Banking Reform and Financial Intermediation of Some Selected Deposit Money Banks in Nigeria

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***Abstract*—**This study basically evaluates the effect of the baking reform on the financial intermediation of Deposit Money Banks (DMBs) in Nigeria. It utilizes both primary and secondary data for the period of 14 years ranging from 1999 to 2012. The techniques employed for the purpose of analyses are Paired Sample T-test, Simple Percentage and Chi-square Test. The results of the study provide evidence for the failure to reject the two null hypotheses formulated. The study therefore concludes that the recent 2004 banking reform has no significant effect on the quantum of intermediation carried out by banks. The perception of the respondents also indicates that the reform has no effect on the intermediation function of banks. Hence, the study recommends that regulatory authorities should ensure that effective supervision and monitoring are imposed in the banking sector in order to ensure conformity to statutory and regulatory rules.

***Keywords*—**Banking Reform, Intermediation, Deposit Money Banks.

I. Introduction

ONE of the major functions of Deposit Money Banks (DMBs) is financial intermediation. That is, the act of channeling funds from surplus economic units to deficit ones. With effective and efficient intermediation banks can lead to economic growth and development. This view was recognized as far back as 1934 in which Schumpeter argued that financial intermediation by banks and other financial institutions is a necessary condition for economic development as they ensure through the intermediation function that no viable project is frustrated due to lack of funds. Similar view is also expressed by King and Levine (1993).

In an effort to create a stable banking sector that can effectively and efficiently intermediate, Nigerian banking sector has undergone series of transformations. According to Balogun (2007), from the year 1986 after the introduction of structural Adjustment Program (SAP) to the year 2004 when the new reform of the banking sector was introduced, the sector has undergone four phases of banking reforms.

The introduction of the 2004 reform led the sector to become highly concentrate with the top ten banks accounting for more than 50% of the total assets, and many of the 89 banks that are operating are small in size and unable to effectively compete with the bigger ones (Ogunleye, 2005). Despite the reform being in existence for the past eight years and the number of banks operating in the sector drastically reduced from 89 as at the year 2004 to 21 as at the year 2013, the issue of concentration is still of major concern. This is due to the fact that the capital base of the ten major banks is still by far greater than that of other smaller banks that merged and this may affect the quantum of funds that are to be used for intermediation purpose.

Another compounding factor to the situation is the provision made by the Central Bank of Nigeria (CBN) in which banks are allowed to operate universal banking system. This has potential implication of making banks to divert from core banking areas to other range of services that may affect intermediation role. This by extension seems to imply the existence of conflicting position between the regulatory authority and banks' management. While on one hand, most of the banks' management inclined to a traditional theory on intermediation in which they demand enabling environment to execute core intermediation function which is considered to lower transactions costs and improve investor information, regulatory authority on the other, inclined to current theory of intermediation. The authority argue that as a result of deregulation, information provision has improved via technology and this can lead to intermediation without necessarily using banks and hence the need for the banks to diversify to other non-banking activities for sufficient revenue generations. This therefore, prompted the need to investigate the situation empirically to ascertain its effect on the intermediation of banks.

In spite of the various studies that have been conducted to assess the effect of intermediation in Nigeria, we have not come across a study that solely attempt to investigate the effect of the quantum of intermediation taking pre and post banking reform and at the same time investigating management perception as regard the situation. Most of the studies look at intermediation in relation to economic growth and financial intermediaries with banks also inclusively used. The only study that we come across that made use of banks solely was Hesse (2007) in which he investigated financial intermediation in the pre-consolidated banking sector excluding the post-

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consolidation effect. Hence, investigating the pre- and post-effect of the phenomenon may be of paramount value.

The major objective of this study is to investigate the effect of banking reform on the quantum of intermediation of banks in Nigeria. The other objective is to ascertain the perception of banks' management of the effect of the reform on intermediation quantum. The period under study is from 1999 to 2012. The periods are chosen in order to establish trend effect of the reform and hence six years before its emergence (1999-2005) and eight years after its emergence (2006-2012) are selected.

On the basis of the above background, the study formulated the following hypotheses for testing:

H01: Banking reform has no significant effect on the intermediation of banks in Nigeria.

H02: Banks' managers do not perceive banking reform to have any significant effect on the intermediations of banks in Nigeria.

The remaining part of this paper is divided into the following sections. Review of related literature is in section 2. The methodology adopted for the purpose of the study is dealt with in section 3. Section 4 addressed data presentation and analysis, and section 5 presented summary, conclusion and recommendations.

II. Review of Related Literature

Vast literatures exist on both theoretical and empirical studies on financial intermediation. Most of the studies investigate the effect of intermediation on economic growth of countries, notable among which are:

In one of the earlier studies conducted by Goldsmith (1969), an evaluation of a relationship between financial intermediation and economic growth was made of 35 countries. The study establishes rough parallelism between economic and financial development especially when data of several decades are used. Other studies conducted with similar outcomes are found in McKinnon (1973) and Shaw (1973).

In a study carried out by Greenwood and Jovanovic (1990), an examination of financial intermediaries' risk-pooling and monitoring functions was made. The study establishes that among other financial intermediaries, banks ensure higher expected rates of returns that promote growth.

In a similar study to Greenwood and Jovanovic (1990), Saint-Paul (1992) finds that financial intermediation costs are fixed. The other finding of the study establishes that both economic growth and financial development reinforce each other while raising welfare.

Following Schumpeter (1934) approach to investigating intermediation, Chen, Yeong-Yuh, and Ping (1996) generalize Schumpeter's view that financial intermediation results in more investment projects that spurs economic growth with sophistication and specialization of production process.

Loayza and Ranciere (2002) conducted a study to reconcile literatures' contradiction of the effects of financial intermediation on economic activity of countries. The main result of the study is that a positive long-run relationship between financial intermediation and output growth co-exists with a, mostly, negative short-run relationship.

More relatively recent studies in which attempt were made in establishing relationship between financial intermediation and economic growth of countries are found in McCaig and Stengos (2005), Hao (2006), Romeo-Avila (2007), Coccorese (2008), Abu-Bader and Abu-Qarn (2008), Wolde-Rufael (2009), and Bangake and Eggoh (2011).

As the works reviewed above were mostly conducted in advanced economy using cross-sectional countries data, the outcome of the effect of the intermediation may not be similar to the Nigeria's setting due to peculiarities difference, hence the need to investigate its situation distinctly.

Empirical evidence of the effect of bank intermediation from developing countries is very slim. Some of the few studies are Allen and Ndikumana (1998), Chirwa and Mlachila (2004), Hesse (2006), Gries, Kraft, and Meierrieks (2009), Odhiambo (2011), and Kar, Nazlioglu and Agir (2011) among others.

In the Nigerian context some of the few studies include Sealey's (1980), Ajakaiye and Odusola (1995), Ogunleye (1995), Sani and Yakpogoro (1997), Uchendu (1998), Isijiola (2000), Adebiyi (2000a), Adebiyi (2000b), Ezirim and Muoghalu (2002), Enendu (2003), Bello (2005), Victor (2007) and Sebatian (2007) among others.

In spite of the fact that a substantial amount of research has been directed toward financial intermediation of banks in both developed and transition economy, Nigeria inclusive, most of these researches made use of regression analysis which is quite distinct from the methodology that this study intends to make use of. It is expected that as a result of adopting different methodology, distinct outcome of the effect of reform on the intermediation may be established, especially given the fact that different duration period is adopted by the study.

III. Research Methodology

The research methods adopted by this study are descriptive, historical and survey. The data used came from secondary and primary sources and the instruments adopted are respectively documentation and questionnaire. The secondary data have to do with intermediation ratio which is computed by dividing total credit disbursed by banks and gross domestic product. In the case of primary data, questionnaire responses of respondents are utilized.

The population of this study is made up of all the Deposit Money Banks of the Nigerian banking sector and they are 21 in number as at the year ended 31st December, 2012. The sample size of the study is 10 banks drawn from the defined population and it is arrived at by using Krejcie and Morgan (1970) sample size formula, which is represented thus:

$$n = X^2NP(1-P) \div d^2(N-1) + X^2P(1-P)$$

Where:

n = Sample Size

X^2= Chi-square value @ d.f. of 1 and 95% confidence level =3.84
N= Population Size
P = Population Proportion (assumed to be 0.50)
d= Degree of Accuracy (expressed as a proportion, 0.05)

Simple random sampling is a basic sampling design adopted in selecting the sample; this is because it allows equal representation. The selected sample banks are: Access Bank Plc; AfriBankplc; Diamond Bank plc; First Bank plc; First Inland Bank plc; Guaranty Trust Bank plc; Sterling bank; Union Bank plc; United Bank of Africa plc; and Wema Bank plc. The study utilized aggregated data of the respective ten sample banks.

As regard the sample size of the potential respondents that questionnaires are administered to, the study adopted Bedward (1999) stratified random sampling formula, which is represented thus:

$$n = n_1 \div N_1 \times N$$

Where:
n = Number of Potential Respondents from each Bank
n_1 = Number in each Group
N_1= Population Size of the Potential Respondents
N = Total Sample Size of the Potential Respondents

The population size of the potential respondents is 2,734 in number, and it constitutes of all management staff of the ten banks earlier selected as of the year 2013. The total sample size of the potential respondents is 111 derived from all the management staff of the selected banks using Krejcie and Morgan (1970) sample size formula.

The following Table presents the selected banks, management staff, and the proportional distribution of the sample size.

TABLE I
PROPORTIONAL DISTRIBUTION OF SAMPLE SIZE

S/N	*Names of Banks*	*Management Staff*	*Proportion*
1.	Access Bank	122	5
2.	Afri-Bank	70	3
3.	Diamond Bank	270	11
4.	First Bank	469	19
5.	First Inland	466	19
6.	Guaranty Trust Bank	327	13
7.	Sterling Bank	309	13
8.	Union Bank	351	14
9.	United Bank of Africa	300	12
10.	Wema Bank	50	2
	Total	2,734	111

Source: Various Annual Reports and Author's computations

The techniques adopted for the purpose of the analysis were Paired Sample T-test, Simple Percentage, and Chi-square Test and they are explained thus:

Paired Sample T-test is used to determine whether as a result of the banking reform, there has been significant improvement in the performance of banks or not. Instead of computing the result manually, Microsoft Excel is used. The formula for the test computation is given thus:

$$t= \frac{\acute{y}_1-\acute{y}_2}{\sqrt{\frac{\sum d^2-(\sum d)^2/n}{n(n-1)}}}$$

The following table presents variables symbols and their measurements used by the formula:

TABLE II
MODEL VARIABLES

Variable	***Symbol***	***Measurement***
Mean of group one	$\acute{y}_1$	$\Sigma y_1/n$
Mean of group two	$\acute{y}_2$	$\Sigma y_2/n$
Sum of difference square	d^2	*dxd*
Number of sample	*n*	*Total Number of Sample Banks*

Source: Lucey (2000)

The Decision rule for Paired Sample T-test is, the computed value of t is compared with the critical value at 0.05 level of significance, if the computed value is greater than the critical value, the null hypothesis is rejected and the alternative hypothesis is accepted and vice-versa.

Simple Percentage is the comparison of the respondent that responded for or against a particular question in relation to the overall respondents expressed as a percentage in order to see the pattern of response. It is calculated using the formula below.

[(Number of response ÷ Number of expected response) × 100]

Chi-Square Method is frequently used in testing a hypothesis concerning the difference between a set of observed frequencies of a sample and corresponding set of expected or theoretical frequencies. It is computed as follows:

$$\chi^2 = \sum (f_o-f_e)^2 \div f_e$$

Where:
χ^2 = Chi- Square
f_o = Observed Frequency
f_e = Expected Frequency

The Expected Frequency is calculated thus:

$$F_E = [\text{ROW TOTAL} \times \text{COLUMN TOTAL}] \div \text{GRANT TOTAL}$$

The Decision rule for Chi-Square test is the computed value of χ2 is compared with the critical value at 0.05 level of significance, if the computed value is greater than the critical value, the null hypothesis is rejected and the alternative hypothesis is accepted and vice-versa. Instead of computing the result manually, Microsoft Excel is used.

IV. DATA PRESENTATION AND ANALYSIS

As earlier stated, the study used Paired Sample T-test, Simple percentage and Chi-square Test to determine the effect of banking reform on the intermediation of banks in Nigeria. The following tables III and IV present respectively the profile

analysis of the variables that are used in determining intermediation of Nigerian banks and the T-test result.

TABLE III
PROFILE ANALYSIS

Pre-Consolidation			***Post-Consolidation***		
Year	**Variable**	**percentage**	**Year**	**Variable**	**percentage**
1999	4.0189	21.14	2006	2.0758	7.75
2000	4.1650	21.91	2007	3.1543	11.77
2001	3.8728	20.37	2008	3.7933	14.15
2002	4.4573	23.45	2009	4.0209	15.01
2003	3.2883	17.30	2010	4.2621	15.91
2004	1.7068	8.98	2011	4.5605	17.02
2005	1.5194	7.99	2012	4.9253	18.38
Total	19.0096		Total	26.792	

Source: Computed from Various Annual Reports

Table III indicates that from the year 1999 to 2005, that is, the pre-banking period, the year with the highest percentage in terms of the quantum of intermediation was the year 2002 with a percentage figure of 23.45. This is followed by the year 2000 with a figure of 21.91, and the year with the least percentage figure in the pre-banking period was the year 2005 with a figure of 7.99. As from the reform announcement period to the post-reform period, the year with the highest intermediation percentage was the year 2012, with the percentage figure of 18.38. It is then followed by the year 2011, with a figure of 17.02. The period with the least figure after the reform announcement was the year 2006, with the least figure of 7.75. Generally, in the post-banking reform periods, the percentage of the intermediation figures from one year to another has been increasing.

The following Table presents T-test results of DMBs. The mean and standard deviation of pre and post consolidation periods are computed in order to capture an opinion about the general relationships and differences between pre and post consolidation era. The Table shows the means and standard deviations of the variable for pre and post consolidation periods with t statistics. The variable is in the form of financial ratio that presents intermediation function discharge by the banks.

TABLE IV
T-TEST RESULTS

		Pre-Consolidation		*Post-Consolidation*			
Variable	N	Mean	Std. Dev.	Mean	Std. Dev.	t Value	p Value
INT	7	3.2897	1.2001	3.827 1	0.956 6	-.713	0.502

Source: Microsoft Excel Results

The T-test results indicate that the variables appear statistically insignificant. This debunks the argument put forward in the literature that with banking reform, stronger banks with opportunity for greater financial intermediation emerges (Bello, 2005).

As for the perception of banks' management as regard whether the reform could have any significant effect on the volume of intermediation by banks operating in the sector, the following Table presents the respondents' response on the issue. On the overall 111 questionnaires were administered to the management of the selected banks based on the proportion of their staff, out of which 95 representing 86 percent were successfully completed and returned, and hence the analysis is based on the returned figure.

TABLE V
BANKING REFORM VERSUS BANKS' INTERMEDIATION: MANAGEMENTS' PERCEPTION

Possible Options	**Scores from Respondents**	**Percentage of Scores to Total Respondents**	**Ranking**
Strongly Agree	5	5.26	4th
Agree	22	23.16	2nd
Un-decided	10	10.53	4th
Disagree	38	40.00	1st
Strongly Disagree	20	21.05	3rd
Total	95	100	

Source: Questionnaire Administered

From Table V above, 38 respondents representing 40.00 percent disagree with the view that the banking reform could have any significant effect on the volume of intermediation by banks. The second option in terms of ranking has to do with those respondents that agree that the reform could have effect on intermediation. The third, fourth and fifth options in terms of ranking are strongly disagree, un-decided and strongly agree and they are having percentages of 21.05, 10.53, and 5.26 respectively.

The options agree and strongly agree have to do with the response of the respondents that support the argument that banking reform affects intermediation. Their opinion is in line with literature argument put forward by Bello (2005).

The un-decided option has to do with those respondents that cannot vividly establish the effect of the reform on the intermediation. Their opinion seems to tally with the study conducted by Victor (2007) in which due to numerous factors affecting the banking sector doubt exits as regard effectiveness and efficiency improvement due to emergence of new reform.

The options disagree and strongly disagree have to do with the respondents that are supporting the irrelevancy of the reform in catalyzing and boosting intermediation. The opinion of the respondents as regards this situation contradicts Bello (2005).

In an effort to ascertain the perception of banks' management as regard whether they perceive the current banking reform to have any significant impact on banks intermediation, the respondents' opinions in Table 5 are broken down into various components that made up the Table and then subjected to chi-square test.

TABLE VI
BANKING REFORM VERSUS BANKS' INTERMEDIATION: MANAGEMENTS' PERCEPTION BREAKDOWN

Banks	Accs	Afri	Diad	First	First In	Guar	Sterl	Union	UBA	Wema	Total
SA	0	0	0	1	1	0	0	1	2	0	5
A	1	1	2	5	3	4	1	2	2	1	22
UND	1	0	1	2	1	1	1	1	2	0	10
DA	2	1	5	4	6	3	7	6	3	1	38
SDA	1	1	2	4	3	3	3	2	1	0	20
Total	5	3	10	16	14	11	12	12	10	2	95

Source: Questionnaire Administered

On subjecting Table VI to the Chi square test, the results of the analysis reveal the computed chi-square value of 17.41, a degree of freedom (df) of 36, and a p-value of 0.9962, which appears not significant at all. The full results are contained in Appendix I. The implication of this finding is that contrary to the expectations of the regulatory authority that coming up with a banking reform that substantially increase capital base can lead to more intermediation within the banking sector is debunked. This by extension means that there are other underlying factors that are more crucial than mere capital base increment. This seems to tally with the study conducted by Ezirim and Muoghalu (2002) in which legal and regulatory environment are considered as part of influential variables in determining intermediation.

V. CONCLUSION AND RECOMMENDATION

Based on the data analysis and hypothesis testing, the results of the study provide evidence for the failure to reject the two null hypotheses formulated. The study therefore concludes that the recent 2004 banking reform has no significant effect on the quantum of intermediation carried out by banks as the ratio appears statistically insignificant. The perception of the respondents also indicates that the reform has no effect on the intermediation function of banks. Hence, the study recommends that both the regulatory authorities and the managements of banks should strive hard to ensure that they create enabling environment for banks' smooth transactions. The authorities should also ensure that effective supervision and monitoring are imposed in the banking sector in order to ensure conformity to statutory and regulatory rules. Awareness of the relevancy of transacting with banks should be created and reasonable interest rate should be charged by banks.

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