Financial system regulation in a pandemic: Evidence from Nigeria

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Abstract

Financial system soundness in world economies remains germane, but in the same vein, the COVID-19 outbreak had made governments scampering for any and every solution as experience has shown the need to incentivize businesses to enable economy-wide recovery. In this perspective, consideration of the Nigerian case is made, to re-echo possible collaboration by the Central Bank of Nigeria (CBN) and an operationally-associated agency - the Asset Management Corporation of Nigeria (AMCON). This viewpoint shows the role that AMCON could play to recoup extended facilities, in view to ensure financial system soundness, amidst others. Thus, efforts to leverage on this collaboration could aid going forward a fruitful operational effectiveness of so established policy responses.

Keywords: COVID-19 pandemic; Central Bank of Nigeria; economic stimulus packages; Nigeria; financial system soundness; recession

JEL Classification: E5; E52; E58; G28

Introduction

The strive for prudent policy instruments' formulation and the strengthening of financial regulation for financial system soundness in world economies remain germane, but in the same vein the COVID-19 pandemic had made glaring once again, post-2008/2009 global financial crisis, the vivid contemporary integration of world economies as well as the fragile nature of same economies to (macroeconomic) shocks – with rising unemployment, rising inflation in some economies, low real Gross Domestic Product (GDP) growth, and likely recession[1,2,3,4,5,6,7,8,9,10,11,12,13]. Thus, the history of developments in respective world economies has shown over time that, besides financial system delicateness in terms of possible 'weak' efficacy of so established monetary policy decisions (and/or macro/microprudential guidelines)[14,15], some other socio-economic happenings could as well inform economy-wide events. In this perspective, the Nigerian environment is examined to re-echo possible collaboration by the Central Bank of Nigeria (CBN) and an operationally-associated agency - the Asset Management Corporation of Nigeria (AMCON), in view to ensure financial system soundness.

Central Banks though are reputed to ensure compliance to monetary policy (and/or macro/microprudential guidelines) by Deposit Money Banks (DMBs), and more so increasingly these days known in some economies to work with certain financial system supervisory units/arms/agencies aligned to them (inclusive of Asset Management Companies – AMCs) for the preservation of DMBs' health (and or financial system soundness)[5,14,16,17,18]. Still, there is the need for initiatives that could further inform strengthening the efficacy of Central Bank's policy instruments in respective economies, similarly as with the Central Bank of Nigeria whom functions with an agency (such as, the AMCON) for debt recovery due to defaulting loan obligations, in view to guarantee the soundness of the country's financial system[10,19,20].

While, much studies had considered the efficacy of the CBN's monetary policy to ensure DMBs performance in Nigeria, and such thereof had proffered mixed conclusions, less work has investigated on other roles that the AMCON, besides its statutory debt recovery role and as an agency aligned to the CBN, could perform to further strengthen the efficacy of the CBN's policy instruments[15,21,22,23,24,25,26,27]. A proposition consequently in this light, and to address this reiterated gap in the literature, even at these times of the COVID-19 pandemic and afterwards, offers an informed opinion towards strengthening the operational effectiveness of so established policy instruments.

Theoretical perspective

Whereas, from a theoretical standpoint, the public interest theory of financial regulation explains regulation as a response to public concern of the flawed assumption that businesses will always act in society's interest, and not generate externalities in the event of failure[28]. More so, as with the need for a regulatory authority even for the financial system, the twin peaks model of financial regulation makes clear that though prudential supervision of DMBs would lead to the proper conduct of business with more careful attention to risk, such role need not be entirely appropriated to the Central Bank to mitigate the risk of single-point regulatory failure but partly assigned to some entities external but aligned to the Central Bank[3,29,30,31].

This to be a task in which, there is a form of regulation-by-objective, and there is somewhat a shared supervisory function with one institution (the Central Bank) performing the overall safety and soundness supervision, and all other supervisory entities complementing the Central Bank's other ad-hoc oversight (or supervision), such as the regulation of the conduct of day-to-day business (inclusive of consumer protection)[30,31]. Thus, financial system regulation is well appreciated as sine-qua-non for financial system soundness, but the manner to which such could be carried out in recent times for efficiency reasons had been contested to follow the devolution of some roles to certain financial system supervisory units/arms/agencies external but operationally-associated to the Central Bank.

Current perspective

From a previous study,[32] we assert of the Central Bank of Nigeria (CBN)'s responses in the form of varied (economic) stimulus packages to help (or aid) the ailing domestic economy grow, to encourage business re-openings (despite the periodic closure in compliance to state lockdown(s), and risk of non-survival/non-continuity/non-profitability in the interim), to enable economy-wide recovery from the 'pangs' of the COVID-19 pandemic. Although before the COVID-19 pandemic i.e., since mid-2019, the CBN had remarkably maintained a pronounced stance for continued real sector support in the country with accommodative policy decisions[33,34,35,36,37,38]. These efforts have been because the COVID-19 outbreak with a record of country-specific cases put Nigeria also on the global map of countries in strive to defeat this novel coronavirus. The traces of infection in the domestic economy notably have resulted in local economic activities handicapped, gradually recovering, but also with attendant effects on the citizenry's livelihoods and welfare.

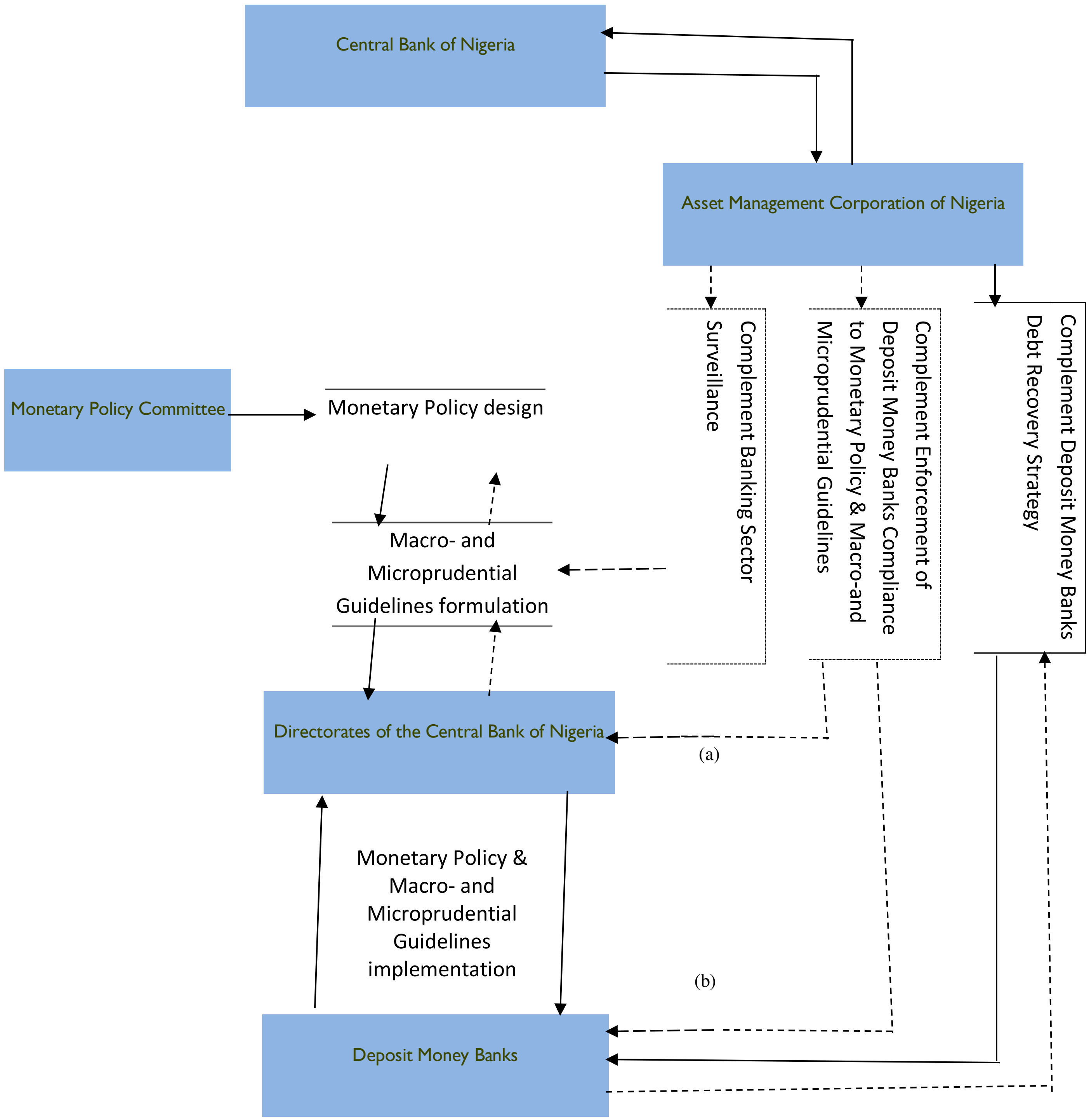
We may recall, the recent spate of cases being recorded of the infamous coronavirus, commonly referred to as COVID-19 and documented to have originated in Wuhan, China with its outbreak in December 2019, has notably thrown the world into a state of panic and while scientists all over the world continually strive to understand the complexity of this aforementioned virus, the ravaging menace of this COVID-19 pandemic has left governments, institutions and people everywhere scampering for any and every solution. While still, now to enable phased-return or gradual-easing of the practice of day-to-day business, the possibility of people to go about their varied means of livelihood, and reopening of the world economies for business activities, experience has shown there is remarkably the need for world governments (and or institutions) to incentivize businesses (or firms) with funds as bail-out aid or 'soft money' to enable their continued operation, prevent further job losses, and foster eventual economy-wide recovery from a potential recession that could be caused by the crippling of business activities due to the COVID-19 pandemic[7,32,39,40].

However, in Nigeria and in the same aforementioned study[32], we attest that to recoup these extended facilities to businesses by DMBs on behalf of the CBN (and or in line with the CBN's monetary policy responses), in these times of the COVID-19 pandemic and post COVID-19, entertains the services of AMCON in their follow-up correspondence with DMBs due to the need to ensure repayment of the extended loan facilities by businesses assisted, to ensure the continued profitability of these DMBs, to avoid a repeat of similar findings of the 2009 financial sector-wide DMBs' stress test in Nigeria, and evade a systemic panic/bank runs (Figure 1). Likewise, such concern as of the function of AMCON here raised will also aid the country's DMBs in their recoup of already extended loan facilities pre-COVID-19 (i.e., recovery of overdue loan obligations from defaulting borrowers), following a fruitful implementation of the recently released Global Standing Instruction (GSI) by the CBN (Figure 1).

Conclusion

In sum, this article had been purposeful to make a reflection on (and or re-echo) the possible CBN – AMCON collaboration, to strengthen financial system regulation in Nigeria during this COVID-19 pandemic and afterwards. Thus, while we expect the CBN to leverage on AMCON's recurrent interface with DMBs in efforts to further strengthen the operational effectiveness of so established policy instruments in this period of the COVID-19 pandemic and at post-COVID-19, we await going forward a fruitful result of the so established policy responses.

Figure 1: The CBN – AMCON Nexus



Source: Uddin, Monehin, and Osuji (2020)

Notes: ---------- indicate non-statutory roles, (a) means indirect complementary enforcement, (b) means direct complementary enforcement.

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