Journal of Association of Professional Bankers in Education (JAPBE)

Nigeria Vol., I No 1, November 2017

http://apbe-cibn.org.ng ISSN 2645-3231

THE IMPERATIVE OF REGULATIONS AND MANAGEMENT OF FINANCIAL INSTITUTIONS IN NIGERIA

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ABSTRACT

This paper examines the historical perspective of Nigeria financial institutions and the important of regulations and management of financial institutions. The aim of this study, to appraise how regulation ensures safety of customers' deposits and confident, reduce systemic distress and promote sound financial stability for economic development. The study used existing empirical and theoretical perspectives. Financial institutionworld-wideis the most regulated, even in Nigeria,however many customers loss hope in the Nigeria financial institutions due to uncoordinated previous regulationsand management of financial institution that led to the banks'undercapitalization, illiquidity,huge bad debts,and poor assets quality challenges negating bank performance. The imperative of regulation and management of financial institution has now helped to restore the depositors' confident in bank. In carrying out the regulation and management of financial institution; the dosage of regulation was too frequent by the regulators and management of financial institution becomes destructive as to the number of banks and personnel, with attendant effectson creativity and innovativeness. There is positive relationship between the banking regulation and banking development in Nigeria.Gradual and periodicincreases in capitalization of the banks and strict implementation of risk-free focused and rule-based regulation recommended for the regulators. The operators and regulators should have an in-depth knowledge and competencyto handle theregulation.

Key words: Economicdevelopment, regulation, capitalization, depositor's confident, financial stability.

INTRODUCTION

Financialsystem is an omnibus structure, consisting interrelated institutions; banks, financial market, insurance and their debts instruments, the framework of laws and regulations, the domestic practices and the work ethics to control the financial resources in the economy. Bankdeals in or uses money instruments, specifically, dealing in money creation and payment systems,Insurance companies protect customers claims by assuming liabilities and Financial market is where financial assets are exchanged and transferred to stimulate the economy; as the three components are strictly interlinked.Financial institutions' role is that of financial intermediation,allocating savings between the surplus and deficit units of the economy and playing pivotal role in economic development, Schumpeter (1911) in Ojomolade(2009).

Funds mobilised are huge compared with the financial institutions' owners contributions, it is therefore essential, having proper management framework in place,curtailing and avoiding excessive risk taking and financial failure with disturbing effect on payment systems with split-over effects to other financial market and the entire economy. Financial management gave an aggregative perception of the financial system,the interdependence of its member systems, interdependence of the financial system and it environmental domains, how to set goals and formulating strategies to achieve growth, confront challenges and threats in term of creative accounting, organisational conflict, risk level, liquidity and capital adequacy.

Financial institutions allocate mobilised funds to alternative investments and consumptions, increase national investment through correct assets multiplier,level of employment, national income and economic growth, realisingthese importance, government keeps close track on how the financial resources are utilised and principally interested in the safety of the depositors' funds and the stability of the financial system for the overall economic growths.

All over the World, governments have now realised the valued roles of financial institutions in moving the economy towards growth and employment generation;developed kin interest in the efficiency and effectiveness of the bank's

operations, mostly in credit formationprocesses; it's this relevance that makes government to establish laws and have regulators to ensure that banks play the expected tasks efficiently and effectively according to the financial regulations (laws and rules) for the benefits of the economy and the stakeholders.
A place of pride has been given to financial institutions (bank and market) by government in an economy due to its importance as agent of economic development, the banks could have preferred self-regulation but government opted for formal regulation. Sometime the regulation is reactive rather than proactive, particular in Nigeria context. The regulation makes Nigeria financial system dynamic and efficient in order to achieve macroeconomic objectives of price stability, high per capita income, standard of living, increase in gross domestic products and balance of payment position. The financial institutions witness an upsurge in the numbers of institutions and branches, so also in deposit taking over the years (Sanusi, 2011&2012).

Despite the presence of self-regulation and formal regulation, banking crises occurred, imposing hardship on the depositors, consumers and the economy, the crises arose both from endogenous and exogenousfactors (environmental factors)affected the financial system; making the institutions vulnerable to technical insolvency, capital inadequacy, poor asset quality and poor management. However, the economic recession leads to loans default; the default eroded the bank capital, consequently bank failures, of which 26 banks were liquidated and many investors loss their investments in the capital market and the public confidence in the banks dwindled due to the failures, further increased by the global economic meltdown,therefore, regulation for management of financial institutions become imperative.

Objective of the Study

The main objective of the study is to critically analyze the extent to which regulations enhance management of Financial Institutions in Nigeria. Other specific objectives are to:

(i. Investigate if there are any positive relationship between regulations and management of financial institutions.

(ii. Ascertain the burden of regulation on the management of financial institutions in Nigeria.

Research Questions

(1. Has the regulation enhances management of financial institutions in Nigeria?

(2. Is there any positive relationship between regulation and management of financial institutions in Nigeria?

(3. Does the regulation add burdeninto the management of financial institutions in Nigeria?

REVIEW OF RELATED LITERATURE

The drivers of regulation for financial institution management look at in this paper are:Public interest theory, Capture theory, Theory of Economic regulation, Agency theory,Risk management theory and Regulatory dialectic theory.

Agency theory developed by Stieglitz in 1989 is to justify the government goals of safety and protection of investors' interest in an organization.Regulatory intervention is required for the protection of public savings when it is threatened by the behavior of financial institutions. The main trust of this theory is that, government agencies must be present to supervise and limit the excesses of financial institutions toward customer safety and protection. Risk management theory, developed by Davis in 1991 to explain why regulators are concerned with monitoring and supervising the management of risks, such as liquidity and credit due to the effect of mismanagement by major banking financial institutions, of the amount and timing of such risks on other parts (layers) of the financial system. The main trust here is, the level of risk in the system; the volatile nature of financial sector requires an ultra-sound to ensure risks are minimal and participants bear less burden in the financial system (Currie, 2003).

The regulatory dialectic theory strives to explain the ongoing struggle between the regulators and financial institutions, whichare driven by safety and the institution by wealth maximization motives.Public Interest Theory says that regulation exists to serve the public interest, says government sought to prevent the society or consumersfrom harmful effect resulting from market imperfections, (Pigou, 1932). Regulation is assumed initially to benefit society as whole rather than particular vested interests (Deegan, 2011).

Capture Theory is mostly propounded by public choice theorists, postulates that regulatory capture occurs because groups or individuals with a high-stakes interest in the outcome of policy or regulatory decisions can be expected to focus their resources and energies in attempting to gain the policy outcomes they prefer, while members of the public, each with only a tiny individual stake in the outcome, will ignore it altogether (Lee, 2006). The theory therefore suggests that a regulatory agency should be protected from outside influence as much as possible (Edmund, 2006).

Alternatively, it may be better to not create a given agency at all lest the agency become victim, in which case it may serve its regulated subjects rather than those whom the agency was designed to protect(Adams, 2008).Theory of economic regulation is an advance of the capture theory; it attempts to provide answer as to why there is regulation and what industries are likely regulated. Stigler (1971) theorizes that regulation demanded by special interest groups and is done for the benefits of these groups who in return pay the regulators with financial and political support so that they continue to stay in office.

The need for regulation is to foster financial stability and confidence in the system (Sanusi 2012). Ajayi (2005) says to attain effective and efficient banking system and according to Okeke (2007) is an action by government to fast track and jump start and consolidate the sector to achieve the desired results, while Ebong (2006) says it deliberate response to correct perceived or impending frauds,crises and failures. It is an addition to the body of existing laws, rules and policies to achieve desirable banking environment (Muagbalu,2004). Kama (2006) says Nigeria banking failed to perform due to vulnerability and distress and macro-economic volatility. OkeandAdeusi (2012) support that Nigeria financial system in trying to be competitive in coping with regulation face with challenges of global financial system.

Concept of Regulation

Regulation is the declaration of a convincing set of rules, convoying some mechanism for monitoring and encouraging compliance with these rules (Baldwin, 2012). Black (2012) gave a more detailed definition of regulation as the sustained and focused attempt to alter the behaviour of others, according to defined standards and purposes with the intention of producing a broadly identified outcome or outcomes, according to Mendoza (2014), Regulation is an abstract concept of management of complex system according to a set of rules and trends. Efficient regulations can be defined as those where total benefits exceed total costs. From the above definitions, it can be seen that there is no universally accepted definition of regulation. However, it is obvious that regulation involves the control of activities aim for the good of the society in which they are enforced and to reduce the risk of manipulation.

Financial Regulation

Financial regulation is a ruleor supervision subjecting financial institutions to certain requirements,restrictions and guidelines, aiming at maintaining the integrity of the financial system,and financial regulatory authority is saddled with the responsibility of exercising autonomous authority over some area of human activities in carrying on financial services (Draxler,2006). Regulatory bodies can also be defined as organizations set up by the Government or an independent body with the responsibility to monitor, guide and control financial sector in the interests of depositors and consumers (Consumer Council, 2010).

Regulatory Bodies Functions

The foremost function of banking regulatory body is to create, implement and enforce policies or compliance that ensure that Banking activities are done in a proper and in an organized fashion (Westerfield, 2001). Also ensure financial soundness of the sector with adequate capital, good asset quality and management and liquidity,avoid system distress and financial liquidation, thereby not injuring the interest of the depositors, the consuming publics and for the economy to achieve growth. Some of the regulatory bodies in Nigeria are: National Insurance Commission,(NAICOM),Nigeria Deposit Insurance Company, Assets Management Company (AMCOM), Credit Risk Management System (CRMs)and others. The regulatory bodies are responsible for ensuring that financial institutions are solvent,not to jeopardize the depositors' interest, sector 12 of BOFIA 1991 as amended.

Banking

Banking is a business of accepting and lending money,safeguarding depositors' interest and the public (Kushimo, 2008), and to create credits,Glossar(2003) and White (2010),licensed to receive deposits, (Luther, 2002)and safe-keep valuables.

Historical perspectives of Banking in Nigeria

There is no accurate account of the history of banking as many scholars traced the history to Babylonian and Assyrian roots. (Heffernan,2005). The success of the new banking techniques and practices in Amsterdam and London helped spread the concepts and ideas elsewhere in Europe (Ahmad, 2010).

The end of the nineteenth century saw increasing dependency on banks as a pioneer of progress in economic development.In Nigeria, the Banking history started during the colonial era with the establishment of Colonial Banks which had the primary aim of meeting the commercial needs of the Colonial Government (Ajayi, 2015). Banking system in Nigeria is regulated through the Central Bank of Nigeria. This Central Bank of Nigeria started operation on July 1, 1959.

In 1892, what was known as African Banking Corporation and British Bank of West Africa, is now known as First Bank of Nigeria, The Anglo-Egyptian Bank and National Bank of South Africa of 1925 gave birth to Barclays Bank D.C.O and now known as Union Bank of Nigeria Plc, (Ojomolade,2009) and (Ajayi, 2015). In 1948, the British and French Bank was established later metamorphosed into United Bank for Africa.

The origin of indigenous bank in Nigeria started with the Industrial and Commercial Bank Ltd in 1929.Thereafter, many mush-room banks came up and died for lack of regulation, thereafter,Nigeria Merchant Bank 1931, National Bank 1933, the Agbonmagbe Bank 1945, the Nigeria Penny Bank 1947, A.C.B. (Tinubu Properties Ltd 1947) the Nigeria Agricultural Farmers and Commercial Bank (1947 - 1952). (Nyler (2015) Out of all these indigenous banks, only (3) three banks survived the 1940's runs due to support they received from their governments (Africa Continental Bank, National Bank and Agbonmagbe bank now known as Wema Bank). The Wema bank has absolved the National Bank. Ever since, the banking industry in Nigeria has grown to an enviable international standing.

Reasons for Banks' Failure

There were many reasons for banks failure in Nigeria in the early 40s which includes: Lack of legal framework: It was not until 1952 before the first law regulating banking was enacted in Nigeria. Lack of training and personnel: The people managing the banks did not have any training in banking and were not the right people to handle banking operations.Lowand inadequate capital base: The capital bases of the banks were inadequate in coping with the volume of transactions.Competition is another contention;the indigenous banks were competing with foreign banks with well trained personnel,therefore, leading to unhealthy competition and distress on the part of local banks. The level of Nigeria economic development was not ripe for such up-surge in the number of banks and their potency in mobilizing enough funds to sustain their operational activities.

Environmental Factors:

The environmental factors that affect the banks' operations positively or negatively were: management, economic, globalization,political, socio-cultural, governmentand technology with respect to: payment delivery, frauds, dishonesty on the part of the customers and operators.

2.6 Classification of the Banking into Era

(a. Era of free banking and foreign banking in Nigeria 1892-1957: This period was when Jacks and Harry engaged in banking activities in Nigeria without the required banking knowledge and banking culture. The period witnessed colonial or foreign banking dominance in Nigeria with well-trained personnel.

(b. The Era of Independent orLegal Banking (1958-1970): The banking system during this period witnessed a lot of banking regulations. The Banking Ordinance of 1952, the Central Bank Ordinance 1958, the Banking Ordinance Amendment 1962 and 1969 Banking Act now replaced with BOFID 1991. The 1968 Companies Act now repealed and replaced with the Companies and Allied Matters Act (CAM) now CAMA 1999.

(c. Era of Indigenization (1970-1985): This period was characterized with economic reconstructing and development; indigenization and rural banking.The period witnessed an increase in state banking and indigenous participation through the indigenization Decree of 1972. The Nigeria Enterprises Promotion Act 1977, now amended and replace with the Nigeria Investment Promotion Commission Decree 16 of 1995, enhance the Nigerian participation in the control of the economy.

(d. The Era of commercialization and liberalization of banking (1986-1992): The period of Structural Adjustment Programme (SAP,) 1986,witnessed establishment of various types of financial institutions – commercial and merchant banks. Finance houses, mortgage institutions and community banks. Decree No. 22 of 1990 set up the Nigeria peoples' bank and the community banking came into being by government budget announcement of 1990.

(e. The Era of Bank Distress, Rehabilitation and Restructuring (1992 – 2004): According to Ebhodaghe, (1995) distress means inability to manage bank properly. The dreadful issue that follows upsurge in the number of licensed banks was distressed, unhealthy competitions, inadequate capital base due to inflation and mismanagement. The CBN took over the management of five banks and liquidated 26 banks in 1996-1998; while 4 bank licenses were revoked. The government quickly intervenes in restructuring and revitalizing the sector due to its significant importance in the economic development and growth. The CBN Decree No. 24 and BOFID Decree No. 25 of 1991 were promulgated to sanitize the banking industry. Failed Banks (Recovery of debt) and Financial Malpractices in Banks, Decree No. 18 of 1994 and Money Laundry Decree No. 3 were also promulgated, all to revamp the economy, and restore confidence in the investing public.

(f. The Era of Recapitalisation, Merger and Consolidation (2006-date): Governor of C.B.N. in June 2004, announced an increased in bankcapitalizationfrom N2b to 25b irrespective of their formal capital base. The reasons were to allow banks to undertake large investmentsopportunities, participate in offshore banking businesses and avoid the problems of systemic and financial distress, however, the N25b capital base leadto banks' merger, andmany banks failures for not meeting the prescribed capital base.

Financial Sector Reforms in Nigeria

The bank regulations and reforms include the 1952 Banking Ordinance amended in 1958 and 1962 and repealed by Banks and other Financial Institutions Decree (BOFID) of 1991, Central Bank of Nigeria Act (CBN), the Nigeria Deposit Insurance Corporation (NDIC), the Securities and Exchange Commission (SEC), the Federal Ministry of Finance and the Financial Services Regulatory Coordinating Committee; and the Company and Allied matters Decree 1990 as amended.The Basel 11, an international banking regulation based on three pillars of minimal capital adequacy, regulatory supervision and market disciplinewas adopted by the Nigeria banking system.

The banking crisis of 2008, made Central Bank of Nigeria articulated a blueprint known as "***The Project Alpha Initiative***" aimed at removing the inherent weaknesses and fragmentation of the financial system, integrating the various ad-hoc and piecemeal reforms and unleashing of the huge potential for the economy (Sanusi, 2012). The policy thrust was to grow the banks and reposition them to play the pivotal roles in driving development across the sectors of the economy. As a result, banks were consolidated through mergers and acquisitions, the capital base raised from N2 billion to a minimum of N25 billion, which reduced thenumber of banks from 89 to 25 in 2005, and later to 24 (CBN, 2011)

The challenges the regulatory authorities faced with the banks' reforms were enormous,the people's perception about the reform and problem to change regarding cashless policy; where people prefer to hold cash (M_1), excess liquidity in the system and unrelenting e-frauds in the banks coupled with systemic distress in the banking sector that needs to be checkmated to restore customers' and international confidence. .

Central Bank of Nigeria (CBN) has established relationship with Islamic banking organization in 2010/2011 for Islamic banking in Nigeria for the Muslim citizen and to address liquidity management matter relating to Islamic banking. The Assets Management Corporation of Nigeria was established to address the issues of toxic debts in the banks. CBN entered into inter-agency committee with FIRS Federal Inland Revenue Services, NASB, Nigeria accounting standard board, this is to enhance positive control and monitoring banking activities.

The government frowns at financial statements window dressing orcreative accountingthereby initiated the prudential guidelines of 1991 as amended to rescue the investing public interest. This policy classified portfolio as to performing, non-performing. The non-performing credits are also categorized into: (a) substandard (b) doubtful and (c) bad .Provision of 10% for non-performing credit of more than 91days but less than 180 days.The doubtful credit attracts 50% provision if principal and interest are not paid after 180 days but less than 360 days, while the bad credit is to be provided for with 100% after 360 days.

Odufu (2005) discussed and listed the shortcomings that lead to regulations as:(i) Insider abuse, (ii) Director's interest in credits,(iii) Lack of competency, weak and mismanagement, ethics and professionalism,(v) Prohibition of interlocking directorship, (vi) Unabated incidents of bad loans impairing banks capital adequacy,(vii) Conflict of interest and others and abuse of trust,and (viii) Misuse of information and Non conformity with standards and guidelines.

Empirical Review

Umar (2015) investigated financial regulation and Nigeria banking sector theoretically, found that there is positive relationship between regulation and banks,it boost the volume and value of transactions in the banking sector.Iganiga (2010) assessed the effect of financial reforms on the effectivenessof financial institution with emphasis on banking sector,using data from 1986,applying classical least square technique,found that the performance of the banking has been greatly influenced by the reform. Idowu (2010) investigated the effect of financial reforms on capital market, using time series data (1986-2010) applying ordinary least square regression found a negative relationship between the variables. Financial reform deterred capital market development. In Ningi (2008), explore the impact of CBN consolidation on the banking sector, they found a significance difference as CBN decision has changed the market structure, increase in efficiency and reliability of banks create opportunities for participants and increase intermediation potentials.

CONCLUSION AND RECOMMENDATIONS

The Nigeria financial system has high numbers of interlinked financial institutions with its up and down, pre and post independent, which made many of the institutions to fail (financial distress and liquidation)and gave the depositors and consumers breaking hearts while breathing for survival, led to loss of confidence by the investing public in the system.The failures have effects on the payment systems and consequential split-over effects on the economic growth.The government enacted laws,knowing the importance of financial institutions on economic development and growth, to enhance the system for effective and efficient performance, reduced systemic distress and enhance safety of the public funds and the economy. In order to rid the financial system of the ugly situation of systemic distress and sudden collapse andnot to jeopardize the interest of the investing public and the economy, financial regulation and management of financial institution becomesimperative or inevitable.

The Central Bank and NDIC has compelling roles which they played recentlyby re-established financial soundness into the banking sector as pivotal for economic development, thereby restoringcustomers' confidence in the banking. The regulators should continue to be pro-active and initiate risk-free based regulation, and strict penalty for deviation.There should be gradual and periodic increase in banks'capitalization in view of the high inflation in economy. Competency framework on banking professionalism should be encouraged. Creativity and innovativeness in banks should be tailed along regulations.

The regulators should be soundand capable of understanding the regulationsenacted for effective enforcement; all members' staff of financial institutions should be corporate governance compliance. The regulators should be pro-active in initiatingenduring regulations rather than been re-active to issues that affect the banks. The operators should be competent and have the capacity to manage the institution, such competency and capacity should be endorsed by Central Bank of Nigeria in collaboration with Chartered Institute of Bankers of Nigeria.

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