A light gray world map is centered in the background. The country of Nigeria is highlighted in a solid green color. Overlaid on the map is the main title text in a large, bold, sans-serif font. The text is color-coded: 'What' is yellow-green, 'Nigerian' is green, and 'banks should become' is dark green.

What Nigerian banks should become

This is an abridged version. For a full version, contact us by sending a request to editorial@ciuci.us

Contents

- 3 Background**
 - 5 Customer segmentation**
 - “who truly are my customers?”
 - 7 Corporate governance**
 - “how do we get it right?”
 - 9 Risk management**
 - “openness is key”
 - 12 Operational efficiency**
 - “how can we get it right?”
 - 18 A final word**
-

Background

The Nigerian banking industry recently experienced the greatest shakeup since the consolidation exercise of 2005 with the central banks' announcement of key reforms aimed at promoting growth and sustainability within the sector. After the fallout of the audit carried out by the apex body in mid 2009, the reforms, which include: bank categorisation and the introduction of tenure limits for CEOs and directors, are poised to significantly alter the structure of the industry and usher in a new phase of banking in the country. Only institutions with clear corporate strategies, strict adherence to corporate governance practices and efficient operations will survive this evolution.

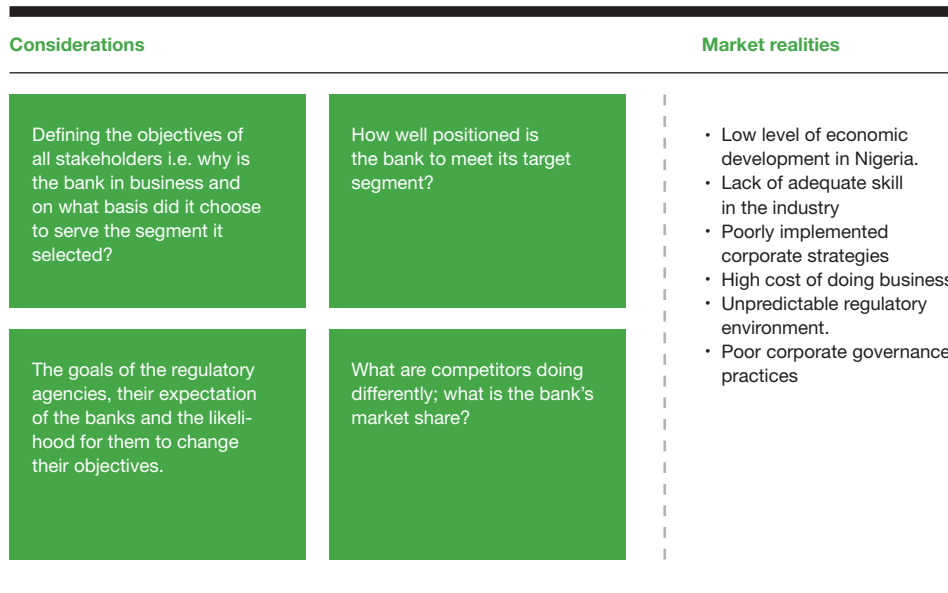
By examining some of the recent reforms/actions initiated by the CBN and their impact on the industry, it becomes clear that banks have no other option but to rethink their strategies and clearly articulate why they are in business.

Table 1: Key actions initiated by the CBN Governor – Sanusi Lamido

S/N	Reforms/Actions	Details	Impact on the banks
1	CBN Audit	<ul style="list-style-type: none"> Discovery of significant liquidity shortages in certain banks leading to the injection of over ₦620 billion into the affected banks. The sacking of eight MDs of the affected banks 	<ul style="list-style-type: none"> Affected banks lost their market share. Change in the rankings in the industry.
2	CEO tenure limits	<ul style="list-style-type: none"> Maximum duration for CEO tenures pegged at ten years, causing some of the chief executives to leave earlier than they had anticipated. 	<ul style="list-style-type: none"> Adequate succession planning has become critical. Change in strategies and a true test of sustainability for banks that suffer from the key man syndrome.¹
3	Bank Categorisation	<ul style="list-style-type: none"> Categorisation of banks by type with different banks having different capital requirements. 	<ul style="list-style-type: none"> It will become imperative for banks to develop sound corporate strategies. A shift from universal banking to specialized and more focused banking.

¹ the tendency for one man, usually the CEO to solely dominate the decision making process of the bank

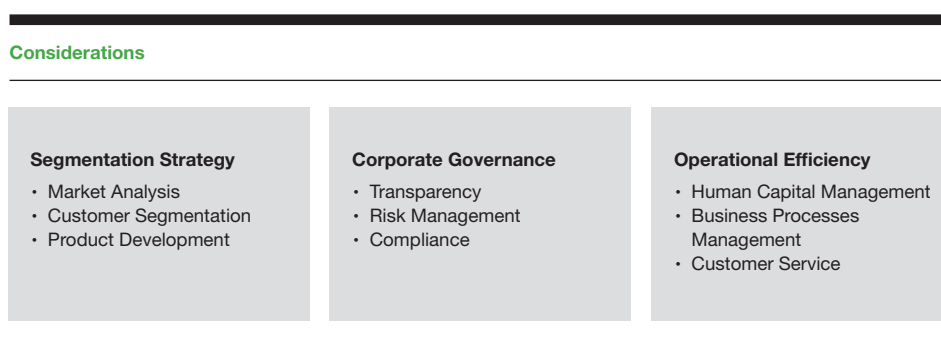
In the processes of rethinking strategies and articulating growth plans, four factors should be considered;



The above mentioned factors can be broadly categorised under the following sub headings:

- Segmentation Strategy – as a fallout of the corporate strategy of the bank
- Corporate Governance – as an internal regulatory mechanism
- Operational Efficiency – as a winning strategy

Figure 2: The Winning Formula



a deviation from core banking operations, which were originally focused on satisfying customer needs. Consequently, a gap was created between customer needs and banking products and services.

Generally, segments in the industry are categorised as either retail or wholesale. The segmentation process requires that these segments are further broken down into smaller sub segments based on specific criteria. Below is an illustration of the process:

Table 3: Possible criteria for segmenting the retail market

Examples of Segment	Segmentation Criteria	Basic considerations in serving segments
Students	Income	Product development
High Net worth	Turnover	IT & other required Infrastructure and support
Individuals (HNIs)	Age	Human capital management
Retirees	Location	Risk management capabilities
Military/Civilian	Gender	Access to data
	Lifestyle	

Splitting customers into segments enables a more detailed study of the segments. At this point, profitability of the customers and their needs are analysed with the objective of ranking segments in order of value (profitability) and benefit to the organisation. The organisation must also consider its capability, in terms of human and material resources in making its decision on what segment to focus on. Capability could imply sales and marketing expertise, infrastructure, governance and other competence related issues. Selecting the segment would then be a function of the size of the segment or the value that can be derived from the segment and the capability of the bank to serve the segment in the immediate and long term. For example, can an investment bank decide to focus on retail banking? Does it have the relevant skills and resources to serve the related customer segment? These are examples of questions that can be asked at this point.

The criteria for determining the category a customer falls into varies from one bank to another. Research has shown that most Nigerian banks do not report their financials by consumer segments, partly because there is no standard method for classifying customers. As a result, it is difficult for a bank to track the profitability of each segment and compare itself with its competitors by the same standards.

Other questions that should be answered following proper segmentation include:

- What are the objectives of the bank?
- What are its key capabilities (strengths)?
- Who are its most profitable customers (customers that the bank makes more profit from and not necessarily the ones with the largest account balances)?
- What are the market opportunities not captured by the bank and what mechanism tracks these opportunities consistently?

Any bank conducting a segmentation exercise should evaluate its internal customers and leverage market studies to glean insights for determining focus. This could lead the bank to divest from some unprofitable segments and build the channels to support the newly identified segments. The process may eventually lead to a change in the bank's organizational structure, as well as its marketing and sales strategies. Segmentation will enable a bank position itself rightly for success as the exercise entails a thorough assessment of the bank's capabilities, a sound evaluation of opportunities available and the development of a strategic roadmap that shows how the bank can get to serve its customers profitably.

Corporate governance – “How do we get it right?”

The role of corporate governance in management of banks has been the subject of much debate, with stakeholders holding differing opinions on how to institutionalise proper corporate governance within banks. Following the reconsolidation exercise in 2005, the CBN set out to establish a corporate governance code to serve as a framework for banks to build their governance systems on. This was done with the objective of mitigating the challenges that came with having bigger banks with greater liabilities, improving public confidence in the banking sector and safeguarding shareholder funds. Highlights of the SEC and CBN Corporate Governance Code for banks include:

Table 4

-
- Separating the roles of CEO and Chairman

 - Improving the quality and performance of board members

 - Merit based holding of top management positions against shareholding based system

 - Transparency and disclosure in all forms of reporting; financial and non – financial

 - Protection of the rights and privileges of all shareholders

 - Definition of the role of the audit committee

Despite the noble attempts made by the regulators towards improving the quality of corporate governance, the infamous CBN audit of 2009 revealed significant corporate governance failures in several banks. It was discovered that chief executives of several banks occasionally flouted laws by approving loans without recourse to laid down loan approval processes. They also allocated funds to projects without proper consultation with their boards and other stakeholders. In some cases, boards were found to be complicit in these malpractices as personal interests were put ahead of the interests of stakeholders. Consequently, the issue remains how to ensure that banks adhere to best practices in corporate governance in order to safeguard the investments of shareholders and enhance the value creation process.

improvements to the business and processes. The overall result is the establishment of a governance superstructure that supports the organisations governance objectives. Consequently, Nigerian banks need to move with the times in which technology has become an integral aspect of business and a critical success factor in the modern age. The goal of institutionalising best practices in corporate governance must be pursued from all possible angles.

Finally, three main conclusions can be drawn:

- Corporate governance must be given priority status by the promoters of the banks.
- Executive management and the board of directors who are primarily responsible for enthroning corporate governance within banks, must take up the challenge and ensure that corporate governance codes are developed in line with regulatory requirements and best practices are developed and strictly adhered to.
- Adopting an integrated approach to corporate governance, risk management and compliance could be beneficial to banks by promoting a governance culture within the bank.

When top level management demonstrate ethical conduct, abide by generally accepted principles and expect no less from employees, they successfully institute moral values and authenticity as a fundamental aspect of the corporate culture and all employees are more likely to embrace those values.

Risk management – “openness is key”

Weak governance, inappropriate incentive structures and poor risk management systems were among some of the main causes of the collapse of the global financial system. Nigerian banks were not left out as most of them failed to adhere to established risk management procedures, resulting in massive loan losses. Most banks were highly exposed to the oil and gas sector and were consequently burnt when oil prices crashed. A significant number of banks were also involved in margin lending which arose as a result of the growth of the stock market. CBN’s special audit report indicated that the total deposit liability of the eight affected banks stood at **₦3trillion** while aggregate non-performing loans stood at over **₦1.5trillion**, representing **61%** of industry total. The full disclosure revealed huge losses of unprecedented proportions in the history of Nigerian banking.

Risk management failures are generally attributed to frameworks and technologies adopted by the banks, but are actually largely affected more so by the executives at the helm of affairs. Some banks gave loans to customers who did not meet guidelines as set by the CBN, but based on ‘perceived gains’ from the businesses and the basis

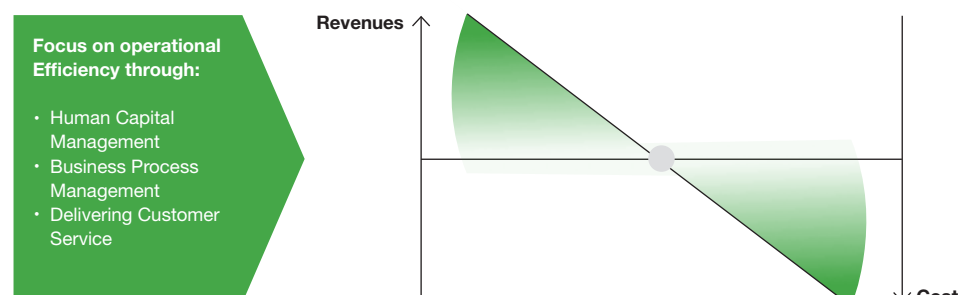
Operational efficiency – “How can we get it right?”

The recent global economic downturn has changed the orientation of businesses globally and especially in Nigeria from focusing purely on turnover (volumes) to efficiency (business optimisation). Companies must now focus on ensuring that fundamental business requirements are taken care of before seeking other lofty objectives (which are often derived after the foundation for growth has been well laid). The need for optimizing business processes has become more obvious than ever before. Most Nigerian banks still have rudimentary processes that negatively affect their ability to serve customers given evolving needs and business conditions. This has resulted in most banks having high cost to income ratios in excess of the industry average 58%. In order to address this, banks must review their processes to identify gaps, determine points of failure and subsequently redesign these processes. Optimised processes provide multiple benefits to banks, leading to better financial performance and an improved reputation. It is pertinent to ensure that skilled persons with the requisite know-how are involved in process design and management as it is the people that play the central role in making systems and processes work.

It is not uncommon to hear customers complain about the quality of service that they receive from their banks. For most, their relationships with account officers are the reasons why they still maintain relationships with their banks. Unfortunately, banks have lost sight of why they are in business. Customers were the premise upon which the practice of banking was founded, for this reason and for the survival of the industry, Nigerian banks need to focus on running efficiently.

After the reconsolidation exercise in 2005, Nigerian banks were awash with funds due to the M&As which produced larger entities and stock offerings which provided capital for investment. They proceeded to expand their operations in line with the regulatory objectives of having bigger and stronger banks, capable of bearing greater risks. In pursuit of these objectives, most banks ignored fundamental issues such as operational efficiency and were consequently caught off guard when the downturn emerged.

Figure 5: Focus on operational efficiency



Nigerian banks have to pay close attention to customer service processes and consider ways to improve them. They need to move quickly with the new trends in technology that eliminate some of the routine tasks. This will provide employees more time to deal with customers.

In a survey conducted before the recent intervention by the CBN, service was one of the top two important considerations for customers.

Figure 8: Top 3 Factors that would prompt a switch in bank (n=440)

- 1st choise
- 2nd choise
- 3rd choise

