BANK REFORMS AND PERFOMANCE OF BANKS IN NIGERIA

OLOKOYO, FELICIA OMOWUNMI (Ph.D)

DEPARTMENT OF BANKING & FINANCE,
COLLEGE OF DEVELOPMENT STUDIES,
COVENANT UNIVERSITY,
KM 10, IDIROKO ROAD,
P.M.B 1023, OTA, OGUN STATE,
NIGERIA.

Email: felicitymy79@gmail.com, felicia.olokoyo@covenantuniversity.edu.ng
Telephone No: +234-802-3948641

Abstract

Bank reforms have played a role in the performance of banks in Nigeria. The purpose of the study was to access the effects of the reforms on the performance of banks in Nigeria. The data required for this study was gathered through the instrument of questionnaire. One hundred (100) copies of questionnaires were administered out of which eighty (80) copies were collated for the analysis. To achieve the objectives of the study, two (2) hypotheses were formulated from the structure of research questions while Analysis of Variance (ANOVA) method was used to test the hypothesis using the statistical package for social sciences (SPSS). The study shows that the recapitalization and consolidation process has had significant effect on the manufacturing sector of the economy and thus on the Nigerian economy at large. The study further reveals that despite the reforms, post consolidation challenges like challenges of increased return on investment still exist. According to some sections of the Nigerian populace, the reforms are seen to have come too soon and thus, rendering sections of the economy such as the lower class, illiterates and the economically active poor, incapable of banking transactions. The reforms however is very necessary for our banks to imbibe best corporate governance practice, improve on self-regulation, institute IT-driven culture and seek to be competitive in today's globalizing world.

Keywords: Bank Reforms, Banking Industry, Performance, Recapitalization, Consolidation

1. Introduction

Are bank reforms veritable means for fostering banking growth and developing the economy as a whole? In a developing economy, such as Nigeria, financial sector development has been accompanied by structural and institutional changes and the sector generally have long been recognized to play a crucial role in economic development of the nation (Kanayo, 2011). Banking reforms have been an on going phenomenon around the world right from the1980s, but it is more intensified in recent time because of the impact of globalization which is precipitated by continuous integration of the world market and economies. (Adegbaju and Olokoyo, 2008). Banking reforms involve several elements that are unique to each country based on historical, economic and institutional imperatives.

In most cases, bank reforms are embarked upon to forestall banking crises or cushion the effects of a recent crisis. Banking sector reforms have come into play due to banks inability to meet up to required obligations or satisfy their stakeholders which overtime have led to subsequent failures and crises. A banking crisis can be triggered by weakness in banking system characterized by persistent illiquidity, insolvency, undercapitalization, high level of non-performing loans and weak corporate governance, among others. (Adegbaju and Olokoyo, 2008). Bank crises in Nigeria were also due to the failure of the CBN and other government bodies with oversight functions for the financial sector. Lack of co-ordination among regulators prevented the CBN from having a comprehensive consolidated bank view of its activities. In addition, regulations concerning the major causes of the crisis were often incomplete. Likewise, Nigeria, just like any other highly open economy, 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.

Some banking reform programmes occur, some of the time, independent of any banking crisis. Irrespective of the cause, however, bank reforms are implemented to strengthen the banking system, embrace globalization, improve healthy competition, exploit economies of scale, adopt advanced technologies, raise efficiency and improve profitability. Ultimately, the goal is 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. 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). Thus, the reforms were to ensure a diversified, strong and reliable banking industry where there is safety of depositors' money and position banks to play active developmental roles in the Nigerian economy. This paper therefore analyzes the effects of banking reforms on the performance of banks and assess if they have been able to achieve predetermined goals and set objectives in Nigeria. This paper has five sections. Following this introductory part, Section 2 shows the literature review. The model specification and estimation techniques are presented in Section 3 and Section 4 covers the result from the estimation process and discussion, while in Section 5 is the conclusion.

2. Literature Review

Banks are the linchpin of the economy of any country. They occupy central position in the country's financial system and are essential agents in the development process. By intermediating between the surplus and deficit savings' units within an economy, banks mobilize and facilitate efficient allocation of national savings, thereby increasing the quantum of investments and hence national output (Afolabi, 2004). Through financial intermediation, banks facilitate capital formation (investment) and promote economic growth. The decade between 1998 and 2008, was particularly traumatic for the Nigerian banking industry; with the magnitude of distress reaching an unprecedented level, thereby, making it an issue of concern not only to the regulatory institutions but also to the policy analysts and the general public. Thus, the need for a drastic overhaul of the industry was quite apparent Afolabi (2004).

In furtherance of this general overhauling of the financial system, the Central Bank of Nigeria introduced major reform programmes that changed the banking landscape of the country in 2004. The primary objective of the reform is to guarantee an efficient and sound financial system. The reforms are designed to enable the banking system develop the required resilience to support the economic development of the nation by efficiently performing its functions as the fulcrum of financial intermediation (Lemo, 2005). According to Afolabi (2004) the reforms were also to ensure the safety of depositors' money, position banks to play active developmental roles in the Nigerian economy, and become major players in the sub-regional, regional and global financial markets.

The key elements of the 13-point reform programme in Nigeria (CBN, 2006) include: Minimum capital base of N25 billion with a deadline of 31st December, 2005; Consolidation of banking institutions through mergers and acquisitions; Phased withdrawal of public sector funds from banks, beginning from July, 2004; Adoption of a risk-focused and rule-based regulatory framework; Zero tolerance for weak corporate governance, misconduct and lack of transparency; Accelerated completion of the Electronic Financial Analysis Surveillance System (e-FASS); The establishment of an Asset Management Company; Promotion of the enforcement of dormant laws; Revision and updating of relevant laws; Closer collaboration with the EFCC and the establishment of the Financial Intelligence Unit (Soludo, 2004).

Two of the above reform elements which have since generated so much concern and reactions from various stakeholders are: (a) Requirement that the minimum capitalization of banks should be N25 billion with full compliance by 31st December, 2005 and (b) Consolidation of banking institutions through Mergers and Acquisitions. Soludo (2004). The main thrust of the 13-point reform agenda was the prescription of minimum shareholders' funds of 25 billion for Nigerian Deposit money bank not later than December 31, 2005. In view of the low financial base of these banks, they were encouraged to merge. Out of the 89 banks that were in operation before the reform, more than 80 percent (75) of them merged into 24 banks while 14 that could not finalize their consolidation before the expiration of deadline were liquidated. Because of the apparent advantage of efficiency related benefits, the banking industry has experienced an unprecedented level of consolidation as mergers and acquisitions among financial institutions have become a general phenomenon globally. For instance, between 1993 and 1996, about 1500 mergers were recorded in the USA, similar experience was observed in the Europe and Asian continents (Lemo, 2004).

To a large extent, this consolidation is based on a belief that gains accrue through expenses reduction, increased market power, reduced earnings volatility, and scale and scope economies. However, the characteristics of the kind of reforms induced mergers and acquisition of the banking industry creates doubts about its potentials of realizing efficiency gains. A deeper look at the 24 banks that emerged after the consolidation shows that most banks that were regarded as distressed and unsound regrouped under new names or fused into existing perceived strong banks not necessarily to correct the inefficiency in their operating system but just to meet the mandatory requirement to remain afloat and to continue business as usual. While this consolidation no doubt has benefits, what is less clear is the effect of this consolidation on the operating efficiency of the banks. In view of this observation, certain issues arise on the desirability or otherwise of this imposed 'one fit all consolidation' exercises: will the increase in market power creates monopoly which theoretically increase price (bank interest rates) and reduce output (financial intermediations)? (Soludo, 2004).

Sanusi was appointed the governor of the Central Bank of Nigeria (CBN) in July, 2009. His entry is a switch in his career, from the regulated in the banking system to become a regulator, the background which equipped him with first-hand knowledge of the banking system in Nigeria. On assumption of office, Sanusi recognized continuous weakness in the system despite the recapitalisation of 2005. He identified weak corporate governance, operational indiscipline and global financial crisis as the major causes of the weakness and prescribed further decisive reforms to forestall total collapse of the sector. The weakness of the financial system was earlier recognized in 2004 by Soludo, who took pragmatic steps to revolutionise the banking sector with the re-capitalisation project through which Nigerian banks were pruned from about 89 to 24 with minimum capital requirement moved from N2 billion to N25 billion at the end of 2005. The core of the reform was to establish reliable and efficient banks that could guarantee depositors' money. By 2009, it was discovered that Nigerian banks could no longer conveniently fulfil their obligations to depositors, a situation which suggested that banking consolidation of 2005 was concluded on false declarations and fraud, lack of depth and almost qualified as a wasteful application of national human, financial and material resources. In essence, the supposed consolidation succeeded as a mere marriage of incompatible banks. The era brought significant corporate indiscipline, fraud and discriminatory practices into banking operation and regulation in Nigeria. Unlike elsewhere in the world, Nigerian banks became obviously disconnected from the rest of the economy and the supposed core mandate as a transmission channel of monetary policies. Nigerian banks were scarcely able to commit themselves to transparent and responsible investments. The system could not guarantee credit flow to the real sector of the economy, specifically, manufacturing, agriculture and the small and medium scale enterprises that are critical to employment and income generation which are strategic to poverty alleviation. The catalytic growth acclaimed by Nigerian banks without equivalent experience in the real sector, thus, only passes for a mere deception. The truth is that growth of the sector should logically correlate with that of the economy within which it functions.

Sanusi's entry into the system with his wealth of experience from the regulated side of the "coin" critically redefined the banking sector, including governance, operations and systems ethics (Sanusi, 2009). His administration is critical of lack of transparency in the manner recapitalization was implemented with doubt over whether or not banks actually raised fresh capital as claimed. Contrary to much criticism that greeted Sanusi's appointment as the CBN governor and much more his policy responses to correct the ills identified in the Nigerian banking system, the results of his efforts have gained both local and international applause in a short time. Sanusi has won national, continental and global awards for excellence within a short period. These awards are core indications that Sanusi is effectively leading in reversing significant capital flight experienced in the economy during the global financial crisis and Nigerian stock market crash. It is important to re-emphasise the obvious, however, that overall gains of reforms will be lost if the current state of the nation is not urgently addressed. The Sanusi initiative, which is currently drawing accolades from the world, is not enough to correct the bad state the Nigerian economy found itself without an enabling environment for real sector revival and business restoration put in place to encourage unrestrained flow of foreign and domestic investments. Political stability is also non-negotiable as no investor will bring money into a highly volatile and unsafe business environment (Imala, 2005). Hence the need to re-assess the position of the banking sector after these major reforms.

3. Model Specification and Estimation Techniques

The survey research design is used because it gives greater room to study the subject matter and ensures that inferences can be made about some characteristic, attitude, or behaviour of the population examined in the study. The data collected for this study was sourced using questionnaires and a total of 100 questionnaires were administered to bank staff. The research instrument used (the questionnaire) is considered most appropriate because it covers the scope implied by the subject and thus has content validity. Each of the statements in the questionnaire was reviewed by an expert to access the extent to which it relates to the effect of bank reforms on the performance of banks in Nigeria. To this end, the instrument was passed through experts who asserted that it represents a true and fair view; therefore, the research instrument is valid.

The data collected was then analyzed using the Statistical Packages for Social Sciences (SPSS). The method implemented for the presentation of data includes the use of tables, percentages and means. The hypotheses formulated were tested using the ANOVA (Analysis of Variance) method. The One-Way ANOVA procedure produces a one-way analysis of variance for a quantitative dependent variable by a single factor (independent) variable. Analysis of variance is used to test the hypotheses to ascertain if several means are equal. The hypotheses tested are stated below:

1. Ho There is no significant impact of bank reforms on the performance of banks in Nigeria
   H_1: There is a significant impact of bank reforms on the performance of banks in Nigeria
2. Ho: Bank recapitalization has no significant effect on the Nigerian economy
   H_1: Bank recapitalization has a significant effect on the Nigerian economy

4. Results and Discussion

A total of 100 questionnaires were distributed. After the questions were collected from the respondents, they were properly screened and sorted out. The details of the questionnaire administered and returned are shown in the table below:

Table 1: Analysis of Rate of Response by respondents

Questionnaire	Respondent	Percentages
Returned	80	80%
Returned but not properly filled	12	12%
Not returned	8	8%
Total Distributed	100	100%

Source: Field Survey (2012)

The table above shows that 100 questionnaires were distributed, out of which 80 were properly filled and returned which represents (80%), 12 questionnaires were returned either not properly filled or unfilled which represents 12% and 8 questionnaires were not returned at all by the respondents which represents 8%.

Hypotheses Testing

Hypothesis 1

Ho: There is no impact of bank reforms on the performance of banks in Nigeria

H_1: There is an impact of bank reforms on the performance of banks in Nigeria

Table 2: ANOVA Analysis of Hypothesis 1

	Sum of Squares	Df	Mean Square	F	Sig.
Between Groups	14.818	4	3.704	8.504	.000
Within Groups	32.670	75	.436		
Total	47.488	79			

Source: Author's Computation

From the above, the F-calculated is 8.504 while F-tabulated is 6.26 at 5% level of significance and degree of freedom of 4. Since the calculated value of F Statistics is greater than the tabulated value, we reject the null hypothesis which states that there is no impact of bank reforms on the performance of banks in Nigeria and concluding based on the result that there is an impact of bank reforms on the performance of banks in Nigeria.

Hypothesis 2

Ho: Bank recapitalization has no effect on the Nigerian economy

H_1: Bank recapitalization has an effect on the Nigerian economy

Table 2: ANOVA Analysis of Hypothesis 2

	Sum of Squares	Df	Mean Square	F	Sig.
Between Groups	7.739	4	1.935	7.325	.000
Within Groups	19.811	75	.264		
Total	27.550	79			

Source: Author's Computation

From the above, the F calculated is 7.325 while F tabulated is 6.26 at 5% level of significance and degree of freedom of 4. Since the calculated value of F Statistics is greater than the tabulated value, we reject the null hypothesis and accept the alternative hypothesis and conclude based on the result that bank recapitalization has effect on the Nigerian economy.

Discussion of Findings

Testing hypothesis one, it was found out that the calculated value of F-Stats which was obtained from the SPSS data was greater than the tabulated value hence, we reject the null hypothesis and accept the alternative, thus concluding that there is an impact of bank reforms on the performance of banks in Nigeria. In testing hypothesis two, it was found out that the calculated value of F-stats was greater than the tabulated value and so the null hypothesis is rejected and the alternative accepted and we therefore conclude that bank recapitalization has effect on the Nigerian economy.

The analysis of data obtained from questionnaire also revealed that there is an impact of bank reforms on the performance of banks in Nigeria. Such impact can be seen by way of increased profitability, stronger capital base, greater operational efficiency, and thus guaranteeing an efficient and sound financial system. It was also observed that by way of accelerating zero tolerance for inadequate corporate governance and ensuring greater transparency, the public sector confidence has been re-instated in the sector as clearly stated by the bank respondents.

The entities resulting from the consolidation of the Nigerian financial sector became bigger (in terms of size, capability and financial might) and thus, are able to compete more aggressively in the market. Also, because the number of banks drastically reduced, more opportunities became available to the evolved banking groups. However, a major consequence of the consolidation of the banking sector will be an increased effort by banks to project them within the market place. For this to be effective, it must be based on more than just a need to put out information on the new entity. Moreover, the study reveals that despite the reforms, post consolidation challenges like challenges of increased return on investment and unhealthy competition and rivalry still exist.

5. Conclusion

The study explored bank reforms and performance of banks in Nigeria. This has become necessary in the face of evolving developments in the banking industry in Nigeria especially with the exchange of baton by the Central Bank of Nigeria (CBN) governors and introduction of new ideas and reforms. As a result of this, the Nigerian banking system has undergone remarkable changes in recent years, in terms of the number of institutions, ownership structure, as well as depth and breadth of operations. However the reform programme has brought about certain implications on the Nigerian banking sector which include brand and structural implication. Brand implications refer to those issues the new entities would face if they are to survive in the long term. They include change of name, change of logo, and change of brand message, to ascertain what the brand would become over time. Structural implication on the other hand refers to issues that have direct impact on staff, customers and the structure of the entire banking sector. From the findings of this study, it is established that there is an impact of bank reforms on the performance of banks as well as on the Nigerian economy. It is therefore important that these new evolved banking groups understand the implications of their consolidation in order to be a successful unit, both in the short and long run which will in turn benefit the banking industry and the Nigerian economy at large. It is clear that the reforms has affected the performance of the banking sector over the period, thus for a stronger and more resilient banking and financial system, banks need to improve their current state of development to be truly classified amongst the top banks in the world.

This paper is of the opinion that some of the reforms have come too soon and thus, rendering sections of the economy such as the lower class, illiterates and the economically active poor incapable of banking transactions. A very good example is the cashless policy in Lagos State, and also the minimum withdrawal requirement set upon banks by the Central Bank of Nigeria. This paper therefore recommends that the implementation of these newer reforms should be made to evolve in a gradual process for proper enlightenment and entrenchment. The Central Bank of Nigeria (CBN) should endeavor to capture the short and long term implications, on all sectors of the economy particularly the rural sector, when making future policy recommendations. The banks should endeavor to drive zero tolerance for inadequate corporate governance and imbibe best practices, improve on self-regulation, institute IT-driven culture and seek to be competitive in today's globalizing world. This would ensure that the public sectors confidence in them is guaranteed.

References

Adegbaju, A.A. and F. O. Olokoyo (2008), "Recapitalization and Bank's Performance; A case study of Nigerian Banks" *African Economic and Business Review,*Vol.6, No.1.pp 1-4.

Afolabi J.A. (2004), "Implications of the Consolidation of Banks for the Nigerian Banking System", *Paper* presented at the NDIC organised Workshop for FICAN Enugu.

Central Bank of Nigeria (2006), *Banking Supervision Annual Report*, Abuja, CBN Press.

Central Bank of Nigeria (2011), *Monetary Policy Reform*, Abuja, CBN Press.

Imala, O.I., (2004); "The Experience of Banking Supervision in Financial Sector Surveillance", *Central Bank of Nigeria Bullion*, Vol. 28, No.1, Pp. 49-53. Lagos: Central Bank of Nigeria.

Imala, O. I. (2005); "Consolidation in the Nigerian Banking Industry: A Strategy for Survival and Development", *Paper* presented to the Nigerian Economics Students' Association (NESA), University of Abuja Chapter.

Kanayo O. (2011), *Financial Sector Reforms in Nigeria: Issues and Challenges*, Enugu, African Institute for Applied Economics.

Lemo, T. (2005), "Regulatory Oversight and Stakeholder Protection" , *Paper* presented at the BGL Mergers and Acquisitions Interactive Seminar, held at Eko Hotels & Suits. V. I.

Maddala, G.S (1997), *Econometrics*, New York McGraw-Hill.. 17, pp. 21-23.

Soludo, C. (2004), "Consolidating the Nigerian Banking Industry to Meet the Development Challenges of the 21st Century". Being an address delivered to the Special Meeting of the Bankers' Committee, held on July 6, at the CBN Headquarter, Abuja.

Soludo, C. (2006), "Financial Sector Reforms and the Real Economy", a *Speech* to the Council of Fellows of the Pharmaceutical Society of Nigeria.

Soludo, C. (2006b), "Beyond Banking Sector Consolidation in Nigeria", Presentation at the Global Banking Conference on Nigerian Banking Reform, available online at: http://www.cenbank.org/out/Speeches/2006/Govadd29-3-06.pdf [Accessed 17 June 2008].

Uchendu, O. A. (2005), "Banking Sector Reforms & Bank Consolidation: The Malaysian Experience", *CBN Bullion* Vol. 29, No2.