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### Public statement on the recapitalization of eight nigerian banks

Central Bank of Nigeria (CBN)

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## CENTRAL BANK OF NIGERIA

### PUBLIC STATEMENT ON THE RECAPITALIZATION OF EIGHT NIGERIAN BANKS

#### **Background**

In mid-2008, the global financial crisis had an adverse effect on both the oil and gas sector and the Nigerian capital markets. A sharp deterioration in the quality of banks' assets followed, which immediately led to liquidity constraints across all the banks. Concerned about the state of some of the Nigerian banks and the overall stability of the financial system, the Central Bank of Nigeria (CBN), commissioned special examinations on all 24 banks in Nigeria. These examinations highlighted significant deficiencies in capital adequacy and liquidity requirements, and illustrated major weaknesses in corporate governance and risk management practices.

#### **Process of Stabilisation**

The examination showed clearly that 9 banks were in a 'Grave Situation', i.e.: Oceanic Bank International Nigeria Plc, Union Bank of Nigeria Plc, Intercontinental Bank Plc, Bank PHB Plc, Afribank Nigeria Plc, Finbank Plc, Equitorial Trust Bank Ltd, Spring Bank Plc and Wema Bank Plc. A tenth bank, Unity Bank, was not deemed to be in grave danger, but still adjudged to have insufficient capital and unacceptable levels of non-performing loans (NPLs). The CBN took proactive steps to prevent further deterioration instead of revoking licenses or handing the banks over to the Nigerian Deposit Insurance Corporation (NDIC). The key initiatives included the injection of N620bn as convertible loan that amounts to Tier II capital into the banks, replacing the Chief Executives and Executive Directors of eight of the banks with competent managers with experience and integrity, introducing the guarantee of the local interbank market to ensure continued liquidity for all banks and guaranteeing

foreign creditors and correspondent banks' credit lines to ensure confidence and maintain important correspondent banking relationships. These initiatives enabled the banks to continue normal business operations and helped maintain the immediate stability of the banking system.

Having averted a crisis in the short run, the CBN, in consultation with the Federal Ministry of Finance (MoF) and other Nigerian regulators, devised a strategy for restructuring, recapitalising and bringing the banks to a "safe harbour". The CBN's priority, in all its actions, was to protect the financial system whilst safeguarding the interests of depositors and creditors, and at the same time, go the extra mile to do all possible to salvage value for the shareholders of the banks. **It is noteworthy that NO action has been taken to date by the CBN without having reviewed and considered all the options available.**

### **Path to "Safe Harbour"**

A number of options were considered by the CBN in order to deliver the "gave-situation" banks to safe harbour. The four most likely strategies were: (a) to allow strategic partners to recapitalise the banks, (b) to allow the banks to recapitalise on their own, (c) to nationalise the banks, or (d) to revoke the licences of the banks and hand them over to the NDIC for liquidation. After due consultation, the first option was deemed the most desirable route.

The option of nationalising banks would return the system to its undesirable historical state where banks were treated as parastatals and politicised prior to privatisation. Liquidation was ruled out based on the explicit directive of the President of the Federal Republic of Nigeria to the CBN to do everything to protect the interest of depositors and creditors. On the other hand, allowing the banks to recapitalise on their own with no oversight of the process by the Regulator was unrealistic, given the state of the capital market, and would in effect, be inviting the individuals and erstwhile managements that mismanaged the banks in the first instance, to return to business as usual. This would not have solved the debilitating corporate governance problems in these banks. Only Unity Bank Plc and Wema Bank Plc were left to recapitalise on their own because there were no major concerns with their existing management and corporate governance practices.

The chosen recapitalisation process was then carefully designed to ensure transparency, consistency and integrity. The first aspect was to further ascertain the nature and depth of the problems at each bank. The CBN commissioned accounting firms to prepare: (i) forensic reports to further look into the management and corporate governance of each bank, and (ii) diagnostic reports to ascertain the true financial state of each bank.

Both the forensic and diagnostic reports on each of the banks confirmed a pattern of bad corporate governance and a suspicion of fraudulent activity in the banks by the removed Chief Executives. The Economic and Financial Crimes Commission (EFCC) and the Honourable Attorney General of the Federation, upon review of the reports on these banks, were also of the firm view that what was disclosed pointed to serious economic crimes. A number of persons in each of these banks have now been charged with a range of crimes; including theft, fraud and money laundering, before the Federal High Court and the Lagos State High Court. The Securities and Exchange Commission (SEC) also came to the same determination of major infractions of securities regulation, leading to actions at the Investment and Securities Tribunal.

To assist in the recapitalisation and turnaround of each bank, financial advisers (FAs) were appointed. These FAs, amongst other things, solicited in a clean and transparent manner, interest from potential strategic partners across both domestic and international banks and private equity firms. The prospective investors were asked to respond to a detailed set of evaluation criteria which were then used to decide, in a fair and consistent manner, which parties would be allowed to enter the recapitalisation process.

For most of the banks, the process then followed a two-phase approach. In Phase 1, a select number of investors were chosen to conduct initial due diligence on the banks. This due diligence was restricted to the review of the diagnostic report, a review of management and audited accounts and preliminary interactions with management. Based on these, each investor was asked to submit a non-binding offer for the specific bank. The boards of each of the banks then reviewed the submitted bids and decided which investor to take into the next phase.

Phase 2 included a comprehensive due diligence exercise which, in some cases, lasted five to six months. This included the review of detailed financial

schedules, management business plans, and loan portfolios. It also involved detailed discussions with senior management and individual business divisions. Each investor was then asked to submit a binding offer. The boards of directors of some of the banks then appointed a second set of independent financial and legal advisers to assist the boards in assessing the bids. Based on these binding offers, the boards decided, with the advice of their various advisers, which investor to enter into exclusive negotiations and eventually agree terms with, that would be captured in a Memorandum of Understanding (MoU).

**It is crucial to note that, at all times, the boards took into account the interest of shareholders who, in all cases, had no asset or claim on the banks, given that all the banks have negative capital well below zero and have been kept as going concerns only by the intervention and Tier 2 capital injection by the CBN.**

Moreover, the CBN met with various shareholder associations of the banks, to assure shareholders that, although their shareholders' funds have been wiped out by the actions of the previous managements of the banks that they had appointed, the CBN would do its best to ensure that the shareholders are accommodated in the recapitalisation process.

As of today, four banks have submitted MoUs for approval by the CBN under the provisions of the Banks & Other Financial Institutions Act (BOFIA).

**A crucial part of the recapitalisation process was the establishment of the Asset Management Corporation of Nigeria (AMCON).** While the banks were engaging with the bidders, the CBN was working in conjunction with the MoF, with the full support of the President of the Federal Republic of Nigeria, and with the invaluable assistance of the National Assembly, to set up AMCON principally to assist with the resolution of the grave situation in the banks. AMCON was created by statute, its Board of Directors quickly constituted, and it went to work immediately, with the assistance and guidance of the MoF, the CBN, SEC and the Debt Management Office.

**AMCON's purpose is to provide the support required by the boards in restoring the rescued banks and salvaging some value for shareholders.** Firstly, AMCON was to acquire qualifying non-performing loans (NPLs) from all banks in Nigeria and secondly to inject equity into the rescued banks in order to bring their Net Asset Value back up to zero. AMCON has now successfully

acquired the bulk of the NPLs from the rescued banks (and some of the NPLs from the other banks) simply to help bring some value to the banks, reduce the losses being suffered, and to stem the drag on business operations by the debt overhang of NPLs. The Board of AMCON, in support of the efforts of the Federal Government to promote a sound financial system in Nigeria, has agreed to inject equity into each of the rescued banks to bring capital back to at least zero, if there is an enforceable agreement and certainty that the banks will be recapitalised by the successful strategic investor or otherwise.

### **The Challenges**

The recapitalisation process is now well advanced, and the MoUs submitted to the CBN have gone through the regulatory process. However, the process risks being derailed by a small number of shareholders, whose prior stakes amount to just a fraction of the banks' shareholding, purporting to be acting in the interest of the wider shareholders but most likely at the instance of some vested interests. These shareholders have filed court actions to stall the recapitalisation process. Indeed, the CBN has been advised that four MOUs and the recapitalisation to complete the restoration of the banks, which would have been formally brought to shareholders for the exercise of their rights to participate (either alone or with the strategic investor), have been effectively blocked by ex-parte orders of injunction obtained to stop the process.

Despite the various improvements that have been implemented by the CBN-appointed management since taking over, the rescued banks remain in grave situation. There continues to be value attrition as the banks record operating losses, thus increasing the potential cost to the Government. As the table below shows, the rescued banks remain technically insolvent since all of them recorded negative Net Asset Values as of December 2010.

***December 2010 NEGATIVE Asset Value, in thousands of millions  
(Billions of Naira)***

Oceanic Bank International Nigeria Plc	(94,261)
Union Bank of Nigeria Plc	(135,894)
Intercontinental Bank Plc	(330,709)

Bank PHB Plc	(242,309)
Afribank Nigeria Plc	(260,940)
Finbank Plc	(104,751)
Equitorial Trust Bank Ltd	(27,253)
Spring Bank Plc	(87,869)

This situation will continue to worsen as long as the hole in the Balance Sheet of these banks, which was created by mismanagement and outright theft, is not filled with capital. So long as these banks continue to fund the gap with interest bearing liabilities, they will continue to run operating losses especially in an environment of rising interest rates.

### **The Way Forward**

- Consistent with its core mandate, the CBN is resolute in seeing through the recapitalisation of rescued banks to restore normalcy and stability to the financial system. It cannot allow the process to be truncated by a small minority of shareholders with vested interest. So long as there are no such disruptions, the M&A transactions would eventually come to shareholders, at an AGM or EGM.
- **The CBN cannot afford to keep the interbank guarantee in place indefinitely, whereas it is solely by this guarantee that the rescued banks have been able to keep going. The cost to the nation, if the banks continue to operate without capital, is incalculable. The risk to the financial system, if these banks fail, cannot be afforded.**
- In the face of attempts by a small minority of shareholders to block the process of returning these banks to normalcy and stability, the CBN is re-evaluating the options available to it under Nigerian law. The route for each bank will be assessed on a case-by-case basis, but the CBN's priority remains to find an expedient solution that will protect the interests of depositors and creditors and ensure the integrity of the Nigerian financial system.
- It is on record that the CBN has in the past, in line with the law, taken over distressed banks and handed them to the NDIC for management,

resale or liquidation. In such an eventuality, the CBN has no obligation to protect or give any value to shareholders who will have to face the reality that their investments have been wiped out by the management teams that they appointed. This option has always been available. **However, the CBN is committed to supporting the Merger & Acquisition (M&A) and recapitalisation process to arrive at a win-win situation and to restore normalcy and stability to the financial system.** The process has reached an advanced stage, and the CBN will not allow itself to be tied up in endless litigation with persons who have no stake in these institutions, and who are willing to use court processes to bring actions that would inflict losses on innocent depositors and savers whom the CBN remains resolute to protect.

- **Having come this far through the crisis with no depositors or creditors losing any money, the CBN reaffirms its commitment to ensuring that financial stability persists throughout this final stage of the recapitalisation process, and that depositors and creditors will not suffer any losses of savings or loans in any of these banks.**

SANUSI LAMIDO SANUSI, *CON.*  
GOVERNOR  
CENTRAL BANK OF NIGERIA  
9<sup>TH</sup> JUNE, 2011