

## APPENDIX C

### GLOSSARY OF SELECTED TERMS

**Approvals in Principle:** This refers to the granting of a permit to any financial institution to operate pending the time it would meet the necessary requirements for operation that would then qualify it for a formal licence.

**Distressed Banks:** These are banks with problems relating to illiquidity, poor earnings and non-performing assets. The extreme case of distress is referred to as insolvency, which implies that a bank's liabilities are more than its assets.

**Prudential Guidelines:** These are guidelines and practices which all licensed banks are required to adhere to in reviewing and reporting their performance, particularly in the areas of credit portfolio classification and disclosure; provision for non-performing facilities, interest accrual; classification of other assets; and off-balance sheet engagements.

**New Issues** are securities raised in the primary market for the first time.

**Offer for Subscription** is an invitation by a company to the public to subscribe to new issues. This increases the capital base of the company.

**Rights Issues** are shares offered to companies' existing shareholders in proportion to the number of shares held and usually at below market price to make the offer attractive.

**Offer for Sale** is an offer to sell existing shares by shareholders to the public. The sale is effected usually through stockbrokers and does not affect the capital base of a company.

**Debentures** are fixed interest-bearing securities. They are usually of two types, debenture with floating charge and debenture with fixed charge. Debenture holders are creditors to the company rather than owners.

Preference Shares are shares of companies on which dividends must be paid before any other shares.

**Market Capitalisation** is the market value of a company's issued share

capital. It is the product of the current quoted price of shares and the number of shares outstanding. The term is also used as performance indicator of the capital market.

**Money Supply** or money stock refers to the total value of money in the economy and this consists of currency (notes and coins) and deposits with deposit money banks. For purposes of policy, there are two variants of money supply in Nigeria – M1 and M2. M1 is the narrow measure of money supply which includes currency in circulation with the non-bank public and demand deposits (current accounts) at the deposit money banks. M2 is the broad measure of money supply and includes M1 and savings and time deposits at the deposit money banks. Savings and time deposits are also called quasi-money. M2 measures total liquidity in the economy. Excess liquidity is the amount of liquidity over and above the optimum level of liquidity determined by the levels of output and prices.

**Bank Credit** is a major determinant of the money supply and it embraces the amount of loans and advances given by the CBN as well as deposit money banks to economic agents. This is the banking system credit to the economy which can be broken down into bank credit to government and the private sector.

**Ways and Means Advances** constitute a portion of credit by the CBN to the government. These are temporary loans to government to bridge short-fall in revenue. Statutorily, the CBN is not to give more than 12.5 per cent of government's current revenue.

**Other Assets (net)** is the other assets of CBN, deposit money banks less (their) other liabilities.

**Net Foreign Assets (NFA)** constitute the foreign exchange holdings of the CBN and the deposit money banks after netting out the claims of foreigners. Changes in NFA should reflect developments in the balance of payments. A deficit in the balance of

payments will lead to a decrease in foreign asset holdings and ultimately the money stock. A surplus in the balance of payments produces the opposite effect.

**Interest Rate** is the price of money. It is the opportunity cost of holding money and the return for parting with liquidity.

**Cost of Capital** is the cost incurred in securing funds or capital for productive purposes. The costs include interest rate, legal administrative and information search charges. This means that cost of capital is likely to be greater than or equal to interest rates on loans.

**Reserve Requirement** refers to the proportion of total deposit liabilities which the deposit money banks are expected to keep as cash in vaults and deposits with the CBN. The CBN can control the money stock by varying the requirement as desirable. Usually, banks keep reserves over and above the legal requirement for safety. The cash ratio requires the deposit banks

to keep a certain proportion of their total deposit liabilities in cash balances with the CBN, while the liquidity ratio stipulate the proportion of total deposits to be kept in specified liquid assets mainly to safeguard the ability of the banks to meet depositors' cash withdrawals and ensure confidence in the banking system. The CBN also has powers to call for special deposits from banks for the purpose of controlling liquidity.

**Monetary Base or high-powered money or reserve money** comprises certain liabilities of the CBN and includes currency with the non-bank public and total bank reserves. The main sources of the monetary base are net foreign assets of the CBN, net claims on government, claims on government, claims on deposit money banks and other assets (net) of the CBN.

**Open Market Operations** involve the discretionary power of the CBN to purchase or sell securities in the financial markets in order to influence

the volume of liquidity and levels of interest rates which ultimately will affect the money supply. When the CBN sells financial instruments, the liquidity (excess reserves) of the banking system reduces. This restricts the capacity of banks to extend credit or induce monetary expansion. On the other hand, when the CBN purchase such instruments, it injects money into the system and banks' ability to expand credit is enhanced.

**Fiscal Deficit** refers to the excess of expenditure over revenue of the government. It is usually assessed by its size in relation to nominal Gross Domestic Product (GDP). The fiscal deficits may be financed in various ways – external borrowing and internal borrowing (banking system and non-bank public). It is inflationary when financed by the banking system, especially the central banks.

**Total Reserves** – the sum of required reserves and excess reserves.

**Required Reserves** are a fraction of deposit money banks' money held for the purpose of backing up their deposit operations and partly to control the level of liquidity in the economy. They are made up of cash reserves and liquid assets, and specified in the form of ratios. The cash reserves ratio is the percentage of deposit money banks cash deposits with the CBN in relation to their total demand, savings and time deposits. The liquidity ratio is the percentage of banks' liquid assets to their total deposits liabilities.

**Vault Cash:** Deposit money banks keep "petty cash" in their vaults for emergency transactions before they can access their accounts with the CBN. The amount so kept is called vault cash.

**Discount House** is a financial institution devoted to trading in government secondary instruments (treasury bills and certificates and other eligible instruments). The discount house submits bids from authorized dealers, including its needs

for OMO instruments, to the Central Bank and facilitates the payments and settlement of the transactions.

**Nominal Interest Rate:** This is the actual rental value paid for the use of money or credit. It includes the effects of inflation and uncertainty.

**Real Interest Rate:** This is the nominal interest rate adjusted for expected inflation. To encourage savings, real interest rate is expected to be positive.

**Savings Deposit Rate:** The savings deposit rate is the amount paid by banks for funds withdrawable after seven days' notice. This restriction is however, seldomly applied.

**Fixed Deposit Rate:** When deposits are for a fixed period of time, say 90 or 180 days, the interest rates paid are called fixed deposit rates. They normally attract higher interest rates, while early withdrawals may attract interest penalties.

**Minimum Rediscount Rate:** This refers to the amount that is charged by the CBN for lending to banks in the

performance of its function of lender of last resort and also as a signal of the desired direction of monetary policy.

**Prime Lending Rate:** This is the interest rate applied to loans made to customers with the highest rating. For each bank, this rate also represents the minimum lending rate.

**Maximum Lending Rate:** This refers to the rate charged by banks for lending to customers with a low credit rating

**Inter-Bank Interest Rate:** This is the rate that applies to transactions among banks, mostly for overnight and other short-term funds.

**Cost of Funds:** This refers to net expenses incurred in raising funds including a reasonable profit margin. The expenses include the interest on deposits, reserve requirements, other administrative expenses, etc, as a proportion of total funds borrowed.

**Yield Curve:** Shows the relationship between the rate of interest and the time to maturity of different financial assets.

**Exchange Rate:** This is the price of one currency in terms of another.

**Foreign Exchange:** This is a means of international payments. It includes currencies of other countries that are freely acceptable in effecting international transactions.

**External Reserves:** These are portions of foreign exchange receipts saved by the monetary authorities for the purpose of enhancing the creditworthiness of the economy, protecting the international value of the domestic currency and financing temporary shocks in the balance of payments. Reserves are held in the form of monetary gold, reserve position at the International Monetary Fund (IMF), Special Drawing Rights (SDRs) and foreign bank balances.

**External Assets:** These are the reserves held by the monetary authorities as well as the banking and non-bank public, in foreign countries. Thus, external assets are external reserves and private sector holdings of foreign exchange.

**Balance of Payments (BOP):** These are records of economic transactions between the residents of a country and the rest of the world during a given period of time. The major components of the BOP are the **current account, the capital account and the official settlement balance**. The current account comprises transactions arising from the sale or purchase of goods and services and unrequited transfers, while the capital account is the record of assets and financial transactions. The official settlement account is used to equalise any imbalance that may exist in the current and capital accounts so that all the BOP accounts sum to zero.

**The Nominal, and Real Exchange Rate:** The nominal exchange rate is the price of one currency relative to another. The real exchange rate is the nominal exchange rate deflated by changes in relative prices. **Foreign Exchange and Balance of Payments Position:** Foreign exchange position is the difference between foreign

exchange receipts and foreign exchange disbursements. If receipts are higher than disbursements, there is a net inflow or an accretion to reserves. On the other hand, if receipts are lower, there is a net outflow and reserves would be depleted. Balance of payments position is the difference between the receipts by the resident of one economy from the rest of the world and the payments by residents to the rest of the world. An excess of receipts over payments shows a balance of payments surplus, while the reverse represents a deficit. When foreign exchange receipts and payments are adjusted for valuation changes in reserves, the net position would be identical to the balance of payments position.

**Internal Balance:** This refers to a state of convergence between domestic output and absorption or expenditure. When output is identical with expenditure, internal balance is considered achieved, and the rate of

inflation is expected to be stable. The achievement of the savings-investment identity is also viewed as internal balance. Monetary and fiscal policies, and external debt management measures are usually applied to achieve internal balance.

**Dutch Auction System (DAS):** This is a method of exchange rate determination through auction where the bidders pay according to their bid rates. The ruling rate is arrived at with the last bid rate that clears the market where the authorities elect to operate a single exchange rate.

**Liquidity Ratio:** This ratio is defined as the ratio of total specified liquid assets to total current liabilities and reflects the liquidity position of a bank.

**Fiscal Operations:** This refers to government financial transactions involving collection, spending and borrowing of the government for a given period.

**Government Expenditure:** Payment or flow of financial resources out from government.

**Recurrent Expenditure:** Expenditure on goods and services (other than capital assets) used in the process of production within one year. Interest on loan is included.

**Capital Expenditure:** Payment for non financial assets used in production process for more than one year. Loan amortization (capital repayment) is included.

**Debt stock/GDP:** This measures the level of domestic indebtedness relative to the country's economic activity.

**Federation Account:** This is an account opened by the Federal Republic of Nigeria into which all revenues of the Federation is paid for eventual distribution by all tiers of government in Nigeria.