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THE IMPACT OF FINANCIAL INTERMEDIATION ON GROWTH AND DEVELOPMENT IN NIGERIA: AN OVERVIEW OF THE BANKING SECTOR

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Abstract
The study titled the impact of financial intermediation on growth and development in Nigeria: an over view of the banking sector' is designed to find out whether banks through their financial intermediation activities cause economic growth and development in Nigeria. From the result of the Regression Analysis tested, it is deduced that, from 1993-2013 the intermediation activities of banks were slightly contributing to the growth and development in the economy. This is therefore an indication of the presence of more influential economic growth factors, which the study conjectured to include such as social infrastructure, roads, power supply, economic and political stability. In the light of the above it is suggested that the governments should pay attention to infrastructural development. Considering the fact that a lot of deposit were mobilized by banks and the regulatory authorities may begin to show a little more than passing interest in what banks use these deposits for. The channeling of these deposits to the productive sector may bring desired results in due cause. The study also recommends that the monetary authorities should design a regulatory frame work which will enable the financial institutions to channel their resources to the most viable sector of the economy and ensure proper control and regulate the activities of financial intermediation in order to achieve a sound financial system in the country.

Keywords: *Financial Intermediation, Real Sector Growth in Nigeria, Development*

Background to the Study

Financial systems have long been recognized to play an important role in economic growth and development. This recognition dates back to the era of Goldsmith (1955), Cameron (1967), McKinnon (1973) and Shaw (1973), they demonstrated that the financial sector could be a catalyst of economic growth if it is developed effectively. The benefits generated from a sound and developed financial system relate to savings mobilization and efficient financial intermediation roles (Gibson & Tsakalotos, 1994). Similarly, the attainment of a steady, viable and speedy economic growth and development in any nation is essentially a function of the availability of financial assets in the economy. Sanusi (2002), was of the opinion that, the availability of investable funds is a key factor in the growth process of any economy. Although not a sufficient condition, resource availability is certainly a necessary condition for output and employment growth. Indeed, there is enough evidence to show that countries that have enjoyed or are enjoying economic prosperity have been linked with an efficient mechanism for mobilizing financial resources and allocating same for productive investment.

On the other hand, an efficiently managed financial intermediation process contributes immensely to a vibrant financial system, higher levels of output, employment, and income and through that enhance economic growth and development. In general, Finance affects economic growth and development, stagnation or even decline in any economic system. Kasekende (2008), argued that, literature in finance provides a supporting argument in respect of countries with better or efficient financial systems grow faster while inefficient financial systems bear the risk of bank failure.

The concept of financial intermediation is not relatively new. For decades, it has been a subject of academic study at both micro and macro level. Considering the macro level, the importance of financial intermediation cannot be over emphasized. However, there are mixed argument about that. Some argued that it facilitate the efficiency of the financial system (Gromb and Vayanos; 2010), and also in (Subrahmanyam; 2008), while others were of the view that it is passive in nature and serves as a conduit pipe through which monetary policy is effected as indicated in the work of (Benstom and Smith; 1975). At the micro level, Araujo and Minetti (2007), express that financial intermediation stimulates the restructuring and liquidation of distressed firms as well as eliminating the inefficiencies associated with the absence of inter temporal smoothing. Recently, the impact of financial intermediation on the growth and development of an economy generated a heated debate. Some studies observed that financial intermediation drives economic growth as stated by (Odedokun;1998), (Nieh, et al; 2009), (Islam and Osman; 2011), While others have argued that economic growth drives financial intermediation. However, Odhiambo (2011), argued that a bi-directional causality exists between financial intermediation and economic growth. Thus, this study seeks to contribute to the body of literature by examining the impact of financial intermediation on growth and development in Nigeria with an emphasis on the banking industry.

Statement of the Problem

There seems to be a consensus in theoretical and empirical literatures that financial development can influence and foster output development, that there is a visible correlation between financial intermediation and economic growth, economic growth being synonymous to Output or GDP growth and that financial intermediation facilitates the efficiency of the financial system of any nation. These core economic facts which appear to be eluding the Nigerian situation because the Nigerian banking industry in recent times has undergone series of financial turbulence and capital adequacy problems, the consequences of which appeared to cast doubts on the role of financial intermediation on the economy.

Similarly, the Nigerian financial sector, like those of many other less developed countries, was highly regulated leading to financial disintermediation which retarded the growth and development of the economy. The link between the banking sector and the growth of the economy has been weak. The real sector of the economy, most especially the high priority sectors which are also said to be economic growth drivers are not effectively and efficiently serviced by the banking sector. The banks are declaring billions of naira profit but yet the real sector continues to be weak thereby reducing the productivity level of the economy and hence affecting the GDP. Most of the operators in the productive sector are folding up due to the inability to get loan from the financial institutions or the cost of borrowing was too outrageous. The Nigerian banks have concentrated on short term lending as against the long term investment which should have formed the bedrock of a virile economic transformation. From the foregoing, this paper seeks to analyze the impact of financial Intermediation on growth or Output (GDP) in Nigeria. In doing so, the study used the endogenous components of financial intermediation such as aggregate short term, medium term and long term Credits as explanatory variables to predict the outcome of our dependent variable which is Output (GDP).

Objectives of the Study

The objectives of this study are to empirically investigate;

1. The impact of financial intermediation on growth and development in Nigeria with emphasis on the banking sector.

2. And to determine the long run relationship between financial intermediation and economic growth and development in Nigeria.

Research Questions

In this study, the following research questions are very important in the realization of the above mentioned objectives;

1. Is there long run relationship between financial intermediation and economic growth and development in Nigeria?

2. What is the impact of financial intermediation on economic growth and development in Nigeria?

Hypothesis of the Study

The study will be guided by the following statement of hypotheses formulated based on the objectives of the study:

Hypothesis I

H_0: There is no positive and significant impact of financial intermediation on economic growth and development in Nigeria.

H_1: There is positive and significant impact of financial intermediation on economic growth and development in Nigeria.

Assumptions of the above Hypothesis are

i. Over the periods of this research, it is assumed that all Governmental expenditure that are injected into the economy are held constant.
ii. The activities of other financial institution in the economy are also held constant
iii. There is a uniform monetary policies over the period the research.

Scope of the Study

The study titled the impact of financial intermediation on growth and development in Nigeria: an over view of the banking sector is designed to achieve the above stated objectives. Variables such as bank credit (short, medium and long term)as well as aggregate GDP are used. The study will focus on Nigerian economy and will cover the period from 1993 to 2013.

Review of Related Literature

Financial Intermediation

The Concept of Financial Intermediation can be trace down to the history of human societies, since the evolution of money, the societies were divided into two that is those who possess money in excess of their immediate needs (surplus economic unit) and those whose current possessions cannot finance their economic activities (deficit economic unit). The realization by the surplus economic unit, that their excess can be used beneficially to meet the shortfall experienced by the deficit economic unit led to the introduction of a credit system. This system was initially characterized by lenders (surplus unit) and borrowers (deficit unit) having to search out themselves and deal directly, a process known as direct financing (Akpan, 2009; Akpanuko and Acha, 2010).

Chinweoke etal,(2014) historically state that, In the primitive stage, before evolution of financial intermediation, anyone who needs to spend more than he could himself provide would have to look for a wealthy person or persons from whom he could borrow. This is known as a system of direct or intermediated finance. While Afolabi (1998), state that as crude as this system was, it probably satisfied the need of that time because financial requirements then were limited to personal uses such as marriages, burial ceremonies and minor commercial activities like farming. He further argued that, intermediation was neither necessary nor sufficient for capital formation to take place. Financial intermediation will thus, not be necessary for instance, if the lender and the borrower can

come into direct contact and would in fact not be necessary if there is no deficit or surplus sector. However, modern economic transactions will be difficult, if not impossible, with un- intermediated finance as the business world nowadays is much more complex and financial requirements are too large. Even without considering the complexity of modern times, un-intermediated finance has its inherent problems such as high tendency for subjectivity, unattractive interest rates, method of security was too crude and at times inhuman, repayment periods were usually too short for any meaningful long-term use, such that it became difficult for long-term projects to be financed from money raised from such medium amongst others.

Bencivenga and Smith (1991), highlighted in the work of Chinweoke etal,(2014), argued that, in the absence of banks i.e. financial intermediation, too much investment is self-financed and long delays exist between investment expenditure and receipts of profits from capital invested. They further argued that the absence of intermediary sector results in a composition of savings that is unfavorable to capital formation. Thus, an intermediation industry permits an economy to reduce the fraction of the savings held in the form of unproductive liquid assets, and to prevent misallocations of invested capital due to liquidity needs. The argument further suggests that, financial intermediaries may naturally tend to alter the composition of savings in a way that is favorable to capital accumulation. Then, if the composition of savings affects real growth rates, intermediaries will tend to promote growth and development. Here, the analysis draws heavily on the contributions of the "endogenous growth" literature, as exemplified by Romer (1986) and Lucas (1988). One of the many insights of this literature is that savings behaviour will generally influence equilibrium growth rates. In particular, to the extent that intermediaries tend to promote capital investment, they will also tend to raise rates of growth.

Requirements of Financial Intermediation

Afolabi (1998) was of the opinion that, for financial intermediation to succeed, three qualities are essential. They are usually called the three C's of intermediation namely: cost, convenience and confidence. Costs refer to the transaction cost that the saver or borrower is made to bear in the process of his dealing with the intermediary. Thus, costs like bank charges, commission and interest payable must be considerably low. For instance, the local money lenders most times charge very exorbitant interest, hence only hard pressed people, who are not likely to be credit-worthy to the bank, do patronize them. If there is appreciable cost of transacting business with an intermediary, many people will prefer to by-pass them. While Convenience on its own has to do with the ease with which people transact business with the intermediary and this will include the formalities involved. Thus, simplicity of operation must be ensured such that it does not require specialist knowledge or certain level of education to deal with an intermediary. There are some costs that have to do with convenience. If, for example, the intermediary is too far away, the customer will have to incur additional transport costs and inconvenience each time he wants to transact business, though the online banking has gone far in reducing this problem. It is therefore imperative that intermediation facilities be very near to the people for effective fund mobilization like rural banking schemes as

the microfinance banks are not only socially desirable but an economic necessity to minimize the volume of funds in the otherwise "unbanked" areas.

On the other hand Confidence is another important requirement of financial intermediation. Ujah (2010), argued that, people must have confidence in the financial intermediary. As a saver, you must have the confidence that your money will be repaid to you as per the terms of the account you saved. That is, if you operate a current account, your money must be made available to you on demand and if you maintain a term deposit account, you must be able to withdraw on the expiration of the term or an expiration of the notice, if notice of withdrawal is required like in call deposit account and so on. Perhaps, confidence is the most pillar upon which financial intermediation rotates. It is therefore important that in an attempt to use financial intermediaries as vehicles for mobilizing savings, a failure-proof system must be designed and sustained (Afolabi, 1998). If a bank fails, it is not only the customers of the bank that will suffer, the economy as a whole will be affected because a dangerous signal, which may affect people's confidence in the financial system generally, has been sent.

Uche (2001), Show how bank failure create a contagious effect on the economy. He further state that, history indicate that, the indigenous banks in Nigeria had problems of confidence in the 1940's because of the failure of many of them in the previous decade. Again, the failure of most finance houses and some banks in the mid-1990s affected the confidence of depositors. Thus, Cost, Convenience and Confidence are not only related to depositors but they are also in relation to borrowers.

Empirical Views of Schumpeter on Financial Intermediation and Growth

Schumpeter made the first articulated statement about how financial transactions take central stage in economic growth. He did not use the modern parlance of financial transactions but he used the banker as an example. Instead of using the term economic growth, he used the term development. Thus, he wrote, "The banker stands between those who wish to form new combinations and the possessors of productive means. He is essentially a phenomenon of development, though only when no central authority directs the social process. He makes possible the carrying out of new combinations, authorizes people, in the name of the society as it were, to form them. He is the ephor of the exchange economy." (Schumpeter, 1934, p. 78) Only in the last decade, Schumpeter's view about the nexus between banking (and finance) and economic development (and growth) is being taken seriously. Schumpeter sharpened his view in later writing. While discussing business cycles, he wrote, "the relation between credit creation by banks and innovation is fundamental to the understanding of the capitalist engine." (Schumpeter, 1939, p. 111)

On the other hand, Becsi and Wang (1997) compare the relationship between finance and economic growth in the context of modern growth theory. "Financial intermediation increases the efficiency of investment by identifying and channeling resources toward high-return projects and by disciplining corporations. While innovation and knowledge creation are the ultimate forces behind broad capital accumulation and growth, financial

intermediation will enhance growth to the extent that the intermediaries perform their functions efficiently. Thus, countries' growth performance should vary with their level of financial efficiency. Financial efficiency in turn depends importantly on the extent to which financial economies of scale have been realized and on how developed and innovative the financial sector is. Financial development can be measured by the size of the financial sector to the extent that activities transform the quality of investments. Also, as the growth model with financial intermediation illustrated, financial development and efficiency are reflected in lower loan-deposit rate spreads. The growth model also predicts that growth rates are positively correlated with real interest rates and negatively correlated with loan spreads. In addition, it has been shown that government intervention can severely affect the efficiency of financial intermediaries and economic growth and alter these correlations." (p. 56- 57).Similarly, modern applications try to capture one or many aspects of these connections between finance and economic growth.

An Overview of the Nigerian Financial System

A financial system consists of different institutions, markets, instruments, and operators that interact within an economy to provide financial services such as resource mobilization and allocation, financial intermediation and facilitation of foreign exchange transactions. The Nigerian financial sector can be categorized into two namely;

1. The informal sector which comprises of the local money lenders, the thrifts and savings associations, etc. It is poorly developed, limited in reach, and not integrated into the formal financial system, but plays a major role in the Nigerian financial system.

2. The formal financial system comprises of the capital and money market institutions and these comprise of the banks and non-banks financial institutions. According to the CBN Annual Report and Statement of Account (2008), the Nigerian financial system consists of the Central Bank of Nigeria (CBN), the Nigerian Deposit insurance Corporation (NDIC), the Securities and Exchange Commission (SEC), the National Insurance Commission (NAICOM), the National Pension Commission (NPC), deposit money banks, microfinance banks, finance companies, bureaux-de-change, stock exchange, commodity exchange, primary mortgage institutions, development finance institutions, discount houses and insurance companies and registered insurance brokers.

According to Gbosi (2005) the deposit money banks (DMBS) emerged following the adoption of the universal banking system in 2000 and the removal of the dichotomy between commercial and merchant banks. A universal bank performed the most important role of financial intermediation in the Nigerian economy. In particular, they had undertaken the following activities Andabai (2010). (i) The business of receiving deposits on current saving or other account's, (ii) paying or collecting cheques drawn or paid by customers, (iii) Provision of financial consultancy and advisory services, (iv)making or management investment on behalf of any person and (v) the provision of insurance market services as could be required by the regulating authorities. Jerome

(2000) contributed that, these services are to be provided after the bank must have complied with the statutory requirement for providing such services. Deposit money banks are in the process of providing loans and advance to their customers.

Aderibigbe (2004) in ogiriki (2014) observed that, the ability of banks to create money is however, limited by statutory reserve requirements of the central Bank. Generally, activities of the deposit money banks impact on the soundness and stability of the financial system hence the special attention accorded them by the regulatory authorities (Umoh, 2005). Andabai (2010) in Ogiriki (2014), posits that, the achievement of financial sector stability is fundamental to the maintenance of macro economic stability is sine-qua-non for sustainable growth and development and they go hand in hand to promote economy growth. Onyido (2004) concluded that, regulating authorities should create favourable financial environment in order to sustain economic growth and development in the country.

Nzotta (2004)argued that, the banking sector is the dominant sector in the Nigeria financial service industry, he also described it as the most vibrant component and whatever difficulties it passes through affects the entire economy greatly. In July, 2004, the CBN launched a 13-point agenda aimed at creating bigger banks with stronger balance sheets, ensuring safe and sound banking practice and enhancing regulatory capacity to supervise the industry. According to Soludu (2004), the key element of the reform program was the increase in minimum capital base of banks from N2 billion to N25 billion by December, 2005 the reform program was driven by the following factor; (i) Nigeria banks were small, depended on government or public sector deposits and unable to meet the economy's funding needs. (ii) Banking penetration was low and retail offering were limited. For example deposits in the hands of small business and individuals was 80% of the total currency in circulation, (iii) the narrow scale and scope of services provided by Nigeria banks led to loss of business to foreign banks, (iv) the industry was fragmented and many banks operated as fringes player, (v) corporate government was poor and insider abuse and sharp practices by directors and other related parties were rampant, and (vi) there was a dividing level of confidence in the banking system.

Similarly, Nnanna (2004) concluded that, the banking reforms by the CBN were therefore intended to address these issues and specifically strengthen the Nigerian banking system, with vision to ultimately make Nigeria the financial hub of African and to stem the systematic distress that have played the system, practically reposition Nigerian Banks to compete favourably with foreign banks, encourage consolidation through mergers and acquisition, enhance professionalism in the conduct of banking business, and make the banking system safers and engender depositors confidence. The banking system has been one of the channels through which government carries out its policy of stabilizing the economy and controlling inflation through the manipulation of some key variable such as interest rate and the quantum of credit, government is able to influence borrowing spending within the economy. These in turn affects employment, produce and price.

Methodology

Research Design

Amaechi and Amara (2005), were of the view that, research design is a blueprint which guides the researcher in his scientific inquiry, investigation and analysis. Research design is a plan and a strategy designed for systematically solving research problems of interest to the researcher within his relevant circumstances (Osuala, 1991). In this study, ex post facto design shall be adopted in obtaining, analyzing and interpreting data relating to the objectives of the study. The choice of this type of design will allow the researcher the privilege of observing variables over a long period of time. For this reason, both the dependent and independent variables will be observed over the period, 1993 to 2013. Data collected will be analyzed and the hypothesis of this study will be tested using the multiple regression technique to determine the impact of the independent variables aggregate that is short term, medium term and aggregate long term credits on the dependent variable which is the percentage of Gross Domestic Product (GDP) at current market price and it serve as a proxy for economic growth and development.

Population and Sample Size Population

According to Onwumere (2009), Population represents a universe or elements with similar characteristics, hence it is a census of all relevant elements and may be finite or infinite while a sample is a group of variables or items derived from a relevant population for the purpose of examination or analysis. Based on this, the population of this study will comprise of all financial intermediaries in Nigeria such as banking sector, because they involved in financial intermediation in one form or the other. Sequel to the fact that there may be obvious difficulties in studying the entire population due to the pattern and size of distribution, sufficient knowledge of the entire population will be gotten from studying a sample of the population. The sample of this study shall be the commercial banks only. The choice of these banks is based on the fact that they are the dominant institution of financial intermediation in Nigeria which encouraged, mobilize savings and channel them into productive investments due to their network of branches and also based on the availability of data.

Nature and Sources of Data

The source of data for this work is secondary in nature. Such data were obtained from published materials such as the Central Bank of Nigeria Statistical bulletins and publications of the Federal Office of Statistics (Bureau of Statistics).

Model Specification

The study was based on two hypothesis which the null hypotheses statethat, there is no positive and significant impact of financial intermediation on economic growth and development in Nigeria. While the alternative hypothesis state that, there isno positive and significant impact of financial intermediation on economic growth and development in Nigeria. The study also adopted the following model where GDP= f (ASC, AMC, ALC) Which can be simplified as $Y = b_0 + b_1 X_1 + b_2 X_2 + b_3 X_3$ where Y= GDP at current market price, Xi=ASC, X2=AMC AND X3=ALC

Analysis of Results and Discussion of Findings

Table I

Based the hypothesis it has shown that the relationship between financial intermediation and economic growth in Nigeria indicated 0.574 relationship at margin with a coefficient of determination of (0.329 x 100) that is 32.9% percent contribution of financial intermediation Variables (ASC, AMC & ALC) on economic growth and development in Nigeria leaving about 67.1% percent un explained as a result of other factors. Thus, we accept the null hypothesis which said there is no positive and significant impact of financial intermediation on economic growth and development in Nigeria.

Table1 Model Summary(b)

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
	R Square Change	F Change	df1	df2	Sig. F Change	R Square Change	F Change	df1	df2
1	.574(a)	.329	.211	2.17528	.329	2.783	3	17	.073

a Predictors: (Constant), ALC, ASC, AMC

b Dependent Variable: GDP

Table 2

The ANOVA table indicates that the P-value (0.073)> ? = (0.05) signifying that the model is insignificant and cannot be used to forecast economic growth in Nigeria.

Table 2 ANOVA(b)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	39.501	3	13.167	2.783	.073 a
	Residual	80.442	17	4.732		
	Total	119.943	20			

a Predictors: (Constant),ALC,ASC,AMC

b Dependent Variable: GDP

Table 3

The coefficient table estimates the significant of the parameters as they contribute to the dependent variable GDP. From the table it has shown that only b0 is significant with p-value at (0.00)< or equal to (0.05) with b0 value at 8.554 while the independent variable are all insignificant since the values of the parameters are all above 0.05 which is ? = (0.05). Thus, the model is represented as GDP= 8.554 - 0.228 - 0.238 – 0.076

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Correlations			Collinearity Statistics	
		B	Std. Error	Beta			Zero-order	Partial	Part	Tolerance	VIF
1	(Constant)	8.554	1.548		5.526	.000					
	ASC	-.228	.162	-.280	-1.406	.178	-.248	-.323	-.279	.996	1.004
	AMC	-.238	.165	-.289	-1.439	.168	-.338	-.330	-.286	.975	1.026
	ALC	-.076	.039	-.388	-1.926	.071	-.418	-.423	-.383	.974	1.027

a. Dependent Variable: GDP

Conclusion

The study was able to assess whether banks through their financial intermediation activities cause economic growth and development in Nigeria. From the result of the Regression Analysis test, it is deduced that, from 1993-2013the intermediation activities of banks were slightly contributing to the growth and development in the economy. This therefore is indicative of the presence of more influential economic growth factors, which the study conjectured to include social infrastructure, roads, power supply, economic and political stability. In the light of the above it is suggested that the governments of developing economies should pay attention to infrastructural development. They should ensure improvement in road network, transportation and power supply. They should also pay due attention to economic and political stability. Considering the fact that a lot of deposit is mobilized by banks, the regulatory authorities may begin to show a little more than passing interest in what banks use these deposits for. The channeling of these deposits to the productive sector may bring desired results in due cause.

Recommendations

The study recommends that the monetary authorities should design a regulatory frame work that will enable the financial institutions to channel their resources to the most viable sector of the economy and ensure proper control and regulate the activities of financial intermediation in order to achieve a sound financial system in the country. Again, efforts should be made by authorities to checkmate banks from possessing excess liquidity, idle funds as well as bad debt within the system because it will assist in controlling or preventing of inflation in the economy. Similarly, there is need for the government to develop our financial intermediaries and it should be geared towards greater effectiveness and efficiency in complement the above findings. There is also the need to reinstate the total productivity factor with a view of enhance efficiency in our financial system and channeling investible funds to the real (productive)sectors of the economy. While on the other hand, banks should embarked lower merchandise financing to the detriment of the real sectors of the economy.

Lastly the government should provide an enabling legal environment to handle all matters of financial activities and that will pave way for a more vibrant economic environment and in turn stimulate intermediation thereby, fostering economic growth in Nigeria.

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