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The Impact of Deregulation of the Economy on Nigerian Commercial Banks;
A Case Study of Some Selected Commercial Banks in Ilesa, Osun State

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ABSTRACT

The study looks at the impact of deregulation of the economy on Nigerian commercial banks; A case study of some selected commercial banks in Ilesa, Osun State. The economy policies pursued prior to 1985 made the Nigeria economy price distortions created by a highly over-valued currency and inappropriate pricing of agricultural and other local products. The control measure introduced prior to deregulation of the economy were unable to improve the economy positively. Instead, that period was characterized by short-supply of industrial inputs, plant closure, large retrenchment of workers, and shortage of goods and price inflation coupled with unfavourable balance of payment. Data were gathered from some selected commercial banks in Ilesa, Osun State Nigeria through issuing of questionnaires and from some secondary sources such as CBN statistical bulletin, Publications and other relevant materials. The major deregulation policies were deregulation of interest rates structure, introduction of second tier foreign exchange market. Since the Federal Government is contemplating deregulation as the only paramount solution to distorted economic structure. The study therefore recommends that banking industry [commercial banks] needs to reposition itself to take full advantage of the gains which might arise from such deregulation. Commercial banks should equally anticipate and sensitize themselves with the challenges of a deregulated economy.

Keywords: *Deregulation, Commercial Banks, Nigeria*

1. INTRODUCTION

The economy of Nigeria had a lot of structural distortions in the 1980's. The economy policies pursued prior to 1985 made the economy of Nigeria vulnerable to external shocks. Consequently the 1986 budget sought to de-emphasize controls and adopted policy aimed at expanding the economy resources base. To attain this goal in 1986 budget at a time in the structural adjustment program which was launched in July 1980 with the introduction of structural adjustment program came to deregulation of the Nigerian economy.

The deregulation policy which the structural adjustment called for is the process by which government removes unnecessary control which tends to inhabit or prevent the effective and efficient program of economic and business activities. It can also be said to be reduction or elimination of laws and regulations that hinder free competition in supply of goods and services, thus allowing market forces to drive the economy.

Deregulation to the economy will bring about a raised level of competitiveness, therefore higher productivity, more efficiency and lower price of overall goods and services. Deregulation policy was designed to restructure and diversify the productivity of the economy in order to reduce dependency on the oil sector and also to achieve fiscal and balance of payment viability. In addition is to lay basis for sustainable non-inflationary or minimal inflationary growth rate.

Finally, is to reduce or lessen the dominance of unproductive investment in the economy, improve the sectors efficiency and intensify the growth potential of the private sector. Besides these listed aims, the banking sector which is a major instrument through which government execute their policies need to appropriately reposition itself to take full advantage of the gains that might arise from deregulation as well as face the challenges.

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1.1 Statement of the Problem

As a result of the underdeveloped nature of Nigerian banking system, it is sometimes said that banks have not met the standard expected from them in the process of economic development especially with the introduction of deregulation policy. There are many problems the economy faced as a result of the introduction of deregulation and the commercial banks are not excluded. One major problem is that commercial banks lack ability to cope with the high demand for bank loans with lending rate. Also, the level of expertise in investment banking and corporate finance is very low given the newly advocated banking policy called universal banking coupled with lack of ability to effectively manage risk

The reluctant competition between commercial banks as a result of the deregulatory policy and the possibility of bank failure which prompted the Federal Government to establish the Nigeria Deposit Insurance Corporation. The purpose of this study is to examine the performance of commercial banks under a deregulated economy with a view of assessing the effect, challenges and benefits as well as achievement such deregulation will pose on commercial banks.

From the above argument, the main objective is to critically identify and analyze the impact of government deregulation of the economy on commercial banks with the aim of making useful recommendations on how to improve commercial banks performance.

Again, emphasis will also be made on the current banking practices and habit as means of bathing with the challenges and the treats deregulation has brought with it. In addition is to identify the various achievements made with the inception of the policy as to examine how effective commercial banks have been since the inception of the policy.

Finally, this study will try to compare the activities of commercial banks under the system of regulation and deregulation in order to know if the aim objective of the policy is being achieved or not. Recommendation that will enhance the efficiency of banks operations will equally be made.

1.2 Significance of the Study

This study is significant on two counts. First, with the recent monetary policy measures, the central bank has been issuing series of policies through which she tries to stabilize price in the country. The central bank of Nigeria which came to operation since 1959, has introduced monetary measures for the achievement of the national economic objectives which range from the maintenance of a healthy balance of payment control or moderation of inflation through the acceleration of the peace of the economic development to the stabilization of the exchange rate of naira with foreign currencies.

In essence, the regulations and deregulation in the banking sector/industry have favoured some while other banks could not stand the weird of constant change in the monetary and banking policies. However, deregulation has it merits and demerits. The merit include the removal of inhabiting controls on economic activities, encouragement on investment and assurance of efficient allocation of resources.

Second, it is understood that deregulation of the economy will definitely pose some challenges to the banking industry. However the ability to cope with the challenges which will come in the forms of competitive lending rate, effective management of credit risk, level of expertise in investment banking and cooperate finance activities will be the important determinant of success for banks.

2. LITERATURE REVIEW

2.1 Empirical Framework

Deregulation of the economy comes in as a result of depression. Depression is said to be a period when there is severe and prolonged down turn in the economy, prices fall, reducing purchasing power. It also resulted into high unemployment, lower productivity, shrinking wages and general economic pessimision. In essence financial depression according to Oriji (1987), refers to the distribution of domestic financial market through measured such as calling on interest rate and credit expansion, selective allocation of credit and high reserve requirement. It is believed that misguided policies have damaged the economy of Nigeria by reducing saving activities.

In essence, the standard recommendation put in place to resuscitate the economy is proper deregulation of the economy which will definitely affect the financial sector.

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According to Adekanye (2002) the deregulation policy was adopted in 1987 against a crash in the international oil market and the reactant deteriorating economic condition in the country due to stringent policies in the financial sector. Adekanye pointed out that the policy was adopted to achieve fiscal balance and balance of payment availability as well as liberation of the financial system by altering and restructuring the production and consumption pattern of the economy, eliminating price distortions, reducing the heavy dependency on crude oil export and consumer goods importation, enhancing the non-exports base and achieving sustainable growth.

The banking sector by its nature of activities is the most heavily regulated sector in most economics. It is based on this criteria that the success of Nigeria's experiment with economic deregulations must inevitably be assessed. The efficient functioning of an economy is to a great extent the responsibility of the banking industry. In this respect the rapid development of the Nigeria economy depends mainly on the depth of involvement of the Banking Industry following from the need for efficient functioning of the economy, the Central Bank decided to deregulate the financial system particularly banking is therefore an attempt to bring out the much desired development. This will broaden the monetary base and encourage competition in the industry. This will also bring about encouraging banking habit among the populace.

Deregulation policy and its impacts on the Nigerian Banking Industry, deregulating the economy through the banking sector will go a long way in developing and efficient money market thereby improving the payment system in the economy. Infact, the deregulation policy has improved the level of awareness of activities of banks among Nigerians.

In the light of this, according to Ebohodoghe (1990) the deregulation measures has continued to pose profound environment challenged to the banking industry. The liberalization of the financial system has led to the massive protuberating of banks with its attendant consequences of tight computation for fair market share of the public fund, competitive interest rates as well as executive reliance on economic rather than prudential regulation which should focus on bank solvency and credit risk. Ebohodoghe went further to say that deregulation has been closely linked with banks failure; he said that the reason for such assumption was due to the simultaneous occurrence of the time events.

2.2 Conceptual Framework

The business of banking according to Oriji (1987) came to Nigeria as a result of the West Africa province trade in the Guinea Cost [Nigeria and the Gold cost Ghana] so trade was the main factor that necessitated the establishment of banks. Elder Dumpster and Company was one of the major European shipping and trading organization that was in the fore front in the drive to establish the banking industry in Nigeria.

Banking operations have existed for more them a country in Nigeria. Its existence can equally be paced to the early colonial period. In 1892 Nigeria's First Bank, the African Banking Cooperation was established. No banking legislation existed until 1952, at which point Nigeria had three foreign banks [the Bank of British West Africa, Barclays Banks and the British and French Bank] and two indigenous banks [the National Bank of Nigeria and the African Continental Bank] with a collective total of forty branches. A 1952 ordinance set standards required reserve funds established bank examinations and provided for assistance to indigenous banks. Yet for decides after 1952, the growth of demand deposits was slowed by the Nigerian propensity to prefer cash and to distrust checks for debt settlements.

British colonial officials established the West African Currency Board in 1912 to help finance the export trade of foreign firms in West Africa and issue a West African Currency convertible of British pounds sterling. But colonial policies barred local investment of reserves, discouraged deposit expansion, precluded discretion for monetary management, and did nothing to train Africans in developing indigenous financial institution. In 1952, several Nigerian members of the Federal House of Assembly called for the establishment of a Central Bank to facilitate economic development. The Nigeria farmers and commercial banks was established during this period but experienced a number of bank failure including the indigenous bank while very few survive, the experience created a lot of public indignation and concern many lost confidence in the banks as a result of this, the government started enacting number of legislation like the ordinance of 1952, 1958 and banking decree of 1969.

The ordinance defined a bank and its business and it also specified the amount of authorized capital of both indigenous and foreign banks. This began in the period of legislative regulation of banking activities in Nigeria. Another regulator body was established in 1959, this was the Central bank of Nigeria [CBN] it was established towards the development of banking system.

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In 1973, the Federal Government in pursuance of its indigenous policy, decided to also indigenous the banking industry so in that year it took enough percentage interest in the foreign banks in the country to raise total indigenous ownership to 401 which was later to 601 in 1976 under the second phase of the [indigenous] section exercise by soon in the number of state government owned bank that were being established the financial system review committee was set up by the Federal Government in 1976 to review the Nigeria Financial System. This committee submitted its export in December 1976. The Nigeria Banking Industry experienced tremendous growth during the period of legislative control especially since the deregulation in Nigeria economy in 1986, define 1986, there were only forty banks in the country. But with the introduction of deregulation policy it increased to 110 as at the end of 1990. Presently it his reduced to 90 following the recent bank failure.

To veil it all, the Nigerian Banking Industry which is regulated by the Central Bank of Nigeria, is made up of deposit money banks referred to as commercial banks, development finance instituting and other financial institution which include; Micro finance banks, finance companies, bureau de changes, discount house and primary mortgage institution.

2.2.1 Functions of Commercial Banks in the development of Nigeria Economy

Commercial banks have long been recognized to play an important role in economic development of Nigeria economy. This recognition dates bank to Gold Smith 1955 which demonstrated that commercial banks could be a catalyst of economic growth if it is well developed and healthy.

Commercial bank is the oldest banking institutions in Nigeria with the First Commercial Bank being established in 1892. Commercial banking is the most important financial institution and also the most popular with the Nigeria public it is unique in its performance of services. According to Osubor (1951:25) commercial banks are destiny wished financial institution, through its saving mobilization and efficient financial intermediary roles. In essence, commercial banks are those institutions that keep deposits and render payment mechanism for their customers. By payment mechanism it means that individuals and corporate bodies only make payments to one another through commercial banks. In this wise, commercial bank functions like a departmental store of financial services. It is the only financial institution where one can get various departments for different service such as saving department, paying department, foreign remittances and so on like departmental store.

In light of this, commercial banks activities towards the development of Nigeria economy could be seen as follows:

- Firstly, they play financial intermediary functions such as saving and borrowing which are linked up and this reduce transactions and search cost. They allow their customers to keep deposits with them in form of saving, current and fixed time deposits i.e. they provide savings facilities for their customers. Equally, they borrow out loan to their customers in form of short term or long term loan. Other borrowing service include overdraft etc.
- Secondly, they create liquidity in the economy by borrowing short term and lending long term.
- Thirdly, they reduce information costs, provide risk management services and reduce risk involved in financial transactions.
- Fourthly the intermediaries bring the benefits of assets diversification to the economy.
- Fifthly, they mobilize savings from atomized individual for investment, thereby solving the problem of indelibility in financial transactions.
- Finally, they mobilize saving in order to invest it in the most productive venture irrespective of the sources of the saving.

2.2.3 The Concept of Structural Adjustment Programme [SAP]

"Structural adjustment" is a name given to a set of 'free market' economic policy reforms imposed on developing countries by the World Bank and International Monetary Fund [IMF] as a condition for receipt of loans. SAPs were developed in the early 1980's as a means of gaining stronger influence over the economies of debt trapped governments in the South. To ensure a continual inflow of funds, countries already devastated by debt obligations have little choice but to adhere to conditions mandated by the IMF and World Bank. SAPs are designed to improve a country's foreign investment climate by eliminating trade and investment regulations to boost foreign exchange by promoting exports and to reduce government deficit through cuts in spending.

By the end of 1985 there were considerable disenchantment both in the government and private with the sue of wide ranging controls as a tool of economic management, particularly which the renewed ware of control between 1982 and 1985 failed to stem the deteriorating external payments problems of that period. Though this control did to some extent assist in reducing excessive foreign exchange expenditure cost to the economy was enormous.

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2.2.4 The concept and areas of deregulation in the economy

There is no doubt that the prior existence of an unstable macroeconomic environment and weakness in the economics structure of Nigeria led to the introduction of the deregulation policy. The introduction of the deregulation policy is aimed at eliminating the inadequacies and distortion of the old system. Deregulatory policy which deals with the removal of selected regulation in business by government were aimed at attaining a realistic naira exchange rate.

These deregulatory rationalization of traffic to estimate and diversify domestic production, dismantling of administrative controls production and specialization of procedures, liberalization and increased reliance upon market forces for the determination of the pattern of resources allocation.

These deregulatory measures were designed to re-orient the economy towards free market in the area where the financial and intermediary role of banks becomes more crucial to the economy. The practical application of the deregulatory policy has been focused on:

i. Institutional deregulation
ii. Interest rate deregulation
iii. Price and trade deregulation

Deregulatory policy was a child birth of structural adjustment programme introduced in July 1986. Before the inception of deregulation the interest rate was highly regulated and there were frequent adjustment of interest rate which was aimed at achieving the monetary objective of the period. With the introduction of the deregulatory policies the interest rate have been gradually deregulated.

On 1st October 1987, all controls on interest rate were removed in line with the prophesies on the deregulation of the economy. Deregulation of interest rate makes the allocation of credit by price possible.

Institutional deregulation saw the period of discontinue government interference in the various institutions for example the deregulations of the oil industry gave market the freedom to airport and determine the prices of product without NNPC assistance. This policy was equally applicable to different institutions that make up the economy.

Given this positive development and need to realism interest rate determination with the policy of financial deregulation, the cap on interest rate which have been imposed since 1994 removed effectively in October 1st 1996. A dynamic market base interest rate policy is now pursued with effective rates reflecting the forces of supply and demand for funds.

3. METHODOLOGY

This chapter presents the details of the procedure through which this research study is carried out. It describes the research design, population and sampling, the research instrument, method of data collection and the method of data analysis.

The research methodology adopted will be aimed at determined the financial performance which will be measured by the study of the profitability, solvency, financial strength and turnover of commercial banksunder deregulated system of economy.

3.1 Research Design

This research work is a descriptive survey involving the use of a questionnaire that was personally administered by the researcher. The study principally makes use of primary data collected through the employment of the questionnaire designed for that purpose. The study sought to examine and compare the impact of deregulation of the economy on Nigeria commercial banks using a case study of Ilesa metropolis. The questionnaire was sub-divided into two sections containing different items with reference to hypothesis testing.

There will be forty questionnaires that will be administered. Ti will be designed and administered among staff of commercial banks, Ilesa, Osun State. In addition to the research questions and answer, interviews may be conducted with top management staff of those commercial banks. The interview will not be a structured one

3.2 Sample Size

The population is all commercial banks in Nigeria, since it is not possible to reach all commercial banks in the country, also due to simplicity of analysis and other important consideration such as time and financial constraints, the sample size is limited to commercial banks in Ilesha, State of Osun. Due to time factor and

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economic constraint, the premises that economic deregulation is a phenomenon that affect the activities of all commercial banks irrespective of the type or name. The sample size for this research was made up of forty [40] respondents consisting the response of staff of commercial banks.

Random sampling will be done using the commercial banks in Ilesha i.e First bank, United Bank for Africa, Diamond Bank, Zenith bank, Eco bank etc. these are the sample use to carry out the research work.

3.3 Sources of Data

Data collected for research is from both primary and secondary sources. It should be noted that the bulk of the data will be collected from primary source. Primary source of data are data from original source and this form of data is being collected by the researcher herself.

3.4 Techniques of Analysis

In analyzing the research data, the data collected will be presented and analyzed to test for validity. The techniques of data analysis and test used to measure the consistency of the test use in this research will be correlation, regression analysis as well as analysis of variance [ANOVA]. The first hypothesis which states that there will be no significant relationship between deregulation of the economy and increase in commercial banks profitability will be analysis using correlation and regression, as well as analysis of variance. The second hypothesis which states that there will be no significant relationship between deregulation of the economy and increase in banks bad and doubtful debt will be subjected to correlation regression and analysis of variance while the third hypothesis is there is no significant relationship between deregulation of the economy and increase in the number of commercial banks in the country. This will also be subjected to the same test

Correlation (r) $\frac{\Sigma XY - \Sigma XY}{\Sigma X^2 - \Sigma (X)^2 (\Sigma Y^2 - \Sigma (Y)^2)}$

Regression Y = a + bx

$$b = \frac{n\Sigma XY - \Sigma X \Sigma Y}{n\Sigma X^2 - \Sigma (X)^2}$$

$$a = \bar{Y} - b\,\bar{x}$$

4. DATA ANALYSIS AND DISCUSSION

This chapter focuses on the analysis of the collected data using various tools and instruments of statistics. Analysis of data involves the braking down and arrangement of data into meaningful groups, together with searching the pattern of relationship among those data groups. Discussions are also made in the findings of the study as privilege by the data. Tabular presentations of the data are based on the hypotheses of the research. Interpretation of each analysis will be presented after the table followed by the discussion of the findings.

Showing the analysis between deregulation of the economy and commercial banks profitability.

	Nigeria is a Deregulated Economy	**Profitability**
Nigeria is a deregulated Pearson correlation economy	1	-0.063
sig (2-failed)		
N		0.698
Profitability Pearson correlation	40	40
Sig (2-failed)	-0.063	1
N		
	0.698	
	40	40

ANOVA

Model	**Sum of square**	**Df**	**Mean square**	**F**	**Sig**
Regression	1.160	1	1.160	0.153	0.698
Residual	288.815	38	7.600		
Total	289.975	39			

a. Predictors: (Constant) Nigeria is a deregulated economy
b. Dependent variable: profitability

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Regression

Model	Unstandardize coefficient		Standardize coefficient		
	B	**Std.Error**	**Beta**	**T**	**Sig**
Constant	9.010	0.851		10.5920	.000
Nigeria is a deregulated economy	-1.48	0.379	-0/063	0.391	.698

Interpretation:

Given the significant value 0.698 above, it shows that there exist a significant negative relationship between deregulation of the economy and commercial banks profitability. This is because the value of the significant value is about 70%. Therefore the following conclusion holds:

Reject H0 and accept H1 i.e. there is a significant relationship between deregulation of the economy and increase in commercial banks profitability.

Regression
Y=a + bx
Y= Independent Variable
X= Dependent Variable
Y = 9.010 - 0.063 X.

There is a negative relationship between deregulation of the economy and the profitability base of commercial banks. That is the more deregulated the economy is, the less the profitability base of commercial banks.

Correlation

	Nigeria is a Deregulated Economy	**Increase in number of Commercial Banks**
Nigeria is a deregulated Pearson correlation economy sig (2-failed) N	1	-0.093 0.568
Increase in Commercial Pearson correlation Sig (2-failed) N	40 -0.093 0.568 40	40 40

Regression

Model	Unstandardize coefficient		Standardize coefficient		
	B	**Std.Error**	**Beta**	**T**	**Sig**
Constant	10.897	0.855		12.7520	.000
Nigeria is a deregulated economy	-0.219	0.381	-0.093	-0.579	0.568

Interpretation

Given the significant value 0.568 above. It shows that there exist significant negative relationship between deregulation of the economy and increase in number of commercial banks. This is because value of significant value is about 57%. Therefore the following conclusion holds.

Reject the H0 and accept H1. This implies that there is a significant relationship between deregulation of the economy and increase in number of commercial banks.

Regression
Y = a + bX
Y = 10.897 - 0.093 X

Discussion

The result obtained from testing the hypothesis revealed that there is a significant relationship between deregulation of the economy and increase in commercial bank profitability. The relationship was found negative. This implies that the more the economy is deregulated, the lower the profitability base of commercial

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banks. In the real sense, the financial performance of commercial banks is very weak, the reason is not far fetch but it lies on the simple fact that commercial banks were given ample chance to make decision that can suit their operation. The policy of the Central Bank will be flexible enough for commercial banks to take decision.

In testing the second hypothesis, it was found out that there is no significant relationship between deregulation of the economy and increase in commercial banks bad and doubtful debts. This was obtained from the correlation analysis made in the table above. While relating it with the regression analysis run along side with it, it is observe that the relationship between deregulation of the economy and commercial banks bad and doubtful debts is positive. This simply implies that the more the economy is deregulated, the more reduced the number of bad and doubtful debts of commercial banks. Looking critically into the meaning of deregulation of the economy, this simply means that government will reduce her control in coordinating the activities of different sectors of the economy. Laws and regulation than can hinder free competition in supply of goods and service will be eliminated therefore allowing the market force to drive the economy.

5. CONCLUSION AND RECOMMENDATION

5.1 Conclusion

This study shows that the adoption of the deregulation policy in Nigeria was in response to the deteriorating economic and social conductions inherent in Nigeria economy among the considered trend were slow output growth, decline exports, rising inflation, inefficient allocation of economic resources, balance of payment problems and rising debt burden.

In order to proffer solution to the un-conducive environment the deregulation policy was introduced to combat with the distortions in Nigeria economy. The deregulation policy encourages the efficient operation of the market which will lead to higher productivity, greater efficiency and efficient allocation of economic resources. The study therefore concludes that;

i. With deregulation of the economy came high technology information which actually reduced incidence of fraud in banking industry.
ii. The deregulation of the economy has resulted into increase in numbers of commercial banks as a result of competitive environment
iii. The deregulation of the economy has resulted in increase in manpower or skilled staff development in the banking industry.
iv. The competitive environment created by deregulatory policy led to an increase in product development.
v. Through deregulation policy, the efficiency with which banks and other institution carry out their business has been on the increase.
vi. The financial performance of commercial banks improved tremendously following deregulation policy.

5.2 Recommendation

Based on the findings of this study, the following recommendations are being made;
The economy should not be totally deregulated it should be a form of ‘sitting on the fence’ between regulated and deregulated economy.

Commercial banks should ensure that adequate collateral are collected before extending loan to customers, irrespective of the competitive environment in order to reduce the incidence of bad and doubtful debts.

There should be some consistency in interest rate policy which will be favourable enough to ensure greater utilization of banking service towards efficient allocation of the economy resources. This is to say that interest rate should not be too low to discourage saving or too high to induce investment.

Since the deregulation measures taken by the Central Bank have not achieved their designed objectives there should be a drastic revaluation of the implementation strategies. The Central Bank of Nigeria should make sure that interest rate changed by commercial banks should be a function of rate payable by central Bank of Nigeria [CBN] on their commercial papers like treasury bills, treasury Certificate, Bonds, and Guarantee etc.

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