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**IMPACT OF SECTORAL DISTRIBUTION OF COMMERCIAL BANKS' LOANS AND  
ADVANCES ON ECONOMIC GROWTH IN NIGERIA**

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**ABSTRACT**

The study investigated the Impact of sectoral distribution of Commercial banks' loans and advances on economic growth in Nigeria for the period of 1986 - 2014. Time series data on commercial banks' loans and advances to Manufacturing sector (CMAN, representing Production sector), commercial banks' loans and advances to Export sector (CEXP, representing General Commerce sector) and commercial banks' loans and advances to Transport and Communication sector (CTC, representing Service sector) was used to capture sectoral distribution of commercial banks' loans and advances to different sectors of the economy, while Real Gross Domestic Product (RGDP) was used to capture economic growth. The techniques of estimation employed in the study include Augmented Dickey Fuller (ADF) test, Johansen Co-integration, Error Correction Mechanism (ECM) and Granger causality test. The result showed that commercial banks' loans and advances to only Transport and Communication sector has a significant impact and is positively related to economic growth, while commercial banks' loans and advances to Manufacturing and Export sector has no significant impact and were negatively related to economic growth. The Granger causality test revealed no causality between CMAN, CEXP and RGDP, while there is a unidirectional causality between RGDP and CTC. Based on the result, it was recommended that, Commercial Banks' should increase their loan to manufacturing and export sector in order to boost our gross domestic product.

**Keywords:** Commercial banks', Economic growth, Sectoral distribution

**INTRODUCTION**

Commercial banks loans and advances to various economic agents which is regarded as sectoral distribution of loans and advances aid in financial intermediation between deficit and surplus unit of the economy. It enhanced productivity, leads to large scale production and enhance forward impact on economic growth. Schumpeter (1911) strongly supported finance lead growth hypothesis, which states that financial sector play a key role in channeling savings into productive investment, particularly in the formal sectors of the economy. Nzomoi & Rutto (2012) asserted that commercial banks' are the key conduit for financial intermediation in the

economy. The vital role of commercial banks loans and advances in generating growth within an economy has been widely acknowledged, Schumpeter (1932) established that banking sector facilitate technological innovation through their intermediary role. His emphasis was that efficient sectoral distribution and allocation of savings through identification and funding of entrepreneur with best chances of successfully implementing innovative product and production are tools to achieve real economic performance. Therefore, no matter the sources of the generation of the income or the economic policies of the country, commercial banks would be interested in giving out loans and advances to their numerous customers bearing in mind, the principles guiding their operations which are profitability, liquidity and solvency subject to safety and suitability.

However, commercial banks' decision to lend out loans and advances are influenced by a lot of determinants such as the prevailing interest rate, the volume of deposits, the level of their domestic and foreign investments, banks' liquidity ratio, prestige and recognition to mention but a few. Loans and advances which maybe on short term, medium or long term basis is one of the services that commercial banks usually render to their customers. In other words, banks do grant loans; overdrafts and advances to individuals, business organizations as well as government in order to enable them embark on developmental activities as a means of aiding their growth in particular or contributing towards the economic growth and development of a country in general. The customer may require fund for the various purposes which may spread through new capital venture bridging loan, farming, contract jobs, and business expansion among others.

Hashim (2002) asserted that despite series of financial institutions reforms aimed at strengthening the banks' ability to effective and efficient services delivery and branch networking towards the real sector so that the Nigerian economy can become more vibrant and very dynamic, problems such as insufficiency in allocating funds to the real sector, lack of long-dated (long-term) funding, decline in domestic credit by the banking sector to the private sector, high concentration of loans to few sectors and mismatch of liquidity in the Nigeria economy still lingers on. These problems facing commercial banks have made it very difficult for them to make its expected contributions to the economy. A survey of literature on this topic in Nigeria revealed that the last empirical work seems to be in the year 2012. Also, the previous studies have focused on the productive sectors neglecting the commercial banks' lending to other sectors. Its against this backdrops that this study intends to fill the above gap and contribute to existing body of knowledge by considering a holistic approach of all the sectors of the economy and updating the data to reflect the impact of current lending to all sectors under the study.

## **2.0 LITERATURE REVIEW**

Some brilliant attempts have been made by various researchers to investigate the impact of sectoral distribution of commercial banks loans and advances on Nigeria economic growth.

Fapetu and Obalade (2015) investigated the impact of sectoral allocation of Deposit Money Banks' loans and advances on economic growth in Nigeria during intensive regulation, deregulation and guided deregulation regimes. Regression analysis of the ordinary least square method was performed for each of the three regimes. The results show that only the credit allocated to government, personal and professional have significant positive contributions on economic growth during the intensive regulation. However, bank credits generally do not contribute significantly to economic growth during deregulation. Introduction of guided deregulation showed that commercial bank's loans and advances to production and other subsector are both positive and significant in determining growth.

Ebi and Emmanuel (2014) discovered that an increased bank credit to industrial sector is significant in determining industrial growth in their investigation on the impact of commercial bank credit on Nigeria industrial subsectors between 1972 and 2012. Econometric Error Correction Model (ECM) was used to determine the longrun relationship on the variables. Ogege and Shiro (2013) reported a long-run relationship between the variables and found that commercial credits contributed positively to growth but it is significant. It employed co-integration and error correction model and covered the period between 1974 and 2010.

Obamuyi and Kayode (2012) examine the specific effect of bank lending and economic growth on Nigeria's manufacturing sector over the period 1973 to 2009, (36 years). The study employs manufacturing production as a function of bank lending, lagged value of manufacturing, inflation rate, maximum lending rate, capacity utilization, financial deepening, exchange rate, real gross domestic product and a dummy of shift in financial policy. Employing co-integration and vector error correction techniques, the study found that manufacturing capacity utilization and bank lending rates significantly affect manufacturing output in Nigeria. On the whole, the study found as indeterminate, the empirical relationship between manufacturing output and economic growth in Nigeria. Using correlation analysis, regression, diagnostic tests, Augmented Dickey-Fuller test and co-integration, Ekpenyong and Acha (2011) investigated the contribution of banks to economic growth. The results depict that credit to private sector has positive and significant impact on growth. Ighodaro and Oriakhi (2011) evaluated the nature of trivariate causal relationship between financial development and economic growth in Nigeria. Employing data that cover both the pre and post Structural Adjustment Programme (SAP) regimes in Nigeria, the study found significant long-run relationship between the study variables – ratio of broad money to income, loan deposit ratio, money supply and real gross domestic product. It concludes that fluctuations in loan deposit ratio and broad money to income may not necessarily affect Nigeria's economic growth.

Adeniyi (2006) found that economies characterized by efficient financial systems tend to have accelerated economic growth relative to those with less efficient financial systems. Evaluating

the relationship between financial development and economic growth, Eatza and Malik (2009) found that bank credits to the private sector significantly increase the productivity of workers (output per worker), and as such, facilitated long-run economic growth. Prakash (2009) investigated finance and economic growth in India and found a bi-directional causal relationship between financial development and economic growth. The study not only confirms evidence of mutual re-enforcement by the study variables within the Indian environment, but evidences a significant level of sophistication of the Indian financial and economic systems. Mba and Dazoue (2013) examined the Nexus between Credit to the Private Sector, Inflation and Economic Growth: Case of Cameroon between 1965 and 2010. Using Vector auto regressive, the results showed that inflation has a positive and significant effect on growth, economic growth has a positive and significant effect on credit to the economy and credit to the economy has a negative and significant effect on inflation. The result also revealed that Inflation granger causes economic growth, economic growth granger causes credit to the private sector and credit to the private sector granger causes inflation.

Modebe, Ugwuegbe, and Ugwuoke (2014) studied the Impact of Bank Credit on the Growth of Nigerian Economy for the period between 1986 and 2012 using Johansen co-integration approach. The result showed a negative and an insignificant relationship between total bank credit to private sectors and Nigerian Economic growth. Nwanyanwu (2010) investigated the impact of bank credit on the growth of Nigerian economy using ordinary least square econometrics techniques and reported that bank credit has a positive and a significant impact on Nigerian economic growth. Cevik and Rahmati (2013) investigated the causal relationship between financial development and economic growth in Libya during the period 1970-2010. The empirical results varied with estimation methodology and model specification, but indicated that there is no long-run relationship between financial intermediation and output growth. In the study of the causal relationship between deposit money bank credit and economic growth in Nigeria over the period 1981-2014 by Okafor, Ezeaku and Ugwuegbe (2016), it was found that a unidirectional causality runs from private sector credit and broad money supply to economic growth. Emecheta and Ibe (2014) investigated the impact of bank credit on economic growth in Nigeria using VAR on data between 1960 and 2011 and found that there is a significant positive relationship between bank credit to the private sector, broad money and economic growth. Chris, Mbat, & Stephen (2016) studied the effect of commercial banks' credit on agricultural output in Nigeria using the ordinary least squares regression technique and found a positive and a significant relationship between commercial banks credit to the agricultural sector and agricultural production in Nigeria. It also revealed a negative relationship between interest rate and agricultural output was found. This signifies that high interest rate charged to farmers has discouraged them from borrowing and thus less agricultural investment.

The above review has shown inconsistency of the reported results in Nigeria. Hence, the impact and direction of causality of these variables has not been established. This, however serve as a further justification for this study.

### **3. Research Method**

#### **3.1 Data and Data Sources**

This study covers a period of twenty-eight years. Data used for this study were obtained from bulletin published by the Central Bank of Nigeria. The explained variable which is the economic growth is proxy by real gross domestic product, while the explanatory variables are commercial bank credit to production, general commerce and service sectors.

#### **3.2 Estimation Technique**

This study examines the long-run dynamic relationship between the variables in the model by employing the Johansen’s co-integration framework. Also, the direction of causal relations (causality) between the dependent variable (Gross Domestic Product) and the independent variables (Manufacturing, Export, Transport and Communication sectors) was determined by the granger causality test with an optimal lag of 2.

#### **3.3 Model Specification**

This study employed an empirical model which is built based on the slight modification of the models in the works of Fapetu and Obalade (2015), Manufacturing represents the production sector, export represent general commerce sector while transport and communication represent the service sector. The model however specifies the dependent variable as Real Gross Domestic Product to be linearly related to the commercial banks loans and advances to the Manufacturing, Exports and Transport and Communication.

The model is given in functional form as:-

$$RGDP = f(CMAN, CEXP, CTC, \mu) \dots\dots\dots 1$$

In econometric form as:

$$RGDP = \beta_0 + \beta_1CMAN + \beta_2CEXP + \beta_3CTC + \mu \dots\dots\dots 2$$

With the variables defined as follows:

- RGDP =Real Gross Domestic Product
- CMAN = Commercial Banks Loans and Advances to Manufacturing Sector.
- CEXP = Commercial Banks Loans and Advances to Exports
- CTC = Commercial Banks Loans and Advances to Transport and Communication sector.

Where:

$\beta_1, \beta_2, \beta_3$  = Regression Parameters

While  $\beta_0$  = constant or intercept of the model

To avoid spuriousity in estimation, the model can also be stated in it log-linearized form as depicted below: -

$$\text{LogRGDP} = \beta_0 + \beta_1\text{LogCMAN} + \beta_2\text{LogEXP} + \beta_3\text{LogCTC} + \mu \dots\dots\dots 3$$

from equation 3 above, the research model can be further restated in the time series form as depicted below:-

$$\text{Log(RGDP)}_t = \beta_0 + \beta_1\text{Log(CMAN)}_t + \beta_2\text{Log(EXP)}_t + \beta_3\text{Log(CTC)}_t + \mu \dots\dots\dots 4$$

Where: -

Log = Natural Logarithm.

t = Time series.

**3.4 Expected Results**

We expect that the relationship between gross domestic product and commercial bank credit to production, general commerce, service and other sectors be positive. The signs of the estimated coefficients are thus expected to be greater than zero respectively.

**4 Findings and Discussion**

**4.1 Granger causality test**

**4.1.1 Hypothesis One**

**CMAN and RGDP**

HYPOTHESIS		F-Statistics	Probability
<b>A</b>	H <sub>0</sub> : - CMAN does not Granger Cause RGDP	0.84056	0.44486
	H <sub>1</sub> : - CMAN does Granger Cause RGDP		
<b>B</b>	H <sub>0</sub> : - RGDP does not Granger Cause CMAN	0.26750	0.76774
	H <sub>1</sub> : - RGDP does Granger Cause CMAN		

**Source:** Author’s Computation 2016 (See Granger Causality test result in appendix)

There exist no causality between Commercial Banks Loans and Advances to Manufacturing sector (CMAN) and Real Gross Domestic Product (RGDP) since the probability value of both case A and B is greater than 10%(0.1) and its corresponding F-statistics is as well lesser than the F-tabulated (2.99), therefore, we accept the Null Hypothesis (H<sub>0</sub>) and reject the Alternative

Hypothesis ( $H_1$ ) in both cases. Hence, no causal relation exists between both variables in the short run.

**4.1.2 Hypothesis Two**

**CEXP and RGDP**

HYPOTHESIS		F-Statistics	Probability
<b>A</b>	$H_0$ : - CEXP does not Granger Cause RGDP	0.14213	0.8683
	$H_1$ : - CEXP does Granger Cause RGDP		
<b>B</b>	$H_0$ : - RGDP does not Granger Cause CEXP	1.07885	0.3573
	$H_1$ : - RGDP does Granger Cause CEXP		

**Source:** Author’s Computation 2016 (See Granger Causality test result in appendix)

There exist no causality between Commercial Banks Loans and Advances to Export sector (CEXP) and Real Gross Domestic Product (RGDP) since the probability value of both A and B is greater than 10% and its corresponding F-statistics is as well lesser than the F-tabulated (2.99), therefore, we accept the Null Hypothesis ( $H_0$ ) and reject the Alternative Hypothesis ( $H_1$ ) in both cases ( GDP to CEXP and as well from CEXP to RGDP) . Hence, no causal relation exists between both variables in the short run.

**4.1.3 Hypothesis Three**

**CTC and RGDP**

HYPOTHESIS		F-Statistics	Probability
<b>A</b>	$H_0$ : - CTC does not Granger Cause RGDP	0.10171	0.9037
	$H_1$ : - CTC does Granger Cause RGDP		
<b>B</b>	$H_0$ : - RGDP does not Granger Cause CTC	4.02031	0.0325
	$H_1$ : - RGDP does Granger Cause CTC		

**Source:** Author’s Computation 2016 (See Granger Causality test result in appendix).

There exist causality between Commercial Banks Loans and Advances to Transport and Communication sector (CTC) and Real Gross Domestic Product (RGDP) since the probability value of hypothesis A is greater than 10%, and the probability value of hypothesis B is less than 10% , and the corresponding F-statistics for A is less than the F-tabulated (2.99), while the corresponding F-statistics for B is greater than the F-tabulated, therefore, we reject the Null Hypothesis ( $H_0$ ) and accept the Alternative Hypothesis ( $H_1$ ) in this case(B). This shows that there is causality between RGDP and CTC and that RGDP Granger cause CTC.

#### 4.2 Unit Root Test

After carrying out the ADF unit root test, the summary of order of integration is presented in the table below;

**Table 4.2.1: Summary of Order of Integration**

Variables	Order of Integration
RGDP	I (1)
CMAN	I (1)
CEXP	I (1)
CTC	I (1)

Source: Author's Computation 2016.

#### 4.3 Johansen Co-Integration

The result of the co-integration test is shown in the table 4.3.1 below:

The concept of co-integration is relevant to the problem of determination of long-run equilibrium relationship in the model. Co-integration is the statistical implication of the existence of a long-run equilibrium relationship between the variables. Co-integration is conducted using Trace Test and Maximum Eigen Test.

**Decision Rule:** The condition for co-integration is that the trace statistic or maximum Eigen value must be greater than 0.05 critical values.

**Table 4.3.1 Presentation Of Trace Test**

Hypothesized	Trace	0.05	
No. of CE(s)	Statistic	Critical Value	Prob.**
None *	43.30719	40.17493	0.0234
At most 1	12.56430	24.27596	0.6585
At most 2	6.095972	12.32090	0.4244
At most 3	1.550718	4.129906	0.2499

Trace test indicates 1 cointegrating eqn(s) at the 0.05 level.

\* denotes rejection of the hypothesis at the 0.05 level.

\*\*Mackinnon-Haug-Michelis(1999) P-values.

Source: Author's computation 2016 (E-Views 7).

From the Trace test table 4.3.1 above, it could be inferred that long-run relationship or co-integration exists among Real Gross Domestic Product (RGDP), Commercial Banks' Loans and Advances to Manufacturing Sector (CMAN), Commercial Banks' Loans and Advances to Export Sector (CEXP), Commercial Banks' Loans and Advances to Transport and Communication Sector (CTC). Trace test indicated 1 co-integrating equation; therefore, there is co-integration in the long run.

**4.3.2 Presentation of Normalized Long Run Equation**

RGDP	CMAN	CEXP	CTC
1.000000	-9.284808	7.422848	2.480360
	(1.18122)	(1.41264)	(0.60712)
	[-4.642404]	[3.711424]	[1.24018]

Source: Author's computation 2016 (E-Views 7).

The above table 4.3.2 shows the normalized co-integration co-efficient with the standard error and t-statistic in parentheses ( ) and [ ] respectively..

The t-statistic shows the significance of the independent variable with respect to the dependent variable in the long run. All the independent variables are statistically significant and positively related to RGDP in the long run except CMAN which is negatively related.

**4.4 Error Correction Mechanism**

The error correction mechanism is the speed or degree of adjustment i.e. the rate at which the dependent variable adjust to changes in the independent variables. Since a long run equilibrium relationship has been established, the next step is test for the speed of adjustment using the short run dynamism of error correction mechanism (ECM).

**Table 4.4.1 Result of Parsimonious ECM Model (ECM<sub>2</sub>)**

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(RGDP(-1),2)	-0.477117	0.157686	-3.025735	0.0067
D(CMAN,2)	-0.093284	0.118882	-0.784675	0.4418
D(CEXP,2)	-0.025412	0.021417	-1.186527	0.2493
D(CTC,2)	0.014121	0.010519	1.342417	0.1945
ECM(-1)	-0.367147	0.134750	-2.724649	0.0131
C	0.003699	0.012212	0.302948	0.7651

**R<sup>2</sup> = 0.447586      DW = 2.252170**

Source: Author's Computation 2016 (E-Views 7).

From the table 4.4.1 above, it shows that the coefficient of ECM is -0.367147. The ECM is significant with the appropriate negative sign. The coefficient of ECM in the parsimonious model indicates that the speed of adjustment of any past deviation to long run equilibrium is 36.71%. This shows that present value of the dependent variable adjust more slowly to changes in the independent variables slightly than what was obtained in the over-parameterized model.

Also, the result reveals that the coefficients of CMAN, CEXP are negative, while CTC is positive. The constant parameter indicates that when all independent variables are held constant, RGDP will fall by 0.003699unit. From the results, it could be deduced that CTC have a direct relationship with GDP because of the positively signed coefficient. The CTC coefficient is 0.014121. This implies that a unit increase in CTC leads to an increase in RGDP by 0.014121units.

The coefficient of CMAN is -0.093284, which signifies that when the CMAN is increased by a unit, RGDP decreases by 0.093284 units because CMAN has negative sign. It can also be deduce that an inverse relationship exist between CEXP and RGDP. This is evident from the negative sign of the coefficient of CEXP. The implication thereof is that a unit increase in CEXP reduces RGDP by 0.025412units while holding other variables constant.

The coefficient of multiple determination ( $R^2$ ) is  $0.447586 \approx 0.45$  which indicates that 45% of total variation or changes in the present value of RGDP is explained by changes of past value in the explanatory variables (CMAN, CEXP, and CTC), While the remaining 55% is explained by other variation outside the model, i.e. the white noise.

#### **4.5 Implication of Findings**

The study examines the Impact of Sectoral Distribution of Commercial Banks' Loans and Advances on Nigeria Economic Growth using Co-integration and Error correction mechanism and Granger Causality model, utilizing annual time series data covering the period from 1986 to 2014. The Augmented Dickey-Fuller test was conducted to test for stationarity of data in order to determine the long run equilibrium or relationship of the model. The stationarity test, i.e. ADF unit root test revealed that all variables (Real Gross Domestic Product (RGDP), Commercial Banks' Loans and Advances to Manufacturing Sector (CMAN), Commercial Banks' Loans and Advances to Export sector (CEXP), Commercial Banks' Loans and Advances to Transport and Communication sector (CTC) were not stationary at level but first difference. The co-integration test revealed that there is one (1) co-integrating equation, meaning that all the variables are closely related in the long run.

In order to determine the goodness of fit of the model, the coefficient of multiple determination ( $R^2$ ) was considered. The  $R^2$  of the parsimonious model is  $0.447586 \approx 0.45$ . This means that 45% of the variation in the present state of RGDP is being explained by all the independent variables and lagged variables, while the stochastic/error term explains the remaining 55%.The F-test conducted at 95% confidence level indicates that the whole model is statistically significant, implying that changes in RGDP can be sufficiently explained by CMAN, CEXP, CTC all put together.

The parsimonious model shows that, the constant term conforms with the economic priori expectation. That is, if for instance all the independent variables are held constant, Real Gross Domestic Product (RGDP) will increase by 0.003699 per cent. The findings of the study revealed that Commercial Banks' Loans and Advances to Transport and Communication Sector contributed significantly to Nigeria's economic growth which was proxied by RGDP. Therefore, there is need to encourage and promote various means of transportation (i.e. Air, Road, Water) through research and innovation in technology, and making more provisions for a better road

network and improvement in communication facilities to be able to interact and staying in touch with the rest of the world.

The findings also revealed that Commercial Banks' Loans and Advances to Manufacturing sector had a negative significant impact on economic growth in Nigeria. This could be as a result of inappropriate or under-utilisation of loans given out, mismanagement, diversion of loans and also inappropriate monitoring on the part of commercial banks to do follow-ups on loans given out, and also granting of loans to over ambitious projects, and also to projects established in ill-sited area. The findings of the study also revealed and indicated that Commercial Banks' Loans and Advances to Export sector has a negative significant impact on economic growth in Nigeria. However, the relationship between commercial banks' loans and advances to manufacturing sector and transport and communication sector and Gross domestic product are in consonance with the priori expectation of the study except commercial banks' loans and advances to export sector.

### **5.0 Conclusions and Recommendations**

The research work examined the impact of sectoral distribution of commercial banks' loans and advances on Nigeria economic growth. The main findings from this study indicate that the sectoral distribution of commercial banks' loans and advances has a significant impact on economic growth in Nigeria. Based on empirical findings, commercial banks' are important in stimulating economic growth and should be more favorable disposed to extending more loans and advances to the real sectors of the economy.

Government and monetary authorities should provide enabling environment and also give grants, loans and advances to companies in the general commerce sector, and also monetary authorities should ensure the continuance of guided deregulation as opposed to intensive regulation or deregulation, better and stronger credit culture should be promoted and sustained; there should be strong and comprehensive legal framework that will continue to aid in monitoring the performance of credit to various sectors, and recovery of debts owed to commercial banks; also, banks should share among themselves information on bad debt; and every well performing sector should be favoured in terms of granting of loans and advances.

In conclusion , its worth noting that continuous credit accessibility has the capacity to induced the nation's sectoral performance which will promote economic growth and development when adequate monetary and fiscal policy are put in place to encourage the demand and supply of commercial banks' loans and advances to the real sectors of the economy.

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