

THE NIGERIAN FINANCIAL MARKET AND THE CHALLENGES OF INFORMATION TECHNOLOGY-BASED OPERATIONAL SERVICES

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Abstract

This paper seeks to examine the Nigerian financial market and the challenges of financial intermediation using ICT-based services. The paper specifically looks at the role of information technology on the banking sector. The paper reveals that information technology has facilitated financial intermediation, through cost reduction and timely delivery of financial services. However, the paper observes that most banks in Nigeria are facing keen competition both within and outside the shores of Nigeria such as mass movement of high-asset based operations towards efficiency thereby combining their advantages of big assets with efficiency which further expands their market and narrows those of the banks with relatively lower assets. Besides, there is the problem of financial fraud aided by information technology. The paper therefore recommends that Nigerians banks should invest in both information technology and human capital to brace up to the challenges of the electronic banking and transaction. Finally, there should be legislative and judicial crackdown on financial crimes which has assumed a monumental dimension with the advent of information technology-based services..

INTRODUCTION

The financial system is created to move funds from surplus economic units to deficit economic units in order to produce goods and services and to make investment in new equipment and facilities so as to facilitate the growth of the economy and improve the standard of living of its citizens. It is generally recognized that financial system plays a catalytic role in the process of economic development.

The financial system of any nation is a function of the size of its economy. A growing economy places more responsibilities on the financial sector to mobilize the needed capital to facilitate production, generate employment and income. An economy that does not experience growth on sustained basis is likely to have a very passive financial sector as there are no incentives for investment. Through the process of growth, financial system offers a wide range of portfolio options for savers and issuable instruments for investors, a function often referred to as financial intermediation (Oke, 1989).

The Nigerian financial system comprises of various institutions, markets and operations that are in the business of providing financial services. These institutions can be broadly categorized into money and capital markets while money market is a market in which short term financial instrument are traded, the capital market on the other hand deals with long term transactions.

The major players in the money market are the banks and discount houses. The intermediation role of banks ensures the mobilization of idle funds from the surplus units to the deficit sector. Just like the money market, the capital market is a major channel for mobilizing long-term funds. The main institutions are the Securities and Exchange Commission (SEC) which is the apex regulatory body, the Nigerian Stock Exchange

(NSE), the issues houses, stock broking firms and the registrars, (Olofin and Udoma, 2008).

However, with the liberalization of licensing of banks following the introduction of Structural Adjustment Programme (SAP) in the mid 1980s, the scope of banking in Nigeria expanded both in size and operation. According to Ochejele (2003) this development heightened the rate of competition among banks. The level of competition has been further intensified in this century because of the effect of globalization and integration of the banking industry into the global system.

Consequently, management of Nigerian financial institutions are faced with tremendous challenges and should brace up to these challenges. Thus only those institutions that are well positioned will become relevant and will be able to withstand the storm of competition. It is based on the foregoing that the paper wishes to examine the challenges faced by the Nigerian financial markets in the deployment of ICT-based services.

Theory of Financial Intermediation

Financial intermediation theory was first formalized in the works of Goldsmith (1969), McKinnon (1973), and Shaw (1973) who saw financial markets, both money and capital markets playing a pivotal role in economic development, attributing the differences in economic growth across countries to the quantity and quality of services provided by financial institutions. Corroborating this view is the result of a research by Nwaogwugwu (2008) and Dabwor (2009) on the stock market development and economic growth in Nigeria, the causal linkage. The result reveals that there is a bi-directional causality between growth in capital market activities and economic growth in Nigeria.

However, this contrasts with Robinson (1952), who argued that financial markets are essentially hand maidens to domestic industry, and respond passively to other factors that produce cross-country differences in growth:

“there is general tendency for supply of finance to move with the demand for it. It seems to be the case that where enterprise leads finance follows. The same impulse within an economy, which set enterprises on foot, make owners of wealth, venturesome and when a strong impulse to invest is fettered by lack of finance, devices are invented to release it... and habits and institutions are developed”

The Robinson school of thought therefore believes that economic growth will lead to expansion of the financial sector. Goldsmith (1969) attributed the positive correlation between financial development and the level of real per capita GNP to the positive effect that financial development has on encouraging more efficient use of the capital stock. In addition, the process of growth has feedback effects on financial markets by creating incentives for further financial development.

McKinnon's thesis is based on the complementarity hypothesis, which in contrast to the Neo-classical monetary growth theory, argued that there is a complementarity between money and physical capital, which is reflected in money demand. According to McKinnon, complementarity links the demand for money directly and positively with the process of physical capital accumulation because “the conditions of money supply have a first order impact on decision to save and invest”.

Shaw (1973) proposed a debt intermediation hypothesis, whereby expanded financial intermediation between the savers and investors resulting from financial liberalization (higher real interest rates) and development increase the incentive to save and invest, stimulates investments due to an increase supply of credit, and raises the average efficiency of investment. This view stresses the importance of free entry into and

competition within the financial markets as prerequisites for successful financial intermediation.

McKinnon (1973) and Shaw (1973) argued that policies leading to the repression of financial markets reduce the incentive to save. They described the key elements of financial repression as:

- High reserve requirements on deposits
- Legal ceilings on bank lending and deposit rates
- Directed credit
- Restriction on foreign currency capital transactions
- Restriction on entry into banking activities

Though the McKinnon-Shaw framework informed the design of financial sectors reforms in many developing countries, country experiences later showed that while the framework explains some of the quantitative changes in savings and investment at the aggregate level, it glosses over the micro-level interactions in the financial markets and among financial institutions which affects the supply of savings and the demand for credit by economic agents and the subsequent effect on economic growth.

This shortcoming later formed the spring board for the development of agency theories of financial intermediation. One of the earliest attempts to interpret the experience of developing countries within this framework can be found in Stiglitz and Weiss (1981) which stressed the importance of imperfect information in financial markets and its effect on the overall allocation of resources and economic growth. They showed that credit rationings for example, may arise from imperfect information about the quality of potential borrowers.

The structuralist approach emphasizes structural problems such as market inefficiencies as the principal cause for economic backwardness of developing countries. They criticized the market clearing assumptions implicit in the financial liberalization school, especially the assumption that higher interest rates attract more savings into the formal financial sector (Van Wijnbergen, 1982 and 1983). Moreover, Van Wijnbergen argued that it could very well be the case that informal markets will provide more financial intermediation. Since institutions in this sector are not subject to reserve requirements and other regulations that affect financial institution in the formal sector. He also argued that in the event that informal sector agents substitute their deposits for that in the formal sector due to high interest rates, the unexpected consequence will be an adverse effect on financial intermediation and economic growth.

CHALLENGES OF THE NIGERIAN FINANCIAL MARKETS

i. Deployment of ICT in operational services

The Nigerian financial market was hitherto dominated by small assets-based banks that were not internationally competitive. Ovia (2002) noted that in repositioning the Nigerian financial market for competitiveness will involve the deployment of information technology to play dominant catalytic role in growing the market. Thus in the face of the keen competition in the industry, market players must devise new survival strategies. Financial institutions world-wide are compelled by the emergence of information technology to fast-forward to more radical transformation of business systems and models. It is in the same spirit that Bill Gates (2001) noted that:

“the successful companies of the next decades will be the ones that use digital tools to re-invent the way the work. These companies will make decisions quickly, act efficiently and directly touch their customers in positive ways. Going digital will put on the leading edge of the shock wave of change. That will shatter the old ways of doing business”.

We are now in a new era of technological revolution. Countries are beginning to compete and fight over control of information rather than natural resources. The vogue today is E-platform which implies offering financial services through electronic media to various customers irrespective of place, time and distance. A customer friendly environment with high quality service delivers needs to be created in order to enhance high patronage. To this end, improvement in banking technology and institutional arrangements for transmission mechanism as well as other operational areas of banking operations to ensure operational efficiency has become a compelling necessity. This encompasses electronic money, internet banking, telephone/mobile banking, reduction of cash transaction, smart card. ATM transactions and capacity to process high volume of transactions among others.

ii. Human resources management

The centrality of the human resource in enterprise management is a generally accepted dictum. It is in this light that management needs to make adequate investment in human factor. It should be noted that there is no competitive weapon more potent and effective in a financial market than the quality of its human resources. As remarked by Sanusi (1995) machines and advanced technology can provide informational and transactional convenience but only manpower can provide the credibility, creativity and care that can build long-term customer and client relationships. In other words, there is need for capacity building in our system to enable us cope with the wind of technological development. Besides, no matter how accurate or competent a computer is, it cannot feed itself with input and it can neither offer a welcoming smile nor a warm handshake (Ochejele, 2000). Banking (and indeed the entire sectors in the financial markets) is people-related and the quality of personnel will make the vital distinction between what constitutes a good bank and a bad one. Consequently, of all the challenges facing the Nigerian financial markets, human capital development is the most daunting.

iii. Fraud prevention and monitoring system

Another major challenge facing the industry is the need to minimize the high rate of frauds and other malpractices in the system. It is imperative that bank managers and other market players give greater attention to the subject of maintaining the highest ethical and professional standards in all their transactions and dealings with their customers. This entails having adequate knowledge of Code of Conduct and Banking Practice jointly designed by the Chartered Institute of Bankers (CIBN), Central Bank of Nigeria (CBN) and the Bankers Committee (General Assembly of Bank Chief Executives). Issues of business integrity, respect for legitimate laws and regulations, concern for the society in which a bank operates will become as much important as profit consideration in the 21st century. Currently, Nigeria has unenviable reputation as one of the most corrupt nations in the world (Dabwor, 2008). Just like the money market, capital market suffers from a number of malpractices perpetuated by the operators in the market, although the level of malpractices is not as pronounced as in the banking sector. Some major malpractices in the capital market as identified by Usman (2002) include "insider dealings, market manipulations, false trading; market rigging and false representations".

iv. Liquidity management

While it is expected that there will be more external resource inflow to fund growth of the economy in this country, financial institutions must recognize their primary role in internal resource mobilization. It is assumed that the economy is awashed with liquidity and substantial portion of this liquidity is held as idle cash balances outside the banking system. The business of resource mobilization should therefore be seen as a major challenge facing the industry. In addition to internal mobilization of funds, market operators must also ensure effective channeling of these resources to productive segments

of our economy. The responsibility of promoting the economy's growth should be seen as a major challenge by all firms in the industry. Fund mobilization and allocation should therefore form a major plank of management policies in this century.

v. *Full autonomy of the Central Bank of Nigeria*

The turnaround of the banking industry and indeed the economy would be difficult without an institutional and operational autonomy of the Central Bank of Nigeria (Ekundayo, 1996). The current situation where the apex institution is only given nominal autonomy which it cannot exercise effectively is not very healthy for the banking industry. The CBN should be given a leverage to establish its authority over its traditional area of jurisdiction. It is only with such authority that the apex institution will be able to formulate viable monetary policies and offer advisory services to the Federal Government on financial matters. To this, may be added the need for internationalization of the Nigeria capital market in spite of the malpractices in the market, the Nigerian Stock Exchange (NSE) has been intensifying efforts at encouraging cross-border listings. The NSE is reported to have signed a memorandum of understanding each with the Nairobi Stock Exchange, the Ghana Stock Exchange and the Johannesburg Stock Exchange NSE should endeavour to fight the malpractices to accentuate the internationalization of the capital market.

vi. *Need for Capital Adequacy*

One of the fallouts from deregulation exercise was the expansion of the financial markets in both size and scope of operation. This development heightened competition especially in the money market. As the number of banks increased, so was the seed of instability sown in the system leading to the trauma of distress. Many financial institutions collapsed. In the main, the financial system was in the turbulent waters of systemic distress. This shook the industry to its very foundation and exposed the weak financial structure of many banks. This posed a serious challenge for the need for adequate capitalization of the firms in the industry. The need for capital adequacy is explained by the solvency objective of banks. Solvency would ensure safe and continuous existence of banks and other financial institutions. Unless this objective is constantly considered, a day will come when the short-run objective of liquidity cannot be met. To protect banks against loss that would result from liquidation of long-term assets in meeting customers' demands for funds, there is the need to strengthen the bank's capital structure so as to provide cushion between capital stock and deposit liabilities (Ochejele, 1999).

vii. *Technological Innovation*

Innovation is another challenge facing the financial markets in the country. Innovation implies new way of doing things. A likely situation that may characterize some organization is the possibility of complacency. Experiences have shown that once some organizations have attained certain regulatory provisions, there would be no further incentive for improvement. It should be pointed out that there is "no bliss point" as far as any system's operation is concerned. This forms the basis of the current literature in management christened. Total Quality Management (TQM), management needs to develop ways that have never been tried before and ways that will give the organization a real edge over its competitors. This calls for the establishment of research department that will monitor development in the markets, the economy and the world at large so as to timely advise management accordingly. Innovation can be achieved through rigorous analysis of current processes, expectations, market, innate experience and common sense with a view to working out a new way of doing things. This challenge also entails strategic business management which allows an organization to be proactive rather than being reactive in shaping its own future. Strategic management allows an organization to formulate and implement better decisions through the use of systematic, logical and

rational approach to strategic choice. One of the benefits of this approach is the empowerment of an individual and the strengthening of his decision-making capacity.

The increase in the number of financial institutions also witnessed an upsurge of crimes perpetrated by individuals and financial institutions. One area which remains a thorny issue for the banks is the high propensity for default by many bank debtors in the country. This has seriously vitiated risk asset quality of many banks despite the promulgation of *offence and Penalties Against Financial Malpractices Decree 18*. The decree makes it an offence against any bank's employee who flagrantly grants any facility with defective security or any bank customer who defaulted payment of facility granted him. This problem of non-performing risk assets of banks has remained a critical issue in which banks have to contend with.

As earlier indicated, the deregulation of the Nigerian economy marked a watershed in the national economy. This development resulted in influx of firms into Nigerian financial markets. Coupled with the wave of globalization, enterprises now face greater number of competitors. Apart from indigenous firms, foreign firms have started spreading their tentacles to the frontiers of the Nigerian financial markets. The pace of globalization as being experienced in the country has been mainly unidirectional; i.e. influx of foreign companies into the domestic financial and oil markets without corresponding investments by our indigenous investors in international money and capital markets. As a mean of diversifying their investment outlets, firms in the financial markets should start to look beyond the shores of the country for investment opportunities in the advanced countries where returns on investments are much higher and investment climate more stable.

RECOMMENDATION

Nigerian banks need to embrace information technology. This is one of the preconditions for a nation to be integrated into the global financial market and reap the benefit thereof.

Banks must train their staff in e-banking which has the advantage of reducing cost of transactions and increasing the speed of transaction and profitability.

There is the urgent need to have an all encompassing legislation on fraud and fraudulent activities, not only in the financial system but in all aspect of human endeavour. China is now an economic giant because of its enforcement of capital punishment on fraudsters and economic saboteurs (Cyber Crime, ATM) etc.

The industrial and agricultural sectors are comatose. As a result, banks indulge in speculations and other unethical conducts some of which led to huge toxic assets in the banking sector and near collapse of the capital market. The Nigerian economy therefore, needs to be diversified.

The regulatory bodies in the financial markets such as the Central Bank of Nigeria (CBN) and Securities and Exchange Commission (SEC) should be granted complete autonomy. This will enable them fight the malpractices in the system and also formulate viable monetary policies that will insulate the financial markets and the economy at large against domestic and external macroeconomic shocks.

Since we are now in a global village, financial institutions should look outside the shores of Nigeria for investment opportunities and portfolio diversification where returns on investments are relatively higher with stable macro economies.

The Assets Management Company of Nigeria (AMCON) should be nurtured and strengthen to enable it play its role of managing assets of commercial banks. This will help build confidence in the financial markets in Nigeria as no bank will any longer deceive investors with false balance sheet.

CONCLUSION

The Nigerian financial markets have grown in leaps and bounds in the last two decades. The proliferation of players in the markets has posed some challenges to the various market participants as well as the regulatory authorities charged with the responsibilities of overseeing different aspects of the markets. In attempting to unfold the challenges facing the financial markets recently, projections are made on the operating business environment. These projections are indexed on the current developments in the market, the economy and the world generally. Although one cannot be exact or certain about the totality of what this century will present, it is however an inescapable fact that a large number of hypotheses posited here will come to pass. The consequences of some of the forces of megatrends may become challenges or opportunities or both for the market players.

The challenges identified in this paper flow directly from Nigerian business environment, the development of the markets and the activities of the market participants. To remain relevant in the twenty-first century, banks and other financial institutions need to adequately address the challenges posed by the deployment of information technology.

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