

# CBN Recapitalization Policy

*Perspectives, Prospects and Opportunities.*

# Executive Summary.

*CBN's Recapitalization Directives: Strengthening Nigeria's Banking Sector for Growth and Stability.*

*The Central Bank of Nigeria (CBN) has a mandate to regulate the activities of banks and ensure the stability of both the banks and the overall financial system in Nigeria. Since the new government came in, various policies have been announced, some of which include unifying the exchange rates, increasing MPR, and a host of others. It is no surprise that the capital requirement for banks was also increased recently to ensure economic stability, expand banks' credit capacity, and boost investors' confidence in our economy. For most banks, the gap between their current capital base and the new requirement is large, implying the need to raise additional capital.*

*Raising capital is usually a long and tedious process. The bank's directors and shareholders must ensure the bank is well run, as potential investors will carry out their due diligence before investing. Furthermore, the bank's promoters must ensure they use the best and most realistic strategy for complying with this directive. Take for instance, it will be more appropriate for some banks to merge rather than raise equity capital.*

*In all, the bank's promoters should understand the complexities that meeting the CBN requirement will entail, the different strategies that can be applied to meet the target, and their implications for the future of the bank.*



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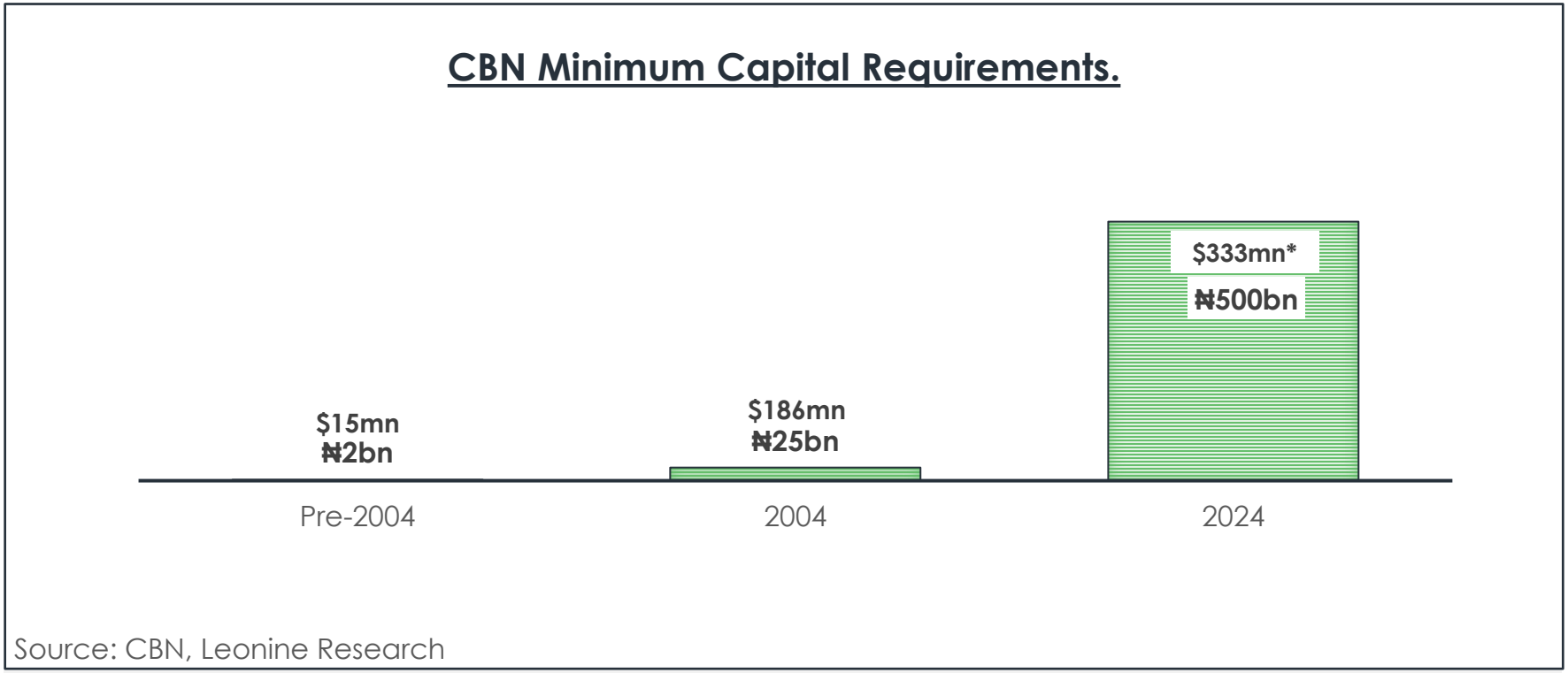


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# Historical & Comparative Analysis of Recapitalization Policies in Nigeria and Africa.

# Past CBN's Recapitalization Policies in Nigeria.

*Over the years, the financial sector has witnessed several recapitalization policies by the CBN, which have led to significant strides in the sector and economy.*




Source: CBN, Leonine Research

*Prior to 2004, the banking sector was characterized by numerous weak institutions, false financial reporting, and impending insolvencies due to the impact of previous military regimes. To address this issues, the Central Bank of Nigeria (CBN) increased the minimum capital requirement for commercial banks from ₦2 billion to ₦25 billion in 2004. This policy direction, released in July 2004, resulted in bank mergers and acquisitions, bringing the total number of banks down from 89 to 25.*

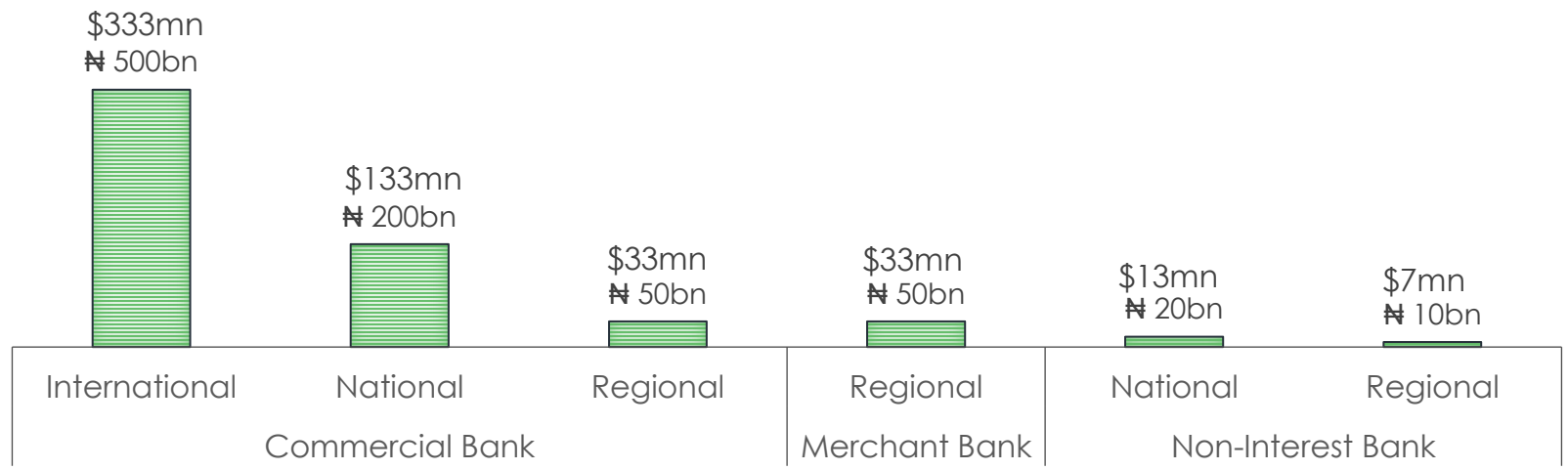
**Note:** * indicates 2024 average exchange rate ₦1,500 (USD/NGN).

# Current CBN Minimum Capital Requirements.

*The recent increase in the minimum capital requirement by the CBN is expected to help Nigeria in its drive to become a $1 trillion economy by 2030.*

*To attain a $1 trillion economy by 2030, the Central Bank of Nigeria (CBN) recently increased the minimum capital requirements of commercial banks from ₦25 billion to ₦500 billion signifying a 1900% increase. This policy is expected to help banks have adequate capital to handle risks, absorb losses, and fuel economic growth. In the same vein minimum capital requirements for merchant and non-interest banks (National and Regional) were raised to ₦50 billion, ₦20 billion and ₦10 billion, respectively.*

## Recent CBN Minimum Capital Requirements for Banks in Nigeria.



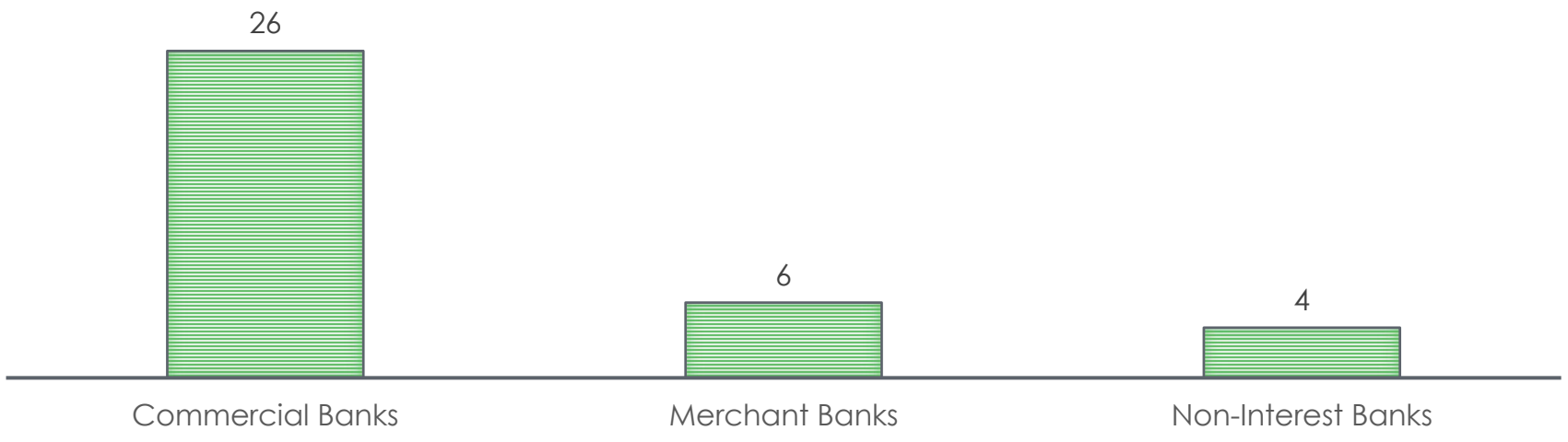

Source: CBN, Leonine Research

**Note:** *Current average exchange rate ₦1,500 (USD/NGN) was used to determine the US Dollar equivalent of capital requirements.*

# Status of Affected Financial Institutions.

*The new capital requirement clearly focuses on commercial, merchant, and non-interest banks, hence creating opportunities for actors in the sector to maximize opportunity and create value.*

**Current Number of Selected Financial Institutions in Nigeria.**

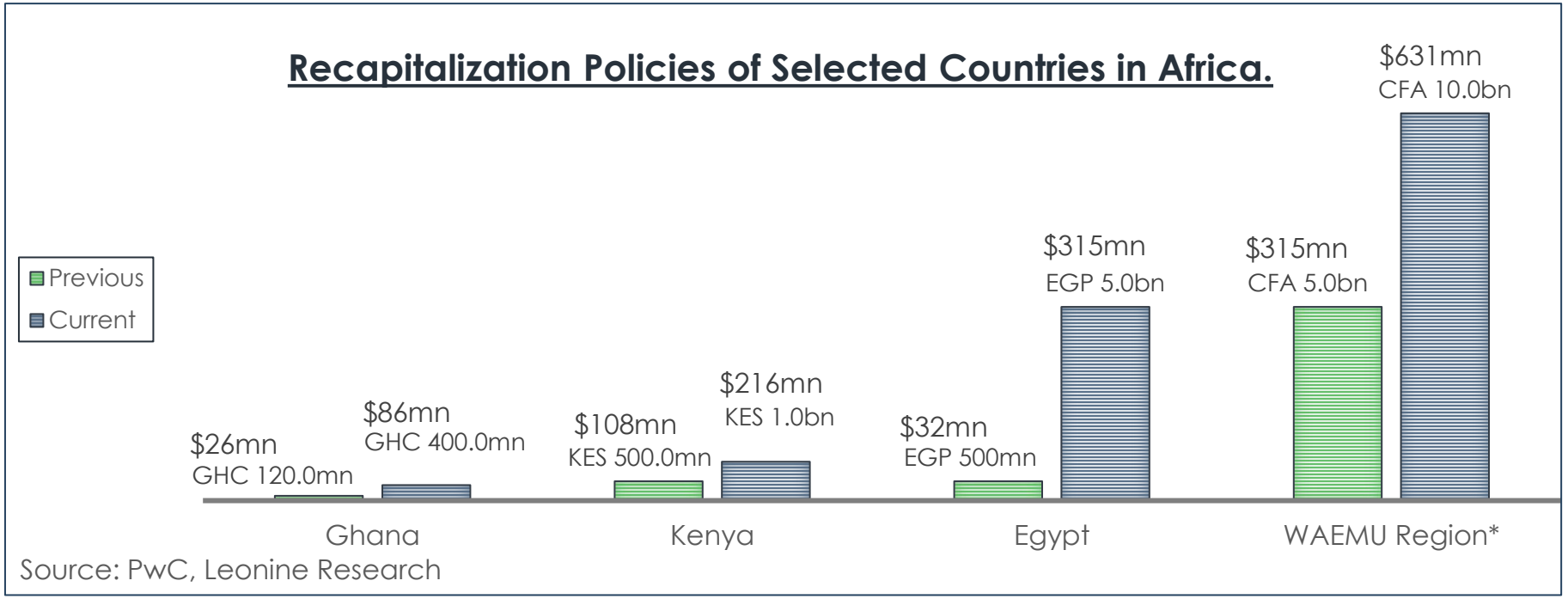



Source: CBN, Leonine Research

*In Nigeria, commercial banks provide a wide range of financial services to individuals and businesses, and they are classified into Tier 1, Tier 2, and Tier 3. This classification is based on the size and scope of service delivery. Merchant banks focus on corporate clients, offering specialized services such as investment banking, corporate finance, and wealth management. Non-interest banks, operating on Islamic principles, provide Shariah-compliant financial products and services, catering to customers seeking ethical banking solutions.*

# Capital Requirements for Banks in Africa.

*Countries in Africa, via their respective apex banks, are trying to keep up with global financial trends and events through raising minimum capital requirements.*




*In Sub-Saharan Africa, apex banks in Ghana, Kenya, Egypt, and Francophone countries have fortified financial stability with countries in the West African Economic and Monetary Union leading the pack in terms of capital requirements. Furthermore, South Africa boasts of a well-capitalized banking sector with a strong focus on risk management that supported economic growth from 2004 to 2009. Concurrently, Kenya enhanced financial inclusion and SME credit access through heightened capital requirements and regulatory improvements in 2012.*

**Note:** * indicates *West African Economic and Monetary Union* (WAEMU)

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# Banking Regulatory Landscape.

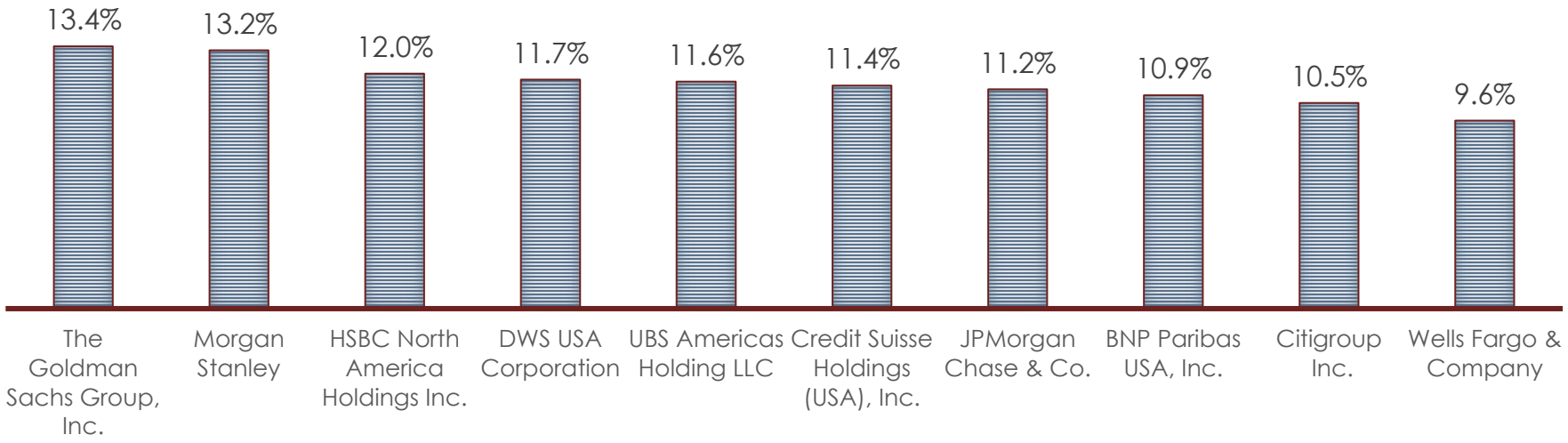


# Feds Influence on Capital Requirements in USA.

*Data have show significant gap in minimum capita requirements of financial institutions in the USA and Africa which is largely attributed to the size of economy and structure of the financial sector.*

*in line with the Federal Reserve Board's capital framework, financial institutions such as bank holding companies and U.S. intermediate holding companies with $100 billion or more in total consolidated assets are required to have a minimum capital of 4.5%. Other important conditions that must be meet include 2.5% Stress Capital Buffer and, in some cases, where applicable a capital surcharge for global systemically important banks of 1%. This clearly shows huge capital requirement in value difference when compared with that of financial institutions in Nigeria and Africa.*

## Capital Requirements for Top 10 Large Banks in USA




Source: Federal Reserve, Leonine Research

# The CBN Financial Sector Regulations/Instruments.

*In Nigeria, several monetary policies have been put in place and regularly reviewed by the CBN to ensure a formidable and stable financial sector.*

### Liquidity management

- The CBN sets a minimum liquidity ratio of 30%.

### Foreign Exchange Risk Management

- Banks are required to limit the Net Open Position of their foreign currency assets and liabilities to 20% of shareholders' funds.



### Corporate Governance & Financial Prudence

- The CBN enforces strict corporate governance standards,
- Banks must keep NPL and LDR below 45% and 65% respectively.

### Capital adequacy ratio

- Tier 1 banks and national banks must maintain a Capital Adequacy Ratio (CAR) of 15% and 10% respectively.

### Monetary policy tools

- The Cash Reserve Ratio (CRR) is 45% for commercial banks and 14% for merchant banks.

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# Recapitalization Strategies and Risk Management.

# Possible Strategies for Recapitalization in Nigeria.

*As players in the financial sector strive to comply with the recent recapitalization directives of the CBN, there are several ways to achieve this, and each has its own unique characteristics and applicability.*

### Raising Funds

Funds can be raised via public offerings, private placements, or rights issues

### Mergers & Acquisitions

To improve efficiency, achieve economies of scale, and enhance market penetration, banks can either acquire or merger with smaller or mid-sized banks.

### License Authorization Upgrade/Downgrade

Upgrade/Downgrade of banking license regional to national or national to international authorization, including non-interest banks.

### Restructuring

Divesting from international markets or reducing overseas investments.

### Exit/Divest

Banks can choose to exit certain markets or divest specific assets as part of their recapitalization strategy.

*Banks can recapitalize through various methods, raising funds (including issuing new equity, rights issues or private placements), engaging in mergers and acquisitions, upgrading or downgrading licenses, or exiting certain markets. Each strategy has distinct advantages and disadvantages, such as raising capital and increasing market reach, but also includes disadvantages like potential shareholder dilution, integration difficulties, and regulatory compliance costs.*

# Recapitalization Strategies Pros and Cons (1/2).

*Financial institutions can recapitalize by raising new capital, mergers and acquisitions, upgrade and downgrade of authorization.*

| Strategy | Pros | Cons |
|---|---|---|
| **Raising New Funds** | • Raises capital and increases equity base.<br>• Allows shareholder loyalty and attracts more equity investors. | • Potential dilution of existing shareholders' ownership.<br>• Costs associated with issuing new shares. |
| **Mergers & Acquisitions (M&A)** | • Stabilizes weaker banks and strengthens the acquirer's position.<br>• Achieves economies of scale and enhances market penetration.<br>• Improves financial sector resilience. | • Integration challenges and regulatory hurdles.<br>• Risk of acquiring non-performing assets.<br>• High costs and complexities associated with due diligence. |
| **Upgrade of License Authorization** | • Opens banks to new markets and expands operational scope. | • Increased risk exposure and higher capital requirements. |

# Recapitalization Strategies Pros and Cons (2/2)

*Restructuring portfolios or exiting certain markets can optimize resource allocation but might reduce competition and increase costs for consumers.*

| Strategy | Pros | Cons |
|---|---|---|
| **Downgrade of License Authorization** | • Reduces capital requirements and compliance burdens. | • Limits scope of operations and potential loss of market share. |
| **Exiting/Divesting** | • Frees up capital, allows focus on core competencies. | • May lead to loss of market share, potential negative perception in the market. |

# Steps to Implementing CBN Capitalization Policy.

*In order for financial institutions to ensure compliance, key stakeholders must develop clear and reasonable plans to properly implement the CBN's recapitalization strategy.*

**Assessment & Planning**
*Identify specific goals such as raising capital, reducing risk, or expanding market reach and develop strategic plan outlining the chosen recapitalization method.*

**Stakeholder Engagement**
*Communicate the recapitalization plan to key stakeholders, including shareholders, regulatory bodies, and employees.*

**Implementation**
*Execute the chosen recapitalization strategies, including issuing new shares, managing mergers or acquisitions, **and restructuring portfolios**.*

**Review & Audit**
*Conduct regular reviews and audits to ensure ongoing compliance and financial stability post-recapitalization.*




**Strategy Selection***
*Evaluate different recapitalization strategies such as issuing new equity, mergers and acquisitions, or restructuring assets.*

**Regulatory Approval**
*Submit the recapitalization plan to CBN and other regulatory bodies for review and approval.*

**Compliance and Reporting**
*Ensure all regulatory requirements and compliance standards are met during and after the recapitalization process.*

**N:B** ** We are equipped to assist you with the strategies outlined in step 2, in terms of financial modeling, business entity valuation, financial due diligence, and capital raising support.*

# Strategic Risk Management in Banking.

*Risk management mitigates market risks, ensures CBN compliance, preserves capital, maintains a positive image, manages credit risk, ensures liquidity, and enhances economic stability and investor confidence.*



***Compliance is critical during and after recapitalization to meet regulatory standards set by the Central Bank of Nigeria (CBN).***

***Utilization of raised capital for ventures beneficial to shareholders, promoting business growth and stakeholder interests.***

***Avoiding damage to reputation and maintaining customer and investor confidence.***

***Implementing robust credit risk management to maintain a healthy loan portfolio is essential during recapitalization.***

***Ensuring the bank can meet short-term obligations without compromising operational efficiency.***

***Protecting against operational risks, including system failures and cyber threats.***

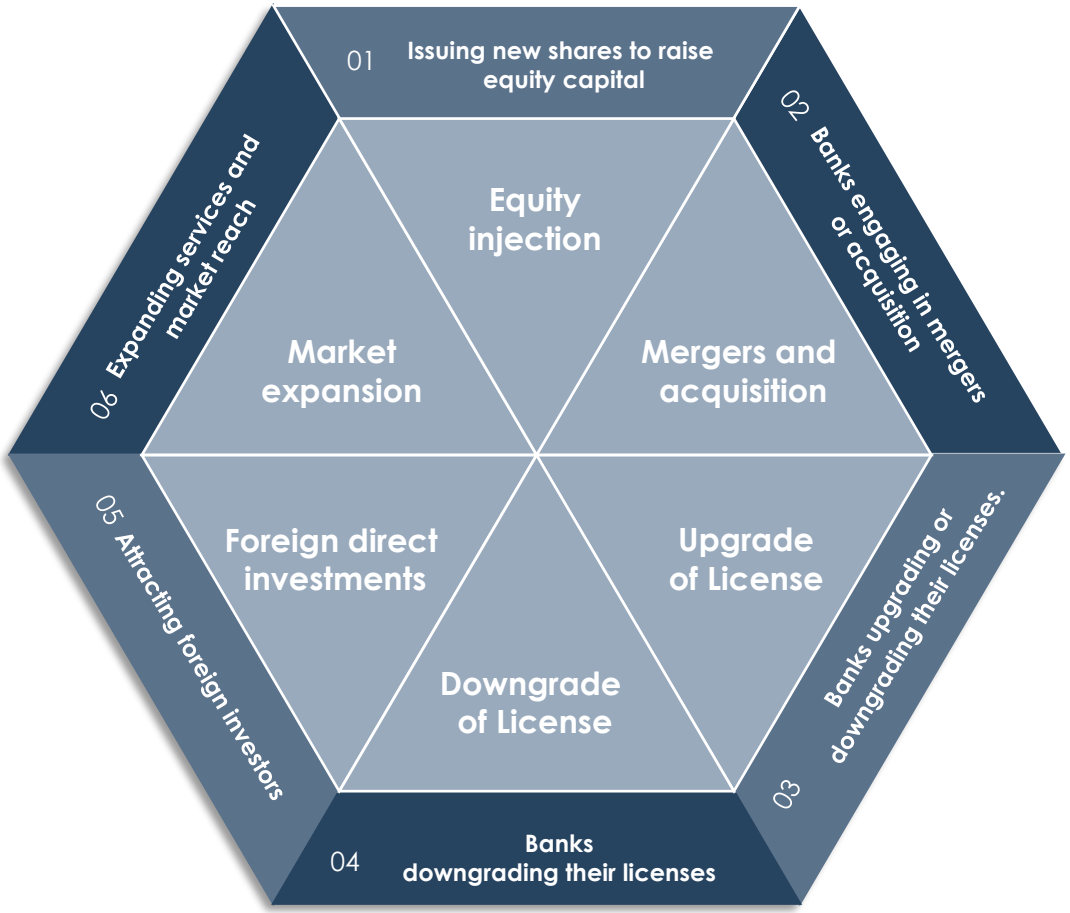
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# Investment Opportunities for Investors and Stakeholders.



# Opportunities for Investors and stakeholders.

*The CBN recapitalization policy creates a strong opportunity for banks to be more resilient.*

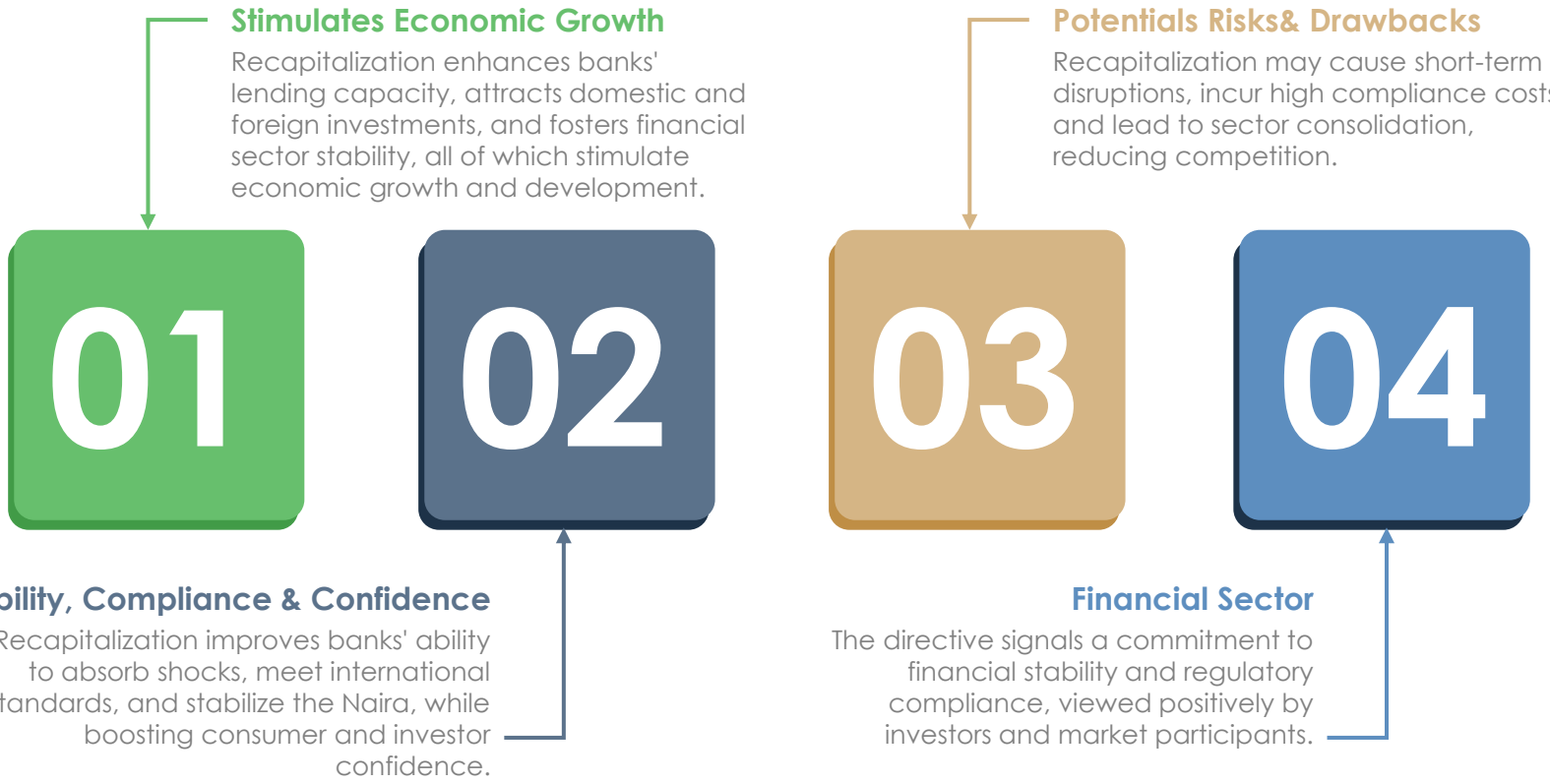



## Opportunities

| | |
|---|---|
| 01 | Existing shareholders and new investors can purchase shares at potentially attractive prices during recapitalisation |
| 02 | Potential synergies, cost efficiencies, improved profitability, enhanced market share, and operational capabilities create opportunities for strategic partners. |
| 03 | Upgrading licenses opens new business opportunities and markets, while downgrading licenses can lead to cost savings and lower compliance burden |
| 04 | Downgrading authorization or licenses leads to a reduction in market each and reduction In capital equity capital. |
| 05 | Offers foreign investors participation in the Nigerian banking sector and the country's economic growth |
| 06 | Expansion into new markets and strengthening of capital base increase future potential returns to investors |

# Recapitalization: Opportunities and Risks.

*The economy, financial sector is expected to benefit immensely from this policy however, there is a need for appropriate consideration and mitigation strategy for identified and potential risks.*



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# Conclusion



# CBN Recapitalization: Impact on Financial Sector.

*The CBN recapitalization policy is part of the strategy to achieve the goal of a $1 trillion economy in Gross Domestic Products by 2030 of the Nigerian Federal Government.*

*The CBN recapitalization policy of 2004 significantly transformed the banking landscape, fostering a more consolidated, robust, and resilient system. These measures have improved lending capacities, attracted investments, and stabilized the financial sector, albeit with challenges such as short-term disruptions and increased compliance costs.*

*Furthermore, in a bid to ensure compliance with the recent recapitalization directives of the Central Bank of Nigeria, this report proposed several possible recapitalization strategies. These recapitalization strategies emphasize the importance of maintaining a positive corporate image, managing credit risk, and ensuring liquidity. The report also highlights the need for financial modeling, business entity valuation, and financial due diligence in supporting capital-raising efforts.*

*In conclusion, the CBN's proactive approach has been and is expected to be instrumental in fostering a stable economic environment, enhancing investor confidence, and positioning Nigeria's banking sector for sustained growth and stability. The policy reflects a commitment to adapting to evolving economic conditions, ultimately benefiting the broader economy.*



# Thank You

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