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The Performances of Commercial Banks in Post-Consolidation Period in Nigeria: An Empirical Review

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Abstract

The current credit crisis and the transatlantic mortgage financial turmoil have questioned the effectiveness of bank consolidation programme as a remedy for financial stability and monetary policy in correcting the defects in the financial sector for sustainable development. Many banks consolidation had taken place in Europe, America and Asia in the last two decades without any solutions in sight to bank failures and crisis. The paper attempts to examine the performances of government induced banks consolidation and macro-economic performance in Nigeria in a post-consolidation period. The paper analyses published audited accounts of twenty(20) out of twenty-five(25) banks that emerged from the consolidation exercise and data from the Central Banks of Nigeria(CBN). We denote year 2004 as the pre-consolidation and 2005 and 2006 as post-consolidation periods for our analysis. We notice that the consolidation programme has not improved the overall performances of banks significantly and also has contributed marginally to the growth of the real sector for sustainable development. The paper concludes that banking sector is becoming competitive and market forces are creating an atmosphere where many banks simply cannot afford to have weak balance sheets and inadequate corporate governance. The paper posits further that consolidation of banks may not necessaily be a sufficient tool for financial stability for sustainable development and this confirms Megginson(2005) and Somoye(2006) postulations. We recommend that bank consolidation in the financial market must be market driven to allow for efficient process. The paper posits further that researchers should begin to develop a new framework for financial market stability as opposed to banking consolidation policy.

Keywords: Consolidation; Profitability; Real Sector; Financial sector

1. Introduction

The consolidation of banks has been the major policy instrument being adopted in correcting deficiencies in the financial sector. The economic rationale for domestic consolidation is indisputable. An early view of consolidation in banking was that it makes banking more cost efficient because larger banks can eliminate excess capacity in areas like data processing, personnel, marketing, or overlapping branch networks. Cost efficiency also could increase if more efficient banks acquired less efficient ones. Though studies on efficiency in banking raised doubts about the extent of overcapacity, they did point to considerable potential for improvement in cost efficiency through mergers. Consolidation is

viewed as the reduction in the number of banks and other deposit taking institutions with a simultaneous increase in size and concentration of the consolidation entities in the sector (BIS 2001)

The driving forces in bank consolidation include better risk control through the creation of critical mass and economies of scale, advancement of marketing and product initiatives, improvements in overall credit risk and technology exploitation. These drivers have led to improved operational efficiencies and larger and better capitalised institutions. The results of this policy are neither here nor there contrary to the policy expectation. The most difficult aspect of consolidation is the ones induced by government through mergers and acquisition. Furlong(1994) claimed that consolidation in banking is distinct from "convergence." He says that consolidation refers to mergers and acquisitions of banks by banks while convergence refers to the mixing of banking and other types of financial services like securities and insurance, through acquisitions or other means. He concluded that the impact of consolidation on bank structure has been obvious, while its impact on bank performance has been harder to discern.

The Government policy-promoted bank consolidation rather than market mechanism has been the process adopted by most developing or emerging economies and the time lag of the bank consolidation varies from nation to nation. Banking sector reforms are part of monetary policy instruments for effective monetary systems and major shifts in monetary policy transmission mechanisms in the last decade in both developed and developing nations. The banking sector in emerging economies has witnessed major changes to compete, attract international investment and increase capital market growth.

There are as many reasons and strategies for bank consolidation as there are banking jurisdictions. When the opportunities in the operating environment for banks, either within the boundaries of a country, an economic zone or geographical sphere, become amenable only to consolidated institutions, there is a tendency for market-induced consolidation. Many cases of bank consolidation that have been recorded to date in the modern history of banking are of this kind, and ready examples are the European and American bank mergers and acquisitions of the 1980s and 1990s. Market-induced consolidation normally holds out promises of scale economics, gains in operational efficiency, profitability improvement and resources maximization. The outcomes have however, not totally confirmed these supposed benefits and they have varied across jurisdictions, especially when compared with the particular pre-consolidation expectations.

Whatever the potential, the research so far on the effects of bank mergers has not found strong evidence, that on balance, merged banks improve cost efficiency relative to other banks. This does not mean that many mergers, including those of some large banks, have failed to lead to significant gains in cost efficiency. It just means that the outcomes for those banks tend to be offset by problems encountered in other mergers, and that many banks have improved cost efficiency without merging.

A new view is that bank mergers are not just about adjusting inputs to affect costs; rather, they also involve adjusting output (product) mixes to enhance revenues. Two research efforts taking this approach are Akhavein, et al. (1997), covering mergers in the 1980s, and Berger (1998), covering mergers in the 1990s. These studies find that bank mergers do tend to be associated with improvements in overall performance, in part, because banks achieve higher valued output mixes. While these studies do not track all of the channels through which bank mergers affect the value of output, they suggest that one channel has been banks' shift towards higher yielding loans and away from securities. This channel is particularly interesting given the other results in these studies. They find that merged banks also tend to experience a lowering of their cost of borrowed funds without needing to increase capital ratios. The lower cost of funds is consistent with a decline in the overall risk of the combined bank compared to that of the merger partners taken separately. This apparently occurs even though a shift to loans by itself might be expected to increase risk. One interpretation of these results, then, is that a merger can result in a reduction in some dimensions of risk, which then affords the post-merger bank more latitude to shift to a higher return, though perhaps higher risk but output mix. The sources of diversification could be differences in the range of services, the portfolio mixes, or the regions served by the merging banks.

The objective of the paper is to review the effectiveness of bank consolidation programme in the banking and the real sectors of the economy. This will enable us recommend appropriate policy mix. The paper is structured into six(6) sections. Section one(1) is on introduction; section(2) is on literature review, while section three(3) deals with the evolution of the Nigerian banking sector. Section four(4) is on experience from other countries, while section five(5) is on post-consolidation performance of the banking sector and economy. Section six(6) in on conclusion and recommendation.

2. Literature Review

Reforms are predicated upon the need for reorientation and repositioning of an existing status quo in order to attain an effective and efficient state. There could be fundamental bottle-neck that may inhibit the functioning of the institutions for growth and the achievement of core objectives in the drive towards enhancing and sustaining the economic and social imperatives of human endeavor. Carried out through either government institutions or private enterprises, reform becomes inevitable in the light of the global dynamic exigencies and emerging landscape.

Consequently, the banking sector, as an important sector in the financial landscape, needs to be reformed in order to enhance its competitiveness and capacity to play a fundamental role of financing investment. Many literature indicates that banking sector reforms are propelled by the need to deepen the financial sector and reposition for growth, to become integrated into the global financial architecture; and involve a banking sector that is consulting with regional integration requirements and international best practices.

The nexus between consolidation and financial sector stability and growth is explained by two polar views. Proponents of consolidation opined that increase size could potentially increase bank returns, through revenue and cost efficiency gains. It may also, reduce industry risks through the eliminations of week banks and create better diversification opportunities. On the other hand, it is argued that consolidation could increase banks' propensity towards risk taking through increases in leverage and off-balance sheet operations. Furlong(1994) stated that an early view of consolidation in banking was that it makes banking more cost efficient because larger banks can eliminate excess capacity in areas like data processing, marketing, or overlapping branch networks. Cost efficiency also could increase if more efficient banks acquired less efficient ones. Though studies on efficiency in banking raised doubts about the extent of overcapacity, they did point to considerable potential for improvement in cost efficiency through mergers.

Banking reforms involves several elements that are unique to each country based on historical economic and institutional imperatives, for example, in Hungary. Evidence show that the reforms in the banking sector was due to highly under-capitalization of state owned banks; weakness in the regulatory and supervisory of deficiencies in the corporate government behaviors of banks.

Craig and Hardee(2004) conducted investigation on bank consolidation and concluded that as the banking consolidation continues, "relationship" lending is becoming increasingly rare. As credit scoring and formal, formulaic methods are used more and more, specifically by the large banks, many small businesses may find out that they do not "fit" the model, especially those enterprises with negative equity. Thus, small businesses may be filling the financing void that is being created by the bank consolidation with non-bank sources of funds.

Hughes and Mester(1997) provide evidence to suggest that there are scale economics in banking, bank managers are risk averse, and banks use the level of their financial capital to signal the level of risk. This is an area of interest in Nigerian banking, especially when the return on equity is calculated in another two to three years and then compared with the historical industry average. Rhoades(1996) reported that American banks consolidated in response to the removal of restriction on bank branching across states, while Hughes, J.P; W. Lang; L.J. Mester; C.G. Moon(1998) concluded that the economic benefits of consolidation are strongest for those banks that engaged in interested expansion, and in particular the expansion that diversifies macroeconomic risk. Evidence has shown of

that that domestic merger improved profitability and operational efficiency, but cross-border (national, not interstate) acquisitions were a surer sources of cost efficiency.

Hughes J.P; Mester, L.J; and Moon, C.G(2000) also provide evidence that scale economies exist in banking but they fail to account for risk. Thus, scale economies that result from consolidation and diversification do not produce better performance in banking, unless choice makes the bank's management more conscious risk and moderates its decisions and actions appropriate larger scale of operation that leads to diversification only reduce liquidity and credit risk under the ceteris bus assumption, and they argued that this is not always. The implication for bank consolidation in Nigeria bank is whether the bigger (not yet mega) banks will set good balance between growth and risk management. However, evidence has shown that consolidation exercise leads to more banks to be established in the long run therby return back to the status quo. The examination of merger and acquisition in European banking and found that industry consolidation was beneficial (by providing social benefits) in the first economic integration stages, but could damage welfare in the more advanced stages as the few big banks safeguard price agreements to forestall foreign competition. The other side to European mergers and acquisitions was because of the possibility of failure. This, of course, ignores the fact that no bank can ever be too big to fail. All it takes for a bank to fail is for "bad news" about a bank to get to its stakeholders (especially depositors) and they all walk in at the same time to take their funds! For such bank to survive, it must have sufficient liquid assets to meet all maturing and long-dated obligations.

Perhaps the most important social benefit that Nigerian banks (after the first round of consolidation ended 31st December 2005) would confer on the banking public and the national economy is a sharp drop in lending rates but later rose beyond pre-consolidation period. There is the likelihood that fewer and colluding banks (especially during the second phase of consolidation that is envisaged) will pursue their own business interests more than they would the national or social interest.

3. The Evolution of the Nigerian Banking Sector

The banking operation began in Nigeria in 1892 under the control of the expatriates and by 1945, some Nigerians and Africans had established their own banks. The first era of consolidation ever recorded in Nigeria banking industry was between 1959-1969. This was occasioned by bank failures during 1953-19590 due mainly to liquidity of banks. Banks, then, do not have enough liquid assets to meet customers demand. There was no well-organized financial system with enough financial instruments to invest in. Hence, banks merely invested in real assets which could not be easily realized to cash without loss of value in times of need. This prompted the Federal Government then, backed by the World Bank Report to institute the Loynes commission on September 1958. The outcome was the promulgation of the ordinance of 1958, which established the Central Bank of Nigeria(CBN). The year 1959 was remarkable in the Nigeria Banking history not only because of the establishment of Central Bank Nigeria(CBN) but that the Treasury Bill Ordinance was enacted which led to the issuance of our first treasury bills in April, 1960.

The period (1959–1969) marked the establishment of formal money, capital markets and portfolio management in Nigeria. In addition, the company acts of 1968 were established. This period could be said to be the genesis of serious banking regulation in Nigeria. With the CBN in operation, the minimum paid-up capital was set at N400,000(USD$480,000) in 1958. By January 2001, banking sector was fully deregulated with the adoption of universal banking system in Nigeria which merged merchant bank operation to commercial banks system preparatory towards consolidation programme in 2004.

In the '90s proliferation of banks, which also resulted in the failure of many of them, led to another recapitalization exercise that saw bank's capital being increased to N500million(USD$5.88) and subsequently N2billion(US$0.0166billion) on 4th 2004 with the institution of a 13-point reform agenda aimed at addressing the fragile nature of the banking system, stop the boom and burst cycle that characterized the sector and evolve a banking system that not only could serve the Nigeria economy,

but also the regional economy. The agenda by the monetary authorities is also agenda to consolidate the Nigeria banks and make them capable of playing in international financial system. However, there appears to be deliverance between the state of the banking industry in Nigeria vis-à-vis the vision of the government and regulatory authorities for the industry. This, in the main, was the reason for the policy of mandatory consolidation, which was not open to dialogue and its components also seemed cast in concrete.

In terms of number of banks and minimum paid-up-capital, between 1952-1978, the banking sector recorded fourty-five(45) banks with varying minimum paid-up capital for merchant and commercial banks. The number of banks increased to fifty-four(54) between 1979-1987. The number of banks rose to one hundred and twelve(112) between 1988 to 1996 with substantial varying increase in the minimum capital. The number of banks dropped to one hundred and ten(110) with another increase in minimum paid-up capital and finally dropped to twenty-five in 2006 with a big increase in minimum paid-up capital from N2billion(USD$0.0166billion) in January 2004, to N25billion(USD$0.2billion) in July 2004(see Table I)

Table I: Minimum Capital Requirement and Number of Banks in Nigeria(1952-2006)

Years	Minimum Capital Requirment	Minimum Capital in *US$	Cumulative No of Banks
1952-1978	£200,000-Foreign £25,000-Nigerian £400,000-Foreign £25,000-Nigerian ₦ 1,500,000-Foreign ₦ 600,000-Nigerian	235,295 29,412 470,588 29,412 1,764706 705882	45
1979-1987	₦ 1,500,000-Foreign ₦ 600,000-Nigerian ₦ 2,000,000-Merchant Bank	1,500,000 600,000 2,000,000	54
1988-Feb.	₦ 5Million –Comm. Bank ₦ 3Million-Merchant Bank	250,000 150,000	66
1988-Oct.	₦ 10million-Comm. Bank ₦ 6million-Merchant Bank	500,000 300,000	66
1989-1990	₦ 20million-Comm. Bank ₦ 12million-Merchant Bank	235,294 141,176	107
1991-1996	₦ 50million-Comm. Bank ₦ 40million-Merchant Bank	586,235 470,588	112
1997-2002	₦ 500million-Comm. Bank ₦ 500million-Merch. Bank	5.88million 5.88million	110
2003-2004	₦ 2billion-Universal Banking	0.0166billion	89
2004 July	₦ 25billion-Unive.l Comm. Bank	0.2billion	25

£=British Pound Sterling $=US Dollar rates as at period of increase N: Nigeria Currency
Sources: Central Bank of Nigeria-Various Financial Publication(1970-2006) and Financial Markets.

Prior to the major policy shift by the Central Bank of Nigeria (CBN), Nigerian banking experienced a steady increase in the number of distressed deposit- money banks, i.e those rated by the CBN as marginal or unsound. This created the fear that Nigerian banking could be heading towards systematic distress. The marginal and unsound banks increased in number from seventeen(17) in 2001 to twenty three(23) in 2002 and 2003, and then twenty-seven(27) in 2004 representing thirty(30) per cent of the operating banks in the system. This figure rose to seventeen(17) per cent only three years earlier. It can be argued that sudden monetary policy shifts was partially responsible for the increase in the number of marginal and unsound banks in 2004(see Table II). The corollary is that the institutions concerned have had inherent and deep-seated weakness that the policy shift exposes, and no matter

what, they would have eventually become distressed. Goldfeld and Chandler(1981); and Somoye(2006) opined that any policy shift must be consistent with market framework if the objective of the policy is to be achieved. They decomposed the total lag between the need for policy and the final effect of policy into four parts. First, *recognition effect*, which refers to the elapsed time between the actual need for a policy action and the realisation that such a need, has occurred. Second, the *policy lag*,which refers to the period of time it takes to produce a new policy after the need for a change in policy must have been recognised. Third, *outside lag*, which is beyond the comprehension of policy, refers to the period of time that elapses between the policy change and its effect on the economy. This lag arises because individual decision makers in the economy will take time to adjust to the new economic condition. Decision of this nature must conform to monetary policy norms if it is to achieve its desired objective. Fourth, *cultural lag*, which measures the banking culture responsiveness to policy change in a predominantly poor banking habit population. In the developing nation, banking culture is still primitive and any changes that may affect their culture take a great deal of education. They concluded that the effect of policy change which could have been distributed over-time and its impact felt was jettisoned. Such omission may bring negative cost to the economy. For instance, Goldfeld and Chandler(1981) stated that monetary policy, though affects the economy less directly, will have a longer outside lag and that monetary policy tends to influence investment, and the lags in the physical process of building plants and machinery are undoubtedly longer than the lags in producing consumer goods. Therefore, the longer outside lag of monetary policy must be balanced against the shorter policy lag in deciding the optimal policy mix.

Table II: Nigeria: State of the Banking Industry

Category	2001	2002	2003	2004	2005	2006
Sound	10	13	11	10	25	10
Satisfactory	63	54	53	51	-	5
Marginal	8	13	14	16	-	5
Unsound	9	10	9	10	-	5

Sources CBN Publication(2006)

However, from Table II, the reason that may advance for the present poor state of the Nigeria banking industry after consolidation could be viewed from the perspective of wrong planning. Consolidation through merger and acquisition and or buy-out requires assets clarification and cleansing of the balance sheets in a situation where unsound banks merge with sound banks. Therefore, strengthening the balance sheet is imperative for those who seek to be acquired and those who are in pursuit of expansion. Banks that are unable to show financial stability through their balance sheets are likely to perish in an increasingly competitive industry as amplified by Shiratori(2002); Okazaki and Sawada(2003); Somoye(2006) and Michiru and Sawada(2003). Shih(2003) points out the possibility that credit risk could increase in the event of a sound bank merging with an unsound one. Also, most of empirical literature suggests that bank consolidations do not significantly improve the performance and efficiency of the participant banks Berger *et al*(1999), and Amel, D; C. Barnes, F. Panetta and C. Salleo(2002). They concluded that if a voluntary consolidation does not enhance the performance of the participating banks, any performance enhancing effect of the consolidation promoted by the government policy is more questionable.

4. Lesson From Other Countries

The banking reform programme of one country may provide some good lessons for others, especially those intending to or are already engaged in such exercise. The lesson may assist in guiding policies and guide lines as well as ensuring that the reform goals are achieved with little or no negative consequences. It is on this basis that this study presents an overview of the banking reform in some selected countries with a view to learning some lessons that will shape our financial sector.

In Yugoslav, the banking industry restructuring was motivated by the need to establish a healthy banking sector that will carry out its financial intermediation role at a minimal cost; which effectively provides services consistent with world standards. The major aim of the consolidation programme in Yugoslav was to store up the capital base of banks consolidated through mergers and takeover of local banks. This allows foreign banks to participate in the banking industry by providing additional capitalization through investment infrastructure in new banking products, operating technologies and buying shares of the existing banks.

The banking sector reforms in Japan involved the reform of the regulatory and supervisory framework, the safety net arrangements as well as mechanisms to speed up attempts at resolution of banks non-performing loans. In an attempt to revitalize the Japanese banking system, a package were used comprising among others: (1) the government would work with the bank of Japan (BOJ) to try to have the bad loan ratios of the big banks; (2) the government would consider the possibility of establishing a new system for the prompt infusion of state capital into under capitalized banks which was called "pre-emptive" capital injections; (3) the government would act to ensure a tightening of the assessment of bank assets quality, possibly involving the use of discounted cash flow (DCF) techniques in the assessment of the adequacy of provision; (4) adoption of stricter criteria concerning the banks' use of deferred tax assets within regulatory capital, with no limits or timetables for implementation; and (5) government conversion of bank preference shares that it already owns because of previous bailouts, into common stock in order to trigger nationalization for institutions whose operations had been seriously impaired and the establishment of a new body to operate *pari passu* with the resolution and Collection Corporation (RCC) to rehabilitate trouble companies whose future prospects appeared bright.

In the United States of America, consolidation of banks through mergers and acquisition is a general phenomenon. The number of banks declined steadily due to consolidation from about 1400 in the mid- 80s to 1222 in 1990 and further to 825 a decade later. The first wave of the mergers/acquisitions in the 1980s was precipitated by attempts by stronger banks to acquire weaker and under capitalized ones, while the second resulted from a response to a legislation that liberalized interstate branch banking sector reforms. The concept of bank consolidation, have also been implemented in Europe, Asia Latin American and Africa at different times for different reasons. Despite all the attempts to restructure the banking sector in the United States, there is growing incidences of bank failures particularly the mortgage sector. It stands to reason that bank consolidation would not in the least a sufficient condition to redress weaknesses in the banking sector. This is the time to begin to look for appropriate mechanism to correct the weaknesses in the financial sector.

The Malaysian banking sectors reform, which resulted from the Asian financial crises in 1990s generated tremendous public research interest because of the extent of the resilience of the financial system and the economy as a whole in withstanding its impact. To ward off the contagious effects, Malaysian initiated policy measures in April and July of 1997 to curtail banks exposure to the real estate sub-sector and capital markets, and aggressively defended the national currency (ringgit) exchange rate, which it eventually floated. This was followed by the series of other policy interventions in 1998 and 1999, which included institutional blanket guarantee for all bank deposition programme of bank, establishment of Assessment Company and bank restructuring and recapitalization agency, as well as introduction of capital controls.

Specifically, the key elements of the Malaysian banking sector reforms centered on beefing up prudential regulations and the establishment of Danamodal Nasional Berhad and Danaharta Nasional Berhad to consolidate, recapitalize and rationalize finance and banking institutions by applying least cost solution principles to minimize the injection of public funds. Accordingly, between 1999 and 2001, 54 banking institutions were consolidated into ten banking groups. By the first quarter of 1999 Malaysian had spent 5 per cent of its GDP or $4.0 billion to purchase non performing loans three(3) per cent and recapitalize banks two(2) per cent of GDP or $34 billion in Thailand made up of Liquidity support fifteen(15) per cent, recapitalization eight(8) per cent and interest cost two(2) per cent; and fifty(50) per cent of GDP or $US85 billion in the Indonesian case, broken down into Liquidity.

Another major reason why Malaysia may have better withstood the impact of the crisis and spent less in weathering the problem were attributed to its strong macro economic fundamentals at the time. Prior to the Asian crisis in 1997, inflation rate in Malaysia as at end 1996 was 3.5 percent compared to 7.9 percent in Indonesia, and to 4.9 percent in Thailand. Furthermore, most of the capital inflows into Malaysia were of longer term nature in the form of foreign currency above certain level was restricted by government. Malaysia also had only one large government –owned commercial bank compared to the other countries where their banking sector was highly dominated by government ownership. Besides, Malaysia's well developed capital market was reported to have limited banking sector financing exposure.

In summary, Delitte(2005) concluded that bank consolidation in Asia is such that competitive and market forces are creating an atmosphere where many banks simply cannot afford to have weak balance sheets and inadequate corporate governance. The results in Nigeria cannot be farther from this, in that, any financial reform that is induced by government, uncertified balance sheets and not market driven is bound to witness some failure.

5. Review of Pre and Post Consolidation Performance of banks and the Economy

5.1. Banking Sector Performance

The history of the Nigeria banking system is replete with growth and burst cycles in the number of operating banks and their branches. Usually, growth spurt are experienced when the policy environment present strange business opportunities in the banking sector, or there is a sudden policy shift that makes it easy for ordinary business people to initiate a process that creates access to public funds in the name of bank deposits.

In terms of Assets, Table III shows that the total asset of all the 89 banks operating in Nigeria in 2004 prior to the consolidation was ₦3,753.28billon(US$28.250billion) and rose to ₦6400.78billion(US$49.88billon) indicating a growth rate of 70.54.16 per cent within one year after consolidation. The asset size of an average bank which was ₦42.172billion(US$0.3174 billion) grew geometrically to ₦267.482billion(US$2.0856billion) within a year after the consolidation exercise, a growth rate of 534.27 percent. This was an impressive performance.

However, an assessment of the level of capitalisation of an average bank prior to the exercise indicates an equity base (Net worth) of ₦ 7.71 billion (US$0.06168billion) rising to ₦38.83billion(US$0.31064billion) in 2006, indicating a growth rate of 404 per cent. The leverage ratio measured in terms of equity to total asset also declined from 18.28 per cent 2004 to 14.52 per cent in 2006 for an average bank. This ratio compares favourably with the CBN minimum level of 10 per cent. The post consolidation ratio is also better in terms of its distribution among the banks compared with the pre-consolidation ratio where more than 70 per cent of the equity and assets were concentrated in(the largest five banks) less than 5 per cent of the existing banks. However, the intermediation activities of an average bank improved significantly by about 1,690 per cent from an average deposit base of ₦10.48billion (US$0.08384) in 2004 to ₦188.48billion (US$1.50784) in 2006

Table III: Pre-Post Consolidation Performance of the Nigerian Banks

Macro economic Indicators	N'm 2004 (a)	N'm 2005 (b)	N'm 2006 (c)	% Change Increase(+)Decrease (-)Or Difference(D±) (a - c)
Average Lending (N'm)	14,371.238	42,380.180	80,788.854	+462.15%
Average Assets(N'm)	42,171.66	132,017.34	267,482.50	+534.27%
Average Deposit(N'm)	10,482.36	85,007.13	188,478.55	+1690.05%
Average Net Worth(N'm)	7,708.73	19,708.88	38,831.31	+403.73%
Return on Equity(%)	35.28	12.72	11.12	-24.16(D)
Retur n on Asets(%)	8.37	3.01	2.07	-6.30(D)
Assets Utilisation(%)	33.62	11.52	11.04	-22.56(D)
Total Bank loan & Advance (₦'m)	1,294,449.50	1,859,555.50	2,338,718.80	+80.67
GDP(Current Basic Prices) (₦'m)	11,411,070.00	14,572,240.00	18,067,830.00	+58.34%
Real GDP (growth %)	6.5	7.06	7.17	+0.67(D)
Inflation Rate	10.00	11.6	10.6	+0.60(D)
Exchange Rate N/$	132.86	129.00	128.3	+3.43(D)
Min. Lending Rate	18.91	17.8	18.30	+0.61(D)
Max. Lending Rate	20.42	19.50	28.70	+8.28(D)
MRR/MPR	12.80	13.0	10.0	+2.80D)
Credit to the Private Sector (₦'m)	311,646.8	442,008.9	525,482.0	+68.87%
Bank Market Capitalisation('₦ m)	662,712.600	1,212,218.545	2,142,745.733	+223.82%
Bank Market Capitalization/NSE Capitalisation(%)	34.41	41.80	41.84	+7.43(D)
Total Market Cap. NSE market Cap. (total)	1,925,937.530	2,900,062.072	5,120,943.220	+165.89%
Bank Mkt Cap. /GDP	5.80	8.32	11.86	+6.06(D)
NSE mkt cap./GDP	5.7	11.8	28.34	+1.22(D)
Credit to Private Sector growth rate (%)	26.6	30.8	27.82	+0.18(D)
Credit to private sector/GDP	2.73	3.03	2.91	+0.18(D)
Average loan/Deposit Ratio (%)	72.8	76.7	96.8	+24(D)
Credit to private Sector/Total loan (%)	24.08	23.77	22.47	+1.6(D)
Loans Adv.	1,294,449.5	1,859,555.50	2,338,718.8	80.67%
Total Assets (₦m)	3,753,277.8	4,515,116.67	6,400,783.9	70.54%
Total Deposit Liabilities((₦'m)	1,661,482.1	2,036,089.9	1,826,275.60	+9.92%
Capital+ Reserves((₦'m)	348,387.6	591,738.7	953,001.20	+173.55%
Comm. Bank Asset/GDP(%)	32.89	30.98	35.43	+2.54(D)
Non-financial Private Sector Bank Credit/GDP(%)	2.73	3.03	2.91	+0.18(D)

Sources: Various audited Accounts of Consolidated banks as at 2006 Financial Year;
Cental Bank of Nigeria Statistical Bulletin 2005
Central Bank of Nigeria Annual Reports and Accounts 2006

The profit efficiency/asset utilization has not been impressive. Although the banks have been able to double their gross earnings from their pre consolidation performance level, their profit and asset utilization efficiencies have declined since the conclusion of the consolidation. For instance, the industry return on equity declined from 35.28 per cent in 2004 to 11.12 per cent in 2006, while return on asset declined from 8.37 per cent to 2.09 per cent over the same period. The asset utilization ratio also declined; while an average bank was able to earn 34 kobo for every N1.0 asset in 2004, this declined to 11kobo in 2006. Thus, while the consolidation has improved the structure of the Nigerian banking industry in terms of asset size, deposit base and capital adequacy, the profit efficiency has not been impressive. The banks will need to become more efficient in terms of their ability to generate enough return to justify the increase in the equity base as well as the resources put at their disposals by their stakeholders.

The lending capacity of the banks improved significantly as a result of the consolidation. As at 2004, an average bank could only lend about N14,371.billion. Whereas, the consolidation strengthen the bank where a typical bank in Nigeria in 2006 could lend an average of N80.788billion. This represents a growth of 462.13 percent growth.(see Table III)

5.2. Banking Sector and the Economy

We analyse the role of the commercial banking sector relative to the economy. This is to enables us appreciate whether the banking industry will assume any appreciable level importance in the aggregate economy as a result of consolidation. From Table III, the assets of commercial banks which stood at 32.89 per cent of the GDP in 2004 rose marginally to 35.43 per cent in 2006. The degree of private sector credit has been suggested to be a better indicator of bank contribution to private investment. In 2004, commercial banks channeled 24.08 per cent of their lending to the non-bank private sector, but this declined to 22.47 per cent by 2006. Likewise, the value of commercial bank credit relative to the GDP which was 2.73 per cent in 2004 rose marginally to 2.91 percent in 2006. There has not been any appreciable growth in terms of the growth in credit to the private sector because the commercial bank credit which has a growth rate of 26.6 percent between 2003 and 2004, grew marginally to 30.8 percent in 2005 and declined to 27.82 percent a year after the consolidation. This confirms the views of Craig and Hardee(2004). In terms of price stability, the level inflation increased from 10.0 percent in 2004- a pre-consolidation period to 12.0 per cent, a post consolidation.

The analysis suggests that banking sector has not shown a serious response of being able to meet monetary policy expectation. The relative performance of the banking size in terms of asset size, private sector credit, relative to the economy have been very marginal such that it can be safely concluded that the consolidation exercise has not brought about any meaningful contribution with respect to some of these performance indicators.

5.3. Banking Sector and the Capital Market

The market capitalization of quoted banks was 34.41 per cent of total market capitalization of the Nigerian Stock Exchange (NSE) in 2004, but rose significantly to 41.80 percent in 2005 and renamed at 41.84 per cent by 2006. The NSE market capitalization grew by 160.70 per cent between 2004 and 2006, whereas, the banking sector market capitalization grew by 223.33 per cent over the same period. In fact, about 46.32 per cent of the total growth in market capitalization came from the growth in banking sector market capitalization. This, from the capital market perspective, indicates that the banking sector has made a significant contribution, and it has further improved the value and liquidity of the Nigerian capital market.(see Table III)

6. Conclusion and Recommendation

The paper has reviewed the effectiveness of bank consolidation and monetary policy in the conduct of sustainable financial system. We notice that there seems to be a presumption that the reform in the banking sector is all that is required to fix the economy. The idea underlying the consolidation policy is that bank consolidation would reduce the insolvency risk through asset diversification. We noted that there is the possibility that credit risk could increase in the event a sound bank merging with an unsound one and that bank consolidations do not significantly improve the performance and efficiency of the participant banks. Thus, strengthening of the balance sheet is imperative to those who seek to be acquired and those who are in pursuit of expansion to avoid bank failure. It is equally noted that consolidation programme through merger and acquisition require time-frame. In Nigeria, however, the recapitalization to strengthen the balance sheets of the consolidating banks in the banking industry has involved drawing much of the money from the rest of the economy and this presents one sided reform that is not matched with equal capacity building in the real economy.

The paper concludes that banking sector is becoming competitive and market forces are creating an atmosphere where many banks simply cannot afford to have weak balance sheets and inadequate corporate governance. The paper posits that consolidation of banks may not necessarily be a sufficient tool for financial stability for sustainable development and this confirms Megginson(2005) and Somoye(2006) postulations. We recommend that bank consolidation in the financial market must

be market driven to allow for efficient process. The paper further recommends that researchers should begin to develop a new framework for financial market stability as opposed to banking consolidation policy.

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