Asset Management Corporation of Nigeria and Bank's Non-Performing Loan Resolution

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Abstract

In Nigeria, the overconcentration of the banking sector loans to the oil and gas sector was responsible for the 2009 banking crisis. Central bank of Nigeria statistical data for 2009 revealed that as at the end of 2009, the deposit liabilities of all regulated deposit money banks in Nigeria, amounted to ₦9.15trillion. During this period, there was high growth of credit to the private sector as loans and advances of the same sector within the period under review amounted to ₦8.45trillion which is about 92.5% of total deposit liabilities. It is with regards to this that the paper sorts to evaluate the resolution mechanism used by AMCON in the purchase, management and disposal of NPLs of commercial banks in Nigeria. The study made use of content analysis to evaluate the mechanisms adopted in the resolution process. Three mechanisms of distress resolution were evaluated namely; Asset pricing methodology; Financing mechanism and Asset Restructuring. It was found that the mechanism used by the corporation such as bundling of non-performing assets into debt securities and debt restructuring have led to only a dismal resolution progress. The recovery performance showed a low total recovery of 28.76% and a fairly high cash recovery rate of 39.76%. This paper recommends that AMCON should have a strict profit maximizing goal and acts as a normal market participant in all its operations, and in this way it will serve as a mechanism that will not only resolve financial distress but ensure that banks channel their loans to other productive non-volatile sectors of the economy.

Keywords: Asset Management Corporation of Nigeria, NPLs, Diversification

JEL Classification: G01, H12.

1. INTRODUCTION

The extent to which the financial system supports diversification of a nation's economy depends on whether financial institutions extend loans to non-volatile productive sectors as well as the extent of the loan defaults. A developmental state committed to industrialization must look towards diversifying its economy for inclusive and sustainable growth. The volatility of the oil sector has overtime remains the major bane of most oil dependent economies of the world, Nigeria inclusive. The continuous dwindling in the world's oil price has yet presented us the opportunity to have a rethink on what positive thing non-oil sector loan concentration will do to the attainment of economic diversification. Most countries depending on the oil sector have faced numerous crises especially in its financial system due to the overconcentration of credit to the downstream oil and gas sector of the economy. This is due to the fact that banks in such economies have seen an avenue to grow their income from loan to this sector capable of improving their profitability. Yet, the unstable nature of the sector presents a risky source of income for the banking sector with consequential effect on banks asset quality performance.

In the real world however, we observe both diversification and concentration strategies on one hand, countries possess rules limiting a bank's exposure to a single borrower (Basel, 1991). On the other hand however, some banks decide to involve in sectors which they have expertise, enjoy comparative advantage and yield the most returns on loans. The subprime crisis, in the year 2008, which later led to global financial crises, is partly due to too much exposure to real estate industry which is highly related to the macro economy (Demyanyk and Vern Hemert, 2011). This crisis, caused by credit portfolio concentration, in return, hit the whole banking industry of US heavily. In the light of financial crisis, diversifications versus concentration have become one of the most important issues to be discussed concerning financial stability.

In Nigeria, the overconcentration of the banking sector loans to the oil and gas sector was responsible for the 2009 banking crisis. Central bank of Nigeria statistical data for 2009 revealed that as at the end 2009, the deposit liabilities of all regulated deposit money banks in Nigeria, amounted to ₦9.15trillion.

During this period, there was high growth of credit to the private sector as loans and advances of the same sector within the period under review amounted to ₦8.45trillion which is about 92.5% of total deposit liabilities. Within the same period of time, ₦2.2trillion or 26% of credit risk assets were non-performing. Most of the expanded credit was used to purchase equities in many cases in the stock of domestic commercial banks that were extending the credit. These excessive margin lending and unhedged loans to oil importers overtime became non-performing leading to systemic distress in the banking sector (IMF Country Repot, 2013). Evidence of oil sector dominating loan and advances in the banking sector is seen in the two year before crude oil prices began falling in mid-2014. The banks in this period lent an estimated $10billion to local oil and gas companies to buy assets from the Royal Dutch Shell, Eni and Total as they retreated from the country's onshore industry. Upstream oil and gas make up an average of around 28% of the banking sector loan books. First banks oil and gas debt for instance make up 47% of the total loan books. Also, a breakdown of the top five sectors in which eligible bank assets (EBAs) originated from, the oil and gas sector make up 27.23% of AMCONs total loan portfolio (AMCON financial report,2011). This was responsible for the banking sector crisis that occurred in 2009 which then became clear that loan diversification in the banking sector is inevitable and an avenue for a developmental state to achieve economic prosperity as well as attain financial system stability.

It is with regards to this that the paper sort to evaluate the resolution mechanism used by AMCON in the purchase, management and disposal of NPLs of commercial banks in Nigeria and its implication for the diversification of the Nigerian economy.

2. STERILIZED FACTS

2.1 An Overview of AMCON Operations in Nigeria

In mid-2008 when the global financial and economic crisis set in, the domestic financial system was already engulfed by several interdependent factors that led to the re-emergence of an extremely fragile financial system similar to the pre-consolidation era. These factors included macroeconomic instability caused by large and sudden capital inflows, major failures in corporate governance at banks, lack of investor and consumer sophistication, inadequate disclosure and transparency about financial position of banks, critical gaps in regulatory framework and regulations, uneven supervision and enforcement, unstructured governance and management processes at the CBN/weaknesses within the CBN, and weaknesses in the business environment. It is apparent therefore, that when the global crisis eventually hit Nigeria, the banking sector was ill equipped to withstand the storm in spite of bank recapitalization. In the real sense the financial crisis had an adverse effect on both the oil and gas sector as well as the capital market where the Nigerian banks were exposed to the tune of N1.6 trillion as at December 2008. The result was a sharp deterioration in the quality of banks' assets which immediately led to concerns over banks' liquidity. Indeed, the Nigerian banking sector was thrown into severe crisis as many of the banks became distressed. At the heart of this crisis is rising non-performing loans that engulf the entire banking sector. In an attempt to resolve this systemic distress in the financial system, policy makers as well as regulatory authorities initiated reforms geared towards the resolution of these problems. One of the policy reforms initiated is the setting up of the Asset management Corporation of Nigeria (AMCON) to serve as an intervention vehicle.

2.1.1 The Need for Loan diversification

Over the years, the Nigerian banking sector has concentrated its effort to extending loans to only specific sectors of the economy which is believed to be volatile and is capable of driving instability in the financial system. The oil and gas sector has dominated loan access from the Nigerian banking sector as revealed by the portfolio of loans of AMCON in the various sectors. The need for loan diversification by the Nigerian Financial system is further necessitated given the experience of the banking sector in 2009. This results from huge loans extended to operators in the downstream oil and gas sector by commercial banks in Nigeria attracted by the huge revenue generated from the sector, thereby, crowding out other less volatile productive sectors of the economy. The quarterly sectoral allocation of loans by commercial banks in Nigeria shows a huge allocation to the oil and gas sector in both the industrial and service sectors. This is as shown in the table below.

1.1 Quarterly Sectoral Distribution of Commercial Banks Loans and Advances in Nigeria for the Year ended 2014 (₦ billions)

Agriculture	Industry				Construction	Trade& Commerce	Government	Services					Others	Total
Q_1-Q_4	Mining & Quary	Manufacturing	Oil/ Gas	Power & Energy				Real Estat	Financial Instituti	Education	Oil/Gas	Pow		
333.6	45.6	1,309.00	1,400.50	242.1	384	705.8	725.5	427	425.9	56.3	906.6	123	3,654.10	10,739.40
400.3	14.2	1,425.60	1,411.90	248.4	468.9	807.7	816.3	456	471.2	75.8	1,065.90	125	3,339.90	11,127.10
394.8	14.5	1,475.40	1,652.40	247.8	411.3	658.1	768.7	443	540.4	70.9	1005.8	125	3,336.90	11,144.80
478.9	18.2	1,647.50	2,047.20	276.1	556.2	1,045.20	732	551	763.4	86	1098.9	151	3,437.50	12,889.40

Source: CBN Statistical bulleting 2014

Furthermore, a breakdown of AMCON top five sectors for which the eligible bank assets originated from also showed that the oil and gas sector of the Nigerian economy make up a large portion of AMCON's NPL portfolio. Table 2.1.2 shows a breakdown of the top five sectors in which the EBAs originated from and constituted about 36% of all EBA purchased by the corporation.

Table 2.2: AMCON's Non-Performing loan Portfolio

Sector	Percentage of AMCON Portfolio
Oil and Gas	27.23%
General Commerce	18.49%
Capital Market	17.93%
Manufacturing	6.24%
Finance and Insurance	5.47%

Source: AMCON financial report, 2011

The need for an AMC in Nigeria was triggered by the distress in the financial system resulting from the trend in the level of NPLs as revealed in Table 2.1 below. It was evident from the table above that the Oil and Gas sector constitute the highest share of AMCON's NPL portfolio.

Table 2.2: Nigeria's NPLs as a % of Total Bank Loans in relation to other Countries

Year	Nigeria	USA	Canada	Australia	Malaysia	UK	Germany	World
2000	22.6	1.1	1.3	0.5	15.4	2.5	4.7	9.7
2001	19.7	1.3	1.5	0.6	17.8	2.6	4.6	9.6
2002	21.4	1.4	1.6	0.4	15.9	2.6	5.0	8.3
2003	20.5	1.1	1.2	0.3	13.9	2.5	5.2	6.7
2004	21.6	0.8	0.7	0.2	11.7	1.9	4.9	5.2
2005	18.1	0.7	0.5	0.6	9.4	1.0	4.0	3.9
2006	9.3	0.8	0.4	0.6	8.5	0.9	3.4	3.1
2007	8.4	1.4	0.4	0.6	6.5	0.9	2.6	2.7
2008	6.3	3.0	0.8	1.3	4.8	1.6	2.9	3.0
2009	27.6	5.0	1.3	2.0	3.6	3.5	3.3	4.2
2010	15.7	4.4	1.2	2.2	3.4	4.0	3.2	4.1
2011	5.3	3.8	0.8	2.0	2.7	4.0	3.0	4.0
2012	3.5	3.3	0.6	1.7	2.0	3.7	2.9	3.7
2013	3.4	2.5	0.6	1.5	1.8	3.1	2.7	4.2
2014	3.0	1.9	0.5	1.1	1.6	1.8	2.3	4.2
2015	5.2	1.7	0.5	1.1	1.6	n/a	n/a	n/a

Source: World Bank (WDI), 2015

The above table shows the behavior of NPLs in the Nigerian banking sector in relation to that of other countries for various years. The figure showed that from 2001 after the introduction of the universal banking model, NPL averaged 21% for the period 2000-2004 and further fell owing to the consolidation and recapitalization reforms introduced in the financial service industry which impacted drastically in reducing the NPL ratio. Available data showed that NPL ratio fell further from 21.6% in 2004, to 6.3% in 2008, indicating an average fall of 10.5% from 2005-2008. The reform had a significant impact on the quality of commercial bank's assets with a 10.63% fall in NPL in the financial system. However, the outcomes of the reforms subsequently reveal the inability of the recapitalization to shore up the problems in the banking system. A reversal in NPL ratio started occurring as non-performing loan ratio rose from 6.3% in 2008 to a record high of 27.6%, triggering distress in the banking sector mainly due to global fall in the price of oil. Compared to other countries whose NPL ratio peaked at 5% over the same period, it then became clear that Nigeria is in need of a resolution mechanism to resolve the systemic distress in the sector.

3. LITERATURE REVIEW

3.1 Conceptual Issues

Asset management is most critical in the financial service sector especially the banking sector. It is important for a business to manage its assets and to make them work to obtain the best possible returns. To achieve these objectives, asset management embraces all of the processes, tools and data required to manage assets effectively (Nemmers, 2004). Emerging efforts to integrate finance, planning, engineering, personnel, and information management to assist agencies in managing assets cost-effectively constitute what asset management is all about. Through this systematic and coordinated activities and practices, an organization optimally manages its physical assets and their associated performance, risks and expenditures over their lifecycles for the purpose of achieving its organizational strategic plan (AASHTO, 1997). From the foregoing, we see asset management as the effective management of commercial banks assets in the form of loans and advances which are declared non-performing or toxic assets. It is necessary that such assets, though toxic, be managed so as not to impede on the stability of the financial system as witness in Nigeria in 2009 when a systemic distress characterized the banking system due largely to the accumulation of Non-performing loans by banks. Effective management of such assets has implication for the banks' loan loss provision, credit growth and earnings performance. Improper asset management constitutes a threat to banks going concern status leading to a cessation of independent operation or continuance without intervention from the government via distress resolution institutions.

Once a bank's risk asset is impaired, it has significant implications for its going-concern status (continuous existence). First, it erodes the bank's capital base and put its capital adequacy in jeopardy. Much more significant is that it curtails its operational capability because it would not be able to lend and thereby constraints its revenue generation. This may lead to illiquidity, which if not properly managed, may end up in insolvency and liquidation.

An Asset Management Company (AMC) is a special vehicle usually created to acquire, manage and dispose impaired banks' risk assets. It is an investment management firm that invests pooled funds in securities in line with its declared financial objectives. One of its core responsibilities is to purchase selected toxic assets (Capital market related) of deposit money banks. An AMC is normally established as one of the major outcomes of the policy frameworks to achieve financial restructuring needed for long term soundness and sustainability of the banking system. It is meant to deal with banks asset quality problems by purchasing the bad loans (assets) of the banks and provide them with cash to enable them promptly resume their role of lending and general financial intermediation. It is therefore usually fallout of a country's banking crisis occasioned by high level of non-performing loans. In view of its peculiarity, an AMC is always a creation of the law, with special enablement. AMC is thus an interventionist strategy and it can be publicly or privately owned or a centralized or a bank-based model.

3.2 Theoretical Issues

The soft budget constraint theory and the financial fragility theories recommended that if there is systemic distress in financial institutions, steps have to be taken to increase the net-worth of the insolvent entities so as to prevent the distress from degenerating into economic instability. One important solution to resolving this problem is for a government sponsored agency to remove the non-performing loans from the balance sheets of insolvent institutions. This will result in improved performance for the financial institutions with the assumption that by removing non-performing loans from the banks, and transferring them to a AMC, banks will regain capacity to intermediate funds in the economy (Konai, Maskin & Roland, 2003).

When banks are saddled with huge unpaid loans, its credit intermediation role is hampered because a huge portion of loanable funds have to be reserved as provisions for possible losses, instead of being productively used for new loans and investments leading to a rise in loan provision.

To rescue the banks from eminent collapse, a soft budget constraint mechanism is necessary. This could be achieved through government intervention in setting up a publicly owned Asset Management Company to abate the debt overhang in the banking system through the removal of the bad debts out of the books of financial institutions and freeing up tied capital. Asset Management Companies, especially centralized ones allow banks to “turn a new leaf” more rapidly and focus more on its core business of financial intermediation and thus serve to drive diversification of the Nigerian economy. In theory, by removing NPLs from banks and transferring them to AMCs, banks regain the capacity to intermediate funds in the economy. The improvement in financial intermediation should be apparent in the uptrend in domestic credit growth to the private sector away from certain volatile sectors.

3.3 Empirical Issues

Studies recommend the removal of non-performing loans from the books of financial institution as a means of resolving financial distress. Resolving such financial distress they argue cannot be achieved simply by flooding the market with liquidity by the Central Bank through a simple monetary policy, but for a government sponsored agencies that will remove non-performing loans from the balance sheets of insolvent institutions (Davidson, 2008; Minsky, 1992). Others argued that although this mechanism is notable in solving the problem of non-performing loans, yet challenges still remain unsolved, and the effectiveness of the approach is still unconvincing. This paper therefore reviewed studies in this area relating to the effectiveness of non-performing loan resolution strategies.

Dong (2004) provides a balanced assessment of the role of the Korean Asset Management Company (KAMCO) in resolving non-performing loans in the Republic of Korea in the aftermath of the 1997-1998 financial crises. Non-performing loans were at the heart of the financial crisis that engulfed the Korean economy during this period. The study investigated whether the strategy implemented in resolving the crisis was effective. The recovery has also been characterized by a rapid and drastic reduction in the level of non-performing loans in the financial system through the setting up of crisis management institutions such as KAMCO. This has made KAMCO to achieve its broad objective of resolving the non-performing loan as the findings suggest a rapid decline in the level of non-performing loans particularly in the banking sector. Non-performing loans decline from 17% as of march 1998 to 2.3% at end 2002.

In a cross country study, Klingebiel (2000) analyzed on the conceptual basis, the advantages and disadvantages of AMCs in managing and disposing of impaired assets; and also gauge the effectiveness of such institutions. Using historical data for the various countries to assess if the AMCs were able to achieve their narrow objectives of expediting corporate restructuring and accelerating the resolution of non-performing loans. The study reviewed AMCs in seven countries namely; Finland, Ghana, Sweden, Mexico, the Philippines, Spain and the United States. The outcome of the rapid asset disposition agencies showed that for Spain, Philippines, and Ghana, banks resume lending and credit to the private sector by banks increases in real terms as credit growth rebounded relatively strongly. However, the experience in Sweden, Mexico and Finland was to the contrary as real credit to the private sector contracted significantly as credit growth remained strongly negative in real terms in the years after the establishment of the AMC. In Ghana, banks appeared to be in difficulties again as state owned commercial banks had non-performing loans exceeding 15% at the end of 1997, while in Mexico, transfer of loans did not succeed in restoring the banking system to solvency as capital deficiency was underestimated and institutions remained weak even after repeated rounds of loan repurchase at above market price. This has raised questions as to how effective AMCs are in resolving financial distress in the banking sector.

Terada-Hagiwara, and Pasadilla, (2004), in their study, examined the experience of Asian AMCs using three indicators - credit growth, corporate profitability, and bank profitability- to assess the macroeconomic impact of Asset Management Companies in Asia. The study revealed that as far as financial intermediation is concerned, bank credit growth regained its momentum in 1999 even as the three AMCs were established in the same year. The findings suggest that profitability of the banking and corporate sectors continue to decline for the first two years after the establishment of the AMCs in Indonesia and Korea. This perhaps reflects the fact that not all non-performing loans are immediately transferred. Banks therefore, remained saddled with a large quantity of non-performing loans, those that are harder to resolve, during the initial stages of assumption by the AMC.

Comparing the common trend across and between six public AMCs in East Asia, Fung et al (2004) identifies and proposes factors and conditions that could contribute to the successful operation of an AMC in resolving bank's NPLs while minimizing costs to the taxpayers. The study compares these different AMCs in terms of asset transfers (amount and pace of asset transferred, types of asset transferred, asset transfer pricing and methods); financing (direct government funding, AMC bond and other borrowing, financing by the central bank); and Asset Resolution (principal resolution approaches, resolution progress and asset recovery, and factors affecting resolution and recovery). The study made use of ratio analysis to estimate specific broad and narrow indicators to clearly explain the question of resolution progress and recovery performance. Generally, the findings indicate that on the basis of the broad measure, Danaharta and KAMCO have been more impressive, achieving a recovery rate of some 50-60%. China's four AMCs have managed to recover 33.6% from their asset resolution.

In contributing to the role of AMCs in distress resolution, Akpan (2013) examined the relevance of Asset Management Corporation of Nigeria to the non-performing loans of deposit money banks in Nigeria. The result shows that the establishment of AMCON has helped in reducing the non-performing loans assets of banks. It shows also that non-performing loans of banks is one of the factors that causes banks illiquidity, thus, capable of limiting lending behavior of the banks. The study also underscores the postulations that the strategies adopted by banks in managing their non-performing loans are moderately effective, thereby questioning the effectiveness of 'Bad Banks' models to manage impaired assets of banks. The study finally revealed that the intervention of AMCON has brought confidence and stability to the banking industry. However, the sustainability of this achievement remains a question yet to be answered. This is due to the fact that although the Corporation might have succeeded in removing the non-performing loan in the system, some of these banks still have large provision for loss loans indicating that non-performing loans still persist in the banking sector above the regulatory threshold which is consistent with the findings of Terada-Hagiwara, and Pasadilla, (2004) for Malaysian distress resolution agency.

Assessing AMCON's role in resuscitating the banking sector during the global financial crisis, Olatunji (2015) assesses the significance of AMCON in the financial sector recovery. The study found out that CAR, NPLs, survival problems which are indices of banks' exposure to global financial crisis will in the not-too-distance future be mitigated completely. On the basis of data presented, AMCON's intervention will be a defensive wall for the financial sector against any future contagion that might threaten their existence. Increasingly, AMCON's impact has been significantly felt but without a very high exposure as AMCON itself is prone to several risks. In the same vein, Adeolu (2015) in his findings also found that AMCON has positively impacted on the asset quality and liquidity of banks selected in his study. Examining the impact of AMCON on the securitization in the banking sector in Nigeria, the study made use of a combination of descriptive and explanatory survey research. His findings corroborated the findings of Akpan (2013) and Olatunji (2013) but with a caveat on the potential moral hazard effect of AMCON and suggesting that banks should take over the responsibility of managing their bad assets.

It is important to note that while some studies such as Dong (2004), Odimgbe (2012), Akpan (2013) and Olatunji (2015) showed that asset management companies impacts on the resolution of financial distress, others showed that the impact is not significant for example Klingebiel (2000), Fung et al (2004), Terada-Haragiwa and Pasadilla (2004). And moreover, the direction of the effect is still a debatable issue in distress resolution policies. Also, the magnitude of the effect of using asset management companies in distress resolution and financial stability is inconclusive, because while some studies revealed that the intervention by asset management companies played a major role in the management of bad debts and equally enhanced bank profitability and improvement in loan, others argued that although selling loans to AMCs was effective in reducing NPLs, but ineffective in some cases as new non-performing loans developed. Moreover, the profitability of the banking and corporate sectors decline continuously for years after the establishment of AMCs, as the asset management companies themselves are prone to very high risks. To this end, one of the key point which has received less attention in the literature so far is that monetary authorities as well as policy makers have not sufficiently interrogated the effectiveness of the mechanisms adopted in the resolution of systemic distress by asset management companies which this study has filled the gap in literature.

3.4 Methodology

To achieve the objective of this paper, which is to evaluate the effectiveness of financial distress resolution mechanism in Nigeria, the study made use of content analysis to evaluate the mechanisms adopted in the resolution process. Our choice of these techniques was informed by the nature of the data. If the resolution mechanism used by AMCON has been effective, we would expect significant progress in asset resolution as well as asset recovery performance. As a research technique that is used to make replicable and valid inferences, data collected gives information about the progress and performance of the corporation through the systematic evaluation of documents of the corporation. Three mechanisms of distress resolution were evaluated namely; Asset pricing methodology; Financing and Asset Resolution. An objective, systematic and quantitative description of the content of the documents was done in order to draw inferences about the mechanism. Specific indicators were used to shed more light on the question of resolution progress and recovery performance adapted from the work of Fung et al (2004). This was done to compare the resolution progress and recovery performance alongside the expected or target recovery. These indicators form the basis of our conclusion about the effectiveness of the mechanisms used by the corporation.

4. DISCUSSION OF RESULTS

4.1 Asset Transfer Pricing and Methods

Transferred asset or purchased loans represents loans acquired by the Asset Management Corporation of Nigeria from Eligible Financial Institutions. These loans are from all banking sector margin loans, all non-performing loans of intervened banks, non-margin non-performing loans from 22 Nigerian deposit money banks, systematically important loans and reprising of acquired eligible bank assets. AMCON purchased a total Eligible Bank Asset (EBA) worth ₦4.02rillion at a price of ₦1.76trillion. Table 4.1 indicates the pricing method adopted in the purchase of non-performing assets.

Table 4.1 AMCON's Purchase Price for Non-Performing Loans

Date	**EBA Value Purchased (₦)**	**AMCON Purchased Price (₦)**
31st Dec, 2010	2.46trillion	866.2billion
6th April, 2011	675.2billion	377.8billion
28th Dec, 2011	885.3billion	515.2billion
Total EBA Purchased	**4.0205trillion**	**1.7592trillion**

Source: AMCON Financial Report, 2013

The table above shows that the corporation using the valuation methodology based on the underline value of the collateral was able to purchase these assets at a discount which is below the real value of the assets. The implication of this is that most of the assets sold to the corporation are poorly backed by adequate collateral which necessitate the corporation to purchase such loans at below its full value.

AMCON acquired over 12500 banking sector non-performing loans with about ₦1.8trillion at fair value price, largely based on the underlying collateral value of the loans which is in accordance with the AMCON guidelines. Purchasing non-performing at fair value is a disincentive for banks to want to accumulate toxic assets and to transfer assets to the corporation.

4.2 Financing Mechanism

In order to purchase the non-performing loans from Nigerian banks and to fund its operations, AMCON used funds from three key sources namely; funds provided by the federal government and the Central Bank of Nigeria; bonds issued by the Corporation; and a fee assessed by the Corporation on bank assets. The federal government provided the initial funding for the Corporation to the tune of ₦10billion contributed evenly by the ministry of finance and the Central Bank of Nigeria. According to the January 2011 memorandum of understanding, CBN will provide AMCON with ₦50billion per annum for ten years beginning in 2012 (AMCON Act Part I S2 (1)). This means that over a ten year period, the CBN will contribute ₦500billion.

Since its creation in late 2010 through 2014, the Corporation has issued five series of bond with the first bond issuance in three tranches to banks in exchange for non-performing assets from Nigerian banks. These bonds are backed by the full faith and credit of the federal government of Nigeria as shown in table 4.2 below.

Table 4.2.: A Breakdown of AMCON Bond Issuance

Issuance	Issuance Date	Purpose	Discounted Value ₦(M)	Bond Face Value ₦(M)	Yield (%)	Maturity Date
Series I Tranche I	21st Dec. 2010	EBAs Acquisition	785,747	1,164,952	10.125	31st Dec. 2013
Series I Tranche II	6th April, 2011	Price Discovery	12,878	17,620	11.800	31st Dec. 2013
Series I Tranche III	6th April, 2011	Additional EBAs	377,76	516,864	11.800	31st Dec. 2013
Series II	8th Aug. 2011	Injection in Bridge Banks	765,299	1,001,772	10.500	Aus. 8th, 2014
Series III	27thSept. 2011	Deposit Restoration Fund	64,500	88,812	10.500	Nov.15th, 2014
Series IV	14th Oct. 2011	Deposit Restoration Fund	1,299,802	1,908,318	13.00	31st Oct. 2014
Series V	28th Dec. 2011	Additional EBAs, Deposit Restoration Fund	644,729	929,404	13.00	31st Oct. 2014
Total			3,894,070	5,464,928		

Source: *AMCON's Full Year audited group Results Presentation for the year ended 31st December, 2011*

The third source of funding for AMCON is an assessment paid annually by banks operating in Nigeria. The Act provides that each Nigerian bank will contribute annually 0.5% (revised from 0.3% in 2012) of their total assets as one of the regulatory induced costs which AMCON mandated banks to pay out of their assets on preceding year balance sheet starting from 2011 to the Banking Sector Resolution Cost Trust Fund (BSRCTF). The fund was created to meet the obligation of the corporation arising from debt securities issued and expenses relating to its function. The sinking fund was set up to assist the AMCON to meet its goals and ensure that government will not bear the cost of financial crisis in future. A review of the financial statements of some banks for the year ended December 2014 showed the following contributions by banks into the Banking Sector Resolution Cost Trust Fund (BSRCTF).

Table 4.3: Banks Contribution to the BSRCTF as at December 2014

S/N	BANK	AMOUNT (billion)
1.	Access Bank	10.52
2.	Diamond Bank	9.67
3.	EcoBank	22.51
4.	FCMB	5.86
5.	Fidelity Bank	5.94
6.	First Bank Holdings	21.72
7.	Guaranty Trust Bank	11.78
8.	Skye Bank	7.11
9.	Stanbic IBTC Bank	4.72
10.	Sterling Bank	4.12
11.	United Bank For Africa	13.82
12.	Union Bank	5.01
13.	Unity Bank	2.01
14.	WEMA Bank	1.91
15.	Zenith Bank	18.76
Total.		144.64

Source: Bank Financial Statement for the year ended December 2014

On the sinking fund which banks have been contributing to AMCON's purse, this has made the banks bear the cost of intervention, which to some extent is considered reasonable. Since these banks were responsible for the distress within the financial sector, it is sensible that they contribute to fixing the problem seemingly caused by their imprudent financial behaviors. However, what this implies is that AMCON bought over non-performing loans at a discount (banks took the loss on that) and will now make the banks to contribute to the sinking fund that will pay the cost of AMCON's intervention, thus, bringing back almost all the entire cost of intervention on the banks. This mechanism though plausible should be done with caution so as not to inflict more pain on the industry's total operating cost, as this will have a huge impact on the financial deductions made from the bank's account by the various regulatory authorities, thereby, eating deeply into the bank's profitability. The summary is that the borrower in question ended up getting away with whatever discount AMCON obtained from the banks and the discount they subsequently obtained from the Corporation. The policy can best be described as a one-sided regulatory application capable of hurting shareholders, thereby making investment in the banking sector unattractive.

4.3 Restructuring and Resolution Mechanism

Just like other asset management companies around the world, AMCON used two broad approaches in its resolution of non-performing assets. The first approach is to convert a non-performing asset into a performing asset, mainly through restructuring of either the loan, or the borrower, or both. The second approach is to dispose of assets including the associated collateral if possible, through various means. The restructuring approach typically often maintains the loan relationship with the borrower, tactically extending the relationship with the borrower to increase their chance of rehabilitation. This rearrangement of debt typically embraces additional financial support so as to alter the time horizon of the loan, grace periods, etc. and is mostly common in dealing with viable borrowers. This approach is one with a longer term perspectives. The second approach puts a greater emphasis on the quick removal of both secured and unsecured non-performing assets from the balance sheets of AMCON. This is executed mostly through straight loan sales (public, private or bulk sale), auctions, foreclosure on collateral, or some form of asset securitization.

In terms of the management and disposal mechanism used, the corporation resolved most of its acquired assets by restructuring of the loan, loan workouts, institution of actions for debt recovery, conversion of debt into equities to secure control of Debtor Company, forbearances and securitization. Achieving a speedy resolution and higher recovery depend on a more focused management/disposition strategy supplemented with some debt restructuring. Purchased loans acquired by the corporation are renegotiated by AMCON after acquisition. The gains or loss on renegotiation is determined as the difference between the purchased price and the settlement amount. Gains on renegotiation of purchased loans is deferred and recognized only when the related loans have been fully repaid. AMCON has restructured several loans over the years as shown in table 4.2.3 below:

Table 4.4: Restructured Loans by AMCON 2010-2014

Year	**Amount (₦ billion)**
2010	-
2011	198.2
2012	152.7
2013	228.6
2014	293.2
Total	**872.7**

Source: Selected Bank's financial report various issues

In restructuring toxic assets, AMCON enters into negotiation with the assets obligor with the aim of strengthening their ability to service and eventually to repay the principal. This usually involves the redefining of the terms of the original contract, a process that often entails some concessions on both the part of the holder and the part of the obligor. In a situation where the debtor fails to pay at the stated date, the corporation reserves the right to foreclose on the debtors assets or to institute a court action against the debtor. AMCON considers a restructured loan which is now performing to be a resolved non-performing loan.

4.4 Evaluation

While transferring non-performing loan at fair value created a potential trade-off between speed and value in practice, this approach carry a less moral hazards risk and reduces fiscal burdens for taxpayers, if sufficient political backing is in place to effect or force speedy stripping-out of non-performing loans. In Nigeria for instance, banks were reluctant to sell their toxic assets to the corporation due to fear of losses. However, with the issuance of policy statement by the regulatory authorities to banks to ensure that their non-performing assets do not exceed the regulatory threshold of 5%, banks had no choice but to comply. Thus, purchasing non-performing loan at fair value is rather a disincentive than an incentive for rising non-performing loan.

In terms of the financing mechanism, the Central Bank of Nigeria's heavy involvement in the financing of the Corporation raises the risk of damaging it balance sheet. The CBN in a bid to ensure that banks were able to meet up with their daily liquidity requirement, prevent bank runs and avoid a collapse of the banking system, injected fresh capital into banks totaling ₦620billion ($3.9billion) so as to averred the problem . In addition, the initial funding for the Corporation was provided partly by the central bank in addition to ₦50billion to be contributed by the CBN annually for ten years to help resolve the problem.

As a result of this, it has raised the central bank's liabilities from ₦2.1trillion in 2009 to ₦6.1trillion in 2013. This development has made over 40% of CBN's asset portfolio unmarketable (Nigerian Banking Sector Report, 2014). For instance, the 190.5% surge in other liabilities from ₦1.2trillion in December 2009 to ₦6.1trillion in November 2013, traceable mainly to the acquisition of AMCON's debt portfolio by the central bank. The potential losses for the central bank are large, given the uncertainty in recovery. If the central bank has to bear these losses, it will affect its ability to carry out monetary policy and it may need government recapitalization (Ma and Fung, 2002). This has implication for its monetary policy operations. This is because the CBN not only provided the initial funding, but also guaranteed its bonds. Depending on AMCON's recovery performance, the central bank has been exposed to the corporation's potential losses.

The implication of these is that first, in the event of another crisis in the banking sector, the CBN might not have the capacity to bail out the banks without avoiding the option of printing more money. This option however might have significant consequences on price stability. Secondly, the central bank might be forced to raise the AMCON levy on banks from the current 0.5% to include another 0.5% of their off-balance sheet transactions in coming years. This is evident in the increase in Nigerian banks contribution to the Banking Sector Resolution Cost Trust Fund (BSRCTF) which was revised by the CBN from 0.3% in 2012 to 0.5% of total assets presently. This will exert further pressure on the banking industry bottom lines as AMCON's fee as a proportion of total operating expenses has risen from 4.6% in the financial year 2012 to 7.6% in 2013 and is expected to cross the 10% threshold in 2015. The central bank's proactive response to the banking sector crises was arguably the right move although this has in itself, magnified CBN's level of indebtedness.

On the sinking fund which banks have been contributing to AMCON's purse, this has made the banks bear the cost of intervention, which to some extent is considered reasonable. Since these banks were responsible for the distress within the financial sector, it is sensible that they contribute to fixing the problem seemingly caused by their imprudent financial behaviors. However, what this implies is that AMCON bought over non-performing loans at a discount (banks took the loss on that) and will now make the banks to contribute to the sinking fund that will pay the cost of AMCON's intervention, thus, bringing back almost all the entire cost of intervention on the banks. This mechanism though plausible should be done with caution so as not to inflict more pain on the industry's total operating cost, as this will have a huge impact on the financial deductions made from the bank's account by the various regulatory authorities, thereby, eating deeply into the bank's profitability. The summary is that the borrower in question ended up getting away with whatever discount AMCON obtained from the banks and the discount they subsequently obtained from the Corporation. The policy can best be described as a one-sided regulatory application capable of hurting shareholders, thereby making investment in the banking sector unattractive.

In terms of restructuring of loans, this raises question as to the status of these loans. While restructuring is a widely used tool for asset resolution, in some cases the restructured loan can overtime become a non-performing loan again which in the end may cost the Corporation more than originally thought. Some debtors have discovered that while it may be riskier to deal with AMCON, it offers them more relief. They can have their loans restructured and repayment scheduled over a long period of time than if they deal with their banks. Upon this, debtors with capacity to repay their debt or who had been cooperating with the banks in their debt recovery efforts suddenly developed cold feet. In this case the banks will get a very low value for the loan since most of them are not secured. Thus, banks would lose and debtors would have succeeded in converting a short term loan to a longer term loan, thereby undermining the profitability and growth of banks. The strategies of asset management and disposition adopted by AMCON has led to the following recoveries in table 4.1.2.

Table 4.5: Disposition and Recovery of Assets Transferred

Transferred Assets	N
Total Transferred Assets	1.75trn
Resolution:	
Disposal	305.13bn
Disposal Rate (%)	60.24
Restructured	872.7bn

Restructured Rate (%)*	**67**
Recovery	
Total Recovery	506.5bn
Total Recovery Rate (%)	28.76
Cash Recovery	201.37bn
Cash Recovery Rate (%)	39.76
Non-Cash Recovery:	
Physical Assets	191.82bn
Financial Assets	113.31bn
Non-cash Recovery Rate (%)*	60.24

Source: Nigerian Banking Sector Report, 2014/ *Author's computation

To shed light on the question of resolution progress and recovery performance, the broad and narrow measures above show that the Asset Management Corporation of Nigeria so far has resolved, dispose of or liquidate some 60% of the total asset transferred to it into their fifth year of operation, thus showing a high pace of asset resolution progress. At this pace, it would probably take less than another five years for the Corporation to entirely unload their acquired portfolios. On the basis of the broader measure, the Corporation has not been more impressive, achieving a recovery performance of some 28%. However, the more demanding cash recovery indicator revealed a somewhat different picture as asset recovery by AMCON is mostly in the form of non-cash restructured loans amounting to two-thirds of their total recovery.

Thus, the total recovery appears to be fairly high but less in terms of cash recovery. A combination of high total recovery and low cash recovery in the case of AMCON indicates some residual risk, as the market value of non-cash recovery remains exposed to fluctuating market conditions and partly because some of the restructured loans may turn to be non-performing, thus, ultimate recovery and final losses of the Corporation remains uncertain. On the whole, while the resolution (in terms of disposal) of transferred assets is seen as effective with a 60% resolution rate, the mechanism used by the Corporation in the purchase, management and disposal of non-performing loan is considered to be less effective given the low total as well as cash recovery rates. Moreover, recovery performance of the Corporation is low due to the fact that non-cash recovery dominated the total recovery of transferred assets.

5.0 Conclusion and Recommendation

An attempt has been made in this study to examine the effectiveness of financial distress resolution mechanism in the Nigerian financial system and explore complementary options for resolving systemic distress in the banking sector. The empirical findings are derived from the data generated for the study and the result of the findings shows that while the resolution (in terms of disposal) of transferred assets shows a high pace and progress of asset resolution with a 60% disposal rate, further findings suggest that on the basis of the broad and narrow measure, the mechanism has not been more impressive with a total and cash recoveries of 28.76% and 39.76% respectively. Moreover, a combination of low total and cash recovery performance of 28.94% and 17.11% respectively indicates some residual risk in the case of AMCON. The lower the recovery progress and recovery performance implies the less effective the resolution strategies.

The content analysis shows that the mechanism used by the corporation is less effective given the low recovery performance. The mechanism for asset management and disposition though seems to be adequate; it however generated a low recovery performance despite the high resolution progress. It was found that while the resolution progress has been somewhat disappointing to date, the government's commitment to maximizing and accelerating NPL recovery is strong, and bulk disposal activities, which require regulatory approval, have picked up considerably. On the strength of findings from this study, the paper recommends that since no single model of Asset Management Company fit all countries circumstances and the optimal strategy could also vary over time, the focus for AMCON should not just be the timely disposal of non-performing asset of the banks but to ensure the maximization of both total as well as cash recoveries. Restructured loans should be seen to be performing and un-restructured ones should be fully recovered both in cash and non-cash. AMCON should have a strict profit-maximizing goal and should act as a normal market participant in all its operations. This goal should guide all its operational policies, including the valuation of assets, funding strategy, and speed of asset disposition. The corporation should consider debt factoring as a mechanism to be used in future resolution options in case of any distress in the financial system.

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