Commercial Banking and Emerging Economies: Evidence from Nigeria

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Abstract

Economic development is about enhancing the productive capacity of an economy, by using available resources to reduce risks, remove impediments which otherwise could lower costs and hinder investment. Invariably, the role of finance in economic development is often, widely, acknowledged in literature. It has been argued that financial intermediation through the banking system played a pivotal role in economic development by affecting the allocation of savings, thereby, improving productivity, technical change and the rate of economic growth. The main thrust of this paper was to examine whether there is any significant association among commercial banking institutions and the Nigerian economy. It was also set out to investigate whether commercial banks play any pivotal role in the smooth running of the financial and commercial operations of other sectors in the economy as well as establishing whether commercial banks have contributed to the growth and development of the Nigerian economy. Survey design method through the administration of structured questionnaires was employed and the techniques of data analysis adopted were analysis of variance, t-test statistic and chi-square statistics. The study found a significant association among the banking institutions and the economy and that banks have contributed relatively to the growth and development of the Nigerian economy.

Keywords: *Commercial Banks, Economic Development, Economic Growth, Nigerian Economy, Banking Institutions*

1 Introduction

The Nigerian financial system is a conglomerate of various institutions, markets, instruments, and operators that interact within an economy to provide financial services (CBN, 1997). Commercial banking institutions, a strong component of the nation's financial system perform the enviable role of an important source of capital for the real sector of the economy. The sector had witnessed chronic systemic crisis as a result of macro-economic instability and weaknesses in corporate governance practices among others. The sector had in addition, initially failed to live up to its expectations of growing in the Nigeria economy by financing in the real sector. Instead it was grossly involved in commerce and other non-banking activities. One of the reasons why Nigerian banks could not embark on such financing is attributable to low capital base of Nigerian banks. Since the government of Nigeria, like any other nations of the world has made economic growth and development as one of its cardinal priorities there have been various reforms especially in the banking sector to change the face of the sector and turn Nigerian banks into active and strong players in the local; regional and global banking sector.

Consequently, a landmark reform was introduced into the sector in July 2004 and which has appeared brought unprecedented changes to the sector. For the first time the erstwhile low capital base of Nigerian banks have been shored up incredibly and the paucity of funds to finance the real sector is no longer an issue. However, there have been divergent views regarding the use of banks enhanced capital to finance the real economy. While some schools of thought argue that the much-orchestrated 2004 banking sector reforms has done a little if at all, to improve the state of the economy, some others have seen the reforms as a way out of Nigeria's economic quagmire and a step in the right direction toward achieving steady economic growth and economic development.

1.1 Statement of the Problem

The Nigerian economy, along with the other developing Sub-Saharan nations of Africa has been be-deviled with seemingly inexorable woes which cannot be said to be unique but exceptional in scope and persistence. Mass poverty, economic stagnation, endemic corruption, political instability, weak institutions and social conflict are some of the traces that can be found in Nigeria. As a result, it has been observed that the economic, social-political and regulatory environment in which the banks operate has remained unstable. (NDIC, 2OO2). Confronted with these challenges, the Nigerian government has repeatedly attempted to overhaul the entire economy by introducing various reform measures such as the Structural Adjustment Programme (SAP) which brought about economic liberalization. Notably, the Nigerian banking sector, like any other sector, also operates within this environment. The turbulent nature of the country, poor governance and economic decay all pose major challenges to the banking sector in Nigeria. This assertion was supported by Professor Soludo in his graphic picture of the unsatisfactorily state of the banking industry in Nigeria. The banking system was also highly concentrated, engulfed in weak corporate governance, and lacked depositor's confidence and could also not make significant impact in the global financial markets (Soludo, 2004)

Nevertheless, the central role that banks play in the development of every economy is the mobilization of resources for productive investments and serving as the conduit for the implementation of monetary policy (Sanusi, 2011). The 2004 reform which emphasized the consolidation policy was necessitated by the need to strengthen the banks. The policy thrust at inception was to grow the banks and position them to play a pivotal role in driving development across the sectors of the economy.(Sanusi, 2012). In spite of the acclaimed decay in the Nigerian economy and the systemic crisis in the banking sector, the expected role of the sector in changing the face of the economy cannot be over-emphasized. The extent to which this role has been played is the central theme of this study.

1.2 Research Questions

(i) Is there any significant association among commercial banking institutions and the Nigerian economy?

(ii) Do commercial banks play any pivotal role in the smooth running of the financial and commercial operations of other sectors in the economy?

(iii) Have commercial banks contributed to the growth and development of the Nigerian economy?

1.3 Objectives of the Study

(i) To examine whether there is any significant association among commercial banking institutions and the Nigerian economy

(ii) To investigate whether commercial banks do play any pivotal role in the smooth running of the financial and commercial operations of other sectors in the economy

(iii) To establish whether commercial banks have contributed to the growth and development of the Nigerian economy

1.4 Research Hypotheses

(i) There is no significant association among commercial banking institutions and the Nigerian economy
(ii) Commercial banks do not play pivotal role in the smooth running of the financial and commercial operations of other sectors in the economy
(iii) Commercial banks have not contributed to the growth and development of the Nigerian economy

2 The Nigerian Financial System and National Economic Development.

Sanusi (2011) observes that *“Economic development* ***is about enhancing the productive capacity of an economy by using available resources to reduce risks, remove impediments which otherwise could lower costs and hinder investment.*** *The banking system plays the important role of promoting economic growth and development through the process of financial intermediation. Many economists have acknowledged that* ***the financial system, with banks as its major component, provide linkages for the different sectors of the economy and encourage high level of specialization, expertise, economies of scale and a conducive environment for the implementation of various economic policies of government intended to achieve non-inflationary growth, exchange rate stability, balance of payments equilibrium and high levels of employment”***

The financial system of any nation on the other hand, plays important roles in the process of economic growth and development of the country. In Nigeria, the financial system has undergone remarkable changes in terms of ownership structure, the depth and breadth of instruments employed, the number of institutions established, the economic environment and the regulatory framework within which the system operates (CBN, 1997). Sanusi (2012) stresses that the financial system is just more than institutions whose main functions are to facilitate payments and extend credits, it encompasses all functions that direct real resources to their ultimate users. The financial system, according to him, is the central nervous system of a market-economy and contains a number of separate, co-dependent components, all of which are essential to its effective and efficient functioning. Mayer (1988), observes that the distinctive feature of successful financial systems is their close involvement in industry. These components of financial systems include financial intermediaries such as banks and insurance companies which act as principal agents for assuming liabilities and acquiring claims. A well-functioning financial system matters to everyone and to the economy at large. Imala (2005) opines that the banking system in any economy plays the important role of promoting economic growth and development through the process of financial intermediation. Development economists argue that the existence and evolution of financial institutions and markets constitute an important element in the process of economic growth.

Globally, it is evident that banks are essential for every economy since no country can attain any significant growth unless savings are efficiently and effectively chanelled into profitable investments. Bello (2005) posits that the banking system is known as the backbone of dynamic financial intermediation through the mobilization and channeling of financial resources. Babalola (2008) observes that the banking sector in Nigeria has undergone significant transformation both in terms of number and product creativity, and the level of operations, which was as a result of economic reform embedded in the structural Adjustment Progranne (SAP) in 1986. The Nigerian economy, like other economies, is linked to the growth of the financial system. Qgubunka (2007) contends that the Nigerian economy, like other economies is organically linked to the growth of the financial system, especially the banking sector. However, as a result of some inadequacies in the role of the banking sector in Nigeria preventing the achievement of the required heights in economic growth and development, the stage was set for a comprehensive banking sector reforms to tackle the apparent inadequacies as they affect the domestic economy.

Abdullai (2006) argues that aside the 2004 reforms, there have been instances of reforms in the Nigerian banking sector. According to him, these reforms have been introduced in response to the challenges posed by developments posed within the economy and the international payment system. Kolawole (2006) opines that banking sector reforms are designed to re-orientate and reposition the sector for attainment of an effective and efficient state and to foster the much-desired economic development. The 2004 banking sector reform which was designed to bring about significant improvement to the domestic economy was introduced Babalola (2008) observes that the banking sector reforms of 2004 have led to an upsurge in the total capital base of banks., it has also brought about an improvement in the gross domestic product and an enhancement to the performance of the banking sector. The banking sector reforms of 2004 have obviously produced positive effects on the Nigerian economy. This development has contributed immensely to setting the economy on a steady pace and a sustainable growth path.

Rostowski (1998) citing Gerschenkron (1968) argues that in the middle of the 19th century, universal banks in Germany – a combination of commercial and investment banks – strongly contributed to the industrialization of the German economy, serving as a substitute for the insufficiency of wealth and entrepreneurial expertise. Abel (2013) posits that banks are the most important financial intermediary in the economy as they connect surplus and deficit economic agents. He further notes that banks are vital institutions in any society as they significantly contribute to the development of the economy through facilitation of businesses. Hussain (2011) identifies commercial banks as the providers of loans and corporate bonds to the households, new start-ups and small medium enterprises to run their businesses. Shah (2010) claims that commercial banks are the most significant of the financial intermediaries and that they play important role in all the areas of financial intermediation except that in overcoming unemployment and encouraging young entrepreneurs, their role would depend on the policies and programmes of their stakeholders. .

Akingunola (2006) contends that economic development continues to be elusive in spite of an avalanche of strategies and measures that have been put in place to turn the economy around since political independence in 1960. Sanusi (2011) on the other hand notes that available data is showing that the macroeconomic environment has improved considerably, inflation rate has moderated at a low double digit while the prime lending rate has gone down significantly and the rate has been relatively stable; an indication that these have impacted on the growth of the real economy. However, the contribution of the banking sector to the Nigerian economy appears relative. Sanusi (2012) believes that although the banking sector has contributed to the economy, rapid financialisation in Nigeria did not benefit the real economy as much as had been anticipated. Many successful emerging markets have seen proactive government actions to ensure that the financial sector contributes to the real economy.

3 Research Methodology

The chosen designs for this study is: public survey i.e. the collection of primary data through the use of structured and close-ended questionnaires administered to a sample size of 80 selected from the working populace within the commercial and financial sector of the Nigerian economy. The sampling technique adopted is purposive sampling which is a non probability sampling method combined with a random sampling approach to select sample elements which has been considered best to provide good outcome. The questionnaires was divided into two (2) sections, Section A was designated to obtain general information relating to the personal data of the respondents. The questions in sections B were designed to obtain information related to commercial banks and the economy. Statistical software i.e. Statistical Package for Social and Science (SPSS) was used to analyze the hypotheses formulated from the data gathered and presented in respect of the study. Three hypotheses formulated are tested to arrive at the empirical findings.

Hypotheses Testing

Hypothesis 1

There is no significant association among commercial banking institutions and the Nigerian economy

Table 3.1

ANOVA

	Sum of Squares	Df	Mean Square	F	Sig.
Between Groups	23.891	3	7.964	73.512	.000
Within Groups	6.825	63	.108		
Total	30.716	66			

Source: Author's Computation 2014

From the result, it is shown that the sum of squares for between groups and within groups are 23.891 and 6.825 respectively. The mean square shows a value of 7.964 and .108 respectively. However, the F-Statistic value which helps to tell about the overall significance of a model and its goodness fit shows a value of 73.512. This result was greater than the tabulated value of 2.68, $v_{1=}v_2$ degree of freedom.

The result from the significance table shows it was highly significant. Hence we reject the null hypothesis (H_o) that there is no significant association among commercial banking institutions and the Nigeria economy and accept the alternative hypothesis (H_i). Therefore, there is a significant association among commercial banking institutions and the Nigerian economy.

Hypothesis 2

Commercial banks do not play pivotal role in the smooth running of the financial and commercial operations of other sectors in the economy

T-test (one sample t-test)

Table 3.2 One-Sample Statistics

	N	Mean	Std. Deviation	Std. Error Mean
Commercial banks do not play pivotal role in the smooth running of the financial and commercial operations of other sectors in the economy.	67	4.4627	.70342	.08594

Source: Author's Computation 2014

Table 3.3 One-Sample Test

	Test Value = 0					
	T	Df	Sig. (2-tailed)	Mean Difference	95% Confidence Interval of the Difference Lower	Upper
Commercial banks do not play pivotal role in the smooth running of the financial and commercial operations of other sectors in the economy .	51.930	66	.000	4.46269	4.2911	4.6343

Source: Author's Computation 2014

The result from the table 3.2 shows that the mean value was 4.4627 with standard deviation of .70342 and the standard error mean of .08594.

From the one- sample test, table 3.2 the t-value shows a value of 51.930 and at 95% confidence interval of the difference between the lower and upper limit. The lower value shows 4.2911 and the upper value 4.6343. The result was significant at 2-tailed with a high percentage. The t_{cal} value of 51.930 is greater than the t_{tab} of 1.98. This shows that the null hypothesis is rejected and alternative hypothesis is accepted. Therefore the study concludes that commercial banks play a pivotal role in the smooth running of the financial and commercial operations of other sectors in the economy

Hypothesis 3

Commercial banks have not contributed to the growth and development of the Nigerian economy

Table 3.4 Chi Square

	Observed N	Expected N	Residual
Neutral	2	22.33	-20.3
Agree	20	22.33	-2.3
Strongly Agree	45	22.33	22.7
Total	67		

Source: Author's Computation 2014

Table 3.5 Test Statistics

	Commercial banks have not contributed to the growth and development of the Nigerian economy
Chi-Square	41.761[a]
Df	2
Asymp. Sig.	.000

Source: Author's Computation 2014

0 cells (.0%) have expected frequencies < 5. The minimum expected cell frequency is 22.3

Degree of Freedom = r-1 = 3-1 = 2 Where 'r' is the number of all alternative type of responses in the questionnaire

With degree of freedom of 1 and at 5% level of significance, X^2 tab = 5.991 from the Chi-square

Decision rule

If $X^2t > X^2c$ accept Ho and reject Hi

If $X^2t < X^2c$ accept Hi and reject Ho

From the calculations, the calculated value (X^2 cal = 41.761) is greater than the tabulated value (X^2 t= 5.991)

Hence, we reject the null hypothesis (Ho) and accept the alternative hypothesis (Hi) which validates that commercial banks have contributed to the growth and development of the Nigerian economy

4 Empirical Findings

(i) There is significant association among commercial banking institutions and the Nigerian economy

(ii) Commercial banks play pivotal role in the smooth running of the financial and commercial operations of other sectors in the economy

(iii) Commercial banks have contributed to the growth and development of the Nigerian economy

5 Conclusion

This study was carried out principally to examine the significance of the Nigerian banking sector to the nation's economy, the pivotal role the sector has played to all the other sectors of the economy and the contribution of the sector to the economy as a whole. Structured questionnaires were administered to elicit responses from a total number of 80 respondents out of which 67 were duly filled and returned. The three hypotheses formulated for the study were tested using analysis of variance, t-test statistic and chi square statistics and for all the hypotheses the null hypotheses were rejected. Consequently the alternative hypotheses were accepted and the study found a significant association among commercial banking institutions and the Nigerian economy. It also found that the banks have played pivotal role to the other sectors of the economy and that the banking sector has contributed immeasurably to the economy of Nigeria. This is because the banking sector consolidation policy introduced and foisted by the Central Bank of Nigeria on the commercial banking institutions emphatically encouraged and monitors real sector financing whose attendant effect is to grow the economy.

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