

THE ROLE OF COMMUNITY BANKS IN ECONOMIC DEVELOPMENT: A NIGERIAN CASE STUDY

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Abstract

The Decree 46 of 1992 created the National Board for Community Banks which was granted the power to license community banks. Community banks were created to: (1) promote rural development through provision of banking and financial services, (2) enhance rural productive activities, and (3) improve economic status of small-scale producers in rural and urban areas. According to Marx (2004), Nigeria has a dynamic informal financial sector. A key to growth strategy is to assist the development of this informal sector. The recent government policy to rid the economy of community banks defeats the original purpose underlying the creation of community banks. In view of the important role of community banks in Nigeria, the authors propose that community banks should continue to be rural financial institutions with specialized methods to serve broad segments of the rural population. The National Board for Community Banks should be vested with power to license, monitor and regulate community banks, and the regulatory power of the Central Bank of Nigeria over community banks should not go beyond that necessary for the performance of its monetary policy function. Furthermore, a partnership should be formed between the National Board for Community Banks, National Association of Community Banks and the Nigeria Agricultural, Cooperative and Rural Development Bank for the purpose of funding rural ventures through loan syndication. The Bankers' Committee initiative for small and medium enterprises funding should be channeled through the Nigeria Agricultural, Cooperative and Rural Development Bank.

Keywords: community banks, banking, economic development, Nigeria

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1. INTRODUCTION

In September 2000, the nations of the world under the umbrella of the United Nations adopted a concerted approach to tackle world development problems through the Millennium Development Goals (MDGs). The MDGs include eradication of extreme poverty and hunger, achievement of universal primary education, promotion of gender equality, reduction of child mortality, improvement of maternal health, combating HIV/AIDS, malaria and other diseases, assurance of environmental sustainability, and development a global partnership. In line with MDGs, the Nigerian government took a bold step to address poverty alleviation in all its ramifications by introducing the National Economic Empowerment Development Strategy (NEEDS). This program is derived from the urgent requirement for transparency in governance and value orientation. Therefore, the bedrock of NEEDS is its vision of a Nigeria with a new set of values and principles, which will facilitate the achievements of national goals of wealth creation, employment generation and poverty reduction.

Therefore, NEEDS is fashioning for Nigeria, a common ground for all economic agents to interplay, in a healthy and sustainable manner. The objectives of NEEDS are mainly threefold:

- Poverty Reduction;
- Employment Generation; and
- Wealth Creation

Given that a significant number of Nigerians live in the rural areas, any poverty alleviation program should be concentrated in the rural communities. Nolan (2003) argues that economic growth and entrepreneurship are interdependent. Moreover, Nolan notes that public programs designed to improve lives in disadvantaged communities were responsible for developing a community in Camden, a borough in London. Carpenter (2001) reports that small and medium scale enterprises (SMEs) help to promote industrial and economic development in Nigeria. Carpenter also reports that SMEs account for 10 percent of total manufacturing output and 70 percent of industrial employment in Nigeria. More important is the funding of SMEs in order to make them relevant for economic growth and development. Moreover, since financial capital is an important ingredient of any poverty alleviation program, the focus should then be on the role of rural financial institutions and markets (Carroll, 2005). According to Bagehot (1873), banks play an active and innovative role by identifying and funding economically worthwhile projects. This point of view is emphasized by Keynes (1936 p. 82) who notes that: "If the grant of a bank credit to an entrepreneur additional to the

credits already existing allows him to make an addition to current investment which would not have occurred otherwise, income will necessarily be increased and at a rate which will normally *exceed* the rate of increased investment."

An efficient financial structure is a critical ingredient of any strategy which leads to economic growth and development (Bagehot, 1873; Schumpeter, 1934). Such a structure helps to generate investment and consequently increased productivity and employment. In a study of industrial and developing countries, Calderon and Liu (2003) report results which suggest that financial development leads to economic development. Levine (1996, 1997) popularizes the view that existence of well-functioning financial institutions and markets are an impetus to technological innovation. This is because the institutions and markets provide funding for entrepreneurial undertakings in innovative products. The role of financial institutions is to promote entrepreneurship.

Nolan (2003) examines that various ways that new but small business enterprises can positively contribute to economic development. These include an enhanced provision of services for local consumers with a resultant increase in local income retention. Another avenue is through employment and income growth which lead to indirect employment and an increased tax revenue base. Osuntogun and Oramah (1992) consider small scale enterprises to have a special role in contributing to employment creation, reducing regional economic imbalance, mobilizing and utilizing resources and developing entrepreneurship culture in Nigeria.

One notable issue in the financial economics literature is that financial markets develop at different rates in different economies. This creates a vicious circle in an economy when financial institutions tend to cluster in high-income areas. This situation begs the question: do financial markets drive economic growth or does economic growth drive creation of financial markets? In a report by Aryeetey et al. (1996) on the financial market fragmentation in Sub-Saharan Africa, the informal financial institutions are found to possess specialized skills for serving the isolated sectors of the population. Yunusa (1998) argues that successive efforts to break the cycle of poverty in Nigeria through several rural finance and development programs had failed. Yunusa observed a lack of the mechanisms needed to encourage savings mobilization at the grassroots level. Based on the foregoing, the objective of this paper is to explore the role designed for community banks in Nigeria's economic development. Moreover, has the role of community banks been met, and, if not, what can be done to refocus community banks to play their role in rural economic development?

2. POVERTY AND POVERTY ALLEVIATION IN NIGERIA

Several poverty alleviation programs had been instituted by successive governments in Nigeria. Ogwumike (2002) dichotomizes these programs into pre-structural adjustment (pre-SAP) programs and post-structural adjustment (post-SAP) programs. The pre-SAP programs include the 1977 rural banking scheme which was set up to achieve at least a branch bank in every local government area in the country. Yunusa (1998) comments on the success of the scheme in terms of meeting the numerical target, but she points out the failure of rural branches to meet the credit needs of the rural people. Other programs include the creation of River Basin Development Authorities, Operation Feed the Nation, Green Revolution, Low Cost Housing Scheme, Agricultural Development Programs, Agricultural Credit Guarantee Scheme, and, the Rural Electrification Scheme. The initial success of these programs could not be sustained because the programs failed to meet the objectives for which they were established (Ogwumike, 2002). Other inadequacies of the programs observed by Ogwumike include, policy instability, a lack of political will and commitment and insufficient involvement of the beneficiaries.

The Post-SAP programs established include Directorate of Roads and Rural Infrastructure, National Directorate of Employment, Better Life Program, Family Support Program and the Family Economic and Advancement Program. In 1989, the Federal Government of Nigeria set up the People's Bank to encourage a savings culture in both rural and urban areas of the country. It was also expected to provide credit facilities for the underserved members of the society. Obadan (2002) concludes that all the poverty alleviation programs employed in Nigeria were ineffective and ineffectual because poverty is still widespread in the country.

A selection of measures of development for Nigeria, are reported in Table 1. In terms of manufacturing capacity, there is a slight increase each year from 1998 through 2003. The number of commercial and merchant banks has been steady at about 90 while the number of community banks declined. Akanji (2002), reports that the level of poverty in Nigeria grew by 50 percent between 1980 and 1985. Moreover, from 1985 through 1992, poverty level dropped slightly. Table 2, gives an overview of an increasing level of poverty in Nigeria since 1980. Tomori et al. (2005) report the widespread as well as the severity of poverty in Nigeria. For example, in 2000, there are seven people in ten who survive on less than a dollar per day in Nigeria.

Table 1. Selected Social and Economic Indicators in Nigeria, 1998-2003

	1998	1999	2000	2001	2002	2003
Life Expectancy (yrs)	53	54	54	54	54	57
Infant Mortality (per 1000 births)	75.1	75.1	74.18	73.34	72.49	71.35
Real GDP Growth Rate (%)	2.4	2.8	3.9	4.2	4.1	3.8
Manufacturing Capacity (%)	32.4	35.9	36.1	39.6	44.3	46.2
Credit to Private Sector (rate)	27.4	29.2	30.9	43.5	19.7	27.1
Growth of Banks' Loan/Advances (%)	126.1	21.6	42.0	36.5	15.7	23.2
Inflation Rate	10.0	6.6	6.9	18.9	12.9	14.0
GDP Per Capita (US \$)	312.84	333.26	418.99	417.22	434.10	384.71
Inter-Bank Interest Rate	17.3	23.4	13.47	24.61	14.14	25.75
# of Merchant & Comm. Banks	89	90	90	90	90	89
# of Community Banks	1015	1018	769	769	769	n.a.

Sources: Central Bank of Nigeria & CIA World Factbook

Table 2. Poverty in Nigeria (% of Population on Less Than US\$1 Per Day

Year	Percentage of Population in Poverty
1980	27.0
1985	46.0
1992	42.0
1996	67.0
2000	70.2

Sources: Federal Office of Statistics (National Consumer Surveys) & UNDP

3. COMMUNITY BANKS IN NIGERIA

Following the introduction of structural adjustment program (SAP) in Nigeria in 1986, a significant number of commercial banks became distressed and many healthy banks closed their rural branches (Aderibigbe, 2002). In view of the aforementioned, the Federal Government established the People's Bank in 1989 and in 1990 created a regulatory environment for Community Banks to be established.

The Central Bank of Nigeria defines a community bank as a self-sustaining financial institution owned and operated by a community or a group of

communities to provide financial services to members of its community. In view of the foregoing, community banks were meant to fill a void created by the formal financial institutions within the Nigerian economy. According to Marx (2004), Nigeria has a dynamic informal financial sector. A key to growth strategy is to assist the development of this informal sector.

The Decree 46 of 1992 created the National Board for Community Banks which was granted the power to license community banks. According to the aforementioned Decree 46, community banks were created to: (1) promote rural development through provision of banking and financial services, (2) enhance rural productive activities, and (3) improve economic status of small-scale producers in rural and urban areas (Ayadi and Ogunsemore, 1995; Okoye and Okpala, 2001).

In a recent publication, the Deputy Governor of the Central Bank of Nigeria (CBN) was quoted to imply that community banks are failing in their duties to the rural communities (Komolafe, 2005). According to the CBN officer, the host communities where community banks mobilize deposits do not benefit from credit disbursements. In the same vein, the World Bank (2000) report argues that the performance of community banks has been disappointing. In terms of growth of assets, the World Bank report indicates that the observed overall performance between 1996 and 1998 was quite modest. Yunusa (1998) reports a more positive view of community banks in Nigeria. According to her, community banks have been successful in credit mobilization and the provision of a credit mechanism to people who would have otherwise been marginalized by modern financial institutions.

Table 3. Average Balance Sheet of Community Banks in 2003

ASSETS	PERCENTAGE	LIABILITIES	PERCENTAGE
Cash	3	Paid-Up Capital	14
Balance with Banks	16	Reserves	7
Placements	23	Current Year's Income	5
Investments	8	Total Owners' Funds	26
Loans and Advances	35	Placement from Banks	0
Fixed Assets	9	Deposits	63
Other Assets	6	Long-Term Loans	0
	—	Other Liabilities	12
TOTAL	100	TOTAL	100+

Source: Marx (2004) Note: Total exceeds 100 because of rounding error.

Table 3 represents a cursory view of the balance sheet of a typical community bank in 2003. The community bank owners contribute 25 percent of its total resources and depositors account for about 63 percent. A significant 35 percent of community banks' resources go into loans and advances while 23 percent are channeled into placements.

Table 4.
Average Deposits of a Typical Community Bank (NGN millions): 2000-2003

TYPE OF ACCOUNT	2000	2001	2002	2003
Demand Deposit	4.830	7.156	8.243	8.448
Savings	8.867	13.572	16.199	19.287
Time Deposit	1.736	3.175	4.561	3.327
TOTAL	15.433	23.903	29.003	31.062

Source: Marx (2004)

Table 4 shows that average deposits grow steadily from 2000 through 2003. This is consistent with the World Bank report (2000) which shows a deposit growth rate of 17 percent in 1997 and 20 percent in 1998. The growth in deposits is more pronounced for smaller community banks than either the medium scale or the largest banks.

Table 5. Selected Financial Ratios for Nigeria's Community Banks

Financial Ratio	Year			
	2000	2001	2002	2003
Pre-tax Profit/Average Assets	0.04	0.06	0.05	0.04
Loans/Deposits	0.47	0.49	0.52	0.55
Equity/Assets	0.37	0.37	0.36	0.38
Savings/Total Deposits	0.57	0.57	0.56	0.60
Cash/Total Deposits	0.75	0.72	0.68	0.80
Expenses/Gross Earnings	0.68	0.61	0.61	n.a.

Source: Marx (2004)

Marx (2004) reports that 804,605 depositors were served by community banks in 2003 while 59,805 were granted loans. Furthermore, community banks influence the mobilization of savings and financing of micro- and small enterprises in the rural areas. Table 5 shows improvements in

loans/deposits, savings/total deposits and expenses/gross earnings between 2000 and 2003. In terms of profitability, community banks have reported modest results. Marx (2004) notes, that community banks became increasingly viable between 2000 and 2002.

Table 6. Zonal Density Distribution of Community Banks in 2002

ZONE	COMMUNITY BANKS PER 100,000 PEOPLE (AVERAGE)
Bauchi	0.23
Benin	0.85
Enugu	1.38
Kaduna	0.20
Lagos	1.13
Makurdi	0.48
Minna	0.34
Uyo	0.60

Source: Marx (2004)

Table 6 shows the zonal density distribution of community banks in Nigeria in 2002. The distribution of community banks is uneven. Enugu zone with the highest concentration has about 1.38 banks per 100,000 people. In Kaduna zone, it is about one bank to about 500,000 people. This is an indication that there are relatively fewer community banks than optimal in Nigeria. According to Marx (2004), although two-thirds of all community banks are located in the rural areas, more needs to be done to increase the number of community banks in the country.

In spite of the many strides achieved by community banks in Nigeria, these institutions are still beset by a myriad of problems which range from insider-related credits, poor and ineffective management, poor credit administration and lack of transparency in operations. According to Komolafe (2005), community banks also experience problems with level of capitalization. There is a lack of automated information processing systems and a competitive service delivery culture.

A new policy was unveiled in December 2005 by the Central Bank of Nigeria. Under the new dispensation, two categories of Micro-Finance Banks (MFBs) would henceforth be licensed by the apex bank. The two categories are: Unit banks and State banks. The Unit banks are one-branch financial institutions which are licensed to operate in local government areas with a

minimum capital requirement of twenty million naira. On the other hand, State banks can operate several branches within a state but must meet a minimum capital requirement of one billion naira.

According to Okwe (2005), all community banks in the country are expected to transform into micro-finance banks by December 2006 by meeting the appropriate capitalization requirements. A community bank that is unable to meet the minimum capital requirement would have its license revoked. The Nigerian President, Chief Obasanjo remarks that MFBs are expected to engage in aggressive mobilization of savings from small depositors in order to shore up their operating funds (Okwe, 2005).

4 COMMERCIAL BANKS AND SMEEIS SCHEME

According to Sanusi (2004), failure of several intervention measures in the development of small and medium-size businesses in Nigeria, led to the creation of a Small and Medium Enterprises Equity Investment Scheme (SMEEIS) in 2001. The SMEEIS scheme is a voluntary initiative of the Nigerian Bankers' Committee. The Nigerian Bankers' Committee, at its December 1999 meeting made a decision to set aside ten percent of each member's annual profit after tax for equity investment in small and medium enterprises (SMEs). In a revised version of the scheme, banks would reduce their annual contributions from ten percent to five percent after five years. The specific objectives of the scheme included economic growth stimulation, local technology development and employment generation. The program was also meant to facilitate the flow of funds for new projects by SMEs as well as expansion and reactivation of on-going projects.

Under the SMIEIS program, the annual cumulative contribution would be invested in equity of SMEs. Equity investment by a bank can be in the form of fresh cash injection or a conversion of existing loans to participating SMEs. Moreover, the member banks would provide financial, technical and managerial advisory support services to beneficiary SMEs. Eligible SMEs are required to register as limited liability companies, as well as comply with all tax laws and regulations in Nigeria. The program covers almost all types of legal business activities except trading/merchandising and financial services.

According to a report by the Central Bank of Nigeria (2005), as of May 31, 2005 the total fund set aside for the SMEEIS reached 30.997 billion naira. Of this amount 9.379 billion naira was the cumulative investment in 187 projects. Sixty-four percent of the invested amount was in the real sector of the economy consisting of construction, agro-allied, manufacturing, printing

and publishing enterprises. The remaining 40 percent went into service-related enterprises. In terms of geographical spread, Lagos state alone (out of 36 states in Nigeria) accounts for about 59 percent of the total amount invested. About 12 states in Nigeria had not benefited from the SMEEIS.

In a recent publication, Obe (2005) reports, that the stakeholders in the SMEEIS blamed the Nigerian government for the low level of development in the small and medium enterprises sector. According to Obe, the project manager for the Nigeria Employers' Consultative Association notes that SMEs continue to face difficulties to access the funds set aside for them under the scheme. Other impediments to the operation of the program include inadequate managerial capacity, high energy cost, bureaucratic bottlenecks in the processing of import/export documents and inadequate physical infrastructure.

5. SUMMARY, CONCLUSION AND POLICY RECOMMENDATIONS

Ogwumike (2002) argues that the poverty alleviation programs instituted in Nigeria failed because they deviated from their original focus. Akanji (2002) concludes that the programs failed because many of them were largely irrelevant, urban-structured, dominated by government with credit system directed to favor the elites in the society. Moreover, the semi-banks created faced several problems including overbearing administrative and personnel costs. The lending procedure placed on the laps of the semi-bank institutions was tortuous. Anyanwu (2004) also notes that the operations of micro-finance institutions in Nigeria are relatively new because most of them were registered after 1981.

As stated earlier in this paper, the Decree 46 of 1992 created the National Board for Community Banks (NBCB) and granted it the power to license, and oversee the activities of community banks in Nigeria. On the other hand, the 1997 amendment to the Banks and Other Financial Institutions Act (BOFIA of 1991), brings all depository institutions, including community banks, under the supervisory purview of the CBN. This happened without a repeal of Decree 46 of 1992. In 2002, the Central Bank of Nigeria, without recourse to the National Board of Community Banks (NBCB), gave directives to community banks on rendering of accounts, inspection of accounts and training of personnel (ThisDay, 2002). According to ThisDay, this amounts to over-regulation which defeats the original intent of taking banking to the grassroots.

Community banks were meant to fill a void created by the formal financial institutions within the Nigerian economy. According to Marx (2004),

Nigeria has a dynamic informal financial sector. A key to growth strategy is to assist the development of this informal sector. Moreover, every community bank should reflect the peculiarities of its locality. The Punch (2005) argues that the community banking system has gained widespread acceptance in Nigeria through its positive impact on the rural economy. Though limited, community banks have succeeded in providing financial services to rural and semi-urban segments of the Nigerian population where no other institutions have been successful (Marx, 2004; Marx, 2004; Yunusa, 1998; Ejiofor, 1994; Ik-wu, 2001; Mabogunje, 1993; Onugu, 2000; The Guardian Online, 2004).

Aryeetey et al. (1997) observe that African financial markets are fragmented because of the weak linkages between the formal and informal segments of the market. More importantly, informal financial institutions in Sub-Saharan Africa use specialized methods to serve broad segments of the population who lack access to the formal financial institutions. The authors of the paper conclude that, greater efforts are required to integrate the informal institutions into the financial development strategies in Africa. Yunusa (1998) argues that community banks in Nigeria have succeeded in serving as credit mobilization and provision mechanism to the segment of the population that has been marginalized by modern banking institutions.

The detractors of community banks and the monetary authorities in Nigeria have capitalized on the collapse of several community banks in the 2001. There was also the inherent weakness of the NBCB to monitor and enforce rules and regulations within the industry. These arguments do not warrant scrapping community banks and replacing them with Micro Finance Banks. The turmoil within the banking industry which led to the collapse of several banks and finance houses also affected community banks. Table 3 shows that a typical community bank places about 23 percent of its funds with commercial banks. A crisis in the banking industry would logically have an effect on the operations of community banks (The Punch, 2005; Ogujiuba et al., 2004). The contradictory regulatory environment renders the NBCB powerless as the CBN turned it into a lame duck.

The statistics in Table 6 show that there is room within the financial landscape in Nigeria for more community bank-type institutions to grow. Many community banks in Nigeria were established using already existing rotating savings and credit associations. The existence of community banks was a catalyst to the development of linkage banking. According to Seibel (1999), linkage banking emphasizes linkages between self-help groups and between savings and credit. Community banks represent a viable means of channeling credit into the rural sector based on a high standard of trust and credibility (The Punch, 2005). The recent policy reversal on the part of the Central Bank

of Nigeria and government which removes community banks from the financial landscape in Nigeria is purely wrong and obviously a misadventure.

It is a worthy attempt to create micro-finance institutions in Nigeria to complement the efforts of existing community banks. The government should as a matter of urgency allow community banks to continue to be rural financial institutions with specialized methods to serve broad segments of the rural population. Moreover, the National Board for Community Banks should be vested with the power to license, monitor and regulate community banks. The regulatory power of the Central Bank of Nigeria over community banks should not go beyond what is necessary for the performance of its monetary policy function. A partnership should be formed between the National Board for Community Banks, National Association of Community Banks and the Nigeria Agricultural, Cooperative and Rural Development Bank for the purpose of funding rural ventures through loan syndication. The Bankers' Committee initiative for small and medium enterprises (SMEEIS) funding should be channeled through the Nigeria Agricultural, Cooperative and Rural Development Bank. The newly established Micro Finance Institutions should also be brought into partnerships with community banks for the purpose of financing rural projects and enterprises. As the major regulatory body for community banks, the NBCB should become my dynamic in training bank personnel and also providing avenues for banks to have access to technology. Community banks are too important because of their specialized skills in dealing with the rural people, to be sidetracked, in any attempt to alleviate poverty in the rural communities of Nigeria.

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Résumé

Les banques communautaires au Nigeria ont été créées pour promouvoir le développement rural et améliorer les conditions des petits producteurs ruraux et urbains à travers l'offre de services financiers. Au Nigeria le secteur informel est dynamique; une stratégie clé pour la croissance est le développement de ce secteur. En vue de l'importance des banques communautaires, les auteurs proposent que ces banques doivent continuer à opérer au niveau rural, sous la supervision du Conseil National des Banques Communautaires. La Banque Centrale devrait limiter son activité au contrôle fonctionnel à la politique monétaire. Les auteurs suggèrent aussi une coordination des acteurs qui opèrent au niveau rural pour le soutien financier des opérateurs ruraux.

