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Bank Recapitalization and Economic Prosperity: A Case of Nigeria Banking Industry

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Abstract
The recapitalization of Nigerian banks arose out of the needs of the society, dynamic nature of the economy and sensitive nature of the banking industry. This study was designed to examine bank recapitalization so as to see whether the recapitalization has led to economic prosperity in Nigeria. Secondary data were obtained from the Central Bank of Nigeria Statistical Bulletin during the period 1992-2013 and Ordinary Least Square estimation technique was used in conducting the statistical tests. Using some bank indices (bank total assets and credits) and economic prosperity measure (Gross Domestic Product), the study suggests that bank recapitalization has significantly affected the bank performance and this in turn has led to economic prosperity. The study recommended that there should be some degree of surveillance on the banking industry by the monetary authorities so as to protect the industry from taking advantage of their status to embark on unwholesome act. In addition, urgent action needs to be taken by the recapitalized banks to make efficient use of their assets and the banking industry should lend more to the real sector of the economy such as agriculture, manufacturing sector so that the economy can witness and harness aggregate growth.
Keywords: Bank Recapitalization, Economic Growth, Total Assets, Total Credits

I. Introduction

The recapitalization of Nigerian banks arose out of the needs of the society, dynamic nature of the economy and sensitive nature of the banking industry. Oderinde (2013) observed that any economy of the world cannot survive if its banking sector is characterized by instability. According to Nnanna (2012), the role of the banking sector in developing an economy cannot be overemphasized, the role it plays in developing an economy ranges from financial intermediation, provision of an efficient payment system, serving as conduit for the implementation of monetary policies, enhanced savings and channeling funds in an efficient and effective manner to ensure that viable projects are not frustrated due to lack of funds. Capital is an essential element in the banking sector which enhances the confidence and permits banks to embark on their banking activities. Capital in the banking sector therefore helps in absorbing losses, serves as a buffer between operating losses and insolvency. The more capital a bank has, the more losses it can sustain without going insolvent (Oviemuno, 2010). The ability of the Nigerian banks to efficiently and effectively grapple the above roles has been hampered due to internal and external issues which are peculiar to the Nigerian environment (Olaiton, 2012). Thus, the regulatory instruments in Nigeria banking industry concede the need for recapitalization of the banking industry so as to promoting the soundness, stability and enhanced efficiency of the banking industry. The remaining part of this paper is divided into: prior literature, methodology, analysis and interpretation of results and conclusion and recommendation.

II. Prior Literature

In Nigeria, the financial system is the hub of productive activity, as it performs the vital roles of financial intermediation and effecting good payments system as well as assisting in monetary policy implementation. The process of financial intermediation encompasses mobilization and allocation of financial resources through the financial markets and the use of financial instruments (Olamide, 2011). Unugbor (2014) opined that the efficiency and effectiveness of financial intermediation in any economy depend critically on the level of development of the country's financial system. In effect, the underdeveloped nature of the financial system in most developing countries accounts largely for the relative inefficiency of financial intermediation in those economies. In Nigeria, the financial system is dominated by banks, which are typically oligopolistic in structure and tend to concentrate on short-term lending as against investments with long-term gestation period.

Prior experiences have established the importance of financial sector stability from the perspective of macroeconomic performance. Such experiences illustrate the extent to which unsound and uncompetitive financial systems resulting from inadequate regulatory frameworks can weaken efficient credit allocation, assets, distort the structure of interest rates, disrupt monetary policy signals and impose significant financial costs, with adverse consequences for economic prosperity (Ernest, 2008). There has been a wave of restructuring and consolidation of the banking sector around the globe, particularly in the developed and the emerging market economies. This has been driven mainly by globalization, structural and technological changes, as well as the integration of financial markets (Idolor, 2012). Banking sector consolidation has become prominent in most of the emerging markets, as financial institutions strive to become more competitive and resilient to shocks. It is also promoted by the desire to reposition corporate operations to cope with the challenges of an increasingly globalized banking system. It was based on the above premise that banking sector consolidation, through mergers and acquisitions, was embarked upon in Nigeria from 2004 (Olaiton, 2012).

Following the banking sector consolidation, notable achievements were recorded in the financial sector among which was the emergence of 25 well capitalized banks from the former 89 banks. The banks raised N406.4 billion from the capital market. In addition, the process attracted foreign capital inflow ofUS$652 million and £162,000 pound sterling. The liquidity engendered by the inflow of funds into the banks induced interest rate to fall significantly, while an unprecedented 30.8 per cent increase was recorded in lending to the real sector in 2005. With a higher single obligor limit, Nigerian banks now had a greater potential to finance large value transactions (Adebisi, 2014). More banks now have access to credit from foreign banks, while the capital market deepened and consciousness about it increased significantly among the populace. The market became active and total market capitalization increased markedly. Ownership structure has been positively affected such that the problems of insider abuse and corporate governance have been reduced. Depositor confidence has improved due to―safety in bigness‖ perception by depositors. With virtually all banks now publicly quoted, there is wider regulatory oversight (Olamide, 2011).

With the inclusion of the Securities and Exchange Commission and the Nigerian Stock Exchange in the regulatory team, resources have been committed to the regulation of few and more stable banks in an efficient and effective manner. The banks have begun to enjoy economies of scale and, consequently, are passing on the benefit in the form of reduced cost of banking transactions. In general, the reform efforts had engendered stable macroeconomic environment evidenced by low inflation and relative table exchange rates. However, not long after, the global financial and economic crises came in 2007, leading to the collapse of many financial institutions across the globe. The financial crisis reduced the gains made in the Nigerian financial services sector from the banking sector consolidation exercise. The experience in the industry however, followed global trends. Following from the impact of the global financial crises, a section of the banking industry was badly affected as some banks were in grave condition and faced liquidity problems, owing to their significant exposure to the capital market in the form of margin trading loans, which stood at about N900.0 billion as at end-December 2008 (Unugbor, 2014).

Further investigation by the CBN identified eight interdependent factors as the main origin of the crisis in the banking sector. These include:

- Sudden capital inflows and macro-economic instability
- Poor corporate governance and character failure
- Lack of investor and consumer sophistication
- Inadequate disclosure and lack of transparency
- Critical gaps in regulatory framework and regulation
- Uneven supervision and enforcement
- Weaknesses within the CBN
- Weaknesses in the business environment

In line with the above, the Central Bank of Nigeria initiated the recapitalization programme which led to the increase in the minimum paid-up capital requirement from N600,000 in 1978 to N25,000,000,000. Banks that failed to meet the requirement were made to forfeit their licenses while new banks must fully comply with the condition before they can be granted licenses (Biodun, 2010). According to Ito and Sasaki (2002), apart from boosting the already failing credibility of the Nigerian banking industry, the introduction of the minimum capital base was to ensure some other functions which include:

a) Provision of fixed assets of banks i.e. provides funds for furniture, building, operational tools, and vehicles for banks.
b) It serves to conform to the requirements of the supervisory authorities of the Central Monetary Authority.
c) It serves to provide cushion to absorb possible losses so that depositors will be fully protected at all times.
d) It serves to assure the public, including business enterprises and other banks of its solvency and to continue to serve the community even under conditions that cause losses on loans and sales of investment at a loss.
e) Where liquidation becomes unavoidable, bank capital is still important, because it helps to reduce the losses which depositors and other creditors would otherwise bear fully.
f) Bank capital also provides some regulatory functions. A bank inspires confidence in depositors and the regulatory authorities if it successfully obtain a banking license of which a paid-up minimum capital is one of the most important pre-requisite, like under the Nigeria Banking Decree.

Bank recapitalization has come to be recognized and accepted as an important element for a strong, stable and successful banking business in Nigeria.

III. Methodology

This study was designed to examine bank recapitalization so as to see whether the recapitalization has led to economic prosperity in Nigeria. Secondary data were obtained from the Central Bank of Nigeria Statistical Bulletin during the period 1992-2013 and Ordinary Least Square estimation technique was used in conducting the statistical tests. Using some bank indices (bank total assets and credits) and economic prosperity measure (Gross Domestic Product) a linear model was specified. The linear model was estimated in a functional form as below:

$$RECAP = F(BTA, BTC, GDP) \qquad eq.\ 1$$

The above function can be written in a linear econometric form as:

$$RECAP = b_0 + b_1BTA + b_2BTC + b_3GDP + U_t \qquad eq.\ 1$$

Where:

RECAP = Recapitalization of Banks (proxied my minimum capital base of banks)
BTA = Bank Total Assets
BTC = Bank Total Credits
GDP = Gross Domestic Products
U_t = Error Term
$b_0b_1b_2b_3$ = Regression Coefficients

The a-priori expectation shows the relationship which exist between the explanatory variable (independent and dependent variables). The a-priori expectation is thus b_1, b_2, $b_3 > 0$.

IV. Analysis and Interpretation of Results

The results obtained from the Ordinary Least Square (OLS) estimation were analyzed below:

Variables	Coefficients	Mean	Std. Dev.	F-ratio	t-ratio	Dw
BTA	-20.81666	425371.0	9379.223	276.8	2.3606	2.0201
BTC	-0.76044	456351.0	4783.391			
GDP	-1.6536	642231.0	8390.852			

$R^2 = 0.99105$; R^2 adjusted = 0.98147;

An estimation of the regression results showed that 99% of the systematic variation in the dependent variable (RECAP) has been explained by the independent variables (Bank Total Assets BTA; Bank Total Credits BTC; and Gross Domestic Product GDP), leaving just 1% to be handled by the error term. This was further supported by the R^2 adjusted which is the coefficient of determination after adjusting for the degree of freedom. The explanatory variation in the dependent variable which was indicated by the R^2 adjusted value of 0.98147 suggests that 98% of the systematic variation in the dependent has been explained by the independent variables. This shows that the model is a good fit. The examination of the individual significance of the slope coefficient revealed that the coefficient of BTC, BTA and GDP were statistically significant at 5% level of significance. These were indicated by the t-ratio. The observed t-value level of 2.3606 is greater than the theoretical t-value of 2.1448 at 5% level of significance. The result thus suggests that bank recapitalization has significantly affected bank performance and this in turn has led to economic prosperity in Nigeria. The Durbin Watson (Dw) suggest that the model is free from the problem of correlation.

V. Conclusion/Recommendation

The study has made tremendous attempt in appraising bank recapitalization and economic prosperity using Nigerian data. Using the Ordinary Least Square estimation technique, the study found out that the recapitalization of the banking sector has indeed impacted significantly on bank performance and has led to economic prosperity. Total asset and credit of bank has a negative value which is attributed to the fact that the assets and credits of bank had not been properly deployed for efficient service delivery and profitability. It is expected that with proper deployment of the assets of the banks and increase in banks' lending rate to the real sector of the economy, the effect of the recapitalization exercise will be much more felt in the country's economy. We recommend surveillance of the banking industry by the monetary authorities so as to protect the industry from taking advantage of their status to embark on unwholesome act. In addition, urgent action needs to be taken by the recapitalized banks to make efficient use of their assets and the banking industry should lend more to the real sector so that the economy can witness and harness aggregate prosperity.

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