

Central Bank of Nigeria Regulation and Performance of Banking Sector

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Abstract

The study investigated impact of Central Bank of Nigeria (CBN) on performance of banking sector in Nigeria. Primary data obtained through questionnaire administered to top staff members of Zenith Bank in head office, Lagos were used for the study.

Data obtained were analyzed with the use of simple regression to test the hypothesis with the aid of statistical Package of Social Sciences (SPSS) to establish the degree at which Central Bank of Nigeria (CBN) regulations affect the performance of banking sector in Nigeria.

Result from the study indicated that CBN regulations have significant impact of the performance of banks in Nigeria. The study also revealed that regulations have significant impact on profitability of banks in Nigeria. The study therefore recommended that requisite surveillance equipment should be obtained at sufficient quantities to assist personnel in discharging their duties and that public should be adequately enlightened about the operations of the Central Bank of Nigeria and Nigeria Deposit Insurance Corporation.

Keywords: Central Bank of Nigeria, Nigeria Deposit Insurance Corporation, Regulation and Performance.

1.0 Introduction

Banking has been one of the most regulated industry. In all countries and at all times since the establishment of banking, governments have imposed controls on banking institutions, even when most other businesses were free to operate, subject only to the statutes and other general rules of law.

Banks are the life-giving force of an economy as they serve as the catalyst for growth and development. Banks are able to perform this role through their crucial functions of financial intermediation, provision of an efficient payments system and facilitating the implementation of monetary policies. Governments the world over attempt to evolve an efficient banking system not only for the promotion of efficient intermediation, but also for the protection of depositors, encouragement of efficient competition, maintenance of public confidence in the system, stability of the system and protection against systematic risk and collapse. Banking regulation is the process of authorizing, monitoring and reviewing the operations of a banking institution through its life cycle to ensure that the institution continues to operate in a safe and sound manner (Udendeh, 2016). Banking regulation involves an understanding that the licenced party will obey the rules, laws and collective agreements governing the conduct of banking business in a given jurisdiction. The submission by the licenced-party to uphold the standard practice in the profession is the condition upon which the licence is premised.

The apex regulatory authority of the Nigerian banking sector is the Central Bank of Nigeria (CBN). CBN develops a regulatory and supervisory framework for on-site and off-site supervision of the banking sector in Nigeria.

Due to the importance of banks to an economy, a place of pride has been given to banks in economic development. As a result, governments have appointed regulatory and supervisory authorities to watch over this important sector. Despite the presence of formal regulation and self-regulation banking crises occur, imposing hardship on depositors, consumers and the economy (Umoh, 2016).

Regulatory guidelines drawn for banks by the CBN are made available to the Nigeria Deposit Insurance Corporation (NDIC) which similarly shares deposit insurance guidelines with the CBN. Examination reports issued by both agencies are exchanged and penalties for contraventions of banking laws/regulations are conventionally imposed by the Central Bank of Nigeria (CBN) as regulator.

The major forms of bank regulation in Nigeria include; capital requirement, reserve and liquidity requirements; control over lending activities and lastly limitations on prices paid and charged. The aim of this study is to investigate the impact of Central Bank of Nigeria regulation on the performance of banking sector in Nigeria.

2.0 Literature Review

2.1 Conceptual Framework

2.1.1 Banking Regulation

Bank regulation originated from the objective of banks as financial intermediaries. The depositors provide funds that are used for issuing loans to borrowers; as such, the stakeholders of the bank are the depositors.

Regulation is seen as a body of specific rules of agreed behavior either imposed by some government or implicit agreement within the industry that limits the activities and business operations of financial institutions. The primary objective of regulating the financial system of a country is to ensure the safety of that country's financial system by checking competitive inequities and other inefficiencies (Ekpeyong, 1995).

2.2.1 Concept of Profitability

Aburime (2008) stated that profit means the difference between the revenue generated from the sale of output and the full opportunity cost of factor used in the production of that output. Included within costs are the premium charged for risk taking and the costs of using the owners capital.

The following ratios are the most important earning ratios used in assessing the bank profitability (Muhammad & Muhammad, 2017).

- i. Return on assets (ROA)

$$\text{ROA} = \frac{\text{Net Income}}{\text{Total Assets}} \times 100$$

- ii. Return on equity (ROE)

$$\text{ROE} = \frac{\text{Net Income}}{\text{Capital}} \times 100$$

- iii. Return on deposit (ROD)

$$\text{ROD} = \frac{\text{Net Income}}{\text{Total Deposit}} \times 100$$

2.2 Theoretical Framework

2.2.1 Financial Intermediation

Role of financial intermediation and the financial system in economic development was rekindled by McKinnon (1973) and Shew (1973). They enunciated the functions of financial institutions in the savings-investment process were underscored as being an effective conduit for the mobilization and allocation of capital by equilibrating the supply of loanable funds with the demand for investment funds, and the transformation and distribution of risks and maturities. They further enunciated the “financial liberalization” theory which they argued that government restrictions on the banking system restrain the quality and quantum of investment.

Pagano (1993) noted that financial intermediation has a positive effect on national economic growth, and that government intervention or restriction in the financial system has a negative effect on the equilibrium growth rate.

2.2.2 Economic Growth

Fadare (2010) learning towards the “assumptions of the neo-classical economic theory” opined that “the long-run rate of economic growth is depended only on the rate of technological progress and the rate of labour force growth, and that capital is always subject to diminishing return”. Thus, given a fixed stock of labour, the impact on output of the last unit of capital accumulated will always be less than the one before. Assuming for simplicity, no technological progress or labour force growth, diminishing returns implies that at some point, the amount of new capital produced is only just enough to make up for the existing capital lost due to depreciation (Solow, 1956). According to Fadare (2010) endogenous growth theory suggests that a strong banking sector promotes economic growth and holds that policy measures can have an impact on the long-run growth rate of an economy. Banking policies which embrace openness, competition, change and innovation will promote economic growth. On the other hand, policies which have the effect of restricting or slowing banking reforms by protecting or favouring particular industries or firms, are likely, over time, to experience unsustainable economic growth.

2.3 Empirical Review

Flamini, McDonald and Schumaker (2009) investigated the determinant of bank profitability in sub-Saharan Africa between 1998 and 2006 using the panel data. With the aid of Arellano-Bond two-step Generalized Method of Moment (GMM), they found that variables such as bank size activity diversification, and private ownership have a positive influence on the level of bank profitability (ROA) in the region.

Sufian and Habibullah (2010) investigated whether economic freedom influences banks' performance in Malaysia using panel data between 1997 and 2007 with ordinary least square (OLS) estimation technique. They found that economic freedom and business freedom have a favourable effects on banks' performance while an adverse effect comes from monetary freedom. They concluded that corruption has a corrosive impact on Malaysia banks profitability.

Sufian and Habibullah (2012) employed an unbalanced panel data of 153 banks to examine the effect of globalization on bank performance in China with the aid of panel regression method. Their results revealed that bank profitability is positively and significantly determined by trade flows, cultural proximity, and political globalization.

Alkhazaleh and Almsafr (2014) in their analysis of determinants of bank profitability in Jordan between 1999 and 2013 using fixed effect regression model. Their result showed that capital structure, bank size, and liquidity exhibit significance influence on bank profitability.

Tarif *et al* (2014) analyzed the determinants of profitability level among Pakistan banks for the sample period 2004-2010 by utilizing both fixed and random effect models. They concluded that independent variables significantly influence profitability.

3.0 Methodology

Research design for this study is a cross-sectional survey of target population. This entails the collection of data and analysis through sampling arrive at a logical conclusion. The study was carried out in Lagos State. The choice of Lagos for this study was as a result of its industrialization and also because it has the largest number of bank branches when compared to other states in Nigeria.

3.1 Population of the Study

The population for this study was the top staff members of Zenith Bank Nigeria Plc.

3.2 Sampling Size and Sampling Technique

A total number of 50 members of Zenith bank staff was selected using simple random sampling method.

3.3 Sources of Data

Primary source of data was used for this study

3.4 Research Instrument

A well-structured questionnaire was developed on the basis of a comprehensive review of relevant literature. The questionnaire was structured in a way that included dependent and independent variable.

3.5 Validity of Research Instrument

The questionnaire used for the study was given to senior academic staff members for scrutiny and corrections. Suggestions made were incorporated to the final draft of the instrument to ensure content validity.

3.6 Administration of Research Instrument

The questionnaires were self-administered to top staff members (senior managers and Assistant General Managers) of Zenith Bank during working hours and collection was due immediately.

3.7 Data Analysis

Data collected from respondents were analyzed with the use of simple regression to test the hypothesis with the aid of statistical package of social sciences (SPSS) computer software and the purpose of using it is to establish the degree at which Central Bank of Nigeria (CBN) regulations affect the performance of banking sector in Nigeria.

Regression analysis was used to express the relationship between the two variables and estimate the value of dependent variable Y based on selected value of the independent variable X that is relationship between CBN regulations and the performance of banking sector in Nigeria.

This is expressed mathematically;

$$Y = a + bx + \mu$$

Where:

Y = Dependent variable

a = Constant

b = Co-efficient of the independent variable

x = Independent variable

μ = Stochastic variable

4.0 Analysis of Result

Central Bank of Nigeria regulation has no impact on banking sector performance

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.982(a)	.965	.953	2.34087

- Predictors: (Constant), CBN regulations
- Dependent variable: Nigerian banks performance
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ANOVA (b)

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	449.561	1	449.561	82.042	.003(a)
Resident	16.439	3	5.480		
Total	466.000	4			

- Predictors: (Constant), CBN regulations
- Dependent variable: Nigerian banks performance

Coefficient (a)

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta	B	
1 (Constant)	-1.707	1.663		-1.026	.380
Effective banking regulation encourage quality services and promote an efficient and competitive banking system.	1.171	.129	.982	9.058	.003

a. Dependent Variable: Performance of commercial banks

Interpretation

It can be seen from the above that the simple regression between CBN regulations and banks performance in Nigeria recorded F-value of 82.042 indicating a strong relationship with a .003 level of significance.

Decision

Since the t-calculated (9.058) is significantly greater than the value of t-tabulated (1.68) given 48 degrees of freedom at 0.05 level of significance. This led to the rejection of the null hypothesis and acceptance of the alternative hypothesis, which states that CBN regulations have a significant impact on the performance of banks in Nigeria.

Central Bank of Nigeria regulation has no impact on banking sector profitability

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.986(a)	.973	.964	2.04371

d. Predictors: (Constant), CBN regulations

e. Dependent variable: Nigerian banks profitability

ANOVA (b)

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	453.470	1	453.470	108.570	.002(a)
Residual	12.530	3	4.177		
Total	466.000	4			

c. Predictors: (Constant), CBN regulations

d. Dependent variable: Nigerian banks profitability

Coefficient (a)

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta	B	
1 (Constant)	-3.106	1.555		-1.998	.140
Effective banking regulation encourage quality services and promote an efficient and competitive banking system.	1.311	.126	.986	10.420	.002

b. Dependent Variable: Profitability of commercial banks

Interpretation

It can be seen from the above that the simple regression between CBN regulations and profitability of banks in Nigeria recorded F-value of 108.570 indicating a strong relationship with a .040 level of significance.

Decision

Since the t-calculated (10.420) is significantly greater than the value of t-tabulated (1.68) given 48 degrees of freedom at 0.05 level of significance. This led to the rejection of the null hypothesis and acceptance of the alternative hypothesis, which states that CBN regulations have a significant impact on the profitability of banks in Nigeria.

Discussion

Data collected and duly analyzed in this study revealed that most of the respondents were of the view that the Central Bank of Nigeria regulatory and supervisory framework encourages quality services and promotes an efficient and competitive banking system. The research also showed that the regular On-site and Off-site supervision has helped in identifying problem areas in banks and it has also helped in reducing unprofessional and unethical conduct in Nigerian banks. The result of the analysis concludes that the Central Bank of Nigeria regulations has a significant impact on banks performance and banks profitability.

5.0 Conclusion and Recommendations

The study investigated Central Bank of Nigeria regulation and the banking sector performance.

5.1 Conclusion

From the study, we can infer that regulation is very important to the growth and survival of banks in Nigeria. Central Bank of Nigeria regulation has a significant impact on banks performance in Nigeria. The study also revealed that Central Bank of Nigeria regulation has a significant impact on banks profitability. The substance of banking system is built around confidence. Banking regulation has made banking public to have confidence in the banking system.

5.2 Recommendations

The following recommendations are made based on the conclusion made from this study:

- i) Effective corporate governance in financial institutions should be enforced in order to facilitate effective supervision.
- ii) Capacity building of both the regulators and operators should be put in place.
- iii) Public should be adequately enlightened about the operations of the CBN and Nigeria Deposit Insurance Corporation (NDIC) as regards bank regulation and supervision.

- iv) Every bank in Nigeria should employ strategy to minimize risks and costs of failure.
- v) Requisite surveillance equipment should be obtained at sufficient quantities to assist personnel in discharging their duties.

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