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Monetary Policy And Deposit Money Banks Lending In Nigerian Economy

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ABSTRACT
The study examined monetary policy and deposit money banks lending in Nigeria Economy between 1986 and 2021. The study used Ex-Post factor research design and it employed a quantitative technique of data analysis using ARDL model. Variables adopted for the study included bank lending rate, broad money supply, monetary policy rate, exchange rate, and inflation rate. The study adopted the Keynesian theory. Data derived from the Central Bank of Nigeria statistical bulletin and the World Bank development indicators were subjected to the Augmented Dickey Fuller (ADF) and Phillip-Perron (PP) unit root test techniques for stationarity determination. The model was estimated using the ARDL modelling approach. The study concludes that monetary policy has an adverse effect on bank lending of deposit money banks in Nigeria. This finding is in line with the Keynesian school of thought who emphasizes the role of money, but involves an indirect linkage between money and aggregate demand through interest rate thereby, making the money supply an ineffective tool for credit control in Nigeria. The ineffectiveness of the money supply variable on the lending ability of domestic money bank, further attests to the fact that the CBN is less interested in using money supply to tackle bank lending, instead, the CBN is more interested in using interest rate targeting through the monetary policy rate and exchange rate to control the lending potentials of deposit money banks in the economy. The study recommends among others, that the Central Bank of Nigeria (CBN) should efficiently harness bank-specific components such as enough capital, dependable risk management efficiency, and strong macroeconomic management of the economy, the currency rate, and the inflation rate is essential for the development of lending capabilities of the domestic money banks in Nigeria.
Keywords: Monetary Policy, Bank Lending , Deposit Money bank, Nigeria Economy.

INTRODUCTION

The vitality of a nation's banking sector is a key determinant in shaping the trajectory of its economic development (Kolapo 2019). Bank Lending in Nigeria has advanced from the primitive system to a more flexible and digital enabled system for a faster, reliable and more convenient process. There is no doubt that the lending activities of financial institutions are essential tools in the monetary transmission mechanism. Banking institutions, similar to other organizations operates with the primary goal of maximizing profits for all of its stakeholders (Solomon 2012).

The current influence of monetary policy on the aggregate lending operations of deposit money banks in Nigeria is a matter of apprehension. In light of this government put more efforts to augment the lending capacities of Deposit Money Banks (DMB) and to foster efficient lending practices with the aim of attaining strong economic performance, poverty alleviation, and developmental stability (Olofinlade 2021).

In the work of Okafor (2009), the efficacy of monetary policy depends on the stability of the financial organizations that are accountable for its execution. Furthermore, the objective of monetary policy since 1986 till date is to control and minimize inflation to a single-digit level, ensure full employment level, favourable balance of payment, and to improve economic growth. In order to ensure a stable exchange rate of the Nigerian currency, it is essential to focus on promoting industry and fostering economic growth (Meshak & Nyamute 2016).

In addition to this, the Central Bank, which is also known as the apex bank has continued to ensure the financial sector's stability as well as the robustness of the banking system. This has been accomplished through making certain that monetary policy actions are efficiently transmitted to the real economy, as well as enhancing the efficiency of the payments system. In July 2004, a 13-point reform agenda was implemented in the banking sector, with the primary focus being the establishment of a minimum capital base of 25 billion naira for DMB (Ibeabuchi, 2007). This measure was undertaken to enhance the resilience of the banking sector and reinforce the benefits of monetary policy.

Furthermore, the CBN implemented several measures; such as cash reserve requirements, exchange rate fixation, capital requirements, and the supervision of deposit money institutions, in order to effectively maintain monetary stability (CBN 2012). By utilizing deposit availability and loans facilities the deposit money institutions have consistently attempted to limit the effect of liquidity transmission. However, these endeavours have not yet reached their maximum efficacy (Ekpung et al 2015). Monetary policy has traditionally placed a key emphasis on achieving and preserving a favourable internal and external balance of payments position.

Prior to 1986 and after then, monetary policy has gone through two distinct epochs. The first stage centred on strict monetary policies, whereas the current phase is driven by market forces. The Monetary Policy Rate (MPR) continued to serve as a major instrument that the Bank uses to transmit the stance of monetary policy and administer it. The monetary policy rate dropped from 13.5 to 12.5 percent in May 2020, resulting in a 100 basis point decrease; nevertheless, the asymmetric corridor around the MPR, consisting of +200 and -500 basis points, was not altered. The (MPR) decreased by an additional 100 basis points, bringing it down to 11.5 percent in September 2020. The asymmetric corridor surrounding the MPR changed from having a range of +200/-500 basis points to having a range of +100/-700 basis points. This was done in an effort to provide additional growth assistance in the wake of the devastation caused by the COVID-19 pandemic.

LITERATURE REVIEW

Conceptual Review

2.1 Monetary Policy

Ezeuduji (1994) defines monetary policy as the policy which involves the adjustment of money stock (through different means), interest rate, exchange rate as well as expectation to influence the level of economic activities and inflation in desired direction, targeting as the mapping up of excess liquidity armed at ensuring a non-inflationary macro-economic environment.Monetary policy entails a policy strategy which the Central Bank employs to control the supply of money stock so as to achieve general macroeconomic goals such as Balance of Payments (BOPs) equilibrium, price stability, economic growth and development, and income redistribution (Atuma & Eze, 2017).

2.2 Bank Lending

Bank Lending is the process by which financial institutions or banks provide funds to borrowers. The institutions that lend out the funds are the lenders, they typically receive interest in return for the loan collected (Okafor, 2011). Lending is a prominent service offered by banks to their clients. The duration of

the loan may vary based on the borrower's needs, with options ranging from short-term to medium-term or long-term. Essentially, banks extend loans and advances to individuals, commercial enterprises, and governmental bodies, enabling them to engage in investment and development endeavours that contribute to the overall economic progress of a nation (Olofinlade, 2021).

2.3 Deposit Money Banks

Deposit money is bank an institution that provides financial services, including issuing credit facilities in various forms, receiving deposits of money, lending money processing transactions and creating credit to enhance financial performance in return (Campbell, 2007).

2.4 Theoretical Review

The study adopted the Keynesian Theory based on the "General Theory of Employment, Interest, and Money" (Keynes, 1936). According to the Keynesian system, monetary policy operates by influencing the interest rate, which in turn impacts on the investment choices of various financial institutions, including banks, as well as the general public, and, as a result, production and income via the multiplier process. According to Keynes's theory, it is the job of the government to stabilize the economy, as well as to keep full employment and sustain economic growth. These goals may be accomplished via the use of fiscal policies. As a result, he suggests using an appropriate combination of monetary and fiscal strategies in order to accomplish monetary goals (Olofinlade 2021).

The Keynesian monetary strategy prioritizes the role of money by creating a hidden relationship between money and aggregate demand via the use of interest rates. From an analytical standpoint, when the economy is initially in a state of equilibrium, the Central Bank of Nigeria (CBN) may enhance the reserve of deposit money banks and increase overall bank reserves by engaging in an Open Market Operation (OMO), whereby government assets are purchased on the open market. Stated differently, the economy will reach a state of balance. Subsequently, the financial institution will proceed to either originate fresh loans or augment its bank credit in order to restore its target ratio to the desired level (Olofinlade 2021).

The provision of these supplementary loans generates the formation of fresh demand deposits, hence resulting in an augmentation of the money supply (MS). An expansion in the money supply is accompanied by a concomitant reduction in the aggregate interest rate. Consequently, this fosters an environment conducive to investment. In contemporary times, central banks have a greater propensity for using interest rate targeting as opposed to the traditional approach of targeting the quantity of money in circulation. Within a financial framework referred to as a corridor, the Central Bank has the responsibility of establishing two distinct rates, namely the rate at which compensation is paid and the lending rate. The lending rate refers to the interest rate imposed by the Central Bank on loans obtained by commercial banks, while the payment rate denotes the interest rate offered by deposit money banks on the reserves they hold at the Central Bank. When the rate is hiked, the bank's ability to lend money to consumers is significantly harmed. The Central Bank of Nigeria has used a range of monetary policy tools, including interest rates, liquidity measures, money supply adjustments, and cash reserve ratios, to regulate the quantity of money in circulation and influence banks' lending capacity. The implementation of credit rationing and the tightening of monetary policy would result in a reduction in the volume of newly issued loans by financial institutions (Olofinlade 2021). This idea is proposed in consideration of the aforementioned, since it aligns with the results of the study inquiry.

2.5 Empirical Review

Dare and Okeya (2017) performed a research to investigate the impact of monetary policy on the operational results of commercial banks in Nigeria. The researchers conducted a case study primarily targeting the United Bank for Africa (UBA) Plc. The findings of the study indicate that there is a positive relationship between the MPR and ROA variables in the chosen bank. However, it is important to note that this connection does not reach a level of statistical significance. The findings of the research indicate that there were non-significant and adverse relationships between the capital adequacy ratio (CRR), the loan-to-deposit ratio (LR), and the return on assets (ROA). The results of the research indicate that the absence of statistically significant relationships seen might perhaps be attributable to the inadequate level of compliance shown by commercial banks in adhering to monetary policy regulations.

In their study, Ndubuaku et al. (2017) conducted research to examine the effects of different monetary policy regimes on the performance of deposit money banks in Nigeria. The gathered data was analyzed by using regression analysis and the Pearson Product Moment Correlation approach. The findings indicate that in the period prior to the implementation of the Structural Adjustment Programme (SAP), the monetary policy rate had little influence on the aggregate value of assets, the accumulation of deposits, the facilitation of loans and advances, and the allocation of credit to the private sector. However, it became apparent in the period after the implementation of the Structural Adjustment Programme (SAP) that the monetary policy rate had a significant impact on several economic indices.

In their study, Afolabi et al. (2018) investigated the relationship between monetary policy tools and the loans and advances offered by Deposit Money Banks in Nigeria. The findings of the research suggest that changes in the framework of the monetary policy system have a statistically significant positive impact on the loan and advances provided by Deposit Money Banks in Nigeria. The study results have shown the presence of a bidirectional relationship between the Monetary Policy Rate (MPR) and the loan and advances provided by Deposit Money Banks in Nigeria.

Lateef et al. (2021) did a study to examine the correlation between lending rates and commercial bank lending in Nigeria. The research used macroeconomic time series data covering the period from 1980 to 2018. The research used the autoregressive distributed lag (ARDL) methodology and observed a statistically significant negative impact of inflation rate and interest rate on loans and advances. The findings from the Granger Causality test suggest that there exists a statistically significant relationship between the inflation rate and the loan rate in Nigeria. On the contrary, empirical evidence suggests that the interest rate has an insignificant influence on the inflation rate in Nigeria. Therefore, it is essential for the monetary authority to prioritize the maintenance of a cautious interest rate.

Olofinlade (2021) performed a recent research examining the influence of monetary policy on the ranging from 1984 to 2020. The primary focus of this research is to thoroughly investigate the direct influence of monetary policy on the overall lending operations of Nigerian deposit money institutions. The findings of the research demonstrate a robust and favourable correlation between monetary policy rate, money supply, and exchange rate, as well as the aggregate lending to the private and public sectors by deposit money institutions in Nigeria. Nevertheless, empirical evidence suggests that inflation has a minimal and statistically insignificant influence on overall loan activity lending practices of deposit money banks.

In their study, Demehin (2021) examines the relationship between monetary policy and the interest rates offered by deposit money banks in Nigeria for lending purposes. The major source of secondary data used in this inquiry was the statistics bulletin produced by the Central Bank of Nigeria. The scope of the study included the period from 1987 to 2018. The research findings reveals that changes in monetary policy rates may influence lending rates, indicating that the implementation of efficient monetary policies may have a substantial impact on fostering steady economic growth in Nigeria.

RESEARCH METHODOLOGY

3.1 Research Design

The research design used is Ex-post factor research design. It enables the researcher to look at how the independent variables influence the dependent variable. It utilizes secondary data spanning the time period of 1986 to 2021 using time series data. The research utilizes the combination of inferential and descriptive statistics to analyze the time series data that would be deployed. The process of descriptive statistics entails the computation of the standard deviation and the mean of the variables. Contrarily, inferential statistics was used to estimate a multiple regression model in order to examine the effect of money policy on the lending activities of Commercial Banks in the country.

3.2 Data Required

The study used data on monetary policy rate, inflation, money supply and exchange rate against bank lending rate in the Nigerian economy. It annual time series data is from the year 1986-2021**.**

3.3 Source of Data

The data were sourced from Central Bank of Nigeria Statistical Bulletins of various years (CBN). The study also used data from World Bank Development Indicators for its analysis (WBDI).

3.4 Method of Data Analysis

This work employed a quantitative technique of data analysis using ARDL method. It used (ADF) for Unit root test. The study also, conducted descriptive statistics to ascertain the behaviour and characteristics of the data included in the model.

3.4.1 Descriptive Statistics

The descriptive and inferential statistics are very important preliminary test conducted before any test on the variables, The descriptive data test was undertaken to determine the nature of the parameters; specifically, it was used to determine whether or not the variables follow a normal distribution in terms of their mean, median, maximum, and lowest values, as well as their deviation from the standard. The Jarque-Bera predictability values serve as the basis for the decision rule that determines whether or not the null hypothesis should be accepted. On the other hand, when the value gotten from the Jarque-Bera probability is higher than 0.5, we adopt the alternative proposition, which states that the variables have a normal distribution and may be estimated using the fitting procedure.

3.4.2 Test of Stationarity or Unit Root Test

The research utilizes the Augmented Dickey-Fuller (ADF) unit root test to examine the existence of a unit root, given the unlikelihood of the stochastic term being white noise. This ADF unit root test incorporates addition of delayed term of the dependent variable to address the issue of autocorrelation.

3.4.3 Definitions and Measurement of variables

Types of var.	Var.	Description	Measurement and justification
Dependent Variable	BL	Rate that banks lend money out (BLR)	Lowest interest rate that banks lend money to customers. Measured in rate.
Independent Variable	MS	Money Supply (MS)	Measured by the broad money in circulation using the Naira
Independent Variable	MPR	Monetary Policy Rate (MPR)	The interest rate established by the Central Bank of Nigeria (CBN) functions as a benchmark rate for transactions conducted inside the interbank money market. The measurement is expressed as percentages.
Independent Variable	EXR	Exchange Rate (EXR)	The exchange rate at which a foreign currency will be converted into the local currency. Measured using the U.S dollar to Naira exchange rate.
Independent Variable	INF	Inflation Rate (INF)	Continuous rise in a nation's products and services prices. Rate-measured.

Source; Author's Computation

3.5 Model Specification

The research study conducted by Okoye and Eze (2013) on the impact of bank lending rates on the performance of depositor's banks in Nigeria presented as followed. BE = *f* (LR, MPR) was adapted.

The model has been adapted in order to align with the specific model requirements of this research investigation. Therefore, it is asserted in the following manner:

$$BLR_t = f(MS_t, MPR_t, EXR_t, INF_t) \quad (3.1)$$

Where;

BLR_t = Bank lending rate in time

MS_t = Money Supply in time

MPR_t = Monetary policy rate in time
EXR_t = Exchange Rate in time
INF_t = Inflation Rate in time
Where:
Ut = Error term
β1 –β4 = Parameters to be estimated
The explicit form of the model (3.1) is written as below:

$$BLR_t = \beta_0 + \beta_1 MS_t + \beta_2 MPR_t + \beta_3 EXR_t + \beta_4 INF_t + U_t \quad (3.2)$$

3.5.2 The ARDL model

$$\Delta LnBLR = {}_0 + Ln + Ln + LnLn\Delta Ln + \Delta Ln\Delta Ln\Delta Ln\Delta Ln\theta ECM_{t-i} + \quad (3.3)$$

Where:

The null hypotheses are as below:

H_0: ${}_0 = {}_1 = {}_2 = {}_3 = {}_4 = = 0$ (No long term correlation exist)

are the long run multipliers (parameters), ${}_0$ is the intercept (the drift component); ,are the short-run parameters, θ is the coefficient of speed of adjustment while ECM_{t-i} is the speed of adjustment and is the stochastic error term.

4.1. DATA PRESENTATION

Appendix 6 contains this study's presentation of the data that was utilized in the investigation. The bank lending rate (BLR), broad supply of money (M2), money policy rate (MPR), Exchange Rate (EXR), and Inflationary Rate (INF) were the variables that were analyzed for this research. The analysis for this study began with the descriptive statistics, which included a summary statistic of the quantitative behaviour of the variables that were incorporated into the model. In addition, the Augmented Dickey Fuller (ADF) and Phillips-Perron (PP) unit root tests are conducted so as to validate the data used in the research and ensure that they were stationary.

Table 4.1: Descriptive statistics

Skewness	0.825	0.405	1.791	1.049	1.738
Kurtosis	4.847	1.523	5.101	3.719	4.700
Jarque-Bera Probability	1.200 0.310	4.257 0.119	25.868 0.000	2.378 0.225	22.457 0.000
Obs.	36	36	36	36	36

Source*:* Author's estimated result.

4.2 Descriptive Statistics

Table 4.1 shows an overview of descriptive information that was reported in this investigation. The evidence shown in the table demonstrates that BLR, M2, MPR, EXR, and INF all have a positive skewness. As a result, the distribution of the research data scattered along the right side or tail, which represents the fact that this data from their frequency distribution is dominated by positive values.

In addition, the kurtosis measure for the distribution of the variables are captured in Table 4.1. As a precondition, the kurtosis of the series is regarded normal if the value of its distribution is 3, relatively normal if it exceeds 3 (i.e., leptokurtic), and negative excess kurtosis or less normal if it falls below 3 (i.e., platykurtic). Hence, Table 4.1 reveals that BLR, MPR, EXR, and INF are leptokurtic while M2 is platykurtic. Also, the normality test conducted for each series using the Jarque-Bera statistic procedure demonstrates that while BLR, M2, and EXR variables are normally distributed, MPR and INF are not normally distributed.

Table 4.2: ADF unit root test

	ADF Test at Level			**ADF Test at 1st Difference**		
	With Constant	With Constant & Trend	Without Constant & Trend	With Constant	With Constant & Trend	Without Constant & Trend
	-1.213	-2.194**	-0.442	-6.543***	-6.770***	-6.651***
	-1.643	-1.659	-0.494	-3.748***	-3.667**	-3.862***
	-2.847*	-3.377*	-1.795*	-5.142***	-6.749***	-5.262***
	3.066	1.038	4.703	-2.340***	-3.024***	1.663*
	-4.659***	-2.699	-1.691*	-2.554	-6.671***	-2.475**

Where *, **, *** indicates significance at 10%, 5%, and 1% respectively, and *l* is the logarithm operator.
Source: researcher's estimated output

Table 4.3: PP unit root test

	PP Test at Level			**PP Test at 1st Difference**		
	With Constant	With Constant & Trend	Without Constant & Trend	With Constant	With Constant & Trend	Without Constant & Trend
	-1.016	-0.558	-0.398	-6.625***	-6.892***	-6.738***
	-1.685	-1.923	-0.490	-3.112**	-3.061	-3.257***
	-2.892*	-3.352*	-1.578	-7.298***	-6.935***	-7.682***
EXR	3.373	1.356	5.088	-2.392**	-2.690**	-1.623*
	-2.905*	-3.377*	-1.497	-7.122***	-6.574***	-7.450***

Where *, **, *** indicates significance at 10%, 5%, and 1% respectively, and *l* is the logarithm operator.
Source: researcher's estimated output.

4.3 Unit Root Test

Before engaging in any economic analysis, a critical step in the process involves ascertaining the level of stationarity of the data being employed. This will help to guide the researcher in any empirical conclusion that is to be taken. The ADF together with PP unit root tests were applied in this investigation to assess the degree of stationarity shown by the variables included in the analysis. The outcomes of the unit root examinations are shown in Tables 4.2 and 4.3. The crucial unit root analysis used tests with a constant, tests with a constant and trend, and tests without a constant and trend.

As shown in Table 4.2 is the ADF unit root outcome, and also Table 4.3 is the PP unit root result. Table 4.2 demonstrates that MPR and INF are level stationary variables. However, a further probe for stationarity showed that BLR, M2, and EXR are first difference stationary variables. Similarly, the PP unit root approach reveals that MPR and INF are I(0) series while BLR, M2, and EXR are I(1) stationary variables. Therefore, this research submits that with exception to MPR and INF that are level stationary series, BLR, M2, and EXR are first difference stationary series. Thus, the ADF together with PP unit root tests significantly reinforced the output of each other.

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

The purpose of this investigation work was to investigate the impact that monetary policy has in the lending practices of Nigeria's commercial banks between the years 1986 and 2021. Four theories were considered by this research and they were the commercial loan theory, monetarist school of thought, loanable fund theory, and the Keynesian school of thought. The variables used in this analysis included the bank lending rate, the broad supply of money, monetary policy rate, the rate of exchange, and the inflation rate. The data that were utilized in this research work were gotten from the statistics publications of the CBN and the development indicators that were provided by the

World Bank. In order to determine stationarity, the data were put through the Augmented Dickey Fuller (ADF) and Phillip-Perron (PP) unit root examination procedures.

Furthermore, the limits cointegration approach was used to ascertain the enduring connection that exists between the independent parameters. Moreover, the study used the ARDL modelling approach to estimate the findings. A comprehensive series of diagnostic tests was conducted, including assessments for normalcy, serial correlation, heteroscedasticity, and the Ramsey reset test. In addition, an ARDL modelling technique was applied in order to provide an estimation of the outcomes of the study.

There were a total of four diagnostic tests carried out, and these included the normality, serial correlation, heteroscedasticity, and Ramsey reset tests. They were used in order to evaluate the accuracy of the estimations provided by the study. In addition, a stability test utilizing the cumulative sum alongside cumulative sum squared techniques was carried out; the results of this test revealed that the research model is stable and may be used for the purpose of making policy recommendations.

5.2 CONCLUSION

The conclusion of this research work is that monetary policy has a negative effect on bank lending by Nigerian deposit money banks. This result is consistent with the Keynesian school of thought, which concentrated on the function of money and entails a hidden relationship between money and aggregated demand through the rate of interest. Ineffectiveness of the money supply variable on the lending capacity of domestic money banks is further evidence that the CBN is less interested in using money supply to combat bank lending. Rather, the CBN is more interested in using interest rate targeting via the monetary policy rate alongside exchange rate to regulate the lending potentials of commercial banks in the economy.

Furthermore, a growing inflationary trend in the short-term and its influence on the lending potentials of banks triggers detrimental effects of monetary policy variables such as financial policy rate alongside exchange rate in the capacity of banks to lend money in the long-term. This is because of the feedback loop between the two factors. In conclusion monetary policy instruments can work better in the Nigerian banking sector if all the variables can be made effective especially the money supply to give a better result.

5.3 RECOMMENDATIONS

Based on the deduced conclusion drawn from the findings of the study, it is advisable that the apex financial institution in the country which is the Central Bank of Nigeria (CBN) should undertake diligent surveillance of the micro-level dynamics of individual bank behaviour. This measure is recommended by the primary motive of augmenting the efficacy of monetary policy in the manufacturing sector in Nigeria, considering that the majority of domestic banks in the country possess the ability to safeguard their loan portfolio from monetary contraction. Moreover, the data pertaining to the banking industry may be used as an input to assess the prospective impact of forthcoming adjustments in interest rates on the economy.

In a similar vein, harnessing bank-specific components such as enough capital, dependable risk management efficiency, and strong macroeconomic management of the economy, the currency rate, and the inflation rate is essential for the development of lending capabilities of the domestic money banks in Nigeria.

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