

AFRICAN REVIEW OF MONEY FINANCE AND BANKING



“GIORDANO DELL’AMORE” FOUNDATION

Centre for Assistance to Financial and Credit Institutions of Transitional Countries

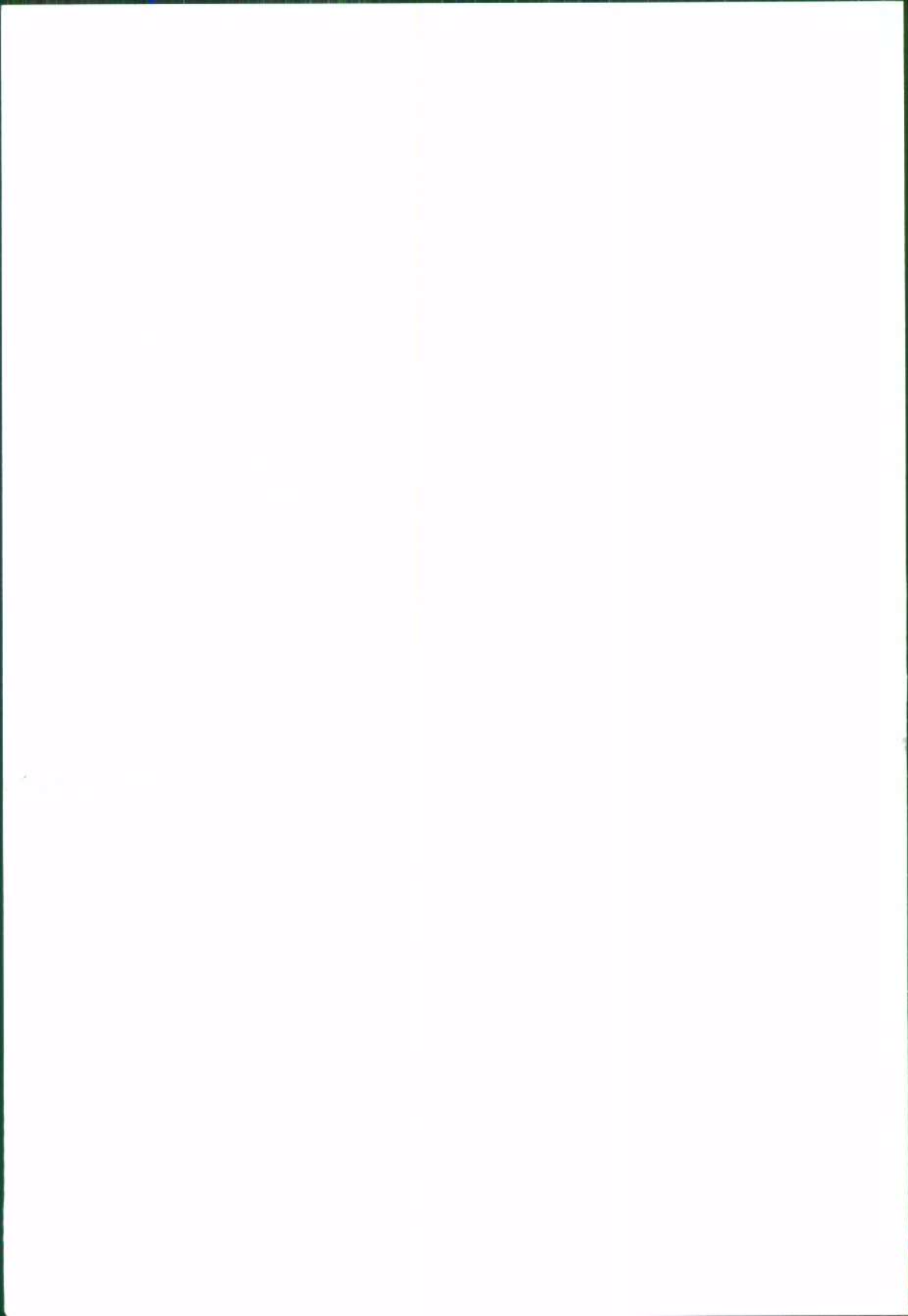
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FINANCIAL LIBERALISATION AND THE GROWTH OF THE CAPITAL MARKET IN NIGERIA

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1. Introduction

Following from the works of McKinnon (1973) and Shaw (1973), the role of finance and more importantly the consequences of a financially repressed economy on the development process has generated a lot of research interest. Finance, it is argued, could act as a catalyst in the process of development but if repressed could become fetters or obstacles to the growth process. Although some recent works (Dornbusch and Reynoso 1993; Cottan and Cavallo 1993) have tended to place more emphasis on the relevance of a favourable financial environment for the attainment of the growth objective, financial liberalization aimed at removing the lid on interest rate ceilings, enhancing competition in the financial sector, improving the functioning of securities markets, increasing the transparency of financial transactions and harmonizing and simplifying standards of prudential supervision have continued to remain common policy prescriptions for developing countries undergoing economic reforms (Versluysen 1988).

In 1987, the authorities in Nigeria commenced an extensive reform of the financial system as part of a structural adjustment programme. Reforms involved the liberalization of interest rates, promotion of a market-based system of credit allocation, and enhancing competition and efficiency in the regulatory and supervisory framework. Attempts have been made at evaluating the success of this programme particularly as it devolves on the banking sub-sector (Ikhide and Alawode 1993; Ikhide and Alawode 1995 and Ojo 1993). However, no attempt has been made at evaluating the success or failure of this programme as it affects the capital market.

Thus, the objective of this paper is to assess the impact of financial liberalization on the growth of the capital market in Nigeria. Specifically, the paper will assess the impact of reform policies such as interest rate deregulation, privatization, debt conversion programmes, regulation and taxation on the traditional, institutional and asset-pricing characteristics of the capital market in Nigeria.

2. An Overview of the Structure of the Capital Market

The capital market in Nigeria can be divided into two-the securities segment and the non-securities segment. The non-securities segment consists of Savings Banks, Mortgage Banks, Development Banks and Insurance companies. Their instruments consist of term loans, mortgages and leases. Mention must be made here of the development companies which complement the activities of the development banks. Their history in most cases predate the establishment of some of the development finance institutions;

they supply loan and equity capital for financing new and existing enterprises. They cater for a wide range of industrial groups in both the public and private sectors. They started in most cases as regional development boards and have undergone different stages to become what they are today - public investment companies. At their inception, they were mainly established to administer and use funds made available to the marketing boards in such areas as agriculture and industry. Most popular among them today are the Northern Nigeria Development Board, the Odua Investment Company Limited and the Central Investment Company Limited, serving respectively the north, west and east. Their investments in banking, commerce and manufacturing run into millions of Naira. Data is not readily available on the activities of these finance institutions but nevertheless they constitute an important segment of the capital market (Okigbo, 1991).

The capital market proper consists of the securities segment. It is instructive to distinguish between the fixed interest securities market (debentures and bonds) and the shares market in Nigeria. The bonds market is dominated by the government whereas private enterprises dominate the shares market. Only a few debentures are issued by the private enterprises. The conventional sources of funds for the purchase of fixed-interest securities are households, individuals and enterprises, particularly financial institutions - commercial banks, savings institutions and the Central Bank.

In general, two groups of transactors place their securities in the market - the government (Federal State and Local governments) and the incorporated enterprises. Government securities dominate the market.

There were a number of legislative actions which supported the market for government securities. Among these were the Income Tax Management Act 1961, which conferred tax-free status on Pension and provident Funds that maintain at least one-third of their total investment in government securities (50 per cent for those approved after 1961); the Trustee Investment Act, 1962 which empowered Trustees to invest in government stocks and industry securities, provided such securities are quoted on the stock exchange; since very few industrial securities are quoted on the stock exchange, the Trustee Investment Act 1962, had the ultimate effect of forcing all Trust funds to be invested in government stocks; and the Insurance (Miscellaneous Provisions) Act 1964 which required insurance companies to invest at least two-fifths of all funds from risk premium in Nigerian securities, one-quarter of which must be held in government stocks. It is not surprising therefore that given these measures and the frequency of issues of government bonds, the demand for government loan bonds comes mainly from financial institutions such as commercial banks and savings-type institutions.

Up to the late 1970s, public issue of industrial securities were very limited. Issues of equity shares were more substantial than industrial bond issues both in terms of values and frequency of issue. Two main events, the indigenization exercise executed through the Nigerian Enterprises Promotion Decree (NEPD) 1972 and 977 and the privatization programme under the current structural adjustment programme, have served as the main impetus for the growth of the equity market between 1972 and 1990. A total of 57 equity securities valued at N146.31 million was traded on the new issues market between 1971 and 1977. Of this, 31 securities valued at N66.18 million were new issues. The privatization of erstwhile government concerns also gave a fillip to the growth of the market. In 1990 alone, the Technical Committee on Privatization and Commercialization (TCPC) on behalf of the Federal government of Nigeria offered to the public a total of 563,373 million ordinary shares worth N653.639 million in seven companies for privatization. All the issues were oversubscribed. Thus, over the year the size of the primary market has grown in absolute terms (volume) as well as in value. The issue of government stocks has dominated total issues while in relation to transactions in the market, the situation has not changed. In terms of values, government stocks also constitute the hub of the market. However, in terms of the number of listings and of the transactions, private (industrial securities) have been growing rapidly in importance particularly in the past decade.

In terms of institutions, the capital market consists of a primary market which is dominated by the investment (merchant) banks, brokers and dealers and ventures capitalists and a secondary market dominated by the Stock Exchange. While the primary markets' main concern is with the primary issues, the secondary market handles already existing issues of the Exchange.

Following from the report of the Barback committee set up in 1959 to advise on the desirability of setting up a stock market in Nigeria, the Lagos Stock Exchange, now known as the Nigerian Stock Exchange (NSE) was established in 1960.

The growth of the market was rather slow in its early years with only six equities quoted as at the end of 1966 in contrast to three in 1961. An average of one equity was quoted for these years except for 1964 and 1965 when no equity was quoted at all. Government stock comprises the bulk of listing with 19 such securities quoted on the Exchange in 1966 as against just five in 1961; an average of three stocks were quoted for these years. On the whole a total of 60 securities was quoted at the end of 1966 with a total transaction value of N18.1 million, government and industry securities accounting for 90.1 per cent and 9.9 per cent respectively. Many factors contributed to the low level of performance in these early years. Some of the identified factors include the lack of infrastructural facilities, the

low level of awareness about the role of a stock market, and the reluctance of many companies to seek quotation on the exchange. Some of these problems still linger in the capital market today thirty years after the establishment of the stock exchange. In terms of number of dealings, however, industry securities were more active, starting with 92 (27.5 per cent) and 242 (72.5 per cent) for Government Securities and industrial securities respectively in 1961 and stood at 204 (21.4 per cent) and 748 (78.6 per cent) for Government Securities and industrial securities at the end of 1966.

For a stock exchange to mobilize savings effectively and channel such savings to the most deserving sectors while promoting national integration and unity, it has to develop suitable strategies for access to savers and users of funds spread across the length and breadth of the country. The decision to decentralize the exchange in 1977 clearly had this objective in view. The establishment of trading floors in Kaduna and Port Harcourt was quickly followed by a decision of the Council of the Exchange on certain policies aimed at dispensing relevant supporting facilities, for example, the licensing of new stockbroking firms specifically for the new trading floors and the encouragement given to existing firms to appoint agents and attachés located in the hinterland. From the Securities and Exchange Report, there were only 20 stock-broking firms in Nigeria as at 1985. The figure was 21 in 1986, and as of 1992 the number had risen to 140. Similarly, from the three trading floors at Lagos, Port Harcourt and Kaduna, new trading floors were opened in Kano 1989, Onitsha 1990 and Ibadan in 1990. The exchange has dual listing requirements; firms listed on the second-tier market are subject to less stringent listing conditions. The dual listing facility is designed to accommodate small and medium scale enterprises.

The Securities and Exchange Commission is the main regulatory agency in the capital market. It licenses stockbrokers and issuing houses, and investigates cases of abuse and 'insider' trading. Presently, there exists in the capital market a network of 140 brokers, investment bankers and brokerage firms.

3. Theoretical Framework

The deepening of financial systems occurs largely through the expansion of the range and use of interest-bearing instruments together with the diversification of financial markets and financial infrastructure. The observed relationship between per capital income and financial depth indicates that expansion of the formal financial system is part of the development process (Popiel 1994).

The implication of this for the growth of the capital market is threefold. For the non-securities segment of the capital market, programmes of financial adjustment that permit

specialized development banks to mobilize deposits from the public by bringing interest rates up to the market levels will reduce their excessive dependence on government and foreign aid, and hence enhance their performance (Vogel 1988). Second, and more importantly, such a programme will help to tilt the unhealthy balance between debt and equity financing that presently characterizes the portfolio of enterprises in developing countries and by so doing help to strengthen the system. Liberalization of interest rates will tend to discourage debt financing by firms and encourage equity financing.

Corporate financing strategies have evoked a serious controversy in the literature. While the works of Modigliani and Miller (1958) and recently Molho (1986) would want to 'delink' corporate financing from interest rates and thus establish that there is no relationship between the cost of capital (interest rate) and the financing mix (the debt-equity ratio), most recent works, Sundararajan (1987) and Bhattacharyay (1988), establish a direct link between administered interest rates, the debt-equity choice of firms, the overall cost of capital and real interest rates. According to Sundararajan, the debt-equity ratio is important because the overall cost of capital to investors - which influences fixed investment, its efficiency, and profits - can be expressed as a weighted sum of the opportunity cost of bank debt and that of equity, with the weights depending on the debt-equity ratio. Given this relationship; the multiplier effects of changes in the cost of bank-debt (i.e. the interest rates) on the overall cost of capital and hence, on investment incentives and the productivity of capital, depend on, among other things, the share of debt in investment financing, and on the induced adjustments in this share, and on the cost of equity. What this implies is that there exists an optimum debt-equity mix for firms which firms will strive to obtain so as to minimize their cost of capital. In other words, at high interest rates, the debt-equity ratio is low. The desired debt-equity ratio will be positively related to the implicit interest subsidy on credit from the regulated financial markets.

The analysis of Sundararajan (1987) together with the works of Cho (1986), Cottani and Cavallo (1993) provide the basis for our expectations about the behaviour of firms when interest rates are liberalized. If we are able to observe a lowering of the debt-equity ratios of firms after liberalization, we will be able to reach some tentative conclusions about the role of high interest rates as a rising cost of capital which firms will strive to run away from and therefore resort to equity financing as an alternative source of financing. And the more the magnitude of capital that is intermediated by banks, the less liberalization of interest rates, in the face of moral hazard and adverse selection, can guarantee an efficient allocation of capital. Certain firms are going to be rationed out of the credit system, and the necessity for the existence of a capital market becomes compelling. Either way, firms will

reduce their debt-to-equity ratios. This will reverse the trend in most LDCs. The heavy reliance on debt has adverse macro-and micro-economic consequences. At the macro level, it has caused severe debt servicing implications. More importantly, for LDCs undergoing financial sector reforms, it has contributed to the occurrence of bank insolvencies. Increasing interest rates in the face of moral hazard and adverse incentive effects, has led to a blooming of bad and doubtful debts in the portfolio of banks as bank customers who have got bank loans at high interest rates are not necessarily those who can pay such loans. High interest rates will tend to force firms to go to the capital markets to raise equity finance rather than borrow from the banks and thus provide long-term debt financing and risk capital through the issue of bonds and shares. This is indispensable for long-term economic growth.

One area that has received the greatest attention in recent times is the expected effects of financial liberalization on the efficiency with which the capital markets allocate credit. The removal of the ceiling on interest rates is expected to eliminate credit rationing. The pioneering work of Cho (1986) adapted by Fry (1988) and Cottani and Cavallo (1993) have demonstrated that where banks' lending activities are characterized by imperfect information and moral hazard, it might be unrealistic to assume that when ceilings on interest rates are removed, excess demand for credit will be automatically removed. Although the demand for credit is inversely related to its cost, the supply does not increase indefinitely with the rate of interest. It is true that banks are likely to increase loans to their customers when the expected revenue increases, but at high interest rates expected revenue could fall. Stiglitz and Weiss (1981) attribute this to two effects. First, the incentive effect causes borrowers to assume more risky projects when the cost of credit increases. Second, an adverse selection effect operates when the banks' most reliable clients are discouraged by high interest rates and are replaced by less solvent debtors, who, because of a lack of perfect information about their credit standing, are indistinguishable from the others. At high interest rates, banks expect revenue to begin to fall because new increases in interest rates are insufficient to compensate for revenue losses that result from the borrower's insolvency. If the rate that equalizes the supply and demand for bank loans is greater than the rate of interest at which bank revenue is maximized, banks will be forced to ration credit. The problem of efficiency in credit allocation arises because of the possibility that, given several groups of borrowers among which inter-group differentiation is possible, intra-group differentiation is difficult and imperfect information results in some groups being totally excluded from the capital market, although the expected returns of the excluded groups' investments may be higher than those of the groups that get credit.

On this basis, Cho (1986) argued that interest rate liberalization in an economy in which all capital is exclusively intermediated by banks does not guarantee an efficient allocation of capital. A well-developed capital market must also exist for efficiency to occur. The nature of bank loans in the face of adverse incentive and adverse selection given imperfect information makes it possible for banks to avoid lending to groups it classifies as risky. If the banks had adequate information on each borrower, it can decide on what borrowers it wants to entertain and who in the group constitutes a risk. In equity financing, this group will be able to get financing. This is because equity is free from adverse selection and moral hazard effects while debt finance is subject to them in the presence of asymmetric information (Cho 1986). To liberalize successfully, a well-organized stock market is indispensable.

Financial liberalization will enhance financial competition. Promoting competitive efficiency in LDCs through the chartering of banks to the utter neglect of non-bank financial intermediaries has implications for efficiency and solvency. Oligopolistic bank structures tend to be more stable, but less efficient; for the maintenance of the stability of the payments system, there may be a need to trade-off stability for efficiency. The development of money and capital markets possess two important features of competitive markets - a greater number of participants and greater ease of entry. The third, transparency and information flow, is a function of appropriate legislation which could come through reforms. Thus, the development of capital markets could foster competition and hence efficiency (Popiel 1990).

Finally, a liberalization of the capital market will enhance the use of indirect techniques of monetary management. Indirect monetary management has a lot of advantages over direct control, in terms of effectiveness and efficiency, the avoidance of undesirable side effects etc. However, indirect monetary management will only function properly where the financial market is efficient and since efficiency is the goal of financial liberalization, initiating a programme of financial reforms is in the right direction.

4. Financial Sector Reforms: Policy Measures as They Affect the Capital Market Segment

Attempts at reforming the financial sector in Nigeria have fallen under five main headings - reform of the financial structure, monetary policy reforms, foreign exchange reforms, liberalization of capital movement and capital market reforms. The details of these measures have been discussed elsewhere (Ojo 1993; Ikhide 1995). Since the emphasis in this work is on the capital market, we will concentrate on those reform

measures that have impacted more on this segment of the financial sector.

Capital market reforms are in two parts. First, we have measures undertaken as part of the structural adjustment programme which had some impact on the capital market. Among such measures are:

- i. Interest rate deregulation.
- ii. Privatization: the privatization of erstwhile public institutions which started under the reform programmes.
- iii. Debt conversion programme: debt swaps were first developed as part of the restructuring programme of Nigeria's external debt which reached a crisis proportion with the structural adjustment programme. Debt to equity swap has had some impact on the capital market since they are a form of securitization.

Second, there are reform measures aimed principally at the capital market. These include:

- a. Deregulation of the capital market: an inter-ministerial committee was set up in 1991 to examine ways of carrying out the proposed deregulation. The main focus is the ongoing deregulation of securities pricing with the intention of stimulating competition and enhancing investment in the market.
- b. The reconstitution of the Securities and Exchange Commission.
- c. Tax policies: the reduction of the withholding tax on dividend, and the reduction of the fiscal burden with respect to the proceeds and yields from debt and equity, although much still needs to be done with regards to the latter.
- d. Regulatory measures: these include measures aimed specifically at alleviating the difficulties involved in listing disclosures and checking insider trading. We now examine some of these measures which we consider crucial in the development of the capital market in more detail.

4.1 Privatization

Privatization (meaning the sale of state-owned enterprises) has been an important element of the reform programme in Nigeria. The objective of privatization in Nigeria as elsewhere includes the need for improved management, efficiency and performance of affected enterprises, reduced government financial burden, increased funding of infrastructures and other facilities, enhanced economic growth and development and instilling of market discipline.

No doubt, one major policy in the Structural Adjustment Programme (SAP) that has impacted immensely on the capital market in Nigeria is privatization. The report submitted by a Committee set up to examine the modalities for the privatization exercise, led to the

enactment of the Privatization and Commercialization Decree No. 25 of June 1988. The Committee categorized all affected enterprises into two schedules. Schedule 1 has a list of 67 companies to be fully privatized, 25 companies for partial privatization and 18 banks and automobile manufacturing companies in which the existing Federal Government holdings were to be retained. The enterprises under this schedule covered a wide range of activities including finance, petroleum, construction, agriculture, tourism, manufacturing and service sectors. Schedule 2 contains 14 and 11 Federal Government enterprises for partial and full commercialization respectively. The Technical Committee on Privatization and Commercialization (TCPC) now known as the Bureau for Public Enterprises (BPE) which came into existence with the decree was given wide powers to implement the programme. Five basic methods have been used to effect the same of enterprises in Nigeria. These are public offer, private placement, management/employee buy-out, deferred public offer and asset sale. By far, public offer of securities has been most popular. It was expected that this method will enhance capital market development and achieve a government objective of widespread shareholdings in the country. Under the programme, the TCPC (as of December, 1992) had offered for sale share equities held by the Federal Government in 55 enterprises. The proceeds from these dis-investments by the public sector amounted to N3.3 billion at the end of the period (CBN 1992). In terms of listing, 27 new companies have so far been quoted on the Nigerian stock exchange. To cater for the policy of widespread share/ownership, preference was given to small investors in the allotment of shares. The guidelines for allotment was such that all small applications are first allotted in full and thereafter the other applicants are allotted. Also, no one individual was to receive more than 5 per cent of the shares sold unless the issue was unpopular and therefore undersubscribed. The privatization exercise has stimulated capital market activities immensely. This has been accompanied by increased equity market capitalization. Trading activities have also improved.

4.2 Debt-Conversion Programme

By the middle of the 1980s, Nigeria's debt crisis had become unmanageable. In spite of a series of debt refinancing and rescheduling agreements, the debt service burden remained high and, given a worsening external trade situation, it became clear that in addition to the measures adopted in the structural adjustment programme, an innovative debt management strategy was clearly needed in order to cope with the demands imposed by a crushing external debt service/repayment.

A market-based debt reduction scheme, Debt-Equity Swap programme styled Debt

Conversion Programme, was initiated in 1988 by the Federal Government of Nigeria with the following objectives in mind:

- i. reduction of Nigeria's external debt by reducing foreign currency denominated debt in order to alleviate the debt service burden;
- ii. improvement of the economic environment in order to attract foreign investment;
- iii. serving as additional incentive for the repatriation of flight capital;
- iv. stimulation of employment-generating investment in industries with significant dependence on local inputs;
- v. encouragement of the creation and development of export-oriented industries, thereby diversifying the export base of the economy; and
- vi. increasing access to appropriate technology, external markets and other benefits associated with foreign investment.

One underlying objective that is crucial for our analysis and emphasized in the above-stated objectives is the need to stimulate foreign investment as a means of reducing the debt stock and enhancing growth.

Four categories of transactions are eligible under the Debt Conversion Programme: first, conversion into cash for the purpose of making a gift/grant to Nigerian non-profit making entities such as educational institutions, research centres, charitable organizations, religious bodies, charitable trusts and foundations; second, conversion for acquisitions of Naira denominated debt instruments issued by the CBN, such as Naira notes, development stocks and other local debt instruments designed specifically for the programme; third, conversion into equity, preference shares, debentures and loan stocks of existing companies for the purposes of acquisition, expansion, recapitalization of existing projects and/or companies in Nigeria and for financing investment in privatized enterprises; finally, conversion for investments in completely new projects.

The performance of the Debt Conversion Programme has been quite encouraging. As at the end of December 1992, the cumulative number of applications received since inception in August 1988 totalled 225 valued at US \$3712.1m. At the end of 1992, external debt stock valued at \$760.9m had been redeemed since the inception of the programme, while the discount received through the programme amounted to \$360.6m. Additional inflows through commissions from the project was close to \$8.9m as at the same period. Since its inception, a total number of 107 projects attracting a cumulative sum of N3837.1m had benefitted from investment under the project at December 1992. A breakdown of the projects shows that the following sectors, manufacturing (41 per cent), agriculture and agro-allied (9.6 per cent), building and construction (14.0 per cent), hotel and tourism (13.5

per cent), gifts and grants (12.1 per cent), mining and exploration (2.3 per cent), services (0.2 per cent), and others (6.8 per cent) have been the main recipients of funding from the project (CBN, Annual Report 1992). Thus, in addition to reducing the nation's external debt, the programme has attracted foreign investment and induced inflow of foreign exchange. A few of the firms under the programme have used proceeds from the conversion to acquire equity shares as a result of the Nigerian privatization exercise-equity swaps. There have also been less of debt for debt conversion where funds realized from the conversion were invested in government treasury bills. A greater part of the projects (93 per cent) went into private sector financing with about a third of this in already existing companies for the purpose of resuscitating operations through the purchase of new machinery and equipment and employing more hands, capitalization restructuring, expansion etc. Judging by the number of conversions in the pipeline, the debt-conversion programme could be a veritable source of alternative financing for a debt-strapped nation like Nigeria and could impact significantly on the development of the capital market.

4.3 Interest Rate Deregulation

The structure of interest rates in Nigeria prior to the commencement of the structural adjustment programme showed clearly that the financial system was severely repressed. Between 1960 and 1986, the level of interest rates was fixed by administrative fiat. Hence, the Central Bank of Nigeria fixed both the lending and deposit rates. The minimum rediscount rate (MRR) averaged about 4.5 per cent between 1970 and 1980. Within this period, the inflation rate was consistently above 20 per cent except for the years 1972, 1973 and 1980 (3.2, 5.4 and 9.9 per cent respectively). Again, between the period 1981-85, the MRR stood at an average of 8.6 per cent and the average inflation rate was about 16.9 per cent. Thus, predominantly, real interest rates were negative for the period 1970-1986 (Table 9). Since the prevailing interest rates could not cope with the inflation rate, disintermediation occurred. Other negative consequences included a high demand for credit far above the existing supply. Loanable funds became scarce as there were inadequate funds to meet up with the demand by loan users at the concessionary interest rates. Even the preferred sectors found it difficult to access funds with the result that most banks could not comply with the prescribed credit policy guidelines. One consequence of the excessive credit demand was credit rationing. Those who got loans were not necessarily those who had the most efficient investment projects to finance but those who had special relationships with the bank managers. The low interest rate thus resulted in inefficient production.

This was the situation in 1986 when the structural adjustment programme began. A system of controlled interest rates gave way to a deregulated system. The Central Bank introduced a market-based interest rate policy in 1987. Initially, a partial deregulation was attempted but by August, all rates became market determined. The purpose of interest rate liberalization was to enable banks to charge market-based interest rates and thus to enhance their savings mobilization and resource allocation efforts. Throughout the period, however, the central bank continued to fix the MRR. Thus, the MRR was initially fixed at 15 per cent in January 1987, but reduced to 12.75 per cent in December of the same year. On average, the savings deposit rate of Commercial Banks stood at 11.5 per cent while the interest rate paid by merchant banks on the 90-day funds stood at 15 per cent. The prime lending rate of commercial and merchant banks were on average 18.0 and 20.5 per cent respectively while their corresponding maximum lending rates were 19.2 and 22.0 per cent.

In 1989, again in an attempt to curtail the rate of growth of money supply, the MRR was raised to 13.25 per cent. Disparities in the interest rate structure of banks in their competitive bids to mobilize deposits forced the rates of interest to rise. Interestingly, much as banks were prepared to raise their lending rates, deposit rates were kept at very low levels. The practice of borrowing from the commercial banks to take advantage of bidding in the foreign exchange market put further pressure on the lending rates. Although the Central Bank towards the end of 1989 fixed the spread between the saving and lending rate at 7 percentage points, and the margin between the prime and maximum lending rates for each bank at 4 percentage points, this did not put a stop to the excessive rise in lending rates in the economy. Most firms under this condition found it extremely difficult to borrow from the banking system to finance both their working capital requirements and the requirement for expansion.

In the same year, the Central Bank in furtherance of the flexible interest rate policy, introduced an auction-based system for the issue of treasury bills and certificates, both money market instruments. The instruments started to carry market-based yields as a prelude to the introduction of open market operations later in the liberalization programme.

Banks were again under pressure (moral persuasion) to observe a maximum lending rate of 21 per cent and a minimum deposit rate of 13.5 per cent in 1991 and 1992 in the face of astronomical increases in interest rates. The average of the commercial bank savings deposit rate rose from 14.0 per cent at the end of 1991 to 16.8 per cent in December of 1992. Time deposit rates within the same period rose from 20.2 to 29.8 per cent. There were variations, however, from bank to bank with merchant banks posting

higher rates. The average on the rates on 90-day deposits rose from 18.2 per cent at the end of 1991 to 39.0 per cent in December 1992 while the average prime lending rate rose from 21 to 44.4 per cent.

These sharp increases in nominal interest rates turned out to be a gain to the capital market. Prime lending rates in commercial banks rose from about 12.5 per cent in 1986 to about 29.8 per cent in 1991, an increase of close to 138.4 per cent. This was a major contributory factor to the search by some corporate bodies for alternative sources for long-term funding. Prior to the deregulation of interest rates, many corporate bodies borrowed short-term funds to finance their long-term projects - a clear example of a mismatch of term commitments. When interest rates were reviewed upwards, the companies involved could neither service old debts nor borrow new funds. In such circumstances equity finance would have cushioned them from the adverse effects of the rising rates. It took the deregulation exercise to drive this advantage of equity as against debt finance home. When interest rates are held below market levels, thus reducing the cost of borrowing, they tend to encourage debt financing instead of equity financing and could stultify the growth of the equity market.

Not much evidence has been provided in this area of the capital market in Nigeria. In a survey of 105 quoted companies in Nigeria between 1983 and 1993, Omole and Falokun (1994) provided some evidence in his regard. Because of the relevance of this study to our work, we take a little more space to outline the main points in their study. The survey covered 105 active quoted companies in Nigeria covering all major industrial classifications excluding Banks and Insurance companies. The selected companies also covered the SITC (productivity) sector such as Food, Beverages, Tobacco, Chemical, Machinery and Transportation. The study's focus was on choices of debt and equity options of financing as well as the decisions relating to financing strategies by companies particularly with financial liberalization. Some key financial variables from the balance sheets of quoted companies such as firm's profits, investment, turnover, long-term debts, and share capital (authorized, issued and fairly paid) were employed for the analysis.

The study undertook an analysis of the debt-equity profiles of the selected companies. The authors found that the effects of interest rate liberalization on the financing strategies of firms is quite significant as there was an appreciable decline in the debt-equity ratios of the firms. This decline implies that "with financial liberalization firms actively relied on and utilized the capital market for raising additional funding, thereby giving some impetus to the activities of the stock market" (Omole and Falokun 1994: 32). In addition, they found out that liberalization has positively affected the turnover, gross profits and investment of

firms since these have increased after liberalization. They concluded that interest rate policy can be used to enhance both the corporate performance of industries and the growth of the capital market. We have summarized their results for easier assessment in line with our before-and-after framework on Table 8 in the appendix. In place of the two periods we have dealt with so far, we have divided our period of analysis on Table 8 into three to coincide with three interest rate regimes: 1983-86, 1987-90 and 1990-93 coinciding respectively with the period before the deregulation of interest rates when real interest rates were negative, the initial period of deregulation when interest rates were moderately negative and the period after the initial deregulation when interest rates became strongly negative again as a result of high inflation. If we classify debt-equity ratios for the different sectors as high, moderate and low (based on sector-specific performance), we will observe that the two strong periods of high debt-equity ratios coincided with the periods of negative and strongly negative interest rates. This relationship will require further empirical investigations before any conclusions can be drawn from here. But what stands out clearly from Table 8 is the fact that for the initial period of interest rate deregulation (1987-1990), debt equity ratios in firms under consideration fell considerably. Taken together with our earlier results, we can conclude that more of the quoted firms actively approached the stock market with interest rate deregulation.

4.4 Regulatory Framework

The objectives of regulation can be summarized as the need for the maintenance of stability in the financial system, the sustenance of confidence in the securities market, and the protection of the investing public. More often than not, considerations in this regard are focussed on three main areas of regulation. These are registration of enterprises, disclosure of information and checking insider abuses. Although there are other aspects to the issue of regulation, these three will receive our attention in this study as we consider them very crucial to capital market development.

The Securities and Exchange Commission (SEC) is the apex regulatory institution in the Nigerian capital market. Emphasis will be placed on the SEC Decree No. 29 of 1988 which is the main instrument of operationalizing the functions of the Commission. The decree has three main objectives:

- i. to protect the interest of investors and thereby enhance their confidence in the capital market;
 - ii. to ensure orderly, fair and equitable dealings in securities; and
 - iii. to promote the growth and development of the Nigerian capital market.
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The hallmark of the 1988 Decree is that apart from its wider coverage, unlike its predecessors, it provides civil and criminal liabilities for contravention, and empowers the Commission to suspend or revoke the registration of erring market operators while vesting the responsibilities for approval of mergers, acquisitions and all forms of business combinations on the commission. Statutory regulations all over the world carry the force of law and are therefore more generally adhered to than non-statutory regulations. To facilitate its regulatory responsibilities, the SEC prepared a comprehensive set of rules and regulations to guide all operations of the securities market bearing in mind the requirements for the maintenance of confidence of the investing public in the securities market through the avoidance of frauds and malpractices in securities dealings. Specific regulatory functions include:

- (a) Registration: registration has been described as the hallmark of regulation. Through registration, the fitness or otherwise of an applicant to do business in the capital market is ascertained and the worthiness of the instrument for offer is assessed. To enable its assessment of prospective registrants, the Commission requires comprehensive personal and business data on applicants and reserves the right, following proper scrutiny of information supplied to it, to grant or deny registration. For each type of registerable activity, the Commission has formulated some minimum requirements which must be met by applicants. These requirements are not static but are subject to review from time to time. For instance, the minimum capital base of a specific registerable activity could be increased in the light of experience. Similarly, the minimum qualification of individuals wishing to engage in a given registerable line of business could also be reviewed when necessary. In line with the practice all over the world, the Commission requires issuers of securities to file prospectuses with it along with other registration documents. A complete set of application forms for a corporate registrant also includes forms for its sponsored persons. Registration fees for classes of registration are payable upon submission of application to the Commission. The Commission requires all registrants to abide by the provisions of the Securities and Exchange Commission Decree 1988 and the rules and regulations made thereunder, as well as the Allied Matters Decree 1990, if they have to continue to operate in the market. To ensure continuous compliance with these registration requirements, the Commission reviews periodically the status of the registrants. Any registrant not in fulfilment of any of its registration requirements is therefore appropriately sanctioned. The Commission also registers stock exchanges and their branches, registrars, investment advisers, securities dealers and their agents in order to protect investors
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from unscrupulous market operators and their agents as well as to maintain proper standards of conduct and professionalism in the securities business. Registration of securities, issuers and market operators entails filing of appropriate registration forms with the Commission. There are also withdrawal forms to facilitate exit process.

The Commission grants registration with due regard to certain perspectives which are very crucial in the attainment of its objectives. These are the security, integrity and operational perspectives. Under the security perspective, security agents are required to pronounce on the criminal records, if any, of individuals being sponsored and promoters of security business companies so as not to unwittingly introduce criminals that may detract from the impeccable operations expected in the securities business. A failure of this test terminates the registration of any sponsored individual. In a similar vein, disclosures under oath are obtained to elicit facts on bankrupts, companies in undischarged and past receivership as well as liquidation under notice, or other compromise arrangements.

For the integrity perspective, great reliance is placed on past employer's testimonial and where this is adverse, the bid for registration is terminated. It is usual to grant registration if at least two nominated referees' reports, the past employer's testimonial and banker's opinion are favourable. As for the operational perspective, critical issues of capital adequacy, professionalism of both the organization and the principal officers and the number of times and the gravity of past offence(s) by either that had evoked market or professional discipline are examined. Operating capital is kept under review to enable market operators to perform effectively and efficiently. Currently, the following minimum paid-up capital amounts are considered adequate for the underlisted capital market business: Investment Advisers (corporate) - NO.5m; Broker Dealer, Investment Advisers and Portfolio Managers - N2.5m; Issuing Houses, Investment Advisers and Portfolio Managers -N5 m; Registrars - N2.5m and Trustees - N5m. In view of the length of time it takes to grant final registration (60 days minimum), it is not unusual to grant registration in two stages; a provisional registration is granted in 30 days subject to the satisfactory of some initial requirements and a final registration may follow at the end of 60 days where an applicant is found to have satisfied all registration requirements (Akingbohngbe, 1994).

- (b) Surveillance. As the watchdog of the capital market, the Commission constantly monitors market activities to forestall manipulative and other illegal practices. The surveillance activities cover trading on the Nigerian Stock Exchange in order to ensure fair and equitable dealings in securities, free from manipulative and other abusive
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devices while the inspectorate undertakes frequent on-the-spot checks of the books and operations of registered market operators. Such exercises do enable the Commission to ascertain whether or not operators are keeping adequate records, and working within the norms of the market (such as the maintenance of proper business conduct). Any suspected breach is referred for investigation and enforcement actions taken where necessary.

The use of privileged information could be harmful to the stability of the capital market. In this regard the decree specifically requires the stock exchange to protect the "integrity of the securities market against abuses arising from the practice of insider trading". The surveillance activities of the Commission is not limited to the secondary market; the primary market is also well-monitored to detect among others any misuse of investor's funds.

- (c) Investigation. The Commission investigates all reports of violations and suspected violations of the securities law. Information leading to investigation usually emanates from the surveillance activities of the Commission or from complaints by investors or operators and other members of the public. Investigation can also arise from press publications on issues affecting the capital market, tips and indeed from rumours. Usually, investigations are carried out privately. In the course of investigation, the Commission may call for information pertinent to the case from any corporate body or individual under its regulatory purview, suspected to be directly or indirectly connected with the case.
 - (d) Enforcement. The Commission has the responsibility of ensuring that participants in the market comply with the securities laws. It has the powers to institute penalties (sanctions) and remedial actions if a violation is established. Where an offender refuses to comply with the provisions of the law, the Commission may institute legal action to force compliance. Action which the Commission can institute against violators does depend on the severity of the offence and includes suspension or revocation of registration, disgorgement of proceeds from illegal transactions, fines and reverting of action. The Commission in 1993 as part of its enforcement function set up an Administrative Hearing Committee for purposes of fair hearing of cases relating to allegations of violations of the securities laws, professional misconduct, manipulation and fraud of the market process.
 - (e) Rule Making. Rule-making is the formulation and review of rules and regulations for the market as occasions may demand. In formulating or reviewing rules, the Commission is guided, inter-alia, by experience and emerging developments in the market and
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the financial system, as well as by the macroeconomic environment, and deficiencies in existing rules. The opinion of market operators is sought from time to time in this regard.

- (f) *Timing of Issues.* SEC is also empowered to control the time and amount of issues in order to avoid demand on the primary market beyond its absorptive capacity at any point in time. This role attained prominence particularly during the second stage of the indigenization programme. When proposed issues clustered, it was the duty of the Exchange to stagger such issues bearing in mind the capacity of the economy.

Other regulator duties of the exchange as contained in the decree included the Review of Accounts of Enterprises covered by the SEC decree, Approval and Management of Mergers and Acquisitions, Approval of State and Local Government Bonds Issues and the Authorization of Unit Trust Schemes (SEC1994).

It is yet too early to assess the performance of the securities market in the light of these recent legislative reforms. What cannot be denied, however is the fact that this new attempt at legislation in the wake of financial liberalization is far more embracing than had hitherto been attempted in the history of the capital market in Nigeria.

4.5 Taxation

Taxation is another important consideration in the development of the capital market under liberalization.

The major forms of taxes that are relevant for our consideration are:

- (i) *Company Income Tax.* The rate of company income tax has remained stable over the years fluctuating between 40 and 50 per cent. The rate of tax was fixed at 45 per cent in 1949 but reduced to 40 per cent in 1958. In 1975, profits less than N6,000 were tax-free, profits in excess of N6,000 but less than N10,000 continued to be taxed at 45 per cent. The rate was increased to 50 per cent in 1979, but reduced to 45 per cent the following year and has remained at that level till date except that from 1982, company income tax took the form of maximum of 2 per cent based on turnover or 45 per cent of taxable profit whichever is higher. The turnover tax was, however, abolished in 1985. As at present there is no differential tax treatment for listed as against other companies. However, a lower rate of 20 per cent was required of small and medium sale enterprises with turnover not exceeding N0.500 billion in the year of assessment, if such companies are in the agricultural and manufacturing sectors or in the mining of solid minerals.
 - (ii) *Dividends.* Withholding tax on dividends was for a long time fixed at 15 per cent but in the spirit of liberalization this was slashed to 5 per cent in 1992. However, this was
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again increased to 10 per cent in 1994. The reduction did not benefit foreign investors. (iii) Capital Gains Tax. In 1992, Capital Gains Tax was extended to movable assets including motor vehicles.

From the above, it is clear that the current tax policy does not contain any clearcut incentive for the development of the capital market. In particular, the increase in withholding tax is a disincentive to investment in capital market especially to small investors since for the banking system it would only apply where the investment is above N5,000. This differential in application of tax to incomes arising from the two markets discriminates against the capital market.

5. Empirical Analysis

A lot of methodological issues have been raised with regards to the evaluation of the performance of reform programmes in developing countries. The two methods that are commonly cited in the literature are the 'before-and-after approach' and the 'modified-control group' approach. Summarily, the 'before-and-after approach' has been criticized on the grounds that it is difficult to determine whether observed changes in our variables of interest can be ascribed to the policies under observation or to other factors implicitly held fixed or not considered in the analysis. The approach fails to answer the question as to whether observable changes would have occurred even without the policies under consideration. The modified-control group approach is essentially an econometric approach. It allows estimates to be made for the marginal contributions of programmes for given initial conditions and exogenous shocks. Since the approach allows for the recognition of other factors unrelated to programmes that also affect performance and adjusts for the counterfactual policy stance that would have prevailed in the absence of the programme, it is a better approach for approximating programme performance (Elbadawi et al 1994).

In spite of its apparent usefulness over the 'before-and-after approach', we have not used this approach in this study for the following reasons. First, the econometric approach will not be of much assistance given the nature of our analysis which is essentially qualitative. Second, even where we decide to run an econometric programme we are likely to be hamstrung by the number of data points. Third, the modified-control group approach is more helpful when assessing programme performance across a group of countries which is not our main objective in this study. Hence, we have relied mainly on the use of the before-and-after approach.

The traditional, institutional and asset-pricing characteristics of the capital market are

gauged by how well it performs its capital mobilization function, the depth of the securities market, movements of securities prices and market participation or more generally pattern of equity distribution. The new issues ratio is used as measure of the capital mobilization capability of the capital market. Thus, we compute the new issues ratio as a proportion of such variables as Gross Fixed Capital Formation, Gross Domestic Product, Total Gross Domestic Savings and observed the trend before and after the commencement of reforms. The results are summarised in Table 1.

The depth of the securities market or its market capitalization is chiefly a function of the number of securities listed and the volume of each security made available for trading. Here we examine such variables as the total number of securities quoted on the stock exchange, the value and volume of transaction, securitization (that is, the raising of finance in the form of marketable debt rather than in the form of loans), market capitalization of quoted companies and the turnover of securities transactions.

Market capitalization as an index of the growth of the stock market is crucial for our analysis. When the new issues are computed as the ratio of market capitalization, they reflect the issue capacity of the market over time. Computed as a ratio of GDP, it serves as an index of the contribution of the stock market to development. Also, the value of stock market transactions could be computed as a ratio of total stock market capitalization, as an indicator of the stability of shareholdings in listed companies, and stock market capitalization could be related to the volume of physical capita in the economy. Each ratio has a unique interpretation. The movement in security prices could be helpful as a barometer of the health of a stock exchange particularly in a low inflationary situation. If the correlation between this index and inflation is low, a high correlation between the index and market capitalization could be indicative of a strong non-inflationary growth in the capital market.

This study is limited to the period 1970-93. This gives us an opportunity to do a trend analysis for before the liberalization (1970-85) and after the reforms (1986-93) and thus be able to account for discernible trends. The data used for this study are essentially from the publications of the Securities and Exchange Commission, and the Nigerian Stock Exchange. We also made use of publications from the Central Bank of Nigeria, the Federal Office of Statistics and the International Finance Corporation.

6. Summary of Major Findings

The major focus of this study has been on the provision of evidence from the Nigerian economy on the performance of the capital market during the ongoing deregulation

exercise. We can summarize our main findings as follows:

- (i) The capital market witnessed some substantial growth in the area of capital mobilization during the period of liberalization. Tremendous improvements were recorded in all our measures of capital formation. First, by relating new issues to GDP, we observed that though low by international standards, this ratio has increased from 1.1 per cent for the period 1971-75 to about 1.6 per cent for the 1986-90 period, a period within our framework that coincides with the implementation of the adjustment programme. As a percentage of gross national savings, new issues have also increased from barely 6.2 per cent to about 17.5 per cent during the same period. Three sources of such increases were identified in the study: the improvement in new listings in the capital market during the period of observation. The number of listed companies during the period 1972-92 increased from 93 to 153. Second, there was an intensification of activity of already listed companies in the stock market which by our indirect measure also increased during this period; and third, through the activities of the non-securities segment of the capital market, the last two traceable to the likely impact of the deregulation of interest rates.
- (ii) Our measure of the depth of the capital market revolved around the concepts of securitization and market capitalization. Securitization has grown rapidly in the period of adjustment reflecting the growing awareness by corporate institutions to raise finance more in the form of equities rather than debt. Our analysis shows that in addition to the fact that the number of securities in the market increased from 163 in 1981 to 251 in 1992, there was a discernible structural change. Government stocks are gradually being supplanted by industrial loans and equity in the finance of investment and more importantly this structural change occurred between the period 1986-92 (Table 2). Also, the value and volume of transactions have also increased significantly over the period and the relative improvement in the performance of industrial securities over government stocks both in value and volume terms is worthy of note (Table 3 and 4). One major problem that plagued the securities market in Nigeria prior to financial liberalization was the relatively low average value of transactions in industrial securities, a reflection of the relative unimportance of the corporate sector in the financial market. The structural change that occurred during the reform programme may have implications for the erstwhile narrowness or shallowness of the market.
- (iii) Our results confirm that the ratio of new issues to stock market capitalization has declined over time and has remained almost constant for the period 1979-92. This is in conformity with our expectation for a growing capital market reflecting growing

increase in listing and increasing importance of equity financing. The impact of stock market growth on economic development as measured by the ratio of market capitalization to GDP may be minimal as is more often than not the case but for our purpose this ratio has shown an increasing trend over the years rising from about 1.8 per cent for the period 1972-75 to 7.8 per cent for the 1986-90 period. The year 1971 is an outlier year and is excluded from this computation (Table 5). Although our analysis showed that the turnover rate is low (a reflection of the fact that in Nigeria people still buy stocks to hold), the concept of the turnover rate as a measure of the stability of stockholding in the economy has to be viewed against the background of the distribution of transactions per listed security since there is the tendency for transactions to be concentrated on the most sought-after securities. For instance, according to the SEC Annual Reports for 1992, the 20 most active equities in the Nigerian Stock Exchange, with a total of 64,155,263 ordinary shares changing hands during the year, accounted for 60.68 per cent of the aggregate volume of shares traded during the year. The top 20 companies controlled about 70 per cent of the total value of shares in the exchange. Finally, our results on the ratio of stock market capitalization to gross fixed capital formation showed a value that ranged from 41.1 per cent in 1980 to about 119.6 per cent in 1985, indicating that listed companies have contributed immensely to the growth of productive capital in the economy.

- (iv) We computed a simple correlation between the stock market index and the inflation rate in Nigeria which returned a figure of 0.46. However, we observed a close correlation between the index and market capitalization (0.97) which is indicative of the vertical growth of the market. Given a correlation coefficient of 0.96 for market capitalization and listings which reflect the horizontal growth of the market and taken in conjunction with other information in this study, we could conclude that the stock market has grown both vertically and horizontally in the past decade.
 - (v) We also observe that during the period of deregulation, the stock market has attracted the inflow of both portfolio and direct investment. Portfolio investment which had virtually stagnated in the economy prior to the structural adjustment programme has been reawakened. Two measures, the correlation coefficient between stock market index and portfolio investment and the ratio of net portfolio investment to GDP were computed and the results were quite instructive. The first recorded a figure of 0.72 could be interpreted to mean that portfolio investment as a source of financing could serve as a means of reducing the cost of own capital for listed companies (Table 6).
 - (vi) We indirectly provided information on the fact that the liberalization of interest rates
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- made debt finance more expensive for corporate firms who had to go to the capital market to raise funds as evidenced by the increased tempo of activities in this market. We also provided additional evidence to this effect from a study which was recently done for the Nigerian economy which showed that there was an appreciable decline in the debt-equity ratios of firms quoted on the stock exchange during the period of reforms. This decline put side by side with the results of our earlier analysis particularly with reference to improved listing and securitization in the capital market during the period of interest rate liberalization would tend to confirm that firms actively relied on and utilized the capital market for raising additional funding this period (Tables 7 and 8).
- (vii) The institutional characteristics of the capital market in this study focussed essentially on regulation and taxation. Decree 29 of 1988 is the main instrument for the regulation of the capital market during the period of adjustment. Our analysis reveals that this decree is quite comprehensive as it covers all aspects of capital market operations. Moreover, it shows an improvement over previous decrees not only in terms of its coverage but also in the provisions of penal codes for defaults which in extreme cases could lead to delisting. The Decree also gave more muscle to the Securities and Exchange Commission as the main regulatory agency in the capital market. With regard to taxation, the current tax policies do not contain enough incentives for the development of the capital market. Apart from the recent increases in the withholding tax on dividends, the use of tax policies as an instrument of coercion for firms that are big enough but have refused to go to the capital market or as an incentive for firms that are just getting enlisted is minimal. Moreover, the discrimination in tax policies against the capital market would rather serve as a disincentive to operators in the market.

7. Conclusion

This study has attempted to examine the impact of the series of reform measures undertaken in the Nigerian economy particularly in the financial sector on the growth of the capital market. Specifically, the impact of privatisation, debt conversion programmes, interest rate deregulation and changes in the regulatory framework on the institutional and asset-pricing characteristics of the capital market were investigated using a 'before-and-after' policy measure approach.

The study established that the capital market in Nigeria witnessed some growth during the period of the reform as measured by the improvements in the institutional and asset-pricing characteristics of the market. However, it is difficult to ascribe these changes to any well-thought-out or planned programme of financial liberalization focussed on the capital

market. It is tenuous to attempt to link the results of increasing securitisation or market capitalisation to the deregulation of interest rates. Programmes such as privatization and debt conversion though part of the overall structural adjustment programme do not strictly fall within the ambit of financial sector reforms. And one is not surprised therefore that with the decline in the number of enterprises to be privatised and a fall in the tempo of debt conversions, the growth in the capital market has become unsustainable as witnessed by the period 1990-93 in our analysis. What this calls for therefore is the formulation of a programme of reforms specifically directed at the capital market given the crucial role of this segment of the financial system in economic development.

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Appendix

Table 1: New Issues Ratio 1971-1992

	1971-75	1976-80	1981-85	1986-90	1991-93*
New issues/GFCF	6.6	3.8	5.5	16.7	6.8
New issues/GDP	1.1	0.9	0.9	1.6	0.4
New issues/GNS	6.2	4.3	12.7	17.5	5.6
New issues/Sec Mkt	12.7	11.3	3.3	10.3	6.0

Source: Computed from The Securities and Exchange Commission Annual Reports: Various Issues.

Table 2: Listed Securities, Stock Brokers and Listed Companies on the Exchange

Year	Number of Listed Securities				No. of stockbrokers	Listed companies
	Govt. Stocks	Industrial Loans and Bonds	Equities	Total		
1981	56	14	93	163	12	93
1982	57	18	93	168	13	93
1983	61	25	92	178	16	92
1984	56	27	92	175	18	92
1985	57	28	96	181	20	96
1986	58	29	99	186	23	99
1987	54	31	100	185	33	100
1988	51	35	102	188	43	102
1989	47	40	111	198	61	111
1990	43	43	131	217	80	131
1991	40	57	142	239	110	142
1992	36	62	153	251	140	153

Source: Central Bank of Nigeria Research Department Occasional Paper No. 8, Statistical Appendix (August 1993)

Table 3: Dealings on the Nigerian Stock Exchange

Year	No. of Firms Quoted ⁽¹⁾	Dealings on Govt. Stocks ⁽²⁾	Dealings in Industrial Securities ⁽³⁾	Total Deals ⁽⁴⁾	2 as % of 4 ⁽⁵⁾	3 as % of 4 ⁽⁶⁾
1971-76	28	229	1047	1276	17.9	82.0
1976-80	51	248	2836	3084	8.0	91.9
1981-85	96	272	14237	14509	1.8	98.1
1986-90	168	166	24541	24707	0.7	99.3
1991-93	174	36	39079	39115	0.1	99.9

⁽¹⁾Industrial Securities include Industrial Loans and Equities

Figures are averages of period values

Source: Computed from SEC Annual Reports; Various Issues

Table 4: Value of Transactions (period averages)

Year	Govt. Stocks (Nm)	Growth Rate	Industrial Securities (Nm)	Growth Rate	Total Value (Nm)	Growth Rate
1971-75	92.6	-	1.4	-	94.0	-
1976-80	221.5	2.1	3.4	2.8	224.9	57.8
1981-85	285.5	5.7	11.2	45.8	296.7	24.1
1986-90	315.8	2.1	53.0	66.2	364.1	18.5
1991-93	55.4	-470.0	204.5	74.0	259.9	-40.5

Source: Computed from Central Bank of Nigeria Statistical Bulletin Vol 4 No 2 Dec

Table 5: Market Capitalisation

Year	Mkt Cap	Primary Market	Secondary Market	Share Issue Market (Value in Nm)	Market Cap/GDP (%)	Share Issue Mkt/Mkt Cap	Growth Rate of Mkt Cap
1971	40.7	87.0	36.2	123.2	20.1	3.02	315.9
1972	169.3	70.6	27.2	97.8	2.1	0.57	15.1
1973	194.8	134.3	92.4	324.5	1.6	1.66	39.9
1974	272.6	76.7	50.7	127.4	1.4	0.46	40.5
1975	313.9	451.5	63.7	515.2	1.4	1.64	15.3
1976	458.3	441.3	111.9	553.2	1.7	1.20	46.4
1977	618.5	478.7	180.0	658.7	1.8	1.06	34.9
1978	1071.5	220.0	189.7	409.7	2.9	0.38	73.2
1979	2631.6	238.6	254.4	493.0	6.0	0.19	145.5
1980	4464.2	378.8	388.7	766.7	8.7	0.17	69.6
1981	4970.8	455.2	304.8	760.0	9.7	0.15	11.3
1982	4025.7	533.4	215.0	748.4	9.7	0.18	19.0
1983	5268.0	448.5	397.9	846.4	9.2	0.16	30.8
1984	5514.9	159.7	256.5	416.2	8.6	0.075	4.7
1985	6670.7	817.2	318.6	1135.8	9.2	0.17	20.9
1986	6794.8	835.0	497.9	1332.9	9.3	0.19	1.8
1987	8297.6	450.7	382.4	833.1	7.6	0.10	22.1
1988	10020.7	399.9	133.4	533.3	6.8	0.053	20.7
1989	12848.8	1629.66	570.0	2199.0	5.7	0.17	28.2
1990	16348.4	9964.5	238.0	10202	6.0	0.062	27.2
1991	23124.9	1869.9	234.4	2103.4	7.1	0.091	41.4

Source: SEC Annual Reports Various Issues and CBN Statistical Bulletin

Table 6: Net Direct Investment, Net Portfolio Investment and Stock Market Growth in Nigeria

Year	Net Portfolio Investment (Nm) (1)	Net direct Investment (Nm) (2)	Stock Index (3)	Market Capitalisation (Nm) (4)	1 as % of 4 (5)	2 as % of 4 (6)	1 as % of Total External Debt (7)
1986	151.6	735.8	130.8	6794.8	2.2	10.8	0.4
1987	4351.3	2452.8	133.1	8297.6	52.4	29.5	4.3
1988	2611.8	1718.2	139.0	10020.8	26.0	17.1	2.0
1989	-1618.8	13877.4	152.5	12848.7	-12.6	108.0	-0.6
1990	-435.2	4686.0	170.5	16358.4	-2.6	28.5	-0.1
1991	-594.9	6916.1	192.9	23124.9	-2.5	29.9	0.1
1992	36851.8	14463.1	227.2	31272.5	117.8	46.2	6.7

Source: Nigeria's Balance of Payments; Central Bank of Nigeria, Statistical Bulletin Vol 4 No 2, December 1993

Table 7: Debt-Equity Ratios of Quoted Companies by NSE Classification

<i>Classification</i>											
No/NSE Sectoral Classes	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993
Automobile and Tyre	49.74	1.85	59.84	60.55	26.78	63.73	52.54	55.71	167.1	97.76	79.07
Breweries	10.50	5.97	4.27	6.26	5.58	5.12	8.71	5.70	5.38	5.67	5.53
Building Materials	73.17	58.33	38.75	35.65	70.08	30.69	34.50	33.83	13.63	35.90	25.94
Chemical Paints	28.70	32.42	26.23	24.24	16.62	10.78	9.76	11.31	10.59	9.69	14.79
Commercial	115.3	202.70	258.93	264.21	56.22	61.44	42.04	22.34	17.46	27.41	23.66
Computer and Office Equipment	40.83	39.25	27.18	11.94	8.82	7.75	21.33	2.44	3.47	18.70	28.19
Conglomerates	42.14	35.98	31.91	24.60	23.15	15.88	21.36	41.73	36.71	19.25	14.78
Construction Engineering Technology	5.29	5.16	5.16	5.32	20.27	9.48	181.24	155.73	107.60	103.50	66.11
Food, Beverages and Tobacco	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Footwear	33.33	19.87	22.80	10.24	16.52	21.09	24.98	24.98	27.97	41.92	28.82
Industrial and Domestic Products	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Machinery	28.96	19.27	12.70	45.92	120.21	88.64	62.71	62.71	52.52	50.32	66.86
Packaging	13.89	20.39	136.28	76.65	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Petroleum	0.00	253.20	224.44	183.04	41.45	41.45	28.31	28.31	20.62	13.13	13.56
Pharmaceuticals and Animal Feeds	1.62	7.48	6.25	6.98	6.78	6.78	1.31	1.31	0.00	7.28	11.20
Publishing	24.72	21.54	19.77	12.36	17.88	17.88	14.24	14.24	20.08	23.25	14.89
Textiles	231.4	281.5	272.97	52.85	102.78	102.78	64.57	64.57	50.22	14.12	24.12
Second-Tier Securities Market	69.45	39.26	25.59	18.08	44.03	44.03	34.63	34.63	39.29	68.50	71.03
Yearly Sector Average	0.00	14.72	41.44	67.75	85.37	85.37	155.72	55.72	41.80	41.68	36.10
Yearly Sector Average	40.83	58.36	63.92	58.24	34.90	34.90	32.30	34.63	32.34	30.42	27.62

Source: Extracted from Omole and Falokun (1994).

Table 8: Debt-Equity Ratios of Quoted Companies (II)

Non NSE Sectoral Classification	1983-1986	1987-1990	1991-1993
Automobile and Tyre	55.40	49.60	114.60
Breweries	6.75	6.27	5.52
Building Materials	51.40	42.0	25.10
Chemical and Paints	27.89	12.10	11.69
Commercial	210.30	45.52	22.8
Computer and Office Equipment	29.80	10.08	16.78
Conglomerates	33.65	25.53	23.58
Construction	5.21	91.80	92.40
Engineering Technology	0.00	0.00	0.00
Food, Beverages and Tobacco	21.56	20.10	32.90
Footwear	0.00	0.00	0.00
Industrial and Domestic Products	26.70	79.85	36.50
Machinery	61.80	0.00	0.00
Packaging	220.20	31.61	15.77
Petroleum	5.58	4.24	9.74
Pharmaceuticals and Animal Foods	19.59	14.29	19.40
Publishing	259.6	74.51	29.50
Textiles	38.09	40.50	59.60
Second-Tier Securities Market (SSM)	30.90	72.69	39.86
PERIOD SECTORAL AVERAGE	55.52	33.29	30.10
Summary of Ratings*			
No. of Sectors with High Debt-Equity Ratios	8	2	5
No. of Sectors with Moderately Low Debt-Equity Ratios	3	8	4
No. of Sectors with Low Debt-Equity Ratios	4	5	7

The classification is based on sub-period averages in relation to the entire period.

Source: Computed from Table 4.9

Table 9: Interest Rate Structure and the Inflation Rate in Nigeria

Year	Deposit rate (Savings Nominal) (d)	Lending Rate First Class Advances (Nominal)	Spread	Inflation Rate (e)	Real Deposit Rate*
1975	4.0	6.0	2.0	33.9	-22.3
1976	4.0	6.0	2.0	21.2	-14.1
1977	4.0	6.0	2.0	15.4	-9.8
1978	5.0	7.0	2.0	16.6	-9.9
1979	5.0	7.5	2.5	11.8	-6.1
1980	6.0	7.5	1.5	9.9	-3.5
1981	6.0	7.75	1.75	20.9	-12.3
1982	7.5	10.25	2.75	7.7	-0.18
1983	7.5	10.00	2.5	23.2	-12.7
1984	9.5	12.50	3.0	39.6	-21.5
1985	9.5	12.50	3.0	5.5	3.8
1986	9.5	10.50	1.0	5.4	3.8
1987	14.0	17.50	3.5	10.2	3.4
1988	14.5	16.50	2.0	38.3	-17.2
1989	16.4	26.80	10.4	40.9	-17.3
1990	18.8	25.50	6.7	7.5	10.5
1991	14.3	20.00	5.7	13.0	1.2
1992	16.1	29.80	13.7	44.5	-19.6
1993	18.0	35.25	17.25	57.2	-24.9

Real rate of interest computed as $[(1+d)/(1+e)-1] \times 100$

Source: CBN Statistical Bulletin, Vol 4 No 2.

Abstract

Attempts at evaluating the impact of reform measures on the financial sector in Nigeria have often focussed on the banking sub-sector. Recent studies have however been emphasising the relevance of the liberalization of the capital market sub-sector for a successful programme. This work examines the impact of policy measures such as privatisation, debt-conversion programmes, interest rate deregulation, regulatory and taxation reforms on the institution and asset-pricing characteristics of the capital market. The results show that there is a significant improvement in these characteristics for the period immediately following the implementation of the programmes, although this has not been sustained for the post-reform period. Thus, the paper concludes that the observed changes could not have resulted from any internal, fundamental reforms of the capital market per se and suggests the need to design policies that will target this sector of the economy.

LIBÉRALISATION FINANCIÈRE ET CROISSANCE DU MARCHÉ DE CAPITAL AU NIGÉRIA

Résumé

Les efforts pour évaluer l'impact des mesures de réforme sur le sous-secteur financier au Nigéria ont été centrés sur le sous-secteur bancaire. Cependant, des études récentes mettent l'accent sur la pertinence de la libéralisation du sous-secteur du marché de capital comme un programme couronné de succès.

Ce travail étudie l'impact des mesures politiques, à savoir, les privatisations, les programmes de conversion de dettes, le dérèglement des taux d'intérêt, des réformes de réglage et de charges fiscales sur l'institution et les caractéristiques d'évaluation des actifs du marché de capital.

Les résultats montrent que, pour la période suivant de très près la mise en pratique des programmes, il y a une amélioration significative en ce qui concerne ces caractéristiques, même si ceci n'a pas été soutenu pour la période après la réforme.

Donc, l'article conclut que les changements constatés ne proviennent nullement des réformes internes et fondamentales du marché de capital en tant que tel, et suggère qu'il est nécessaire d'élaborer des systèmes visant ce secteur de l'économie.

