PDF - BANK SPECIFIC ATTRIBUTES AND OFF BALANCE SHEET ACTIVITIES OF QUOTED DEPOSIT MONEY BANKS IN NIGERIA - researchcub.info**CHAPTER ONE**

INTRODUCTION

1.1Background of the Study

In the recent decades, banking deregulation, technological changes, financial deepening and innovation have lead to a more market oriented structure where firms greater than ever relying on financial market to fund their investments. This change cut across most financial markets especially in Canada, US, Europe, Asia and in different places around the world (Calmes & theoret, 2010; Calmes, 2004; Roldos, 2006). The resulting outcome is major change in corporate financing characterized by relative cut in the share of bank loan and increased share of bonds and stocks. The transformation is challenging banking business and justified, in part, with the financial deregulation where banks are increasingly allowed to act as security dealer and to offer fiduciary services and portfolio advice to investors. In addition to traditional practices, banks also begin to securitize loans, trade in financial instruments such as guarantees, commercial papers, acceptances, letters of credit, performance bonds, indemnities that are more in line with financial deepening process. These non tradition activities are loosely seen as off balance sheet activities. Off balance sheet activities therefore are transactions that are not currently recognized as assets or liability on the balance sheet but nonetheless give rise to credit risk, contingencies and commitments are reported off balance sheet. Off balance sheet activities have become an issue of global significance gathering controversy.

Off balance sheet activities expose banks to much danger such as earnings management, creative accounting, and insolvency to mention but a few through the use of Special Purpose Vehicles (SPVs). Some banks engaged in manipulating their books, colluding with other banks to artificially enhance their financial positions and consequently stock prices. Practices such as converting non-performing loans into commercial papers and bank acceptances and setting up Special Purpose Vehicles to hide losses were very common (Akintoye & Owojori, 2011). Moreover, Sanusi (2010) pointed out a series of scandal associated with SPVs such that the CEO of Oceanic Bank controlled over 35% of the bank through SPVs borrowing customers deposit. A CEO set up SPVs to lend money to themselves for stock price manipulation and purchase of estates all over the world.

Some bank management also set up one hundred fake companies for the purpose of perpetrating fraud. Sanusi (2010) also revealed that much of the capital apparently raised by the so called mega bank was fake capital financed from depositors funds and 30% of the share capital of intercontinental bank was purchased with customers deposits among others. Thus, it was discovered that in many cases, consolidation was a sham and the banks never raised the capital they claimed they did (Sanusi, 2010).

Deposit Money Banks are linked with specific attributes which impact on their off balance sheet activities either positively or negatively. One of such is credit risk. Banks engage in off balance sheet activities as a risk management instrument against the increasing credit risk (Khasawneh, 2007). Banks used off balance sheet items to generate more income and compensate for the loan losses. Credit risk relates to the risk associated with the quality of a bank earning assets, namely its loan (Tamrat, 2013).

Asset quality is also the second component of a banks CAMEL rating. Moreover, decline in asset quality lead to write off and reduced earnings from the loan portfolio (Chaudhry, 1994). Kargi (2011) pointed that credit risks are found in all activities in which the success depends on counterparties, issuer or borrower performance. Credit risk has traditionally been considered to be the most important risk for a commercial banks and poor quality asset has probably been the cause of more bank failures than any exposures to be discussed. Bennett (1986) claimed that credit risks are found in OBS activities since it provides an opportunity to increase leverage significantly without additional regulatory requirements.

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