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Research Article

Multiplicity of Financial Intermediation in Nigeria: A Catalyst for Financial Stability in Globalized Business Environment

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Abstract: The recent worldwide economic downturn, which also had an impact on the Nigerian economy, showed how economic unpredictability could hinder a developing economy's achievement by leading to a credit crunch, insolvency, massive volume of bad loans, failure to fund the real sector, and the collapse of a number of banks and non-bank financial establishments. Investigating the relationship between financial stability (FS), credit financing (CF), monetary financial deepening (FD), and inflation in Nigeria was the investigation's main goal. The CBN's yearly reports for the years 1985 through 2020, inclusive, were used as the secondary data source for the study. An initial unit root test and co-integration test of the ECM short-run result for financial stability were undertaken as part of the investigation. The results showed that Nigeria's economic growth had no beneficial effects on the nation's financial sector volatility. The study concluded that in order to enhance sustainable finance to the productive units of the Nigerian economy and guarantee financial security, an adaptive and sustained effort through policy guidelines is required.
Keywords: Financial intermediation, financial stability, inflation, financial deepening, globalization, monitoring policy.

Introduction

The task of creating reform policies to tackle the main causes of financial volatility and tactics required to stabilise the financial system typically falls to the highest regulatory bodies. According to the European Central Bank (2008), such measures should be effectively transmitted through a reliable monetary policy transmission system. So that the country's public and private economic sectors have access to enough finance to speed up production, distribution, and consumption. Without a thorough grasp of the complex dynamic relationships between interest rates, inflation, and financial deepening and their effects on financial soundness in the economy, these aims cannot be attained. Nigerian banks control the majority of the stock market and more than 90% of the financial sector's assets. The real estate industry is one area of the economy that receives a lot of bank funding. Therefore, financial system stability is crucial for increasing loans to multiple sectors as well as for fostering investor confidence in the economy. Ijaiya and Abdulraheem (2000) contend that the generation of credit and the variety of financial intermediations, which act as the cornerstone and spur for steadiness and economic progress in a extremely globalized corporate setting, are better able to achieve sustainable economic expansion. Financial intermediaries are crucial to the running of most economies, according to Levine's (2002) argument. A solid and robust financial system also enhances this steady economic expansion.

Statement of the Problem

The current worldwide economic downturn, which also had an impact on the Nigerian economy, showed how financial instability could hinder an emerging economy's performance. Thus, there was

a credit crunch, illiquidity, a significant quantity of non-performing loans, difficulty financing the real economy, and failure of several banks and other financial establishments. To address the problems of financial instability in Nigeria, a number of policy reforms have been implemented, including the banking sector liberalization policy of 1986, the bank consolidation policy 2004, and the banking sector sanitization exercise of 2009.

Objective of the Study

To inspect the link between inflation, credit financing, financial stability, and deepening in Nigeria.

Literature Review

Conceptual Framework

Financial Stability

Financial stability, according to the European Central Bank (ECB, 2011), is "*the property of a financial system in which financial institutions and markets are continuously able to carry out their functions of providing financial services without impeding economic growth*". The stability guarantees that there won't be any hiccups in the financial intermediation process that might seriously disrupt the logical allocation of limited resources to worthwhile and more lucrative economic possibilities in the nation. Most developing or emerging economies experience financial system instability, which has a significant impact on the effectiveness of macro-economic monetary policy in attaining the highly sought progress. Onoh (2002) noted that the quick changes in the financial systems of different nations, the expansion of technical innovation in banking, and the globalization of trade and other business activities had exposed the banking industry to potential risk and all other types of factors that were likely to contribute to financial instability on a global scale.

Many developing nations have experienced significant financial instability, which has continued to be a top policy concern, particularly in the years following the global financial crises of 2007. Financial shocks, according to Mishkin (1999), are expressions of financial instability that, when they happen, interfere with the ability of the financial markets to properly perform their financial intermediation tasks, causing systemic disruption. While Schinasi (2006) argues that the capacity of a financial system to provide financial services to anybody without limitation, preserving the soundness of the economy via efficient and effective financial intermediation, is a sign of its soundness. The causes of financial instability, which might include things like economic booms or busts or changes in the economy's macro-economic policy focus, determine how to handle the problem using monetary policy. The degree of financial stability is determined by the system's capacity to successfully provide financial intermediation, manage risk, and absorb shocks, which are frequently brought on by abrupt changes in the system.

Empirical Review

Amali, *et al.,* (2022) used auto-regressive distributed lag (ADRL) methodologies using time series data from the first quarter of 2006 to the fourth quarter of 2020 to inspect the influence of financial steadiness on economic progress in Nigeria. The experimental variable and a stand-in for economic growth is real GDP, whereas indicators of financial stability include the share index, capital sufficiency, non-performing loans, liquidity ratio, and ROAs of the banks. According to the findings, capital adequacy, non-performing loans, and liquidity ratios all have a detrimental effect on economic growth. Given the paucity of research in this area, the study adds to existing knowledge by providing fresh perspectives on the link between crucial indicators of financial steadiness and economic progress in Nigeria. It revealed a conflict between Nigeria's economic expansion and financial stability.

Akintola and Aroyewun (2022) examine monetary policy and stock market return in Nigeria from 2010-2019. The study established a significant relationship between monetary policy and stock market return in Nigeria. The study recommended that monetary authorities in Nigeria should

implement favourable monetary policies in order to keep the Nigerian stock market to be attractive to investors.

Between 1986 and 2017, Ajisafe, *et al.,* (2022) looked into the diminuendos of monetary policy's impact on financial stability in Nigeria. These variables-financial stability index, exchange rate channel, financial deepening, and price stability-were used in the study. In terms of financial stability, the findings indicated that the exchange rate channel dominated other channels for the transmission of monetary policy in Nigeria. The study came to the conclusion that monetary policy adjustments had a major impact on Nigeria's financial stability and that the exchange rate was the primary means through which monetary policy was transmitted to maintain that stability.

The system's capability to properly offer financial intermediation, regulate risk, and withstand upsets-which are typically spurred by unexpected alterations in the system-determines the level of financial stability. They used the Engle Granger two-step co-integration analysis and error correction approach to show a long-term relationship between financial depth and economic progress in Nigeria.

Researchers Judith *et al.,* (2014) examined how credit financing affected the expansion of the Nigerian economy. Data for the years 1992 to 2008 were used, with GDP and credit finance serving as the explained variables. The investigation found that credit financing had little effect on Nigeria's economic expansion during the time.

Theoretical Framework

Monetary Policy and Financial Stability Theory

This theory assumes a normal economy with sparse instances of inflation and deflation. The financial system, comprising the establishments and the markets, can run smoothly in such a stable situation. The efficacy of banks, other financial establishments, and the level of financial markets all play a role in how well the monetary policy transmission mechanism works. Banks significantly influence interest rates and the amount of money that is lent to the economy for productive purposes, which in turn influences GDP growth. The rate of inflation, which affects both consumption and investment, determines the real rate of interest on investments. Financial instability can result from market inefficiency brought on by knowledge asymmetry that affects loan financing.

Research Method

The study utilised data from secondary sources, and it was taken from the yearly books and statements of the Central Bank of Nigeria (CBN) for the years 1985 through 2020, inclusive.

The Model

The ratio of bank capital to assets serves as a proxy for the dependent construct, financial stability (FS), while the ratio of credit to GDP serves as a proxy for credit financing (CF). Money supply (M2), that is the proportion of the widecash supply to the GDP and inflation as expressed by the combined price index, is used to measure financial deepening. The paper develops a short-run vigorous equation of financial firm to assess the dynamic interaction between the constructs in the Nigerian financial system.

The work, in particular, methodically estimated an error correction model which thus: $LnFST_t = b_O + b_1CRE + b_2FDP + b_3INF + b_4ECM + u$……..1

Where:

FST = Financial stability as measured by the ratio of bank capital asset; CRE = Credit financing of the banking sector as a ratio of gross domestic product; FDP = Financial deepening which is the ratio of broad money supply to gross domestic product; INF = The rate of inflation; ECM = Error correction term; u = Error term.

Data Analysis

Unit Root Test

A unit root test of the model analysis's variables was conducted to start the analysis. To determine the variable's time series attribute, do this. The unit root test with Augmented Dickey Fuller (ADF) statistics was examined to look at the characteristics of the variables and determine if they are stationary at their levels or in their initial difference.

Table 1. Unit Root Test of Variables at Levels

Variables	ADF Statistics	Critical Value	Remark
LCRE	0.2080	2.9510	Non-stationary
LFDP	0.7660	2.9591	Non-stationary
LFSB	1.5401	2.9592	Non-stationary
LINF	0.5490	2.9590	Non-stationary
Source: Authors' computation (2022)			

Table 1.2. Unit Root Test (First Difference)

Variables	ADF Statistics	Critical Value	Remark
D (LCRE)	3.7240	2.9620	Stationary
D (LFDP)	4.1320	2.9620	Stationary
D (LFSB)	5.3610	2.9620	Stationary
D (LINF)	8.2090	2.9620	Stationary
Source: Authors' computation (2022)			

The outcome showed that none of the constructs was static at level, but after being differentiated once, they all became stationary. This indicates that all of the constructs are integrated in order one 1(1), and not any of the constructs were integrated in order zero 1(0).

Analysis of Co-Integration Test Analysis

Investigating the long-term relationships between the variables was the purpose of this study. The Johansen co-integration test was therefore used to check whether there was co-integration between the variables.

Table 2. Johansen Co-integration Test Results

Hypothesized no of EC(S)	Eigen value	Likelihood ratio	Critical values 5% (1%)	No of co-integrating equations
None**	0.6390	59.1980	47.21 (54.46)	One
At most 1	0.4565	27.5765	29.68 (35.65)	
At most 2	0.2295	8.6695	15.41 (20.04)	
At most 3	0.0187	0.5856	3.76 (6.65)	
Source: Authors' computation (2022)				

According to the aforementioned finding, the H0 of no co-integration between the chosen variables is not accepted. Greater than both the 5% and 1% crucial values is the likelihood ratio (59.198). This demonstrates the co-integrating relationship between the level series and the existence of one co-integrating equation. This indicates that even if the constructs are combined to order one, or 1(1), when the variables are co-integrated, the linear combination of these 1(1) variables becomes 1(0). This suggests that the long-term equilibrium between the variables is stationary.

A vector auto regression analysis was performed to confirm the nature of the relationship between the variables, and an impulse analysis was also performed to look at how each variable changed over time in response to shocks to both itself and to other variables.

Table 3. ECM Short-run Results for Financial Stability

Variables	Coefficients	P-value
ΔLn (CRE)	1.8470* (5.6290)	0.000
ΔLn (FDP)	-0.9190 (-1.0880)	0.352
ΔLn (INF)	-0.1450* (-9.7250)	0.000
C	1.6560*** (1.9590)	0.026
ΔLn (FSB)	-1.2460* (-3.2590)	0.000
Cointζq1	1.7980** (2.9460)	0.002
Unadj. R^2	0.9260	0.000
Adsj. R^2	0.8590	
F-statistics	15.7270	
DW-stat.	2.0030	
*significant at 1%; **significant at 5%; ***significant at 10%; t-value in bracket		
Source: Authors' computation (2022)		

The aforementioned error correction demonstrates that F-statistics, which gauge the degree of statistical fit, are highly significant. Variables in the explanatory constructs, specifically CF, FD, and inflation as determinants, were shown to account for about 99% of the systematic variation in credit to the banking sector. This shows that the explanatory variables are important factors in determining the FS as expressed by the proportion of bank assets to capital. The effect of the prior period's FS was notable among the individual explanatory factors. This demonstrates how the previous values have a substantial impact on financial stability. Additionally, at a level of 5%, the effect of CF was statistically substantial. While the influence of inflation was only marginally substantial at 1%, that of financial deepening was not. The results show that there is no stability in the Nigerian banking industry, with the error correction coefficient of FS being positive and weighty at a t-ratio of 2.946.

Research Findings

The outcome demonstrates that any short-term shock to the nation's financial system won't be recovered over time. FD has a negative coefficient (-0.919). FD has thus had a negative effect on Nigeria's financial sector volatility. As a result, the negative FD coefficient does not match a priori expectations. Because of this, the rate of financial deepening does not contribute to the expansion of Nigeria's financial stability. This means that both in the short and long term, CF of the banking sector favorably and significantly adds to FS. Financial instability would be decreased if banks consistently and successfully implemented their credit financing policy initiatives.

Conclusion and Recommendations

The level of financial system development must be taken into consideration in order to expand the Nigerian economy because it may improve the effectiveness of capital accumulation and/or raise savings and investment levels. Therefore, in order to enhance workable CF to the productive parts of the Nigerian economy and ensure FS, a resilient and sustainable effort through policy guidelines is required. Macro-economic policy initiatives should be developed to reduce inflation rates, and long-term financial deepening policies should be implemented to support Nigeria's economic growth. The Nigerian central bank should support efficient ways for banks to increase their lending channels and liquidity to private businesses, and they should pursue an aggressive policy to remove any barriers that would impede the expansion of credit to the private sector.

Declarations
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Conflict of Interest: None.
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Author Contributions: HOA, NMN and AGO contributed to the design and implementation of the research, to the analysis of the results and to the writing of the manuscript.

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