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The Implication of Banking Reforms for Economic Development in Nigeria (A Case Study of Zenith Bank Plc)

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Abstract
This study assessed the relevancy of banking reforms in Nigeria and its contribution to banking industry by empirically investigating its implication on the nation's economic development through their credit facilities' capacity. Simple linear regression was adopted to develop a model that will systematically capture the dynamics of macroeconomic variables used in this study by isolating the impact of financial reforms on Zenith bank's solvency. Results of the study also showed that the recent banking reforms have had stimulating effect on the Nigerian economy through increased shareholders' fund and consequent increase in loans and advances available to the customers. This was in accordance with the expected transmission effect on the economy, Soludo reform of bank recapitalization resulted in more funds being available to customers' for lending. The banking reforms contribution to development of the financial sector was significant as banks' capacity to play their financing role in the economy was enhanced through increased capital base. Zenith Bank's equity grew from N6.73billion in 2001 to N321.17billion in 2010 representing about 4,772% growth over the period of study.
Keywords: Banking reforms, Economic development, Regression, Nigeria

1. Introduction

Banks are very important for the smooth functioning of financial markets as they serve as repositories of vital financial information and can potentially alleviate the problems created by information asymmetries (Adegbaju and Olokoyo, 2008). Banking reforms thus, become necessitated and more intensified in recent times due to the impact of globalisation which was precipitated by continuous integration of the world market and economies. In Nigeria, banking sector reforms have resulted from deliberate policy response to correct perceived or impending banking sector crises and subsequent failures. A banking crisis can be triggered by weakness in banking system considered by persistent illiquidity, undercapitalization, high level of non-performing loans and weak corporate governance, among others. Similarly, highly open economies like Nigeria, with weak financial infrastructure, can be vulnerable to banking crises emanating from other countries through infectivity. Banking crisis usually starts with inability of the bank to meet its financial obligations to its stakeholders. This, in most cases, precipitated runs on banks making the banks and their customers to engage in massive credit recalls and withdrawals which sometimes necessitate Central Bank liquidity support to the affected banks. (Adegbaju and Olokoyo 2008)

Consequently, substantial numbers of banks have failed in the past, mainly because of non-performing loans. Poor loan quality has its roots in the informational problems which afflict financial markets, and which are at their most acute, result from the problems of moral hazard and adverse selection. Some terminal intervention mechanisms may occur in the form of consolidation (mergers and acquisitions), recapitalization, use of bridge banks, establishment of asset management companies to assume control and recovery of bank assets, and outright liquidation of non-redeemable banks. Banking sector reforms in Nigeria are driven by the need to deepen the financial sector and reposition the Nigeria economy for growth; to become integrated into the global financial structural design and evolve a banking sector that is consistent with regional integration requirements and international best practices. It also aimed at addressing issues such as governance, risk management and operational inefficiencies, the center of the reforms is around firming up capitalization (Ajayi, 2005).

In the past years, the success of the banking reform and the on-going strides by the Central Bank of Nigeria (CBN) suggests a complementary approach in liberalizing the economy to encourage the needed growth in all sectors. An economy with a buoyant banking sector without articulated growth on other service sectors is yet to achieve economic development. The existence of a favorable economy would attract overseas companies to invest, bringing with them international best practices and better skills and technologies. The entry of foreign services providers is not necessarily a negative development and can lead to a better services for domestic consumers, improve the performance and competitiveness of domestic service providers, as well as simply attract FDI/fo into the country. (Uchendu, 2005). The primary objective of the reforms is to guarantee an efficient and sound financial system. The reforms are designed to enable the banking system develop the required flexibility to support the economic development of the nation by efficiently performing its functions as the pivot of financial intermediation (Lemo, 2005).

Nigerian banking sector has been generally viewed as a weak link in the economic system which continued to necessitate a reform essential for the sustainable development and further growth of Nigerian economy. The Nigeria banking system was in a poor state before the recent recapitalization reform agenda. The banking sector was highly fragmented with concentration on the import business related activity. In order to ascertain the relative efficiency of the reforms which suggest an improved performance in the banking industry, a cursory look at the various reforms in the banking sector is necessitated.

Focusing on the Nigerian economy, a country whose banking industry has witnessed a large number of reforms in a relatively short time, the aim of this paper is to attempt to close the gap in economic literature by investigating whether recent banking sectors have had any effect in stimulating economic growth in Nigeria and to provide answers to the following research questions: Are banks playing the pivotal role of driving development, Is there any relationship between financial system and economic development and to what degree has the recent banking reforms contributed to development of the financial sector in Nigeria.

2. Review of related literature

The Nigerian banking sector have undergone series of complex, but comprehensive phase of restructuring, with a view to making it sound, efficient, and at the same time forging its links firmly with the real sector for promotion of savings, investment and growth. Given the importance of the financial system and the critical role it had played in shaping development of countries, a considerable economic literature have been devoted to study the relationship between the various reforms in banking sector and nation's economic development. The direction of causal relationship between economic growth and the banking sector is one area of contention amongst researchers. Theoretically, banking sector openness had a direct and indirect effect on economic growth through a combination of improvement in access to financial services, and the efficiency of financial intermediaries as both of these cause a lowering of costs of financing which in turn stimulates capital accumulation and economic growth. A review of empirical literatures indicate that there have been considerable research on the economy's aggregate response to reforms in banking sector examining the correlation among the different related macro-economic variables.

Adegbaju and Olokoyo (2008) investigated the impact of previous recapitalization in the banking system on the performance of the banks in the country with the aim of finding out if the recapitalization is of any benefit. The study employed secondary data which were analyzed using both descriptive i.e. means and standard deviations and analytical techniques such as the t-test and the test of equality of means. It was found that the mean of key profitability ratio such as the Yield on earning asset (YEA), Return on Equity (ROE) and Return on Asset (ROA) were significant meaning that there is statistical difference between the mean of the bank before 2001 recapitalization and after 2001recapitalization. Fadare (2010) investigates the effect of banking sector reforms on economic growth in Nigeria over the period 1999 – 2009 using the ordinary least square regression technique. He found out that although there was a strong and positive relationship between economic growth and the total banking sector capital, the relationship between economic growth and other exogenous variables of interest rate margins, parallel market premiums, total banking sector credit to the private sector, inflation rate and cash reserve ratio revealed the wrong signs. The implication which emerges from the empirical results with regards to the wrong signs of these parameters is that theoretical expectations would only be valid when all conditions are normal. Bayraktar and Wang (2004) demonstrated that the role of foreign banks was both statistically and economically significant in increasing growth and improving the operations of local banks. While Berglof and Roland (1995) showed that soft budget constraints and repeated bank bailouts by governments were a function of poor quality of loan portfolios, the absence of collateral, low bank capitalization, and political pressure to refinance unprofitable firms in transitional economies.

Güryay et al (2007) research work was on the effect of financial development on economic growth of Northern Cyprus. Their findings showed a positive but negligible effect. Tuuli (2002) employed the ratio of banks' claims on the private sector to GDP, annual consumer price index, and the interest rate margin to analyse the relationship between finance and economic growth. He used a fixed-effects panel model and data from 25 transition countries for the period 1993-2000. His findings were that the interest rate margin is significantly and negatively related to economic growth. He argued that the outcome is in line with theoretical models and has important policy implications. Balogun (2007) specified more expansive theoretical models which included money supply, minimum rediscount rates, private sector credit, ratio of banking sector credit to government, ratio of stock market capitalization to credit to the private sector, and exchange rates. His findings were that many of these variables are often incomplete, subjective, and difficult to systematically compare. Olofin and Afangideh (2008) in their research found out that several determinants of economic growth especially in cross-section studies which exist in literatures (such as the years of schooling - human capital, black market premiums, bureaucratic efficiency, corruptions etc.), are usually obtained from periodic surveys. Hence, data on these variables makes consistent time series are unavailable.

Banking Sector and Economic Development

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 role of finance in economic development is widely acknowledged in the literature. In particular, Schumpeter (1911) put the role of financial intermediation at the center of economic development. He 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. He believed that efficient allocation of savings through identification and funding of entrepreneurs with the best chances of successfully implementing innovative products and production processes are tools to achieve this objective.

From the foregoing, it can be inferred from the models, concept and theories reviewed that the various literature and contributions of other researchers on the general practices and trends related to the research, resides in its use as a mapping device from which researchers can draw inference and synchronize their research expectations. These theoretical underpinnings provide the framework for analyzing the implications of recent banking reforms on the nation's economic growth.

3. Methodology

The methodology employed in this study is a simple statistical technique to generate empirical evidences. The nature and sources of data are secondary. Time series data of over a period of 10years (i.e. from 2001 to 2010) covering the pre and post period of recent banking reforms of Nigeria's democratic economic development was used. Data were sourced from Central Bank of Nigeria Statistical Bulletin and Zenith bank plc's annual reports covering the pre and post period of recent banking reforms within Nigeria's democratic economic development.

Sample and Sampling Procedure

This study does not involve probability samples but a result of the objective judgment of the researcher. Zenith Bank Plc was the only sampled deposit money banks used as case study. A statistical non-probabilistic sampling technique was employed in the collation of data used tailored to suit the research work.

Simple Linear Regression

This model was formulated to empirically investigate the implication of banking reforms on the economic development as specified in the statement of the hypothesis thus:

GDP = f(Total Credit facilities) -------------------------------------- 1.1

This can be explicitly specified as follows:

GDP = $ß_0 + ß_1$ TC + Ɛ ---------------------------------- 1.2

Where;

$ß_0$ = represents the intercept

GPD = represents Gross Domestic Product

TC = Total credit facilities given out by commercial banks

Ɛ = represents every other variable not captured in the study

4. Data Analysis and Techniques

Simple linear regression analysis was carried out to evaluate the impact of banking reforms on Zenith Bank Plc using time series data. Total assets, capital and reserves and total credit to the real sector of the economy were tested so as to fully show the empirical effect of the reforms.

Correlations

		GDP	Total Credit Facilities
Pearson Correlation	GDP	1.000	.914
	Total Credit Facilities	.914	1.000
Sig. (1-tailed)	GDP	.	.000
	Total Credit Facilities	.000	.
N	GDP	10	10
	Total Credit Facilities	10	10

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.914[a]	.835	.815	3.59957E6	.835	40.614	1	8	.000	1.032

a. Predictors: (Constant), Total Credit Facilities
b. Dependent Variable: GDP

Gross Domestic Product (GDP) was used to depict the activity of Nigerian economy during the period under study, while Total Credit (TC) depicted the aggregate credit facilities pumped by commercial banks into the economy. TC was regressed on GDP to assess the direction and degree of relationship of the two macroeconomic variables and whether there exist any at all. The results from the simple regression analysis carried out showed positive relationship between the variables. 83.5% of the macroeconomic variables that drive GDP which is the regressand were caused by TC, the regressor while only 16.5% were caused by variables not captured in the study. Hence, we posit that banking reforms have significant implications on the Nigerian economy. The R^2 is 83.5% while the adjusted R^2 is 81.5% indicating that change in the dependent variable is largely captured by the explanatory variable. Specifically, the correlation coefficient of 91.4% shows significant statistical relationship between TC and GDP growth rate at 5% level of significance. Durbin-Watson result is low showing presence of autocorrelation. Overall, the study concludes that Banking reforms have significant implication(s) on the Nigerian economy.

5. Findings and conclusion

The findings of the study given the set of data employed showed that banks play pivotal role in driving economic development through lending. Its impact on economic development was measured through GDP. Money supply and capital market experienced significant growth. The dynamic of Nigeria financial system was measured by regressing the total credit facilities available in the economy on the GDP. The correlation coefficient of the macroeconomic variables was 91.4% showing strong relationship. Results of the study also showed that the recent banking reforms have had stimulating effect on the Nigerian economy through increased shareholders fund and consequent increase in loans and advances available to the customers that is consistent with CBN guidelines. This was in accordance with the expected transmission effect on the economy, Soludo reform of bank recapitalization resulted in more funds being available to customers' for lending. The total bank loan was N126 billion in 2005, the year of recapitalization, which is 129% over that of 2004. This invariably had stimulating effect on Nigerian economy through the various sectors where the loans were channeled. Although, the Sanusi reform emphasized on tightening of loan procedures due to observed lapses by the regulatory, yet loan given increased by 24% in 2010 over 2009 though the increase was lower as compared to 54% which was the proportion of increase in 2009 over 2008. The banking reforms contribution to development of the financial sector was significant as banks capacity to play their financing role in the economy was enhanced through increased capital base. Zenith bank's Bank equity grew from N6.73billion in 2001 to N321.17billion in 2010 representing about 4,772% growth over the period of study.

From the result generated by the study, we can deduce that the implication of banking reforms in Nigeria has produced tremendous effect on the economy of Nigeria through the transmission mechanism of credit facilities. Banks are now positioned to play their role effectively in developing the core real sector of the economy. Thus, the results bring evidence on the dynamic role of financial system. However, from the analysis carried out, tightening measure should be put in place by the bank's management to control their non-interest expenses such that the reforms can produce lasting effect on the economy. Central bank should sustain mandatory high-quality disclosures of information by deposit money banks to help proper measurement of

impact of various reforms being introduced and early detection of problems faced by banks in the market in order to reduce the severity of market disruptions. Banking reforms are thus, significant and should be more intensified in recent times due to the impact of globalisation precipitated by continuous integration of the world market and economies. Consequently, the goal to strengthen the intermediation role of banks and to ensure that they are able to perform their developmental role of enhancing economic growth, which subsequently leads to improved overall economic performance and societal welfare will be achieved.

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