

Effects of Economic Recession on Nigerian Banks: A Case Study of Kaduna State

Kudirat I. Adebisi

Department of Business Education, Federal College of Education, Zaria, Nigeria
kiadebisi@gmail.com

Abstract

Nigeria, the world recognized economic hub of African continent because of her natural and human resources experienced low economic activities as a result of what experts refers to as economic recession. The purpose of this study was examined effect of economic recession on Nigerian banks in Kaduna State. Quantitative approach, and a survey method with 41 commercial bank employees in Kaduna State. Pearson Product Moment Correlation Coefficient (PPMC) was used to test significant relationship between variables in hypotheses. Results suggested that economic recession has negative relationship on bank's lending to customers in Kaduna State. Findings showed negative relationship between economic recession and bank's loan recovery. The paper found negative relationship between economic recession and banks stability in Kaduna state. In view of the findings, this paper concluded that recession leads to decline in gross domestic products; increases unemployment rate, high inflation rate and poor living standards of people. The study was assessed using both managers and loan officers from commercial banks in Kaduna State. There is need for central bank of Nigeria to assist commercial banks during economic recession with special funds to enable banks to fulfill its obligations to customers. The results of this study contribute to the frontier of knowledge regarding the effects of economic recession on bank's lending, loan recovery and banks stability.

Keywords: Economic Recession; Bank's Lending; Loan Recovery; Bank stability; Nigerian Banks

Introduction

Nigeria, the world recognized economic hub of African continent because of her natural and human resources experienced low economic activities as a result of what experts refers to as economic recession. Adeniran and Sidiq (2018) researched on the economic recession and the way-out: Nigeria as a case study and described that Nigeria, the hub of West Africa's economy has remained stagnant, following the declaration of global economic and financial crises which became major concerns for political leaders, economists and managers of financial institutions across the globe. Economic recession can be noticed in the declined GDP as well as poor living standard of people. Okibe and Ogwa (2018) looked into the current economic recession in Nigeria opined that though alleged to be global problem is more felt in developing countries Nigeria inclusive. Economic recession in Nigeria was confirmed by the Central Bank of Nigeria (CBN) Governor Godwin Emefiele and the Minister of Finance, Kemi Adeosun that Nigeria's economy was officially declared to be in a technical recession based on the new trend figures released. This implies that government at all levels and Nigerians should prepare to face the hardships which usually accompany recession whenever it occurred. The GDP, revenue generation, and general prices of goods and services of the country would be affected.

National Bureau of Statistics, (2016) researched on the labor force statistics: unemployment and under-employment report summary. Q1-Q3 2017, found that economic activities as measured by the gross domestic product (GDP) declined by 0.36 percent in the first quarter, 2.06 per cent in the second quarter and 2.24 percent in the third quarter. These imply Nigeria experienced economic recession in 2016. During economic recession government revenue stand remain at lowest, interest rate went up, and payment of worker salaries become a big task. The impact of economic recession on financial institution is inability of people to save money; borrowers were unable to

repay their loans resulting to increase bad debts for banks. Komolafe (2016) looked into how economic recession constrained banking in 2016 and noted that 2016 was a year Nigerian bankers would not want to experience again. It was the year the industry suffered heavily from the worst nightmare of bankers – bad loans. It has been observed that economic recession negatively affect Nigerian bank's performance as regards bank's lending to customers, loan recovery and interest rate because most of the loans granted to individual and corporate organization may not be repaid during this period which lead to increase in bad loans. Financial Stability report of the Central Bank of Nigeria (CBN), documented that banks recorded N1.02 trillion bad loans in the first half of 2016. Non-performing loans (bad loans) in the period under review grew by 158 per cent from N649.63 billion at end-December 2015 to N1.68 billion at end-June 2016, the CBN stated. As a result, the ratio of bad loans to total loans more than doubled to 11.7 percent in the first six months of the year from 5.3 percent at the end of 2015. This implies that for every N100 of loan granted by banks, borrowers could not repay N11.30. In view of this, the paper hypothesized that there is a significant relationship between economic recession and bank lending.

Literature Review

According to Mckinney (2017), economic recession is a general downturn in any economy. A recession is associated with high unemployment, slowing gross domestic product, and high inflation. It can be described as reduction in economic activities of a particular country. Merriam-Webster Online Dictionary, 2018 refers recession to a business cycle contraction which results in a general slowdown in economic activity. It can also be view as a decline in GDP and increase in the local price of goods and services in a particular country. According to US National Bureau of Economic Research economic recession is defined as a significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real gross domestic products, real income, employment, industrial production and wholesale-retail sales. National Bureau of Economic Research (2016), defines recession as a significant decline in economic activity spread across the global economy, lasting more than a few months. Nigeria experienced high inflation rate during economic recession. There was increase in the general price of goods and services as people complaining of low circulation of money in the economy.

According to Okibe *et al.* (2018), economic recession has led to high inflation. Shobo (cited in Komolafe, 2016) explained that banking business was also affected by rising inflation in 2016. According to the NBS (2016), Nigeria's economy growth has been decelerating since Q2 2014 culminating in an economic recession in Q2 2016. The technical indicator of a recession is two consecutive quarters of negative economic growth measured by country's gross domestic product. The economic recession was technically over in Q2 2017. An economic recession is consistent with an increase in unemployment as jobs are lost and new jobs creation is stalled. However, several economic activities are still contrasting or recovering sub optimally. Itsibor (2017) discussed how CBN's efforts helped Nigeria's exit from economic and concluded that evidence has shown that beyond its key mandate of banks and other financial institutions regulations, the CBN's intensive complementary roll in recent time are yielding the desired results in no small measure. For instance, as part of efforts to get the economy back on the part of recovery and growth, the central has more than ever, performed some outstanding developmental functions, focused on key sectors of the Nigerian economy–financial interventions, agriculture and industrial sectors through the different departments of the bank. Between 2016 and now, the CBN has made unprecedented interventions in the country's agricultural sector. CBN in November 2015 rolled out N40 billion naira Anchor Borrowers Programme (ABP) aimed at empowering about 600,000 farmers to increase capacity utilisation in the agro-allied industry from the current levels of less than 50 per cent to at least 70 per cent and achieve self-sufficiency in food production by 2020.

Economic Recession and Bank's Lending Rate

Bank lending is the total amount of money that has been lent by banks in a country or region (Cambridge Business English Dictionary, 2018). While, economic recession referred to economic crisis, or financial crisis; it is a period of economic slowdown that is characterized by declining productivity and devaluing of financial institutions often due to reckless and unsustainable money

lending (Adeniran, *et al.* 2018). The effect of recession was felt in the bank lending policies in Nigeria as many banks were afraid of giving out loan to private individual and corporate organizations and government. Mckinney (2017) observed that poor and irrational lending policies from the financial industry led many people to buy houses they could not afford because everyone thought housing prices would continue to rise. In 2006, the bubble burst as housing prices started to decline. An escalating foreclosure rate caused panic, many banks and hedge funds who had bought mortgage-backed securities on the secondary market suddenly realized they were facing huge loses. By August 2007, banks became afraid to lend to each other because they did not want these toxic loans as collateral. This led to the \$700 billion bailout from the government to help save several large financial institutions from bankruptcy. By December 2008, employment was declining faster than in the 2001 recession, and the United States fell into. Dvorkin and Shell (2016), looked into bank lending during recessions: tightening of lending standards can account for part of the negative loan growth during the 2007-09 recession and noted that loan growth at commercial banks decreased substantially and remained negative for almost four years after the 2007-08 financial crisis. Based on the above evidences, this study hypothesize that economic recession has a relationship with bank's lending.

Economic Recession and Bank's Loan Recovery

The CBN and NDIC conducted a stress test on the banks in the country during the Great Recession of 2007-2008; only fourteen scaled through, while ten were adjudged to be in distress, with substantial non-performing loans; weak capital adequacy; poor corporate governance and illiquidity (Sanusi, 2011). This necessitated the establishment of the Nigerian "bad bank", the Asset Management Company of Nigeria (AMCON), which acquired the toxic assets from banks balance sheets and supplied liquidity to the banking system to avoid bank runs and systemic banking failures. Teniola (2017) in his article remarked that our financial services sector has, for the past year, teetered on the cusp of a monumental breakdown. Banks call in loans; borrowers don't have the money to pay and one by one the dominoes fall. To put this into perspective, non-performing loan ratios for Nigerian banks are reported to have reached 14% as at June 2017 – that is almost three times above the 5% limit imposed by the CBN. These loans are taken out of depositors' funds and shareholders' funds. Skye Bank was already a victim of a major bank falling to bad debt and non-performing loans.

A very important consideration in the recession is how the banks reacted to rising ratios of non-performing loans. To reduce their ratios, they have begun reducing the amount of loans granted to the private sector. Another reaction is in reduced lending to the private sector with bank lending favouring the public sector. In response, the CBN further tightened money supply, increasing the Monetary Policy Rate (MPR) first to 12% in March and then to 14 percent in July. In addition, the CBN increased the Cash Reserve Ratio (CRR) of banks to 22.5% from 20 percent. This translated to 300 basis points increase in the MPR and 250 basis point increase in the CRR. While the aim was to attract more savings into the banking system and dollar investments into the economy, these moves, however, led to the withdrawal of about N2 trillion from the banking system, thus reducing the money available to banks to do business. It also increased their cost of funds, which translated to reduction in interest rate margins. Based on the above evidences, this study hypothesized that economic recession has a relationship on banks stability.

Economic Recession and Bank's Stability

Omotola (2013) explained that the stability of banks and other financial institutions in the country were also threatened by the crisis. Many of the banks were already exposed to the oil and gas sector when it was booming and were left counting their losses when oil prices fell. Others had also placed huge bets on the stock market and it was estimated that the banks lost over 900 billion to the stock market crash. Huge loans had also been granted to firms and individuals who defaulted on payment and to make matters worse, the loans were not backed by adequate collateral. The Non Performing Loan (NPL) ratio of the banks rose to 20.7% in 2009, which is close to the 22% NPL that preceded the banking consolidation of 2007. The banks were already filled toxic assets and facing serious liquidity challenges, which impaired their ability to give

credits to the real sector. Many of the banks even had to downsize on staffs and tighten expenditure to scale through the challenges; thus increasing the number of the unemployed in the country.

The CBN has entrenched stability in the currency market, while market confidence has rebounded following the introduction of various foreign exchange regimes including the importers and exporters and small and medium enterprises (SMEs) windows; a development experts say was instrumental to the attractive level of capital imported into the country in the second quarter of this year, 2017. Data from the released by the NBS (2017) on its Q2 -2017 Capital Importation Report, showed that the domestic economy recorded notable improvement in capital inflows review period, expanding by 97.34 per cent q/q and 71.98 per cent year -on -year to \$1.79 billion, from \$908.27 million and \$1.04 billion respectively. Portfolio Investment rose from 145.69 per cent quarter-on -quarter and 128. 43 year -on -year to \$70.51 million, accounting for the most inflows into the country in the three months to June, followed by other investments in the form of loans (95.02% q/q and 43.59 per cent year- on- year to \$747.47 million), and Foreign Direct Investment (29.80% q/q and 48.88% y/y to \$274.37 million). While the apex bank's management stands firms on its determination to endear proper and more professional banking system in the country, it has assured of its continued intervention in the inter-bank Foreign Exchange market in order to sustain liquidity and stability in the sector. Based on the above evidences, the study hypothesizes that economic recession has a relationship with bank's stability.

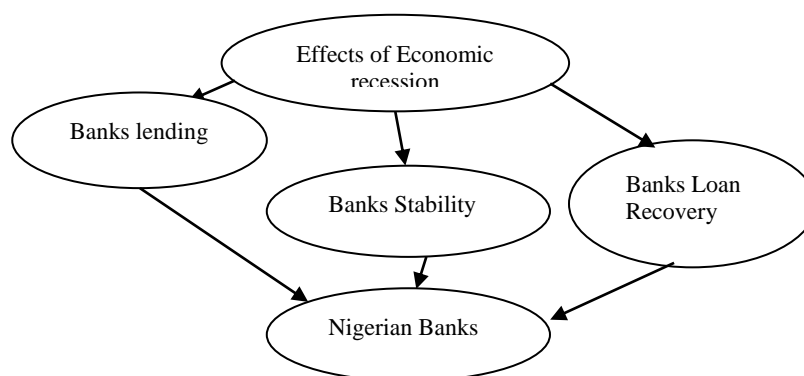


Figure 1: Effects of Economic Recession on Nigerian Banks

Figure 1 above illustrates a conceptual framework that models a relationship between independent variable (economic recession) and the dependent variable (Nigerian commercial banks stability) which could be determined by (bank lending, and loan recovery by banks). In turn, the independent variable (bank lending, and loan recovery by banks) and the dependent variable of Nigerian banks stability have been conceptualised with the use of a conceptual framework above that uses the idea of research model. It also shows how bank lending and loan recovery process impacts commercial Nigerian commercial banks stability. Economic recession usually slow down or lead to total short down of business activities in the country. During recession banks customers may not willing to make more deposits with banks, instead, they withdraw more money saved with banks thereby decrease banks cash and ability to lend to customers. In addition, loan recovery is difficult during recession which threatened commercial banks stability. In view of this, economic recession has shown to have a negative relationship on Nigerian commercial banks.

Methodology

This paper looked into the recession effect on a Nigerian State. Both empirical and descriptive survey method was used for this study. Population was 45 employees from four commercial banks in Kaduna State. Sample was 41 commercial banks workers in Kaduna state using Krejcie and Morgan (1970) table for sample size determination. Data collection instrument was questionnaire titled Effects of Economic Recession on Nigerian Banks Questionnaire (EERNBQ).

This questionnaire was duly validated and its reliability tested at 0.786. Data were analyzed using both descriptive and inferential statistics Pearson Product Moment Correlation Coefficient (PPMC) to test the significant difference among variables in null hypotheses 1-3 at 0.05 significant level.

Results

H1: There is a significant relationship between economic recession and banks lending.

The results of the significant relationship between economic recession and banks lending are presented below:

Table 1: Relationship between economic recession and banks lending

Variable	Correlation		
	r	N	p
Economic Recession and Bank's Lending	-.982	41	.0001

Relationship is significant at 0.05

The above showed that there is a strong and negative significant relationship between economic recession and banks lending ($R = -.982, p = .000$). Therefore, we accept hypothesis H1 since a relationship is confirmed to exist between the two variables.

H2: There is a significant relationship between economic recession and loan recovery by banks.

The result of the relationship between economic recession and loan recovery by banks is presented below.

Table 2: Relationship between economic recession and loan recovery by banks

Variable	Correlation		
	r	N	p
Economic Recession and Loan Recovery by Banks	-.202	41	.0006

Relationship is significant at 0.05

The above showed that there is a strong and negative significant relationship between economic recession and loan recovery by banks ($R = -.202, p = .0006$). Therefore, we accept hypothesis H2 since a relationship is confirmed to exist between the two variables.

H3: There is a relationship between economic recession and banks stability.

The result of the relationship between economic recession and bank's stability is presented below.

Table 3: Relationship between economic recession and bank's stability

Variable	Correlation		
	r	N	p
Economic Recession and banks stability	-.504	41	.0012

Relationship is significant at 0.05

The above showed that there is a strong and negative significant relationship between economic recession and banks stability ($r = -.504, p = .0012$). Therefore, we accept hypothesis H3 since a relationship is confirmed to exist between the two variables.

Discussion

Hypothesis one which states that there is a relationship between economic recession and banks stability was retained because a strong and negative significant relationship was found between economic recession and banks lending ($r = -.982, p = .000$). Based on the results, it was discovered that economic recession affect bank's lending to customers. This indicated that

banks were afraid of giving out loans to customers during recession because of low economic activities in the country which affect individual businesses, trade and investment, reduction in the national gross domestic product. In recession, government activities were affected as revenue generation decline to the extent that salaries of public workers were delayed, and contractors were owed. With this situation, commercial banks recorded low deposits and cash deficit which make it impossible to lend to individual customers, cooperate organizations and government. This finding agreed with Adeniran *et al.* (2018) that economic recession is a period of economic slowdown that is characterized by declining productivity and devaluing of financial institutions often due to reckless and unsustainable money lending. In order to avoid this, hypothesis two was retained because, a strong and negative significant relationship was established between economic recession and loan recovery by banks ($r = -.202, p = .0006$). This result shows that borrowers were unable to pay back loans secured from banks during economic recession. This implies that during economic recession commercial banks experiences increased cases of bad debt profile and non-performing loan ratios for Nigerian banks is at its peak at recession period. With this scenarios, the performance of banks were rated to be low which means that banks stability is at risk. This finding correlated with financial stability report of the Central Bank of Nigeria (CBN) (2016), that banks recorded N1.02 trillion bad loans in the first half of 2016. Non-performing loans (bad loans) in the period under review grew by 158 per cent from N649.63 billion at end-December 2015 to N1.68 billion at end-June 2016. As a result, the ratio of bad loans to total loans more than doubled to 11.7 percent in the first six months of the year from 5.3 percent at the end of 2015. According to the CBN, interest rate contributions (interest margins) to total income of banks declined to 54.3 percent in the first half of 2016 from 63.8 percent in December 2015.

In order to improve loan recovery process, the CBN and commercial bank managements should embark on client appraisal to determine the suitability or otherwise of the customers to repay back loan granted before given out loans. CBN should also review upward the recapitalization funds of commercial banks so as to guarantee their stability during recession. The loan collection process of the banks should be improved upon by adapting a more stringent policy to a relax policy for effective and efficient loan recovery. Hypothesis three which states that there is a relationship between economic recession and banks stability was retained because, there is a strong and negative significant relationship between economic recession and banks stability ($r = -.504, p = .0012$). This result shows that banks performance were at decline as a results of slow down economic activities which reduce savings from individuals, cooperate organizations and government and at the same time increase withdrawer of funds from banks. This usually leads to cash crunch without deposits, many commercial banks has closed shops while others merged together with new name. The paper finding showed that economic recession result into poor standing of banks. Ndugbu and Peter (2015) researched into monetary policy and the performance of deposit money banks-the Nigerian Experience. They found that amongst all the monetary policy variables (bank deposit rate, bank lending rate, cash reserve ratio and liquidity ration) considered in the model, only bank deposit rate has significant relationship though inverse relationship.

Conclusion

In view of the findings, this paper concluded that economic recession leads to decline in gross domestic product; it increases unemployment rate and result into high inflation rate with negative effects on the prices of goods and services as well as poor living standards of people. This paper has brought into limelight some of the positive and negative lessons learnt from recession. Both government and individual have learnt to inculcate the habit of saving for the dry session. Furthermore, the economy diversification is been seen to be possible solution to economy recession. Based on the findings, this paper recommended that federal, state and local government should put in place laws that would encourage firms to employ the service of local technician to help in fixing equipments. This would increase employment opportunity for young. Federal and state government should review existing economic planning and policies to meet international best practices. This would make people to take government serious in terms of provision of enabling environment for investors to come into the country to establish new businesses that

would not only provide jobs for unemployed youths but also, improve the revenue generation for the government.

References

- Abimbola H.O. (2013 November 11). Impact of the global financial crisis on the Nigerian economy. Retrieved on 14th August, 2018 from: ray.echebiri@businessworldng.com.
- Adamu, A. (2009). The effects of global financial crisis on Nigerian economy. DOI: 10.2139/ssrn.1397232.
- Adeniran, A.O. and Sidiq, B.O. (2018). Economic recession and the way-out: Nigeria as a case study. *Global Journal of Human Social Science: E-Economics*, 18 (1), 1-2.
- Cambridge Business English Dictionary. Definition of bank lending. Cambridge University Press. Accessed from: <https://dictionary.cambridge.org>, 2018.
- Dvorkin, M. A. and Shell, H. (2016). Bank Lending during recessions: Tightening of lending standards can account for part of the negative loan growth during the 2007-09 recession. Accessed on the Retrieved on 14th August, 2018 from: <https://doi.org/10.20955/es.2016.2>.
- Itsibor, Mark (2017, September 11). How CBN's efforts helped Nigeria's exit from economic recession. Accessed on August 14, 2018 from [www.leadershipngr](http://www.leadershipngr.com), 2018.
- Krejcie, R.V. and Morgan, D.W., (1970). Determining sample size for research activities. *Educational and Psychological Measurement*. Available at: <https://www.kenpro.org/tag/krejcieand-morgan-tablefor-determining-sample-size>.
- Komolafe, B. (2017, January 1). How economic recession constrained banking in 2016. Nigerian Vanguard Newspaper. Available from: <https://www.vanguardngr.com/2017/01>.
- Mckinney, P. (2017). What is economic recession? definition, causes and effects. Accessed on August 23 2018 from: <https://study.com/academy/lesson>.
- National Bureau of Statistics (2017). Labor force statistics: unemployment and under-employment report summary.- Q1-Q3 2017. 1, 4. Available at: www.nigerianstat.gov.ng.
- National Bureau of Economic Research (2016). Economic recession in Nigeria: causes and solutions. Accessed from: [www.educainform.com/economic recession-Nigeria](http://www.educainform.com/economic-recession-Nigeria) on 6th July, 2018.
- Ndugbu, M.O. and Peter A.O. (2015). Monetary policy and the performance of deposit money banks -the Nigerian Experience. *European Journal of Business and Management*, 7 (17), 1-5.
- Okibe, O.G. and Ogwa, A.V. (2018). Influence of economic recession on the management of secondary schools in Benue State: Implication for counselling. *International Journal of Academic Research in Business and Social Sciences*, 8 (3), 610.
- Teniola Akeju (September 22, 2017). On Nigerian banks, loans and the economic recession. Retrieved August 14th 2018 from: articles@nairametrics.com