephone subscriptions. There are another four licensed Code Division Multiple Access (CDMA) mobile network operators (Starcomms, Visafone, Reltel and Multilinks) with approximately 4.8 million subscriptions.

The CBN is in the process of drafting mobile payments guidelines to promote branchless banking. Discussions with members of the CBN's Banking Operations Department indicate that there is a well developed understanding of the many legal domains implicated by a comprehensive branchless banking regulatory regime. These domains include the often complicated issues presented by the use of agents, Anti-money laundering/ Combating the financing of terrorism (AML/CFT) requirements and consumer protection. There is good reason to be optimistic that the mobile payments guidelines, when released for comment, will be a thorough and well conceived effort. Still, given that effective branchless banking requires the cooperation of parties outside the control of the CBN, such as telecommunications service providers and consumer protection agencies, it is unclear how effective the mobile payments guidelines will be in practice. In addition, even parties under CBN supervision, such as private switch operators, appear to be resistant to CBN efforts at promoting interoperability, a primary component of expanding access to finance. However, reports indicate that draft operational rules for interoperability through a National Central Switch are awaiting CBN approval.

Key recommendations to improve branchless banking are summarized here and explained further in Section 8.2:

- Promote interoperability of the retail payment system (short-term)
- Ensure that mobile payments guidelines address key issues (short-term)
    - Use of agents and/or third party service providers
    - Prudential risks involved in nonbank-led models of mobile banking

SME Finance

Only 5 percent of SMEs have access to a loan, and 59 percent report difficulties accessing financial services. Given the potential that SMEs have in boosting growth and employment, Nigeria can gain substantially from removing bottlenecks to their growth. A 2008 World Bank Investment Climate Assessment (ICA) study identifies the top constraints of SMEs as the electricity shortage, low access to finance and a poor transportation network. Such constraints add considerably to the cost of doing business – an estimated 16 percent loss in sales per year.

SME finance is constrained by lack of data, regulations and infrastructure for collateral and insufficient credit information. Policy making for the sector is severely constrained by the lack of data that would allow a better understanding of the problems and performance of ongoing initiatives. Regulations require loans to be collateralized and limit the types of acceptable collateral. At the same time the laws relating to security over movables (i.e., equipment) are antiquated, fragmented and do not offer Nigerian businesses an effective means of raising capital. The current credit information system does not address the needs of the SME sector. However, with quick approval of well designed regulations, Nigeria could establish a competitive and open credit information industry where private credit bureaus working alongside the Credit Risk Management System (CRMS) can quickly begin to cover the population.

Financial providers are challenged to offer adequate services to SMEs. Checks, which are normally used as security in supplier credit (particularly in developing nations), have a very bad reputation in Nigeria. As a result, checks are not considered reliable and hence do not function as credit or collateral. As noted earlier, the migration to electronic payment systems, including debit cards, should be a high priority for the CBN within its overall strategy to modernize payments.

However, the use of post-dated checks as a source of credit could be encouraged and strengthened in the meantime, until electronic payments have wider acceptance.

With some exceptions, there are no real SME finance products. Banks and other authorities tend to treat SMEs as "small corporates" with no clear understanding of SME profiles. Globally, leasing is a widely-used service for SMEs, although the lack of a leasing law is constraining development of this sector in Nigeria. Finance companies have limited tools for credit risk assessment and lack of information and understanding of value chains that are important in the development of factoring services.

Past attempts to promote SME finance have not been successful, and this could lead authorities (and skeptical banks) to be hesitant in implementing new policies for the sector. Five venture capital companies were established to manage the Small and Medium Enterprises Equity Investment Scheme (SMEEIS) funds, and they offer strong potential for SME finance given that they are still operational and have valuable experience and understanding of the sector. At the microfinance level and corporate finance levels, Nigeria is witnessing significant growth, and both the private and public sectors should remember the missing middle of SME finance.

Key recommendations to improve SME access to finance are summarized here and explained further in Section 8.3:

- Improve collection and dissemination of information on SMEs and SME financial services produced by SMEDAN, CBN, and Company Affairs Commission (short-term)
- Establish a credit information system (short-term)
- Increase the use of checks as an SME credit instrument (short-term)
- Promote the introduction of new products for SME finance (medium term
- Leverage SMEEIS experience (medium/long term), particularly that of venture capital companies established to manage equity investments under the program
- Review, and where necessary reform, legislation and regulation on collateral and registries (medium term)

Other General Policy Issues for Access to Finance

Nigeria's access to finance regulatory framework is well developed, dynamic and benefits from a large degree of support by engaged and motivated regulators. Nevertheless, some key regulatory areas suffer from a lack of legal clarity. For example, the applicability of the Monetary Policy Rate (MPR) to the determination of interest rate caps is unclear, with wide disparities in the market and even within the CBN as to whether interest rate caps exist, how they are to be calculated and whether they will be seriously enforced. AML/CFT regulations need greater clarity with many different regulations, circulars and other authoritative documents in conflict with each other.

Key recommendations to improve broad issues for access to finance are summarized here and explained further in Sections 8.4 and 8.5:

- Clarify the policy on interest rate caps (short-term)
- Harmonize all AML/CFT regulations to permit clear operation of risk-based approach (medium term)

- Enhance consumer protection by facilitating consumer access to credit reports and requiring disclosure of "disputed" status (medium/long term)
- Establish a consumer protection body dedicated to protecting consumers of all financial services, not just mobile payment services (medium/long term

Acknowledgements

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The main objective of the diagnostic was to (i) analyze the current state of access to finance in Nigeria, (ii) identify areas for improvement and (iii) propose recommendations with respect to a coordinated and effective program to scale up access to finance in the country as part of the broader FSS 2020 implementation framework.

During the ten-day mission and supplementary phone interviews, the access team met with more than 110 people from microfinance banks, NGOs, commercial banks, payment providers, mobile phone networks, consulting/training providers, funders, credit registries, the Central Bank of Nigeria, and government agencies and initiatives in Abuja and Lagos. Additional information was gathered by Jennifer Isern, Amaka Agbakoba, and Estelle Lahaye (CGAP) through phone interviews and desk reviews from July through November 2008.

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Abbreviations and Acronyms

AMBIN	Association of Microfinance Banks in Nigeria
AML	Anti-money laundering
ASA	Association for Social Advancement
BOI	Bank of Industry
CAC	Corporate Affairs Commission
CAMEL	Capital Adequacy, Asset Quality, Management, Earnings, and Liquidity
CBN	Central Bank of Nigeria
CDF	Community Development Foundation
CDMA	Code Division Multiple Access (secondary mobile phone standard)
CFT	Combating the financing of terrorism
CGAP	Consultative Group to Assist the Poor
CPC	Consumer Protection Council
CRC	Credit Reference Company
CRMS	Credit Risk Management System
COWAN	Country Women Association of Nigeria
DAI	Development Alternatives Incorporated
DARC	Development Alternatives Resource Center
DEC	Development Exchange Center
DFD	Development Finance Department
DFID	UK Department for International Development
E-FASS	Electronic Financial Analysis and Surveillance System
EFInA	Enhancing Financial Innovation and Access
ELAN	Equipment Leasing Association of Nigeria
FADU	Farmers Development Union
FAO	Food and Agriculture Organization of the United Nations
FCT	Federal Capital Territory
FSS	Financially Self-Sufficient
GBP	Great Britain Pound Sterling (British Currency Code)
GSM	Global System for Mobile (international mobile phone standard)
GoN	Government of Nigeria
GTZ	German Agency for Technical Cooperation
ICA	Investment climate assessment
IFC	International Finance Corporation
KYC	Know Your Customer
LAPO	Lift Above Poverty Organization
MAN	Manufacturer Association of Nigeria
MARKETS	Maximizing Agriculture Revenue and Key Enterprises for Target Sites
M-BANKING	Mobile Banking
MFB	Microfinance Bank
MCF	MicroCredit Fund
MFI	Microfinance Institution
MIX	Microfinance Information Exchange
MPR	Monetary Policy Rate

MSME	Micro, Small, and Medium Enterprises
NACCIMA	Nigerian Association of Chambers of Commerce, Industry, Mines and Agriculture
NACRDB	Nigerian Agricultural Cooperative and Rural Development Bank
NAPEP	National Poverty Eradication Programme
NASME	National Association of Small and Medium Enterprises
NASSI	National Association of Small Scale Industrialists
NBCB	National Board of Community Banks
NCS	Nigerian Central Switch
NDIC	Nigeria Deposit Insurance Corporation
NEEDS	National Economic Empowerment and Development Strategy
NGO	Non-Governmental Organization
NGN	Nigerian Naira (Currency code)
NIBSS	Nigeria Inter-Bank Settlement System
NIMC	National Identity Management Commission
NPLs	Non-Performing Loans
NPSC	National Payments System Committee
OFID	Other Financial Institutions Department
PMFB	Prosperity Microfinance Bank
PoS	Point of Sales
PRISMS	Promoting Improved Sustainable Microfinance Services
SEAP	Self-Reliance Economic Advancement Programme
SMEs	Small and Medium Enterprises
SMEDAN	Small and Medium Enterprises Development Agency of Nigeria
SMEEIS	Small and Medium Enterprises Equity Investment Scheme
UBA	United Bank of Africa
UNCDF	United Nations Capital Development Fund
UNDP	United Nations Development Programme
USAID	United States Agency for International Development

Map of Nigeria

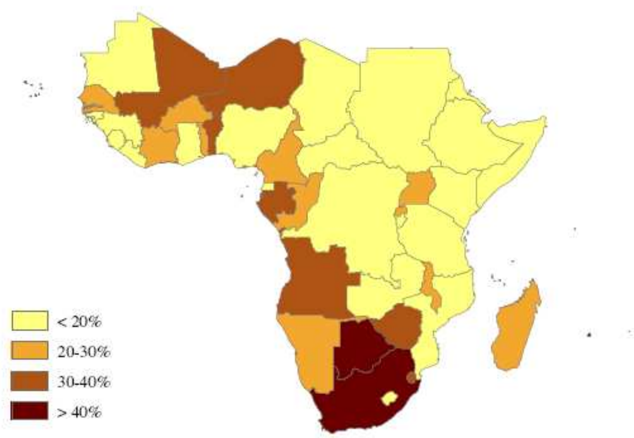
Source: www.nigeriannews.com

Financial Access in Nigeria

1. Demand for Financial Services

Approximately 70 percent of Nigeria's population of 140 million lives below the poverty line[1] and the percentage of the population with access to formal financial services is among the lowest of African countries (Figure 1). In 2005, the CBN estimated that approximately 35 percent of the economically active population had access to formal financial services, of which less than two percent of rural low-income people had access to formal financial services.[2]

Figure 1: Percent of Population with Access to Finance in Sub-Saharan Africa[3]



1.1 Demand for Microfinance

The recently completed FinScope survey conducted by EFInA[4] assessed the demand for financial services by surveying 22,000 people with a statistical representation of 87 million adults. The survey estimates that 74 percent of the adult population (64 million) has never been banked. Women are even more financially excluded with 85 percent never banked.[5] With a total population of 140 million people, approximately 70 percent (98 million)[6] of Nigerians live below the poverty level estimated at US$ 1.25/day by the World Bank poverty data. GNI per capita is approximately US$ 930 (less than US$ 3/day).[7] About 72 percent of adults (63 million) are

[1] UNDP/UNDCF, "Support to the Development of Sustainable Microfinance Sector in Nigeria: Mid-term Evaluation Report", September 2007.
[2] Central Bank of Nigeria, "Microfinance Policy, Regulatory and Supervisory Framework for Nigeria", December 2005.
[3] Making Finance Work for Africa, World Bank, 2008.
[4] 2008 FinScope Survey; http://www.efina.org.ng
[5] Soludo, Charles, *Creating an Inclusive Economy for the Nigerian woman presentation*, October 6, 2008.
[6] UNDP/UNDCF, "Support to the Development of Sustainable Microfinance Sector in Nigeria: Mid-term Evaluation Report", September 2007.
[7] World Bank, *World Development Indicators Database*, September 2008.

considered rural, and access to finance is especially difficult for them. Approximately 86 percent of rural adults (47 million) are currently unbanked.

The salaried population has been more widely targeted by financial service providers with an estimated 71 percent (9.6 million) of salaried adults using banking services compared to only 15 percent (4.3 million) of farm workers. Financial products available to the banked segment include savings and current accounts, insurance, ATM cards, debit and credit cards, fixed deposit accounts, value cards, mortgages, other loan products, overdrafts, vehicle finance, Islamic Financing Investment and Islamic loans.

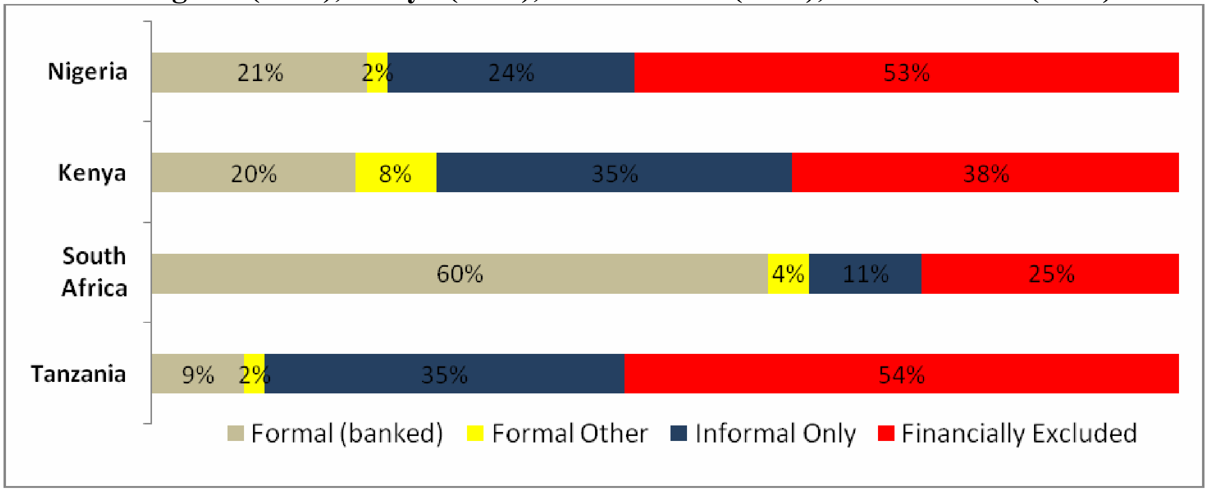
Text Box 1: Key Access Figures

- 74 percent of adults (64 million) have never been banked
- 21 percent of adults (18million) have bank accounts
- Men have better access to finance; only 15 percent of women currently have bank accounts
- 71 percent (9.6 million) of salaried workers vs. 15 percent (4.3 million) of farm employees are banked
- 86 percent of rural adults are currently unbanked
- 80 percent penetration rate of mobile phones presents excellent opportunity for mobile banking

Source: FinScope Nigeria 2008 conducted by EFinA

Figure 2 compares the level of financial inclusiveness across selected African countries. In comparison to Kenya, South Africa and Tanzania, Nigeria has the second highest percentage of people who are financially excluded from the banking system. Given Nigeria's population, the number of financially excluded people in absolute terms is higher than any other African country. This represents a huge market for financial service providers given an enabling policy environment.

Figure 2: FinScope Survey Cross Country Comparison
Nigeria (2008), Kenya (2006), South Africa (2007), and Tanzania (2006)



Source: EFInA 2008 FinScope survey

Individuals and micro businesses are currently using five types of financial services:

Bank Accounts: Savings accounts have the highest usage rate with 92 percent of bank clients reporting having a savings account. Of these, 37 percent hold current accounts, while 11 percent hold fixed deposit accounts. Approximately 18 million people maintain bank accounts. The major deterrents to opening bank accounts include lack of funds for the minimum balance, irregular income and distance from a bank location. Some banks allow customers to open an account for as relatively small initial balances such as NGN 1,000-2,000 (US$ 9-17).[8]

Savings: Sixty-seven percent of adults (58 million) currently have some form of savings. Approximately 55 percent of savers (19 million) save primarily at home or with a savings club. The highest motivation for savings is to prepare for emergencies.

Loans: Only seven percent of adults (6 million) have bank, NGO or MFB loans while 18 percent of adults (16 million) have credit facilities at a shop or kiosk. Fifty-three percent of borrowers (3 million) plan to use the funds to start or expand a business.

Insurance: Personal savings is the most widely used tool for mitigating both business-related and personal risks. Only two percent of the adult population (1.8 million) uses formal insurance as a risk mitigation tool, and vehicle insurance is the most popular insurance service. Based on the FinScope survey, 48 percent of the adult population reports never hearing of insurance, and 17 percent not understanding the service.

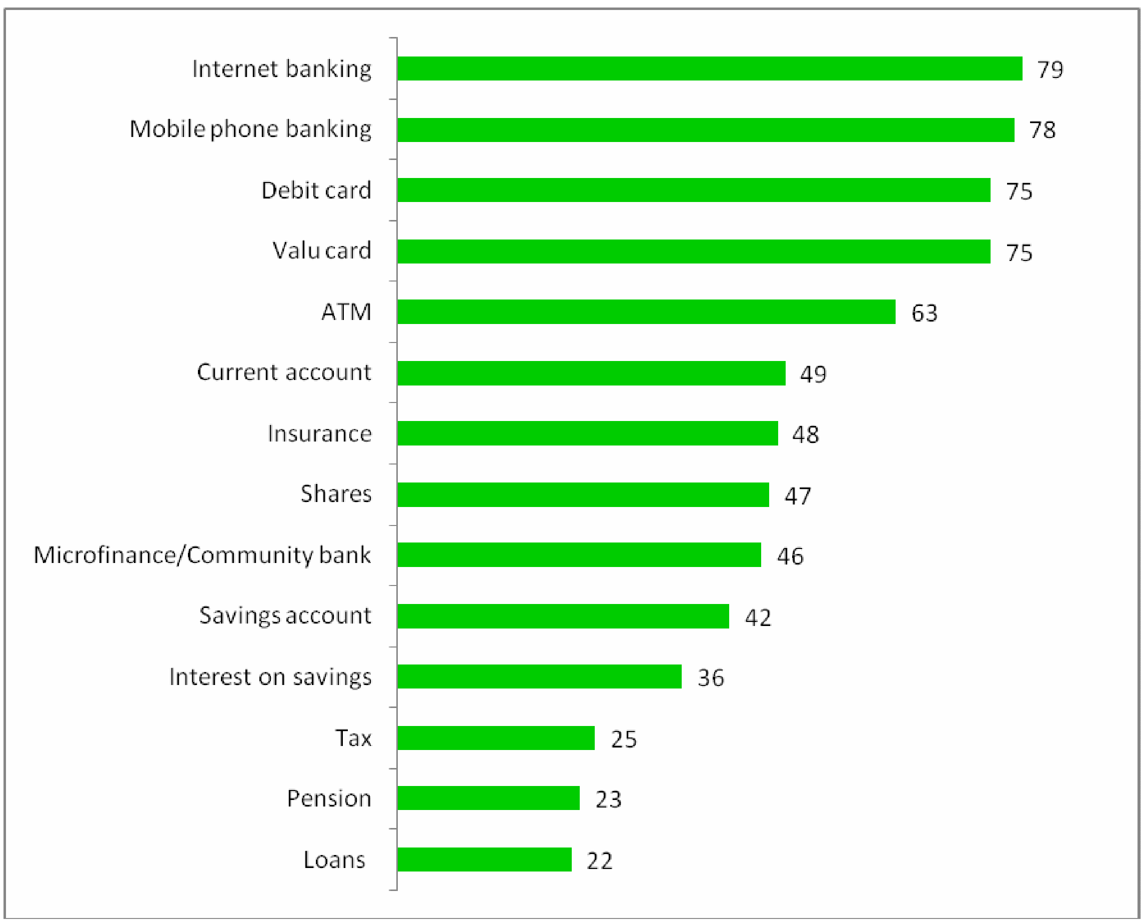
Money Transfer Services: Money transfers include domestic payments and cross-border payments such as remittances. Domestic payments by check and electronic channels are growing dramatically (see Section 3 on the Financial Infrastructure). Remittances into the Nigerian economy are estimated at NGN 507 billion (US$ 4.2 billion) per year with an

[8] Bun, Chinyere & Hernández-Coss, Raúl "UK-Nigeria Remittance: Challenges of Embracing Formal Transfer Systems in a Dual Financial Environment", 2007.

additional, and perhaps equal, amount of unofficial transfers. Nigerians in the diaspora remit monies to family for school fees, meeting basic needs for food and shelter, emergency expenses, investments, and other purposes. It is unclear what percentage of remittances ends up in the hands of the unbanked population. However, only 37.5 percent of the estimated volume of remittance flows NGN 102 billion (US$ 842.7 million) is originated by Money Transfer Operators (MTOs) and disbursed by banks. All other flows originate from correspondent bank transfers, SWIFT, foreign domiciliary accounts, non-commercial imports, private sector imports and other in-kind transactions.[9] Microfinance institutions are currently allowed to provide domestic remittance services.

While access to finance is low, basic knowledge of financial services is even lower. Based on the FinScope survey conducted by EFInA in late 2008, the level of financial literacy among Nigerian adults is extremely low for several types of services including internet banking, mobile phone banking, card-based services, microfinance services, savings and interest (Figure 3).

Figure 3: Percentage of adults who have never heard of the listed services and products.



Source: EFInA 2008 FinScope survey

[9] Bun, Chinyere & Hernández-Coss, Raúl "UK-Nigeria Remittance: Challenges of Embracing Formal Transfer Systems in a Dual Financial Environment", 2007.

Given low financial literacy levels in Nigeria, marketing and consumer awareness will be a key element to building a more inclusive system. At least 46 million Nigerian adults are currently excluded from the banking system, and a majority of the financially excluded dwell in rural areas.

Mobile banking provides financial institutions a real prospect for increasing financial access by channeling services through a less costly alternative to expensive brick and mortar branches. Mobile phones in Nigeria reportedly enjoy an 80 percent penetration rate.[10] However, much of the success of mobile banking will depend on educating the end user of the products. As many as 78 percent of adults (67 million) have no knowledge of what mobile banking entails.

Microfinance banks (MFBs) represent an opportunity for reaching the unbanked. However, the FinScope data suggest that only 3 percent of adults (2.6 million) currently use MFBs as their main bank. Microfinance institutions have a competitive advantage because of their proximity to rural centers and in-depth knowledge of their local markets. However, these institutions can only play a meaningful role in expanding outreach of services if they are financially and operationally sound.

1.2 Demand for SME Finance

The development of a robust SME sector is vital to job creation and poverty reduction in Nigeria. Only a small number of people are formally employed (4.5 million out of 41.5 million working Nigerians).[11] In addition, underemployment is estimated at 70.5 percent, while unemployment peaks at 60 percent among young people.[12]

Nigerian SMEs, particularly in the manufacturing sector, remain fragile and uncompetitive. The oil boom in the early 1970s, which led to the appreciation of the naira and a surge in imports, contributed to the loss of export competitiveness of the Nigerian industry. The poor level of infrastructure (particularly energy and transport), the lack of finance, the low level of skills and education, and poor governance contributed to an underperforming business environment. Given these factors, the contribution of SMEs to the national economy has been declining steadily over the years. Considering particularly the manufacturing sector, the overall share of SME contribution to GDP growth has halved (from 8.4% to 4.6%) between 1980 and 2005.[13] A recent World Bank Investment Climate Assessment (ICA) study (2008) identifies the top constraints for Nigerian SMEs as the electricity shortage, low access to finance and the poor transportation network, in order of importance.

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[10] Senge, Miebi, "Nigeria has achieved 80 percent phone penetration—NDUKWE", October 20, 2008. However, EFInA FinScope data suggests that 49 percent of people have access to mobile phones, actual personal or household ownership is 42 percent. Further, approximately 45 percent of people regularly use mobile phones.

[11] Employment data: National Bureau of Statistics, Social Statistics in Nigeria, 2005. Total working population is 41.5 million out of which 70.50% is underemployed (NBS: Social Statistics in Nigeria 2005). The ICA report (20%) and NSB (4%) have different figures for total unemployment due to different methodologies. However, for unemployment amongst youth (15 – 22 years old), the rates are very similar, at 60 and 55% respectively.)

[12] Nigeria ICA, 2008.

[13] Malik, A. & F. Teal, "Towards a More Competitive Manufacturing Sector", in Collier et al., 2008.

Little information on SME firms by economic sector, number of employees, revenues or assets is available publicly.[14] The Corporate Affairs Commission (CAC), the governmental entity charged with registering and regulating the formation and management of companies in Nigeria, does not have a formal mechanism for providing statistics. As membership in chambers of commerce or other associations is entirely voluntary, membership data (when available) cannot be used for statistical purposes. Based on available estimates, there are approximately 600,000 companies currently established in Nigeria, of which an estimated 400,000 are inactive but have not yet been purged from the records (though such a process has been initiated). There are an additional 1.2 million registered "business names" or sole proprietorships.

A rough analysis of sector GDP data provided by the National Bureau of Statistics (NBS) seems to indicate that the SME sector in Nigeria is much smaller than in other developing countries, with MSME (including microenterprises) accounting for close to 50 percent of GDP (compared to 80% for many developing countries). However, even this figure is not an adequate representation of the reality, as 33 percent of GDP is agricultural and the non-agricultural MSME sector accounts for less than 17 percent of GDP.[15] Manufacturing as a whole, normally a sector with heavy SME presence (and few micro enterprises) and an important source of formal employment, accounts for less than five percent of GDP, with SMEs accounting for half of this.[16] Compared to other developing countries, this contribution to GDP is extremely low and contributes to low levels of formal employment.

Only 5 percent of firms have a loan, despite the fact that 80 percent of SMEs seek financing. Figure 4 shows the extent to which access to and cost of financing are a problem for Nigerian firms. The constraints for funding depend on size of the firm. About 59 percent of small firms report difficulties in access to finance compared to 35 percent of medium firms and 11 percent of large SME firms.[17]

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[14] There are reports of a limited number of private SME market studies, sometimes available for subscription, although these were not made available to the authors. The dearth of reliable data available prompted the team to use the World Bank Investment Climate Assessment of Nigeria as the main basis of analysis, supplementing it with anecdotal evidence and other information from the interviews carried out during the mission.

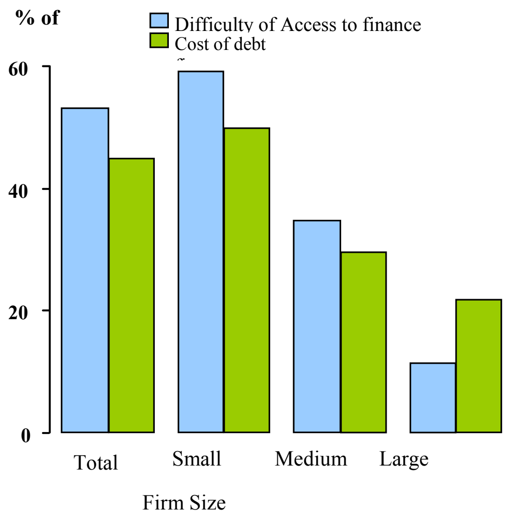
[15] National Bureau of Statistics, GDP data for 2005.

[16] This estimate is based on anecdotal data from conversations with the Nigerian Manufacturers Association (MAN) who mentioned that more than 75% of manufacturing enterprises were either small or medium enterprises, but that their total sales would be about the same as large manufacturers.

[17] Malik, A. & F. Teal, "Towards a More Competitive Manufacturing Sector," 2008.

Figure 4: Difficulty in Accessing Finance and Cost of Debt- Nigeria

(Percentage of firms reporting access to finance and cost of debt as a problem)

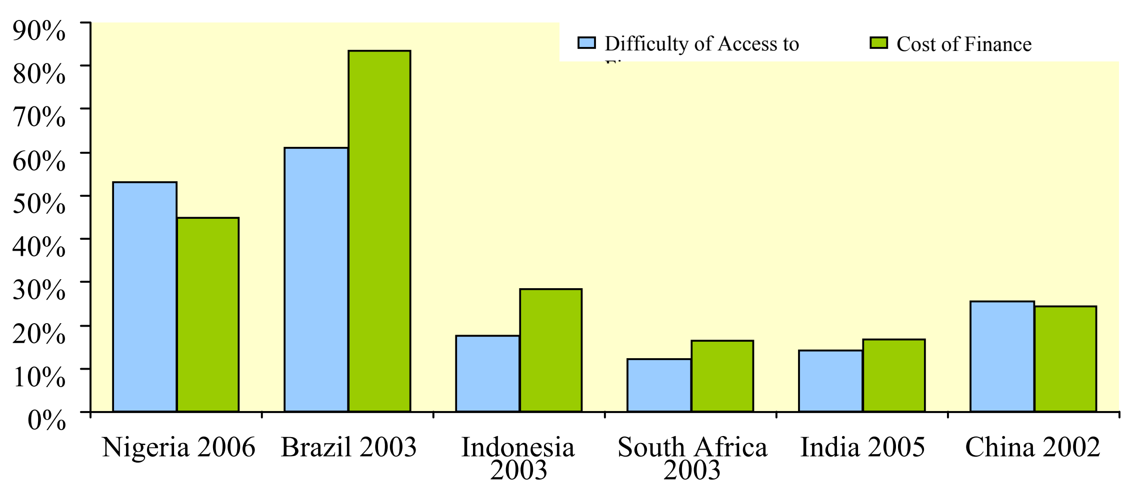


Source: ICA Report (2008)

When compared to relevant countries globally, Nigeria's results exceed those of Brazil but lag behind results for India, China, South Africa, and Indonesia (Figure 5).

Figure 5: Difficulty of Access to Finance: International Comparison

(Percentage of firms reporting access to finance and cost of debt as a problem)



Source: ICA Report (2008)

The 2008 ICA study notes that only around 10 percent of the surveyed SMEs applied for a loan or a line of credit and about 70 percent of them saw their application rejected. However, 80 percent of SMEs that did not apply for financing would like to have a loan/line of credit, compared to only 20 percent of large firms. Hence, SMEs would seem to demand credit, but not apply for it. The main reasons Nigerian SMEs give for not applying for loans are:

- Cumbersome application procedures
- High interest rates
- Inaccessible collateral requirements
- Loan terms (maturities) are much shorter than what companies require.

Despite firms' perceptions of excessively high interest rates, the cost of finance is found to compare favorably with that of the aforementioned countries and generally the issue relates to the amount (monetary value) of the installment as opposed to the cost of credit. When installments are high (due to inadequate loan maturities or inadequate product structure) the interest rate is perceived to be high. Low installment amounts, even when these represent a much higher interest rate, are perceived as being less expensive. The term or maturity of loans is also a serious issue, as Nigeria seems to have the shortest average loan maturity (21 months) among comparable countries such as Kenya, Brazil, China and India.

Collateral is a real deterrent for applying for credit, since every loan of over NGN 10 million (US$ 86,000) must be collateralized (per CBN regulation) with land or buildings and smaller loans generally also require some form of collateral (per market practice). SMEs report that unacceptable collateral or co-signers are the most likely reason (over 50% of firms) for rejection of their loan application.

2. Supply of Financial Services

The Nigerian banking system has recently completed a consolidation process that reduced the number of banks operating in the country from 89 (in 2004) to 24 today. This consolidation was the result of the CBN's decision in July 2004 to raise the minimum capital base for all universal banks to NGN 25 billion (US$ 204 million). The CBN reports that over US$ 1 billion of foreign investment has poured into the sector, and that total capitalization of the banks has increased over the last few years from NGN 293 billion (US$ 2.5 billion) to over NGN 1.1 trillion (US$ 9.4 billion). Non-performing loans (NPLs) as percentage of total loans decreased from about 23 percent before consolidation to less than 8 percent, while total deposits almost doubled.[18] Credit to the private sector is growing at an annualized rate of 72 percent (data for first quarter 2007). The retail network is also expanding, with 4,579 branches and cash centers at the end of 2007, from 3,200 prior to consolidation.

In terms of assets, the majority of bank lending goes to the government (over 15% of total assets),[19] followed by inter-bank lending, then corporate lending (mostly oil and gas, and telecommunications). As to be expected after such massive capitalization, the banks were relatively liquid during the mission in September 2008. Based on international experience, high levels of liquidity often translate into increased retail lending, with consumer lending and mortgage lending leading the way. This has not been the case in Nigeria, as consumer loans are the smallest loan sector, with only around 5 percent of assets in mortgages and auto loans. Recently, Nigeria's financial sector is starting to be affected by the global financial crisis as financial institutions are finding it harder to identify liquidity from international sources; the short- and long-term effects are still unclear.

Nigeria's financial system includes a range of institutions (Table 1) providing microfinance, consumer lending, SME lending, housing finance, investment services, currency exchange, and other services.

Table 1: CBN Regulated Financial Institutions

Banks	24
Discount Houses	4
Development Finance Institutions	5
Bureaus de Change	610
Primary Mortgage Institutions	90
Finance Companies	76
Microfinance Banks	744

Source: CBN

[18] This statement should be understood in the context of the mission where little information was provided from financial institutions or other sources on non-performing loans and other financial performance. Further, NPL data can be distorted to appear smaller by rapidly growing loan portfolios, as has been the case in Nigeria for the past 2-3 years.

[19] CBN Banking Supervision Annual Report 2007 and Goldman Sachs "New Markets Analyst," October 2008.

Retail lending is growing modestly in Nigeria due to a series of factors including the low income (low consumption and payment capacity) of a large percentage of the population, very low formal employment (4.5 million formal jobs[20]), lack of formal identification and credit history, collateral requirements including registration of mortgages and liens, and other factors.[21]

2.1 Supply of Microfinance Services

The following sections describe informal finance and formal institutions including NGOs, legacy community banks, savings and loan cooperatives, and new entrants.

2.1.1 Informal Finance

The 2004 Food and Agriculture Organization (FAO) assessment of community banks estimated that 25 percent of all Nigerians access some informal source of financing.[22] A 2005 USAID demand survey estimates that a majority of funding for MSMEs comes from personal savings, gifts from family members and informal lending schemes known as "*esusu*".[23] In October 2008, the EFInA FinScope survey noted that 24 percent of respondents use informal finance services. However, reliable information on informal services is scarce. The mission was unable to locate information on suppliers or products commonly used in informal finance.

2.1.2 NGOs

NGO[24] microcredit programs in Nigeria date back at least as far as the late 1980s or early 1990s. The Ford Foundation began supporting the sector with the Community Development Foundation in 1993 and until 2004 had provided capacity building grants to 123 organizations worth NGN 19 million (US$ 180,000 at the 2000 exchange rate) and refinancing loans to 241 organizations worth NGN 205.4 million (US$ 1.7 million). The small volumes per organization are indicative of the fragmentation of the sector and very small scale of the NGOs, a condition that persists today with few exceptions.

Only a handful of Nigerian NGOs have developed microcredit operations to an institutionally sustainable scale. At the end of 2007, COWAN and LAPO, the two largest NGOs, reported loan portfolios of NGN 2.2 billion (US$ 18.6 million) and NGN 2 billion (US$ 16.5 million) respectively. Only three other NGOs, SEAP, DEC and FADU, had portfolios greater than NGN 120.8 million (US$ 1 million), and none of these surpassed NGN 362.4 million (US$ 3 million). Collectively, these leading NGOs had NGN 4.9 billion (US$ 40.6 million) in portfolio with 550,000 credit clients, with average loan balances ranging from NGN 1,300-15,000 (US$ 11–126). Most of the NGOs use a version of Grameen solidarity groups to provide small loans to groups. Information on the savings activities of clients is unclear and in any case qualified by the fact that most savings activities are simply obligatory collateral requirements. NGOs may only legally collect deposits from their "members."

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[20] National Bureau of Statistics, Annual Abstract of Statistics 2006, chapter 7 Employment.

[21] The Hire-Purchase Act is a very regimented approach to regulating finance that incorporates rules that protect debtors over lenders and eliminates many traditional incentives to lend

[22] FAO, "Federal Republic of Nigeria: Assessment of Community Banks", September 20, 2004.

[23] USAID, "Micro, Small and Medium Enterprises, Financial Services Demand Survey," July 2005.

[24] The term "NGO" is used in Nigeria to refer to non-profit organizations.

Table 2: NGO Performance Indicators (December 2007)

	COWAN	LAPO	SEAP	DEC	FADU	TOTAL
Total Portfolio	$18,612,528	$16,452,193	$1,339,097	$2,739,040	$1,458,922	$40,601,780
Borrowers	228,000	130,972	24,276	31,705	134,538	549,491
Savers	84,000	35,215	-	-	156,064	275,279
Financial Revenue	na	36.7%	42.8%	30.3%	27.6%	
Financial Expenses	na	6.8%	2.1%	2.9%	2.1%	
Net Financial Margin	na	29.9%	40.7%	27.4%	25.5%	
Operating Costs	na	21.6%	36.5%	24.7%	25.2%	
RoA	na	8.3%	4.3%	2.7%	0.4%	
RoE	na	39.1%	53.1%	-0.7%	0.5%	

Source: Interviews. Financial indicators are percentage of total assets.

The five largest microfinance NGOs include COWAN, LAPO, SEAP, DEC and FADU, and combined they serve 550,000 borrowers and manage a total loan portfolio of NGN 4.9 billion (US$ 40.6 million). Though the number of viable microcredit NGOs is small, these successful organizations play an important demonstration role in Nigeria. They are perceived to have developed a viable model of making very small loans to rural populations, particularly women. LAPO has recently secured commercial bank funding backed by a Grameen Foundation loan guarantee and has expanded rapidly in 2008, reporting NGN 4.8 billion (US$ 40 million) in assets as of September 2008.

The CBN reports that each of the NGOs listed in the table is in the process of applying for a microfinance bank license. The microfinance regulations require that all NGOs with total assets greater than NGN 20 million (US$ 169,000) or more than 2,000 clients are required to transform into an MFB. However, other contacts suggested that there is some resistance from NGOs unwilling to seek an MFB license under the new conditions.

2.1.3 Community Banks

The GoN introduced the Community Bank (CB) license in the early 1990s to promote the growth of banks dedicated to rural areas and lower income groups. The National Board for Community banks (NBCB) issued 1,355 licenses with a minimum capital requirement of NGN 5 million (US$ 43,000) by 1995 but bank failures reduced the sector significantly by the end of the decade. In 2000, the CBN assumed responsibility for regulation and supervision of community banks and relicensed the institutions. By 2002, 881 community banks remained.[25] The 2005 Microfinance Framework allowed the legacy community banks another opportunity for relicensing under the new NGN 20 million (US$ 172,000) minimum capital requirement. The CBN granted provisional MFB licenses to community banks in 2007 although they were required to fulfill

[25] FAO, "Federal Republic of Nigeria: Assessment of Community Banks," September 20, 2004.

certain conditions. As of the December 2007 deadline, only 232 had fully qualified and 375 were pending a final approval by the CBN.[26]

Reliable information about community bank operations is scarce. The 2004 FAO study provides some analysis of the sector between 2000 and 2003 but admits to significant problems with data availability and reliability. More recent GTZ-funded studies of 13 legacy community banks provide a more detailed analysis of individual institutions. In addition, the CBN has published a consolidated balance sheet of the sector at least since 2005. Together, these sources provide a picture of the sector that is also consistent with the views of CBN supervisory staff who have observed the institutions over the years.

Community banks were privately held companies licensed to take deposits from the public and provide basic credit services. As the table shows, the community banks were generally successful at mobilizing deposits and they funded themselves primarily with owner's equity and deposits. The community banks were much less accomplished, however, as lenders. The low allocation of assets to loans that is evident in the 2005–08 balance sheets is indicative of the community banks throughout their history. The community banks are perceived to have been very cautious with their lending, mostly limited to middle income wage earners, pensioners, and to some extent associations and groups. The FAO report estimates that the average loan size was about NGN 43,000 (US$ 353), and the average deposits NGN 6,500–8,400 (US$ 54–70).[27] As the table shows, the community banks have generally preferred to place assets with banks and investments.

Table 3: Community/Microfinance Banks: Key Indicators

	2008 June	2007	2006	2005
[Equity + Deposits] / Assets	85%	83%	85%	85%
Loans / Assets	34%	30%	30%	32%
Investments / Assets	44%	49%	53%	50%

Source: CBN annual supervision reports and 2008 interim reports

The aforementioned sources report an array of organizational weaknesses and governance problems that have been pervasive in the sector. Most of the community banks have been too small to reach an efficient economy of scale. The 2004 FAO study suggests that the average operating cost ratio in the early 2000s was about 42 percent of average portfolio, but that does not include the costs (e.g., loan loss provisions or allowance for impaired loans) associated with what is perceived to have been a wide spread problem with non-performing loans.

Some part of the rapid growth of community banks, and the motivation of their investors, has to do with opportunism and regulatory arbitrage. Banking has long been perceived as a lucrative business in Nigeria, but a commercial banking license became increasing inaccessible to most investors as capital requirements increased and the CBN simply curtailed new licenses during the

[26] CBN/OFID Reports.
[27] World Bank, Rural Finance in Nigeria, Integrating New Approaches, April 4, 2008.

1990s. For some investors, the CB license was the more accessible option. The performance of the community banks suggests that few of these investors entered the business with the interest or capacity for developing financial services for poorer income segments. This history provokes the more relevant question about the motives and talent of the MFB sector, since many of the same institutions, perceptions and opportunities exist today.

2.1.4 Savings and Loan Cooperatives

In comparison to neighboring countries, savings and loan cooperatives are conspicuously invisible on the landscape of formal financial intermediaries in Nigeria. A 2007 survey by the Cooperative Department in the Ministry of Agriculture found over 27,000 Thrift Credit and Investment Societies registered as cooperatives at the state government level, but no data is available regarding their financial position or activity. The Cooperative Department has launched an initiative to create a national structure of cooperatives capable of facilitating collective loans from commercial banks backed by the Agricultural Credit Guarantee Scheme of the CBN. However, these cooperatives are simply organizing members into a borrowers association. If there are any savings and loans cooperatives active in Nigeria, neither the CBN nor the Cooperative Department were able to share financial and outreach information on them.

2.1.5 New Entrants

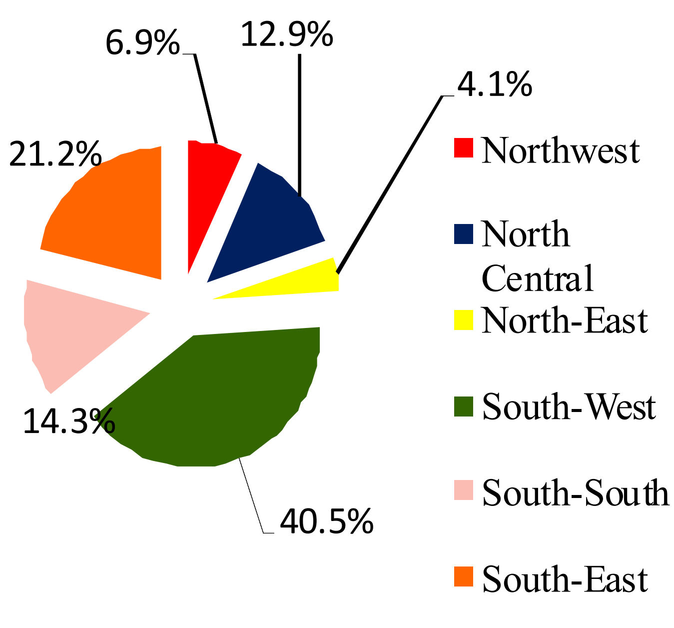
As of July 2008, 175 new investor groups had applied for an MFB license and are either fully licensed or licensed pending incorporation. Among these new entrants is a significant number of internationally experienced microfinance network organizations, investors and technical service providers. ACCION International, for example, has partnered with Citibank-Nigeria, Ecobank, Zenith Bank, IFC, SME Manager (a local investment fund), and another international investor to form ACCION MFB. In various capacities, the International Finance Corporation (IFC), LFS (Access Holding), Shorebank, K-REP (Kenya), BRAC (Bangladesh), Quality Financial Services (Egypt), MicroCred and the DAI group have launched, partnered or are in discussions to enter the market with an MFB license.

CBN reports that ten Nigerian commercial banks have also launched microfinance services, with seven establishing MFB subsidiaries and three creating microfinance departments within the bank. For example, the UBA group launched UBA Microfinance Bank with NGN 3 billon in capital and ambitions to reach assets of NGN 48 billion (US$ 414 million) over the next twelve months. Ecobank entered the market on two levels. At the retail level, they joined ACCION International and Zenith Bank to launch ACCION MFB. In addition, Ecobank is developing a business line of correspondence and treasury services for MFBs.

The sudden influx of international and domestic capital and microfinance expertise is impressive and promising. On the domestic side, some part of this sudden enthusiasm for the microfinance sector is driven by the recent consolidation and over-capitalization of the 24 remaining commercial banks, which are rapidly expanding their investments in many sectors. Some of these entrants are accomplished microfinance investors who are demonstrating enthusiasm for the Nigerian market and a basic level of confidence in the CBN's microfinance bank framework. While most of the new entrants have only recently launched operations, some are growing rapidly. Integrated MFB is the largest, reporting a portfolio of NGN 846 million (US$ 7 million) at the end of 2007 with 8,641 credit clients. By September of 2008 Integrated

MFB reported 126,000 clients, of which 50,000 are savers, with an additional 4,000-5,000 new clients per week. Other leading MFBs are reporting similar rates of growth.

Figure 6: Total Number of MFBs



As a group, the new entrants represent a significant wave of capital and talent in the microfinance sector. However, their rapid expansion entails some risks that are already evident in early indicators. First, many of the new MFBs are very small, inexperienced and inadequately capitalized. The new entrants are also heavily concentrated in the same markets, with 100 licensed in Lagos state and 16 in Abuja FCT. MFB managers in Lagos already report that they are competing with other MFBs for the same clients in some areas of the city.

The legacy community banks are also reporting competition from commercial banks that are opening branches in the same town and offering the same services.

It is also significant that the few MFBs that report their portfolio performance rates to third parties are already showing early signs of repayment problems, with portfolio in arrears >30 days around 10 percent of the total portfolio.

2.1.6 Summary of the MFB Sector

The legacy community banks, the new entrants, and some NGOs are integrating into what is becoming a rapidly growing MFB sector. As of October 2008, a total of 724 MFBs were in operation with 607 converted community banks and 117 new entrants. CBN has granted approvals in principle to another 94 MFBs, which will grow the total number of MFBs to 818. Almost all (98.9%) of the MFBs are classified as unit, with only nine classified as state MFBs.

Based on CBN interim reports as of June 2008, assets for the MFB sector have grown 136 percent since 2005 while equity has increased by 248 percent, resulting in a more capitalized sector (Table 4).

Table 4: Consolidated Balance Sheet of Microfinance/Community Banks (in US$ million)

	2008 June	2007	2006	2005
Exchange rate (NGN to US$1)	115.00	120.00	134.00	130.00
Total Assets	838,174	629,583	410,866	354,329
Loan Portfolio	282,929	190,419	123,124	111,903
Total Liabilities	563,123	447,826	315,727	275,277
Deposits	437,180	343,481	253,797	220,950
Equity	275,051	181,757	95,139	79,052

Source: CBN annual supervision reports and 2008 interim reports

OFID reports that as of August 2008, the average capital adequacy ratio is 37.3 percent and that the quality of new loans is satisfactory while old loans from the legacy community banks are less than satisfactory.

These consolidated numbers do not show the significant differences in capital, scale, and operational capacity of the institutions. Most of the legacy community banks have relicensed with too little capital to overcome the problems that have plagued the sector since the early 1990s. Some new entrants bring capital and talent to the industry, but not in equal measure, and they are competing fiercely in urban areas.

For this diagnostic, an accurate assessment of institutional strength in the MFB sector is impossible for two reasons:

- Obtaining reliable financial and performance reports on the legacy institutions is extremely difficult. Neither the institutions themselves nor the regulator publish such data. A notable exception is the small number of NGOs and MFBs that now publish some data in the MIX Market.[28]
- The new entrants are still very new—many starting in late 2007 or early 2008—and therefore difficult to benchmark, even if data were available.

Although information on individual Nigerian institutions is not readily available, global data from the MIX Market can help give context to the performance of Nigerian institutions. Table 5 below provides global and regional benchmarks, including categories of African MFIs noted by size of loan portfolio.

Comparing data from selected institutions in Table 2, the larger NGO MFIs have strong outreach to clients and high levels of total assets compared to their peers globally and in Africa in Table 5 below. It is not possible to compare the legacy community banks, MFBs, or other institutions given lack of available data. However, going forward, it would be helpful to have a more detailed picture on the health and performance of institutions in Nigeria to permit comparison with global benchmarks.

[28] Thirteen Nigerian MFBs and NGOs publish in the MIX Market at www.themix.org, although not all information is current, and this limits the possibilities for benchmarking performance of Nigerian institutions with other African or global benchmarks.

Table 5: Global and African Benchmarks for MFI Performance

	Total Assets (US$)	Deposits to Loans (%)	Portfolio to Assets (%)	Number of Active Borrowers	Average Loan Balance per Borrower (US$)	Average Deposit Balance per Depositor (US$)	Yield on Gross Portfolio (%)	Portfolio at Risk > 30 days (%)	Return on Assets (%)	Return on Equity (%)
MIX 2007 Benchmarks										
Global	6,897,451	0	77.9	11,041	520	287	29.9	2.7	0.6	3.2
Africa	5,060,916	24.8	62.9	9,800	317	131	33.4	4.8	(1.1)	(3.2)
Africa Small FSS	1,608,174	70.3	49.1	2,871	308	149	40.4	5.2	2.1	13.6
Africa Medium FSS	6,231,614	29.3	62.5	8,040	410	104	36.6	3.1	2.5	11.8
Africa Large FSS	44,407,357	78.9	60.6	44,887	897	215	32.2	3.8	2.8	14.2

Source: MIX Market 2007 Benchmark Report. Based on information for 890 financial institutions in 94 countries. Africa Small FSS peer group includes institutions with less than US$2 million in gross outstanding loan portfolio that are financially self-sufficient (FSS) Africa Medium FSS peer group includes institutions with US$2 to 8 million in gross outstanding loan portfolio that are financially self-sufficient. Africa Large FSS includes institutions with over US$8 million in gross outstanding loan portfolio that are financially self-sufficient. See report for definitions of indicators and other peer groups. Report available at http://www.themix.org/pub_popup.aspx?publicationID=255&latest=yes&hidepath=yes

2.2 Supply of Branchless Banking

Branchless banking is the delivery of financial services outside conventional bank branches using information and communications technologies and nonbank retail agents. Due to its potential to radically reduce the cost of delivery and to increase convenience for customers, branchless banking can expand coverage to previously unserved segments of the population. Technology can help a range of market actors push the boundaries of access to finance, including banks, MFIs, SME finance providers, mobile phone operators, and technology companies.

Nigerian financial institutions, mobile network operators and private switch operators are paying an increasing amount of attention to the delivery of financial services through innovative technologies outside bank branches. Although electronic payment transactions currently account for less than 1 percent of all payment transactions in Nigeria, they are increasing rapidly: the value of funds transferred electronically in July 2008 is nearly double the amount transferred in January 2008. The growth rate is expected to continue as banks scale up prepaid/debit card issuance and expand ATM/POS networks. (Payments and other aspects of Nigeria's financial infrastructure are discussed more in Section 3.)

However, mobile telephone payment platforms may have the most dramatic effect in increasing the volume and value of electronic payment transactions. Mobile banking products, currently being offered primarily by private switch operators include bill payment, retail payments and funds transfer to a bank account, mobile account or prepaid card.

Interswitch reports that more than 18 million debit/credit cards and 6 million prepaid cards can access its network. Interswitch's mobile funds transfer platforms are currently being used by 8 banks, 5 microfinance banks and one mobile network operator. Another private switch operator, eTranzact, which already provides mobile banking platforms to 20 commercial banks, is about to launch an ATM "cardless transaction" product (called "CardlexCash") by which money can be sent to even unbanked mobile phone subscribers via an SMS containing information which, together with a code provided separately by the sender, can be entered into an ATM machine to convert the electronically stored value into a cash withdrawal.[29] New services under consideration include managing multiple bank accounts via a single mobile telephone.

A mobile network operator is planning on venturing with a commercial bank to launch a mobile payment platform which will permit customers to make deposits into a mobile-accessed account through the use of scratch cards. The reliance on scratch cards is intended to manage any risk associated with "cash-in" transactions conducted at retail outlets.

MoneyBox is also preparing to launch a savings and payment system based on deposits made through scratch cards. The system will permit electronic value stored on a mobile phone to be used to pay bills, buy mobile airtime and send money. Value can also be cashed out at agent locations and MoneyBox has recently signed an agreement with the Nigerian Postal Service (NIPOST) to use NIPOST's approximately 3,000 branches as agent locations. MoneyBox envisions using different tiers of KYC review based on the value of the intended funds transfer.

[29] "E-Tranzact to Launch ATM Mobile Cardless", Daily Independent, October 21, 2008.

2.3 SME Finance

Nigerian firms tend to rely heavily on retained earnings and their own funds (70% of firms) for financing, while bank lending is very low (1% of firms). Supplier credit is also low, accounting for only a quarter of SME financing as seen in the table below.[30]

Table 6: Sources of SME Finance in Nigeria

Percentage of financing from:	Total	Small	Med.	Large
Own Funds/Retained Earnings	70%	70%	71%	61%
Borrowed from banks and other financial Institutions	1%	1%	2%	2%
Purchases on credit from suppliers and advances from customers	25%	25%	25%	35%
Borrowed from family, friends and other informal sources	4%	4%	2%	1%

Source: ICA Survey (2008)

When compared with global experience, SME finance in Nigeria seems especially limited (Table 7).

Table 7: Sources of Financing: International Comparison

Percentage of short term financing from:	Nigeria 2008	Brazil 2003	China 2003	India 2005	Indonesia 2003	Kenya 2007	S. Africa 2003
Internal Funds/Retained Earnings	70%	44%	13%	47%	38%	73%	66%
Borrowed from banks and other financial Institutions	1%	30%	27%	32%	16%	7%	17%
Purchases on credit from suppliers and advances from customers	25%	15%	2%	9%	4%	17%	12%
Borrowed from family, friends and other informal sources	4%	5%	8%	9%	20%	3%	1%
Issued new equity/debt	-	4%	12%	2%	2%	-	1%

[30] It is to be noted that this table refers only to short-term financing. For long-term financing, firms, supplier credit is not an option, so firms tend to rely on own funds over 90 percent of the time.

Source: ICA Survey (2008)

Results are similarly low for other credit products like overdrafts and lines of credit, often a preferred way of providing working capital to SMEs. Table 8 shows that only 4 percent and 8 percent of Nigerian SME firms have access to a line of credit or an overdraft, respectively. As noted above, access for small firms is much lower than for medium firms.

Table 8: Access to SME Credit by Firm Size in Nigeria

Percentage of firms with:	Total	Small	Medium	Large
Overdrafts	8	6	13	24
Lines of Credit/loans	4	3	6	15

Source: ICA Survey (2008)

As seen in Table 9, access to credit (overdrafts, lines of credit, loans) also varies by economic sector. The firms with the highest access are those in the food industry, as validated by the recent proliferation of local fast food chains and restaurants witnessed in Nigerian urban areas over the past few years. The garment sector attracts the lowest volume of credit, followed by other manufacturers. These results indicate that Nigerian banks and financial institutions may prefer lending to the retail and services sector, which generally have shorter turnaround times and can pay back debts more quickly than manufacturing firms. These impressions were confirmed during interviews with the Nigerian Association of SMEs (NASME), the Manufacturers' Association of Nigeria, and other contacts.

Table 9: Access to SME Credit by Sector in Nigeria

Percentage of firms with:	Manufacture: Food	Manufacture: Garments	Manufacture: Other	Retail	Other Services
Overdrafts	11.0	0.5	6.0	10.6	7.5
Lines of Credit/loans	5.5	1.0	2.3	5.0	4.1

Source: ICA Survey (2008)

2.3.1 Leasing

Contrary to many other countries, leasing companies are not regulated financial companies in Nigeria, including those that specialize in financial leasing.

A popular credit option among SMEs is equipment leasing, which seems to be easier to obtain than other types of equipment financing and includes tax incentives. Between 2003 and 2007, the Equipment Leasing Association of Nigeria (ELAN) recorded a quadrupling of leasing volumes granted by its members. This substantial growth is especially significant given the lack of a leasing law[31] and judicial use of the hire-purchase act when dealing with leasing cases.[32]

[31] A leasing law has been drafted and was approved by the National Assembly in 2007, however it has not yet received presidential approval nor signed into law.

[32] The Hire-Purchase Act was introduced in October 1968 and regulates all hire-purchase and credit-sale agreements of less than NGN 2000, and all automobile financing. This Act gives the government ample powers to modify

The hire-purchase act is a much regimented approach to regulating finance that incorporates rules that protect debtors over lenders and eliminates many traditional incentives to lend.

A total of NGN 242 billion (US$ 2 billion) was registered in 2007, out of which approximately 20 percent was in the form of operating leases and 80 percent were financial leases. Although no data break down is available by firm size, a comparison of amounts by sector indicates that only 30–35 percent of the total NGN 245 billion (US$ 2.1 billion) in leasing went to SMEs. Of the total leasing volume recorded for 2007, NGN 56 billion (US$ 482.8 million) went to the manufacturing sector, NGN 52 billion (US$ 448.2 million) went to transport and NGN 6 billion (US$ 51.7 million) to agriculture.

Small independent financial and leasing companies cater more to the SME market, while banks tend to serve larger companies (predominantly for oil and gas) with bigger leasing amounts.[33] Of the estimated 250 leasing companies in Nigeria, most are non-financial companies that do not accept deposits (and are not regulated by the CBN). These companies typically face high costs of funds, as they borrow at commercial rates from the banking system. ELAN mentioned that most leasing companies are able to access loans from the financial system at rates between 22 and 30 percent per annum. With margins, the final cost to the SME customer is between 35 and 50 percent. The fact that such leasing is growing in spite of the high costs involved is a clear indication of the lack of financing alternatives.

Additionally, and probably due to the problems with mortgages (liens) on moveable assets, vehicle financing is mostly done through leasing, and most car dealers or car companies have leasing arms. Leasing is often favored in countries that have weak systems for enforcing liens on moveable assets as the ownership of the item tends to remain with the lessor and upon non-payment repossession of the asset does not require legal action. This would certainly be the case in Nigeria where lease payments are often secured with post-dated check and enforcement is informal. For example, enforcement is often limited to having a police officer accompany the lessor's agent to the lessee's place of business and repossessing the asset while threatening the lessee with jail for using a check with insufficient funds.

2.3.2 Finance Houses

Finance houses in other countries generally focus on consumer lending, but the lack of such a market in Nigeria and their inability to compete in the "corporate" market has led them to focus on lending to SMEs. Finance houses appear to be mostly active in short term working capital loans, discounting of invoices (factoring), and some purchase order financing. Equipment leasing, particularly of small industrial equipment (especially generators), is also on the increase. On the liability side, these companies are not allowed to take deposits, but can accept "borrowings" from individuals to a minimum of NGN 100,000 (US$ 862). The sector's reputation has suffered as many informal and non-regulated deposit taking companies have called themselves finance companies. This has led the CBN along with the Finance Houses Association of Nigeria (FHAN), to look at ways to strengthen and reposition the sub-sector.

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contracts and severely limits the recourse a seller has against a purchaser who defaults, to the point that after a percentage of payments has been made, the seller looses all right of recovery, thus in effect encouraging buyers to cease payment.

[33] Some banks have reportedly established subsidiaries to expand this line of business beyond the oil and gas sector.

2.3.3 Factoring

Factoring is a much less common form of finance in Nigeria. Most factoring is granted by banks to companies in the oil sector or select large corporate clients with lower perceived credit risk. In other sectors, where little or no value chain analysis is carried out, banks perceive higher risk in providing factoring finance to an SME.

2.3.4 Microfinance Banks

MFBs are very lightly involved in the SME finance sector, but this is expected to change, especially for some of the new MFBs launched by banks. A number of MFBs have already visited business associations such as the National Association of Small and Medium Enterprises (NASME) and the Manufacturing Association of Nigeria (MAN) to promote their services. However, MFBs are formally limited to keep 60 percent of their portfolio below the NGN 500,000 (US$ 4,310) loan threshold.

2.3.5 SMEEIS Funds

The Small and Medium Enterprises Equity Investment Scheme (SMEEIS) was initiated by the Bankers' Committee in 1999 (becoming operational in 2001) as a response to the Government's concerns for the promotion of SMEs as vehicles for rapid industrialization, sustainable economic development, poverty alleviation and employment generation. The scheme required all banks to set aside ten percent of their annual after tax profits for SME promotion and investment in SMEs. The investments could take the form of loans or equity, although a mandated nine percent interest rate cap on loans reduced incentives to lend and led banks to seek equity investments in SMEs. SME equity investments are especially difficult given due diligence requirements and difficulties to exit the investment through sale of shares, and this was compounded by the banks having little experience with this type of investment. Understandably, the banks had difficulty identifying suitable SMEs.

As of end-December 2008, SMEEIS investments totaled NGN 28 billion (US$ 194.4 million[34]) in 333 companies (Table 10), out of a total NGN 42 billion (US$ 291.6 million[35]) in the fund.

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[34] Exchange rate as of 23 January 2009: N1=$144 (Central Bank of Nigeria).

[35] Exchange rate as of 23 January 2009: N1=$144 (Central Bank of Nigeria).

Table 10: SMEEIS Investments

Sector	Number of Projects	Amount (NGN millions)
Agro processing (including wood work and water bottling)	45	2,312
Manufacturing	144	8,104
Construction	13	2,786
Minerals	3	59
Information Technology and Telecommunications	24	1,788
Education	6	398
Services	76	5,313
Tourism and Leisure	23	7,454
Total	333	28,204

Source: Central Bank of Nigeria: Development Finance Department

In its original form, SMEEIS suffered from design flaws that reduced its scope for success. However, some banks realized that equity investing and SME investing required a special set of skills and characteristics that were not present in the banking industry at the time. As a result, specialized institutions were established as venture capital companies with the Securities and Exchange Commission of Nigeria. Examples of these new venture firms include:

- Amalgamated Capital: Manages SMEEIS funds for a few banks
- Aureos: Manages SMEEIS funds for a few banks
- First Funds: Subsidiary of First Bank
- First SMI: Manages SMEEIS funds for 3 banks
- SME Manager: Manages SMEEIS funds for 14 banks
- UBA Private Equity: Subsidiary of UBA
- Unique Venture Capital: Manages SMEEIS funds for a few banks.

In addition to these above mentioned SMEEIS fund managers, the early experience in venture capital led a few institutions to develop investment vehicles that would not be subject to SMEEIS restrictions. These include:

- Actis: Funded in part by CDC Capital Partners (part of the Commonwealth Development Corporation), a UK government fund specializing in venture investing in less developed countries. Not solely an SME fund, it applies mezzanine type financing for deals in the sector.
- Aspire Nigeria: A $30 million US dollar fund dedicated to investing in SMEs set up by Diamond Bank, Shell Petroleum Development Company, and GroFin of South Africa.
- Avante Capital: Promoted by Ocean and Oil Holdings, this is more of a typical venture fund focusing on larger deals.
- Capital Alliance Nigeria: A Nigerian private equity firm whose funds focus on medium sized companies in Nigeria. The IFC is an investor in these funds.

- Vectis: An Athens (Greece) based private equity firm that allocated NGN 9.9 billion (US$82 million) for investment in Nigerian firms. Minimum investment size restrictions indicate that it will not be directly investing in SMEs.

In early 2008, the low level of funds invested, as well as changing national priorities, led the Bankers Committee to revise SMEEIS and transfer the balance to a MicroCredit Fund, in effect eliminating SMEEIS at a time when the venture funds created by the banks had acquired the necessary skills and were beginning to make a difference.

2.3.6 Development Banks

Of the five development finance institutions in Nigeria, two are active in SME lending. The Nigerian Agricultural, Co-operative and Rural Development Bank (NACRDB) was created with the objective of providing affordable credit and developing a savings culture in rural and poor segments of Nigerian society. The bank reportedly serves approximately 700,000 micro enterprise clients, especially those in rural areas, (with loans up to NGN 250,000) and 300,000 SME (with loans from NGN 250,000 to NGN 5,000,000). Interest rates are capped at a highly subsidized rate of 8 percent per annum. NACRDB has generated losses every year, and due to capital depletion to finance administrative costs and loan losses, it has substantially reduced its lending and in 2007 provided approximately NGN 1.7 billion (US$ 14.7 million) in loans.[36]

A more successful attempt by the government to support SMEs is the work carried out at the Bank of Industry (BOI), which has committed 89 percent of its portfolio in loans to 65 small and medium enterprises.[37] BOI targets firms that use local resources, the agricultural sector, firms with capacity to generate employment, export-oriented firms, firms with linkages to larger enterprises, and firms run by women entrepreneurs. Loans are in the range of NGN 10–200 million (US$ 86,000–1,700,000) with a three to seven year tenure and one year moratorium. BOI interest rates are capped at 10 percent. The BOI reports total assets of NGN 23.6 billion (US$ 203.4 million), and growth is limited by its small equity base, lack of deposits and its lengthy process for loan disbursement.

2.3.7 Other Bank Initiatives for SME Finance

A few banks are beginning to offer services adapted to SMEs. Diamond Bank is partnering with the IFC to extend credit to SMEs, help them with their cash-flow and provide them with business development services. Services include both asset financing and working capital (guarantees, letters of credit, overdrafts, etc.) for which a credit scoring exercise is done immediately at the branch and the pre-approved application is sent to headquarters where all credit risk assessment is finalized. Diamond Bank is also establishing a venture capital fund for SME equity investment in partnership with Shell. EcoBank is starting a very similar process, with an SME expert provided by the IFC due to arrive before year end 2008. Oceanic Bank is being assisted by McKinsey in developing its SMEs operations. Currently, Oceanic Bank provides both asset

[36] Net lending in 2007 was less than the bank's non-interest expenses of NGN 2.7 billion for the same year.
[37] Data as of June 2007 from the BOI "Delivering our Mandate" publication dated July 2007. Two other figures were verbally given to the team, one of 181 SMEs and another of 300, as of August 2008.

financing and working capital and is considering loans to establish franchises, currently a popular line of business.

3. Financial Infrastructure for Access to Finance

3.1 Training, Capacity Building, and Associations for the MFB Sector

Training and capacity building resources have been delivered for the most part through donor supported projects. The Ford Foundation has sponsored a program that has provided capacity building grants to NGOs since 1993. UNDP implemented Microstart through 2003, and the follow up program starting in 2005 provided capacity building for some of the strongest NGOs to replicate the Association for Social Advancement (ASA) model. LAPO, DEC and JDPC were selected as “break-through” organizations and received training from ASA. The UNDP project also aspired to train an additional group of NGOs and strengthen the Community Development Foundation as an industry network association, but neither component will be fully implemented prior to the project end in 2008. The CBN has recently organized the first seminars that are part of a broader MFB management training program. GTZ is currently providing on-site management capacity support to 4–6 MFBs in Niger and Nasarawa States. The World Bank/IFC-supported MSME project is also providing capacity building grants in six of the new MFBs.

In the past, the Community Development Microfinance Roundtable served as an association of NGO MFIs, although it is no longer functional. There are currently two initiatives competing for the status of an official industry association for the MFBs. The National Association of Microfinance Banks is a reincarnation of the former Association of Community Banks. The Association of Microfinance Banks of Nigeria is a new initiative launched by managers of the newly licensed MFBs. Neither organization appears to be staffed or operational. In parallel, the CBN has organized an Association of MFIs that operates in six geopolitical zones.

3.2 Credit Registries

3.2.1 Credit Risk Management System

The CBN maintains a credit information system called the Credit Risk Management System (CRMS). This system was set up as a result of the rise in non-performing credit portfolios in banks during the 1980s and 1990s. The existence of “predatory debtors” in the banking system who abandoned debt obligations in some banks only to contract new debts in other banks was also cited as a factor. On the part of the regulators, the paucity of credit information had inhibited consistent classification of credits granted to certain borrowers and their associated companies.

The decision to establish a credit bureau in Nigeria was authorized by CBN Act 2007. The enabling legislation empowered the CBN to obtain monthly bank reports on all loans with a minimum outstanding balance of NGN 100,000 (US$ 862), now NGN 1 million (US$ 8,620). Banks are also required to make status enquiries on any intended borrower to determine their eligibility, and banks are penalized for non-compliance.

Presently the CRMS is a web-enabled database that allows banks and other stakeholders to conduct status inquiries on borrowers as a support mechanism for bank credit decision procedures.[38] The CRMS provides a credit history (both positive and negative data is maintained as well as historical trends) of borrowers in the system plus a profile on the total liabilities a debtor has acquired within the banking system. Information dating back to 1994 is maintained by CRMS. As of 31 December 2008, fewer than 30,000 borrowers were registered in the system.[39]

Banks are reportedly only required to list loans as nonperforming 90 days after due. Consequently habitual late payers that pay their obligations within 90 days would have a "clean" credit history. Loan classifications are not a part of the information generated at this time, thus a debtor may have different classifications in different banks with no sharing between banks. The absence of loan classification, or any scoring mechanism, also limits the benefits that the system provides.

The lack of a unique identifier for individuals, and to a much lesser extent companies, poses a significant challenge for credit information registries in Nigeria. There are various forms of personal identification (including a national ID), but all have limited coverage and none is fully reliable. Additionally names can be altered by use or habit, and birth dates and addresses are unreliable. The CRMS generates its own ID for every new debtor introduced into the system by the bank the individual is borrowing from. This CRMS-generated ID then becomes obligatory for use by all banks. While the CBN is proud of its achievement in this area, it also recognizes that duplicates sometimes get past the different filters and that the database contains some ID errors. Efforts must be made to safeguard the CRMS system and make it even more efficient, particularly from a regulatory point of view. If the CRMS system is truly effective, the CBN should make CRMS information an integral part of its off-site supervision.

The CBN Microfinance Framework indicates that the current CRMS System shall be expanded to accommodate MFB clients. In effect, this would lower the information threshold for reporting the CRMS from the current NGN 1 million (US$ 8,620) to less than NGN 50,000 (US$ 431) for MFB loans. This has not yet occurred and is unlikely to occur for practical reasons. The existing system is designed for managing risks associated with large borrowers and, according to CBN staff, cannot handle the volume of small loans expected to develop in the MFB sector. Further, the CRMS would be unable to cope with such an expansion without dramatically increasing ID duplicates and lowering the quality of information. Such an expansion would critically endanger a system that, though very small, works relatively well. Since credit information systems are important for microfinance and branchless banking clients, other alternatives beyond the CRMS should be identified.

[38] The CRMS is not a formal department within the CBN. A CRMS Committee manages the system and is composed of staff from throughout the CBN. The committee consists of thirteen officers from Banking Supervision plus two officers from each of the following departments: Legal, Banking Operations, IT and OFID. Such officers maintain the database in addition to their regular duties in their respective departments.

[39] Data verbally provided by CBN staff. Unfortunately the team was unable to access published data.

3.2.2 Private Credit Bureaus

An integral part of a well functioning credit information system is private credit bureaus that would cover all sectors of the economy that can gather and provide information from a range of credit sources.

The Banking Supervision Department established a working group to prepare guidelines that would define the licensing, operational and regulatory requirements for private sector credit bureaus in Nigeria. This committee prepared a draft regulation and is currently receiving assistance from the World Bank/IFC-supported MSME Project. The draft dated October 2008 is well designed and should pave the way for a competitive credit information system to develop in Nigeria. Based on this draft, certain issues such as the use of a unique identifier, the dispute resolution process and data subject rights may need to be revised in order to strengthen the system.

A total of four private companies of significant size (and as many as four others) in Nigeria are currently working on credit bureau initiatives.[40] Three of these bureaus are located in Lagos: Credit Reference Company on Victoria Island, Credit Registry in Marina and CreditChex in Apapa. XDS Solutions is the only one of these bureaus located in Maitama, Abuja. The most comprehensive of these registries is the Credit Reference Company (CRC), which started in 2005. CRC is owned by 11 member banks in partnership with Dunn and Bradstreet, an international credit registry firm. The initiatives are at various advanced stages of development but none are fully operational as they have not yet been licensed by the CBN, pending finalization of credit reporting regulations.

Having private credit bureaus exchange client identifier information (particularly biometric, which seems to be the preferred solution by the likely new entrants) would probably help solve the ID problem in a relatively short period of time (if common standards are applied in biometric data collection/verification).

These advances would place Nigeria in the enviable position of being able to have a fully functioning, competitive credit reporting industry in the very short term. This would enable Nigeria to reach respectable levels of database coverage much faster than other countries.

3.3 Collateral and Company Registries

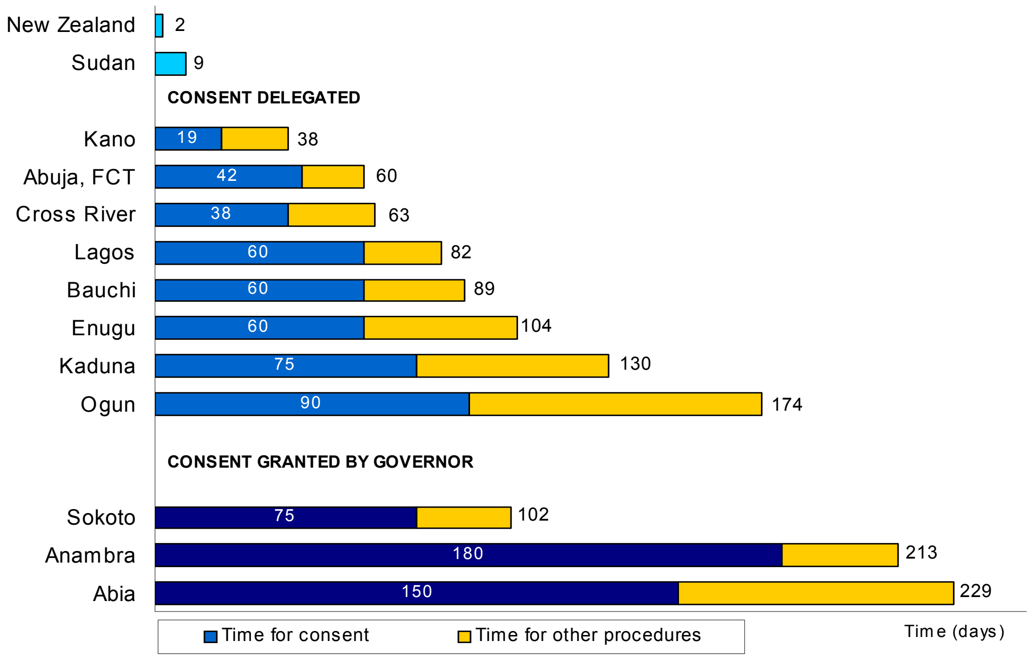
3.3.1 Mortgage Registry

SME loans are often guaranteed by real estate, either the home of the owners, or the company's warehouse or offices. Mortgage financing is therefore normally an important component of SME finance. In Nigeria, the Land Use Act of 1978 vests ownership of all land in the Governor of each state, who is entitled to allocate land for development through 99 year leases. Thus ownership of land is in reality a “right of occupancy” which is recognized through a certificate of occupancy. This right of occupancy is transferable, with the Governor's consent.

[40] Interview with MSME project staff in Nigeria.

All transactions in property, including sales, leases, mortgages and other charges, are subject to complex requirements including the consent of the State Governor, which adds a significant amount of time to the registration process as the figure below shows for Nigeria compared to global benchmarks.

Figure 7: Time to Register Property

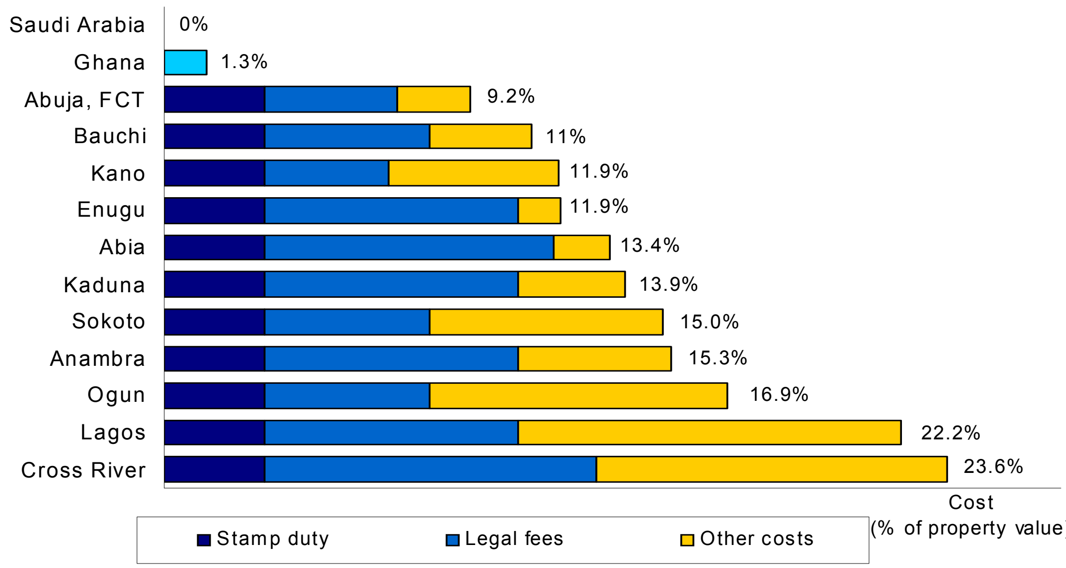


Sources: Presentation to FSS2020 Legal Working Group Committee Meeting, prepared by Mahesh Uttamchandani, Senior Counsel, World Bank; and Doing Business in Nigeria 2008, Doing Business, IFC.

In addition to the time it takes to register property, there is a complex and expensive system of registration charges, which cumulatively are among the highest in the world. To further complicate matters, there seems to be an equally complex system of waivers, derogations and special deals so that the full impact of the charges may be mitigated for the privileged few.

The 2009 World Bank Doing Business report ranks Nigeria at number 176 (out of 181 countries) for registering property with 14 procedures, a duration of 82 days and costs of 21.9 percent of property value. As noted in the figure below, total fees are estimated at 20–30 percent of the mortgage, although developers and others can negotiate waivers for particular developments or even defer payments.

Figure 8: Cost to Register Property (Fees by Locality)



Source: Presentation to FSS2020 Legal Working Group Committee Meeting, prepared by Mahesh Uttamchandani, Senior Counsel, World Bank; and Doing Business in Nigeria 2008, Doing Business, IFC.

Mortgages must be registered at the lands registry of the state where the property is registered and, in the case of a corporate borrower, also at the CAC registry. Land registries are not interconnected with the CAC registry, and searching for details of security given is unreliable for many reasons. As a result, there is a widespread practice of taking but not registering security over land (mortgages), especially for short-term borrowing. This practice leaves lenders completely unprotected from a legal viewpoint, but it has some "moral" value as the borrower has in fact agreed to give the real estate as security. One reason for this common practice is that the cost of registration can easily negate any potential profit on the loan, or alternatively, if the cost is passed to the borrower, the cost of the loan would then be prohibitive (even exceeding informal market rates). Typically mortgages are only registered prior to legal action being required. Consequently, information held by land registries is often inaccurate and of little use to credit providers seeking to establish the credit-worthiness of potential borrowers. Given these complications, short term working capital loans or overdraft facilities guaranteed by mortgages are simply not available to lesser known or younger SMEs, even if they have real estate to offer as collateral.

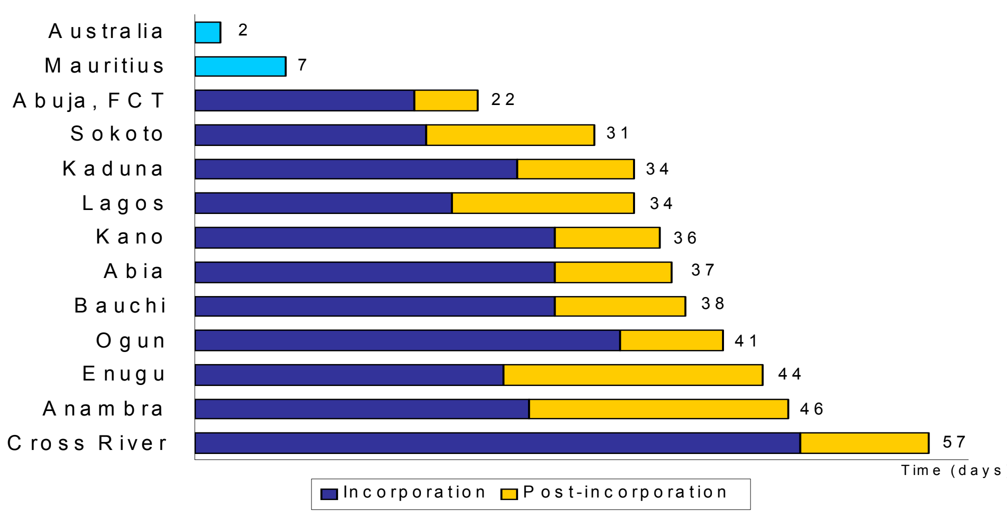
3.3.2 Lien Registry

As mentioned previously, financial institutions are required to rely on collateral for lending, as unsecured lending is limited to small loans. Most financial institutions only establish lines of credit, loans or overdraft facilities against the security of real estate, notwithstanding the difficulties explained above. In terms of liens on moveable assets, including equipment, the situation is even more challenging. The CAC maintains a registry where claims against the assets of companies can be registered, but these are general claims on total assets of the company (i.e., debentures), and individual assets cannot be singled out. Furthermore the registration is limited to companies. Sole proprietorships, most partnerships and individuals are excluded. As noted in the recent World Bank Report on the Observance of Standards and Codes (ROSC) in respect of Nigeria's insolvency and creditor rights (ICR) system, banks generally have a low level of confidence in this registry. There is currently no registry of movable assets or any dependable method of establishing what, if any, claims exist on these assets. The lack of such a registry rules out the possibility of equipment or asset financing for SMEs, with the exception of leasing.

3.3.3 Company Registration

The CAC is also the entity charged with registering and regulating the formation and management of companies in Nigeria. The incorporation process is reasonably agile, although it varies between regions in Nigeria. As SMEs require relatively larger loans and longer terms (comparatively to micro enterprises), banks often require that they become formal companies prior to establishing credit relationships. In many developing countries the process for becoming "formal" may be so time consuming and costly that it becomes an obstacle to SME finance, but this is not the case in Nigeria, as seen below. The system is sufficiently effective and costs sufficiently low that SME can become formal with relative ease, either by incorporating, or by registering a "business name," in effect a sole proprietorship.

Figure 9: Time to Register a Company



Source: Presentation to FSS2020 Legal Working Group Committee Meeting, prepared by Mahesh Uttamchandani, Senior Counsel, World Bank; and Doing Business in Nigeria 2008, Doing Business, IFC.

3.4 Retail Payment Systems and Branchless Banking Infrastructure[41]

The CBN has reconstituted the National Payments System Committee (NPSC) and its technical sub-committees as a forum for high level representation of the key stakeholder groups. Seven key initiatives have been identified to promote the usage of electronic payment instruments, with working groups established to carry out the activities.

The main payment instruments available in Nigeria include large-value credit transfers, checks, retail electronic debit and credit transfers, and payment card systems, among others. Electronic

[41] Portions of Section 3.4 have been adapted from the August 2008 draft of the World Bank's Diagnostic Report of the Payment and Settlement Systems and Reform Strategy in Nigeria.

purses (a form of stored value cards), internet-based banking along with mobile payment services have recently been introduced.

3.4.1 Real-Time Gross Settlement System

The CBN in 2006–07 commissioned a real-time gross settlement (RTGS) system which it owns and operates. The RTGS system was implemented with the primary aim of reducing risk and enhancing efficiency in the payment systems though the World Bank FSS 2020 diagnostic study on the Nigerian payment system indicates that the system meets neither international standards for risk mitigation and efficiency nor the needs of users. Currently, the provision and repayment of intraday liquidity is not automated in the RTGS system. Non-automated processes often result in intraday credit spilling over into overnight lending. In addition, connectivity between the RTGS system and the banks' internal systems still does not permit straight-through-processing.

3.4.2 Nigerian Central Switch

The CBN also recently established the Nigerian Central Switch (owned and operated by the Nigerian InterBank Settlement System or NIBSS) in order to promote interoperability for Nigerian retail payment systems. Despite the 2003 Guidelines on Electronic Banking in Nigeria, which encourage private switch operators to interconnect,[42] private switches are still not interoperable. This lack of interoperability results in (i) cost inefficiencies as multiple ATMs and POS terminals are deployed to the same high-traffic areas (such as hotel lobbies and airports), while leaving other areas unserved, and (ii) limits on the number of financial access points available to Nigerian consumers who are denied the use of access points that are not part of their bank's network. In an effort to promote interoperability, the Nigerian government has privately informed all licensed switch operators that they must connect to the newly established Nigerian Central Switch (NCS), operated by NIBSS. NIBSS is owned by each of the 24 commercial banks and the CBN. Many of the commercial banks also have ownership interests in the private switches.

There are currently five private switching companies operating in Nigeria, the largest of which (with an estimated market share of more than 90%) is Interswitch, to which all 24 commercial banks are connected. The others are Cards Technology Limited (CTL), Valuecard, eTranzact and 3 Line. With limited but growing numbers of access points and providers, policy should encourage competition among payments providers (see Section 8.2.1).

The Nigerian Central Switch (NCS) is still not operational, although one switch, eTranzact, has technologically interconnected. Reports indicate that the private switches are delaying interoperability until the operational guidelines of the NCS are clarified. Of particular concern is the fact that NIBSS, established in 1993 to settle interbank funds, also provides a number of payment services to Nigerian banks, including bulk payments such as salary disbursements and most recently, dividend payments. These payment products are seen as competing with the payment products of the private switches.

[42] CBN, Guidelines on Electronic Banking in Nigeria (2003), Section 1.4.7(d): "In order to promote interoperability, all licensed switch operators are encouraged to inter-connect to each other."

3.4.3 Automated Clearing House

The Automated Clearing House (ACH), owned and operated by NIBSS, facilitates the electronic clearing and settlement of local checks on a multilateral net basis, typically after physical exchange of items. Interbank settlement in the ACH currently occurs on t+1. Direct debit and credit transfers are also facilitated in the ACH. However, the World Bank FSS 2020 diagnostic study on payments notes that the existing rules do not adequately delineate the rights, responsibilities, and obligations of participants, including customers, in the use of these instruments. Relative to its peers of emerging nations, Nigeria's payments system is very paper-based. Checks are used for wholesale as well as retail payments and currently account for over 90 percent of non-cash payments. This becomes particularly significant given the high dishonored check ratios. According to NIBSS 13 percent of checks are returned unpaid, out of which 3 percent are returned for insufficient funds. The remainder are returned for technical reasons such as inadequate signature or illegibility.

3.4.4 Automated Teller Machines (ATMs)

For the first seven months of 2008, ATM transactions represented nearly 91 percent of the value of all electronic fund transfers in Nigeria.[43] CBN estimates that there are approximately 7,000 ATMs in the country, representing a low penetration rate of only one ATM per 20,000 individuals. Given low levels of inter-operability among payment providers, the situation is arguably even lower than these figures imply. In addition, the cost of ATM operation is relatively high due to (i) the need for frequent replenishment of the ATMs (given the limited capacity of the machines and the low value of the highest denomination note, NGN 1,000), (ii) the difficulty and cost of sourcing adequate quantities of ATM-fit notes and of monitoring machines for cash-outs and jams (occasioned by the poor note quality), (iii) the unreliability of electricity supply and the concomitant need to maintain alternate source of electricity at all ATMs, and (iv) the cost of physically securing both the ATMs and their generators or other sources of electricity.

3.4.5 Point-of-Sale (POS) Terminals

For the first seven months of 2008, POS transactions represented over 4 percent of the value of all electronic fund transfers in Nigeria. At the end of 2007, Nigeria had approximately 6,700 Point-of-Sale (POS) terminals.[44] The POS penetration rate represents a ratio of less than 50 POS terminals per 1 million inhabitants—an extremely low penetration rate compared to other countries in Africa: 130 POS terminals per 1 million inhabitants in Zimbabwe, 350 in Egypt, and 14,000 in South Africa.[45]

[43] CBN, Data on Electronic Payments Channels for 2008, received September 11, 2008.
[44] CBN, Banking Supervision Annual Report 2007, p. 43.
[45] Low inter-operability also affects the PoS network, as some merchants may be required to use several terminals.

Table 11 : POS Terminals Per 1 Million Inhabitants[46]

	Nigeria	Zimbabwe	Egypt	South Africa
Population (millions)	140	11.5	82	49
POS terminals	6,700	1,500	28,700	686,000
POS Terminals per 1 million inhabitants	48	130	350	14,000

Source: Adapted from the August 2008 draft of the World Bank's Diagnostic Report of the Payment and Settlement Systems and Reform Strategy in Nigeria.

3.4.6 Mobile Telephones. As of June 2008, Nigeria had four licensed mobile network operators (MTN, Glo, Zain (formerly Celtel), and Mobile Telecommunications Limited) with approximately 50 million mobile telephone subscriptions.[47] In addition, another four licensed CDMA mobile network operators (Starcomms, Visafone, Reltel and Multilinks) have approximately 4.8 million subscriptions. Although this number undoubtedly includes inactive mobile subscriptions, it nevertheless represents a penetration rate of approximately one mobile phone per three individuals—a much higher rate of penetration than ATMs or POS terminals and a testament to the potential of using mobile technology to provide financial access to a much larger segment of the Nigerian population than is currently being served. For the first seven months of 2008, mobile transactions represented approximately one tenth of one percent of the value of all electronic fund transfers. However, mobile funds transfers represented 7.5 percent of the total number of funds transfer transactions[48] (higher than both POS and internet transactions, which were 2.19 percent and 2.93 percent, respectively), indicating promising customer uptake although for small value transactions (Table 12).

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[46] Based on draft Diagnostic Report on the Payment and Settlement Systems and Reform Strategy in Nigeria (August 2008), World Bank.
[47] Nigerian Communications Commission, available at http://www.ncc.gov.ng/index5.htm

[48] Excluding intrabank funds transfers initiated by a bank and processed through the core settlement system.

Table 12: Steady Growth of Electronic Payments, January-July 2008

	ATM		POS		MOBILE		INTERNET		TOTAL	
Month	**Volume**	**Value (NGN thousands)**	**Volume**	**Value (NGN thousands)**	**Volume**	**Value (NGN thousands)**	**Volume**	**Value (NGN thousands)**	**Volume**	**Value (NGN thousands)**
January	2,269,974	18,783,085	71,779	1,267,008	140,602	18,059	105,970	876,820	2,588,325	20,944,972
February	2,348,427	18,483,863	78,997	1,053,841	185,730	19,576	112,610	1,160,949	2,725,764	20,718,229
March	3,144,468	25,325,868	89,221	1,016,360	156,983	17,662	113,207	1,330,789	3,503,879	27,690,679
April	3,279,834	25,701,652	91,800	1,207,012	247,252	32,846	115,669	1,454,528	3,734,555	28,396,038
May	3,613,079	28,308,899	93,648	1,188,933	392,274	31,548	116,428	1,440,947	4,215,429	30,970,327
June	4,299,160	26,714,093	109,931	1,035,924	453,366	45,062	121,023	1,365,604	4,983,480	29,160,683
July	5,881,896	36,530,727	86,521	1,243,148	556,083	63,244	146,629	1,570,106	6,671,129	39,407,225
Total	24,836,838	179,848,187	621,897	8,012,226	2,132,290	227,997	831,536	9,199,743	28,422,561	197,288,153
Percent	87.38	91.16	2.19	4.06	7.50	0.12	2.93	4.66	100	100

Source: CBN Banking Operations Department. Table excludes intrabank funds transfers initiated by a bank and processed through the core settlement system.

4. Legal and Regulatory Framework for Access to Finance

With a vision to become one of the world's largest twenty economies by the year 2020, the Nigerian government has implemented an ambitious process of financial and other reforms known as the Financial System Strategy 2020 (FSS 2020). FSS 2020 is discussed more in detail in section 5.1 on government interventions. A number of FSS 2020 components directly address access to finance regulation, including the promotion of an electronic payments system, and the enforcement of AML/CFT rules.

The supervisory function of the CBN is structured into two departments: Banking Supervision and Other Financial Institutions. The Banking Supervision Department carries out the supervision of banks and discount houses while the Other Financial Institutions Department supervises finance companies, MFBs and other non-bank financial institutions. The supervisory process involves both on-site and off-site arrangements. The directors of these departments report to the Deputy Governor, Financial Sector Surveillance.

4.1 Microfinance

4.1.1 Microfinance Regulatory Framework

In 2005, the CBN issued its Microfinance Policy, Regulatory and Supervisory Framework for Nigeria (hereafter, the Microfinance Framework). The Microfinance Framework presents the CBN's vision of a microfinance industry that serves multiple purposes:

- provide financial services to the poor
- mobilize savings for intermediation
- increase productivity and employment for the poor, and in general terms integrate the poor into the socioeconomic development process
- administrate and channel government microcredit programs
- render payment services for government agencies.

At the core of the Microfinance Framework are the CBN guidelines for the licensing of Microfinance Banks (MFBs). The CBN created the MFB licenses to encourage existing institutions and future investors to house their microfinance operations within a fully regulated and supervised non-bank financial institution. In addition to defining the legal, regulatory and supervisory guidelines for MFBs, the Microfinance Framework envisages the creation of industry support organizations, industry associations, a deposit insurance scheme, a liquidity facility, and state-funded wholesale programs.

In the Microfinance Framework, the CBN has created the MFB as a form of non-bank financial intermediary (NBFI) with a narrow scope of operations and prudential guidelines that address risks specific to microfinance institutions. In general, the regulatory and supervisory guidelines reflect a comprehensive and coherent set of regulations that is obviously informed by research into similar models that have been successful in other countries. Since the regulatory and supervisory guidelines are still largely untested in the Nigerian market, the following description is based on comparison of the policies to international standards of good practice. Observations about possible challenges that may arise in the Nigerian context are summarized in the issues section.

The MFBs have a mandate to provide deposit, credit and payments services. And the regulations allow individuals and corporations, both national and foreign, to own an MFB. This has made the MFB license an attractive option to a range of actors that aspire to offer financial services through an NBFI. As noted previously, the large NGOs and specialized microfinance investors intend to use the MFB license to create specialized MFIs. However, not all of the institutions with an MFB license necessarily have the capacity or intention to provide microfinance services. The history of the legacy community banks suggests that most of them do not, and little is known about the intentions of many of the new entrants. There is already a significant variety in the level of capacity and in the business plans of the institutions operating with an MFB license. Time will tell whether this diversity creates a healthy industry of financial innovation, or opportunities for arbitraging bank regulations with the less demanding MFB license.

The CBN guidelines for establishing a MFB provide two license options. Unit MFBs are licensed to operate within the local government area in which they are registered. The minimum capital requirement for a unit MFB is NGN 20 million (US$ 172,000). Unit MFBs may operate within their Local Government Area and expand subject to the NGN 20 million capital requirement per branch. State MFBs are licensed to operate in all parts of the state in which they are registered and are subject to a minimum capital requirement of NGN 1 billion (US$8.6 million). State MFBs can open branches anywhere in their registered state, but have to cover at least two-thirds of the state before applying for a license, and raise an additional NGN 20 million to open a branch in another state.[49] As of September 2008, almost all (98.9%) of the MFBs are classified as unit, with only nine classified as state MFBs.

The regulations also include prudential and non-prudential measures to manage risks typically associated with microfinance institutions with lower capital requirements. MFBs are not allowed to engage in complex financial services that have currency, counterparty, or political risks. For example, they may not engage in foreign exchange transactions or check clearing. MFBs are also prohibited from accepting public sector deposits, and this limitation is seen as a control on political interference and exposure to large depositors. There are exceptions, however, for channeling public credit funds, and this has significant potential risks that are discussed below in the issues section. Regulations regarding the qualifications of board of director members and management reflect clear expectations about good governance.

The prudential regulations provide specific guidelines in all important areas. Capital adequacy requirements are set under the assumption that most of the MFB loans will be unsecured and that capital is therefore a critical component of credit risk management. The capital adequacy ratio is set at a risk-rated 10:1 ratio and there are strict guidelines for establishing reserves and for dividend pay-out policies. Liquidity ratios also establish conservative parameters for liquidity management at 20 percent of deposit liabilities.

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[49] Central Bank of Nigeria, Micro Finance Policy, Regulatory and Supervisory Framework in Nigeria, 2005, p.16.

Risk concentration is controlled by a limit on individual loans to no greater than 1 percent of unimpaired shareholder funds (5 percent for a group borrower). Insider lending is strictly controlled with an aggregate limit of 5 percent.

The regulations also address risks specific to microfinance portfolios. Portfolio in arrears is clearly defined consistent with international practice. Provisioning requirements are specific and aggressive, requiring 100 percent loss provisions for loans over 90 days in arrears or restructured. The regulations contain a definition of "microloans" with a "maximum" loan size of NGN 500,000 (US$ 4,300), that are "typically" unsecured, and that have loan terms that are "ordinarily" 6 months. Although the status of this definition as a specific regulation is unclear, CBN officials explain that they require that at least 60 percent of MFB's portfolios be in loans that comply with the definition. Loans over NGN 50,000 (US$ 430) require collateral (although group or third party guarantees are sufficient collateral for microloans). The MFBs also have limits on the amount of resources they can invest in fixed assets or equities of other companies.

Since early 2008, depositors in MFBs are protected by the Nigerian Deposit Insurance Fund for amounts up to NGN 100,000 (US$ 862). MFBs pay a premium of 0.5 percent on deposits for this coverage.

4.1.2 Supervision of Microfinance

The Other Financial Institution Department (OFID) of the CBN is responsible for off and on-site supervision of the MFBs. OFID has 170 examiners and expects to be able to conduct on-site inspections on around 400 MFBs every year. OFID had completed 150 by the end of July 2008, with another 130 underway.

Offsite supervision is based largely on the monthly reports that MFBs are required to send to OFID. The monthly report formats consist of detailed financial statements and 24 supplementary schedules. The report formats are available on an Excel worksheet file and some MFBs are submitting reports electronically to OFID. However, most are preparing and submitting hardcopies of the monthly reports, although a significant number of MFBs are not reporting at all. The system is obviously cumbersome and overwhelming for OFID, given the large number of MFBs and the level of detail they are required to submit on the monthly reports. OFID aspires to move the industry towards a system of electronic filing,[50] but management acknowledges that many of the MFBs lack the basic information systems to prepare the reports or send them electronically.

OFID also plays a training role in the sector that is related to regulations that require MFB management to be certified in microfinance banking operations. OFID has launched a management training program and aspires to develop the initiative into an official certification program. Four training sessions in different parts of the country were underway at the time of the diagnostic in September 2008.

[50] OFID described the system as building on the EFAS system that CBN uses for commercial bank reporting. Such a system may need adaptations to handle hundreds of MFB reports, and many MFBs may not be capable of electronic filing in the short term.

The CBN expresses an intention to develop a risk-based supervision approach to the MFBs. The regulations outline a basic CAMEL rating model as an appraisal tool, and OFID staff stress the importance of assessing management capacity. Conspicuously absent, however, is a commitment to public disclosure of performance data. The CBN publishes sparse and only consolidated balance sheet data for MFBs in its annual supervision report. The CBN has expressed interest in encouraging MFBs to report to the MIX Market, and the MSME program supported by the IFC and World Bank is planning a seminar on financial reporting in mid-2009. The importance of making performance data readily available to the public cannot be overestimated in the Nigerian market, where investors, wholesale lenders, and industry analysts are likely to play an important role in enforcing performance expectations.

Text Box 2: Summary of Guiding Principles on Regulation and Supervision of Microfinance

- Prudential regulation and supervision are necessary for the microfinance industry to reach its full potential
- Supervisory capability, costs, and consequences should be examined earlier and more carefully than is sometimes the case in present regulatory discussions
- Minimum capital needs to be set high enough so that the supervisory authority is not overwhelmed by more new institutions than it can supervise effectively
- A microlending institution should not receive a license to take deposits until it has demonstrated that it can manage its lending profitably enough to cover all its costs, including the additional financial and administrative costs of mobilizing the deposits it proposes to collect.

Source: CGAP, Microfinance Consensus Guidelines: Guiding Principles on Regulation and Supervision of Microfinance, 2003.

4.1.3 Policy Making for the Microfinance Sector

The CBN divides responsibilities for the microfinance sector between OFID and the Development Finance Department (DFD). OFID is responsible for licensing, regulation, supervision, and ensuring compliance with regulatory guidelines for MFBs. DFD is responsible for capacity building for MFBs and their clients, development of the sector, policy formulation and implementation, sensitization, and functions related to non-licensed microfinance institutions.[51]

Within the CBN, the DFD plays a decidedly promotional role for the microfinance sector, whereas OFID is charged with keeping it orderly. Based on interviews and observations, these two interests may conflict in practice. The issues section below details potential risks associated with some of the regulations designed to promote the CBN's vision of the sector. The long term efficacy of the CBN as the regulator will have much to do with how well the CBN can reconcile the promotional and supervisory roles of its two departments.

[51] Roles of the two departments as noted in correspondence from DFD 24 December 2008.

For example, OFID staff is already aware that the majority of the unit MFBs are small and weak, and that they require enormous resources to supervise. Understandably, OFID staff talk frankly about a long term objective of capitalizing the sector by raising minimum capital requirements. In contrast, some DFD staff consider the current unit capital requirement too high because they have not seen the proliferation of rural institutions they expected. There are similar differences of opinion about the level of sophistication required in an MFB. At least one DFD representative voiced a preference for thousands of simple MFBs that reach rural populations by nurturing community-based self-help groups. This is difficult to reconcile with OFID's interest in MFBs having adequate management and information systems to make off and on-site supervision possible.

4.2 Interest Rate Policies

While interest rate efficiency and transparency are important policy objectives, interest rates in Nigeria compare favorably with other relevant countries as noted in Table 13.

Table 13: Cost of Debt: International Comparison

	Nigeria 2008	Brazil 2007	China 2007	India 2007	Indonesia 2007	Kenya 2006	South Africa 2007
Average annual interest rate	14	44	7	13	14	14	13
Real interest rate	6	38	2	8	2	4	5

Source: ICA Survey (2008); World Bank DDT Database.

Banks are required to display their lending and deposit interest rate at their offices.[52] Until December 11, 2006, the minimum rediscount rate (MRR) policy was in effect with respect to interest rates. Under the MRR, banks could receive liquidity credit from the CBN at a rate of 13 percent and were permitted to charge up to 400 basis points above the MRR in interest.

Effective December 11, 2006 the CBN implemented a new interest rate framework in which a monetary policy rate (MPR) was established which determined the lower and upper limits of the CBN lending rate and "is expected to have the capability of acting as the nominal anchor for other rates."[53] Because the MPR is based on economic indicators outside the control of the CBN, CBN officials often refer to interest rates as "free market" rates, implying that interest rates are freely negotiated in the market. There is no CBN indication of how commercial interest rate caps are to be calculated based on the MPR, although the MPR is routinely revised (most recently in September when it was reduced from 10.25 percent to 9.75 percent).[54]

CBN and bank sources state that, according to CBN circulars, the current cap on commercial interest rates based on the MPR is 19 percent (though banks may charge an additional 2 percent in fees). However, neither the CBN nor any bank was able to provide a copy of any CBN

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52 Banks and Other Financial Institutions Act, Section 23, CAP B3 LFN 2004.

53 Press release, CBN Communique No. 48 of the Monetary Policy Committee (November 28, 2006).

54 CBN Communique No. 58 of the Monetary Policy Committee (September 18, 2008).

circular setting forth such a cap. Current rates charged by banks, MFBs, SME finance providers and others range above 20-30 percent for loans, overdrafts, and other lending products. Overall, there is considerable confusion among financial service providers and policy makers as to the existence, calculation and enforcement of an interest rate cap.

4.3 Collateral Requirements

According to CBN regulations, every loan of over NGN 10 million (US$ 86,000) must be collateralized with land or buildings and smaller loans generally also require some form of collateral. Additionally, not all forms of collateral are equally accepted by banks, and their preference is determined by present and anticipated transaction costs in establishing and enforcing property rights, the ease of liquidation, and the position vis-à-vis other creditors in case of insolvency. This market preference for collateral based on "administrative issues" in addition to central bank regulations is limiting access to credit to SMEs, as explained in Sections 2 and 3. Furthermore the collateral regulation is probably imposing distortions in the flow of credit, as companies that lack acceptable collateral may seek financing in informal credit markets with less stringent collateral requirements but higher costs of lending. These issues are also discussed in Section 3 on Financial Infrastructure.

4.4 Insolvency and Creditor Rights

The ROSC regarding insolvency and creditor rights in Nigeria concludes that the insolvency and creditor rights regime is deficient in many aspects, and that there is an urgent need of reform in the areas of secured transactions and insolvency (Bankruptcy Act).[55]

4.5 Deposit Insurance

The Nigerian Deposit Insurance Corporation (NDIC), established pursuant to the 2006 Nigerian Deposit Insurance Corporation Act,[56] insures all deposit liabilities of licensed banks and other deposit taking financial institutions. Such insurance is required of all such institutions. Required premiums pursuant to the original act equaled 15/16 of 1 percent of deposits.

In January 2008, the NDIC moved to a "risk-based" premium based on perceived exposure to pay out. The premium for commercial banks (deposit accounts insured up to NGN 200,000 (US$ 1,720) is now anywhere from 23–44 percent less than the 15/16 of 1 percent of deposits provided under the original NDIC Act. Also in January 2008, the NDIC started requiring MFBs to pay premiums equal to half of 1 percent (deposit accounts insured up to NGN 100,000; US$ 862). MFBs pay slightly higher premiums than commercial banks based on the insured amount. This difference may be justified given perceived risks.

Although the NDIC has been criticized for duplicating supervisory efforts with the CBN, the NDIC insists that there is no duplication and that most NDIC supervisors originate from the supervisory branch of the CBN (and therefore use the same methodologies) and banks are

[55] World Bank Report on Observance of Standards and Codes: Nigeria, Insolvency and Creditor Rights, dated October 2007.
[56] Nigerian Deposit Insurance Act, 2006, (2006 Act, No. 16) repealing the Nigeria Deposit Insurance Act 1988

allocated to either the NDIC or the CBN for supervision on an annual basis so as to avoid duplicative efforts. Nevertheless, supervisory capacity is highly limited; the NDIC reports 43 examiners for 24 commercial banks but only 33 for approximately 700 Microfinance Banks.

4.6 AML/CFT Regulations

Nigeria is a member of the regional FATF-style body for Africa, the Inter-Governmental Anti-Money Laundering Group in Africa (GIABA). In June 2006, Nigeria was removed from the list of countries deemed to be non-cooperative in the international community's efforts to combat money laundering and the financing of terrorism.

The CBN is responsible for regulating AML/CFT procedures, however the Economic and Financial Crimes Commission is responsible for enforcement. The regulatory regime in Nigeria surrounding Anti-Money Laundering and Countering the Financing of Terrorism (AML/CFT) is currently the subject of a number of regulations which are not easily understood as a cohesive body. The primary regulation governing AML/CFT is the Money Laundering (Prohibition) Act (most recently amended in 2004). However, secondary documents governing AML/CFT include (i) the CBN's Know Your Customer Manual for Banks and Other Financial Institutions in Nigeria, (ii) the Advance Fee Fraud and Other Related Offences Act, (iii) the Guidelines on Electronic Banking in Nigeria, and (iv) a wide array of circulars and other documents issued by the CBN.

The Money Laundering (Prohibition) Act provides that a financial institution "shall verify its customer's identity and address" before opening an account or engaging any other business relationship.[57] It further provides that a customer must provide (i) proof of identity through an official document bearing name and photograph and (ii) proof of address through recent public utility receipts.[58] These provisions imply that non-face to face account opening and a risk-based approach to AML/CFT concerns are prohibited. In addition, the official document requirement could be too difficult to meet for many low-income individuals.

However, the Know Your Customer Manual (2003) appears to conflict with the Money Laundering (Prohibition) Act. On one hand, the KYC Manual is more permissive by expressly providing guidelines on non-face to face accounts[59] and permitting documents other than utility bills to prove address.[60] On the other hand, the KYC Manual is more restrictive, requiring (in addition to the requirements of the Money Laundering (Prohibition) Act) the collection of business information, such as the nature of the customer's business, purpose for opening the account, and sources of income.[61] However, the Guidelines on Electronic Banking in Nigeria provide yet another requirement, namely that "Banks are obliged not only to establish the identity of their customer (KYC principle) but also enquire about their integrity and reputation."[62] And lastly, a 2003 CBN Circular requires that the minimum account opening requirements for individuals include name, date of birth, office address and telephone, spousal

[57] Section 3(1)
[58] Section 3(2)
[59] Section 4.8
[60] Section 4.2.3(ii)
[61] Section 1.2.2
[62] Section 3.0

information, nature of business, references, passport photograph, and identification (proven through any one of eight specified documents).[63]

Driven by a desire to expand financial access through mobile technology, and in response to the expected growth in mobile payments, the CBN has drafted mobile payments guidelines. The mobile payments guidelines have yet to be released for comment. However, according to representatives of the CBN, the draft mobile payments guidelines provide for three levels of AML/CFT requirements based on transaction values:

Level 1 unbanked:	Self-declared name and telephone number permits up to NGN 3,000 (US$ 25) per transaction with a daily limit of NGN 30,000 (US$ 253).
Level 2 semi-banked:	Proof of address and verifiable ID card permits up to NGN 10,000 (US$ 84) per transaction with a daily limit of NGN 100,000 (US$ 844)
Level 3 fully banked:	Same as level 2 but with references and credit check. Permits up to NGN 100,000 per transaction with a daily limit of NGN 1 million (US$ 8,443)

The Money Laundering (Prohibition) Act makes no reference to the ability of applying a risk-based approach to AML/CFT procedures. However, the KYC Manual references a risk-based approach but still requires even for the most simple of accounts, verification of identity and address.[64] It is consequently unclear how to apply the risk-based approach, particularly in light of CBN's inclusion of three defined AML/CFT tiers in the draft Mobile Payments Guidelines.

Another discrepancy exists with respect to one-off transactions. The Money Laundering (Prohibition) Act does not require any AML/CFT procedures for one-off transactions below the equivalent of NGN 604,000 (US$ 5,000).[65] The KYC Manual requires verification of identity even for one-off transactions.[66]

The Advance Fee Fraud and Other Fraud Related Offences Act requires that mobile telephone companies obtain full names and residential addresses from each customer or subscriber. This requirement in practice is not observed and is not enforced, although the Nigerian Communications Commission believes this provision will be enforced more strenuously in the future.

4.7 Credit Registry Regulation

In October 2008, the CBN issued Guidelines for the Licensing, Operations and Regulation of Credit Bureaus in Nigeria ("Credit Bureau Guidelines"). The Credit Bureau Guidelines require CBN licensing for the operation of a credit bureau. Banks may only invest in a single credit bureau and the Credit Bureau Guidelines limit bank ownership to 10 percent of the credit

[63] CBN Circular (BSD/12/2003), August 11, 2003, Annex A.
[64] Sections 4.1.4 and 4.1.5.
[65] Section 3(5)
[66] Section 2.3.1

bureau's total paid-up capital.[67] A credit bureau is permitted to collect customer information related to determine such customer's "overall debt exposure and repayment behavior."[68] The ability to access credit bureau information is restricted only to lending entities or individuals and only for a "permissible purpose" such as to obtain credit scoring, obtain information on borrower's existing loan facilities or opening a new account as part of KYC principles. Banks must obtain credit reports from at least two credit bureaus before extending credit. With a number of private credit bureaus now being launched, this requirement should be feasible in the short- to medium-term. Under the new Guidelines, a consumer has the right to inspect (at a credit bureau) his or her credit information and to request an investigation of any information such consumer considers inaccurate.

4.8 Consumer Protection for Financial Services

The principal consumer protection body in Nigeria is the Consumer Protection Council (CPC) whose functions include "speedy redress" and awareness campaigns.[69] The CPC, whose definition of consumer extends only to individuals and not legal entities,[70] is largely product focused and does not expressly provide for the CPC's jurisdiction over financial services. Although the CBN could argue for a more direct consumer protection role with respect to financial services by invoking its general obligation to maintain adequate and reasonable financial services under the Central Bank Act (which also appoints the Governor of the CBN as the banking ombudsman), the CBN nevertheless has expressly recognized the Consumer Protection Commission Act's authority over the provision of financial services.[71]

However, in practice, protection of financial services consumers is rarely addressed by the CPC, which reports only 16 complaints related to "financial matters" from 2000–06 (inclusive).[72] Despite assertions by the CBN that the CPC has authority over financial matters, the CBN included data privacy provisions in the Guidelines on Electronic Banking in Nigeria[73] and in addition, publicly invites consumers to lodge complaints directly with the CBN Supervision Department regarding "disputes bordering on non compliance with credit/monetary guidelines or clear infringement of the banker's tariffs."[74] Banking authorities also mentioned that many departments within the CBN investigate consumer complaints and a number of such complaints are referred to the Ethics and Professionalism Subcommittee of the Bankers' Committee, a banking association comprising commercial banks and headed by the CBN, but with limited power to sanction banks.[75]

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[67] Guidelines for the Licensing, Operations and Regulation of Credit Bureaus in Nigeria, October 2008, Section 3.1(ii).
[68] Guidelines for the Licensing, Operations and Regulation of Credit Bureaus in Nigeria, October 2008, Section 5.2.
[69] Consumer Protection Council Act, Sections 2(a) and 2(e).
[70] Consumer Protection Council Act, Section 32, defines "consumer" as "an individual who purchases, uses, maintains or disposes of product or services".
[71] Guidelines on Electronic Banking in Nigeria, CBN, Section 3.0f.
[72] Statistics of Complaints Received by the Consumer Protection Council from 2000-2006, Digest of Statistics 2006, Federal Ministry of Commerce and Industry, p. 30. Press reports indicate that the CPC is largely ineffective with e-mail complaints bouncing back and a average processing time of 3 months.
[73] Sections 3.0c and 3.0d.
[74] CBN, Frequently Asked Questions, located at http://www.cenbank.org/FAQS/FAQ.asp
[75] Obajemu, Moses, "Bank-Customer Feud: How Far can ACAMB Go?," THISDAY, Volume 13, No. 4890, p. 43.

Perhaps due to concerns about the CPC's effectiveness,[76] the Nigerian Communication Commission (NCC) has challenged CPC dominance in the area of consumer protection by establishing its own consumer protection guidelines and dispute resolution mechanisms for the telecommunications sector.[77] The NCC Act empowers the NCC to prepare a consumer code of practice, which was completed in 2007. The code addresses a wide array of consumer protection matters including disclosure, billing, data privacy and consumer redress. The NCC defines "consumer" more broadly than the CPC to include legal entities.[78]

Decentralization of consumer protection appears to be a trend. The CBN reports not only that its draft Mobile Payments Guidelines envisions a consumer protection body dedicated to protecting consumers of mobile payment services but also that a member of the CPC served on the drafting committee which establishes this new consumer protection regime.

4.9 Taxation

Section 3 of the Value Added Tax Act (VAT) exempts the services of community banks from VAT. The same exemption is also found in the Federal Inland Revenue Services information circular dated January 1, 1999.[79] According to Nigerian counsel, the conversion of community banks to MFBs did not affect VAT policy, and MFBs enjoy VAT exemption on their services. Indeed, the microfinance bank guidelines expressly provide that the CBN shall "collaborate with the appropriate fiscal authorities in providing a favorable tax treatment of MFBs' financial transactions, such as exemption from VAT on lending, or tax on interest income or revenue. Similarly, the principle of exemption from profit tax shall be applied to any MFB that does not distribute its net surplus but ploughs it back and reinvests the surplus to finance more economically beneficial micro, small, and medium entrepreneurship." [80]

Commercial banks have no such exemptions, even with respect to microcredit services. Consequently, commercial banks will charge 5 percent VAT on their fees, making microloans offered by a commercial bank marginally more expensive than if the same loan were offered by an MFB.

The purchase of mobile phone airtime is subject to a 5 percent VAT. Although the amount of the VAT is low relative to many VAT rates around the world, it could significantly hinder the uptake of mobile payment services if "cash-in" transactions are taxed as airtime purchases. In other words, customers will be much less likely to use mobile payment services if the cash used to fund such payments is subject to a five percent levy. Consequently, any mobile payment regulatory framework should clarify that VAT and other taxes will not be levied against deposited funds.

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[76] Press reports indicate that the CPC is largely ineffective with e-mail complaints bouncing back and a average processing time of 3 months. Ayisha Osori, "What to do When you get a Raw Deal," THISDAY Lawyer, September 9, 2008, p.ix.
[77] Nigerian Communications Commission Act 2003, Sections 104–106.
[78] The Nigerian Communications Commission Competition Practices Regulation (2007) defines consumer as "any subscriber, customer or other consumer of communications services, whether an . . . individual corporation or other legal entity."
[79] Federal Inland Revenue Service Information Circular No. 9901 (January 1, 1999), paragraph 7 (ii)(b)
[80] CBN, Microfinance Policy, Regulatory and Supervisory Framework in Nigeria, Sections 12.1 and 12.2.

4.10 Foreign Exchange Policy

The Foreign Exchange (Monitoring & Miscellaneous Provisions) Act, 2004 ("Forex Act"), provides for the monitoring and supervision of foreign exchange transactions. The Nigerian Naira may be freely exchanged with foreign currencies provided that such transaction is properly documented and does not relate to illegal activities.[81] Foreign exchange dealers (bureaux de change) must be licensed by the CBN and demonstrate evidence of adequate resources and capacity to operate in accordance with the provisions of the Forex Act. Foreign exchange dealers must maintain exchange records for seven years[82] and report any cross border transactions by individuals in excess of NGN 604,000 (US$ 5,000) or its equivalent.[83]

4.11 Foreign Investment Policy

The Nigerian Investment Promotion Commission (NIPC), established by the Nigerian Investment Promotion Commission Act,[84] regulates foreign investment in Nigeria. The NIPC is empowered to adopt policies towards the enhancement of foreign investment in Nigeria and to propose policy, legal and regulatory reforms conducive to foreign investment.[85] Attracting foreign investment is a priority of the FSS 2020 effort, and the CBN reports that foreign direct investment in Nigeria more than doubled in 2006 with US$ 7 billion invested that year.

There is no prohibition on foreign banks operating in Nigeria, although, like Nigerian banks, they must obtain prior approval from the CBN.[86] Similarly, foreign communications service providers, like Nigerian providers, must obtain a license from the NCC in order to provide communications services in Nigeria.

The Nigerian Enterprises Promotion (Repeal) Decree No. 7 of 1995 has generally abolished any restrictions on foreign shareholding of Nigerian registered or domiciled enterprises. The only enterprises which are still exempted from free and unrestrained foreign participation are those involved in sectors included on the "negative list" which includes; (i) production of arms, ammunition, etc., (ii) production of and dealing in narcotic drugs and psychotropic substances, (iii) production of military and para-military wears and accoutrement, including those of the police and the customs, immigration and prison services, and; (iv) such other items as the Federal Executive Council may determine.[87]

4.12 Competition Policy

There is no official policy on competition or comprehensive legislation governing competition in Nigeria. However, there has been a draft Federal Competition Bill before the Nigerian National Assembly since 2002. The bill would establish a Federal Competition Commission.

The Central Bank Act empowers the CBN to issue guidelines and regulate the activities of the banking sector with the aim of establishing a sound financial system. Although power to

[81] Forex Act, Section 10
[82] Forex Act, Section 24
[83] Forex Act, Section 12(2)
[84] Decree No. 16 of 1995, now Cap N116, LFN 2004.
[85] www.nipc.gov.ng/about.html (last visited November 7, 2008)
[86] Banks and Other Financial Institutions Act, Section 8.
[87] NIPC Act 2004, Section 31

regulate competition is not expressly stated, it is widely accepted that such power does indeed lie with the CBN. In July 2004, the CBN Governor, Charles Soludo, expressed concern that the Nigerian banking sector was not competitive due to a number of factors including (i) low capital base leading to a number of small and noncompetitive entrants, (ii) dominance of a few banks, (iii) poor asset quality, and (iv) weak corporate governance.[88] As a result of the weakness of the sector, and as part of the FSS 2020 national strategy to strengthen the competitiveness of the Nigerian economy, the CBN raised the capitalization requirement for commercial banks to NGN 25 billion to be paid up by year-end 2005. The increase forced a consolidation of the banking sector as smaller, weaker banks were forced to merge with other banks or lose their banking license. The new policy contributed to a dramatic change in the banking sector from 89 banks with a capital base of less than NGN 362.4 billion (US$ 3 billion) to a stronger sector of 24 banks with a capital base of approximately NGN 1.09 trillion (US$ 9 billion).

With respect to the telecommunication sector, Section 90 of the National Communications Commission Act provides the NCC with exclusive competence to regulate and enforce competition within the communications market.

There are no reports of recent anti-competitive practices within the financial or telecommunications sectors. However, the question of competition may be hindering interoperability of retail payment systems (see Section on Financial Infrastructure and Recommendations).

[88]CBN Governor Professor Charles Chukwujma Soludo, "Consolidating the Nigerian Banking Industry to Meet the Development Challenges of the 21st Century." Speech delivered before the Special Meeting of the Bankers' Committee (July 6, 2004).

5. Review of Government Activities

5.1 FSS 2020 Strategy

In 2007, the Nigerian government introduced an ambitious process of financial and other reforms known as the Financial System Strategy 2020 (FSS 2020). FSS 2020 is part of a strategic planning process headed by the National Council on Vision 2020, itself chaired by the President of Nigeria. A number of FSS 2020 components directly address access to finance regulation, including the development of the MSME sector and promotion of an electronic payments system. The FSS 2020 also stresses the development of a risk-focused and rule-based financial regulatory regime, including the revision and update of current laws as well as the introduction of new laws.

A sub-committee is in the process of drafting implementation guidelines for strategies outlined in the FSS 2020 Credit Market and Small and Medium Enterprises sector reports. Although the implementation guidelines are still in draft form, they aim to include comprehensive outputs, actors responsible, and timelines for a number of initiatives that will promote access to finance. Such initiatives include:

- changes to the existing Nigerian legal framework, including the creation of specialized commercial courts
- credit infrastructure including credit reporting systems and collateral registry
- measures aimed at macroeconomic stability, including highly political issues such as discontinuing CBN financing of fiscal deficits without alternatives
- creation of a credit institute to train and certify financial institution credit officers and managers
- savings mobilization, including changes in the administration of pensions.

The proposed initiatives should have a positive impact on access to finance and especially SME credit markets. However, the scope of the proposed workplan is broad, and this raises the risk of accomplishing too little by trying to accomplish too much. Prioritizing the workplan and completing smaller, more specific interventions could pave the way for greater impact and additional reforms in the future.

5.2 Public Wholesale Funding for MFBs

As part of the Microfinance Policy Framework, the CBN in collaboration with the Bankers Committee has created the Micro Credit Fund (MCF) to partner with state governments to channel credit to the microenterprise sector. The MCF was launched with the resources remaining in the SMEEIS, which was funded by a levy on commercial bank profits as described in section 2.3.5. The CBN reports that the balance of those funds available to the MCF at the end of 2007 was around NGN 20 billion (US$ 172 million).

Specific lending policies for the MCF were not shared with the diagnostic team. Nevertheless, the intended scale of the operation is enough to warrant concern about the impact on the MFBs. Accounting for the state matching funds, the current balance of the MCF is already 80 percent of the total deposits in the MFBs at June 2008; the 2010 projections for the MCF are four times the amount of current deposits.

There are at least two adverse effects that can result from an initiative of this size. The first is a general disincentive for the MFBs to develop capacity for mobilizing savings. In itself, the MCF reflects an emphasis on credit that is pervasive in Nigerian policy discussions around access to finance. If large volumes of wholesale funds are made available to the MFBs, they will have less interest in providing savings services, and may become dependent on wholesale borrowing to fund growth.

The second adverse effect can already be observed in the various microfinance credit programs associated with the National Poverty Eradication Programme (NAPEP). NAPEP channels funds through the MFBs to local organizations and individuals. The MFB pays NAPEP 1 percent for the funds and is limited to a 400 basis point margin, charging the borrower 5 percent. The margin is insufficient to cover the MFB's operational costs. Repayment performance with loans associated with public funds in Nigeria is also very poor, which exposes the MFB to additional losses. Finally, the allocation of NAPEP funds, like most subsidized credit programs, is perceived to be politically motivated. To the extent that is the case, these transactions expose the MFB to political influences that can undermine independence and portfolio quality in the long run.

Text Box 3: Global Lessons from Apex (wholesale lending) Facilities[89]

- Apexes probably expand the supply of resources available for unlicensed microfinance institutions, at least in the short term.
- However, microfinance development in most countries is held back more by a shortage of strong microfinance institutions at the retail level than by a shortage of wholesale funding.
- Apexes have not been successful in building bridges between MFIs and commercial funding sources. Indeed, the incentive to seek commercial funds is weakened by the availability of easier funding from the apex.
- Apexes for unlicensed microfinance institutions (such as NGOs) are most likely to be useful when they are created in response to the existence of a critical mass of competent retail MFIs, as was the case with PKSF in Bangladesh.
- Planning documents for apexes typically overestimate the number of retail MFIs that will be strong enough to channel the apex's funds effectively.
- Donors and governments tend to create unrealistic disbursement pressure for apexes. It would usually be preferable for initial funding of an apex to be modest, with larger amounts added later in response to demonstrated demand and capacity.
- Political interference is a common problem in apexes, despite assurances to the contrary at the planning stage. The best protection will usually be to keep state participation in the governance of the apex to the minimum level possible.
- The most important function of apex management is probably the selection of MFIs to be funded. Because the number of qualified MFIs is usually limited, managers have trouble applying proper selection criteria when they are faced with political pressure or pressure to disburse large amounts quickly.
- In the apex's supervision of the MFIs it funds, focusing on institutional performance targets that are few in number, precisely defined, and seriously enforced is probably more effective than requiring massive reporting on detailed uses of funds.

[89] Summarized from "Apex Institutions in Microfinance." CGAP Occasional Paper 6, 2002.

5.3 Initiatives for SMEs

The National Economic Empowerment and Development Strategy (NEEDS) emphasized the importance of private sector led growth via the creation of an appropriate enabling environment, to support wealth creation and poverty reduction in the country. Despite surpassing its growth targets in the agricultural and manufacturing sectors, the program fell short on job creation, relying too heavily on trickle down effects. Its successor, NEEDS 2, (launched for 2008–11 by the current administration) attempts to address this issue by, among others, emphasizing the role of SMEs for poverty reduction, employment creation, and economic empowerment. Moreover, President Yar'Adua's Seven Point Agenda further stresses the need for wealth and employment creation via the industrialization of the country.

As noted earlier in Section 2, the SMEEIS Fund became operational in 2001; as of 31 December 2008, SMEEIS investments totaled NGN 28 billion (US$194.4 million[90]) in 333 companies out of a total NGN 42 billion (US$291.6 million[91]) in the fund. As described in section 2.3.5, the SMEEIS fund has now been transferred to the MicroCredit Fund.

6. Funder Initiatives

6.1 Microfinance

6.1.1 CGAP Funder Survey

In 2007, funders had total commitments of NGN 8.3 billion (US$ 69 million), covering 21 projects in Nigeria. Funding commitments in Nigeria represent approximately four percent of the total commitments from funders in sub-Saharan Africa. Projects supporting access to financial services in Nigeria represent three percent of projects on the continent.[92] The active funders in Nigeria that reported to the CGAP Funder Survey in 2007 are: DFID, the Dutch Platform, EC, FIRST, the Bill & Melinda Gates Foundation, GTZ, IFAD, IFC, USAID, the World Bank. For more detail on the survey, please see Annex 2.

6.1.2 Specific Funder Programs

A large number of funders are active in Nigeria, as summarized in the previous section. This section provides short profiles of the projects supported by the main donors and investors interviewed during the mission.

[90] Exchange rate as of 23 January 2009: N1=$144 (Central Bank of Nigeria).

[91] Exchange rate as of 23 January 2009: N1=$144 (Central Bank of Nigeria).

[92] This section covers only the activities of funders in Nigeria based on data from the comprehensive CGAP funder survey in sub-Saharan Africa for 2007. In order to better understand funder activity, in 2005 CGAP began surveying funders working in Africa on increasing access to finance. In 2007, 40 respondents provided self-reported information on their general projects, specific activities in each country, and funding.

EFInA

EFInA is the new national initiative to promote access to finance launched in 2008. EFInA is cofunded by the UK Department for International Development (DFID) and the Ford Foundation with a budget of £8.2 million over five years (2007-2011). EFInA's main areas of focus are: improving the level of market information available, strengthening capacity of regulators through policy research, and providing funding through grants to support innovative products for the poor. In October 2008, EFInA released the first FinScope report on demand for financial services in Nigeria, as noted in Section 1.

Ford Foundation

Among development partners active in Nigeria, Ford Foundation is the earliest and one of the most active in supporting access to finance since the 1970s. Over the years, examples of Ford Foundation support to the sector includes the launch of several NGO MFIs, the first ratings of MFIs in Nigeria, technical assistance to the CBN on microfinance issues, and capacity building for MFIs such as COWAN, FADU, LAPO and DEC-Bauchi. Ford Foundation's current funding is focused on the EFInA Initiative that is cofunded with DFID.

The World Bank Group including IFC

The Micro, Small, and Medium Enterprise (MSME) Project is a pilot project of the Federal Government of Nigeria, aimed at increasing employment and production in selected non oil sectors of the Nigerian economy with a focus on the pilot states of Abia, Kaduna and Lagos. The MSME project is funded by the Government of Nigeria together with the World Bank and IFC. Initially designed as a five year project (from July 2004), the project has been extended through 2010. The project currently has five components:

- Access to Finance: Supporting the development of a new commercial microfinance industry in Nigeria. The project has given performance grants to eight new MFBs. The grantees serve 100,000 clients with over US$ 12 million of credit.
- Business Development Services: Providing 59 matching performance grants to BDS providers (for roughly NGN 362.4 million; US$ 3 million) to support innovative, strategic, commercially oriented business development services in the three target states. So far an estimated 5,600 MSMEs have been served.
- Investment Climate: Developing a common set of forms and procedures for the CAC and the Federal Internal Revenue Service (FIRS) and a system linking their computers.
- Regulations: Assisting the CBN with developing the legal and regulatory framework for private sector credit bureaus
- Dispute resolution: Promoting alternative dispute resolution.
- A final sub-component to promote secured lending using movables collateral and leasing is being prepared.

The Access to Finance component had disbursed performance grants totaling US$ 8.4 million (NGN 1 billion) to eight MFBs by August 2008. The program is also planning technical assistance to CBN to develop policies and regulations related to MFB supervision, mobile-phone banking, and credit registries.

In addition to the MSME project, the World Bank has supported the FADAMA project phases one and two. FADAMA provides community grants for rural development, asset accumulation and capacity building. The third phase of FADAMA is currently being designed and will include a savings requirement linked to a community bank account for associations that participate in the program.

IFC

IFC's first equity investment in the Nigerian microfinance industry is a partnership with Accion Microfinance Bank, a greenfield project and new entrant to the MFB sector; IFC is providing equity and technical assistance funding to this start up initiative. IFC recently made a second equity investment and is providing technical assistance with another international partner to launch a greenfield MFB called Access Microfinance Bank. In addition, IFC has investments of US$ 90million in credit lines plus additional technical assistance to Diamond Bank to support the growth of its MSME operations.

UNDP/UNCDF

UNDP has supported the microfinance sector in Nigeria for several years through the MicroStart project that provided capacity building for MFIs. Since 2005, UNDP provides funding for follow up activities to the MicroStart program on policy advocacy with the CBN and capacity building of three microfinance institutions: LAPO, DEC and JDPC (now called CGEE). Going forward, UNDP and UNCDF are planning a private sector development project to focus on small scale agricultural producers in 4–10 states. As part of this project, support may be provided for rural finance through MFBs, cooperatives, banks and supply chain finance. In addition, UNDP and UNCDF are in discussions with the government to support an update to the National Microfinance Strategy that would build on the Microfinance Framework of 2005 and the FSS 2020 Strategy of 2007.

USAID

USAID's support includes several initiatives linked to access to finance. The PRISMS/MARKETS projects supported the microfinance industry at the retail and regulatory level. In 2005, the project assisted LAPO in developing a business plan and then seeking funding with a local commercial bank, backed by a Grameen Foundation guarantee. The PRISMS project supported the Microfinance Strategy Committee of the CBN during the development of the Microfinance Framework. The project also developed the training modules that have been adopted by the CBN/OFID for its training and certification program. The MARKETS project provides training to farmers on income management and business records to help make them more 'investment ready' when approaching banks. The project also links farmers to local and international buyers for their crops and promotes mechanized farming. USAID/Washington is also providing technical assistance to CBN on bank and MFB reporting guidelines. In addition, the USAID West Africa Trade Hub provides policy advisory services to the CBN, banks, and other actors in bank downscaling, new product development, and initial analysis of payments issues.

GTZ

As part of the Employment Oriented Private Sector Development Program, GTZ launched a microfinance and SME finance component in 2008. This component will provide capacity building for up to 13 MFBs in the states of Niger and Nasarawa. In addition, GTZ and CBN are discussing a possible certification program for MFBs. The program has fielded a resident technical assistant e provider that will support the six MFBs that qualify for the program.

DFID
As noted above, DFID designed the EFInA initiative and provides co-funding with the Ford Foundation. In addition, DFID funds the IMF to provide resident technical advisors to the CBN on monetary policy and banking supervision.

International Fund for Agricultural Development (IFAD)
IFAD's program in Nigeria focuses on rural finance, agricultural production, and infrastructure. Projects include the Microenterprise Development Project with the Ministry of Agriculture, the Rural Enterprise Project with SMEDAN, and the newly approved Rural Finance Institution Building Program (RUFIN) with the Ministry of Finance. RUFIN will provide capacity building for MFBs, capacity building for non-bank MFIs (especially NGOs), support for NACRDB, and implementation and technical assistance support to CBN on regulation and supervision of MFBs.

6.2 SME Finance

Few donors are active in SME finance, and the most important actors are the World Bank, the IFC, and USAID.

World Bank Group
In addition to the MSME Project, mentioned above, the World Bank is supporting the Commercial Agricultural Project, which includes matching grants for SMEs and other client groups. The IFC also supports several other initiatives with a resident technical advisor already working with Diamond Bank and a new program to launch soon with Ecobank.

USAID
In the past, USAID supported SME development through the PRISMS project, and relevant SME finance has transitioned to the MARKETS project as described above. As of July 2008, USAID is working with the African Development Bank in providing joint guarantees bank lending. Ecobank is the first institution to sign up for the program that covers four countries including Nigeria.

7. Conclusions and Recommendations

The following conclusions and recommendations are organized in the following categories: microfinance, branchless banking, SME finance, and cross-cutting issues. The recommendations are provided as short-term, medium-term, or long-term interventions. To be clear, all of these recommendations deserve immediate attention and policy decision; however, the designation of medium or longer term signals that the implementation of policy decisions will be a longer sustained effort.

7.1 Microfinance Conclusions

The Microfinance Framework is a coherent strategy for regulating and supervising the Nigerian microfinance industry. Moreover, many of the framework components have been designed after careful study of the microfinance sectors of other countries that are often held up as models of good practice. At the same time, the Microfinance Framework creates conditions that have potential to undermine the performance of the sector.

- **Low unit MFB capital requirements have permitted a large number of undercapitalized and weak institutions.** As of September 2008, almost all (98.9%) of the MFBs are classified as having a unit MFB license. The minimum capital for a unit MFB is NGN 20 million (US$ 172,000). This is not a sufficient amount of capital to launch or operate a deposit-taking institution in Nigeria, certainly not one with the level of governance, management capacity, and operating systems required by the regulations. The level was set to accommodate the transformation of the majority of the community banks and consequently, the initial MFB sector is populated with many institutions with a history of poor performance. Equally important, low capital requirements have permitted new entrants to be licensed without the resources necessary to conduct operations in such a way as to eventually become profitable and self-sustaining. As a result, the CBN is overwhelmed by many weak institutions at a critical time when they need to ensure orderly development of the sector, particularly for the largest institutions.
- **High state MFB capital requirements create incentives for explosive growth.** While minimum capital for unit MFBs may be too low, the minimum capital for state MFBs may be too high. An initial capitalization of NGN 1 billion (US$ 8.7 million) for a state license requires rapid growth to reach profitable levels of leverage. A state MFB will have to grow assets to NGN 10 billion (US$ 87 million) to fully leverage the minimum capital amount with a 10:1 capital asset ratio. MFBs that cannot grow to that size will be underleveraged and inclined to charge higher interest rates to generate acceptable returns on equity. As of September 2008, only nine MFBs had received a state license. MFIs that have achieved national scale in comparable markets like Peru or Uganda did so gradually by launching with capital levels of less than US$ 500,000 (NGN 60.4 million) and growing at a controlled pace. For example, Peruvian MFIs like Edyficar or Confianza[93] initially entered the regulated system as smaller institutions with a minimum capital of US$ 225,000 (NGN 27.2 million) and have subsequently relicensed as finance companies, subject to a minimum capital

[93] As of 2007, Edyficar manages US$ 150 million (NGN 18.1 billion) in assets, and Confianza manages US$ 77 million (NGN 9.3 billion) in assets.

requirement of US$ 2.5 million (NGN 302 million). Similarly, Ugandan MFIs first entered the regulated market after 2003 with a minimum capital requirement of US$ 290,000 (NGN 35 million) for a national license.

- **MFB capacity to manage growth is limited**. Nigeria's microfinance sector is experiencing explosive growth with new greenfield institutions and significant volumes of deposits and loans under management. Yet many institutions interviewed identified capacity building needs for their own management and operations. This is consistent with observations made by donors and investors and the mission's own findings during interviews with NGOs, MFBs and banks.
- **The lack of readily accessible market and financial institution performance data undermines the decision-making of all of the stakeholders in the microfinance industry: policy makers, the regulator, investors, managers, and the public.** The lack of basic information about the performance of the different non-bank financial service providers is dire in Nigeria. Reliable and accessible performance information informs the decisions of all stakeholders, from policy makers to investors to clients, of a financial market. This information is, in any practical sense, almost wholly absent in Nigeria.
- **The geographic restrictions associated with the unit and state licenses have concentrated the most aggressive MFBs in urban areas, and will limit the growth opportunities of both small and large MFBs as the sector develops.** In practical terms, the regulations confine the initial growth options of new entrants to their original local government area or state. Understandably, new investors selected heavily populated areas. But as a result, 57 percent of the newly licensed MFBs are domiciled and will operate in Lagos state; another 9 percent are in Abuja FCT. This can encourage unhealthy competition for the same clients, fueled by the aforementioned incentives for rapid growth. Similarly, unit MFBs in isolated areas will not be able to expand geographically if local demand is not robust enough to support a sustainable scale of operations.
- **The geographic restrictions may also impede beneficial specialization, consolidations and mergers.** As currently written, the geographic restrictions will also limit options for growth through product specialization or mergers. The most successful NGOs provide evidence for these concerns; the past growth of successful NGOs like LAPO that cover a large geographic area with a specialized financial product can no longer be recreated under either of the two unit or state licenses.[94] The geographic restrictions may also complicate the merger of MFBs whose combined operations would extend beyond a single jurisdiction. The regulations are not clear about the minimum capital requirements of a merger, or whether it will even be possible for MFBs in different jurisdictions. This is particularly important because mergers may well be necessary for the small MFBs to reach sustainable economies of scale.

[94] The CBN has indicated its intentions to accommodate the structure of existing NGOs under the new MFB license.

Text Box 4: ARB Bank in Ghana: Strengthening and expanding unit rural banks

- Bank of Ghana launched the idea of rural banking in the 1970s to create a separate category of banking institutions to serve the special needs of the rural population in Ghana.
- Practical experience with unit banks led the BoG to promote the creation of an Association of Rural Banks in the 1990s which developed into the Apex Rural Bank, or ARB Apex Bank Ltd.
- The Apex Bank provides each unit rural bank with oversight, liquidity management, internal controls, training, and standards of operation.
- Over 125 rural banks in Ghana's ten regions are currently linked to the ARB Apex Bank.
- Consolidation of the rural banking sector has enabled ARB strengthen the unit rural banks operations and expand outreach in rural areas. ARB provides each unit rural bank with oversight, liquidity management, internal controls, training, and standards of operation.
- Supervision by the BoG is simplified with ARB Apex Bank as the first line of supervision and control.

Source: ARB Apex Bank website available at http://www.arbapexbank.com/

- **Subsidized funding schemes will compromise the integrity and viability of the MFBs.** The Microfinance Framework expresses an assertive public sector interest in promoting the MFB sector with wholesale funding facilities. In addition to the federal level Microfinance Fund, the framework sets a target of two-thirds of state and local governments developing funding facilities for the MFBs. This kind of decentralized public sector support can easily evolve into a fragmented and politicized wholesale funding market that undermines the commercial discipline of the retail institutions.[95] Some of these tendencies are already evident in Nigeria. Some local governments have provided funds to help the legacy community banks meet the MFB capital requirements. The NAPEP wholesale funding program that limits MFB margins to less than their operating costs is unprofitable for MFBs. Moreover, repayment performance in publicly funded credit schemes is historically poor in Nigeria and this can easily create expectations in clients that they do not need to pay back MFB loans.

The aforementioned conditions are particularly significant because they are associated with the deliberate policy objectives, implicit and explicit, of the Microfinance Framework. The distinction between the unit and state license, as well as the regulations that govern their expansion, represent the CBN's deliberate "organic growth path" strategy to "promote an even spread of microfinance banks, their branches and activities, to serve the un-served but economically active clients in the rural and peri-urban areas."[96] The low minimum capital for unit MFBs was part political accommodation to the legacy community banks and part of the CBN's real interest in developing many MFBs in remote areas. And the Microfinance Fund, NAPEP, and similar subsidy schemes, are a reflection of interest in making public funds available via credit to disadvantaged populations. Though the policy objectives are well

[95] This effect was well documented, for example, in the case of Nicaragua by the CGAP CLEAR report on that country in 2006. More relevant to Nigeria is the experience of the Cajas de Crédito in Mexico.
[96] Micro Finance Policy, Regulatory and Supervisory Framework in Nigeria, Central Bank of Nigeria, 2005. P. 16.

intentioned, any of these conditions can undermine the development of a commercially healthy MFB sector, and ultimately sustainable access to finance.

7.2 Microfinance Recommendations

7.2.1 MFB Regulations

The CBN is encouraged to consider the following key issues as it adapts the MFB regulations to evolving market conditions:

- **Raise the minimum capital requirement for unit MFBs (timeframe: short-term).** The minimum capital requirement for unit MFBs is currently too low support sound and efficient microfinance institutions. Specifically, the minimum capital is insufficient to pay for the infrastructure and start up costs, with enough capital remaining to maintain capital adequacy levels as the institution grows by mobilizing savings. The minimum should be based on a calculation of how much capital is required to carry an MFB from initial investment through to profitability. The benchmark for that calculation should be based on the experience of successful MFBs in the market that comply with regulatory expectations regarding reporting capacity, governance, management, and operational systems. The capital requirement can be raised either by regulatory change or more simply by requiring new and existing MFBs to invest a capital amount that is consistent with their financial projections and business plan. The CBN can assess business plans to ensure adequate investment and insist on appropriate levels of capitalization. At the same time, capital requirements for branch expansion should be based on the MFB's overall business plan and financial projections as opposed to a fixed amount.
- **Allow acquisitions and mergers without geographic restrictions (timeframe: medium term).** Mergers and acquisitions can help successful MFBs expand their operations to underserved populations while salvaging weak MFBs that are struggling to operate on their own. However, the geographic restrictions on the unit and state licenses need to be removed or modified in the CBN microfinance guidelines to allow these partnerships to occur naturally between complementary business models and markets, as opposed to political boundaries. Overall, the goal should be to encourage existing MFBs to grow and develop their branch network, rather than creating multiple small "unit" institutions.
- **Ease geographic restrictions on MFB expansion (timeframe: short-term).** Easing geographic restrictions in the CBN microfinance guidelines will ease pressure where MFBs are currently concentrated and allow MFBs to grow, and capitalize, where market opportunities exist.
- **Promote capacity building initiatives aligned with MFB needs, CBN requirements, and funder programs (timeframe: short- and medium-term).** Given explosive growth, the MFBs and other institutions face ever more acute needs for capacity building. CBN and several funders have designed training and technical assistance programs, and a coordinated approach focusing on priority areas should be developed with the MFBs/NGOs, technical assistance providers, and funders. Training and technical assistance needs should be analyzed carefully with the MFBs and other financial institutions taking a lead. Funders may be willing to support capacity

building, although this should be closely coordinated to avoid redundancy and promote aid effectiveness.

7.2.2 MFB Supervision

The CBN is encouraged to consider the following key issues related to MFB supervision:

- **Publish historic financial statements, financial and outreach performance data and interest rates of all MFBs on the CBN website (timeframe: immediate).** This will enable clients, managers, investors, and wholesale lenders to exert their expectations about performance in the market. Equally important, policy makers will be better informed about the performance of the market.
- **Prioritize supervision efforts on the largest MFBs (timeframe: immediate).** This may be accomplished with a multi-tiered approach to supervision that applies different levels of supervision according to the size of the MFB. It is equally important to inform the public of the supervisory status of each MFB, because this adds additional incentive for MFBs to evolve to the highest category.
- **Develop off and on-site supervision tools and training programs (timeframe: immediate).** The CBN is encouraged to borrow and adapt techniques that have been successful in other jurisdictions. This will likely be an ongoing effort as the sector develops. Given the large number of MFBs subject to CBN supervision, priority should be given to developing off-site monitoring capacity. The CBN needs to be able to generate reports on individual MFBs that show the evolution of key performance indicators over time and against peer averages. The reporting system should also have an automatic early-warning feature so that individual cases are flagged on a monthly basis if performance benchmarks are not met. The CBN will also have to insist that MFBs submit their monthly reports in a standardized electronic format. Off-site supervision officers will need training in the new monitoring system. In broader scope, the CBN will likely benefit from ongoing development of supervision capacity in the following areas:

    - On-site inspections techniques
    - Management of on-site inspections, including correspondence and meetings with the board of directors and management, formulation of recommendations, and follow up.
    - CBN mandates regarding MFB external audits, including drafting of core terms of reference for audits and sanctions against auditing firms that fail in compliance or performance.
    - An on-going OFID staff training and development program.

Text Box 5: The Banking Superintendent in Peru:
A Case Study in Capacity Building

In the late 1990's, the Banking Superintendent of Peru collaborated with the Federal Reserve of the US and the Universidad del Pacífico of Lima to develop an ongoing training course for bank examiners. The Federal Reserve provided initial training to Pacífico staff, and the university then developed an extensive program that provides the basic training to aspiring applicants to the banking superintendent. This partnership has linked the Peruvian banking superintendent with technical partners in the Federal Reserve and in academia, enabling the superintendent to govern the development of one of the most advance microfinance industries in the world.

7.2.3 Align all MFB wholesale lending programs with a market-based model (timeframe: immediate). On an operational level, the most important components of this model are pricing and eligibility requirements. Refinancing rates should be market-referenced so that wholesale funding does not provide disincentives to mobilizing savings. Rates should be risk-based so that MFB borrowing amounts and pricing is based on their financial strength. Eligibility requirements should require compliance with robust financial performance benchmarks and limit borrowing to prudent amounts relative to assets. These measures will reinforce incentives for good financial performance generally. As part of this recommendation, it will be important to coordinate approaches for wholesale lending from Federal Government, State Governments, and Funder programs. Within the context of FSS 2020 and a revived funder coordination group, the CBN and funders should develop general guidelines for wholesale facilities that would build on international good practices.

Most countries have been able to maintain discipline in wholesale funding markets by centralizing public sector funds in a national level facility. In contrast, markets with regional development banks or fragmented public sector programs struggle to maintain consistent performance incentives. Consideration should be given to consolidating the various wholesale lending programs under a unified approach and/or management structure.

7.2.4 Promote the development of a single MFB industry association (timeframe: medium term). A strong industry association can facilitate orderly dialogue between the MFB sector and the monetary authorities and assist with dissemination of market information.

7.3 Branchless Banking Conclusions

- **Based on discussions with members of the mobile payments guidelines drafting team, there is good reason to be optimistic that the mobile payments guidelines, when released for comment, will be a thorough and well conceived effort**. Although a draft of the mobile payments guidelines was not made available, discussions with members of CBN's Banking Operations Department indicate that there is a well developed understanding of the many legal domains implicated by a comprehensive branchless banking regulatory regime. Members of the mobile payments guidelines drafting team assert that the mobile payments guidelines will address the often complicated issues presented by the use of agents, AML/CFT requirements, and consumer protections although no specific measures were provided for the mission to review. A key issue will be the guideline's treatment of systemic risks associated with non-bank led branchless banking models.

- **Still, given that effective branchless banking requires the cooperation of parties outside the control of the CBN, such as telecommunications service providers and consumer protection agencies, it is unclear how effective the mobile payments guidelines will be in practice**. In addition, even parties under CBN supervision, such as private switch operators, appear to be resistant to CBN efforts at promoting interoperability, a primary component of expanding access to finance.

7.4 Branchless Banking Recommendations

The CBN is encouraged to consider the following key issues related to branchless banking:

7.4.1 Promote interoperability of the retail payment system (timeframe: short-term). To achieve interoperability as rapidly as possible, the CBN should clearly define the role of the NCS and in particular whether it will be permitted to compete with private switches in the payments products sector. Attention should be given to ensuring that the NCS will not have an unfair competitive advantage in terms of product pricing, interchange fees or access to financial regulators. Operational guidelines should be drafted in such a way as to give comfort to private switch operators that the NCS (given its existing infrastructure and partial government ownership) will not have any competitive advantage in the payments arena. Interoperability will promote greater competition within the switching sector by removing infrastructural advantages currently hindering growth of smaller switches and discouraging new entrants. As interoperability encourages new participants in the payment services market, more access points and ultimately more affordable pricing and greater use of payment services is expected.

7.4.2 Ensure that mobile payments guidelines address key issues (timeframe: short-term). Branchless banking regulations from other jurisdictions could serve as useful models in finalizing Nigeria's mobile payments guidelines. A number of countries around the world have already implemented branchless banking regulation with varying degrees of success. Of particular note are Brazilian regulations with respect to the use of financial services agents and Filipino legislation with respect to nonbank-led models of mobile banking. In particular, it will be important for the Nigerian mobile payments guidelines to include clear guidelines on the following:

- *Use of agents and/or third party service providers, including qualifications and liability*. Mobile payment models often include the use of retail and other agents as "cash-in, cash-out" points of service. Under common law principles of agency, financial institutions in Nigeria routinely outsource provision of services to a wide array of third parties. However, the 2003 Guidelines on Electronic Banking in Nigeria impose obligations on banks with respect to using third parties for electronic banking services.[97] Such obligations include (i) due diligence in evaluating third party reputation, financial status and viability, (ii) monitoring third party performance, and reporting to government authorities of the existence of any such

[97] CBN, Guidelines on Electronic Banking in Nigeria (2003), Section 1.6.

outsourcing/agency relationship. The mobile payments guidelines should set forth the extent of the applicability of the Guidelines on Electronic Banking to agents involved in mobile banking and should further clarify related provisions, such as what kind of individual or legal entity may provide mobile services on behalf of a bank and eligibility requirements (such as literacy, cash handling experience, lack of criminal record, minimum age, etc.) to which such entities are subject. In addition, the mobile payments guidelines should clearly indicate the extent of bank liability to end users for actions taken by agents and third party service providers.

- *Managing the prudential risks involved in nonbank-led models of mobile banking*. Representatives of the CBN have explained that the mobile payments guidelines will permit nonbank-based models of mobile banking in which customers have no direct contractual relationship with a fully prudentially licensed and supervised financial institution.[98] Instead, the customer typically exchanges cash via an agent in return for an electronic record of value. This virtual account is stored on the server of a nonbank, such as a mobile operator, and the balance in the account can be used for making payments, storing funds for future use, transferring funds or converting back to cash. Because such accounts may be used as substitute bank accounts, the mobile payments guidelines must clearly address how the potential prudential risks of nonbank-based models will be managed. The mobile payments guidelines should address (i) the applicability (or lack thereof) of federal deposit insurance to monies deposited with non-prudentially regulated institutions, (ii) whether such deposits will earn interest, (iii) whether such deposits can be intermediated,[99] (iv) whether such deposits will be isolated from the nonbank's creditors, and (v) whether there is a cap on the amount permitted to be deposited or the length of time such monies may stay in electronic form.

7.4.3 Ensure that the mobile payments guidelines addresses consumer protection challenges unique to mobile banking (timeframe: short term). The CBN indicates that the mobile payments guidelines provides for consumer protections specific to the mobile payments sector. Such provisions should address the new consumer protection challenges unique to mobile banking, including:

- Whether mandatory disclosures may be provided via a subscriber's mobile phone
- How long will a sender be required to wait for an electronic confirmation message before assuming a failed transaction and the ability to resend without fear of double payment
- How a customer would prove transactions if a lost phone means a lost SMS record
- The customer duty of due care and negligence
- How to resolve a case of mistaken recipient identity (this can be highly problematic if all that is needed to effect a payment is the recipient's phone number since, unlike lengthy and unrelated bank account numbers, phone numbers can often be only one digit away from that of a different person)

[98] The inclusion of nonbank-led models of branchless banking represents a shift from the Guidelines on Electronic Banking in Nigeria (2003), which permits only "authorized financial institutions" to undertake electronic funds transfer services (Section 1.4.10) and requires all deposits to be subject to reserve requirements (Section 2.0).
[99] Drafters of the mobile payments guidelines should be aware of a possible conflict with Section 2.0b of the Guidelines on Electronic Banking in Nigeria requiring all categories of electronic money to be treated as part of deposit liabilities and subject to reserve requirements.

- How to protect data privacy, particularly if such data are transferred overseas as part of the authorization process
- Whether (and which) computer generated documents (such as SMS transaction logs) will be admitted as evidence in a Nigerian court of law[100]
- What records will financial institutions, agents, and mobile network operators be obligated to maintain; for how long, and in what form
- Whether direct marketing to the customer's phone (including SMS spam) will be permitted and if so by whom (just the financial institution or third parties); charges, if any, to the customer for such SMS
- Whether agents be required to provide written receipts for transactions.

7.5 SME Finance Conclusions

Despite a dynamic SME sector, there are several inhibitors to SME finance, as follows:

- **Policy making for the sector is severely constrained by the lack of data**. Beyond the World Bank's ICA survey, relevant agencies (including the CBN, SMEDAN, and Ministry of Industry) do not collect systematic data on the sector. In order to adequately set policy and to have a baseline against which results can be compared, data needs to be collected and made available to relevant policy making agencies, private sector, industry associations, and the broad public.
- **Regulations require loans to be collateralized while limiting the types of acceptable collateral**. At the same time the laws and registries on collateral (especially for movables such as equipment) need to be updated to promote their use in raising capital.
    - Asset-based lending based on movable business assets as security has not yet developed in Nigeria.
    - While there is a workable system of registering floating claims on the assets of companies at the CAC, the registry does not identify individual assets, and only incorporated business can make use of the registry.
    - CBN regulations and banks prefer real estate as collateral. Even when an SME or its owners are able to present real estate collateral, the cost of registering such collateral is so prohibitive that, if registered, loans would be priced out of range. Consequently mortgages are rarely registered (until required prior to a judicial process), thus severely limiting the effectiveness of the mortgage registry
- **A well-functioning and competitive credit information system that incorporates positive and negative information and covers all sectors of the economy (not just financial institutions) is imperative for credit to continue to develop in Nigeria.** Without access to reliable information on the financial condition of a debtor, and his willingness to pay as evidenced by historical payment patterns, creditors tend to limit the amount of credit by relying only on the value of security (collateral) available. With the approval of well-designed regulations for the operation of private credit bureaus, within months Nigeria could have private credit bureaus functioning alongside the CRMS and complementing it. By

[100] The Guidelines on Electronic Banking in Nigeria expressly warn that "Digital signatures should not be relied on solely as evidence in e-banking transactions, as there is presently no legislation on electronic banking in Nigeria." (Section 3.0b). In addition, the 2001 Court of Appeal decision in Nuba Commercial Farms Limited v. NAL Merchant Bank Limited and Another (16 NWLR, Part 740 at page 510) held that a lower court was wrong in admitting a computer print out as secondary evidence of manual entries in a banker's ledger.

starting with access to the historical CRMS database, the industry could concentrate on adding information and data subjects. By using a common (probably biometric) identity mechanism, the private bureaus could contribute to solving the identity problems of individuals and owners of firms.

- **Expanding use of credit cards could allow SMEs to sell more and take advantage of credit card receivables financing**. Checks are often used as security in supplier credit, but they are not widely used in Nigeria given their poor reputation and lack of enforcement of the Dishonored Checks Act. Checks plus credit, payment and debit cards are a tiny component (although rapidly growing) of the payments system in Nigeria. If use of credit cards were expanded, SMEs could sell more and take advantage of credit card receivables financing. Clearly other underlying issues still need to be solved in the payment system before credit card usage can be increased, as noted in section 7.2.
- **With notable exceptions, there are few appropriate SME finance products**. Banks and other authorities tend to treat SMEs as "small corporate clients" with no clear understating that SMEs need specific product design and delivery.
- **Leasing is working well, growing and providing asset financing to SMEs**. This is despite the lack of a leasing law and limited funding for leasing firms.
- **Finance Companies are currently serving the SME sector through products such as factoring.** However for this particular product, finance companies have limited tools for credit risk assessment and lack of information/ inadequate understanding of value chains. The reputation of finance companies has suffered as many informal and non-regulated deposit taking companies have inaccurately called themselves finance companies. The CBN and the Finance Houses Association of Nigeria (FHAN) are looking at ways of strengthening and repositioning the sub-sector.
- **Unsuccessful past attempts to promote the SME sector could lead authorities (and skeptical banks) to resist new SME policies due to a perceived high risk of failure**. Past attempts to promote the sector, including the SMEEIS, have not lived up to expectations. However, the existing five venture capital companies that were set up to manage the SMEEIS funds are operational, have experience, and know the sector. The private sector could build on this experience to focus on proven "debt-plus" mezzanine funding mechanisms to promote greater SME financing. Debt -plus financing for SMEs consists of hybrid loans that allow the company to repay the loan on the basis of its cash flow instead of a pre-determined amortization table. In exchange, the lender has the right to share in the company profits or receive an equity interest in the company that can be sold back to the principals at a premium.
- **Rapid growth at the top and bottom ends of the market could distract both the public and private sectors from the missing SME middle**. Banks are rapidly expanding at the top end of market and are also expanding regionally and internationally. At the micro credit level, MFBs are growing and professionalizing. However, too little is being done to promote growth of the missing middle in SME finance, and policy makers and funders should refocus efforts on this vital sector.

7.6 SME Finance Recommendations

7.6.1 Improve data collection and dissemination (timeframe: short-term). The value of having adequate public data on supply and demand of SME finance and SME activities cannot be sufficiently stressed. As was recently demonstrated with the release of the findings of the

FinScope Nigeria survey by EFInA, information is the first step in understanding and overcoming a challenge. To improve data, CBN could take the following steps:

- Use the SMEDAN definition of SMEs. This is a good standard that is relatively well known in Nigeria but not systematically applied by financial institutions supervised by CBN.
- Expand open item code 10860 of the Monthly Statement of Assets and Liabilities (MBR 300) to include lending products such as leasing and factoring and loans under credit lines issued to SMEs.
- Begin to classify the SME data by type of loan, loan size, company size, and economic sector. This will be feasible as CBN refines its database with the additional SME information provided by financial intermediaries.
- Make the aggregate data (sum total for all financial institutions) public via the CBN website and CBN reports.

The Company Affairs Commission (CAC) can also play a crucial role in improving SME data, as it manages the database on companies and business names and collects annual financial returns for all companies. The CAC already provides some data online, however the data are not free and in order to access the data a card must be physically bought in Nigeria. Along with making it easier to access the current data, the CAC should update its database to clearly identify operative companies, along with name, address, current managers, number of employees, reported sales, and the industrial or economic sector of the company. SME firm data classified by size, sales, and sector would allow the market (and authorities) to track the number of formal SMEs and trends in employment and sales.

7.6.2 Establish a credit information system (timeframe: short-term). A well functioning and comprehensive credit information system with both positive and negative information is imperative for credit to continue to develop in Nigeria. Efforts are already underway, and the CBN is drafting guidelines for the licensing, operations, and regulatory requirements of private sector credit bureaus in Nigeria. The October 2008 draft guidelines are robust, however, further attention may be needed on use of a unique identifier, the dispute resolution process, the authorization process, and data privacy. Once the guidelines are approved, three to four private credit bureaus will be ready to apply for licenses and begin operations.

The CRMS could be established as a separate unit within the CBN to supplement existing CBN off-site supervision. Incorporating all MFBs in the CRMS should be reconsidered, as this could compromise its operations and lower overall quality of information. While credit information systems are important for microfinance and branchless banking clients, other alternatives beyond the CRMS should be identified. For example, the private credit bureaus could play a role in identifying a sample of MFBs capable of providing accurate information on a regular and timely basis, and over time more MFBs and their clients could be incorporated into private bureaus.

Having private credit bureaus exchange client identifier information (particularly biometric, which seems to be the preferred solution by the likely new entrants) would probably help solve the ID problem in a relatively short period of time (if common standards are applied in biometric data collection/verification).

7.6.3 Increase the use of checks as a credit and payment instrument (timeframe: short-term). Checks have limited acceptance in Nigeria both at the retail and inter-company levels given low confidence and limited enforcement of the Dishonored Cheques Act. Given advances in electronic payments, the use of checks as merely a payment medium will continue to decrease. However checks also serve as de facto credit instruments, particularly for inter-company transactions and supplier credit. To increase the use of checks as a relatively risk-free credit instruments, CBN could revise regulations governing procedures for checks with insufficient funds. The regulations would need to address internal bank procedures for dealing with such checks, provision of relevant information to the CRMS and private credit bureaus, and sanctions for insufficient funds (e.g., fees, account limitations, impact on client credit rating).

7.6.4 Promote introduction of new products for SME finance (timeframe: medium term). SME financing poses specific challenges. To improve understanding of SME finance, public and private sector actors from SMEs and financial institutions could organize a "product conference" to discuss products for SME finance that may be appropriate for Nigeria. CBN and SMEDAN are well placed to facilitate this discussion with the private sector, along with the involvement of the MSME project. In addition, development programs could include technical assistance for financial institutions interested in developing and introducing new products for SME finance.

7.6.5 Leverage SMEEIS experience (timeframe: medium/long term). The private sector could leverage the expertise of venture capital companies established to manage equity investments under the SMEEIS program. To be more effective, the funds could be modified to incorporate debt- plus financing in addition to the existing equity structure while maintaining their venture capital approach. This process would introduce a dramatically different loan process, spur banks to try new lending mechanisms, and provide financing to worthwhile projects that currently do not have sufficient guarantees. To fund these venture funds, the government should consider fiscal incentives on earnings, promoting listing (and trading) of participations in the funds through the exchange, and perhaps approaching donors and quasi investors for "matching" funds. Each fund should be allowed to choose its operational objectives and management approach rather than requiring a general methodology as was done under the SMEEIS program.

7.7.6 Review and where necessary reform legislation and regulation on collateral and registries (timeframe: medium term). Legislation and regulations should be reformed to incorporate the realities of the Nigerian SME market, broaden the definition of acceptable guarantees, and improve use of debtor credit history.

- **Leasing.** A draft leasing law has been passed by the National Assembly but has not yet been signed into law by the President. This draft was not made available to the team and hence was not reviewed. Approval of the leasing law will be positive for the country. The law and implementation should ensure that leasing companies will be able to seek new sources of funds. As one option, leasing companies could be left as non-banking institutions that seek bank loans and eventually raise funds directly in the capital markets, as is the case now. Alternatively leasing companies could be brought into the fold of CBN regulated financial institutions that are able to mobilize deposits. The best option will depend on a range of factors, including CBN supervision capacity and market development.

- **Finance companies.** A study of the factoring market and role of finance companies would help CBN and FHAN determine if any amendments are required to legislation or regulation. Since finance companies are already active in SME finance an adequate reform of the sector could provide a substantial boost to finance.
- **Moveables registry.** While the CAC manages a workable registry of floating claims on company assets, the registry does not identify individual assets, and only incorporated businesses can make use of it. Reforms are urgently needed to improve the registry and legal system for liens on moveable assets. The World Bank/IFC-supported MSME project is preparing terms of reference for consulting services in this area, and this analysis should be done in close coordination with the World Bank team that prepared the Report on Observance of Standards and Codes: Nigeria, Insolvency and Creditor Rights.

7.7 Broad Access to Finance Conclusions

Nigeria's access to finance regulatory framework is well developed, dynamic and benefits from a large degree of support by engaged and motivated regulators. Nevertheless, some key regulatory areas need additional clarity.

- **Interest rate policy needs to be clarified.** Based on interviews with dozens of people, there are wide disparities in the market and even within the CBN as to whether interest rate caps exist, how they are to be calculated, and whether they will be seriously enforced. If interest rates are freely determined, as is good practice globally, then CBN should clarify this among their own personnel and to financial service providers.
- **AML/CFT regulations need greater clarity**. Many different regulations, circulars and other authoritative documents are in conflict with each other, and this needs to be addressed.
- **Standards for consumer protection need to be established**. Given growth of the financial sector and increasing competition among providers, it may be time to consider a consumer protection body specialized in financial services. The mobile payments guidelines may introduce a mobile payments consumer protection body, although this would introduce a consumer protection body with a mandate that is too narrowly defined—leaving the vast majority of financial consumers without consumer protections.

7.8 Broad Access to Finance Recommendations

7.8.1 Clarify the policy on interest rate caps (timeframe: short-term). Based on interviews with CBN personnel, banks, MFBs and local counsel, the policy and enforcement of interest rate caps was not clear. There are wide disparities in the market and even within the CBN as to whether interest rate caps exist, how they are to be calculated and whether they will be seriously enforced. The CBN should (i) clarify to its own personnel and to the market whether and how interest rate caps are set, and (ii) ensure that any caps do not limit the ability of microfinance banks to set interest rates at levels necessary to remain sustainable. Interest rate caps may effectively prohibit the rise of sustainable microfinance banks, which, due to the high transaction costs of relatively small loans, rely on higher interest rates to cover expenses.

7.8.2 Harmonize all AML/CFT regulations to permit clear operation of risk-based approach (timeframe: medium term). The lack of harmonization of all regulations addressing AML/CFT matters can result in both over-protective applications (if financial institutions apply the most stringent standards, even for simple accounts, rather than risk noncompliance) and under-protective applications (if financial institutions "cherry pick" the least stringent standards in an effort to promote greater income through a larger customer base and increased number of transactions). In addition, the lack of a clear risk-based approach may severely restrict consumer uptake of mobile banking models that target low income populations who often have no official identification or documentary evidence of address. In order to fully realize the goals of the FSS 2020 strategy and to promote access to finance in Nigeria, a harmonization of AML/CFT regulations should be undertaken to (i) define verification requirements, (ii) establish a realistic array of documentary evidence permitted to meet such verification requirements,[101] (iii) permit non-face-to-face account opening and clarify the procedures related thereto, (iv) clearly define the AML/CFT applicability to one-off transactions, and (v) adopt a risk-based approach to all account opening, and particularly with respect to mobile accounts and other accounts aimed at low-income segments of the population. In addition AML/CFT procedures with respect to financial services should be harmonized with identity requirements for telecommunications services.

7.8.3 Enhance consumer protection by facilitating consumer access to credit reports and requiring disclosure of "disputed" status (timeframe: medium/long term). The Credit Bureau Guidelines permit consumers unhindered access to their credit information but only at the credit bureau's physical establishment. Long distances and limited opening hours may effectively restrict a consumer's ability to access credit information. The CBN should consider alternative means of providing credit information to consumers, including via internet, mobile telephony, the postal system, offices of financial service providers where they have accounts, and/or a secure agent network. To avoid undue burden on the credit bureaus, such alternative means may be limited in frequency or subject to a fee after an initial free annual copy. In addition, although the Credit Bureau Guidelines require credit bureaus to investigate data a consumer has disputed, this would only lead to a correction where the creditor agrees with the consumer that an error was made. However, in the event there is a genuine dispute between a creditor and consumer as to whether amounts reported as delinquent were actually due, the Credit Bureau Guidelines imply that only the creditor's view will be reflected in the consumer's credit report. Provision should be made to require credit bureaus (or require creditors when reporting data to credit bureaus) to indicate on the credit report when items reported as delinquent are in fact disputed by the consumer. Given timing in licensing and launching the credit registries, this level of consumer protection will need to be phased in over the medium/long term.

7.8.4 Establish a consumer protection body dedicated to protecting consumers of all financial services, not just mobile payment services (timeframe: medium/long term). The mobile payments guidelines reportedly provide for the creation of a consumer protection body devoted to mobile banking customers and issues. While mobile payment services undoubtedly present new consumer protection challenges, a consumer protection body dealing only with mobile payment customers excludes the vast majority of financial services customers also in need of consumer protection, particularly with respect to loans.[102] As in the Nigerian

[101] The National Identity Management Commission is currently planning to roll out multi-purpose smart cards (managed on a central database) to serve as a national form of identification. See www.nimc.gov.ng.

[102] In 2004, the CBN issued a circular to remind commercial banks that they are prohibited from charging customers in excess of the agreed rates set forth in the Guide to Bank Charges. CBN Circular BSD/2/2004, April 23, 2004

telecommunications sector, a new consumer protection body, independent from the CPC, should be established to address the vast array of consumer protection matters of special relevance to the provision of all financial services, including (i) whether protections extend to legal entities or simply individuals, (ii) appropriate disclosure, (iii) consumer recourse mechanisms (including whether such consumer protection body will have binding authority, or must be used prior to having access to the court system and/or only after an internal investigation by the financial institution in question), and (iv) consumer awareness programs. Such a consumer protection body, which should also be required to maintain data for regulatory review, may be best established under the authority and supervision of the CBN due to the CBN's experience and knowledge of financial products and its ability to balance prudential concerns with consumer protection.

7.9 Funder Conclusions

Improved coordination: A wide range of funders are active in microfinance, rural and agricultural finance, and SME finance in Nigeria. During the mission, several funders expressed the need to improve coordination and promote good practices. UNDP has organized a Microfinance Board to facilitate discussions among donors and the government. The large government programs in support of microfinance, rural finance, and SME finance (the new Microfinance Development Fund, NAPEP, CBN's initiatives managed by DFD, etc.) should also be invited to donor coordination meetings. Improved coordination fits well within Nigeria's FSS 2020, and the Secretariat could also play a role in promoting funder coordination.

7.10 Funder Recommendations

Re-activate donor coordination (timeframe: short-term). Given the number of funders and GoN programs active in access to finance, coordination is essential for aid effectiveness. Donors active in the sector include UNDP/UNCDF, DFID, USAID, GTZ, the World Bank Group, and others. In particular, the EFInA and MSME programs are covering a range of activities in microfinance, branchless banking, and SME finance, and they may be appropriate programs to facilitate funder coordination. These discussions should also include government programs on access to finance. The FSS 2020 Secretariat may also be an option to facilitate funder and government coordination.

Annex 1:

NIGERIA PAYMENT SYSTEMS: TANGIBLE RECOMMENDATIONS AND RESULTS THAT CAN REALISTICALLY BE IMPLEMENTED WITHIN A REASONABLE TIMEFRAME

QUICK WINS AND MEDIUM/LONG-TERM ACTIONS

Medium-term Outcome 2012	Timeframe	Action Item:	What's Involved	Donor Assistance Required
Microfinance Services				
MFBs are adequately capitalized. All MFBs have sufficient capital for initial investment and pre-profitability period.	24 months	Raise the minimum capital requirement for unit microfinance banks.	Calculate on the basis of the experience of successful microfinance banks in Nigeria how much capital is required to carry a microfinance bank from initial investment through to profitability. Calculate on the basis of microfinance banks overall business plan and financial projections capital requirements for branch expansion. Revise minimum capital regulations or simply require applicants to invest a capital amount that is consistent with their financial projections and business plan.	None required.
MFBs are free to adapt individual business plans to market conditions.	3 months	Ease geographic restrictions on microfinance bank expansion. Allow acquisitions	Easing geographic restrictions in the CBN microfinance guidelines will ease pressure where MFBs are currently concentrated and allow MFBs to grow, and capitalize, where market opportunities exist. Remove geographic restrictions on the	None required.

Medium-term Outcome 2012	Timeframe	Action Item:	What's Involved	Donor Assistance Required
		and mergers without geographic restrictions	unit and state licenses in the CBN microfinance guidelines to allow mergers and partnerships to occur naturally between complementary business models and markets, as opposed to political boundaries.	
Build capacity of MFBs.	36 months	Develop a capacity building strategy for microfinance banks, to serve as a mechanism for donor coordination.	Funder group coordinating with CBN to take the lead in developing a capacity building strategy with MFBs, the national MFB association, training organizations, and other relevant stakeholders.	Support from funders is required to finance the various capacity building initiatives specified in the strategy.
Supervision oversight ensures safety and soundness in the MFB sector.	6 months	Publish key data on the CBN website.	Post on the CBN website historic financial statements, data on financial and outreach performance, and interest rates of all microfinance banks.	None required.
	6 months	Focus supervision efforts on the largest microfinance banks.	Adopt a multi-tiered approach to supervision that applies different levels of supervision according to the size of the microfinance bank Post regular reports on the CBN website on the supervisory status of each microfinance bank to create incentives for microfinance banks to reach to the highest category.	None required
	24 months	Develop off-site and on-site supervision capacity in the CBN.	Develop off-site and on-site supervision tools and training programs for monitoring of microfinance bank performance, including: • On-site inspections techniques. • Management of on-site inspections,	Advisory services from experts with experience from more advanced supervisory regimes.

Medium-term Outcome 2012	Timeframe	Action Item:	What's Involved	Donor Assistance Required
			including correspondence and meetings with the board of directors and management, formulation of recommendations, and follow up. • CBN mandates regarding external audits of microfinance banks, including drafting of core terms of reference for audits and sanctions against auditing firms that fail in compliance or performance. • An ongoing OFID staff training and development program.	
MFBs develop sustainable and scalable funding strategies	6 months	Align all microfinance bank wholesale lending programs with a market-based model.	Issue a lending policy for the Microfinance Fund that (a) ensures refinancing rates are market-referenced, (b) establishes risk-based rates so that amount and pricing of a microfinance bank borrowing reflects its financial strength, and (c) limits access to the fund to microfinance banks that comply with robust financial performance benchmarks, and (d) limits borrowing to prudent amounts relative to assets.	Access to lessons learned from successful global experience with government-owned microfinance wholesale facilities
Branchless Banking				
Payment systems become more secure and efficient • Proportion of non-cash transactions made by cards rises from 1 percent in 2007 to 10+ percent in 2012. *Source*: CBN data.	3 months	Promote interoperability of the retail payment system.	Define the role of the National Central Switch in relation to private switches. Prepare operational guidelines that ensure that the central switch does not have an unfair competitive advantage in terms of product pricing, interchange fees, or access to financial regulators (given its	None required.

Medium-term Outcome 2012	Timeframe	Action Item:	What's Involved	Donor Assistance Required
• Number of transactions made by mobile telephone triples by 2012. *Source*: CBN data.			existing infrastructure and partial government ownership).	
	3 months	Ensure that mobile payments guidelines address key issues and consumer protection challenges unique to mobile banking.	Ensure that the mobile payments guidelines address: • Use of agents and/or third party service providers, including qualifications and liability. • Management of the prudential risks involved in nonbank-led models of mobile banking, including how the potential prudential risks of nonbank-based models will be managed. • Consumer protection challenges unique to mobile banking.	Given this relatively new area for mobile payments, international experience may be useful to draft or review the guidelines.
Small and Medium Enterprise Finance				
Increase in Access to SME finance Proportion of short-term financing for SMEs from (a) banks and other financial institutions and from (b) credit from suppliers and advances from customers rises from 26 percent in 2007 to 40+ percent in 2012. *Source:* World Bank Investment Climate Surveys.	6-12 months	Improve data collection and dissemination.	Immediate actions that the **CBN** can take, include: • Using the SMEDAN definition of SMEs. This is a good standard that is relatively well known in Nigeria but not systematically applied by financial institutions supervised by CBN. • Expanding open item code 10860 of the Monthly Statement of Assets and Liabilities (MBR 300) to include lending products such as leasing and factoring and loans under credit lines issued to SMEs. • Classifying the SME data by type of	None required.

Medium-term Outcome 2012	Timeframe	Action Item:	What's Involved	Donor Assistance Required
			loan, loan size, company size, and economic sector. This will be feasible as CBN refines its database with the additional SME information provided by financial intermediaries. • Making the aggregate data (sum total for all financial institutions) public via the CBN website and CBN reports. Immediate actions that the **Company Affairs Commission** can take, include: • Making it easier to access the data currently posted online. • Updating the CAC database to clearly identify operative companies, along with name, address, current managers, number of employees, reported sales, and the industrial or economic sector of the company.	
	3-12 months	Establish a credit information system.	Ensure that the draft guidelines for licensing, operations, and regulatory requirements of private credit bureaus address: • Use of a unique identifier • Dispute resolution process • Authorization process • Data privacy. Approve the guidelines. Reconsider incorporating all microfinance banks in the Credit Risk Management	The MSME project funded by the WB and IFC is already involved in technical assistance on this issue. However the consultants may need to focus more attention, along with market participants and the CBN, on setting standards for the use of a unique identifier.

Medium-term Outcome 2012	Timeframe	Action Item:	What's Involved	Donor Assistance Required
			System, as this could compromise its operations and lower the overall quality of information. Make the Credit Risk Management System available to all private credit bureaus. They would be able to build on the current database (instead of having to spend years rebuilding it) by adding information and data subjects. This could help solve the ID problem in a relatively short period of time.	
	6-12 months	Increase the use of checks as a credit instrument.	Strengthen enforcement of the Dishonoured Cheques Act. Consider revision of regulations governing procedures for checks with insufficient funds. The regulations should address internal bank procedures for dealing with such checks, provision of relevant information to the Credit Risk Management System and private credit bureaus, and sanctions for insufficient funds.	This could be undertaken by the CBN directly unless there is a need for additional research and legal analysis.
	1–2 years	Promote introduction of new products for SME finance.	Host a product conference to discuss potential products for SME finance. Encourage existing or new projects and programs to include technical assistance for financial institutions interested in developing and introducing new products for SME finance.	Consider organizing this through the SME committee of FSS 2020 in conjunction with the MSME project, the IFC, the WB, and other funders active in SME finance.
	1–2 years	Reform regulation	Review legislation and regulations on	Before final approval

Medium-term Outcome 2012	Timeframe	Action Item:	What's Involved	Donor Assistance Required
		on collateral and registries.	collateral and registries and reform where necessary to facilitate SME finance. Key actions include: • Approve the draft leasing law. • Conduct a study of the factoring market and role of finance companies to determine if amendments to legislation or regulation are needed. • Implement recommendations of the consultancy being financed under the MSME project on the moveables registry.	and presidential sign-off, the draft leasing law could be reviewed in order to address the funding issue. International consultants should work with local industry participants on the study of the factoring market and the role of finance companies.
Overall Access to Finance				
Access to finance rises Proportion of adult population (18+) that uses financial services provided by formal financial service providers rises from 26 percent in 2008 to 40+ percent in 2012. *Source:* FinScope survey to be carried out in Nigeria every 24 months. The baseline survey was completed in 2008.	1 month	Clarify the policy on interest rate caps.	Clarify to CBN staff and to other stakeholders the policy on interest rate caps, and ensure that any caps do not limit the ability of microfinance banks to set interest rates at levels necessary to remain sustainable.	None required.
	1 year	Harmonize all AML/CFT regulations to	A harmonization of AML/CFT regulations should (a) define verification requirements, (b) establish a realistic array	Coordinate closely with CGAP, WB, and IMF to

Medium-term Outcome 2012	Timeframe	Action Item:	What's Involved	Donor Assistance Required
		permit clear operation of risk-based approach.	of documentary evidence permitted to meet such verification requirements, (c) permit non-face-to-face account opening and clarify the procedures related thereto, (d) clearly define the AML/CFT applicability to one-off transactions, and (e) adopt a risk-based approach to all account opening, and particularly with respect to mobile accounts and other accounts aimed at low-income consumers. In addition, AML/CFT procedures should be harmonized with identity requirements for telecommunications services.	incorporate global lessons on AML/CFT measures that incorporate inclusive finance considerations.
	1–3 years	Enhance consumer protection by facilitating consumer access to credit reports and requiring disclosure of "disputed" status.	Revise the credit bureau guidelines (a) to give consumers access to information in their credit reports through low-cost and convenient means, such as internet, post, or telephone, and (b) to require credit bureaus (or to require creditors when reporting data to credit bureaus) to indicate on the credit report when items reported as delinquent are in fact disputed by the consumer.	This issue is already being supported by the MSME project.
		Establish a consumer protection body dedicated to protecting consumers of all financial services, not just mobile payment services.	Establish a new consumer protection body under the authority and supervision of the CBN to address the consumer protection matters of special relevance to the provision of all financial services. CBN is well placed to oversee such a consumer protection body because of its experience and knowledge of financial products and its ability to balance prudential concerns with the need to protect consumers of the	International expertise may be useful to scope the approach, resources, and timing needed for the consumer protection body. Depending on scale of the operations, donor support may

Medium-term Outcome 2012	Timeframe	Action Item:	What's Involved	Donor Assistance Required
			services.	be required.
Increasing the Effectiveness of Donor-Financed Programs				
Stronger coordination and improved impact of donor-financed programs	3-6 months	Promote funder coordination.	Reactivate the donor coordination group.	

Annex 2:

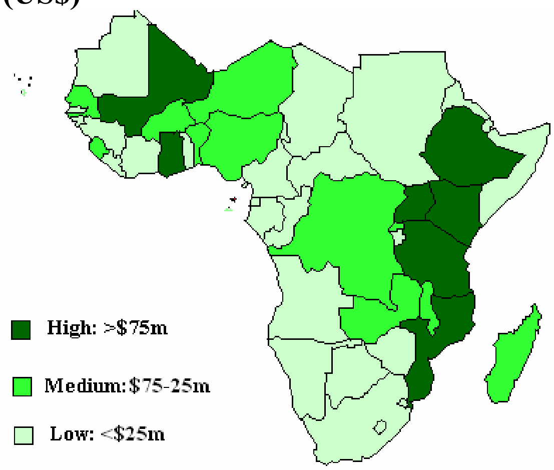
Funder Initiatives in Nigeria

This annex summarizes the activities of funders in Nigeria based on data from the comprehensive CGAP funder survey in sub-Saharan Africa for 2007. In order to better understand funder activity, in 2005 CGAP began surveying funders working in Africa on increasing access to finance. In 2007, 40 respondents provided self-reported information on their general projects, specific activities in each country, and funding.

Funding in Nigeria

In comparison to the rest of the region, Nigeria stands as one of the heavily funded countries. It is among the top 10 funded countries and is eighth after Ghana, Uganda, Kenya, Tanzania, Ethiopia, Mali and Mozambique. Funders' commitments in Nigeria represent 11 percent of total commitments in Western Africa.

Figure 10: Funding Amounts per Country (US$)

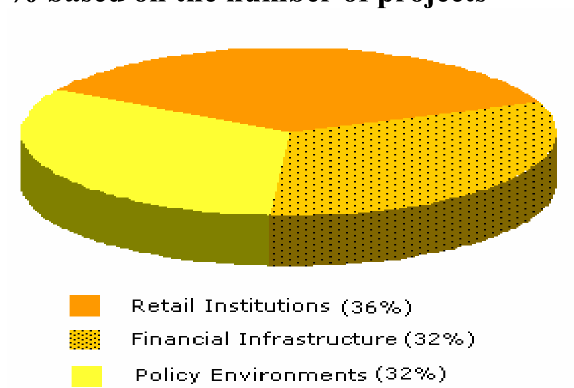


Projects by Activity Levels of the Financial System

Access to finance projects are distributed among three types of activities:

- Retail institutions projects (36 percent) support a wide range of financial and non-financial institutions.
- Financial Infrastructure projects (32 percent) support locally available market infrastructure and services, including auditors, rating agencies, networks and associations, credit bureaus, transfer and payment systems, information technology and technical service providers.
- Policy Environment projects (32 percent) support government policies and systems, including laws and regulations and enforcement bodies, such as banking supervision.

Figure 11: Projects by Activity Level
% based on the number of projects



Seven percent of committed funding, NGN 543.6 million (US$ 4.5 million), is channeled to one level of the financial system, although they account for 48 percent of the number of projects (10 of the 21 projects) with an average of NGN 54.36 million (US$ 450,000 million) per project. These projects can be considered single-level projects. However, 58 percent of committed funding, NGN 4.8 billion (US$ 40 million), operates on several levels of the financial system. These multi-level projects represent 38 percent of the projects (8 of 21 projects), with an average of NGN 604 million (US$ 5 million) per project.

Projects Supporting Retail Institutions
There are 12 projects—either single-level or part of multi-level projects—supporting retail institutions. Projects at this level are divided between those providing funding (59 percent) through grants and loans, to MFIs and those providing technical assistance (33 percent) through grants.

Figure 12: Retail Institution Projects
Percent based on the number of projects

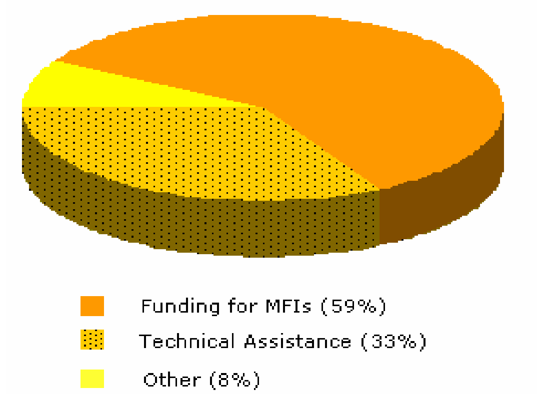
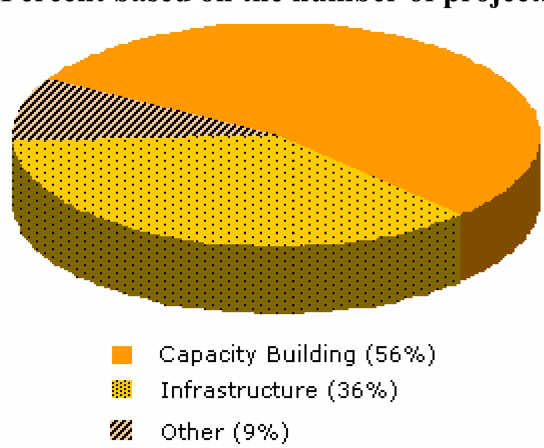


Figure 13: Financial Infrastructure Projects
Percent based on the number of projects



Projects Supporting Financial Infrastructure
There are 11 projects—either single-level or part of multi-level projects—that support financial infrastructure.
Projects at this level are divided between (a) capacity-building activities (55 percent) such as training of trainer courses, audits, MIS, and MFI ratings, and (b) infrastructure (36 percent) in the form of support toward payments systems and credit bureaus and accounting standards.

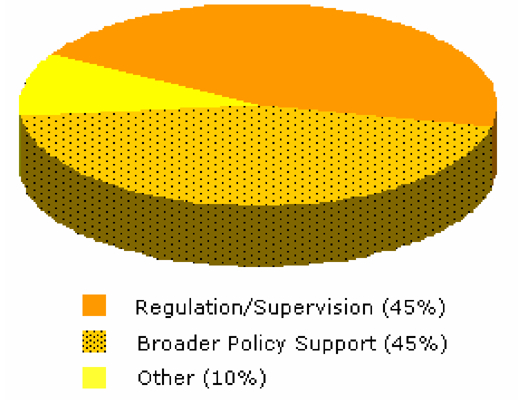
Projects Supporting Policy Environments

There are 11 projects—either single-level or part of multi-level projects—that support policy reforms.

Policy projects are equally divided into regulation/supervision (45 percent) and broader policy issues (45 percent), such as interest rate regime, tax issues, and national strategies.

There is a trend of funder collaboration at the policy level as these projects tend to be large, and they allow funders to pool resources, provide specialized expertise, and achieve economies of scale. Thirty percent of all policy projects are supported by two or more funders; they are mostly multilateral and bilateral donors.

Figure 14: Policy Environment Projects
Percent based on the number of projects



Projects by Funder Type

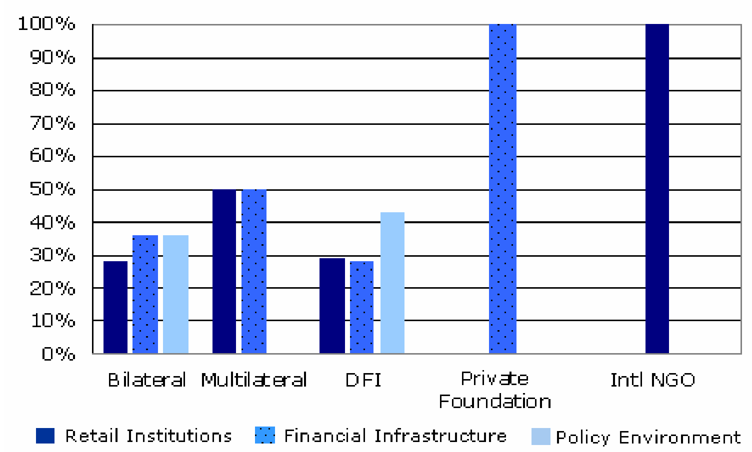
In Nigeria, international NGOs and multilateral organizations are the primary funders to support retail institutions.

Financial infrastructure is primarily supported by multilateral and bilateral funders, and private foundations.

Bilateral funders, along with DFIs are the primary funders of policy environment projects.

The figure at right shows how different types of funders spend their money.

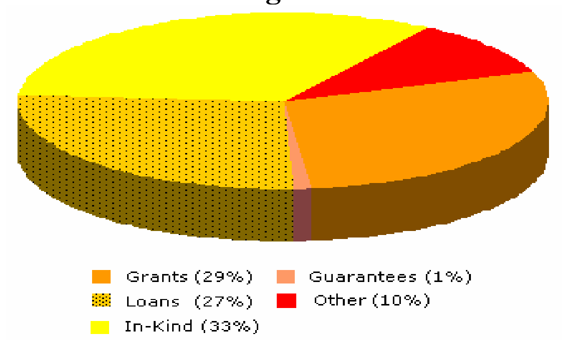
Figure 15: Projects by Funder Type
% based on the number of projects



Funding by Funding Instruments

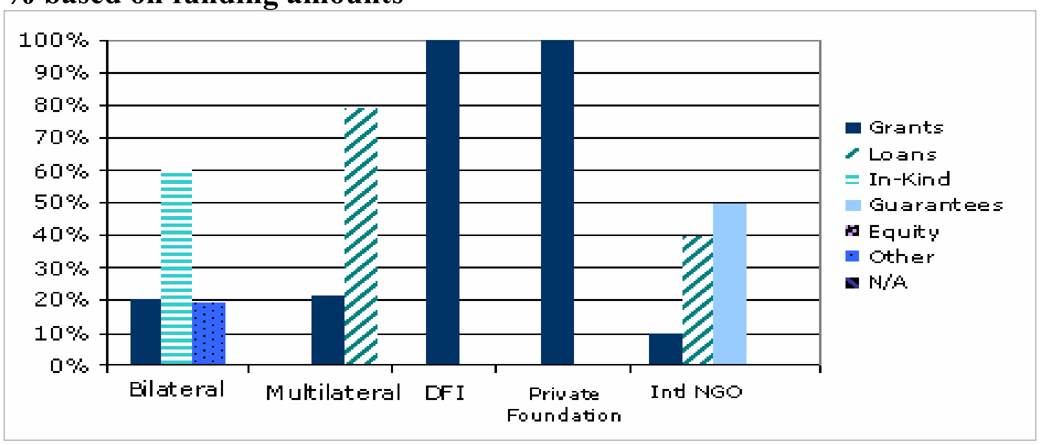
In Nigeria, funders use a range of instruments, but they favor in-kind funding (33 percent), grants (29 percent) and loans (29 percent). In-kind funding is typically coupled with either a loan or a grant. Bilateral funders and international NGOs are the main providers of grants, while loans are funded primarily by DFIs, MIVs, private foundations, multilateral funders and international NGOs.

Figure 16: Funding Instruments
% based on funding amounts



As seen in the figure below, bilateral donors and international NGOs are using wide variety of instruments that allows flexibility in working with the private sector.

Figure 17: Funding Instruments
% based on funding amounts



Note: Instruments at less than 5 percent not shown.

Annex 3

List of People Interviewed

City	Institution	Department/Division	Officials	Title
Abuja	**Central Bank of Nigeria**	Deputy Governor	Suleiman Barau	Deputy Governor
Abuja	**Central Bank of Nigeria**	Banking Supervision	H.O. Amazu	Deputy Director
Abuja	**Central Bank of Nigeria**	Banking Supervision	D.N. Gana	Deputy Director
Abuja	**Central Bank of Nigeria**	Banking Supervision	D.A.N. Eke	Deputy Director/Head Wholesale Payments Office
Abuja	**Central Bank of Nigeria**	Banking Supervision	Dozie Okwuosah	Assistant Director
Abuja	**Central Bank of Nigeria**	Payment Systems/Banking Operations Dept.	James K. A. Olekah	Director, Banking Operations Department
Abuja	**Central Bank of Nigeria**	Payment Systems/Banking Operations Dept.	Emmanuel C. Obaigbona	Head, Payment Systems Division
Abuja	**Central Bank of Nigeria**	Payment Systems/Banking Operations Dept.	A. Oyedele	Head, Wholesale Payments Office
Abuja	**Central Bank of Nigeria**	Payment Systems/Banking Operations Dept.	Akinwunmi Olubukola A.	Payments Analyst
Abuja	**Central Bank of Nigeria**	Audit	Sam Oni	Director
Abuja	**Central Bank of Nigeria**	Credit Registry	M.W. Muazu-Lere	N/A
Abuja	**Central Bank of Nigeria**	Development Finance	Joe Alegieuno	Head, Microfinance
Abuja	**Central Bank of Nigeria**	Development Finance	P.I. Esenwah	Deputy Director
Abuja	**Central Bank of Nigeria**	Development Finance	Asuma G. Ehilebo	Deputy Director
Abuja	**Central Bank of Nigeria**	Development Finance	Uji Amedu	Deputy Director, Microfinance Division
Abuja	**Central Bank of Nigeria**	Development Finance	B.I. Adamu	Deputy Director

Abuja	**Central Bank of Nigeria**	Development Finance	Uzoma F. Onuoha	Assistant Director
Abuja	**Central Bank of Nigeria**	Development Finance	Ogunlaja Babatunde	N/A
Abuja	**Central Bank of Nigeria**	Project Management Office	Sam C. Okojere	Senior Manager (PMO)
Lagos	**Central Bank of Nigeria**	OFID	Okpokor Ezewu	Officer
Lagos	**Central Bank of Nigeria**	OFID	Olufemi Fabamwo	Acting Director
Lagos	**Central Bank of Nigeria**	OFID	Kehinde A. Omole	Assistant Director
Lagos	**IFC**	Africa Department	Olayemi Idris-Animashaun	Investment Officer
Lagos	**Akinwunmi & Busari Law Firm**		Seyi Akinwunmi	Partner
Lagos	**Akinwunmi & Busari Law Firm**		Uche Ugoji	Senior Associate
Lagos	**Akinwunmi & Busari Law Firm**		Yetunde Bamidele	Associate
Lagos	**Nigerian Association of SMEs**		Eke U. Ubiyi	Executive Secretary
Lagos	**Nigerian Association of SMEs**		Samson Gbadamosi	Head, Finance and Admin.
Lagos	**Nigerian Association of SMEs**		Maxwell E. Akpoigbe	Head, Research, Training and Consultancy

Lagos	**Nigerian Association of SMEs**		Dr. Ike Abugu	President and Chairman
Lagos	**Credit Registry**		Taiwo Ayedun	Chief Executive Officer
Lagos	**Oceanic Bank**		Arowosafe Babajide	N/A
Lagos	**Oceanic Bank**		Boluwade E. Olamide	N/A
Lagos	**Oceanic Bank**		Aliu Fatimah	N/A
Lagos	**Equipment Leasing Association of Nigeria**		Andrew Efurhievwe	Executive Secretary
Lagos	**Equipment Leasing Association of Nigeria**		Akinde Obatuyi	Assistant Executive Secretary
Lagos	**Lagos Chamber of Commerce and Industry**		Yinka Adegoyin	Officer Membersip Relations
Lagos	**Lagos Chamber of Commerce and Industry**		Soluke Oloniyo	Manager Memebership Relations
Lagos	**Manufacturers Association of Nigeria**		Segun Ajayi-Kadir	Executive Secretary
Lagos	**Diamond Bank**		Emeka Onwuka	Group MD/CEO
Lagos	**Diamond Bank**		Tony Onwu	Managing Director
Lagos	**Diamond Bank**		Uzoma Dozie	Executive Director, Retail Banking
Lagos	**Diamond Bank**		Ohis Ohiwerei	Executive Director, Chief Financial Officer
Lagos	**Diamond Bank**		Michael Emmanuel	Treasury & Correspondent banking Group
Lagos	**Ecobank**	Consumer Finance Unit	Funmi Sodipo	Head, Consumer Finance

Lagos	**Ecobank**		Omotefowe T. Diejomaoh	N/A
Lagos	**Ecobank**		Adebayo Osikomaiya	N/A
Lagos	**Ecobank**		Christopher Olusola	Microfinance & SMEEIS, Retail Banking Group
Lagos	**Bank of Industry**		Mohammed G. Alkali	General Manager
Lagos	**NACCIMA**		Abiodun Awogbemi	Public Relations Manager
Abuja	**Ministry of Commerce and Industry**	Small and Medium Enterprises Department	L.G. Salami	Deputy Director
Abuja	**SMEDAN**		Wale Fesanya	Acting Director-General
Abuja	**SMEDAN**		S. Olufemi Adebiyi	Group Head, Enterprise Promotions, Management and Extension Services
Abuja	**Credit Investments Ltd - Finance Company**		Cynthia Akachukwu	Credit Officer
Abuja	**USAID**	Economic Growth	Ron Greenberg	Director, Economic Growth Office
Abuja	**USAID**	Partnership Office	Leslie Flagg	Private Sector Advisor, Partnership Office
Abuja	**USAID**		Nikhil Jaisinghani	Project Development Officer
Washington	**USAID**	MARKETS	Christopher Barltrop	Senior Financial Markets Advisor
Abuja	**Corporate Affairs Commission**	Compliance Department	Bello Mahmud	Director
Abuja	**Corporate Affairs Commission**		Abdurrahman Babale	Advisor to the DG

Abuja	**Fortis Microfinance Bank**	Development Finance Department	Sewuese Agugu	
Abuja	**Fortis Microfinance Bank**	Development Finance Department	Godfrey Ajayi	Bank Manager
Abuja	**Fortis Microfinance Bank**	Risk Management	Terhemba Yongu	
Abuja	**Fortis Microfinance Bank**		Deji Fisho	Managing Director
Lagos	**IFC**	Global Financial Markets Group	Sola Olubi	Associate Investment Officer
Lagos	**Integrated Capital (Money Box)**		Adeniyi Elumaro	CEO
Lagos	**Money Box Africa**		Damien Oguchi	Chief Finance Officer
Lagos	**Money Box Africa**		Lai Labode	Chief Marketing Officer
Lagos	**Money Box Africa**		Kelechi Nzekudu	Chief Technology Officer
Lagos	**Money Box Africa**		David Kaye	Chief Operating Officer
Lagos	**Money Box Africa**		Abu Taoheed	Chief Customer Care
Lagos	**EFInA**		Modupe Ladipo	CEO
Lagos	**EFInA**		Magnus Adiele	Research specialist
Abuja	**NAPEP**		Magnus Kpakol	National Coordinator
Abuja	**NAPEP**		Edgar Otowo	Director of Programs
Lagos	**Accenture**		Adedotun Sulaiman	Chairman
Lagos	**Development Alternatives Resource Center**		Ngozi Ezi-Ashi	Executive Director

Lagos	**Microenterprise Place**		Edna Ishaya	Founder/CEO
Abuja	**MSME Project Nigeria**		Emeka Ile	Team Leader & Access Finance Specialist
Abuja	**MSME Project Nigeria**		Thomas Timberg	Senior Adviser, Access to Finance Specialist
Abuja	**Alliance Microfinance Bank**		Daniel O. Ibrahim	
Abuja	**Alliance Microfinance Bank**	Legal	Hafsat A. Abdulaziz	
Abuja	**Alliance Microfinance Bank**	Marketing	Onen Okoi	
Abuja	**Alliance Microfinance Bank**	Accounting	Kazeem A. Hammed	
Abuja	**Alliance Microfinance Bank**		Oche Obe	Program Director
Abuja	**Economic & Financial Crimes Commission (EFCC)**	Compliance & Enforcement	A. Babashani	Head, Compliance & Enforcement
Lagos	**UBA Microfinance Bank Ltd.**		Lizzy Osunde	Managing Director/CEO
Lagos	**Zain**		Latunde Etiko	Specialist; Messaging
Lagos	**Zain**	Innovation & Service Management	Bankole Ojutalayo	Acting Head
Lagos	**Zain**		Gbolade Shobowale	
Lagos	**Zenith Bank PLC.**		Osakwe Osadebe	General Manager
Lagos	**Zenith Bank PLC.**	Risk Management	Joshua Uwedinisu	
Lagos	**Zenith Bank PLC.**	RAMCE Group	Erhi Oputu	
Lagos	**Credit Reference Company**		Ahmed Tunde Popoola	Managing Director/CEO
Lagos	**Credit Reference Company**		Ademola Adesalu	

Lagos	**Credit Reference Company/Accenture**		Niyi Yusuf	Project Manager
Rome	**IFAD**	Programme Mgmt	Perin Saint Ange	Regional Portfolio Advisor
DC	**Carana Corporation**		Ann Cassanova	
DC	**Grameen Foundation**		John Ikeda	Program Officer - Sub-Saharan Africa
Benin	**Prosperity Microfinance Bank**		Jude Nasagie	N/A
Lagos	**First City Monument Bank**		Dennis Ezaga	Head, Payment & Transfers
Lagos	**eTranzact**		Valentine Obi	CEO
Lagos	**Nigeria Inter-Bank Settlement System (NIBSS)**		O. Paul Lawal	Managing Director/Chief Executive
Lagos	**Nigeria Inter-Bank Settlement System (NIBSS)**		J.O. Obiekwe	Deputy General Manager, Operations
Lagos	**Nigeria Inter-Bank Settlement System (NIBSS)**		Rosemary Isunuoya	Deputy General Manager, Internal Control
Abuja	**Nigeria Deposit Insurance Corporation (NDIC)**		Peter Umoh	Executive Director (Operations)
Abuja	**Nigeria Deposit Insurance Corporation (NDIC)**		Mr. Ogunleye	Managing Director
Abuja	**Nigerian Communications Commission (NCC)**	Tariff & Charges Department	Henry Ojiokpota	N/A
Abuja	**National Identity Management Commission**		Chris Onyemenam	Director General/CEO
Lagos	**Interswitch**	Business Development Group	Jonah Adams	N/A

Lagos	**Interswitch**	Finance Management Group	Dapo Omoni	CFO
Lagos	**MTN**	Marketing & Strategy Department	Abiodun Ogunlabi	Program Manager, MTN MobileMoney
Abuja	**GTZ**	Financial Services	Hubert Rauch	Chief Advisor
Abuja	**GTZ**	Financial Services	Peter Taiwo Ologunagba	Financial Services Officer
Abuja	**UNDP**	Poverty Alleviation Unit	Adiya Ode	Team Leader
Abuja	**UNDP**	Poverty Alleviation Unit	Fatima Sada	Program Analyst
New York	**UNDP**	Private Sector Division, Partnerships Bureau	Jonathan Brooks	Policy Team Leader
Abuja	**Consultant to UNDP**	Working with Jonathan Brooks on project design	Bayo Akindeinde	Consultant
Dakar	**UNCDF**	BIFSA program	Issa Barro	Regional Technical Advisor
Abuja	**Nigerian Consumer Protection Commission**		Mr. Chamberlain	N/A
Accra	**USAID West Africa Trade Hub**	Working on Nigeria and Ghana	Judd Welsh	Consultant
Lagos	**Ford Foundation**		Adhiambo Odaga	Representative, West Africa
Lagos	**ACCION Microfinance Bank**		Bunmi Lawson	CEO
Abuja	**DFID**	Economic Growth	Kevin Quinlan	Team Leader
Abuja	**World Bank**	Country Management Team	Onno Ruhl	Country Director

Abuja	**World Bank**	Country Management Team	Volker Treichel	Lead Economist
Abuja	**World Bank**	Sustainable Development	Simeon Ehui	Sector Leader, Sustainable Development
Abuja	**World Bank**	Private Sector Development	Ismail Radwan	Senior Private Sector Development Specialist
Abuja	**World Bank**	Sustainable Development	Abimbola Adubi	Senior Agricultural Specialist

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