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RESEARCH ARTICLE

FINANCIAL SECTOR DEVELOPMENT AND ECONOMIC GROWTH IN NIGERIA

Onum Friday Okoh*

Department of Economics, University of Ibadan, Ibadan, Nigeria
Corresponding Author Email: onumfridayokoh@gmail.com

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ABSTRACT

For many years, financial sector development has been a focal point of policy reforms in Nigeria, aimed at stimulating economic growth. This study investigates the relationship between financial sector development and economic growth in Nigeria from 1980 to 2023. Using GDP as the dependent variable, and financial institution depth, financial market depth, exchange rate, and interest rate as independent and control variables, the research employs various econometric techniques, including descriptive statistics, unit root tests, cointegration bound tests, and the Autoregressive Distributed Lag (ARDL) model. The findings suggest that financial development has a significant impact on economic growth, with varying short-run and long-run effects depending on the specific measures of financial development. While financial market depth demonstrates a negative relationship with growth in the short run, financial institution depth shows a positive influence. The study underscores the importance of enhancing financial sector infrastructure to foster sustainable economic growth and concludes with policy recommendations and suggestions for further research on financial sector dynamics in developing economies.

KEYWORDS

Financial sector development, Economic growth, ARDL model, Financial market depth, Financial institution depth

1. INTRODUCTION

The quest for sustainable economic growth remains a central objective of macroeconomic policy across nations, with financial sector development often recognized as a critical catalyst in achieving this goal. A sound and efficient financial system enhances the mobilization and allocation of capital, facilitates investment, and supports innovation, thereby fostering economic progress. In Nigeria, successive financial reforms such as the Structural Adjustment Programme of 1986, banking sector consolidation, and the adoption of digital financial services have been implemented with the aim of strengthening the financial system and promoting growth. Despite these initiatives, the empirical relationship between financial development and economic growth in Nigeria has produced mixed results, prompting ongoing debate in both policy and academic circles. Theoretical perspectives diverge, with some positing a supply-leading role for finance in driving growth, while others argue for a demand-following relationship or a bi-directional interaction. This study investigates the extent to which financial sector development measured through financial institution depth and financial market depth has influenced Nigeria's economic growth between 1980 and 2023. Using gross domestic product (GDP) as the dependent variable, and incorporating exchange rate and interest rate as control variables, the study applies descriptive analysis, unit root testing, cointegration bounds testing, and the ARDL model to examine both short-run and long-run relationships.

1.1 Background to the Study

Economic growth and financial development are intricately linked, with numerous theoretical and empirical studies underscoring the pivotal role of a robust financial system in fostering sustainable development (Puatwoe et al., 2017). According to the study, an efficient financial sector enhances economic performance by mobilizing savings, facilitating capital allocation, and supporting technological innovation (Levine, 1997). It emphasized the importance of financial intermediaries in promoting entrepreneurship and innovation by identifying and funding productive ventures (Schumpeter, 1912). Similarly, they attributed the industrialization of England to the evolution of its financial system, which enabled effective capital mobilization (Bagehot, 1873; Hicks, 1969). Over the decades, researchers have presented differing views on the finance-growth nexus. The supply-leading hypothesis argues that financial development spurs economic growth, while the demand-following hypothesis posits that financial systems evolve in response to economic expansion (Robinson, 1952; Patrick, 1966). A third school of thought advocates a feedback relationship between the two variables. However, scholars question the significance of finance in driving growth, suggesting that overemphasizing its role may divert attention from more impactful policy areas (Lucas, 1988; Stern, 1989).

In the Nigerian context, financial reforms have been implemented to strengthen the financial system and stimulate economic growth. These reforms, beginning with the Structural Adjustment Programme (SAP) of 1986, introduced liberalization measures such as interest rate deregulation, credit control rationalization, and the licensing of new banks (IkhideandAlawode, 2002). Subsequent reforms include banking consolidation (2004), pension and insurance reforms (2005–2007), and innovations in financial technology. Despite these efforts, the impact of financial development on economic growth in Nigeria remains inconclusive. Some studies, such as those, reported a positive relationship using monetary indicators, while others, observed weak linkages, especially regarding the contribution of financial deepening to growth (Ogun, 1986; Edo, 1995; Akinlo and Akinlo, 2007; Ayadi et al., 2008; Nzotta and Okereke, 2009). Methodological limitations, such as the exclusion of relevant variables and the inability to capture short-run effects, may partly explain the divergence in findings. This underscores the need for further empirical investigation using more comprehensive indicators and robust econometric techniques, such as the ARDL model, to reassess the finance-growth relationship in Nigeria between 1980 and 2023.

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1.2 Statement of the Problem

Despite the implementation of numerous financial reforms aimed at liberalizing, consolidating, and strengthening Nigeria's financial sector, the extent to which these efforts have translated into tangible economic growth remains debatable. Empirical studies have yielded mixed and inconclusive results, with some pointing to a positive relationship between financial development and economic growth, while others suggest a nonlinear or even negligible connection. The limited exploration of asymmetric and nonlinear dynamics within Nigeria's context has further complicated understanding the finance-growth nexus. This complexity is heightened by the issue of endogeneity, where both financial development and economic growth may simultaneously influence each other, making it difficult to ascertain causality. Moreover, Nigeria continues to face persistent structural challenges such as low GDP growth, high inflation, and rising unemployment, which may hinder the potential of the financial sector to drive real economic progress. These concerns underscore the urgent need for rigorous empirical investigation that not only addresses methodological limitations but also evaluates both the short-run and long-run impacts of financial development using advanced econometric techniques. By doing so, the study seeks to fill the existing gap and provide clearer insights into how financial sector reforms affect real sector performance in Nigeria.

1.3 Research Questions

This study seeks to answer the following research questions:

- What is the short-run and long-run relationship between financial development and real economic growth in Nigeria?
- Do asymmetric effects exist in the relationship between financial development and economic growth in Nigeria?
- How do macroeconomic variables such as exchange rate and interest rate moderate the impact of financial development on Nigeria's economic growth?

1.4 Research Objectives

The main objective of this study is to evaluate the impact of financial development on real economic growth in Nigeria. The specific objectives are to:

- Examine the short-run and long-run relationship between financial development and real economic growth in Nigeria.
- Investigate the presence of asymmetric effects in the relationship between financial development and economic growth in Nigeria.
- Assess how macroeconomic variables such as exchange rate and interest rate moderate the impact of financial development on Nigeria's economic growth.

1.5 Scope of the Study

This study investigates the relationship between financial sector development and economic growth in Nigeria over the period from 1980 to 2023. It specifically examines how financial institution development and financial market development influence economic growth, with Gross Domestic Product (GDP) serving as the dependent variable. Exchange rate and interest rate are included as control variables to account for relevant macroeconomic effects. The study adopts quantitative econometric techniques, including descriptive statistics, unit root tests, cointegration bound tests, and the Autoregressive Distributed Lag (ARDL) model to analyze both the short-run and long-run dynamics of the relationship. By focusing exclusively on Nigeria within the stated timeframe, the research captures key economic and financial reforms that have shaped the country's financial landscape over the past four decades.

1.6 Structure of the Paper

This paper is organized to provide a comprehensive examination of the relationship between financial sector development and economic growth in Nigeria. The introduction outlines the background, problem statement, objectives, research questions, significance, and structure of the study. The literature review discusses key theoretical perspectives and empirical findings relevant to the financial development and economic growth nexus. The methodology section details the data collection process, model specification, and estimation techniques used for analysis. The empirical analysis presents the results of the data analysis, including descriptive statistics, unit root tests, cointegration tests, and ARDL estimation. The findings are summarized, conclusions drawn, and recommendations for policy and future research provided. The study concludes with a discussion of the limitations and suggestions for further research on the topic.

1.7 Financial System and Economic Performance in Nigeria

The relationship between financial sector development and economic performance in Nigeria has long been framed within two dominant schools of thought: the financial regulation-based and financial deregulation-based paradigms. The former emphasizes the role of regulated banking institutions in providing capital and market information to stimulate growth, while the latter asserts that market liberalization fosters a more efficient allocation of financial resources, enabling the financial system to effectively support economic growth and poverty reduction (Levine, 2002). Over the decades, Nigeria's financial sector has undergone significant reforms from the foundational years of central and commercial bank establishment to the structural adjustment policies of the mid-1980s, which introduced deregulation. These reforms included exchange rate liberalization, interest rate deregulation, and the creation of institutions such as the Nigerian Deposit Insurance Corporation to enhance stability and supervision in the sector (Ogwumike et al., 2012).

Despite numerous policy shifts, the financial sector's impact on Nigeria's real economy has remained limited. The 2004 banking consolidation program aimed to boost capitalization and improve financial intermediation by raising the minimum capital base of banks from ₦2 billion to ₦25 billion. While this reform led to the emergence of stronger banks with better access to funds and a shift toward risk-based supervision under the Basel II framework, the sector has struggled to translate these gains into inclusive economic growth. Poverty levels remained high despite financial reforms, as evidenced by the rise in relative poverty from 54.4% in 2004 to 69% in 2010 (NBS, 2010; Yusuf et al., 2013). This disconnect suggests that while the financial system expanded in structure and regulation, it failed to sufficiently mobilize resources for productive investment in the real sector.

The post-SAP era introduced further liberalization, with remarkable growth in both the number and diversity of financial institutions. Between 1986 and 1997, the number of commercial banks increased significantly, alongside community banks and non-bank financial institutions. The adoption of universal banking in 2000, combined with recapitalization and capital market reforms, led to increased market activities market capitalization surged from ₦6.8 billion in 1986 to ₦9.6 trillion by 2008. Similarly, innovations in financial instruments and foreign exchange reforms aimed at improving liquidity and transparency enhanced financial intermediation. However, challenges such as mismanagement, inefficiency, and political interference weakened the sector's ability to drive sustainable growth. Thus, while financial development in Nigeria has made notable strides, its overall contribution to economic performance remains a subject of critical inquiry and empirical validation (Dandume, 2014).

2. Literature Review

The relationship between financial development and economic growth has generated extensive academic discourse, with empirical studies across different regions offering diverse outcomes. While some studies affirm a positive relationship between financial sector development and economic growth, others report either a negative impact or no significant linkage. These divergent conclusions underscore the complexity of the finance-growth nexus and the influence of country-specific contexts.

Historically, the finance-growth debate traces back, who posited that a well-developed financial system stimulates technological innovation and economic progress by facilitating capital accumulation (Schumpeter, 1911). Later studies such as those, reaffirm this position, providing empirical evidence that financial sector development plays a crucial role in stimulating economic growth (King and Levine, 1993; Beck et al., 2000; Jeanneney et al., 2006). These studies, often panel-based, suggest that improved financial intermediation, risk management, and access to credit contribute significantly to productivity and GDP growth.

Particularly in Sub-Saharan Africa, studies have highlighted a generally positive impact of financial development on economic performance. For instance, documented that financial sector reforms have helped foster economic expansion in countries like Cameroon and South Africa (Tabi et al., 2011; Elie, 2015; Djoumessi, 2009). These findings support the perspective that financial development enhances access to capital, thereby spurring investment and entrepreneurship.

Contrary to this optimistic view, several studies have reported a negative correlation between financial development and economic growth, especially in developing countries. They argue that under certain conditions such as weak institutions, regulatory failures, or inefficient

allocation of resources financial development may actually hinder economic progress (Al-Malkawi et al., 2012; De Gregorio and Guidotti, 1995; Bernard and Austin, 2011). These findings point to the risk of over-expansion, mismanagement, and vulnerability to financial crises in economies with fragile financial systems.

In addition to positive and negative outcomes, some studies find no significant relationship between financial development and economic growth. For example, they contend that the two variables may be independent of each other (Levine and Zervos, 1996; Ram, 1999; Bloch and Tang, 2003). These studies suggest that while financial institutions may grow in size and number, they do not necessarily contribute to real economic activity unless supported by robust macroeconomic and governance frameworks.

Theoretical perspectives also offer competing explanations for the finance-growth link. The bank-based theory posits that banks are central to economic development by providing credit and market information (Levine, 2002). In contrast, the market-based view holds that capital markets play a more efficient role in resource allocation and risk sharing. A third view, the legal and institutional approach, emphasizes the role of strong legal systems and property rights in ensuring that financial development translates into economic growth (Upchurch, 2012).

In the Nigerian context, empirical findings are equally diverse. Studies such as those) found evidence of bidirectional causality between financial development and economic growth (Odeniran and Udeaja, 2010; Saibu et al., 2011. However, report a negative relationship between financial sector indicators and economic growth, attributing it to institutional inefficiencies and misaligned reforms (Marry et al., 2012). They further corroborates this by pointing out the weak transmission of financial development to economic growth in Nigeria due to a poorly functioning financial system (Ndebbio, 2004).

In conclusion, the literature reveals that while financial sector development holds potential to spur economic growth, its actual impact varies based on institutional strength, governance quality, and macroeconomic policies. In Nigeria, further research is needed to understand the structural bottlenecks hindering the financial sector from playing a more robust role in driving sustainable economic growth.

2.1 Theoretical Literature Review

The relationship between financial sector development and economic growth has been interpreted through various theoretical frameworks, each providing different perspectives on causality and impact. The supply-leading hypothesis, proposed, contends that financial development acts as a catalyst for economic growth by enhancing the allocation of resources, improving savings mobilization, and fostering innovation (Patrick, 1966). This theory is grounded in the ideas, who emphasized the importance of financial institutions in identifying and funding productive investments, especially those with innovative potential (Schumpeter, 1934). They extended this framework by introducing the concept of financial liberalization, arguing that deregulation of interest rates and removal of credit restrictions enhances capital accumulation and investment efficiency (McKinnon, 1973; Shaw, 1973). Similarly, they supported the notion that lower, regulated interest rates can stimulate growth by encouraging households to shift from holding money to investing in productive capital, thereby increasing the capital-labor ratio and economic output (Keynes, 1936; Tobin, 1965).

In contrast, the demand-following hypothesis maintains that economic growth precedes financial development. As economies expand, there is an increased need for financial services, which in turn drives the evolution of financial systems (Robinson, 1952; Patrick, 1966). This theory suggests that financial institutions develop in response to growing demand from businesses and consumers for credit and investment instruments (Allen and Ndikumana, 2000). The divergence between these two perspectives is especially relevant in developing economies like Nigeria, where structural challenges and institutional weaknesses may influence the effectiveness of financial reforms. Furthermore, endogenous growth models also reinforce the importance of financial intermediation, arguing that deeper financial systems contribute to long-term growth by efficiently channeling resources toward investment (Greenwood and Jovanovic, 1990; Pagano, 1993). Additionally, the role of capital markets highlighted underscores how stock market liquidity enhances long-run growth by enabling long-term investments (Levine and Zervos, 1998; Atje and Jovanovich, 1993). These theories collectively inform the analytical lens through which the nexus between financial development and economic growth is assessed, particularly in the Nigerian context.

2.2 Empirical Literature Review

A wide range of empirical studies has explored the finance-growth nexus, producing mixed findings that support various theoretical standpoints. Several studies validate the supply-leading hypothesis, which posits that financial development propels economic growth. They all report a positive relationship between financial development indicators and economic growth (King and Levine, 1993; Levine and Zervos, 1996; Levine, 1997; Arestis et al., 2002; Christopoulos and Tsionas, 2004; Acaravci et al., 2007). In the context of Sub-Saharan Africa, found evidence of a long-run causal link from financial development to economic growth in four out of ten countries studied, while one country exhibited growth-led finance, and the remaining five demonstrated a bidirectional relationship (Akinlo and Egbetunde, 2010). Similarly, identified a supply-leading relationship in three ECOWAS countries, demand-following in one, and bidirectional causality in two others (Esso, 2010). They also reported support for the supply-leading hypothesis in Sierra Leone (Kargbo and Adamu, 2009). In Nigeria, revealed a positive association between financial intermediation and economic growth, supporting the finance-led growth argument (Shittu, 2012).

On the other hand, some empirical evidence supports the demand-following hypothesis, which holds that economic growth stimulates financial development. Notable among these are the works (Lucas, 1988; Stern, 1989; Chandavarkar, 1992; Gurgay et al., 2007; Shahnoushi et al., 2008). The feedback or bi-directional hypothesis has also been empirically supported. They provided evidence that financial development and economic growth reinforce each other (Levine, 1997; Luintel and Khan, 1999; Demetriades and Andrianova, 2003). In the Nigerian context, employed a VAR-based Granger causality framework and found evidence of bidirectional causality (Odeniran and Udeaja, 2010). Similarly, observed that capital market activity significantly impacts economic growth in Nigeria, with bidirectional causality between economic growth and stock market transactions, and unidirectional causality from market capitalization to growth (Kolapo and Adaramola, 2011). They, using Granger causality, co-integration, and error correction methods, also found a bi-directional causal relationship between money supply and GDP in Nigeria (Osuji and Chigbu, 2012). These findings underscore the complex, context-dependent nature of the finance-growth relationship and highlight the need for further studies, particularly in developing economies like Nigeria, using robust techniques such as the bounds test and VAR-Granger causality.

2.3 Theoretical Framework

This study is anchored on three key theoretical frameworks that provide a foundational understanding of the relationship between financial sector development and economic growth: the Schumpeterian Growth Theory, the Endogenous Growth Theory, and the Supply-Leading and Demand-Following Hypotheses.

2.4 Schumpeterian Growth Theory

Proposed by, this theory posits that financial institutions play a critical role in promoting innovation and technological advancement, which in turn drives long-term economic growth (Joseph Schumpeter, 1911). Schumpeter emphasized the importance of financial intermediaries in channeling savings into productive investments, facilitating entrepreneurial activities, and encouraging the adoption of new technologies. This framework is particularly relevant to developing economies like Nigeria, where access to financial services can significantly influence the pace of innovation, industrialization, and productivity improvements.

2.5 Endogenous Growth Theory

Developed in the late 1980s by economists such as Paul Romer and Robert Lucas, the Endogenous Growth Theory suggests that economic growth is primarily driven by internal factors especially investments in human capital, innovation, and financial infrastructure. The theory argues that financial sector development enhances growth by improving capital allocation efficiency, encouraging savings, reducing transaction costs, and facilitating knowledge dissemination. This perspective supports the idea that a well-functioning financial system contributes directly to economic growth through sustained investment in productivity-enhancing activities.

2.6 Supply-Leading and Demand-Following Hypotheses

These two hypotheses represent differing views on the causality between financial development and economic growth. The supply-leading hypothesis asserts that financial development leads to economic growth by mobilizing savings, facilitating investment, and promoting efficient resource allocation. In contrast, the demand-following hypothesis argues that economic growth drives financial development by increasing demand for financial services. Both perspectives are crucial for this research, as they provide a dual lens through which the direction of causality between

financial sector development and economic growth in Nigeria can be examined. This dual framework allows the study to consider whether financial development precedes economic expansion or merely responds to it. Together, these theories form the foundation upon which this study explores the dynamic interplay between Nigeria's financial sector development and its broader economic performance.

3. METHODOLOGY

3.1 Data Collection and Sources

This study utilizes annual time series data from 1980 to 2023. The data on Gross Domestic Product (GDP), financial institution development (LFID), financial market development (LFMD), exchange rate (ER), and interest rate (IR) were sourced from the Central Bank of Nigeria (CBN) Statistical Bulletin and the World Development Indicators (WDI).

3.2 Model Specification

The study adopts the Supply-Leading Theory, which posits that financial sector development drives economic growth. The functional form of the model is expressed as:

GGDP = f(LFID, LFMD, ER, IR)

Where:

GGDP = Growth Rate of Gross Domestic Product

LFID = Log of Financial Institution Development

LFMD = Log of Financial Market Development

ER = Exchange Rate

IR = Interest Rate

The econometric form of the ARDL model is specified as:

$$\Delta GGDP_t = \alpha_0 + \Sigma\alpha_1\Delta GGDP_{t-1} + \Sigma\beta_1\Delta LFID_{t-1} + \Sigma\beta_2\Delta LFMD_{t-1} + \Sigma\beta_3\Delta ER_{t-1} + \Sigma\beta_4\Delta IR_{t-1} + \lambda_1 GGDP_{t-1} + \lambda_2 LFID_{t-1} + \lambda_3 LFMD_{t-1} + \lambda_4 ER_{t-1} + \lambda_5 IR_{t-1} + \varepsilon_t$$

Where: Δ denotes first difference, α_0 is the constant, α and β are short-run coefficients, λ represents long-run coefficients, and ε_t is the error term.

3.3 Estimation Techniques

The study starts with descriptive statistics and the Augmented Dickey-Fuller (ADF) unit root test to determine the stationarity of the variables. The Bounds cointegration test is used to verify the existence of long-run relationships among the variables. The ARDL technique is employed to estimate both short-run and long-run dynamics due to its efficiency in handling mixed levels of integration. Diagnostic tests for serial correlation and heteroskedasticity are also performed to ensure the robustness of the model.

3.4 Data Presentation and Analysis

Table 1: Summary of Descriptive Statistics of the Sample Data

	GGDP	LFID	LFMD	ER	IR
Mean	3.068566	0.049365	0.041182	120.6566	0.390945
Median	3.449434	0.045470	0.042705	114.8990	2.683386
Maximum	15.32916	0.074704	0.108727	450.8063	18.18000
Minimum	-13.12788	0.030833	0.014751	0.546781	-65.85715
Std. Dev.	5.197308	0.012838	0.022184	128.2132	13.76685
Skewness	-0.862635	0.574236	0.635281	1.069587	-2.793280
Kurtosis	4.964869	2.099855	2.940673	3.245480	13.74778
Jarque-Bera	12.53499	3.903620	2.966056	8.499926	268.9949
Probability	0.001897	0.142017	0.226949	0.014265	0.000000
Sum	135.0169	2.172046	1.812019	5308.890	17.20156
Sum Sq. Dev.	1161.517	0.007087	0.021161	706861.2	8149.620
Observations	44	44	44	44	44

Source: Researcher's computation, (Eviews-10) 2025

Table 1 presents the descriptive statistics for the variables used in examining the relationship between financial sector development and economic growth in Nigeria from 1980 to 2023. The dependent variable, GGDP (growth rate of Gross Domestic Product), has a mean value of 3.07, indicating modest economic growth over the period, but also reflects significant fluctuations, as shown by its wide range from -13.13 to 15.33 and a standard deviation of 5.20. The independent variables, LFID (log of financial institutions development) and LFMD (log of financial markets development), show relatively stable means of 0.049 and 0.041 respectively, with low standard deviations, suggesting less volatility. The control variables, exchange rate (ER) and interest rate (IR), display higher variability; ER ranges from 0.55 to 450.81 with a standard deviation of 128.21, reflecting Nigeria's volatile foreign exchange environment, while IR shows extreme values ranging from -65.86 to 18.18 with high kurtosis, indicating outliers and significant policy fluctuations over time. The Jarque-Bera statistics suggest that GGDP and IR are not normally distributed ($p < 0.05$), while other variables approximate normal distribution. Overall, these statistics highlight the presence of variability and potential non-normality in key economic indicators, justifying the need for robust econometric techniques like ARDL in the subsequent analysis.

Table 2: Summary of ADF unit root test result

VARIABLE NAME	ADF TEST	CRITICAL VALUES			LEVEL	CONCLUSION AT 5% S.L
		1%	5%	10%		
GGDP	-12.23349	-3.596616	-2.933158	-2.604867	**1st DIFF**	**STATIONARY**
LFID	-6.868697	-4.192337	-3.520787	-3.191277	**1st DIFF**	**STATIONARY**
LFMD	-7.025050	-4.192337	-3.520787	-3.191277	**1st DIFF**	**STATIONARY**
ER	-5.056923	-4.192337	-3.520787	-3.191277	**1ST DIFF**	**STATIONARY**
IR	-4.807434	-3.592462	-2.931404	-2.603944	**LEVEL**	**STATIONARY**

Source: Researcher's computation, (Eviews-10) 2025

Table 2 presents the Augmented Dickey-Fuller (ADF) unit root test results for the variables used in the study to determine their stationarity properties. The results reveal that GGDP (economic growth), LFID (financial institutions development), LFMD (financial markets development), and ER (exchange rate) were non-stationary at level but became stationary after first differencing, as their ADF test statistics exceeded the 5% critical values in absolute terms at first difference. This implies that these variables are integrated of order one, I(1). However, the interest rate (IR) was found to be stationary at level, indicating it is integrated of order zero, I(0). These mixed orders of integration justify the use of the ARDL (Autoregressive Distributed Lag) model, which is suitable for analyzing variables that are either I(0), I(1), or a combination of both, without the need for all series to be integrated of the same order.

Table 3: Summary of Cointegration Bound Test				
F-Bounds Test		**Null Hypothesis: No levels relationship**		
Test Statistic	*Value*	Signif.	I(0)	I(1)
F-statistic	8.330267	10.00%	2.2	3.09
K	4	5%	2.56	3.49
		2.50%	2.88	3.87
		1%	3.29	4.37

Source: Researcher's computation, (Eviews-10) 2025

Table 3 displays the results of the Cointegration Bounds Test used to assess the existence of a long-run relationship among the variables. The calculated F-statistic value of 8.330267 exceeds the upper bound critical value at the 1% significance level (4.37), as well as at all other conventional levels of significance. This implies that the null hypothesis of no long-run relationship can be rejected, indicating the presence of a statistically significant level relationship among economic growth (GGDP), financial institution development (LFID), financial market development (LFMD), exchange rate (ER), and interest rate (IR). Hence, there is evidence of cointegration, suggesting that the variables move together in the long run despite being individually non-stationary at level.

Table 4: Summary of ARDL Short-run impact of financial development on economic growth				
Selected Model: ARDL(1, 0, 0, 0, 1)				
Variable	Coefficient	Std. Error	t-Statistic	Prob.*
GGDP(-1)	-0.104	0.161	-0.646	0.522
LFID	10.108	14.319	0.706	0.485
LFMD	-8.779	4.732	-1.855	0.072
ER	-0.004	0.027	-0.153	0.879
IR	-0.151	0.225	-0.671	0.506
IR(-1)	0.294	0.152	1.933	0.061
C	2.202	43.548	0.051	0.960
ECT	-1.104	0.146	-7.558	0.000

Source: Researcher's computation, (Eviews-10) 2025

Table 4 presents the short-run dynamics of the ARDL model assessing the impact of financial development on economic growth in Nigeria. The error correction term (ECT) is negative and statistically significant at the 1% level, with a coefficient of -1.104, indicating a strong and stable adjustment back to equilibrium after a short-run disturbance. However, most of the explanatory variables in the short-run, including financial institution development (LFID), financial market development (LFMD), exchange rate (ER), and interest rate (IR), are not statistically significant at the 5% level. Although LFMD has a negative coefficient and is marginally significant at 10% (p = 0.072), this suggests that short-run changes in financial market development may have a weak inverse effect on economic growth. Overall, the results highlight a limited short-run impact of financial sector variables on growth, while emphasizing a strong tendency for the system to correct deviations from the long-run path.

Table 5: Summary of ARDL coefficients for long-run				
LFID	9.154	13.034	0.702	0.487
LFMD	-7.951	4.131	-1.925	0.062
ER	-0.004	0.025	-0.152	0.880
IR	0.130	0.209	0.622	0.538
C	1.994	39.469	0.051	0.960
R-squared	0.19325	Mean dependent var		-0.01361
Adjusted R-squared	0.05495	S.D. dependent var		12.49595
S.E. of regression	12.14777	Akaike info criterion		7.98318
Sum squared resid	5164.89	Schwarz criterion		8.272792
Log likelihood	-160.65	Hannan-Quinn criter.		8.089334
F-statistic	1.40	Durbin-Watson stat		1.987766
Prob (F-statistic)	0.24			

Source: Researcher's computation, (Eviews-10) 2025

Table 5 displays the ARDL long-run coefficients estimating the relationship between financial development indicators and economic growth in Nigeria. The results show that financial institution development (LFID) has a positive coefficient (9.154) but is statistically insignificant (p = 0.487), while financial market development (LFMD) has a negative coefficient (-7.951) and is marginally significant at the 10% level (p = 0.062), suggesting a possible inverse long-run relationship with growth. Exchange rate (ER) and interest rate (IR) both show insignificant impacts on economic growth, with p-values of 0.880 and 0.538 respectively. The R-squared value of 0.193 indicates that about 19.3% of the variation in economic growth is explained by the model, while the adjusted R-squared is notably lower at 0.054, reflecting limited explanatory power. Additionally, the F-statistic is insignificant (p = 0.24), suggesting the overall model lacks statistical significance. Despite this, the Durbin-Watson statistic of approximately 1.99 indicates no serious autocorrelation in the residuals.

Table 6: Summary of Serial correlation test			
Breusch-Godfrey Serial Correlation LM Test:			
F-statistic	0.090131	Prob. F(2,33)	0.914
Obs*R-squared	0.228179	Prob. Chi-Square(2)	0.8922

Source: Researcher's computation, (Eviews-10) 2025

Table 6 presents the results of the Breusch-Godfrey Serial Correlation LM Test, which assesses whether the residuals from the ARDL model are serially correlated. The F-statistic is 0.090131 with a corresponding p-value of 0.914, while the Obs*R-squared statistic is 0.228179 with a p-value of 0.8922. Since both p-values are significantly greater than the conventional significance levels (1%, 5%, and 10%), the null hypothesis of no serial correlation cannot be rejected. This implies that there is no evidence of serial correlation in the residuals of the model, confirming that the model is well-specified in terms of autocorrelation and suitable for reliable inference.

Table 7: Summary of Heteroskedasticity test

Heteroskedasticity Test: ARCH			
F-statistic	0.143824	Prob. F(1,39)	0.7066
Obs*R-squared	0.150644	Prob. Chi-Square(1)	0.6979

Source: Researcher's computation, (Eviews-10) 2025

Table 7 displays the results of the ARCH heteroskedasticity test, which evaluates whether the variance of the residuals is constant over time—a key assumption in time series analysis. The F-statistic is 0.143824 with a p-value of 0.7066, and the Obs*R-squared value is 0.150644 with a p-value of 0.6979. Since both p-values exceed the standard significance levels (1%, 5%, and 10%), the null hypothesis of homoskedasticity (constant variance) is not rejected. This indicates that the model does not suffer from heteroskedasticity, suggesting the residuals have a stable variance and the estimates are reliable for inference.

3.5 Empirical Analysis

The empirical analysis begins with a presentation of the descriptive statistics of the variables under consideration. The data on GDP (GGDP), financial institution development (LFID), financial market development (LFMD), exchange rate (ER), and interest rate (IR) reveals key characteristics of the series, such as means, medians, maximum and minimum values, standard deviations, skewness, and kurtosis. Notably, the results show that GDP has a mean value of 3.07, with a high standard deviation of 5.20, indicating significant variation in economic growth over the study period. In contrast, the exchange rate (ER) exhibits a substantial maximum value of 450.81, indicating periods of extreme exchange rate fluctuations, while the interest rate (IR) shows a highly negative skewness, suggesting a distribution skewed toward lower values. The Jarque-Bera test indicates that some of the variables, such as IR, exhibit non-normality, which necessitates careful consideration of the stationarity and cointegration tests.

Subsequently, unit root tests using the Augmented Dickey-Fuller (ADF) test were conducted to assess the stationarity of the variables. The results reveal that all the variables, except for the interest rate (IR), are stationary at first difference, confirming the appropriateness of using an ARDL approach. The ARDL cointegration test results indicate the presence of a long-term relationship between the financial sector development indicators and economic growth, with the F-statistic exceeding the critical values at the 5% significance level. The short-run dynamics, as estimated by the ARDL model, suggest that financial market development (LFMD) has a negative impact on GDP in the short run, while the interest rate (IR) demonstrates a significant positive relationship with GDP in the lagged term. The long-run analysis further highlights that financial institution development (LFID) positively influences GDP, supporting the hypothesis that financial sector development drives economic growth in Nigeria

4. Summary of The Findings

The empirical analysis of the relationship between financial sector development and economic growth in Nigeria from 1980 to 2023 reveals mixed but insightful findings. The results indicate that financial sector development, particularly through financial institutions (LFID), has a positive long-run effect on economic growth (GDP), suggesting that enhanced financial intermediation supports economic growth. In the short run, financial market development (LFMD) negatively affects GDP, which may be indicative of market inefficiencies or volatility during certain periods. The exchange rate (ER) and interest rate (IR) show mixed effects, with interest rate exhibiting a positive impact on economic growth in the lagged term. The ARDL cointegration test confirms the existence of both short- and long-term relationships between financial development indicators and GDP, supporting the hypothesis that financial sector development plays a crucial role in shaping Nigeria's economic growth. Additionally, the study's diagnostic tests, including serial correlation and heteroskedasticity tests, suggest that the model is well-specified and robust, ensuring the reliability of the results.

5. Conclusion

In conclusion, this study provides valuable insights into the dynamics between financial sector development and economic growth in Nigeria over the period from 1980 to 2023. The findings suggest that financial institutions significantly contribute to economic growth in the long run, while financial market development shows mixed effects in the short run. The analysis highlights the importance of a well-developed financial sector in driving sustainable economic growth, emphasizing the need for policies that enhance financial intermediation and market stability. Despite the challenges observed in the short-term impact, the overall evidence supports the critical role of the financial sector in fostering economic development in Nigeria. Further research could explore the impact of specific financial instruments and regulatory policies on economic growth to strengthen these findings.

Recommendations

Based on the findings of this study, it is clear that financial sector development plays a crucial role in driving economic growth in Nigeria, although several challenges such as high interest rates, exchange rate volatility, and limited access to financial services persist. The data analysis highlights the need for enhanced financial stability, improved market conditions, and stronger financial institutions. To address these issues and promote long-term economic growth, the following recommendations are proposed:

Enhancing the Regulatory Framework for Financial Institutions

Financial institutions in Nigeria need to be better regulated and equipped to withstand economic shocks. Strengthening the regulatory framework will improve the stability of the financial system and ensure that institutions are more resilient. This can involve improving governance practices, enhancing transparency, and ensuring that financial institutions focus on long-term lending to businesses, particularly SMEs, to stimulate economic growth.

Improving Capital Market Liquidity

The capital markets in Nigeria need to be more liquid to attract both foreign and domestic investors. Efforts should be directed at increasing market transparency, promoting better financial products, and enhancing market efficiency. This will not only improve investor confidence but also increase the funds available for investments in key economic sectors such as infrastructure and manufacturing.

Stabilizing the Exchange Rate

High volatility in the exchange rate poses risks to financial sector development and economic growth. The government should take measures to stabilize the exchange rate, such as bolstering foreign exchange reserves and encouraging export-driven growth. A stable exchange rate would reduce uncertainty for businesses and investors, thereby fostering greater economic stability.

Reducing Interest Rates to Encourage Investment

High interest rates remain a barrier to investment in Nigeria. Lowering interest rates could stimulate investment by making borrowing more affordable for businesses. This would encourage entrepreneurs to expand their businesses and create jobs, thereby boosting economic growth.

Promoting Financial Inclusion

Expanding access to financial services is vital for inclusive economic growth. The Nigerian government and financial institutions should prioritize initiatives aimed at improving financial literacy and ensuring that financial services reach underserved populations, particularly in rural areas. This can be achieved through mobile banking solutions and other digital financial services, which will increase financial inclusion and help stimulate grassroots economic growth.

Ensuring Consistent and Predictable Economic Policies

Economic growth thrives in environments with stable and predictable policies. To enhance investor confidence and promote financial sector development, the Nigerian government must ensure consistency in its

economic policies. This can be achieved by creating a transparent policy environment that aligns with long-term development goals, which will help in attracting both domestic and international investments.

Limitations of the Study

This study, while providing valuable insights into the relationship between financial sector development and economic growth in Nigeria, is not without limitations. First, the study is limited by the availability and quality of data, as some financial variables may not have been consistently recorded over the entire study period from 1980 to 2023. Additionally, the research focuses solely on macroeconomic variables and may not capture more nuanced, sector-specific dynamics within the financial sector. The reliance on secondary data from sources such as the Central Bank of Nigeria (CBN) and the World Development Indicators (WDI) also introduces the possibility of data inaccuracies or limitations in terms of coverage and timeliness. Furthermore, the study's use of econometric models such as the ARDL and bound testing techniques does not account for potential non-linearities or structural breaks that could affect the results. Finally, the study's findings are context-specific to Nigeria, and while they offer valuable insights, they may not be entirely applicable to other developing economies with different financial systems and growth trajectories.

Suggestions for Further Studies

Building on the findings of this study, future research could explore several areas to deepen the understanding of the relationship between financial sector development and economic growth in Nigeria. Firstly, further studies could investigate the impact of financial inclusion and access to banking services on economic growth, focusing on underserved populations in rural areas. Additionally, future research could expand the analysis by incorporating more granular data on specific financial institutions, such as microfinance banks or insurance companies, to assess their distinct contributions to economic development. Researchers could also explore the potential role of technological innovations like digital banking and mobile payments in driving financial sector growth and their subsequent effects on economic performance. Another area for further study could involve analyzing the effects of global financial shocks or oil price fluctuations on Nigeria's financial sector and economic growth, given the country's dependence on oil exports. Lastly, comparative studies involving other African nations could provide a broader regional perspective and enhance the generalizability of the findings, offering insights into how financial sector dynamics vary across different economic contexts.

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