ASSESSMENT OF GROWTH IN THE BANKING INDUSTRY AND ECONOMIC DEVELOPMENT OF NIGERIA

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Abstract:

The study examined the contribution of FDI in the banking industry of Nigeria to the development of the economy. Data for the study were collected for the period 1997 – 2006 from the Central Bank of Nigeria (CBN), the Ministry of Statistics and other relevant periodicals which are used for the analysis. The findings of the study showed significant contribution of the foreign investments in the banking sector to the GDP of the country. However the literature reviewed that the influx of FDI in Nigeria is as result of the good economic climate, government incentives and the stable political atmosphere. We found that the FDI in the banking industry has stimulated keen competition in among domestic banks. Capital inflow has increased in the wake of the merger and acquisitions that swept across the sector. The findings also revealed a drop in number of employment following the mergers in the bank. The study recommends that caution should be exercised to ensure that any bank acquisitions by foreign investors do not involve the control of the main stream banks in the country. Foreign investors should be encouraged to acquire community and other rural banks to help develop and establish the banking system in the rural areas and communities.

Keywords: foreign direct investment, banks, investments, domestic, foreign

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Introduction:

The positive impact of FDI can also be viewed from the amount of capital investment in the banking sector particularly since the influx of foreign investors into the sector. This is especially noticeable from the period of democracy in 1999 in Nigeria when trust and efficiency was injected into the political system. There has been rise in the domestic capital in the banking sector. This rise is doubtless a function of both private and foreign owners in the sector. The Table 1depicts the trend of capital investment in the banking sector since 1999.

Table 1: Domestic investments in Nigerian banks (1999 –2006)

	Year	Capital Investment (=N=million)
1	1999	193,412.9
2	2000	285,294.4
3	2001	192,731.8
4	2002	435,601
5	2003	434,299
6	2004	677,957.4
7	2005	834,522.9
8	2006	701,667.3

Source: Federal Ministry of Statistics of Nigeria (2007)

The report by UNCTAD (2005) shows that the Nigerian economy is significantly expanding and attracting FDI inflow in comparison with other African countries. According to UNCTAD (2001), Africa attracted $8198 million ($5582m for SSA) in 2000 representing 0.65% (0.44% for SSA) of total FDI flow and 3.4% (2.3% for SSA) of total developing country FDI flows. The main recipients were Angola ($1800m), Egypt ($1235m) and Nigeria ($1000m).

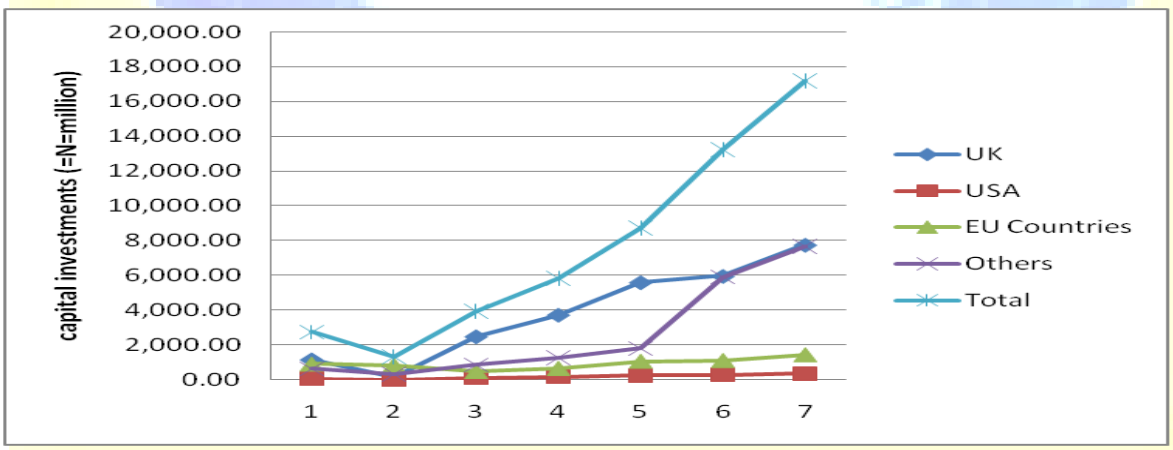
Interestingly, the amount of capital investments by foreign countries operating in Nigeria indicates that most of the capital inflows come from the EU countries while the USA has the least capital flow in the country. Ironically, Nigeria has been the 3rd largest supplier of crude oil to the

US and most US products find their ways into the country (UNCTAD Report, 2005). The above assertion is supported by the Table 2 below extracted from the CBN Report (2006). It shows that total amount from major countries investing in Nigeria within 1999 to 2005.

Table 2: Net Capital Flow (Unremitted profit) by Country of Origin (=N= million)

Year	UK	USA	EU Countries	Others	Total
1999	1,159.6	38.3	885.7	636.1	2,719.7
2000	157	0.0	820.4	315.8	1,293
2001	2,486	98	464.	863.4	3,911.4
2002	3,729	163	641.3	1,265.4	5,798.7
2003	5,594	253	1,045.7	1,806.6	8,699.3
2004	5,960	263.9	1,090	5,903.5	13,217.4
2005	7,748	343.1	1,417	7,674.6	17,182.6

Figure 1: The distribution of FDI by countries of origin



An important reason for FDI in Nigeria stems from the motives of the multinational firms to dominate the market particularly in the banking sector. Large chunk of the big banks in Nigeria such as Union bank, FBN are affiliates of the some foreign banks such Barclays. This attempt to dominate the financial market has informed the Central Bank of Nigeria (CBN) resolve to institute legislations to control the amount of ownership of foreign banks in Nigeria (CBN, 2006).

This reason concurs with the view of Buch et al (2005) who assert that FDI who are active in foreign countries usually maintain foreign affiliates that are above average size and more profitable and commands large sales. Since the country is a growing and developing economy, FDI in the banking sector has been predicted on the attempt of providing access to fund to local and even entrepreneurs who often may not such access due to stringent conditions attached to such loans

However, caution need to be exercised in embarrassing such capital inflow into the sector because FDI investments also attract some repatriation in from of profit and other foreign capital (Udese, 1990). But the net benefit is determined when the inflow outweighs the outflow. The Table 2 shows however that the net capital flow is positive as more funds seem to have flowed into the economy than the outflow of such investment funds.

Another factor in the FDI in the banking sector of Nigeria is the effect on the number of workforce in Nigeria. The advent of FDI in the banking sector ushered in mergers and acquisition in the bank industry. The impact of the M&As on the bank workforce as well as the employment level in the country are also discussed.

Despite the foregoing, the negative impact of FDI in the bank sector can be perceived by the structural adjustments in the sector. As a result of the FDI and the subsequent regulations in the bank sector, the number of the banks has fallen from over 89 commercial banks before 2001 to less than 23 banks. The economic implication of this involves losses of employment resulting from retrenchments, downsizing and mergers. With such huge impact on employment and other vital areas, a study to examine the overall impact of the FDI in the banking sector is very vital.

FDI, Mergers and Acquisitions in the Nigerian Banking System:

The Nigerian financial sector has undergone tremendous reformation leading to an unprecedented record of the mergers and acquisitions (M&As) in the banking institution. The doctrine of consolidation follows the presumption that synergy and efficiency can be achieved in the amalgam of banks. If the assumption is correct as suggested by some studies (Akhigbe et al, 2004; Amel & Rhoades, 1989) the overall effect will be improvement in the performance of the banks and increase in shareholder returns; which can be distributed through dividend.

Where the merged bank is more valuable, both in operating performance and management than the aggregate of the two separate pre-merger banks; the resulting entity from the merger becomes beneficial. In addition, merger builds up a strong capital base for financially creeping institutions. The Nigerian experience has added some form of credibility and strong capital formation into the banking system.

The initial number of banks prior to the 2005 consolidation amounted to nearly 89 banks, with some poorly capitalised and depended on public deposits for operation. The Central Bank of Nigeria (CBN) poised on building not only a formidable banking system but also to ensure a diversified, strong and reliable banking sector, which will ensure the safety of depositors money and thus play active developmental roles in the Nigerian Economy and become competent and competitive players both in the African and global financial systems.

The CBN also set up measures to ensure and encourage the emergence of regional and specialized banking system. The minimum capitalisation target for all banks in the country was raised to N25billion (approx $250million) from N2billion (approx $15million) with full compliance before the end of December 2005. The CBN as a tradition does not publish the condition of individual banks. In times of distress, such banks are shielded from massive withdrawals capable of collapsing them (CBN, 2006).

According to Akugbue and Aliko (2005), it was the belief of the CBN that such banks in distress can be revived through managerial repositioning. In dealing with this issue, the CBN decided that by the end of December 2005, the names of Banks that meet up with a minimum capital base would be published. The idea is to enable potential depositors have enough information about the status of the Banks.

This target date and coupled with the amount of capital requirement, ignited the flux of the unprecedented consolidation in the Nigerian banking. The number of banks has consolidated to 25 after an initial 26 banks licenses were revoked in 1998 (Beck et al, 2005). In the past, some financial institutions showed glaring inability to maintain an efficient flow of funds within the economic system; and most rarely paid dividends. The sharp practices of some Banks together with the unsoundness of others led to a wide spread of financial sector distress and losses to depositors.

During the merger wave, some of the Nigerian banks were acquired by foreign investors. Thus, such foreign banks as The Nigerian International bank (a subsidiary of Citibank), Societal General Bank and the Standard Chartered bank have remains strong mark of FDI in the banking sector.

Government Incentives to Foreign Direct Investment:

The Federal Government of Nigeria in its effort to influence the decisions of foreign firms to investment in the country, exercises direct and indirect controls. Some of these controls could be in forms of incentives or regulations such as the tax and tariff concessions and the non – tax financial incentives (CBN, 2006). Some of the incentives are as discussed below.

The tax and tariff concessions: These are tax relieves for purpose of research and development. Under this incentive, a company which undertakes research and development activities in a year is entitled to a tax deductible allowance equal to 120 percent of the amount expended in the research if it's in the area of raw materials. Thus FDI is stimulated by taking advantage of the incentive to carry out vital programmes in the country.

Pioneer status: Relevant companies granted a pioneer status are entitled to tax holidays on corporate income for 3 years in the first instance and an extension of two years thereafter. This is aimed at encouraging beneficial companies. Multinational firms and foreign firms that embark on manufacturing products or providing services that are uncommon are given the pioneer status. This exempts them from tax payment for a period of time. In the banking industry, banks that are innovative in their services are granted this status. The status was granted to banks that initiated the online banking and credit card payments in Nigeria (Adolphus, 2004).

Corporate income tax: The incentives under corporate income tax provisions are usually specified during the annual final budget. For example in 1988 the percentage was reduced from 45 to 40 to stimulate investment and growth in the Nigerian economy. The government introduced 20 percent tax rate for small firms in manufacturing, agriculture and solid mineral processing sector.

Tax free dividends: With effect from 1989 any individual or company deriving dividend from any company is entitled to tax free dividend for a period of three years, if the company paying the dividend is incorporated in Nigeria between the beginning of January 1987 to the end of 1992, and if the recipient's equity in the company constitutes at least 10 percent of share capital of the company.

Most FDI have benefited from this scheme as it has helped to reduce the amount of corporate profits that have been repatriated abroad. Akino (2004) acclaims that the tax free dividend reduces the coincidence of double taxation particularly for multinational firms.

Investment in economically disadvantaged areas: In areas classified as disadvantaged, companies enjoy seven years income tax concession under the pioneer status scheme as well as special fiscal concession by the relevant state governments and additional five percent on the initial depreciation allowance. The Federal Government of Nigeria provided further incentives to foreign firms under this scheme to expand their investments in the rural areas. In 2001, all foreign banks were directed to establish a rural banking scheme to accommodate the needs of the rural communities. Garba (2005) confirmed that economic activities were stimulated in such beneficiary communities.

Duty draw back and suspension scheme: As stipulated by the CBN Investment report (2005), the government could refund import duty on raw materials used for the production of export products. This rebate scheme is to exempt imported raw materials and components used in export production from import duty. To qualify for this incentive the exportation of the associated product must be within eighteen months from the date of importing the materials.

There are also non tax incentives which may include government interest rate policy, exchange rate, and other regulatory frameworks governing foreign investors in the country. Udese (1990) list them as follows:

Interest rate structure: Until 1997, interest rate in Nigeria was administered by the central bank of Nigeria who fixed the deposit and lending rate. They determined the preferred sector of the company and the lending distribution to this sector. From 1987 August to December 1993, the era of deregulation framework reigned and in January 1994 administrative framework was reintroduced. This periodic adjustment was always at the dictate of the economy and they geared towards boosting savings and investment toward economic growth. Foreign banks are therefore under obligation to comply with such regulations.

Exchange rate: The auction system was introduced in 1986, this brought about significant adjustment in the real exchange rate for the Naira. Between 1988 and 1992 the auction system underwent several modifications which gave birth to the inter-bank system (Garba, 2005). This is one among other reasons to encourage foreign investors.

Introduction of domiciliary account: Under this scheme, exporters are allowed to keep 100 percent of their export proceed in foreign currency. Withdrawal is allowed for transaction relating to export business. This gives easy access to foreign exchange procedures. The result of the introduction of the scheme on FDI particularly in the banking sector has been overwhelming. Adolphus (2004) confirms that there has been a regeneration of business interests and transactions among local entrepreneurs who buy manufacturing materials abroad. Ownership of domiciliary foreign banks is facilitated by foreign banks such as Citibank, Societal Generale etc.

Review of the indigenization policy: These laws were enacted banning foreign investors from delving into some sectors of the Nigerian economy and even ownership structure of foreign companies. This was reviewed and foreign firms were allowed to go into some areas of the economy. Among such laws are Nigerian enterprises promotion decree of 1972 and the indigenization decree of 1997(Nigerian Foreign Policy Handbook, 2001).

Establishment of industrial forum: This was a decree aimed at bringing prospective foreign investors and the local business together to consider joint venture deals.

Review of the repatriation of dividend and capital: The regulations and procedures governing the repatriation of dividends and the capital have been eased as parts of efforts towards making Naira convertible and encouraging foreign capital inflow.

Bilateral investment protection agreement: The current bilateral investment through which Nigeria government hopes to enter into bilateral agreement with foreign countries Nigeria are not tampered with. Under such agreements, the Federal Government agrees to speed up any process that enhance establishment of foreign firms and offers to give adequate security protections to such firms.

Non-voting equity share: For companies whose shares are quoted on the Nigerian stock exchange, government has permitted the issuance of non voting share to enable them attract capital from foreign investors (1998 Decree). The decree was introduced to provide investment opportunities to foreign investors including existing foreign partners and individuals. Payment for the shares is to be made in convertible foreign currency. The share shall be qualified for both dividend and capital repatriation.

Involvement in commodity exchange market: The government has removed restriction on foreigners' involvement in commodity exchange market (comex) and participation in export processing zone. Central bank of Nigeria report (2006) shows that COMEX is one of the ways foreign investors can earn and expatriate profits by the private sector, with the commencement of the export processing zone in Calabar, Nigeria in 1995. It is expected that the required foreign capital will flow in to take advantage of the infrastructural amenities installed in the zone.

Contribution of FDI in the Nigeria Nigerian Banking Sector

The annual foreign private investment survey (CBN, 1991) covered seven hundred and fifty six establishments that are either fully foreign or Nigerian. Through the managerial and technological capabilities, FDI have helped to develop the material and productive resources of Nigeria. The report shows the following contributions of FDI in the economy of the country.

1). The FDI investment has stimulated the diversification of Nigerian economy. Focus has thus being removed from solely on the oil and gas sectors of the economy to the banking industry. The influx of foreign banks has stimulated competition among banks; stirred up mergers and acquisitions and privatization of some of the ailing banks.

2).The capital inputs have helped most State Governments to fulfill nationality defined economic development goals. Most banks and the various State Governments have partnership pacts in undertaking some developmental projects. Loans and grants are easily obtained from the foreign banks towards such developments. For instance, the Edo State Government borrowed a total of twenty million dollars towards the building of new roads across the State from the French bank; Societal Generale Bank (SGB) during 2005 (Bank Watch, 2007).

3). FDI contributes to rural development by opening their operation in rural banking scheme established in 1977. As a result, the rural banking scheme has aided in opening bank branches in rural communities. According to the CBN (2006), there is virtually a bank branch in each rural council most of which are made of the foreign banks. This venture has stimulated both economic activities in such areas and revitalized banking services among the community dwellers.

4). The FDI have the modern technology and knowhow for their operation. This is especially true in the banking sector where the

5). They comply with the government more for national self sufficiency by engaging in agricultural project e.g. 4000 hectares farm planted by Guinness Nigeria PLC in Kudu in Niger State.

6). Standard of living is enhanced by the activities of the FDI through increased wage pay compared with what is paid by the Local employers.

7). Manpower development is achieved through the activities of the FDI in the area of giving scholarship to deserving Nigerians e.g. Shell, petroleum, Chevron Scholarship Scheme.

8). Another great advantage of foreign direct investment in Nigeria's industrial development programme was the important part it played in bringing technical and management skill which usually are just as likely to be the limiting factor to industrial development as shortage of foreign exchange.

9). The foreign private investment forms the biggest single source of job creation over the past decade. This becomes even greater if the spill over to other areas of the economy is considered.

10). Foreign companies in Nigeria pay relatively higher wages than Local firms, thereby raising the living standard of Nigerian workers above national average since a sizable portion of Nigerian industrial workforce is employed in the foreign firms.

11) The social investor has assisted and induced government in providing infrastructural facilities and has led to greater national economic efficiency. Also through learning by doing the imported technology has diffused throughout the economy leading to greater utilization of resources.

12) Social responsibility: Despite all odds and the commitment of resources and manpower to their ordinary business, some foreign firms still have time to devote to social responsibilities. For example, Coca cola company spends about N 1.5 million every year to sponsor sporting activities nationwide (Sporting NEWS, 2006). Guinness Nigeria plc has built three eye hospitals for the less fortunate ones in the society. The hospitals are located at Kaduna, Lagos and Onitsha. It is believed that with resources, technology food and trained manpower unevenly distributed throughout the world, FDI has the potential for bringing about a more equitable distribution of goods and services and improved living standard (Asheghian, 2004).

The inflow of external finance undoubtedly facilitated the expression of Nigeria's industrial sector to contribute more to GNP, the growth of the industrial opportunities and the improvement of the balance of payments. Foreign finance participation, which took the form of the foreign exchange, had the beneficial effect of directly relieving the foreign exchange shortage. At the same time, it directly operated in an anti inflationary manner by permitting more of the existing foreign exchange resources to be used to bring in consumer goods to lessen the pressure on the prices. These fundamental advantages are unique to foreign investments (Akino, 2004).

Methodology and Results :

In order to establish the significant impact of the FDI in the Nigeria banking to the economic growth, both data on the GDP of the country as published by the Federal Ministry of Statistics and the CBN (the apex bank of the country) and the GDP contribution by the foreign banks over the period of 10 years.

The sample of the study includes all foreign acquired banks and other such banks that are known to have foreign partnership abroad. Such banks as Citibank, Standard Chartered Bank, ECOBank, Stanbic Bank, NBM bank, Indo- Nigerian Bank and Habib Bank constitute the sample of the research. The samples are chosen from the list of banks operating in Nigeria.

At present, there are 28 operational banks in Nigeria with over 12% of such banks either wholly owned or partly controlled by foreign interests. Such banks are at the hub of the country banking institution. This has led the government to outlined plans of curbing the likelihood of the control of entire major Nigerian banks by foreign investors (Aderinokun & Eroke, 2007). The chart below gives illustrates the proportion of ownership in the banking industry of Nigeria.

Table 3: Banks ownership in Nigeria

Federal Government	2
State Government	4
Privately owned	81
Foreign investors	12
Acquired by Central Bank of Nigeria	1

Test of the Hypothesis:

Null Hypothesis: There is no significant impact of FDI in the banking sector to the economic growth of Nigeria.

In testing the above null hypothesis, the standard regression is used. Three main variables are used in the analysis. These include the GDP of the foreign banks (FORBANKS), the GDP of all other Nigerian banks (NIGBANKS) and the total GDP of the country (TOTGDP) which is also the dependable variable. The result is as stated below.

Table 4: Standard regression result

Dependant variable: GDP

Variables	t-value	Sig.
Constant	1.816	0.119
Foreign banks	5.272	0.002
Domestic banks	-0.393	0.071
VIF	1.06	
F-Value	15.01	
Mean	44.27	
Standard deviation	19.21	
R Sq	13.4	
ANOVA	0.004	

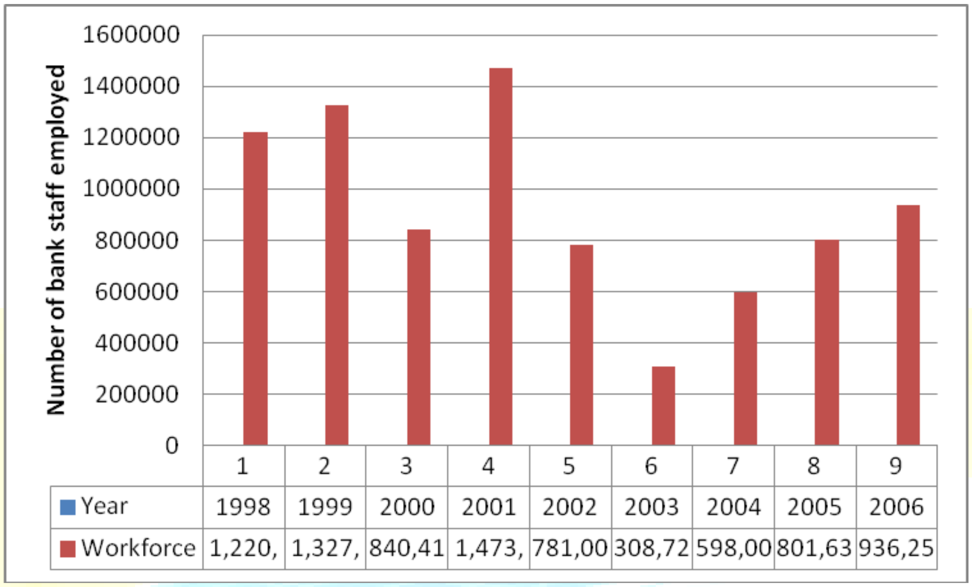
denotesignificance at 5% degree of freedom significance at 10% degree of freedom degree of significance

The regression result in Table 4 indicates that the **t- value of 5.272** suggest that the foreign banks have stronger impact on the GDP of the country than the other national banks which have a negative beta of **–0.393**. The **VIF value of 1.06**, which is above 1, shows that the variables are linear and their collinearity is satisfactory and adequate.

However, the GDP contributions of the foreign banks towards the economic growth are by no means futile. This is indicated by the ANOVA value of 0.004 which indicates **a sig. value of 0.004** and F-value of 15.01. Pallant (2006) indicates that a **sig. value below 0.05** is satisfactory and significant and shows the contribution of the variables. Thus, the result indicates that the foreign banks contribution is though insignificant but positive towards the country total GDP. Therefore, the above null hypothesis is rejected.

Another important factor in the FDI in the banking sector is the effect on the number of workforce in Nigeria. As shown in Figure 2 , the merger in the bank sector in Nigeria had some impact on the level of employment. There was a sharp drop in the number of personnel employed in the sector in 2000 from the over 1,327,850 to 840,419 employees. This was as a result of the number of failed or liquidated banks. The following year witnessed the swift changes in operational policy of banks coupled with the democratization of the polity. There expansion

Figure 2: Bank mergers and employment rate in Nigeria



Source: The Bank Watch Magazine, March, 2007.

As shown in figure 2, the merger in the bank sector in Nigeria had some impact on the level of employment. There was a sharp drop in the number of personnel employed in the sector in 2000 from the over 1,327,850 to 840,419 employees. This was as a result of the number of failed or liquidated banks. The following year witnessed the swift changes in operational policy of banks coupled with the democratization of the polity. There expansion and rebuilt of some banks including rise in number of community banks; which were licensed to grant limited amount of credit facilities to farmer and peasant traders. Thus, the number of employment rose to 1,473,084 (Bank Watch, 2007).

Events following the change of leadership of the CBN led to the instituting of the consolidation era. The banks were given a capital base target of twenty five billion naira (£100 million) which was difficult for some of the banks to meet up with. They were obliged to consolidate with others. The big foreign affiliate banks acquired most of the banks. By 2003, the number of employees shrank to 308,725 as most bank branches were closed down. But the number of bank employees has been on the rise from 598,000 in 2005 to 801,631 in 2006. Most of the new banks have acquired and resumed operations using the existing branch facilities of their acquired banks (Bank review 2006).

Summary of Discussion:

The findings and discussions in this study have been revealed some interesting issues of foreign direct investment particularly in the banking sector of Nigeria. Some reasons have been adduced from the reviewed literature on the mechanism and investment of multinational companies in Nigeria particularly in the banking sector.

A number of reasons have been adduced in the literature as the cardinal factors in FDI in the banking sector. Such reasons range from palatable environment to good economic climate. The mergers and acquisitions in the sectors have helped in consolidating the banks and positioning them in competitive market.

The foreign banks are yet to made significant contribution to the economic growth of the country despite the huge investment in the sectors. This may be as result of the repatriation of profits to their foreign countries, which does not help the Nigerian economic growth.

The Nigerian economy offers more than palatable environment for foreign investors to exploit. The huge merger activities in the banking sector have been unprecedented resulting in consolidated banking system that has become very competitive. The impact on the employment is also worrisome as 20% of the bank employees have lost their jobs during the process (CBN 2007).

The present issues in FDI have departed from the concept of viewing it as a matter of capital inflow to exploit by firm in foreign market. These views also have varying empirical implications. It goes beyond the flow of capital from rich to poor countries. Just as Markusen (2002) points, FDI could establish the fact that multinational banks can be established in skilled labour countries and have their investments concentrated in such territories

Conclusions:

In the past, the uncertainties of the political and economic situation in the country over the past decades made it very difficult for economic indicators to play their role in attracting FDI and in dictating the trend of the economy. The lawless behavior of some business also deterred some vital decision of foreign investors. Some Nigerians have not helped matters as they have constituted themselves into a log in the wheel of progress of the country in the bid to make a quick wealth by collaborating with some foreign investors in defrauding the country in some ways.

Economic climate of Nigeria when stabilized will go a long way in encouraging existing FDI and also attract new ones. The political stability of the country has much to do with the stable operations of FDI in the country. FDI has both positive and negative effect on the economy of the country. The positive contributions include capital transfer to the country, creation of employment; though the employment level declined following the mergers and acquisition in the industry. Other contributions include higher standard of living brought about by higher salary and good working conditions.

The bad impact on FDI on the Nigerian banking system as highlighted is the strict competition it has subjected the domestic banks. There are also concerns that foreign banks are making attempts to acquire and control the most viable domestic banks. This concern has led the CBN to formulate policy that will ensure restriction in ownership and acquisitions by foreign bank investors.

Although the study has shown that FDI in the banking system has made no significant contribution to the economy of Nigeria measured by the GDP of the country, it however reveals some interesting contributions achieved in the industry through FDI. The government policies on business are aimed at encouraging foreign direct investment and at the same time achieve economic development.

Recommendations:

1) The government regulation and legislation guiding business can be reviewed to create conducive business environment for the attraction of foreign investors.

2) Government should carryout enlightenment campaign in host communities of FDI with the aim of managing the FDI for rural and national development and ensuring mutual co-existence.

3) Government needs to stabilize the Nigerian Economy so as to encourage existing FDI and attract new ones.

4) The Federal Government through it agencies should monitor the operations of the foreign investors in Nigeria to check against acts of unpatriotism and culprits prosecuted.

5) Government should continue to welcome genuine foreign investors who are ready and willing to invest in any sector of the economy. Such investors should however be asked to operate within the limit of the regulations as provided by the Nigerian Investment Promotion Council (NIPC).

6) Any mergers and acquisitions in the banking sector should be approved by the government or its agencies. Care should be exercised to ensure that such acquisitions do not involve the control of the main stream banks in the country. Foreign investors should be encouraged to acquire community and other rural banks to help develop and establish the banking system in the rural areas communities.

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