


# Deposit Money Bank Credit and the Nigerian Economic Growth: An Empirical Analysis

Emmanuel Ifeanyi Ajudua

Department of Economics, Faculty of Social Sciences, National Open University of Nigeria, University Village, Nnamdi Azikiwe Express Way, Plot 91 Cadastral Zone Jabi, Abuja, Nigeria

 <https://orcid.org/0000-0003-3519-8670>

e-mail: [eajudua@noun.edu.ng](mailto:eajudua@noun.edu.ng)

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**Abstract:** *This paper set out to empirically evaluate the impact of deposit money banks' credit on the performance of Nigerian economic growth. Data covering 1986 to 2020 were collected from secondary sources and unit root test, cointegration test and the ECM method used in analyzing the data. Findings from the study revealed that total bank credit and money supply both had a positive significant relationship with economic growth. Private sector credit had a positive but not significant relationship with economic growth while lending rate had a negative and significant relationship with economic growth. The study thus recommends that the monetary authorities should implement policies favourable to deposit money banks' credit creation and intensify efforts to attract credit to the private sector in order to stimulate economic growth while policies to support the growth of the financial market and banking industry should be enacted and implemented.*



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*E51; E52; G21*

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## Introduction

In Nigeria, rapid and sustained growth and output have been of great importance and the major focal point of the government over the years. Consequently, plans geared towards improved economic productivity, economic diversification, increased output, and economic stability has been major objectives targeted by successive government. In pursuance of these objectives, the availability and provision of huge capital outlay necessary for large scale production become essential. The deposit money bank credit has been a source of capital and has acted as a necessary intervention towards the provision of credit in the economy required by industries for production.

The importance of deposit money bank credit in generating economic growth has been widely recognized. According to Schumpeter, the banking industry fosters technical innovation in their intermediation role by efficiently allocating savings through the selection and support of businesses with the greatest potential of successfully producing ingenuity (Ulgen, 2014). Nwanyanwu (2010) posited that the banking sector in Nigeria facilitates the availability of

credit to economic agents so as to meet operating expenses. Business firms obtain such credits to purchase raw materials, machinery equipment etc.; farmers can purchase farm inputs like seeds and fertilizer with credit.; government obtain credit to meet her capital and recurrent expenditure all aimed at increasing and improving total economic output.

The monetary authority in recognition of the importance of deposit money bank credit to the Nigerian economy has implemented several banking reforms. The Nigerian banking system was reformed in 2001 with the implementation of the Universal Banking System such that the previously existing divisions between commercial and merchant banks were eliminated. This made it possible for banks to take on the function of intermediation and assume the responsibility of increasing credit availability and accessibility while also enhancing their ability to play a crucial role in financial intermediation in the provision and accessibility of credit in the Nigerian economy. This has led to improved banking services over the years. According to statistics, Nigerian Deposit Money Banks' gross loans and advances climbed from N17.06 trillion in December 2020 to N17.75 trillion by the conclusion of 2021 first quarter (CBN,2021). The increase in loans from Nigerian banks coincides with the expansionary policies of the Central Bank of Nigeria (CBN) and its growth plan intended to revive the economy, particularly in the wake of the COVID-19 outbreak and its effects on Nigeria's economy. While the major objective of these reforms centred on credit availability, it also targets financial stability and additionally guarantees that the financial sector contributes to the growth of the real sector of the economy (Ojong, Ekpuk, Ogar & Emori, 2014). The CBN as the monetary authority, therefore, plays the lead role through the use of monetary policy instruments to control the overall credit flow and expansion while also determining the proportion of loans and advances from banks allocated to sectors so as to stimulate productivity.

Deposit money bank credit (bank loans and advances) assists in bridging the financial gap between deficit and surplus units and is seen as a driving force behind economic growth. The perception of the theory of finance-led growth emphasizes how financial development contributes to domestic savings and investment through its mobilization role by means of a more liberalized and open financial system, and in fostering productivity by establishing a successful financial market.

Despite findings positing a link between financial development and economic growth, there is a lingering argument on the channel and direction of causality and as such remained unresolved in both theory and empirical research (Fitzgerald, 2006). In the case of Nigeria, in spite of numerous bank reforms targeted at improving the bank's capacity for providing effective service geared toward raising funds for the real sector ultimately leading to a vibrant economy, there are still problems. There is a glaring case of inadequate funding to the sector, a fall in domestic credit allocated to the private sector by the banking sector, a high concentration of loans to few sectors etc. the shortcomings of institutional credits in Nigeria have been attributed to ineffective supervision, inadequate funds, political meddling, lengthy loan processes loan defaults etc.

The financial difficulties confronting the real sector performance demand the re-examination of the finance-growth link. This is so given that sector impact is important given that underperformance has implications for employment, inflation, income inequality and poverty which are vital for an evolving economy like Nigeria. It thus becomes pertinent to ask; what is the trend in deposit money bank credit to economic growth in Nigeria? Does bank credit significantly affect the growth of the Nigerian economy? How accessible is bank credit? Against this background, this study becomes necessary and has an objective of ascertaining the impact of deposit money banks on economic growth in Nigeria. Though deposit money banks' activities began before the country's political independence, the study is limited to the Structural Adjustment Programme (SAP) programme era (1986 - 2020), which focuses on a policy transition from direct control of the economy to an economy defined by market forces. Furthermore, the study will be guided by the following research hypothesis:

$H_0$ : There is no significant relationship between deposit money bank credit and economic growth in Nigeria.

## **Literature Review**

### **Theoretical Underpinning**

The theoretical underpinnings upon which this study is built, centre on financial intermediation theory. Goldsmith (1969) presented stylized evidence on financial structure and economic development. He discovered that as a nation's economy develops, its financial system expands more quickly than its national wealth. The primary factor that determines the relative size of a country's financial system is the functional separation of saving and investing among different economic units. In essence, the rationale for this viewpoint is that economic growth is promoted through the effective allocation of capital within an economy (Levine, 1997). Financial intermediation has an impact on economic growth through the rate of saving, the percentage of savings channelled to investment and the social marginal productivity of investment (national product's net investment contribution in addition to the private investor's return). According to Goldsmith (1969), the positive relationship between financial development and the level of real per capita GNP is due to the favourable impact that financial development has in promoting more effective use of the capital stock and as a result, he believes that financial markets are crucial to economic growth. Consequently, he explained that the volume and calibre of services offered by financial institutions account for the variations in economic growth between nations.

The Wicksell theory is hinged on the comparison between the marginal product of capital and the cost of borrowing money. Developed by Knut Wicksell, the theory posited that entrepreneurs would take out loans to buy capital goods at the money rate if the interest rate on borrowing money was lower than the natural rate of return on capital leading to a rise in demand and in turn prices. In the Wicksellian view, an artificial boost of the money supply through the banking system would unevenly impact pricing dynamics, even more so in the capital goods industries which will shift real wealth unevenly and could even cause business cycles.

### **Empirical Review**

Aliakhue and Chukwudi (2020) investigated the influence of Deposit Money banks on the Nigerian economy from 2009 -2018. Employing the Ordinary Least Square (OLS) technique to ascertain the relationship between gross domestic product and the explanatory variables, their findings revealed that the Deposit Money Bank's credit has a significant influence on Nigeria's economy within the period under study.

Shittu (2012) employed the unit root test, co-integration test, and error correction model to analyze the effects of financial intermediation on economic growth in Nigeria between 1970 and 2010. The study discovered that a key factor in influencing economic growth in Nigeria is financial intermediation, particularly deposit mobilization.

Olokoyo, Taiwo and Akinjare (2016) utilized ANOVA, one sample test, and simple percentage to examine how deposit money bank activity affected Nigerian economic development. Their findings demonstrated that the activities of deposit money banks have a considerable impact on Nigeria's economic development.

Using a two-stage least squares method and covering the period 1970 to 2008, Akpansung and Babalola (2012) investigated the relationship between banking sector credit and economic growth in Nigeria. Their findings showed that while lending rates hindered economic growth, private sector credit had a positive impact.

Ojeaga, Odejimi, Okhiku, and Ojeaga (2013) investigate the effect of bank lending on growth in Nigeria using sample of data from 1989 to 2012 while employing the quantile regression estimation method. Their finding revealed that commercial bank lending had a negative effect on growth during the period under study.

Using unit root, cointegration, and error correction models, a study by Samson and Abass (2013) examined how deposit money banks contributed to economic growth in Nigeria from 1974 to 2010, and found a long-term link between GDP and the independent variables which included.

Using secondary data for the period 1992 – 2012 and employing OLS, Yakubu and Affoi (2014) analyze the impact of commercial banks' credit on economic growth in Nigeria. Employing commercial bank credit to the private sector of the economy as the independent variable and GDP as the dependent variable, the study revealed that commercial bank credit significantly influences Nigeria's economic growth.

Imoughele and Ismaila (2013) employing the OLS technique investigated the impact of deposit money bank credit accessibility and sectoral output performance in Nigeria covering the period 1986 – 2010. The study discovered a long-term relationship exists between commercial bank credit and sectoral output performance

In their study, Fink, Haiss, and Mantler (2005) found a substantial correlation between financial intermediation and economic growth in eleven developing countries between 1990 and 2001. The study discovered that in these developing countries, the productive sector acted as a growth stimulant. The study also noted that improvement of the financial sector will only have a short-term impact on growth in the economy instead of a long run growth.

The literature on the causal relationship between deposit money banks and economic growth has remained inconclusive and still contested in the Nigerian context. This has not been helped by the volatility of oil price (as a monocultural economy), economic policies such as the liberalization policy, the global economic crisis and most recently, spillovers from the COVID-19 outbreak. Such gaps in the research on the finance-growth nexus are attempted to be filled in this paper.

## Data and Methodology

An experimental factorial design was used in the study as it increases the validity of the study by enabling the researcher to examine the effects of two or more independent variables on the dependent variable at the same time. Using time series data for the period 1986 -2020 sourced from the Central Bank of Nigeria Statistical Bulletin, the Ordinary Least Square regression method was employed in the study to analyse if there exists any link between the dependent and independent variables in the study. Additionally, the Error Correction Mechanism (ECM), which specifies the length of adjustment while correcting for all short-run errors to improve the long-run relationship, was adopted. The mathematical functional relationship between the dependent and independent variables for the study is stated thus:

$$RGDP = f(TBC, MS, PSC, LR) \quad (1)$$

Econometrically, the function above becomes

$$RGDP = \alpha_0 + \alpha_1 TBC + \alpha_2 MS + \alpha_3 PSC + \alpha_4 LR + \mu_t \quad (2)$$

In order to overcome the issue of heteroskedasticity, it becomes necessary to transform the measurement scale of the variables, and as a result, the model is expressed in a logarithm form as:

$$RGDP = \alpha_0 + \alpha_1 \text{Log}TBC + \alpha_2 \text{Log}MS + \alpha_3 \text{Log}PSC + \alpha_4 LR + \mu_t \quad (3)$$

Where:

RGDP =	Real Gross Domestic Product;
TBC =	Total Bank Credit;
MS =	Money Supply;
PSC =	Private Sector Credit;
LR =	Lending Rate;
$\mu$ =	Error Term;
$\alpha_0$ =	Intercept;
$\alpha_1$ to $\alpha_4$ =	Parameters.

Given the assumed relation, based on apriori reasoning the expected signs for the parameter estimates are  $\alpha_1 > 0$ ,  $\alpha_2 > 0$ ,  $\alpha_3 > 0$  and  $\alpha_4 < 0$ .

There may be a case of spurious regression if the model specified is stationary. This calls for a diagnostic preliminary test so as ascertain the behaviour of the variables. To determine whether the variables being used are stationary, the Augmented Dickey Fuller unit root test will be used. Additionally, the Johansen Co-integration test will be run to determine whether the series is actually co-integrated.

## Result and Discussion

### Unit Root Test

Table 1 reports the results of the ADF stationarity tests at both the level and the first differencing for all the variables used in the study. None of the variables in the table exhibited stationary behaviour at level (I(0)). However, the results of the ADF Test Statistic for all variables in comparison to that of the 5% critical value show that all variables became stationary after the first differencing (I(1)). A co-integration test was also conducted in the study utilizing the Johansen co-integration method and the result is presented below.

**Table 1.** Summary of Augmented Dickey Fuller (ADF) Unit Root Test Results

Variables	LEVEL			FIRST DIFFERENCE		
	ADF Test Statistic	5% Critical Value	Status	ADF Test Statistic	5% Critical Value	Status
LogRGDP	-1.398	-3.553	I(0)	-5.181	-3.558	I(1)*
LogTBC	-0.763	-3.563	I(0)	-4.971	-3.574	I(1)*
LogMS	-1.834	-3.558	I(0)	-4.107	-3.558	I(1)*
LogPSC	-2.453	-3.553	I(0)	-4.858	-3.558	I(1)*
LR	-1.841	-3.553	I(0)	-5.190	-3.558	I(1)*

Source: Author's computation from Eviews 9.

### Cointegration Test

From Table 2, we reject the null hypothesis that there is no cointegration since at the 5% level of significance, and using the trace test, two cointegrating equations were found. This is so because their Trace Statistic value exceeded the 0.05 Critical Value. The existence of cointegration among variables is supported by findings from maximum eigenvalue. At a 5% level, the maximum eigenvalue revealed two cointegrating equations.

Having all variables reach stationarity at first difference (I(1)), then the need for the error correction mechanism (ECM) becomes necessary. Furthermore, there is an indication that the long run static OLS is realistic and reliable due to the fact that the short run dynamic model will eventually adjust to long run equilibrium after overcoming the short run drift. Below is the presentation of the long run estimation and the parsimonious ECM result.

**Table 2.** Johansen Cointegration Test

Lags interval (in first differences): 1 to 1

Unrestricted Cointegration Rank Test (Trace)

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None *	0.806514	84.58495	69.81889	0.0018
At most 1 *	0.505195	47.86211	47.85613	0.0498
At most 2	0.344224	15.57343	29.79707	0.6771
At most 3	0.112857	3.888512	15.49471	0.9104
At most 4	0.005147	0.176825	3.841466	0.1961

Unrestricted Cointegration Rank Test (Maximum Eigenvalue)

Hypothesized No. of CE(s)	Eigenvalue	Max-Eigen Statistic	0.05 Critical Value	Prob.**
None *	0.811341	45.61124	33.87687	0.0016
At most 1 *	0.525412	28.31200	27.58434	0.2915
At most 2	0.341126	12.61760	21.13162	0.5107
At most 3	0.131046	3.750128	14.26460	0.7791
At most 4	0.006714	0.220125	3.841466	0.6565

Max-eigenvalue test indicates 2 cointegrating eqn(s) at the 0.05 level

Source: Author's computation from Eviews 9.

### Long Run Estimation

The long run estimation illustrating the linear relationship between the dependent variable and the independent variables is shown in Table 3. This finding is reliable since the variables used in the model exhibited a long-term relationship.

**Table 3.** The Ordinary Least Square Regression Result

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	11.52919	1.733249	6.651776	0.0000
LogTBC	0.186467	0.032186	5.793367	0.0000
LogMS	0.593644	0.081942	7.244701	0.0000
LogPSC	0.463075	0.338749	1.367015	0.1825
LR	-0.046545	0.016713	-2.784992	0.0095
R-squared	0.937707	Mean dependent var		13.11243
Adjusted R-squared	0.902809	S.D. dependent var		0.844148
S.E. of regression	0.225233	Akaike info criterion		-0.004633
Sum squared resid	1.420441	Schwarz criterion		0.222111
Log likelihood	5.076439	Hannan-Quinn criter.		0.071660
F-statistic	35.13731	Durbin-Watson stat		1.729305
Prob(F-statistic)	0.020331			

Method: Least Squares, Dependent Variable: LogRGDP, Sample: 1986 2020, Included observations: 35

Source: Author's computation from Eviews 9.

The OLS result in Table 3 displays a statistically significant positive constant, indicating that the model is sound and that the major variables having an impact on Nigeria's GDP were properly accounted for. The major independent variable total bank credit (LogTBC) showed the

anticipated sign and is significant. This connotes that in Nigeria, total bank credit has a strong impact on its GDP. The magnitude of the coefficient is 0.186467, indicating that a unit rise in total bank credit by one unit will lead to 0.186467 unit increase in GDP in Nigeria. Money supply also conforms to expectations, is rightly signed and is statistically significant. Based on its coefficient, it suggests that a unit increase in money supply will bring about 0.593644 unit rise in GDP.

Though rightly signed, Private sector credit (LogPSC) was not statistically significant. This suggests that encouraging increased private sector financing is essential as increasing credit will provide the necessary aid required for improvement thereby leading to increased production, employment and profits. Lending rate (LR) conforms to expectations as it is negatively signed and statistically significant. This means that one-unit increase in lending rate will lead to 0.046545 unit fall in GDP in Nigeria.

The R Squared ( $R^2$ ) which measures how well the model fits is 93%. The  $R^2$  is an indication of a strong relationship between economic growth (GDP) and the independent variables (Total Bank Credit, Money Supply, Private Sector Credit and Lending Rate). It implies that 93% of the variation in economic growth is explained by the independent variables and 7% is not captured by the independent variables in the model. Also, the model's fitness with regard to additional missing variables is gauged by the adjusted R-square, 0.902809, and means that the exogenous variables would still be able to explain 90% variations in economic growth. The model's overall fitness, as determined by the F-statistics and its probability value demonstrates the robustness and statistical significance of the entire model at the 5% level of significance given that the probability value (0.020331) is less than 0.05. This indicates that the study's model is dependable at a 95% level of confidence such that conclusions drawn about the model are valid and supported.

### Short-run Dynamic Error Correction Model

The short-run dynamics results from Table 4 demonstrate that total bank credit (TBC), when one lag is included, has a positive and statistically significant impact on economic growth in Nigeria in the short run. Money supply in the same vein, when one lag is included shows a positive and significant effect on economic growth in the short run. The same goes for private sector credit (PSC) when one lag is included. A positive and significant relationship was seen. Lastly lending rate (LR) when one lag is included exhibited a negative and significant impact on economic growth. The coefficient of determination ( $R^2 = 0.730221$ ) and its adjusted- $R^2$  (adjusted- $R^2 = 0.695474$ ) show the existence of goodness of fit while the F-test was significant at 5% level as there was a goodness of fit. This indicates that all the variables were jointly significant.

**Table 4.** Short-run Dynamic ECM

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	6.319048	1336469.	0.472817	0.6404
D(LGDP(-1))	0.317156	3.280510	3.130640	0.0489
D(LOGTBC(-1))	0.006218	3.091266	3.068134	0.0492
D(LOGMS(-1))	0.029139	2.048958	-3.211637	0.0370
D(LOGPSC(-1))	0.022011	3.335900	3.165527	0.0483
D(LR(-1))	-0.064824	4.094908	1.845881	0.1242
ECM(-1)	-0.281109	2.999817	-3.986106	0.0310

Table 4 (cont.)

R-squared	0.730221	Mean dependent var	63211.62
Adjusted R-squared	0.695474	S.D. dependent var	6244895.
S.E. of regression	6.101254	Akaike info criterion	34.27653
Sum squared resid	9.323114	Schwarz criterion	34.59716
Log likelihood	-5.414244	Hannan-Quinn criter.	34.38281
F-statistic	6.246140	Durbin-Watson stat	1.943108
Prob(F-statistic)	0.037141		

Method: Least Squares, Dependent Variable: LogRGDP, Sample (adjusted): 1988 2020, Included observations: 35

Source: Author's computation from Eviews 9.

The error correction coefficient in Table 4 is estimated as  $-0.281109$  with a probability value less than 0.05 (0.0310). This conforms to the decision rule which posits that the ECM must be negative and statistically significant.  $-0.281109$  is the speed of adjustment from the short-run equilibrium to the long-run equilibrium and suggests that any disequilibrium in the short-run will converge to long-run equilibrium at the speed of 28%. For the sake of policy analysis, there is a need to ascertain if the model is stable. This calls for the employment of diagnostic post estimation. To evaluate the stability of the model, the Ramsey Linearity test, the Breusch-Pagan-Godfrey serial correlation LM test and the Breusch-Pagan-Godfrey heteroskedasticity test were employed.

The result of the Ramsey Reset Test in Table 5 above was employed to ascertain if the dependent and independent variables in the model were linear. The model is linear and properly defined will result in the null hypothesis being rejected. However, the outcome suggests that the null hypothesis is accepted since the likelihood ratio, t-statistics, and F-statistics are not statistically significant at 5 percent level of significance.

Table 5. Ramsey Linearity Test

	Value	df	Probability
t-statistic	0.924537	29	0.3628
F-statistic	0.854769	(1, 29)	0.3628
Likelihood ratio	1.016707	1	0.3133

Equation: UNTITLED

Specification: LOGRGDP C LOGTBC LOGMS LOGPSC LR

Omitted Variables: Squares of fitted values

Source: Author's computation from Eviews 9.

The result in Table 6 shows the Breusch-Godfrey Serial Correlation LM Test which evaluates the possibility of autocorrelation. Since the F-statistics is not significant at 5% level of significance, we conclude that there exists the absence of autocorrelation. As a result, we accept the null hypothesis that there is no serial correlation in the model.

Table 6. Breusch-Godfrey Serial Correlation LM Test

Breusch-Godfrey Serial Correlation LM Test:

F-statistic	3.129314	Prob. F(2,29)	0.0637
Obs*R-squared	6.865779	Prob. Chi-Square(2)	0.0723

Source: Author's computation from Eviews 9.

The heteroscedasticity test was adopted to check for the existence of interdependence of error terms across time in the model. The result in Table 7 above shows that the F-statistics is not significant at 5% level of significance and as such, there exists the absence of



heteroskedasticity. This thus implies that we accept the null hypothesis and come to the conclusion that the model does not exhibit heteroskedasticity.

**Table 7.** Heteroskedasticity Test

Heteroskedasticity Test: Breusch-Pagan-Godfrey

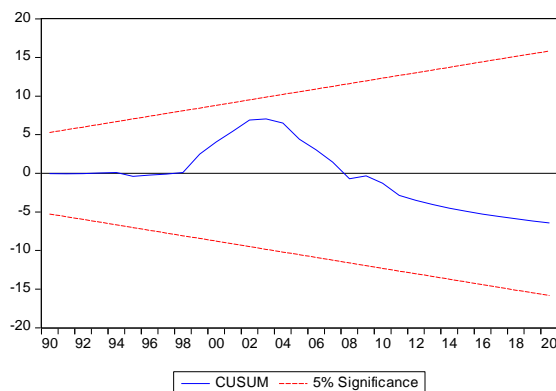
F-statistic	0.600822	Prob. F(4,30)	0.6649
Obs*R-squared	2.595881	Prob. Chi-Square(4)	0.6276
Scaled explained SS	2.953158	Prob. Chi-Square(4)	0.5657

Source: Author’s computation from Eviews 9.

**Stability Test**

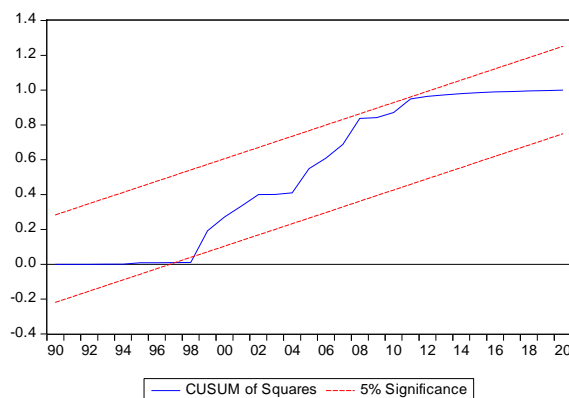
The study determined the model's stability using the cumulative sum (CUSUM) and cumulative sum squares (CUSUMSQ) tests. This is crucial because, given the independent variables employed in the study, the stability test enables us to predict the dependent variable in a regression with a decent degree of precision.

The CUSUM and CUSUMSQ are depicted in Figures 1 and 2. The plots from the data fell inside the 5 percent critical lines, indicating that the model is stable. This suggest that throughout the period of study, the variables employed did not display structural instability. As a result, estimated parameters are reliable and will be helpful for policy decisions.



**Fig. 1.** CUSUM Test

Source: Author’s computation from Eviews 9.



**Fig. 2.** CUSUM of Squares Test

Source: Author’s computation from Eviews 9.

## Conclusion and Recommendation

The relationship between deposit money bank credit flow and economic growth in Nigeria between 1986 to 2020 was examined with the framework of ECM model. From the findings, it was established that total bank credit and money supply had a significant relationship with economic growth and conform to expectations. Also, private sector credit had a positive relationship with economic growth but was not significant while lending rate had a negative and statistically significant relationship with economic growth. Stemming from the key findings that this work revealed, the following recommendations are reached. Credit is highly essential for improved productivity, consumption and investment in Nigeria and as such, the monetary authorities should implement policies favourable to deposit money banks in credit creation. Since the findings revealed a positive but insignificant relationship between private sector credit and economic growth, efforts should be intensified to attract credit to the private sector in order to stimulate economic growth. The financial market and banking industry are crucial to the production of credit in the Nigerian economy, hence policies to support their growth are also required.

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