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DOES FINANCIAL STRUCTURE DEVELOPMENT DRIVE ECONOMIC PERFORMANCE? THEORETICAL AND EMPIRICAL EVIDENCE FROM NIGERIA

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ABSTRACT

The paper questions the extent to which financial structure development theoretically and empirically drives economic performance in Nigeria. It adopts mixed methodological framework to tease out the relationship between financial structure development and economic performance. In terms of theoretical exploration, the paper recognizes the critical nature of the financial system and outlines it role in driving economic growth. This paper integrates Bwire and Musiime (2006) and Ajadi Adegbite and Ajadi (2008) models to develop an alternative model that fits into the reality of Nigerian financial and economic environment. The study relies on secondary data and ordinary least square method to analyze the relationship between financial structure development and economic performance.

The paper discovers that financial system is necessary for economic performance but outline some policy issues which distorted the potency and significant posture of the financial system in accelerating economic performance in Nigeria.

The main contribution of this paper to knowledge lies on its robust engagement with debates on financial structure development and the link between finance and economic growth. This knowledge enhances our understanding about diverse models which shape financial development in theory and practice.

In conclusion, the paper highlights pragmatic policy implications which will facilitate better relationship between financial systems and economic performance in Nigeria.

Key Words: *Development, Economy, Growth, Intermediation, Performance and Structure*

I. Introduction

The role of financial structure in accelerating economic performance has long been recognized by many scholars in financial system. Prominent among them was Schumpeter (1934) who acknowledged the positive link between financial structures through entrepreneurial development and economic growth. Followers of this proponent are Gurley and Shaw (1955), Gurley (1967), Goldsmith (1969), Patrick (1966), Grigg (1971), Cameron (1972). These early work generated great interest in the study of financial structure development both in the developed and developing countries (see: Mckinnon 1973; Shaw 1973; Ojo 1974; Taylor 1980; Gertler and Rose 1991; King and Levine 1993; Stiglitz 1993; Levine 1997; Aziakpono and Babatope-Obasa 2003; Rajan and Zingales 1998; Haslag and Koo 1999 and Khan 2000).

Financial structure is made up of rules, regulations, institutions and arrangements that facilitate the flow of funds from the surplus unit to the deficit sector. Generally, the financial system is divided into money and capital market. The money market is the short term end of the financial market while the capital market provides arrangement for long term funds. However, the importance of financial structure on economic performance is not quite clear. Some authors such as Hicks (1969) hold the view that financial structure plays crucial role in the mobilization of capital for development. On the other hand, there are scholars who hold contrary view. The issues and problems of financial structures are always in focus because of importance of the financial sector on economic performance. The financial structure is critical as such, the industry is heavily regulated, being a services industry where products traded are mostly non physical items which are mostly susceptible to fraud. The financial structure is founded on trust and it growth depend on the volume of financial transactions undertaken with trust and confidence with minimum risk which require sound financial structure practices. Unlike most other business, the failure of the financial sector has far implications for the whole economy. The confidence and trust that the financial system of an economy enjoys could be shaken to its foundation when a single operator within the financial sector fails. Hence, failure of the financial system would erode people's confidence on the financial structure.

The benefits accruable from a healthy and well developed financial structure include savings mobilization and efficient financial intermediation roles. Besides, through the financial intermediation functions of the financial intermediaries; the surplus unit as well as the deficit side are linked together to reduce transactions and search costs. Further, they create liquidity which drives the economy by borrowing short term and lending long-term. In addition, financial structures reduce information costs and reduce risk involved in financial transactions through risk and portfolio management services offered to their customers. More so, the financial institutions bring the benefits of asset diversification to the economy. Besides, they mobilize saving from atomized individual for investment thereby solving the problem of indivisibility in financial transactions and finally mobilized savings are invested in the most productive venture irrespective of the source of the saving. Following the accrued benefits of financial intermediation which extend to the large economy, there is need for financial development, particularly where the system is considered underdeveloped in order to increase the size of domestic savings channeled through the formal financial sectors, ensure efficiency of intermediation process and promote the effectiveness of monetary policy.

Therefore, this paper questions the role financial structure development plays in driving economic performance in Nigeria. Apart from the general introduction, the paper unravels the theoretical and conceptual thoughts which shape financial structure development discourse in theory and practice. The next section highlights the review of financial structure development in Nigeria in order to reveal various changes that have taken place within the Nigerian financial system. The section that follows presents the structure of the Nigerian financial system to understand the role various institutions play in the operation of financial system. In subsequent sections, the paper explains the methodological framework that governs the study and finally presents the results that follow from the data collection.

II Theoretical and Conceptual Nexus of Financial Structure Development

The role of financial structure from different theoretical approaches is necessary in order to understand how financial structure development accelerates economic performance. The debate on financial structure development and the link between finance and economic growth is usually preceded by detailed thumbprint of theories of financial development. The underlying facts of these theories are presented below.

Demands follow and supply leading: the demand following referred to the role of financial structure in the process of development as been passive and financial structure develops out of the market needs. Patrick (1966), Greenwood and Jovanovic (1990) supported this view. The scholars note that financial institutions merely react to the demand of financial services. This argument differs from the reasoning of Ryan and Zingales (1998) who argue that financial structure development may predict economic performance because financial market anticipate growth, and hence the dynamics of financial structure development could be a supply leading where financial institutions are positively active in devising and providing financial service for the real sector in anticipation of demand. Historically, Nigeria, borrowed from Great Britain epitomizes demand following type of financial institutions. While Japan and Germany adopted supply leading financial development. Patrick (1966) however noted that the phenomenon is not likely to be static through the different stages of economic development. Thus the scholar remarked that before sustainable industrial growth gets under way supply leading would induce real innovative type of investment. As the process of real growth occurs, the supply leading impetus gradually become less important and demand following financial response become dominant.

Financial Repression: Mckinnon (1973) and Shaw (1973) view constraints to economic growth arising from financial repression. The scholars assert that, the role financial structure plays in economic development is nothing but growth inducing except if repressed. According to the apostle of financial repression hypothesis, the sources of repression are government legislations and policies such as legal restriction on activities and interest rate policy that distort the full operation of the market mechanism. Nigerian financial structure was repressed prior to the adoption of structural adjustment program in 1986. The sources of repression are direct monetary approach such as selective credit guidelines, ceilings on credit expansion, interest rate controls and use of reserve requirement. Thus access into banking business was limited and government owned financial institutions dominated the financial system.

Structuralist Theory: This theory is based on the study of Gerschenkron (1962). The kernel of Gerschenkron theorist is that the roles financial system plays in the economic progress of a country basically depend on the structure of the economy. In the work Gerschenkron, the writer classifies countries at the threshold of industrialization in a list with very advanced countries at the top and most backward countries at the bottom. Based on historical perspective of the financial structure particularly at the point of European countries industrialization, economy like Great Britain have limited role for financial institutions but place much reliance on internal finance of the entrepreneurs. The moderately backward economy such as Germany relied heavily on the financial structure for economic progress due to limited financial resources available to most business. However, financial structure is insignificant but attributed greater role to public sector for economic progress of the most backward countries. The development of Russia is perhaps inevitable from this description of that country's economic and financial environment at the point of industrialization. The scarcity of capital in Russia was such that no financial institutions could conceivably succeed in attracting sufficient funds to finance a large scale business. The standards of honesty in business were so disastrously low. The general distrust of the public is so great, that no bank could have hoped to attract even small capital funds as were available, and no bank could have successfully engaged in long-term credit policies in an economy where fraudulent bankruptcy had been almost elevated to the rank of general business practice. Gerschenkron's description of Russia can be replicated today for many developing countries. Although this description may fit most countries particularly Nigeria, unfortunately this implied prescription is irrelevant for two major reasons. First, commercial banks in these countries already have a substantial strangle-hold on the financial resources of the economies as the main financial intermediary. Second, the governments of these countries, having elected the capitalist path of development, fashionably described as mixed economy, have not now the political will to undertake the unpalatable decision of centralizing economic decision making.

Circuit Theory: Bossone (1998 and 2000) in articulating the circuit theory of finance incorporated a microeconomic dimension into the theory. Central to the circuit process is the complementary functions of banks and non-banking financial intermediaries in originating money and making it circulate in a manner beneficial to all agents. The implication is that those financial systems where money and capital market functions are segmented but rudimentary or absent as in many developing economies are prone to circuit malfunctioning and instability. Rajan and Zingales (1998) pointed out that it is the availability of investment opportunities that drives growth. The scholars added that, the exante development of financial markets facilitates the expost growth of sectors dependent on external finance and concluded that the link between financial development and growth is one by-product of the theory of financial markets and institutions, which reduce the cost of external finance for firms.

A sound financial structure is the engine that drives economic performance through entrepreneurship growth as noted by Schumpeter (1934). Others like Goldsmith (1969) Mckinnor (1973) and Shaw (1973) also acknowledged this view through positive response of saving to interest rate. Green Wood and Jovanovic (1990) developed a model in which financial structure and economic performance are endogenously determined. They scholars stressed that by pooling idiosyncratic investment risk and eliminate uncertainty about rate of return; financial structure can stimulate faster economic progress.

Bencivenga and Smith (1991) postulated that financial structure particularly banking sector would enhance economic growth by channel saving to the activity with high productivity but offering and illiquidity assets while allowing the individuals to reduce the risk associated with their liquidity needs. The upshot of these studies is that financial structure leads to stronger economic performance. Levine and Zervos (1998) noted slow economic performance recorded particularly in the developing countries may not be unconnected with underdeveloped and repressed financial structure, policy description of Mckinnor and others therefore places faith in undistorted perfect market as the principle mechanism that lead to macroeconomic stability promote investment and economic performance. Reoubini and Sala-i-Martin (1992) cited in Aciakpono (2003) postulated that financial structure, if repression would slow down the productivities of capital, reduce saving and hamper economic performance. Ojo (2006) noted that the provision of financial services in Nigeria has been poor in term of needed finance to foster economic and industrial performance. Akintola-Bello (2006) examined the financial structure reform and economic development within the context of pension reform in Nigeria and concluded that the financial sector has potential impact on economic growth.

Ziorklui (2001) examined the impact of financial sector development banks efficiency and financial deepening for sustainable savings mobilization within the context of Ghana financial system. In his study he adopted financial ratio analyses and parametric statistical method for the examination of policy research questions using both primary data and secondary data collected in Bank of Ghana on measure of Banks efficiency, risk measurement, capital adequacy, financial intermediation, management competence earning and profitability, liquidity management and market share analysis. The findings reveal that financial structure development had considerable impact on the capacity of the Ghanian banking sector to mobilize savings and thereafter enhance economic performance. In term of financial deepening, the study shows that individual real assets holding declined despite significant progress in financial intermediation.

Tella (2006) discovers that Nigerian economy has witnessed continuous and extensive structural reforms. Many of the reforms have affected the financial structure and the country's economic performance. He identifies some of the challenges bedeviled with management of financial institution in sustaining economic performance. These are poor asset and liability management, unprofessional behaviour of bank owners and managers, excess liquidity, growth of non bank financial institutions, persistent fiscal deficit, unstable political environment and vulnerability to systemic risks. In conclusion, the author suggested that the challenges of management of Nigeria financial system could be tackled through appropriate legal framework, corporate governance and robust portfolio approach to sustain economic performance.

Akingunola and Adegoke (2006) argue that economic problems in Nigeria mirror deep concern considering the avalanche of strategies and measures reflecting various thoughts implemented to achieve development. The authors stress that recapitalization directive in 2005 by the central Bank of Nigeria has resulted into mergers and acquisitions. The study looked into merger and acquisition as capitalization option and banks reconsolidation experience in Nigeria. The study explores secondary data and adopted descriptive-cum-comparative analytical method. Finding of the study reveals that poor performance of financial sector particularly the banking system in sustaining economic performance in Nigeria may not be unconnected with the low capitalization of the sector and the expectation of the emerging mega banks to impact positively on economic performance.

Somoye, Awotundun and Bakare (2006) posit that financial structure is critical for accelerated economic growth and development. The scholars identify some of the recent development in the Nigeria financial system and developed a model using total credit, total deposit and prime lending rate as a measure of financial system development in sustaining economic performance. Findings of the research shows that financial system particularly banking sector would perform better in improving economic performance if financial reforms are further strengthened to capture the expanded segment of the financial system.

Somoye, Awotundun, Bakare and Subair (2008) assess the capital market reforms and the development of Nigerian's financial sector within the context of the contribution of Nigerian stock exchange to the overall economy. The research employed ordinary least square method to investigate basic operational indices of stock market performance, economic growth and development. The study reveals that market reforms had positive impact on the development and performance of the Nigerian stock exchange. Marked improvement occurred in all the indices evaluated after market reform was instituted but the level of improvement was however not significant enough when compared to change in overall economy. Thus, the contributions of the stock exchange to our economy remain low even after market reforms.

Ojo (2007) highlights main features of financial sector mal -adaptation, the expected role of financial structure in economic performance, the resource curse and financial sector mal-adaptation link. The paper collected data on revenues generation in Nigeria, growth performance in Asia and Sub-Sahara Africa countries (SSAC), indicators of economic performance and governance in Botswana and Sub-Sahara Africa and other group of countries. The findings of the paper show that the expected role of mature financial structure is to appropriately adapt the mobilization and utilization of huge financial resources emanating from petroleum exploitation in Nigeria which would impact positively on the economic and social development of the country such that the natural resources curse imposed by petroleum could have turned out to be a blessing. However, he postulated from the data collected that the oil boom has become a doom to constitute development dilemma manifested in form of high level of poverty, poor impact of reform on economic and social transformation and mass exodus of Nigerians to other countries. The scholar recommended the need to evolve new financial culture, productive management and utilization of petroleum resources, diversification of the economy and the apex monetary authority should take positive measures and make development a priority task.

How does Financial Structure Promotes Economic Performance?

The existence of an institution and its associated market in a society is a clear indication that such institution offers valuable services for the progress of the economy. This line of argument could be true for virile financial system. Development economist have postulated that finance and market play critical role in advancing economic performance, by enhancing financial strength of individual and group economic activities through: (i)Mobilization of savings particularly of the house hold sectors (ii) Financialization of savings that is to say saving transform into investment (iii) ensure the most efficient allocation of these savings to the other sectors of the economy (iv) providing reliable payment mechanism to various economic agents and (v) enabling economic agents to pool trade and price risk. (vi) increase the fraction of societal resources devoted to interest yielding assets and long run investment which in turn argument economic growth (vii) enables investor portfolio diversification by providing insurance and prefect monitoring information.

The extent to which financial structure efficiently mobilize saving and channel saving into investment by eliminating costly distribution to production process reduce fraction of society savings held in unproductive liquid assets and economize holding of non- performing assets e.g (cash under the pillow) to improve economic performance. The process of efficient financialization of saving between savers and investors, gathering information about viable projects, monitoring the projects in which depositors funds are invested are growth inducing dimensions. The financial system also provides business advisory service such as insurance to risk averse savers and investors in the process of pooling individual savings and enabling investors to hold a diversified portfolio with varying liquidity characteristics and protect premature liquidation of the firm's capital in which they invest. It is clear that, the capacity of the financial structure to perform its functions effectively is to large extent, determined by the financial health of the individual institutions themselves and the soundness and viability of the economy.

How does Economic Performance Sustain Financial Structure?

Economic performance appears to aid financial structure development. Some scholars hold the view that finance aids economic performance while others postulate that economic performance triggers financial development. The linkage between financial structure and economic performance is obvious. The financial structure performs intermediation function. However, the size and robustness of the real sector determine the volume of resources that can be mobilized and invested. Put differently, the greater an economy, and the greater would be the volume of financial intermediation. This is because as the economy follows the path of growth, several financial institutions crop up to provide variety of financial services. Consequently, innovation and expansion in financial services would be demand driven until economic growth goes beyond certain threshold of modern banking habit. The demand driven approach postulated by Patrick (1966) shows that economic performance trigger financial structure development. Thus growth in an economy influences variety of financial services found in an economy.

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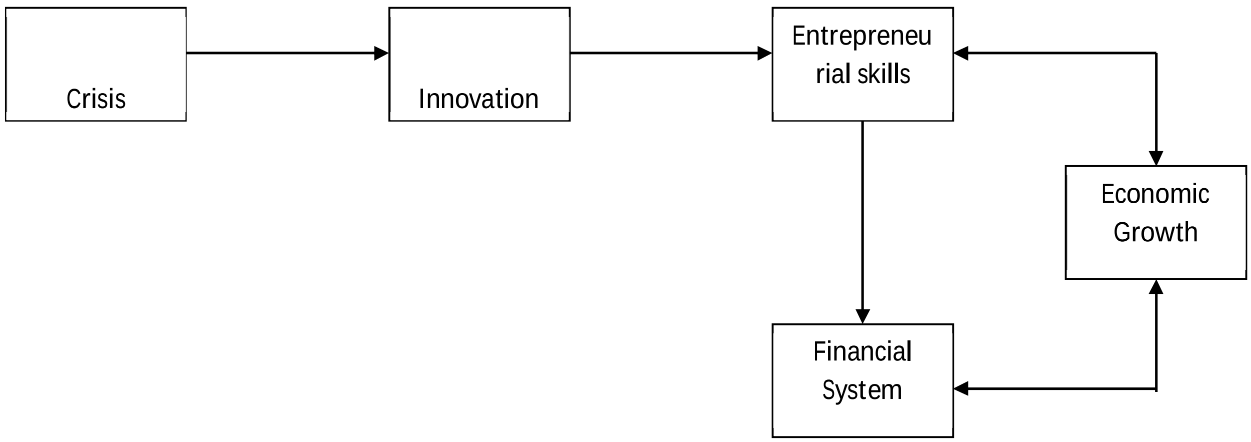
Financial Structure and Economic Performance Model

The diagram in Figure (2) shows financial structure and economic performance model. It illustrated the path of economic growth as postulated by Schumpeter (1934). Growth in an economy is a product of crisis which could be political, economic, technological, cultural and international in nature.

Figure 2

Financial Structure and Economic Performance Model



Source: Authors modification from Schumpeter (1934)

Crisis within a society if positively tapped as shown in the diagram would propel innovative thought, generate ideas and redefine vision and mission of existing institutions in the society. Innovation would be sharpened by knowledge and information to develop entrepreneurial skills. If the entrepreneurial skill is backup or supported by financial system there would be economic growth.

This model has performed creditably in most developed countries like, Great Britain, United state of America, Germany etc. However, the reverse is the case in Sub-Sahara African countries (SSAC) particularly Nigeria, where the path of economic growth sometime thwarted. Financial system failed to provide adequate credit for the small and medium scale enterprise as reveals in measure of financial deepening

III. Review of Nigerian Financial Structure Development

Prior to independence, the Nigerian financial system was under-developed. Most of the complex ramifications, which are integral part of the financial system, were not there. The central Bank was established two-year before independence and up to 1952 there was little or no regulation of the financial system. What existed then was the regime of free banking system of which the result was catastrophic. Large scale banks failure triggered off, consequently the 1952 banking ordinance was promulgated. The introduction of the Banking ordinance marks the beginning of era of regulation of financial system. Most of the recommendations of the banking ordinance were in line with the strengthening of banking regulation and supervision. Subsequently the banking act was amended in 1969 and 1978 respectively. Thus, the financial system was repressed. In order to meet the needs of the country for rapid economic performance, the financial system review committee otherwise known as the Okigbo Panel was set up in 1976 to examine the adequacy, relevance or otherwise of the institutions and the structure of the financial system. The committee recommended a number of practical policy measures amongst which the federal government accepted to implement the following:

i. The establishment of securities and exchange commission;
ii. The establishment of the Nigerian Stock exchange to replace the Lagos Stock Exchange
iii. State and local government as well as state owned corporations to be encouraged to float their own bonds in the securities market.
iv. As part of the effort to improve the monetary management advisory functions of the CBN, all financial institutions are required to make returns of their financial information to the CBN.
v. Setting up of more commercial bank branches in the rural areas of the country.
vi. A comprehensive programmes for training and manpower development in the banking system;
vii. Strengthening of the banking legislation to reflect the distinction in practice between commercial and merchant banks and
viii. Increased banking supervision and regulation to encourage specialization of financial institutions.

Inspite of Okigbo panel recommendations, the financial system was subjected to intense regulation up till 1986. Some authors described period between 1976 to 1985 as era of stiff regulation while other scholars define the period as 1952 through 1986.The measures and controls introduced at the inception of the financial structure development produced distortion which retarded economic progress thereby creating an environment described as financial repression which discouraged savings stimulated current consumption, provided damaging scope for corruption, encouraged inefficient investment and unproductive or non-performing loans which impaired the health of the financial system as noted by Oke (1993).Consequently comprehensive financial sector reforms which was part of structural adjustment programme (SAP) was adopted in 1986 .

The main financial policies applied were deregulation of interest rates and exchange rate, liberalization of access into banking business. Other reform measures included, establishment of Nigeria Deposit Insurance Corporation (NDIC), strengthening the regulatory and supervisory institutions, upward review of capital adequacy standards, capital market deregulation and introduction of indirect monetary policy instruments. Some distressed banks were liquidated while the central bank took over the management of others. Government share holdings in some banks were also sold to the private sector. (See Nnana, 2002 for the details and the sequencing of the reform measures). The expectation of this policy is to increase reliance on market forces, promote competition in the economy, encourage greater deposit mobilization, improve access to credit and promote the economic growth. But these have not happened in many cases. A lot of unholy deals and practices also surfaced and before long we had the bank distress.

The desire to ensure that the core mission and vision of the apex bank made it necessary for central bank of Nigeria in 2004 to implement 13 point proposal. Top on the list was minimum capital base of N25 billion at the time when some banks were still battling with the extant of N1 billion, phased withdrawal of public sector funds, consolidation of banking institution, adoption of a risk focused and rule based regulatory frame work. Others are automation of the returns rendition process, establishment of hot line for direct access to the CBN governor, enforcement of contingency planning framework for systemic banking distress, establishment of asset Management Company for distress resolution, enforcement of dormant laws in the banking system, revision and updating of relevant laws for effective operation of banks. Other measures are closer collaboration with the economic and financial crimes commission (EFCC), the enforcement of the anti-money laundering and other economic crime measures and rehabilitation and effective management of the mint to meet the security printing need of the country.

After the implementation, the number of banks fell from 89 to 25 big banks and now 23 banks as at 2009. Other development in the financial system during Soludo era are new CBN act, the contagion effect of the consolidation on other part of financial industry, appointment of foreign reserve managers and money market dealers, the micro finance revolution, the establishment of credit referral companies, the post consolidation code of corporate governance and the financial system strategy FSS 2020. The aftermath of Soludian agenda is that it has not been well with the industry the financial system remains highly oligopolistic in nature and crisis in some of the banks put consolidation on trial. The margin loan crises

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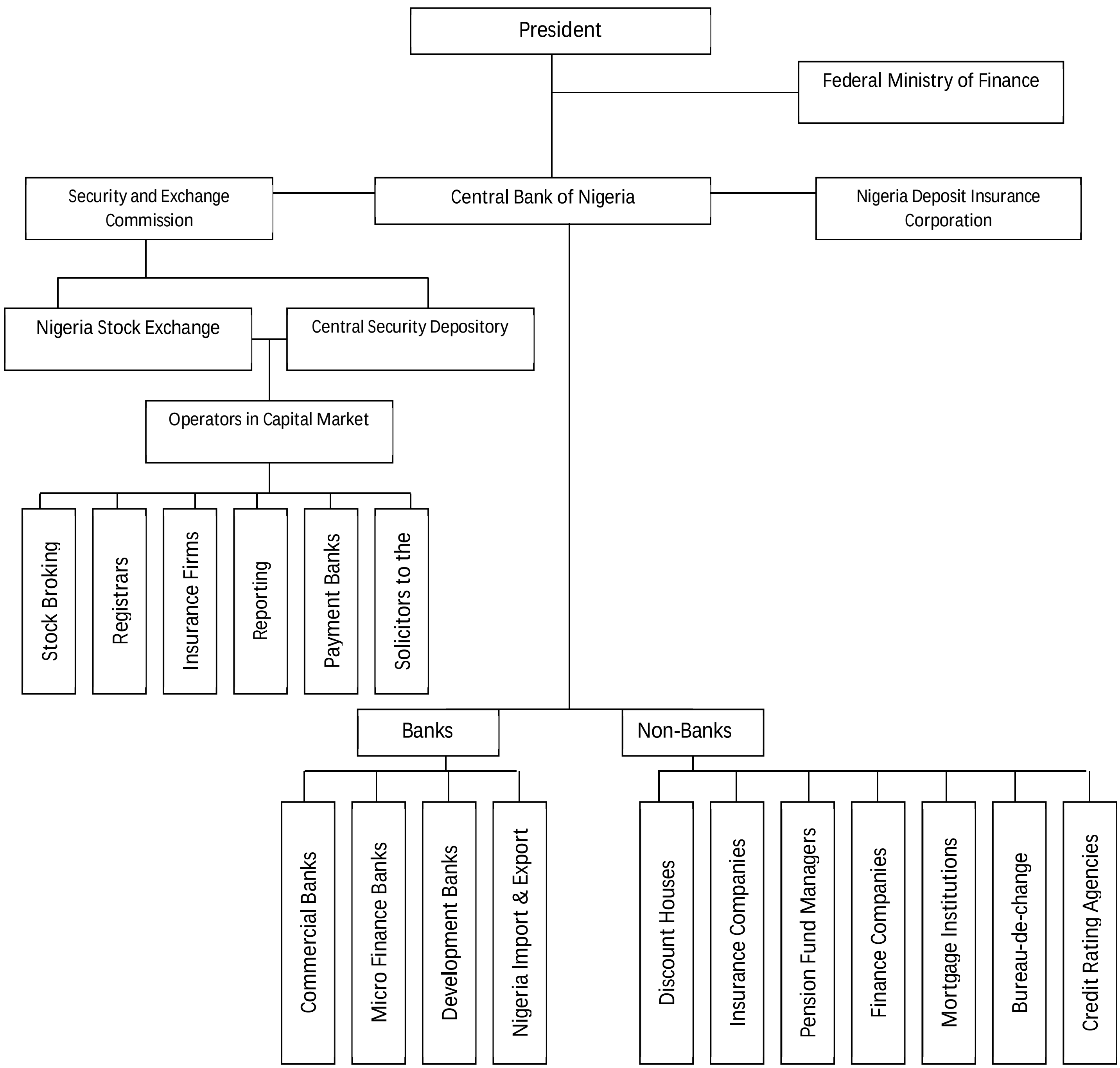
which shows that financial structure was maladapted, the devaluation of the naira, the on going global financial meltdown and other panicky measures were the response to Solodian hypothesis. In September 2009, the central bank of Nigeria reviewed the performance of the existing banks and discovered that some of the banks were not healthy due to high volume of non performing loan which were not collaterised. Consequently, the board of the affected banks was dissolved and interim management was appointed to run the activities of these banks with N500 billion injected to bail out these banks from distress which generated several reactions at the national assembly about the power of central bank to bail out distress banks.

IV. Structure of Nigerian Financial System

The Financial system is made up of institutions and entities which can be identified and classified in a number of ways. Basically, the Nigerian financial system can be divided into formal and informal financial system (see figure 1).

STRUCTURE OF NIGERIA FINANCIAL SYSTEM



Informal financial system is very important within the context of African countries and its finance are provided by institutions which are not regulated and unlicensed which may or may not be outlawed. The operators in the Nigeria informal financial market are cooperatives, credit and theft association, professional money lenders and pawn brokers.

The informal financing dominates the activities in the rural areas, and compliment the activities of formal financial systems. Agriculture and small scale industrial enterprises are the principal sectors which seek finances from the informal sector. However, the informal lending has some drawbacks among others are small scale nature of operations, limited range of services provided, fragmented markets and exorbitant interest rates, technical inability to assess viable projects in non traditional way thereby ruling out the financing of new activities which are not popular.

Development in the Nigerian financial sector has provided mechanism through which the informal financial system could be linked to the formal financial system through encouragement of operators in the informal financial market to have bank accounts, use informal lenders to mobilize deposit at some nominal fee and promotion of semi formal banking institution like micro finance banks.

Formal financial system comprises of the Central Bank of Nigeria (CBN) as the apex monetary authority in Nigeria, the Nigeria Deposit Insurance Corporation (NDIC) protecting the depositor interest in the banking sector and the Security and Exchange Commission (SEC) monitoring and regulating the activities in the Nigerian capital market. The CBN report directly or indirectly through the Federal Ministry of Finance to the Office of the President, which represent the financial public sector and giant financial institution in the system. Its role includes generating resources for other institutions in the system and final regulator of the system.

The CBN as the apex monetary authority control and regulate the activities in the money market. The Nigerian money market is made up of banking and non banking financial institutions. The banking sub sector of the money market comprises Commercial Banks operating retailing and wholesale banking business. We also have the Microfinance Banks performing the banking business at the community level. There is Developmental Banking Institution made up of Bank of Industry (BOI), Federal Mortgage Bank (FMB) and Nigerian Agriculture Development Bank (NADB). Other institutions in the Nigeria banking sector are Nigeria Import and Export Banks (NEXIM). The non banking financial institutions are the Discount Houses, Finance Companies, Insurance Companies, Pension Funds Managers, Primary Mortgage Institution and bureau-de-change. The Nigerian capital market is under the control of Security and Exchange Commission assisted by Nigerian Stock Exchange to provide arrangement for buying and selling of shares, stock and bond, while the Central Securities Depository (CSD) act as the clearing house of the Nigerian Stock Exchange. Operators in the Nigerian capital market are Stockbroking firms who are dealing members of the Nigerian Stock Exchange, the Registrars which are firms that deal directly with the stock broking firms acting on behalf of investor or shareholders. Others are Solicitors representing the legal counsel to the issues at the floor of the Nigeria Stock Exchange, the Reporting Accountants which provide necessary and reliable financial information in respect of company seeking quotation at the floor of the (NSE) and the Insurance Company acting as the under writers to the issues.

IV. Methodology

Many studies have been conducted on the financial development and economic performance. Some of these studies relied on Nigerian data. Ajakaiye and Odusola (1995) examine the relationship between the real deposit rates and financial savings mobilization as a measure of economic performance in Nigeria. They adopted model specified by Fry (1978) as follows:

Gfs/y = f (g, rr, sf/y, exr)

Where :

Gfd/y	=	The ratio of gross domestic financial saving to GDP
g	=	Growth rate of real GDP
rr	=	Real deposit rate of interest
sff/y	=	Ratio of foreign savings to GDP
exr	=	Exchange rate

Apriori expectation being b_1, b_2, $b_3 > 0$ and b_3, $b_4 < 0$. Their findings revealed that positive link exist between deposit rate and saving mobilization which improved economic performance during period of financial repression while it was negative during period of deregulation. The revelation of the model also confirmed that saving mobilization required not real deposit rate but other policies measure such as foreign saving and exchange rate movement indeed are crucial for economic performance.

Adewumi (1981) using Harrod – Domar model represented by the following equation.

K = ky ------------------------ (1)

$\underline{dk}$ = sy ----------------------- (2)

dt

Where: k = capital stock

y = National Income

s = Saving propensity

k= capital –output ratio

The equation (1) states that there exist a fixed relationship between stock of capital and production. While equation (2) denotes the theoretical expected equality between the rate of increase in capital stock and saving. Given the two phenomena, Adewunmi (1981) used time series data to find the evidence of association between growth in real sector and monetary sector using correlation analysis. The result of the finding suggested that positive, but strong association exist between the real sector and the monetary development.

Ajadi, Adegbite and Ajadi (2008) relied on Beck, Demirguc-Kunt and Levine (2000) model which measure whether or not economic growth and financial sector development correlates. The set of data tested using spear man's rank correlation analysis are:

1. The ratio of deposit money banks assets to central bank assets (DMCD)
2. Ratio of liquid liabilities to gross domestic product (LLGDP)
3. Ratio of Central Bank Assets to Gross Domestic Product (CBGDP)
4. Ratio of deposit money bank assets to Gross Domestic Product (DMGDP)
5. Ratio of bank deposits to Gross Domestic product (BDGDP)
6. Ratio of financial system deposit to Gross Domestic product (PSGDP)
7. Ratio of private credit by deposit money banks to Gross Domestic product (PCDM)
8. Ratio of private credit by deposit money banks and other financial institution to Gross Domestic Product (PCDO)
9. Ratio of stock market capitalization to gross domestic product (SMGDP)
10. Ratio of stock market total value traded to gross domestic product (SVGDP)
11. Ratio Of stock market turnover to gross domestic product (STGDP)
12. Rate of economic growth to growth in real per capital income.

Their finding revealed that the relationship between financial development and economic growth during the post Structural Adjustment Programme (SAP) was marred by policy reversals which resulted in poor performance of financial sector of the economy. Consequently financial development and economic growth have no consistent relationship in post SAP era in Nigeria.

Bwire and Musiime (2006) within the context of Solow growth theory specified the following model.

$$Gy = \beta_0 + \beta_1 FR_t + \beta_2 TCP_t + \beta_3 IRR_t + \beta_4 INF_t + \beta_5 DEF_t + \beta_6 EXR_t + \beta_7 POP_t + \beta_8 TEX_t + \beta_9 Dq_2 + E_t$$

Where Gy_t = economic growth; FR_t = Financial intermediation ratio provide by M_2/GDP; TCP_t = bank credit to the private sector as a ratio of GDP (a measure of financial development); IRR_t = real interest rate; INF_t = expected inflation rate; DEF_t = Fiscal deficits; EXR_t = exchange rate ; Pop_t = population; TEX = Total Export; Dg_2 = dummy variable and E_t = error term. From the equation it is expected that β_1, β_2, β_3, β_7, β_8 should be positive while β_5, β_6 are negative but β_4 is indeterminate.

The study used data collected from Uganda for period of thirty five (35) years adopted modern multivariate cointegration technique developed by Johansen (1988). Finding showed that supply-leading hypothesis hold for the case of Uganda. The study also confirmed that financial development is necessary but not sufficient condition for economic performance. Other policy measures such as fiscal discipline and trade policy were responsible for robust economic performance in Uganda.

This paper adopts Bwire and Musiime (2006) model. The model would also be modified with Ajadi Adegbite and Ajadi (2008) in order to meet the reality of Nigerian financial environment. By combining both models, the paper specifies the following relationships:

$G/E = f(EDM_2GDP, CPSGDP, ETTT, FATGDP, GDPGR, ER, DR, LR, \text{and } IR)$

$G/E = f(\beta_0 + \beta_1 EDM_2GDP + \beta_2 CPSGDP + \beta_3 ETTT + \beta_4 FATGDP + \beta_5 GDPGR + \beta_6 ER + \beta_7 DR + \beta_8 LR + \beta_9 IR + \mu)$

Gy/E = Gross domestic product to credit to small and medium scale enterprises

EDM_2GDP = Money supply M_2 to gross domestic product

CPSGDP = Credit to private sector to Gross domestic product

ETTT = Export to total trade

FATGDP = Financial asset to gross domestic product

GDPGR = Gross domestic product growth rate

ER = Exchange rate

DR = Deposit rate

LR = Lending rate

IR = Inflation rate

μ = Error term

b_1, b_2, b_3, b_4, b_5 and $b_7 > 0$; b_6 and $b_8 < 0$; while b_9 is indeterminate

The study collects secondary data from central bank of Nigeria (CBN), Security and exchange Commission (SEC), Nigeria Deposit Insurance Corporation (NDIC), Federal Office of Statistic (FOS) and others. The data collected comprises: gross domestic product, bank loan to small and medium scale enterprises, money supply (M_2), and credit to private sector, exchange rate, total export, total trade and inflation rate. The data collected span for 1992-2009. The ordinary least square (OLS) method would be adopted to estimate the various parameters of the model.

VI. Discussion of the Results

The linear regression result shows that economic performance measure by percentage of gross domestic product to bank credit to small and medium scale enterprises have positive relationship with measure of financial deepening (EDM2GDP), Financial widen (CPSGDP), export to total trade (ETTT) and gross domestic product growth rate (GDPGR) but negatively related to financial assets to gross domestic product (FATGDP), exchange rate (ER), deposit rate (DR), lending rate (LR) and inflation rate (IR).

The estimated parameters complied with theoretical expectation except financial assets to gross domestic product (FATGDP) and deposit rate (DR) which came out with wrong sign. The standard error of estimate revealed that all the estimated parameters were in-significant in determining economic performance except gross domestic product growth rate because the standard error computed is greater than half of the coefficient of the estimated parameter as shown in the table above. The co-efficient of determination (R^2) indicates is 0.973 indicates that there is a very strong positive linear relationship between the dependent variable and the explanatory variables. It also shows that 97% of the variation in Gy/E is explained by the explanatory variables for the period under consideration. The remaining 3% variation in the Gy/E is explained by other exogenous variables that are excluded in the models (error term). This implies that the coefficients are high as 97%. Therefore the models are good fit as only less than 3% of systematic variation is left unaccounted for by the model. Also, a brief look at the adjusted R-squared value of 92.3% indicates that after removing the effect of insignificant repressor' (explanatory variable), about 7.7% variation in the Gy/E is still accounted for by the explanatory variables. Therefore, the model is a good fit.

The conclusion under linear regression model is that the explanatory variables thought have effect on economic performance but insignificant in Nigeria. This made it necessary to find the result of an alternative model specification for further confirmation of the behaviour of the explanatory variables.

Presentation of the Result (Linear Function)

Variables	**Coefficient**	**Standard Error**	**t^2**	**Significance**
Constant	-12938.5	32464.639	-0.399	0.707
EDM2GDP	1402.134	766.094	1.830	0.127
CPSGDP	1001.793	981.010	1.021	0.354
ETTT	340.998	419.334	0.813	0.453
FATGDP	-396.380	456.715	-0.813	0.425
GDPGR	95.520	35.172	2.716	0.047
ER	-78.896	106.732	-0.739	0.493
DR	-805.546	1441.238	-0.559	0.600
LR	-749.430	883.897	-0.348	0.435
IR	-67.123	190.204	-0.353	0.739

Source: Data Analysis

R = 0.986

R^2 = 0.973

Adjusted R^2 = 0.923

Durbin Watson = 2.937

Presentation of Result (Logarithm Function)

Variables	Coefficient	Standard Error	T-test	Significance
Constant	3.414	2.464	1.386	0.225
EDM2GDP	1.135	0.520	2.183	0.081
CPSGDP	1.544	0.62-	2.490	0.055
ETTT	0.509	1.113	0.457	0.667
FATGDP	-0.990	0.206	-4.810	0.005
GDPGR	-0.047	0.093	-0.505	0.636
ER	-0.043	0.240	-0.179	0.865
DR	-0.032	0.608	-0.052	0.960
LR	-1.599	0.754	-2.121	0.087
IR	-0.101	0.237	-0.426	0.687

Source: Data Analysis

R = 0.978

R^2 = 0.956

Adjusted R^2 = 0.877

Durbin Watson = 2.286

F-test = -12.052

The table above presents the logarithm function of the dependent and independent variables, the result shows that economic performance has positive relationship with measure of financial deepening (EDM_2GDP), financial widen (CPSGDP) and export to total trade as discussed under linear model. However, the model also reveals that economic performance responded negatively to the percentage financial assets to gross domestic product (FATGDP), gross domestic product growth rate (GDPGR), exchange rate (ER), deposit rate (DR), lending rate (LR) and inflation rate (IR). The estimated parameters of the model came out with the right sign except financial asset to gross domestic product, gross domestic product growth rate and deposit rate which came out with wrong sign. This result is similar to that of linear regression model.

The standard error test of the estimated parameters for financial deepening (EDM_2GDP), financial widen (CPSGDP), financial assets to gross domestic product FATGDP and lending rate (LR) were significant at 95 percent confident internal with probability of 0.081, 0.055, 0.005 and 0.087 respectively showing that these parameters explained the variation in economic performance in Nigeria. This is because the standard error tests computed for each of these parameters were less than the half of the coefficient of the parameters.

The result also revealed that the percentage of export to total trade, gross domestic growth rate, exchange rate, deposit rate and inflation rate were not significant at 95 percent confident interval with probability of 0.667, 0.636, 0.865, 0.960 and 0.687 respectively. These parameters did not explain the variations in economic performance.

However the coefficient of determination represented by (R^2) shows that 95.6% of the explanatory variables predicted variation on economic performance and the remaining 4.4% was due to other factors. This position was also confirmed by adjusted R square.

The significant posture of financial deepening, financial widening lending rate gross domestic product growth rate and financial assets to gross domestic product to the measure of economic performance shows that financial sector would aid economic performance if properly developed. This result supported the postulation of Ziorkhu (2001) and Bwire and Musinne (2006). However, the insignificant posture of export to total trade, exchange rate, deposit rate and inflation rate shows the evidence of perverted financial system as indicated by Ojo (2007).

VII. Missing Link in Nigeria Financial System (Policy Issues)

The insignificant posture exhibited by export to total trade, exchange rate, deposit rate and inflation rate show that there is distortion in the path of economic performance in Nigeria. The distortion was compounded by poor governance, maladapted type of economics, weak institutional frame work, poverty and financial sector mal adaptation.

Poor Governance

The disconnection between wealth and poverty in Nigeria is governance as noted by Clinton (2009). The country experienced poor governance for several decades which resulted into collapse social infrastructure, corruptions and sharp practices among political class and circumvention of due process. Thus, the significance of export to total trade, exchange rate, deposit rate and inflation rate would be crippled and as such retarded economic performance while oil become the major sustenance of Nigerian economy.

Maladapted Type of Economics

The monolitic nature of Nigerian economy based on crude oil production with little or no serious effort to develop the real sector made successive government to mal-adapt Nigeria economy into distributive type of economy where revenue earned from the crude oil is only distributed among the various tiers of government while the government at local, state and federal level shared the oil wealth among the political class inform of emoluments, allowances, fictitious and over inflated contract pricing that do not impact on the lives of average Nigerians. Thus, the struggle for fair shares of the oil wealth has turned Nigerian political system into the survival of the fittest. These challenges negatively thwarted the significant posture of the explanatory variables and economic performance.

Weak Institutional Frame Work

Economic growth and development is anchored on the effectiveness of vibrant institutions. However, non-functionality and unco-ordinated institutions in Nigeria has rendered the potency of the independent variable used in the model formulated above very weak. From all indication, Nigeria is geometrically gravitated toward a failed state where it becomes extremely difficult to find workable institutions in the system. Experience has revealed that most of the institutions in Nigeria are characterized by high level of corruption, indiscipline and circumvention of due process.

Poverty

Poverty has been described as the bane of Nigeria economy characterized by high level of unemployment and wide income gap between the poor and the rich. These features sometime make it difficult to translate policy into action plan. In view of the endemic poverty in Nigeria, any deliberated policy to increase deposit rate to enhance the ability of financial system to mobilize funds from the surplus unit may not see the light of the day in the face of low level of income in Nigeria.

Financial Sector Mal-adaptation

The financial system could be maladapted type when the institutional structure, culture, orientation and operational pattern are foreign transplanted type and not appropriately adopted to suit the local environment as well as not made relevant to the developmental needs of the economy. Ojo (2007) noted instances of alien institutional practices not attuned to the peculiar needs and requirement of Nigeria environment and people; weak designed and strategies to provide financial services for small and medium enterprises (SME) and indigenous entrepreneurs that constitute the bulk of the economic unit and financial system dominated by commercial banks that are sluggishly reacted to industrial development but favourably disposed to retailing and commercial activities, as evidence of maladapted financial system in Nigeria.

The consequence of maladapted financial system is that banks and other financial intermediaries perform their financial intermediation functions inefficiently and contribute poorly to economic performance. Some time, measures taken by regulatory authorities to make the operators in the financial system change the unsatisfactory practices often become unsuccessful.

VII. Conclusion

The paper discussed the financial structure development and economic performance in Nigeria. It recognized the critical nature of the financial system in driving economic growth and development and outlines some functions which financial sector has to perform to become relevant in the process of economic development in Nigeria. Theories of financial development such as demand follows and supply leading financial repression, structuralist hypothesis and circuit theory were reviewed. The paper also reviewed the developments in the Nigerian financial system and clearly pointed out how financial structure aid economic performance and how economic growth could boost financial structure development. Model of financial structure and economic performance was also discussed. Such discussion clearly showed how the path of economic growth became thwarted. Selected literatures were reviewed and appropriate model was specified. The finding of the study shows that financial system is necessary for economic performance in Nigeria but attributed the insignificant posture of some of the estimated co-efficients to policy issues. In view of the findings, the paper recommends the following measures if financial sector is to drive robust economic performance in a developing economy like Nigeria:

i. Promotion of good governance at all levels of government and institutions, with stronger focus in the financial sector.
ii. Restructuring Nigerian economy from mal-adaptation into a more realistic local financial environment and adoption of policies that will propel the real sector to support the financial system.
iii. Promotion of due process and reduction of corruption and sharp practice for workable institutional framework.
iv. Reduction of the level of unemployment and adoption of pragmatic policy that will reduce the wide income gap between the poor and the rich
v. Adoption of financial structure and institution that is peculiar to our local need and environment.

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