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The Effect of Financial Reforms on Banking Performance in an Emerging Market: Nigerian Experience

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Abstract
The paper examines effect of financial reforms on banking performance in emerging market: Nigerian experience. The study covers between 1992 and 2011, because the last reform in banking sub-sector was in 2005 during Prof. Charles Soludo as CBN governor (Pre-Lamido era). Automated Statistical Package Technique (ASPT) was used to analyze the model and Ordinary Least Square method was adopted to analyze existing relationship of variables and their behaviors. The study reveals that the effect of financial reform on banking performance is mixed. It was discovered that financial reform is not a causal factor for effective banking performance and development; but there is need for strong capital account policy to regulate short- term capital flow and exchange rate volatility. In addition, the Central Bank of Nigeria (CBN) should ensure the stabilization of financial markets and banks in order to control and manage risk aversion among domestic and foreign investors in the economy. The paper further recommends non-stopping reforms in the financial sector so as to serve as check and balances, which would be used to manage and control economic distortion's trend in the financial sector. Moreover, policymakers such as Monetary Policy Committee (MPC); regulatory government ministries, departments and agencies (MDAs) such as Ministry of Finance, CBN, Nigerian Deposit Insurance Corporation (NDIC), etc. should adopt economic policies that could strengthen and promote allocation of efficient resources to achieve efficient bank performance in Nigeria.
Keywords: Financial reform, Banking, Deregulation, Financial markets, CBN, NDIC, Nigeria.

1.1 Introduction

Financial reform is a possible change made to a household, system, firm, government, economies etc. in order to perform and operates in a more effective and efficient way within the context of stipulated regulatory policies (Oke, 2008). The reform of financial markets and banks remain a persistent force in the growth and development of financial sector in developed economies, developing economies and emerging markets (Nigeria inclusive). The reform of the financial sector could easily be traced to banks' competitive actions, assisted with continuous rise in government regulations over the soundness of banks' strong financial positions (Kent & John, 2008). The financial markets and mostly banks remain the strategic engine of economic growth of developing, developed and emerging economies (Nigeria inclusive). It must be noted that Deposit Money Banks (DMBs) play financial intermediary roles in the mobilization of available resources from surplus economic units to satisfy the requirements of the deficit unit of the economy. The financial intermediary act being performed by DMBs, allows banking sub-sector to easily influence the direction of available resources, thereby greatly affecting the rate of economic development. Though, Banks mediate between demand for credit and supply of deposit globally, but for these to work effectively and efficiently, there should be a platform for fair and healthy competition, that must be tolerated in the sector; which would impliedly require reform in the financial sector and creating a perfect competitive situations, which would help to harmonize: numerous suppliers / buyers of roughly equal size, free flow of information and homogenous products and services etc., hence, in such situations, either government or banks are permitted to interfere in the market.

The financial reforms have helped to facilitate capital formation and generate growth in the economy, but the consistent and persistent financial intermediation roles of Banks have been able to foster national and international development via the means of channeling resources into sectors of priority for sustainable development. The development of Nigerian financial institution system could be characterized by changes in structure, growth and emerging challenges since the era of Structural Adjustment Programme in 1986 to date (see Ahmed, 1987; Lamberte, 1989; Soyinbo & Adekanye, 1992). It is believed that the financial system of developed economies, third world economies and emerging markets remained the framework within which the capital formation takes place through the intermediation of the financial institutions processes (Akingunola, 2006). Therefore, the reform of financial markets and banks in twenty-first century involves the processes of financial innovations, globalization and deregulation in advanced- economies banking sector; but operations of other financial institutions if not checked might affect the performance of banks in any economy (See John & Kent, 2008; Obadeyi, 2013, CBN, 2014). However, the authorities via Central Bank of Nigeria (CBN) should intervene in the operation of the banking system in order to correct the shortcoming of price fixing mechanism so as to ensure that what is commercially rational for an individual bank also possesses approximate characteristics of social rationality as much as possible. Thus, the interest rate charge by bank is regulated to encourage savings mobilization and to ensure enough investment for rapid economic growth. In Nigeria, year 2013 has witnessed high interest rate of (MPR) at 12% (CBN, 2013); Cash Reserve Requirement (CRR) has increased from 50% to 75% on all government deposit with commercial banks and increase from 12% to 15% on private deposit with commercial banks (CBN, 2014). The interest rate (MPR) is the rate at which banks borrow from Central Bank to cover their immediate cash shortfall (Obadeyi, 2013); while Cash Reserve Ratio / Requirement (CRR) is the amount of cash that banks have to keep with the Central Bank and is often used to control excess liquidity in the economy. The adoption of 75% on public deposit and 15% on private deposit of CRR would not protect the pressure on exchange rate and inflation as a result of continuous increase in government spending culture. The high interest rate would only lead to increase in the cost of borrowing – enforcement of the policy; the (CRR) has further led to the withdrawal of about #1.2 trillion (US$7.5billion) from the banking system in July, 2013 (CBN, 2013). Surprisingly, it has also forced banks' lending rate to rise sharply to average of 25%; this has led to market impactions and externalities in financial market especially in emerging markets which may often, induced financial intervention. There is need for operators, regulators and policymakers in the financial sector to understand that reform does not imply 'no regulation' but entails restructuring of the financial system, allowing the forces of the demand and supply to dictate price mechanism as well as liberalizing the financial system further to foster the set objectives of the government in promoting economic transformation (Levine, 2000; Obadeyi, et al, 2013). Demetriades & Andrianova (2005) argues that financial reform is not the key factor behind the diverse result of financial development and economic growth of countries, but institutions and political economy; which are the likely factor that are responsible for the success of some countries to succeed in developing their financial systems while other have not.

2. Literature Review

2.1 Financial reform and Banks' Performance in Emerging Market.

The financial reform in Nigeria may be categorized into three: the pre –reform era, reform era and the post – reform era. The pre –reform era only focused on the development of a mixed economy, where the public sector had a predominant role in economic activities (see Freddy et al, 2003; Okereke-Onyiuke, 2004; Bakare, 2006). During the 1980s, the financial sector was highly stretched. The directed and concessionary bank credits were with serious references to some sectors, which eventually resulted into distorting interest rate mechanism and the liquidity and profitability positions of banks were adversely affected (Nyoung, 1997; Alayande, 2006). During this pre –reform era, financial sector was highly repressed, with ceilings on credit expansion, thereby forcing the banks to develop an inability experience to maintain an efficient flow of funds within the financial system; and sadly, the Nigerian banks were with weak balance sheet, with a high involvement in risk lending; and without provision for foreign exchange exposure (Temple, 2011). Though, during this period, the prevailing interest rate could not keep with inflation, thereby resulting to negative real interest rates; in addition, the demand for credit soon exceeded the rate of savings and a large proportion of government borrowing had to be financed by Central Bank of Nigeria (CBN).

Reform era: During the reform era, there was deregulation on interest rate and exchange rate. The regulatory government agencies such as Nigerian Deposit Insurance Corporation (NDIC) and CBN were strengthened and capital adequacy of banks were thoroughly reviewed (Odozie, 2004). During the reform era, the regulatory, monetary and supervisory authorities had taken some measures to facilitate the financial deregulation process in the economy to bring about smooth operation in the financial system. Though, the measures helped in achieving the intentions and motives of the authorities; but unfortunately, they had sometimes been misconstrued in certain quarters as contradictory to the reform policy of government. The liberalization of interest rate was designed to have a favorable impact on the economy by stimulating keen competition among banks for deposits with savings mobilization to be fostered by higher interest rate. Effective bank lending rates had been diverged considerably from the market, which is determined by Monetary Policy Rate -MPR (Adekanye, 1991). Banks have the primary fiducially responsibility to be closely involved in supporting the financial requirements of their customer. It was not difficult for the government to curtail the liberal interest rate regime as announced in the 1991 in the Federal Government Budget in order to support the productive sector (i.e. agriculture and manufacturing) of the economy, as intended under SAP (Ojo, 1991). The introduction of Foreign Exchange Market (FEM) and trade deregulation during SAP has enhanced access to foreign exchange for various industries. It has also encouraged the inflow of foreign exchange from non-official sources, reduced capital flight and adjusted the demand for imports. However, FEM has deregulated the responsibility that examines the pattern of allocation of foreign exchange to the banking industry though, there may be need to address the differential between and within each category of essential and non-essential imports in the allocation of foreign exchange. To achieve a greater significance in the financial sector, the banks need to be supported for continuity and stability in the foreign exchange management system and the modalities for administration of the exchange rate policy (Kwan, 2004). Another measure is the progressive increase in minimum required capital for establishing banks, which now stands at ₦25b since 2005 till date, because it symbolizes the year Nigerian economy witnessed last financial reform. This derived from the desire of the monetary authorities to stabilize the banking system in view of the greater risks. It must be noted that Banks are more exposed to risks and uncertainties due to the volume of business of the banks and the gross devaluation of the naira, but some banks seek refuge through merger or acquisition (Ebhodagbe, 1991).

Post reform era: The post reform era started after 2005 banking reform and the recapitalization in the insurance sector in 2006. Since then, no concrete reform till date. The deliberate and systematic removal of regulatory controls, structures and efficient allocation of scarce resources in an economy promotes economic growth. The main philosophy of the financial reform of an economy is the belief that factors of production, goods and services are optimally priced and allocated when their prices are freely determined in a competitive environment. The sign that often brings about the need for financial reform was the prevalence of supply and demand gaps in both the products/services and factor markets, but overall, the reform of financial market was re-examined in order to accelerate the availability of credit to the market (Zingales, 2003). Interest rate policy encourages and promotes the accumulation of domestic financial assets by offering the assets holders enough attractive rates. At the same time, other structural reforms could be used to increase the efficiency of financial system; such reforms include the removal of regulations imposed on the number of existing financial institutions where appropriate, support for the broadening of the range of financial instruments etc.

Bank remains an intermediary between those with surplus funds and those who need to borrow these funds. In emerging markets (Nigeria inclusive), banking industry is not a heavily regulated sector due to lack of adequate pace of technological innovation for the development of new financial products and services, which has resulted to unit cost. The availability of banks' products / services such as e-banking, internet banking, credit cards, debit cards, electronic fund transfer (EFT), point of sale (POS) etc., could improve cash management practice, and have the ability to reduce the cost of delivery of cash management services in a country (reverse is the case in Nigeria). For instance, some of the challenges faced among the Banks in Nigeria: the (Automated Teller Machine-ATM will debit the account of customers, when payment has not been made to the customer – dispense error; it is difficult for customers to have easy access to cash within 24 hours, currencies dispensed by most ATM machines are often rough, torn and dirty), absence of application of telecommunication and computer technology to the improvement of money management methods for customers; the incomplete customer information file, which hinders financial institutions to gather information about the spending patterns and the financial needs of their clients in order to get closer to the customer; therefore, while considering all these, the purpose of 'Know Your Customer – KYC' might have been defeated.

As financial intermediaries, banks assist in channeling funds from surplus unit to deficit unit to facilitate business transactions and economic development; though, government frequent intervention in the activities of the financial markets, banks and non-banks have often hindered these institutions' intended objectives. It must be noted that in order to remove financial distortions, policy makers have often resorted to economic reforms, which affect all the sectors of the economy including the financial sector (Demirguc-kunt & Detragiache 1998). However, banking crises are not likely to occur in liberalized financial systems due to control measures adopted by regulatory, supervisory, monitory government agencies and policymakers in these economies, with the exceptions of global financial crises in 1930s, 1980s and recently between 2007 and 2009 (see Balogun, 2007; Obadeyi, 2013, Oke et al, 2013).

The effect of financial liberalization on the fragility of the banking sector may be negative if the institutional environment is weak and the future remains uncertain- lack of rule of law, high degree of corruption in government Ministries, Departments and Agencies (MDAs), etc. But there is need to note that financial development and growth support the view that financial reform should be approached cautiously to ensure contract enforcement and effective prudential regulation particularly when macroeconomic stabilization has been achieved, in addition, financial reform is associated with higher financial development and higher output growth, while banking crises have the opposite effect; but international financial reform softens financial constraints and improves risk-sharing, thereby fostering investments. It may also have a positive impact on the functioning and development of financial systems, and on corporate governance (Demetriades & Law, 2005). The real interest rate has a small positive effect on financial development, there is also evidence to suggest that the direct effect of 'repressive' policies on financial development are sometimes positive and quite large, but non-tight financial repression may turn out to have positive effect under certain conditions such as severe financial repression, which is likely to result to under -development due to large negative real interest rates, and other disincentive effects (Demetriades & Luintel 2001).

2.2 Financial Reform and Recent Development in Nigerian Banking System

However, for emphasis, reform does not really mean laissez-faire - a complete absence of regulation, but a continual process of examining existing regulatory framework with a view to deregulate when appropriate and regulate when necessary to allow market forces to play greater roles in pricing system (CBN, 2013). The emphasis therefore is on the necessity for a particular regulation and appropriateness of any deregulatory measure. Reform means allowing economic agents and factors of production to respond freely to market forces (Ojo, 1991). The liberalization of the financial system has led to a great proliferation of banks. Three years prior to the commencement of Structural Adjustment Programme (SAP) in August 1986, only eight banks were in existence (Abdullahi, 1989). Presently, there are more than 20 banks in the banking sub-sector with several branches within the country. It is obvious, that banking sub-sector will improve economic efficiency and the productivity of investment as a result of the elimination of distortions, such as subsidized interest rates and credit rationing; therefore, in the process of financial reform and market interest rates, they both play important roles in Macro-economic policy. Financial reform has influence on domestic expenditure, inflation and external payment but also ensure the equilibrium level of saving and investment inequalities by increasing the interest rate; that is, making it high enough to make the equilibrium possible. Conversely, equilibrium in the market for saving would occur at positive interest rate which ensured an increase in supply of either domestic or foreign savings, assuming such supply is interest elastic, to guarantee some reasonable level of private sector investments. This analysis therefore suggested that the elimination of distortions in the market for financial savings would be expected to yield a vital profit in terms of achievement of a higher rate of fixed capital formation and growth of output that was hitherto impracticable. With the temporary downturn in the general level of economic activity due to restricted credit expansion, this may lead to low effective demand for goods and services, as well as other recessionary factors. However, the large growth in the number of banks competing for a limited customer-base in an environment of shrinking margins may compel the banking industry to greater commitment in terms of efficiency and customer satisfaction, which may serve as a key for survival and success factors (Lamido, 2011). The Nigerian banking system has undergone remarkable changes over the years in terms of the numbers of institutions and ownership structure. The recent shake-up in Nigerian banks could be regarded as the continuation of ‘skeletal / partial’ financial reform in the banking sub-sector centred on ensuring full disclosure, zero tolerance to weak corporate governance and adopting strong and vibrant risk management approach (Lemo, 2011; Lamido, 2012). Though, the core roles and responsibilities of banks in any economy are to render financial assistance to the productive sector. The recent financial reforms, which may be regarded as ‘skeletal / partial’ financial reform in banking sub-sector embarked upon by Nigeria apex banks (CBN) to have removed the eight bank executives over alleged exposure to ₦1.143 trillion with Non-Performing Loans (NPL) in first phase. Though, exposure to the oil and gas sector amounted to N487.02 billion, which are merely holistic approaches aimed at ensuring and targeting macroeconomic stability, growth and development (Lamido, 2009). The principle of full disclosure, good corporate governance and a sound and vibrant risk management practices would build the confidence of the international community in a developing economy -Nigeria inclusive. The CBN recent actions on consolidated banks would lead to a prospect of quick recovery of the Nigerian economy in line with positive signals of recovery from the recession being experienced globally since six years ago. The recovery of crude oil prices and improved oil and gas output are to enhance and improve the fiscal and foreign exchange balances. The real Gross Domestic Product (GDP) growth is projected at 5% and GDP for non-oil growth is expected to remain robust and active at 6.3%. Inflation rate has reduced from 15% at the end of 2008 to 11% at the end of August, 2009, but as at June, 2013; inflation remains at 9.1% (CBN, 2013). Also the level of external reserves has remained high and net outflow significantly moderated. As a clearing and settlement financial institutions, banks constitute useful channel in the payment system and the medium through which the effect of monetary policy are transmitted to the rest of the economy. The ability of financial institutions (banks) to perform those roles efficiently is dependent on the health and the sophistication of the banking system as well as on the level of development of financial system (Ajifs & Hamid, 1992; Soludo, 2004; Lamido 2009). In any organization where the business is not flourishing and there are indications of failure, one of the options available to the owners is to reorganize the business to close gaps and streamline avenues for improvement. However, the bank recapitalization was embarked upon by the monetary authority, CBN on July 6, 2004 to ensure a diversified, strong and reliable banking sector that will play active developmental roles in the Nigeria economy and be competent and competitive players in the African and global financial system as a means to address the menace of bank failures that characterized the industries in the recent years (Soludo, 2004). No doubt, bank recapitalization from the financial reform has been adopted by most of the developed countries and presently the emerging markets by carrying out the different recapitalization policies in order to downsize inefficient and ineffective banking sector. Gbodume, (2004) argues that financial reform (bank recapitalization) does not necessarily mean an automatic improvement in the banking sector, but emphasized that financial reform alone cannot solve the present crisis in the Nigerian banking system as well as in the economy because it is just one of the techniques that could be employed to promote efficiency in the banking sector; and it has to be complimented by several other reforms so as to achieve an ultimate overall change in the sector. The consolidated banks in Nigeria involve in the lax credit administration process and non-adherence to credit risk management policies thereby leading to lack of doctrines of sound credit management system, inability of application of ethical credit monitoring and recovery tools as it occurred globally (Ajakaiye & Omole, 1994; CBN, 2009).

The provision of adequate information enhances the integrity of banks and reduces the reputational risks that could lead to loss of confidence and patronage. The recent reduction in the market uncertainty and restriction in the risk of unwanted contagion have helped to encourage, stimulate, enhance and promote market discipline (Lamido, 2009). The monetary policies are expected to improve growth without jeopardising both price and financial stability. To manage liquidity both effectively and efficiently, there is need to ascertain credit, which is determined by interest rate and the trends are monitored in prices. The CBN has persistently assured Nigerians that none of the 24 post-consolidated banks would be permitted to be distressed / failed in 2005 (Soludo, 2004). The number of banks is now twenty-three including the Islamic bank- Jaiz bank as at 2013. Despite the CBN's promise, the Nigerian banking industry continues to display phobic reactions to these measures particularly the swirling rumours on some customers, who might become apprehensive of the possible loss of their deposits. It must be understood that during the economic reform in the banking sub-sector in 2005, the CBN reiterated its effort to bring monetary policy in line with current economic exigencies, thawing liquidity frozen at the inter-bank exchange market (Nwude, 2005). Obviously, the banking sector shake-up is the effort of the Central Bank of Nigeria (CBN) that resolves to stick to the common year-end accounting system, in order to allow banks make full disclosure, provide and guide against non-performing loans comprising margin facilities and loans extended to other sectors of the economy, majorly oil and gas sector. The affected banks were unable to meet obligations to creditors and were in a grave situation; while management of affected banks acted in a manner detrimental to interest of depositors and creditors. The Central Bank of Nigeria (CBN) injected the sum of N420 billion naira in the first phase and in the second phase N200 billion was injected, totalling N620 billion (Six hundred and twenty billion naira) to salvage the affected eight banks as a bail-out fund to cushion the effect of the liquidity problems or from going under (Lamido, 2009). The injection of the fund into the banking system would go a long way to address the illiquidity that had been rocking the capital market. The injected funds into the banking sub-sector were essential in building a sound financial sector, which is capable of promoting long-term and consistent development with the goals being set at per with vision FSS2020 (i.e. Financial System Strategy, 2020).

3.1 Methodology

The method of the paper is based on a financial reform banks' performance relationship equation as used by Demetriades and Law. The model as used by the authors is stated thus: fd = f (RGDPC, R, ROL, POL, BC, OP). FD is financial development; RGDPC is real GDP per capital; R is the real interest rate; ROL is rule of Law; POL is political stability / Political Economy; BC is bank concentration and OP is openness, which is measured by total trade (Imports + exports) over GDP.

One category of financial development/performance indicators is employed, namely banking sector development. The banking sector indicators are the ratios of liquid liabilities, private sector credit and domestic credit provided by banking sector to GDP. But the study is only concerned with the banking sector and effort geared towards using the three indicators of financial development / banking sector performance as used by Demetriades and Law, while interest rate is the only exogenous variable used and is taking as the best financial reform policy. In essence, the study analyzed the following equation.

$Logfd_l = \beta_o + \beta_1 LogR + \mu_1$ …………………… (1)

$Logfd_l$ is a function of independent variable of Log R. This equation shall test the effect of interest rate on ratio of liquid liabilities to GDP.

Where

R	=	Real Interest rate
β_o & β_1	=	Estimate parameters
μ_1	=	Error terms
fd_l	=	is the ratio of liquid liabilities to GDP

$Logfd_p = \beta_0 + \beta_1 LogR + \mu_2$…………………… (2)

$Logfd_p$ is a function of independent variable of Log R. This equation shall test the effect of interest rate on ratio of private sector credit to GDP.

Where

R = Real Interest rate
β_o & β_1 = Estimate parameters
μ_2 = Error terms
fd_p = is the ratio of private sector credit to GDP.

$Logfd_d = \beta_0 + \beta_1 LogR + \mu_3$…………………… (3)
$Logfd_d$ is a function of independent variable of Log R. This equation shall test the effect of interest rate on ratio of domestic credit provided by banking sector to GDP.
Where

R = Real Interest rate
β_o & β_1 = Estimate parameters
μ_2 = Error terms
fd_d = is the ratio of domestic credit provided by banking sector

Consequently, the equations stated above are estimated with Ordinary Least Square (OLS) to determine the parameter estimates of the models. In this paper, some assumptions are made about the stochastic element/residual value (error term).

Given the above assumptions about the error term, the unexplained or residual part of the regression equation is assumed to be zero or completely ignored since the expected value is zero. Therefore, we concluded that there is no relationship that exists between the dependent variable and the error term.

4.1 Result

The model specified above was estimated with the Automated Statistical Package and the result was presented below for the empirical analysis. As stated above the variables were transformed to logarithm form in order to achieve the best result.

Extract of the Regression Result

DEPENDENT VARIABLE: BANKING SECTOR DEVELOPMENT			
	Model 1 liquidity liabilities-log (FDL)	Model 2 Private sector credit-log (FDP)	Model 3 Domestic credit-log (FDD)
Constant	1.095789 (0.751653)	1.369976 (0.900900)	0.796320 (0.426819)
Log (R)	0.719679 (1.485706)	0.4753396 (0.840857)	0.828672 (`.336728)
R-square	0.059747	0.046873	0.090304
F-statistic	2.207324	0.885212	1.786840

Note: Figures in the parentheses are the t-statistics.
Source: Regression Output.

The table above revealed the regression result of Model 1 – 3 specified above. Accordingly, the result of model 1 summarized in the below equation.

$LogFd_l = 1.095789 + 0.719676LogR$……………. (1)
t^c (0.751653) (1.485706)
F^c (2.207324)
$LogFD_p = 0.719679 + 0.059747LogR$…………… (2)
t^c (0.900900) (0.940857)
F^c 0.885212
$Log\ FD_d = 0.796320 + 0.828672LogR$…………….. (3)
t^c (0.426819) (1.336728)
F^c 1.78640

The above equation (1) revealed that there is a positive relationship between financial liquidity ratio and real interest rate as predicted in the study. The same can be said of the result of model 2 and 3, this means that increase in the financial reform policy or the more the government deregulates the financial sector, the better the performance of the banking sector. However, the parameter estimates obtained from each model is not statistically robust and they are very little. This indicates that much have not been benefited from the government deregulation of the financial sector of the Nigerian economy especially as regards the banking sector performance.

Furthermore, the coefficient of determination revealed that the entire independent variable has little power in explaining the variation in the dependent variable and they are not statistically significant. This means that financial reform has small positive effect on banking performance.

4.2 Conclusion

This study empirically examined the effect of financial reform on banking performance in emerging market: Nigeria experience. Findings from the study shows that real interest rate has a small positive effect and there is a direct effect of repressive policies on financial development (bank performance). The study holds the view that the Mckinnon-Shaw hypothesis, which emphasized that higher real interest rates resulting from financial liberalization will enhance financial development relates little in this study. There is need to accept a positive relationship between international financial liberalization and economic growth. However, the presence of financial and economic distortions may reduce the positive effects of liberation. However, information asymmetries may lead to a poor allocation of capital, weak financial and legal systems; and it could induce capital flights towards countries with better financial institutions. However, the success of financial reform on economic growth depends on the level of financial development achieved in such an economy. Some countries succeeded in their liberalization via economic growth policies, results were different for other economies as a result of various crises rocking the financial system. This study revealed that financial reform has not boost (banking performance) financial sector in Nigeria as a result of various macroeconomic and institutional problems facing the Nigerian economy, which include inappropriate macroeconomic policies, inadequate policy coordination, social -political instability, high cost of doing business and multiple taxes and levies etc. All these factors prevail in the Nigerian financial sector and make the risk of investing in Nigeria high. This discourages the penetration of foreign direct investment into the Nigerian economy and discourages other capital flows. However, for Nigeria to benefit from the current wave of globalization especially in the area of banking operations, its financial services must go beyond liberalization. Government need to maintain a stable macroeconomic policy especially in the area of stable inflation, realizable exchange rate policies and fiscal balance. Finally, the country need to be more involved in international services such as shipping, Insurance, Banking, etc. Nigeria still needs to create and secure economic environment without which domestic and foreign investors will continue to shy from the many profitable business opportunities the country offers. It is highly noted to this end that the importance of the financial reform in our economy cannot be overemphasized. Hence, if our vision is to ensure a sound and reliable banking structure for the 21st century, now is the time to plan for the required, dynamic, qualified and competitive banking system. The reform programme will also redefine the nature of competition in the banking industry such that each institution will have no choice but to assign priority to its capacity to deliver superior value to its clients. Hence, there is the need for more reform in the banking sector, such that the interest rate and inflation rate can be reduced to a digit and exchange rate can be reduced, controlled and managed. Also, there is need for institutions and political economy to remain stable, so that business environment can attract investors, by way of promoting capital flow into the economy.

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APPENDIX 1
NIGERIAN REAL INTEREST RATE AND BANKING PERFORMANCE INDICATORS

Year	R	FD_l	FD_p	FD_d
1992	10.50	33.14	23.77	50.40
1993	17.50	29.47	23.40	43.10
1994	16.50	29.45	20.50	39.47
1995	26.80	20.59	13.76	21.91
1996	25.50	24.90	14.05	22.13
1997	20.01	26.59	13.99	25.87
1998	29.80	234.78	145.43	311.15
1999	36.09	28.47	13.07	40.26
2000	21.00	30.90	16.50	47.99
2001	20.18	16.12	10.69	23.99
2002	19.74	13.11	7.86	11.77
2003	13.54	14.63	9.35	10.93
2004	18.29	18.75	12.21	16.86
2005	21.31	20.97	13.58	18.85
2006	17.98	20.87	11.97	13.40
2007	18.29	23.33	15.16	15.05
2008	24.40	25.00	16.00	21.84
2009	20.48	31.74	20.81	29.64
2010	19.15	27.39	18.24	24.44
2011	17.78	17.63	13.09	15.53

Sources: CBN Statistical Bulletin, Vol. 18, December, 2011.

Note : R = Real Interest rate
fd_l = is the ratio of liquid liabilities to GDP
fd_p = is the ratio of private sector credit to GDP,
fd_d = is the ratio of domestic credit provided by banking sector to GDP.

APPENDIX II
NON-LOG REGRESSION RESULT

Department variable : Fdl
Method : Least Squares
Date 30/06/2013 Time : 10:40
Sample : 1992 – 2011
Included observations : 20

Variables	Coefficient	Std. error	T-statistic	Prob.
C	-31.91587	39.28381	-0.812443	0.4272
R	3.196231	1.830234	1.746351	0.0978

R-squared	0.144883	Mean dependent variable	34.38196
Adjusted R-squared	0.097376	S. D. dependent variable	47.53584
S.E. of regression	45.16214	Akaike info criterion	10.65261
Sum squared resid	36713.14	Schwarz criterion	10.85261
Log likelihood	-103.5303	F-statistic	3.049744
Durbin-watson stat	2.441133	Prob (F.statistic)	0.097793

APPENDIX III
NON-LOG REGRESSION RESULT

Department variable : Fdl
Method : Least Squares
Date 30/06/2013 Time : 10:42
Sample : 1992 – 2011
Included observations : 20

Variables	Coefficient	Std. error	T-statistic	Prob.
C	-41.12508	53.75282	-0.913907	0.3738
R	4.307764	2.504345	1.720116	0.1026

R-squared	0.141172	Mean dependent variable	40.22870
Adjusted R-squared	0.093459	S. D. dependent variable	64.90357
S.E. of regression	61.79627	Akaike info criterion	11.18020
Sum squared resid	68738.01	Schwarz criterion	11.27978
Log likelihood	-109.8020	F-statistic	2.958798
Durbin-watson stat	2.354068	Prob (F.statistic)	0.102557

APPENDIX IV
NON-LOG REGRESSION RESULT

Department variable : Fdp
Method : Least Squares
Date 30/06/2013 Time : 10:42
Sample : 1992 – 2011
Included observations : 20

Variables	Coefficient	Std. error	T-statistic	Prob.
C	-14.98880	24.74146	-0.605817	0.5522
R	1.768913	1.152705	1.534575	0.1423

R-squared	0.115693	Mean dependent variable	21.70288
Adjusted R-squared	0.066565	S. D. dependent variable	29.44943
S.E. of regression	28.44371	Akaike info criterion	9.628371
Sum squared resid	14562.81	Schwarz criterion	9.727944
Log likelihood	-94.28371	F-statistic	2.354921
Durbin-watson stat	2.450419	Prob (F.statistic)	0.142278