

## The CBN May Soon Regulate Bank Profits

Martin N. Oluba Ph.D., DBA is the President/CEO of [ValueFronteira Limited](#). He is also Professor of economics & finance at the SMC University, Switzerland; faculty (mentor) for doctoral dissertations at Northcentral University, Arizona USA. Send him your comments at [martin@valuefronteira.com](mailto:martin@valuefronteira.com) or visit his personal website at [www.martinoluba.com](http://www.martinoluba.com) for his views on other subjects of national concern.

As part of its strategy to strengthen the financial system, the current CBN regime is tinkering with the idea of sitting down around a table with bank executives to discuss and agree what profit targets should be set for the banks. The underlying strategy here is to rein on variously defined versions of unhealthy competition and greed very much at the root of most of the exposures that many banks are currently being rewarded for by the central bank itself. Although, the current regime is prepared to give this idea a very serious push, it nevertheless has its roots in the regime before now.

The CBN had reasoned quite erroneously that unbridled competition was the cause of Nigeria's version of the financial crisis and had accordingly stated that "given the unusual global crisis and the consequent impacts on Nigeria, there is a need to moderate competition and lay greater emphasis on the safety and soundness of the system." Although reference was made to unhealthy competition implying that there was a healthy one, sweeping action is nevertheless tilted towards the moderation of competition generally. This notion understandably flows from some of the myths about the cause of global or Nigeria's economic or financial crisis which tries to situate it on such factors as entrepreneurial greed, deregulation or over concentration of key economic activities in the hands of private persons etc. Let's examine the concept of greed for instance. Is it bad to legally and legitimately buy up all the stocks in the Nigerian stock market at a price that will give you tremendous gains with loans that are legitimately obtained from the banks? Definitely not! It can be interpreted as normal business smartness or risk taking geared to make more profit. This can only be different if the pursuit of higher profits means greed. Again, is it greed for the banks to legitimately lend increasingly higher amounts at lower rates to individuals with eased conditions in order to earn more income? I do not think so. But then if these actions were based on greed then it is not the individual actors that ought to be blamed but the person who has given room for extremely relaxed lending conditions which gave access to tremendous amounts of credits and exposed the banks to massive unsecured loans. That person/institution is the central bank. So the crisis was fundamentally the result of incentives that encouraged irresponsible behaviour within the financial system.

But some competition can actually be unhealthy. For healthy competition, the focus of the competing participants is to do very well and beating one or more persons in the process. In the animal kingdom, a competition is a do-or-die affair because of limited resource availability. This is not exactly the case with humans who possess the ability to expand resource availability through new discoveries. However the equivalence of such do-or-die is the desperation which is often manifested by competing participants. Where this desperation leads to unethical conducts, competition becomes unhealthy; otherwise it remains the same competition which is the force for human economic progress. But another variant of the same unhealthy competition is a consequence of the undermining of the objective of competition which is primarily to do well and beat some other participants. Examples include (a) situations where some competitors have undue advantage and are able to access information for competing when others are denied such privileges (b) some of the competing firms can violate rules and walk away unscathed while others will do the same thing and get seriously penalized for that. Other situations exist where some competitors can easily de-market others and walk away even though they are known. We think that it is noble if this is what the central bank really wants to eliminate. It is however debatable whether that is the case. But in an era of full disclosure how can demarketing possibly gain strong ground? Every important thing

concerning the bank would have been known.

It is the profit expectation that guides the actions of the entrepreneur, to that extent it is equally same expectation that drives market. Accordingly the overall economic growth and development of a country in turn depends essentially on how profitable the various entrepreneurial activities within the economy are. Thus, when more of the firms in the economy are recording positive economic value added (economic profits) there is natural expansions in real output and to some extent qualitative economic developments. The reverse is true. In turn profit arises because the entrepreneur is smart enough to discover gaps and inefficiencies in overall market co-ordination and is able to quickly fill them or take appropriate advantages as the case may be. Filling these gaps and taking advantage of such market disco-ordination defines the value which the entrepreneur brings and for which he earns profit subject to the correctness of the entrepreneurs judgment in attendant aspects of same activity.

But the entrepreneur of a businessman is never allowed to swim in clean water. As soon as other entrepreneurs notice or suspect the profit-making moves of the first, they quickly enter the same market. Thus competition becomes inevitable. But it is the pressure of competition or the avoidance of its intensity and profits to be made that leads to the various actions of the entrepreneur in trying to leverage the disco-ordinations in the market. The end result is the creating of more economic value and profits. These created values are in turn enjoyed by more persons. Now in so far as these are done within the ambits of the laws, in compliance with regulator-dictated operational codes as well as the firm specific standards, there is nothing wrong with how much of such profits that are made. On the contrary the actors should be encouraged to make more of such profits which is known to obviously rub-off positively on many more economic agents.

The CBN's attempt at negotiating or persuading banks to anchor their profit drive around a particular figure or indicator as they may eventually decide will not be at the interest of the financial services industry. For now it may look as suasion but if allowed may turn out to be a form of profit-regulation. This should be resisted by banks particularly those ones that comply fully with codes of corporate governance and credit administration. The height of the futility of the intention is that it will not even curb the so-called greed and unhealthy competition. The apex bank should therefore rethink that strategy and do more in the area of building strong structures and processes for monitoring compliance and abuses which it has started on a strong and positive note rather than negotiating how prosperous a bank should be or not. And any bank management that therefore gives its shareholders the lame excuse that they are trying to comply with any profit target or benchmark set by or agreed with the CBN while other competitors are doing much better within same industry ought to be fired.

***Martin Oluba, Ph.D., DBA is the President/CEO of ValueFronteira Limited.  
martin@valuefronteira.com***