# IMPACT OF QUANTITATIVE TOOLS OF MONETARY POLICY ON THE PERFORMANCE OF DEPOSIT OF COMMERCIAL BANKS IN NIGERIA

# ABSTRACT

This study focused on examining the effects of quantitative policy instruments on the deposit performance of commercial banks in Nigeria, namely First Bank of Nigeria Plc and First Inland Bank Plc. In order to guide the trajectory of the economy, government authorities utilise several economic policies, including monetary policy. Banks serve as the intermediary institutions through which the government executes monetary policy, and in the course of this execution, banks are subject to various influences. This study aims to investigate the impact of monetary policy on the performance of commercial banks within a specific time frame. It seeks to determine the extent to which monetary policy influenced the performance of these banks, if indeed it did. Therefore, the research will also aim to investigate if monetary policy has had an impact on the loans and advances, as well as the profitability, of First Bank of Nigeria Plc and First Inland Bank Plc. The utilisation of basic percentages for data analysis and the application of the chi-square test for hypothesis testing will be employed. The preferred monetary policy instruments that I would like to utilise include interest rates, cash reserve ratios, minimum rediscount rates, liquidity ratios, and foreign exchange rates. In summary, the implementation of monetary policy has had a beneficial impact on the deposit performance of commercial banks, contributing to the stabilisation of the economy.

# CHAPTER ONE

# INTRODUCTION

# Background of the Study

Government polices are used to pursue development objectives of government that bothers on meeting the welfare of the citizens, they could be socially, politically, economically, religious wise, environmentally population and so on. These policies are used to pursue these goals through the use of economic policy. They are open market operation (OMO), moral suasion, special deposit, credit control and discount rate. The banks are one of the financial institutions that formulate the policy objectives and achievement of these goals.

This research involves the case study, first bank of Nigerian plc and first inland bank plc.

First bank of Nigerian plc was incorporated as a limited liability company on March 31, 1894 with head office in Liverpool by Sir Alfred Jones, a shipping magnate. It started business in the office of elder Dempster and company in Lagos under the corporate name of the bank of British West African (BBWA) with a paid up capital of 12000 pounds sterling, after absorbing it predecessor, the African banking corporation, which was established earlier in 1892. In the early years of operation the bank has an impressive growth. The changing of the bank name occurs in 1979 and 1991 to first bank of Nigeria plc.

First inland bank was incorporated as inland bank (Nigeria) plc on 20th April 1988 as a private limited liability company. It commenced business operation on October 1988 and was converted to a public limited liability company in June 1992.

2005 the bank went into a merger arrangement with former fist Atlantic bank plc. IMB international bank plc and NUB international bank limited to form first inland bank plc. The shares of the new bank, first inland bank plc are quoted on Nigeria stock exchange. The consolidated bank, first inland bank plc..

# Statement of the Problem

1. The under-developed nature of the Nigeria financial market.

2. There is very much presented in Nigeria whereby expected revenue fall below expenditure. This occurrence leads to direct injection to aggregate demand and increase pressure on general price level.

3. The issue of non bank financial institution (NBFI), which are graving in numbers and operations. They adopt deposit but up till now, they are not under the central bank of Nigeria CBN.

4. The delay in the conduct of monetary policy in Nigeria.

5. The delay in releasing the federal government annual budget, which cause economic units to suspend their activities.

# Objectives of the study

1. The primary objective of this research is to meet higher national diploma in banking and finance in federal polytechnic nekede Owerri.

2. To determine if monetary policy has had any influence on the profit of the first bank of Nigeria plc and also on its loan deposit and advances, over the study period.

3. Finally to make necessary recommendations that would improve monetary policy in Nigeria.

# Statement of Hypothesis

This section would outline some hypotheses of this research project.

Hi: monetary policy tools have an influence on the profit of commercial banks in Nigeria.

Ho: there is significant relationship between monetary policy tools and profit deposit and loans of commercial banks in Nigeria.

# Significance of the Study

1. Student would use it for reference purpose when conducting their researche.

2. Practicing bankers would find relevance in this study, this is because, it will help to find out which monetary policy instruments influence bank performance of the most and to them in important matters of decision.

3. It is also vital to central bank and other monetary authorities. Monetary authorities have this work of keeping economic indicators within reasonable limits; this research would definitely be of assistance to the monetary authorities in achieving this aim because it will provide an insight as to which tool would be most appropriate for influencing the economy.

4. An ultimate aim of this study is to bring about stability in the banking system and hence the economy as a whole and this would be of significance to the citizens of the economy.

# Scope of the Study

As Anyanwu (2000), specified out “A research is not expected to cover a discipline in the cause of this study. In line with this statement this project work would not cover every thing on this study ,it will significantly determine the reliability of its findings. Hence, only two performance indicator would be analysed.

Despite the fact that there are others like “Net income before taxes total assets deposit and income”

The monetary policy tools that would be involved in this study are open market operation (OMO), required reserve ratio (RRR) the cash reserve ratio ( CRR) interest rate policy (IRP), and exchange rate policy (ERP).

The following monetary policy instrument will be excluded such as discount rate policy (DRP) and moral suasion.

It is an experimental study, it is not a full experiment since I would not require a pre-test and post-test analysis neither will it require an experiment and control group analysis.

It is a case study research and will therefore be particular about banks.

First bank of Nigeria plc and first inland bank plc with there size and spread of operations is a representative case study. It has two branches in Owerri, that is first bank and first inland bank plc has two branches in Owerri, and has other branches in the nation.

 **LIMITATION OF THE STUDY**

In conducting a research work of this nature, certain restrictions are bound to affect the study. These include the following: money, time and effort.

Money being a scarce commodity, a student will not have enough money to meet up all there financial obligations by travelling to many organization which is a pre-requisite for a research project. As a result of this defect, this study will centre on the impact of quantitative tools on the performance of deposit of commercial banks in Nigeria with reference to first bank of Nigeria plc and first inland bank plc.

A research work of this nature can not be accomplished within a short period of time. It requires time if one actually wants to write exhaustively on the topic.

Also some employees of the bank and to who questions were asked declined interest should every attempt to persuade due to their own time schedule being a limitation to a project.

# Definition of Terms

* + 1. **Financial Performance**

LAG: This is the period between the conception of an idea and the time of implementation.

FINANCIAL SYSTEM: This is the conglomeration of market institutions, regulatory authorities, intermediates and the dealers in the economy.

INFLATION TREND: The upward or downward i.e. increase in the rate of inflation.

LENDING RATE: This is a rate at which banks make advance to their customers.

MONEY SUPPLY: This is summation or total amount or stock of many in circulation.

CONTROL: This is the process of insuring that firm activities confirm to as planed in ensuring that objectives are achieved.

OBJECTIVES: These are goals on enterprise seek to achieve by its existence and operation.

TOOLS: These are instrument used for a particular kind of work.

OPEN MARKET OPERATION: This is defined as the selling or buying of government securities in the financial markets by the central bank.

MONETARY POLICY: This can be defined as the major economic stabilization weapon which involves measure designed to regulate the volume, cost availability and direction of money and credit in the economy.

LIQUIDITY TRAPS: This is defined as a case where the interest rate falls so low that individuals and business wish to hold any new money created in the banking system as speculative balance.

HYPOTHESIS: This is an educated guess which the researcher made ahead of time which will be put to test for acceptances or rejection.

STABILIZATION SECURITY: These are securities specifically issued by the central bank at time it deems fit for the purpose of moping up excess liquidity in the banking system.

INTEREST RATE: This is a price of capital to the borrower and a return on capital to the saver or lender.

DISCOUNT RATE: This is also known as minimum rediscount rate or bank rate is a rate at which central bank offer financial assistance to financial institutions through loans or discounting bills.

DEPOSIT ACCOUNT: This is an account in which a person keeps a specific sum of money for an agreed period of time.

CASH BUDGET: This is a type of budget prepared by an organization based on the availability of cash.

BALANCE SHEET: This is a financial statement that shows the activities of an organization within a specified period.

QUASI MONEY: These are money that are not cash or paper-money but are also used for transaction purpose and also regarded as money.

# CHAPTER TWO LITERATURE REVIEW

# Introduction

This chapter reviews various theories that inform economic development and their macroeconomic effects, seeks to locate the place of our focus subject and its relevance to the finance discipline. A critical review of empirical studies is undertaken and an effort to evaluate contributions is made and pertinent knowledge gaps identified.

# Conceptual Framework

* + 1. **Concept of Monetary Policy**

Ezenduyi (2004) defines monetary policy as the policy which involve the adjustment of money stock (through different means) interest rate exchange rate as well as expectation to influence the level of economic activities and inflation in desired direction, targeting as the mapping up of excess liquidity armed at ensuring a non-inflationary macro-economic environment. Monetary policy can be defined as the instruments at the disposal of the monetary authorities to influence the availability and cost of credit/money with the ultimate objective of achieving price stability as demonstrated by Ibeabuchi, (2012). Onouorah, et al (2016) defined monetary policy as a rule and regulation imposed by the monetary authority into controlling the money supply inflation and achieves economic growth. Onyeiwu (2012) defines monetary policy as a technique of economic management to bring about sustainable economic growth and development has been the pursuit of nations and formal articulation of how money affects economic aggregate. Chigbu & Okonkwo (2014) held that monetary policy generally refers to the deliberate efforts of the government to use changes in money supply, cost of credit, size of credit and direction of credit

to influence the level of economic activities to achieve desired macroeconomic stability in an economy.

Richard (1999) stated that the instrument tools of monetary policy have been classified broadly in two categories traditional and non-traditional quantitative instrument. Monetary policies, as adopted in Nigeria, have four broad objectives.

1. **To maintain a high level of employment (full employment):** Full employment means employment of labour, plant and capital at a tolerable capacity to achieve the set goals of national economic policy aimed at combating recession and economic depression.
2. **To maintain stable price level:**Price level stability goal is related in an important sense to the control of inflation refers to a situation of sustained and rapid increase in the general level of prices, however, generated (Nnanna, 2006). According to Ibeabuchi (2012), inflation reduces real disposable income and consequently the purchasing power of money.
3. **To maintain the highest sustainable rate of economic growth:** This means both quantitative and qualitative increase in the total quantity of goods and services produced in the economy annually. Nnanna (2006) opined that economic growth is said to be achieved in a country in a situation where there is an increase in the income position of the citizens of the country and also a corresponding increase in the amount of goods and services which a given quantity of money can buy.
4. **To maintain the highest equilibrium in the balance of payments:** A country’s balance of payment may be in total equilibrium of there exists between total payments and total receipts, that is, the avoidance of larger or chronic deficit or surplus in the balance of payments

# Concept of Bank Profitability and Financial Performance

The profitability of a bank is determined by interior and exterior determinants (Sattar, 2014) which agrees with (Ongore, 2013; Al-Tamini et al., 2015). The interior determinants are called micro or bank specific determinants of profitability because they are initiated from bank accounts like balance sheet or profit and loss account. While on the other hand, the exterior determinants are the variables which are not in the control of banks’ management such as monetary policy interest rates. Chen et al. (1996) explained that these macroeconomic factors are significant in explaining firm performance (profitability) and subsequent returns to investment. Gilchris, (2013) agrees that the financial performance is commonly measured by ratios such as Return on Equity, Return on Assets. There are many different mathematical measures to evaluate how well a company is using its resources to make profit (Irungu, 2013). Financial performance can be measured using the following techniques; operating income, earnings before interest and taxes, net asset value (Gilchris, 2013). Irungu (2013) described financial performance analysis as the process of identifying the financial strengths and weakness of the firm by properly establishing the relationship between the items of the balance sheet and profit and loss account. It’s the process of identifying the relationship between the component parts of financial statements to ascertain an organization position, performance and prospects. Financial performance analysis can be undertaken by management, owners, creditors, investors (Chenn, 2011. Quarden (2009) argued that financial performance analysis helps in short term and long term forecasting and growth and can be identified with the help of financial ratios such as asset Utilization/efficiency ratios, deposit mobilization, loan performance, liquidity ratio, leverage/financial efficiency ratios, profitability ratios, solvency ratios and coverage ratios can be used to evaluate bank performance (Bekant, 2016). The performance of banks gives direction

to shareholders in their decision making (Panayiotis et al., 2011). Wainaina, (2013) says the effect of macroeconomic factors in other sectors of the economy will always affect the banking sector and what goes on in the banking sector will affect the other sectors of the economy. Chen et al., (1996) maintains that these macro-economic factors are significant in explaining firm performance (profitability) and subsequent returns to investors. Gilchris (2013) agrees that financial performance is commonly measured by ratios such as return on equity, return on assets, return on capital, return on sales and operating margin. A firm has several objectives but profit maximization is said to be paramount among these (Damilola, 2012; KPMG, 2010; Raheman and Nasr, 2012). Profit is a tool for efficient resources allocation because it is the most appropriate measure of corporate performance under competitive market conditions (Pandey, 2010). Conceptually profit connotes the excess of revenue generated by a firm over its associated costs for an accounting period. Operationally the term profit is imprecise, as many variants exist. The term profit could refer to profit before tax, profit after tax, gross profit, net profit, profit per share, return on assets, among other variants (Damilola, 2012; Pandey, 2010). This imprecision has often posed decisional challenges to researchers who must select an appropriate variant to proxy profitability. However, the most commonly used variants as appropriate measure of profitability include Gross operating profit, Net operating profit, Return on Assets (Deloof, 2008; Teruel and Solano, 2011; Lazaridis and Tryfonidis, 2010; Raheman and Nasr, 2012). According to Okafor (2016) the profitability performance also can be accessed from both book value and market value perspectives.

# Concept of Interest Rates

According to Keynes, interest rate is the reward for not hoarding but for parting with liquidity for

a specific period of time. Keynes’ definition of interest rate focuses more on the lending rate.

Adebiyi (2009) defines interest rate as the return or yield on equity or opportunity cost of deferring current consumption into the future. Some examples of interest rate include the saving rate, lending rate, and the discount rate. Professor Lerner, in Jhingan (2008), defines interest as the price which equates the supply of ‘Credit’ or savings plus the net increase in the amount of money in the period, to the demand for credit or investment plus net ‘hoarding’ in the period. This definition implies that an interest rate is the price of credit which like other price is determined by the forces of demand and supply; in this case, the demand and supply of loanable funds.

Ibimodo (2010) defined interest rates, as the rental payment for the use of credit by borrowers and return for parting with liquidity by lenders. Like other prices interest rates perform a rationing function by allocating limited supply of credit among the many competing demands. Bernhardsen (2013) defined the interest rate as the real interest rate, at which inflation is stable and the production gap equals zero. That interest rate very often appears in monetary policy deliberations. However, Irving Fisher (1956) states that interest rates are charged for a number of reasons, but one is to ensure that the creditor lowers his or her exposure to inflation. Inflation causes a nominal amount of money in the present to have less purchasing power in the future. Expected inflation rates are an integral part of determining whether or not an interest rate is high enough for the creditor.

The real interest rate represents a fundamental valuation of temporary provision of capital (money) corresponding to a price level constant in time. It is also obvious from the above relation that if inflationary expectations change, nominal interest rates have to change aliquot at a constant real interest rate (Cottrell; 2010). The real interest rate concept is irreplaceable in the research into the mutual relations of inflation, because assuming that the creditors are rational,

inflation and nominal interest rates influence each other. For similar reasons, the real interest rate is used in broader economic analyses. Expected inflation is an unobservable quantity. In an expose analysis, it can be replaced by the actual rate of inflation in the following period, which is equivalent to assuming rational expectations (Bencik; 2014).

Theoretically less satisfactory, but easier to apply, is the assumption of adaptive expectations; this replaces expected inflation in the future by actual inflation in the present. Inflation is very important, because when there is increased inflation over a long period of time, economic agents recognize the actual value of money, stop suffering from money illusion and accept increased nominal rates. Therefore, investment as the main link between the interest rates and the real economy is considered a function of the real interest rates, as standard (Bencik; 2014).

# Monetary Policy in Nigeria

CBN act 1959 clearly states that the objectives to be achieved by the CBN act to include the following: (1) Full employment attainment, (2) Long term interest rate stability 3) Optimal exchange rate target pursuance. According to Onyeiwu (2012) the CBN monetary policy in use has been charged with authority of devising and enforcing monetary policy of the CBN act (1958). The development of monetary policy is categorized in two stages: (1) direct control era (1959-1986) and (2) market-based controls era (1986-date). Direct control phase was an exceptional time in Nigeria’s monetary management period. This is because it aligned with different changes in the structure of the economy. This includes economic base shift from agriculture to petroleum, civil war enforcement, the boom and crash in oil prices in both 1970s and 1980s, with the establishment of the structural adjustment programme. In this era, the monetary policies of the central bank was concentrated on putting in place and managing the rate

of interest and exchange, discerning allocation to certain sectors, discount rate manipulations, finally moral suasion.

SAP commenced in 1986 and adjustments made to the CBN act in 1991 brought in a new era of implementation of monetary policy in Nigeria. This precisely guaranteed CBN goal autonomy and full instrument. Employing this method, CBN influences parameters in the economy indirectly via its OMO. The activities conducted are mainly on TB and REPOs serving a complimentary role with reserve requirements usage, Liquidity ratio and Cash Reserve Ratio. The above instruments set is employed to cause changes in the quantity base nominal anchor (monetary aggregates) employed in monetary programming.

In other way, the cash reserve ratio (CRR) is used as the price based nominal anchor in swaying the direction in the economy cost of fund. Movements in this rate is a signal to the banks’ monetary disposition, either it is pursuing a tightening or an expansionary monetary policy. They are generally placed within 26% and 8% range from 1986. The CBN latter established in 2006 the monetary policy rate (MPR) to replace CRR which states the rate of interest corridor added and subtract 2% point of existing MPR.

# Monetary Policy Instruments

The instruments of monetary policy can be categorized into two namely:

1. Direct or quantitative instruments
2. Indirect of qualitative instruments

# Direct Instruments or Qualitative Instruments of Monetary Policy Tools

Though there is an avalanche of instruments available for money and credit control, the instrument mix to be employed at any time depends on the goals to be achieved and the effectiveness of such instrument to a large extent hinges on the economic fortunes of the country.

1. **Reserve Requirement:** The Central Bank may require Deposit Money Banks to hold a fraction (or a combination) of their deposit liabilities (reserves) as vault cash and or deposits with it. Fractional reserve limits the amount of loans banks can make to the domestic economy and thus limit the supply of money. The assumption is that Deposit Money Banks generally maintain a stable relationship between their reserve holdings and the amount of credit they extend to the public.
2. **Special Deposits:** The central bank has the power to issue directories from time to time requiring all banks to maintain with it as special deposit an amount equal to the percentages of the institution’s deposits liabilities or the absolute increase in its deposit liabilities over an amount outstanding at a certain date.
3. **Moral Suasion:** Moral suasion simply means the employment by the monetary authority of friendly persuasive statement, public pronouncement outright appeal the monetary authority sometimes uses the less tangible technique to influence the lending policies of commercial banks. Consequences to the banking system and the economy as a whole, the Central Bank of Nigeria holds periodic meetings with the bankers committees and on other occasion meets formally or informally with the leaders in the banking community (CBN, 2013). With the leaders in the banking community – such contracts are geared towards the development of confidence between the central bank and other banks. It affords the central bank opportunity to discuss the improvement in standards and conducts in the banking industry.
4. **Selective Credit Control:** According to Nnanna (2006), this instrument is used to distinguish among the sectors of the economy into preferred and less preferred sectors. This is usually designed to influence the direction of credits in the economy so as to ensure that

credits go to those sectors designed “preferred”. It is very useful where a country operates development plans like Nigeria. When plans are drawn up these credit controls will be integrated in the budget. In course of the government’s programme to revitalize agricultural production which is the most favored sector, credits to the favored sector is at lower interest rate while the least favored sectors pay the highest rate of interest.

1. **Direct Credit Control:** According to CBN (2013), the Central Bank can direct Deposit Money Banks on the maximum percentage or amount of loans (credit ceilings) to different economic sectors or activities, interest rate caps, liquid asset ratio and issue credit guarantee to preferred loans. In this way the available savings is allocated and investment directed in particular directions.
2. **Prudential Guidelines:** The Central Bank may in writing require the Deposit Money Banks to exercise particular care in their operations in order that specified outcomes are realized (CBN, 2013). Key elements of prudential guidelines remove some discretion from bank management and replace it with rules in decision making.

# Indirect Instruments or Quantitative Instruments of Monetary Policy

Fiduciary or paper money is issued by the Central Bank on the basis of computation of estimated demand for cash. To conduct monetary policy, some monetary variables which the Central Bank controls are adjusted-a monetary aggregate, an interest rate or the exchange rate-in order to affect the goals which it does not control. The instruments of monetary policy used by the Central Bank depend on the level of development of the economy, especially its banking sector. The commonly used instruments are discussed below (CBN, 2016):

1. **Open Market Operations:** The Central Bank buys or sells (on behalf of the Fiscal Authorities (the Treasury) securities to the banking and non-banking public (that is in the

open market). One such security is Treasury Bills. When the Central Bank sells securities, it reduces the supply of reserves and when it buys (back) securities-by redeeming them-it increases the supply of reserves to the Deposit Money Banks, thus affecting the supply of money (CBN, 2013; Ibeabuchi, 2012; Ojo, 2013; & Solomon, 2013).

1. **Lending by the Central Bank:** The Central Bank sometimes provide credit to Deposit Money Banks, thus affecting the level of reserves and hence the monetary base (CBN, 2013).
2. **Interest Rate:** The Central Bank lends to financially sound Deposit Money Banks at a most favourable rate of interest, called the minimum rediscount rate (MRR). The MRR sets the floor for the interest rate regime in the money market (the nominal anchor rate) and thereby affects the supply of credit, the supply of savings (which affects the supply of reserves and monetary aggregate) and the supply of investment (which affects full employment and GDP) according to Obidike, Ejeh, &Ugwuegbe (2015)
3. **Exchange Rate:** The balance of payments can be in deficit or in surplus and each of these affect the monetary base, and hence the money supply in one direction or the other. By selling or buying foreign exchange, the Central Bank ensures that the exchange rate is at levels that do not affect domestic money supply in undesired direction, through the balance of payments and the real exchange rate. The real exchange rate when misaligned affects the current account balance because of its impact on external competitiveness (Akpan, 2013: Imoisi, Olatunji&Ekpenyong, 2013; Ibeabuchi, 2012; & Sanusi, 2009).
4. **Rediscount Rate:** The rediscount rate is the rate at which the central bank stands really to provide loan accommodation to commercial banks (CBN, 2013). As a lender of last resort, such lending by the central bank is usually at panel rates. By making appropriate changes

in the rate, the central bank controls the volume of total credits indirectly. This has the purpose of influencing the lending capacity of the commercial banks. During the periods of inflation, the central bank may raise the rediscount rate making obtaining of funds from the central bank more expensive. In this way, credit is made tighter. Similarly, in depression, when it is necessary to encourage commercial banks to create more credits, the central bank will lower the rediscount rate.

1. **Cash Reserve Requirements:** Ojo (2013) posit that the reserve requirement can be manipulated by the central bank to reduce the ability of commercial banks to make loans to the public by simply increasing the ratio or enhancing their lending position by decrease in the ratio. Reserve requirement is loan of the most powerful instruments of monetary control (CBN, 2013). A change in the required reserve ratio changes the ratio by which the banking system can expand deposit through the multiplier effect. If the required reserve ratio increases, the multiplier decreases and thereby reduces the liquidity position of the banking system.

# Monetary Policy and Economic Growth

Taylor (2009) mentions that monetary Policy is a key component of any pro-growth economic system and much so in developing economies such as the Nigerian Economy. In general terms, monetary policy refers to a combination of measures designed to regulate the value, supply and cost of money in an economy in consonance with the expected level of economic activity. For most economies, Nigerian economy inclusive, the objectives of monetary policy includes price stability, maintenance of Balance of Payments equilibrium, promotion of employment and output growth.

Gbosi (2007), posits that monetary policy aims at controlling money supply so as to counteract all undesirable trends in the economy, these undesirable trends may include; unemployment, inflation, sluggish economic growth or disequilibrium in the Balance of Payments. Monetary policy may either be expansionary or restrictive. An expansionary monetary policy is designed to stimulate the growth of aggregate demand through increase in the rate of money supply thereby making credit more available and interest rates lower. An expansionary monetary policy is more appropriate when aggregate demand is low in relation to the capacity of the economy to produce goods and services.

On the contrary, if the quantity of money is reduced or restricted, money income will rise slowly so that consumers spend less and funds for investment are difficult to acquire thereby decreasing aggregate investment (restrictive monetary policy) (Imoisi, Olatunji, &Ekpenyong, 2013).

Nnanna (2006) observed that the pursuit of price stability invariably implies the indirect pursuit of objectives such as Balance of Payments (BOP) equilibrium. Anyanwu (2009) posits that an excess supply of money in the economy will result to excess demand for goods and services and in turn causes rise in prices and also, affect the Balance of Payments position. With the achievement of price stability, the uncertainties of general price level will not materially affect consumption and investment decisions. Rather, economic agents will take long-term decision without much reservation about price change in the macro-economy.

The condition in the financial markets and institutions would create a high degree of confidence, such that the financial infrastructure of the economy is able to meet the requirements of market participants (Nkoro, 2008). In other words, an unstable and crisis ridden financial system will render the transmission mechanism of monetary policy less effective, making the achievement and maintenance of strong macroeconomic fundamentals difficulty.

Akomolafe, Danladi, Babalola & Abah (2015) noted that as a stabilization policy, monetary policy involves the use of monetary instruments to regulate or control the volume, cost, availability and the direction of money and credit in an economy to achieve some specific macroeconomic policy objective. According to Onouorah, Shaib, Oyathelemi, & Friday (2016), it is a deliberate attempt by the monetary authority (Central Bank) to control the money supply and credit condition in the economy so as to achieve certain economic objective. Some of the macroeconomic objectives include price stability, full employment, sustainable economic growth, balance of payment equilibrium. The monetary instruments include bank rate, open market operation, reserve requirements etc. Economic activities are not directly affected by monetary policy instruments; they work through their effects on the financial markets. It affects economic activities through its effects on available resources in the banking sector (Akomolafe, Danladi, Babalola & Abah, 2015).

# The Role of Deposit Money Banks in the Nigeria Economy

The traditional role of banks is to accept deposits and make loans and derive a profit from the difference in the interest rates paid and charged to depositors and borrowers respectively. The process performed by banks of taking in funds from a depositor and then lending them out to a borrower is known as financial intermediation (Sanderson, 2013). Through the process of financial intermediation, certain assets are transformed into different assets or liabilities. As such, financial intermediaries channel funds from people who have extra money or surplus savings (savers) to those who do not have enough money to carry out a desired activity (borrowers). Banking thrives on the financial intermediation abilities of financial institutions that allow them to lend out money and receiving money on deposit. The bank is the most important

financial intermediary in the economy as it connects surplus and deficit economic agents. Sanderson (2013) summarized roles of deposit money banks to include:

1. **Credit Provision:** Credit fuels economic activity by allowing businesses to invest beyond their cash on hand, households to purchase homes without saving the entire cost in advance, and governments to smooth out their spending by mitigating the cyclical pattern of tax revenues and to invest in infrastructure projects.
2. **Liquidity Provision:** Businesses and households need to have protection against unexpected needs for cash. Banks are the main direct providers of liquidity, both through offering demand deposits that can be withdrawn any time and by offering lines of credit. Further, banks and their affiliates are at the core of the financial markets, offering to buy and sell securities and related products at need, in large volumes, with relatively modest transaction costs.
3. **Risk Management Services:** Banks allow businesses and households to pool their risks from exposures to financial and commodity markets. Much of this is provided by banks through derivatives instruments transactions. Banks also enable individuals and businesses to take part in the global foreign exchange and commodity markets indirectly. It would be very difficult for example for a small company needing only a few million Japanese yen to import a vehicle from Japan to get onto the global currency markets without the aid of a bank.
4. **Remittance of Money:** Cash can be transferred easily from one place to another and from one country to another by the help of a bank. It has facilitated transactions in distant places. This, in turn, has expanded the internal and external trade and market. The men have become free of the risks of carrying cash, gold, silver etc. The credit instruments issued by

banks such as cheque, draft, Real time gross settlement, credit cards have facilitated the transfer of money.

1. **Rapid Economic Development:** the banks make available loans of different periods to agriculture, industry and trade. They make direct investments in industrial sectors. They provide industrial, agricultural and commercial consultancy hence facilitating the process of economic development.

# Determinants of Financial Performance

The determinants of bank performances can be classified into bank specific (internal) and macroeconomic (external) factors. Internal factors are individual bank characteristics which affect the bank’s financial performance. These factors are basically influenced by internal decisions of the management and the board. The CAMEL framework is often used to proxy the bank specific factors. CAMEL stands for Capital Adequacy, Asset Quality, Management Efficiency, Earnings Ability and Liquidity Management. External determinants of bank profitability are factors that are beyond the control of a bank’s management. They represent events outside the influence of the bank. However, the management can anticipate changes in the external environment and try to position the institution to take advantage of anticipated developments.

# Capital Adequacy

Capital is the amount of owner funds available to support a bank's business and act as a buffer in case of adverse situation (Athanasoglou, Brissimis and Delis, 2010). Bank’s capital creates liquidity for the bank due to the fact that deposits are most fragile and prone to bank runs. Moreover, greater bank capital reduces the chance of distress. Capital adequacy is the level of capital required by the banks to enable them withstand risks such as credit, market and

operational risks they are exposed to in order to absorb the potential loses and protect the bank's debtors. The adequacy of capital is judged on the basis of capital adequacy ratio (CAR). Capital adequacy ratio shows the internal strength of the bank to withstand losses during crisis. Capital adequacy ratio is directly related to the resilience of the bank to crisis situations. It has also a direct effect on the profitability of banks by determining its expansion to risky but profitable ventures or areas (Sangmi and Nazir, 2015).

# Asset Quality

The bank's asset is another bank specific variable that affects the profitability of a bank. The bank asset includes among others current asset, loan portfolio, fixed asset, and other investments. More often than not the loan book of a bank is the major asset that generates the major share of the banks income. The loan portfolio quality has a direct bearing on bank profitability. The highest risk facing a bank is the losses that arise from non-performing loans. Thus, nonperforming loan ratios are the best proxies for asset quality. It is the major concern of all commercial banks to keep the amount of nonperforming loans at a low level. Thus, low nonperforming loans to total loans ratio shows good health of the portfolio a bank. The lower the ratio the better the deposit money banks financial performance (Sangmi and Nazir, 2015).

# Management Efficiency

Management Efficiency is one of the key internal factors that determine the bank profitability. It is represented by different financial ratios like total asset growth, loan growth rate and earnings growth rate. Yet, it is one of the complex subject to capture with financial ratios. Moreover, operational efficiency in managing the operating expenses is another dimension for evaluating management quality. The performance of management is often expressed qualitatively through subjective evaluation of management systems, organizational discipline, control systems, quality

of staff, and others parameters. The capability of the management to deploy resources efficiently, income maximization, reducing operating costs can be measured by financial ratios. One of the ratios used to measure management quality is operating profit to income ratio (Sangmi and Nazir, 2015). The higher the operating profits to total income (revenue) the more the efficient management is in terms of operational efficiency and income generation. The other important ratio that proxy management quality is expenses to asset ratio. The ratio of operating expenses to total asset is expected to be negatively associated with profitability. Management quality in this regard, determines the level of operating expenses and in turn affects profitability (Athanasoglou et al. 2010).

# Earnings Ability

Financial institutions in the recent years have increasingly been generating income from off- balance sheet business and fee income. Albertazzi and Gambacorta (2011) noted that the decline in interest margins forced banks to explore alternative sources of revenues leading to diversification into trading activities, other services and non-traditional financial operations. The concept of revenue diversification follows the concept of portfolio theory which states that individuals can reduce firm specific risk by diversifying their portfolios.

Sufian and Chong (2014) found a positive relationship between total non-interest income divided by total assets, a proxy for income diversification, and a bank profitability using data from all commercial banks in Philippines.

# Liquidity Management

Liquidity is another factor that determines the level of bank performance. Liquidity refers to the ability of the bank to fulfill its obligations, mainly of depositors. Adequate level of liquidity is positively related with bank profitability. The most common financial ratios that reflect the

liquidity position of a bank are customer deposit to total asset and total loan to customer deposits. Other financial ratios can be used to measure liquidity. Ilhomovich (2014) used cash to deposit ratio to measure the liquidity level of banks in Malaysia.

# Macroeconomic variables

Macroeconomic conditions may affect banking performance in a number of ways. Firstly, there will be a higher demand for bank credit in times of economic boom than in times of recession. A high aggregate growth rate may strengthen the debt servicing capacity of domestic borrowers, and therefore, contribute to less credit risk. Alternatively, adverse macroeconomic conditions hurt banks by increasing the amount of non-performing loans. Thus, it is expected that an improvement in economic growth helps bank performance.

Secondly, it is generally believed that a rising interest rate should lead to higher banking sector profitability by increasing the spread between the saving and the borrowing rates. Hanweck and Kilcollin (2004) found that this relationship is particularly apparent for smaller banks in the USA during the 1976-1984 period. They noticed that falling interest rates during recession lead to slower growth in loans and increase in loan loss. Consequently, banks, particularly the small ones, may have difficulty in maintaining profit as market rate drops. Further studies by Demirguc-Kunt and Huizinga (2009), Staikouras and Wood (2008) and Cheang (2010) all notice a positive relationship between interest rates and bank profitability.

Finally, the effect of inflation is also another important determinant of banking performance. In general, high inflation rates are associated with high loan interest rates and thus high income. Perry (2002), however, asserts that the effect of inflation on banking performance depends on whether inflation is anticipated or unanticipated. If inflation is fully anticipated and interest rates are adjusted accordingly, a positive impact on profitability will result. Alternatively, unexpected

rises in inflation cause cash flow difficulties for borrowers, which can lead to premature termination of loan arrangements and precipitate loan losses. Indeed, if the banks are sluggish in adjusting their interest rates, there is a possibility that bank costs may increase faster than bank revenues. Hoggarth et al., (2008) even conclude that high and variable inflation may cause difficulties in planning and in negotiation of loans.

The findings of the relationship between inflation and profitability are mixed. Although the studies of Guru et al., (2007) in Malaysia and Jiang et al., (2008) in Hong Kong show that higher inflation rate leads to higher bank profitability, the study of Abreu and Mendes (2005), nevertheless, reports a negative coefficient for the inflation variable in European countries. In addition, Demirguc-Kunt and Huizinga (2009) notice that banks in developing countries tend to be less profitable in inflationary environments, particularly when they have a high capital ratio. In these countries, bank costs actually increase faster than bank revenues.

# Financial structure variables

Many studies in the banking literature investigate whether financial structure, which is defined as the relative importance of banks, plays a role in determining banking performance. In general, a high bank asset-to-GDP ratio implies that financial development plays an important role in the economy. This relative importance may reflect a higher demand for banking services, which in turn, attracts more potential competitors to enter the market. When the market becomes more competitive, banks need to adopt different strategic moves in order to sustain their profitability. Demirguc-Kunt and Huizinga (2009) present evidences that financial development and structure variables are very important. Their results show that banks in countries with more competitive banking sectors, where bank assets constitute a large portion of GDP, generally have smaller margins and are less profitable. Also, they notice that countries with underdeveloped financial

systems tend to be less efficient and adopt less-than-competitive pricing behaviours. In fact, for these countries, greater financial development can help to improve the efficiency of the banking sector. Consequently, the market structure of the banking industry shows important implications for profitability.

Furthermore, studies by Smirlock (2005), Bourke (2009) and Staikouras and Wood (2008) suggest that industry concentration has a positive impact on banking performance. The more concentrated the industry is, the greater the monopolistic power of the firms will be. This, in turn, improves profit margins of banks. However, there are also some studies that report conflicting results. For example, Naceur (2008) reports a negative coefficient between concentration and bank profitability in Tunisia. Also, Karasulu (2006) finds that the increasing concentration does not necessarily contribute to profitability of the banking sector in Korea.

# Theoretical Framework

The performance of deposit money banks is influenced by a host of many factors some of which are macro-economic, institutional, regulatory and legal. The common features of the theories discussed in Uchendu (2010) indicated that in attempting to maximize profits, banks must comply with capital adequacy and liquidity considerations. Uchendu (2010) rightly stated that regulatory influences of monetary authorities include those on interest and exchange rates, bank reserves (indicating credit availability), labour cost or productivity

# Classical Theory

The widely accepted approach to monetary economics was known as the quantity theory of money, used as part of a broader approach to micro and macro issues referred to as classical economics from the works of Irving fisher who lay the foundation of the quantity theory of money through his equation of exchange. Diamond (2008) states in his proposition that money

has no effect on economic aggregates but price. The classical school evolved through concerted efforts and contribution of economists like Jean Baptist Say, Adam Smith, David Richardo, Pigu and others who shared the same beliefs. The classical economists decided upon the quantity theory of money as the determinant of the general price level. Most were of the opinion that the quantity of money determines the aggregate demand which in term determine the price level as posited by Amacher & UIbrich (2006).

Onouorah, Shaib, Oyathelemi, & Friday (2016) mentions that the quantity theory of money was not only a theory about the influence of money on the economy and how a Central Bank should manage the economy’s money supply, but it represented a specific view of the private market economy and the role of government. The private market such as banks provided the best framework for achieving socially and economically desired outcomes. According to the theory, the role of government was providing a system of laws and security to protect private property, as well as providing a stable financial and monetary framework. Solomon (2013) acknowledges that theory posit that money affects the economy which is the reason why Central banks adopt monetary policy to control the flow of money in the economy through banks that are regarded as the private market industry that mobilizes the largest volume of money in any economy. The economic depression of the 1930s, according to Onyemaechi (2010) drastically changed attitudes about the role of money and monetary policy as a tool of economic stabilization. Monetary policy was then viewed as an ineffective method of fighting depressions, and the belief in a self- regulating market that reached socially desirable results was destroyed.

# The Keynesian Theory

The Keynesian Economists think of monetary policy as working primarily through interest rate. In Keynesian transmission mechanism, an increase in the money supply leads to a fall in interest rate to include the public to hold additional money balances.

Consequently, a fall in interest rate may stimulate investment. The increased investments also increase the level of income or output through the multiplier, which may stimulate economic activities. Thus, monetary policy affects economic activity indirectly through their impact on interest rates and investment. Therefore, the Keynesian transmission mechanism is characterized by a highly detailed sector building up of aggregate demand and a detailed specification of portfolio adjustment process that attaches central role to interest as an indirect link between monetary policy and fiscal demand.

In simple terms, the monetary mechanism of Keynesians emphasizes the role of money, but involves an indirect linkage of money with aggregate demand via the interest rate as symbolically shown below:

OMO RMSr IGNP Where, OMO = Open Market Operation R = Commercial Bank Reserve

MS = Stock of Money r = Interest Rate

I = Investment

GNP = Gross National Product

On a more analytical note, if the economy is initially at equilibrium and there is open market purchase of government securities by the Central Bank of Nigeria (CBN), this open Market

Operation (OMO) will increase the commercial banks reserve (R) and raise the bank reserves. The bank then operates to restore their desired ratio by extending new loans or by expanding bank credit in other ways. Such new loans create new demand deposits, thus increasing the money supply (MS). A rising money supply causes the general level of interest rate (r) to fall. The falling interest rates affects commercial bank performance and in turn stimulate investment given businessmen expected profit. The induced investment expenditure causes successive rounds of final demand spending by GNP to rise by a multiple of the initial change in investment. On the other hand, a fall in money supply causes the general level of interest rate (R) to rise or increase thereby increasing the commercial banks profitability (Jhingan, 2010).

# The Monetarist Theory

The Monetarist Economist recognize that money is not just a close substitute for a small class of financial assets but rather a substitute for large spectrum of financial and real asset. Given an equilibrium position, an increase in money supply raises the actual proportion of money relative to the desired proportion. Symbolically, the monetarist conception of money transmission mechanism can be summarized below:

OMO MS Spending GNP

The monetarist argument centres on the old quantity theory of money. If velocity of money in circulation is constant, variation in money supply will directly affect prices and output or income (GNP), (M. L. Jhingan, Monetary Economics 6th Edition, P. 418 – 419).

# Anticipated Income Theory

This theory states that banks should involves themselves in a broad range of lending which may include long-term loans to business, consumer installment loans and amortized real estate mortgage loans considering the fact that the likelihood of loan repayment which generates a cash

flow that supplement bank liquidity depends on the anticipated income of the borrower and not the use made of the funds. This implies that a high excess reserve increases profitability of banks by increasing the availability of loanable investment funds.

# Liability Management Theory

The theory holds that banks could satisfy any liquidity need and short-run profit opportunity by issuing money market liabilities such as certificate of deposit (CD). Another version of the theory states that money market bank liabilities should be used along with bank assets to meet liquidity needs, which will lead to deposit money banks profitability.

# Shiftability Theory

The central thesis of this theory holds that the liquidity of a bank depends on its ability to shift its assets to someone else at a predictable price. Better still; the theory of shiftability exposes the banks vulnerability to government security for liquidity. Whether or not a bank can quickly realize liquidity through this means depends on the marketability of the securities and their relative prices. The theory tries to broaden the list of assets demand legitimate for ownership and hence redirected the attention of bankers and the banking authorities from loan to investment as source of bank liquidity.

It is hypothesized that an increase in capital investment will lead to commercial banks profitability. However, increase in profits may also motivate further increase in capital investment, which in turn expands the scope of banking operations for increased profitability. Adequate capital investment provides for a bank to perform the intermediation function and provide related financial services. It also provides protection in conditions of near economic collapse against unanticipated adversity leading to loss in excess of normal expectations and

permits banks to continue operations in periods of difficulty until a normal level of earning is restored.

# Literature on Subject Matter

There are several documented studies on the determinants of financial performance of commercial banks globally. Some of the studies incorporated various monetary tools in analyzing the effect of macroeconomic stability on commercial banks‟ financial performance. Some of these studies are reviewed in this section.

Gambacorta and Iannoti (2010) investigated the velocity and asymmetry in response of bank interest rates (lending, deposit, and inter-bank) to monetary policy shocks (changes) in Italy from 1985-2002 using an Asymmetric Vector Correction Model (AVECM) that allows for different behaviours in both the short-run and long-run .The study shows that the speed of adjustment of bank interest rate to monetary policy changes increased significantly after the introduction of the 1993 Banking Law, interest rate adjustment in response to positive and negative shocks are asymmetric in the short run, but not in the long-run. They also found that banks adjust their loan (deposit) prices at a faster rate during period of monetary tightening (easing).

Rao and Somaiya (2011) investigated the impact of monetary policy on the profitability of banks in India between 1995 and 2000. The monetary variables were banks rate, lending rates, cash reserve ratio and statutory ratio, and each regressed on banks profitability independently. Lending rate was found to exact positive and significant influence on banks‟ profitability, which indicates a fall in lending rates will reduce the profitability of the banks. Also, bank rate, cash reserve ratio and statutory ratio were found to significantly affect profitability of banks negatively. Their findings were the same when lending rate, bank rate, cash reserve ratio and

statutory ratio were pooled to explain the relationship between bank profitability and monetary policy instruments in the private sector.

Younus and Akhta (2014) examined the significance of Statutory Liquidity Requirement (SLR) as a monetary policy instrument in Bangladesh. Using descriptive analysis techniques like trend analysis and summary statistics, they found that statutory liquidity requirement has experienced infrequent changes and past evidence has shown that reduction in SLR produced positive impact on bank credit and investment especially prior to the 1990s. SLR and Cash Reserve Requirement (CRR) were found to be significant tools of reducing inflation and both for scheduled banks are used only in situation of drastic imbalance-resulting from major shocks. They observed that Bangladesh Bank has used open market operations (OMOs), more frequently rather than changes in the Bank rate and SLR as instruments of monetary policy in line with its market oriented approach.

Gul, Irshad and Zaman (2016) research was focused on examining the effect of bank specific and macroeconomic factors on bank profitability by using data of top 15 Pakistan commercial banks over the period 2005-2009. The Pooled Ordinary Least Square (POLS) method was used to investigate the impact of assets, loans, equity, deposits, economic growth, inflation and market capitalization on profitability, measured through return on asset (ROA), return on equity (ROE), return on capital employed (ROCE) and net interest margin (NIM). The results found evidence that both internal and external factors have a strong influence on profitability.

Syafri (2012) study analyzed the factors that affect the profit of commercial banks in Indonesia, using polling data from commercial banks listed on the Indonesia Stock Exchange between 2002 and 2011. Bank profitability was measured by return on assets and results showed that loan to

total assets, total equity to total assets and loan loss provision to total loan have positive effect on profitability.

The study by Frederic (2014) examined the factors responsible for determining the performance of domestic commercial banks in Uganda. The study used linear multiple regression analysis over the period 2000-2011 to analyze the data of all licensed domestic and foreign commercial banks. The study found that, management efficiency; asset quality; interest income; capital adequacy and inflation influence on the bank’s performance in Uganda.

Cekrezi (2015) carried a study to explore the factors that mostly affect financial performance of commercial banks which operate in Albania. The study population consisted of 16 commercial banks with domestic and foreign capital, during the period 2010 to 2013 with a total of 48 data. The investigation used cross sectional time series data which were collected from the Balance Sheet Annual Reports. The study concluded that bank size has a negative but statistically insignificant effect on banks profitability, capital adequacy was one of the bank specific factors that influence the level of bank profitability while liquidity was negatively related with profitability.

Udeh (2015) examined the impact of monetary policy instruments on profitability of commercial banks in Nigeria using the Zenith Bank Plc. experience. The paper used descriptive research design. It utilized time series data collected from published financial statements of Zenith Bank Plc as well as Central Bank of Nigeria Bulletin from 2005 to 2012. Four research questions and four hypotheses were raised for the study. Pearson Product moment correlation technique was used to analyze the data collected while t-test statistic was employed in testing the hypotheses. The study discovered that cash reserve ratio, liquidity ratio and interest rate did not have significant impact on the profit before tax of Zenith Bank Plc. However, minimum rediscount

rate was found to have significant effect on the profit before tax of the bank. The paper concluded that a good number of monetary policy instruments do not impact significantly on profitability of commercial banks in Nigeria. The paper recommended that management of commercial banks in Nigeria should look beyond monetary policy instruments to enhance their profits.

Kiganda (2014) investigated the effect of macroeconomic factors on bank profitability in Kenya with equity bank limited in focus. In view of the previous inconclusive findings on the effect of macroeconomic factors on bank profitability among researchers, the study was to establish the effect of macroeconomic factors on bank profitability in Kenya with Equity bank in focus. The study specifically sought to determine, establish and examine effect of; economic growth (real GDP), inflation and exchange rate on bank profitability in Kenya with Equity bank in focus respectively using annual data for the period of 5 years spanning from 2008 to 2012and examined using multiple regression analysis. The OLS results show that macroeconomic factors have insignificant effect on bank profitability in Kenya with equity bank in focus. Specifically; economic growth (real GDP) and inflation have a positive insignificant effect whereas exchange rate has a negative insignificant effect at 5 % level.

# CHAPTER THREE RESEARCH METHODOLOGY

# Research Design and Sources of Data

The section that could have referred to as either research design or research method is very critical to the entire research process. It is in this section that the research stamps his scientific status on the process. A research design therefore is a blue print or scheme that is used by the research for specific structure and strategy in investigating the relationship that exist among variables of the study as to enable time or her collect the data which will be used for the study. Research designs are basically of four types, which are “experimental, historical, survey and case study research design”. For the purpose of this study, the researcher adopted the case study approach in evaluating the effect of monetary policy on the performance of deposit money bank in Nigeria. Both primary and secondary sources of data were adhered to on the course of this study and the attitude and responses of those interviewed were noted.

# Primary Sources of Data

The primary sources of data are the sampling or study unit from which information is obtained on a first-hand basis. It is very important to note here that the researcher did not adopt any rigid method in the collection of data; rather the data for the research were collected in response to the requirements of the research problem. Creativity and judgment also played a vital role at this stage of the project, bearing in mind the final judgment will be partly constrained be the type and values of information collected. The primary data were gathered from the following sources:

* + - 1. **Oral interview:** Personal interviews were conducted in addition to the questionnaires that were duly administered. The information obtained through the oral interview was use in cross checking the responses to the questionnaire. It either affirmed or disproved the data collected.
			2. **Unstructured interviews:** Unstructured interviews were also collected out through informal discussions with various staff members at different levels of operations.
			3. **Actual field investigation:** The researcher was privileged to see the annual reports in order to fully comprehend their performance as well as its reporting style.

# Secondary Sources of Data

Library and internet materials provided the bulk of the secondary research data collected by the researcher. These resource materials were used to review extensively the facts and the reporting components of all the Banks. For the purpose of obtaining these secondary data the following academic libraries and website were used:

1. Wikipedia.com
2. Google.com
3. The Library

In summary, these sets of data gathered which includes:

* Data from and interview, internet and library materials
* Data from the compilation of other related research work previously conducted The data gathered was used at three different stages as follows:
* In anticipation of these data, the question on the questionnaires were design in order to ensure that the respondents will confirm these data
* The data also formed the basis upon which the review of related literature was carried out
* They also formed part of the analysis that will be carried out in chapter four which led to conclusion which was later arrived at in chapter five.

# Study Population and Determination of Sample Size

Population is described as the entire member of object that needs to be studied. The population in this research work was the deposit money bank in Nigeria in which Union Bank of Nigeria was used as a case study.

A sample is a portion of the population selected for study. It is very important to select sample size that will give sufficient fair representation of the population. There are two basic way of making the sample size decision, one is by rule of thumb and the other one is by calculated method. In this research work, the rule of the thumb was used for this research where 50 workers of total population were selected as the sample size. The sample is also made up of senior and junior staff of the Banks.

# Instrumentation

A questionnaire is a composition of carefully selected and ordered questions, statements presented to the respondents in order to obtain information or data. Data required testing the hypothesis. This test will provide answers to the questions raised in the research problem. The

questionnaires were administered based on the non-random selection of the persons as contained in the sample. This was done in such a way as to get the desired result. The questionnaire contains fifty (50) questions. The questions are from of close-ended where respondents are expected to give their opinion freely without having to choose from any alternative.

Methods for instrument for data collection also include personal observation. Personal observation is the process of data collection, personal tour to the internal accounting department, where the case study was made. The researcher conducted random checking is into various departments for any easy observation and keeping custody of receipts and other relevant documents/information.

# Procedure for Data Collection and Data Analysis

Collection of data refers to the research instruments used by the researcher to collect whatever data needed. The research instruments used in this research include: questionnaires, internet, interviews and library research. Questionnaires were employed by the researcher because it is most practical, economical and easiest way of obtaining information about events. They also helped in collecting information that are valid interview schedule was made use of by the researcher because of its usefulness in following up on unexpected result in order to validate other method or problem motivation of respondents and their reasons for responding the way they did. The primary data gathered were effectively and extensively employed in the next chapter to test the formulated hypothesis.

The researcher translated the data into simple percentages. This was to enable an inferential statement to be made about any relationship. The formulated hypotheses were tested using chi- square (X2) test statistics which measures the significance of the difference between the observed set of frequencies. The computations were done using the chi-square formula which is:

X2 =∑ (oi - ei)2

ei

Where, oi = observed frequency ei = expected frequency

The research hypotheses earlier formulated in the chapter one were tested in chapter four for acceptance or rejection using the Chi-square statistical techniques.

# Limitations of the Study

Limitations envisage in this research work are:

1. Restriction on data generation: the data obtained was restricted to the case study
2. Time frame of this research work is another limitation as more time may be required to get up to date information from bank and clients
3. Also there might be financial and transportation congestion constraints to this study

# CHAPTER FOUR

**DATA ANALYSIS, FINDINGS AND DISCUSSION**

# Introduction

In this chapter, the data collected from questionnaire are presented, analysed and tabulated. Fifty questionnaires were prepared and distributed to the respondent drawn from lower and senior staff of Union Bank Plc.

The analysis were carried out using simple percentage method, the hypothesis will be analyse using the chi-square based on the analysis of the relevant questions.

# Data Analysis and Findings

**Table 4.1.1 Sex distribution of the respondent**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Male | 32 | 64 | 64 | 64 |
| Valid | Female | 18 | 36 | 36 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

As shown in the table above, it was revealed that 32 (64%) of the respondents are male while 18 (36%) are female.

# Table 4.1.2 Age distribution of the respondents

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | 20-30years | 6 | 12 | 12 | 12 |
|  | 31-40years | 24 | 48 | 48 | 60 |
| Valid | 41- above | 20 | 40 | 40 | 100 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

As shown in the table above, it was revealed that 6 (12%) of the respondents fall under the age range of 20 to 31years, 24 (48%) of the respondents fall in 31 to 40 years, while 20 (40%) of the respondents falls to 41 years and above.

# Table 4.1.3 Marital Status of the respondents

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Single | 10 | 20 | 20 | 20 |
| Valid | Married | 40 | 80 | 80 | 100 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

As shown in the table above, it was revealed that 10 (20%) of the respondents are single while 40 (80%) are married

# Table 4.1.4 Academic qualification of the respondents

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | OND/NCE | 16 | 32 | 32 | 32 |
|  | HND/BSC | 22 | 44 | 44 | 76 |
| Valid | MBA/MSC | 8 | 16 | 16 | 92 |
|  | OTHERS | 4 | 8 | 8 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

According to academic qualification of respondent of respondents, the responses in the questionnaires shows that respondents 16 (32%) are Diploma/NCE holders, 22 (44%) respondents are BSC/HND certificate holders while 8 (16%) respondents are MBA/MSC holders.

# Table 4.1.5 Year of Experience of the respondents

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | 0-5YEARS | 12 | 24 | 24 | 24 |
|  | 6 – 10 YEARS | 20 | 40 | 40 | 64 |
| Valid | 11 – 15 | 10 | 20 | 20 | 84 |
|  | 16 and above | 8 | 16 | 16 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

Form the table above it shows that the 12 respondents representing 24% has a working experience for period of 0 – 5years, 20 respondents representing 40% has been working for the period of 6 – 10years, 10 respondents representing 20% has been working for 11 – 15 years while 8 respondents representing 16% has been working for 16 years and above.

# Section B:

**Table 4.1.6 is there any effect of monetary policy on the financial performance of commercial banks in Nigeria?**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 25 | 50 | 50 | 50 |
|  | Agree | 10 | 20 | 20 | 70 |
| Valid | Strongly Disagree | 9 | 18 | 18 | 88 |
|  | Disagree | 6 | 12 | 12 | 100 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

It could be inferred that majority of the respondent strongly agree that there are effect of monetary policy on the financial performance of commercial banks in Nigeria while minority disagreed.

# Table 4.1.7 Does your deposit money bank protect the helpless depositors?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 34 | 68 | 68 | 68 |
|  | Agree | 8 | 16 | 16 | 84 |
| Valid | Strongly Disagree | 4 | 8 | 8 | 92 |
|  | Disagree | 4 | 8 | 8 | 100 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

It could be inferred that majority of the respondent strongly agree that there deposit money bank protect the helpless depositors while minority strongly disagree and disagree.

# Table 4.1.8 Does deposit money bank put inflation into check?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 23 | 46 | 46 | 46 |
|  | Agree | 12 | 24 | 24 | 70 |
| Valid | Strongly Disagree | 10 | 20 | 20 | 90 |
|  | Disagree | 5 | 10 | 10 | 100 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

It could be seen from the table that the majority representing 70% strongly agreed and agreed that deposit money bank put inflation into check.

# Table 4.1.9 Does Central Bank Rate has effect on the financial performance of commercial banks in Nigeria?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 12 | 44 | 44 | 44 |
|  | Agree | 15 | 30 | 30 | 74 |
| Valid | Strongly Disagree | 10 | 20 | 20 | 94 |
|  | Disagree | 3 | 06 | 06 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

From the above table majority agreed that Central Bank Rate has effect on the financial performance of commercial banks in Nigeria whereas minority thought otherwise.

# Table 4.1.10 Does commercial banks create sustainable friendly banking environment in Nigeria?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 30 | 60 | 60 | 60 |
|  | Agree | 13 | 26 | 26 | 86 |
| Valid | Strongly Disagree | 3 | 6 | 6 | 92 |
|  | Disagree | 4 | 8 | 8 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

It could be deduced that the majority representing 86% strongly agreed and agreed that commercial banks create sustainable friendly banking environment in Nigeria.

# Table 4.1.11 Does Deposit money bank imposes or prescribe penalty on any defaulting financial institution?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 15 | 30 | 30 | 30 |
|  | Agree | 22 | 44 | 44 | 74 |
| Valid | Strongly Disagree | 10 | 20 | 20 | 94 |
|  | Disagree | 3 | 6 | 6 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

It could be deduced that the majority representing 74% strongly agreed and agreed that deposit money bank imposes or prescribe penalty on any defaulting financial institution.

# Table 4.1.12 Does deposit money bank policy affect banking operations in its bid to regulate money supply in the economy with particular reference to deposit and credit creation?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 28 | 56 | 56 | 56 |
|  | Agree | 13 | 26 | 26 | 82 |
| Valid | Strongly Disagree | 4 | 8 | 8 | 90 |
|  | Disagree | 5 | 10 | 10 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

The table above shows that almost all the respondents strongly agreed and agreed that deposit money bank policy affect banking operations in its bid to regulate money supply in the economy with particular reference to deposit and credit creation.

# Table 4.1.13 Does Reserve Ratio Requirement have effect on the financial performance of commercial banks in Nigeria?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 30 | 60 | 60 | 60 |
|  | Agree | 10 | 20 | 20 | 80 |
| Valid | Strongly Disagree | 6 | 12 | 12 | 92 |
|  | Disagree | 4 | 8 | 8 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

This table shows that most of the respondent strongly agreed and agreed that the Reserve Ratio Requirement have effect on the financial performance of commercial banks in Nigeria, while few respondents strongly disagreed and disagreed that the Reserve Ratio Requirement have effect on the financial performance of commercial banks in Nigeria.

# Table 4.1.14 Has Central Bank of Nigeria gone far in its achievement of regulating money supply?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 30 | 60 | 60 | 60 |
|  | Agree | 10 | 20 | 20 | 80 |
| Valid | Strongly Disagree | 7 | 14 | 14 | 94 |
|  | Disagree | 3 | 6 | 6 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

From the table above majority of respondents strongly agreed and agreed that the Central Bank of Nigeria has gone far in its achievement of regulating money supply. While only few respondents disagreed.

# Table 4.1.15 Do you think monetary policy has improve the industries in Nigeria as a whole?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 4 | 8 | 8 | 8 |
|  | Agree | 2 | 12 | 12 | 20 |
| Valid | Strongly Disagree | 30 | 60 | 60 | 80 |
|  | Disagree | 10 | 20 | 20 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

The table above shows that majority of respondent strongly disagreed and disagreed that monetary policy has improve the industries in Nigeria as a whole. While minority agreed.

# Table 4.1.16 Is there any impact of exchange rate on the performance of deposit money bank in Nigeria?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 32 | 64 | 64 | 64 |
|  | Agree | 12 | 24 | 24 | 88 |
| Valid | Strongly Disagree | 4 | 8 | 8 | 96 |
|  | Disagree | 2 | 4 | 4 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

It could be seen from the table that the majority representing 88% strongly agreed and agreed that there are impact of exchange rate on the performance of deposit money bank in Nigeria.

# Table 4.1.17 Are there importance of monetary tools in achieving the desired control through bank operations?

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Frequency** | **Percent** | **Valid****percent** | **Cumulative****percent** |
|  | Strongly Agree | 25 | 50 | 50 | 50 |
|  | Agree | 22 | 44 | 44 | 74 |
| Valid | Strongly Disagree | 10 | 20 | 20 | 94 |
|  | Disagree | 3 | 6 | 6 | 100.0 |
|  | Total | 50 | 100.0 | 100.0 |  |

**Source:** Field Survey, (2018)

From the above table majority strongly agreed that there are importances of monetary tools in achieving the desired control through bank operations whereas minority thought otherwise.

# Test of Hypothesis Hypothesis One

**H0:** monetary policy tools have an influence on the profit of commercial banks in Nigeria.

# Table 4.2.1: Testing of the 1st Hypothesis

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Respondent’s view** | **Oi** | **Ei** | **Oi-Ei** | **(Oi-Ei)2** | ∑**(Oi Ei) 2****Ei** |
| Strongly Agreed (SA) | 25 | 12.5 | 12.5 | 156.25 | 12.5 |
| Agree (A) | 10 | 12.5 | -2.5 | 6.25 | 0.5 |
| Strongly Disagreed (SD) | 9 | 12.5 | -3.5 | 12.25 | 0.98 |
| Disagreed (D) | 6 | 12.5 | -6.5 | 42.25 | 3.38 |
|  | **50** | **50** | **0** | **217** | **17.36** |

**Source:** Field Survey, (2018) Therefore X2 calculated = 17.36 X2 tabulated = 9.488

Decision Rule = Since X2 (calculated) is greater than 5% confident level, the null hypothesis is rejected and the alternative hypothesis which states that there is significant relationship between monetary policy tools and profit deposit and loans of commercial banks in Nigeria. is accepted.

# Discussion of Findings

From the above analysis, it is seen that in the Hypothesis tested, respondents agreed that there is a significant relationship between monetary policy and financial performance of Deposit Money bank in selected Banks in Nigeria .

Also in table 4.1.6, shows that 50% respondents strongly agreed that there is advantage to be derived from the implementation of monetary policy in financial institutions in Nigeria. 20% of the respondents agree while 18 of the respondents disagree.

# CHAPTER FIVE

**SUMMARY, CONCLUSIONS AND RECOMMENDATIONS**

# Summary

The general objective of this study was to determine the impact of quantitative tools of monetary policy on the performance of deposit of commercial banks in nigeria. Other specific objectives were to; establish the effect of Central Bank Rate (CBR) on the financial performance of commercial banks and establish the effect of Reserve Ratio Requirement on the financial performance of commercial banks.

A sample is a portion of the population selected for study. It is very important to select sample size that will give sufficient fair representation of the population. There are two basic way of making the sample size decision, one is by rule of thumb and the other one is by calculated method. In this research work, the rule of the thumb was used for this research where 50 workers of total population were selected as the sample size. The sample is also made up of senior and junior staff of Banks. This test will provide answers to the questions raised in the research problem. The questionnaires were administered based on the non-random selection of the persons as contained in the sample. This was done in such a way as to get the desired result. The questionnaire contains nineteen fifty (50) questions. . The formulated hypotheses were tested using chi-square (X2) test statistics which measures the significance of the difference between the observed set of frequencies.

The result of the analysis indicates that

# Conclusion

The study examined the effect of monetary policy tools on the financial performance of commercial banks in Nigeria. The study found that monetary policy tools have no significant effect

on the financial performance of commercial banks in Nigeria. Thus, the study concludes that monetary policy tools do not influence the financial performance of commercial banks in Nigeria.

The study assessed the effect of Treasury Bill Rate (T-Bill Rate) on the financial performance of commercial banks in Nigeria. The results showed that T-Bill Rate had a positive effect on the financial performance of commercial banks. Thus, the study concluded that T-Bill rates have a positive but insignificant affect the financial performance of commercial banks in Nigeria.

The study examined the effect of Central Bank Rate on the financial performance of commercial banks in Nigeria. The results showed that Central Bank Rate had a negative effect on the financial performance of commercial banks. The study therefore concluded that Central Bank Rate has no significant affect the financial performance of commercial banks in Nigeria.

The study also assessed the effect of Cash Reserve Ratio on the financial performance of commercial banks in Nigeria. The results showed that Cash Reserve Ratio had a negative effect on the financial performance of Union Bank. Thus, the study concluded that Cash Reserve Ratio does not affect the financial performance of commercial banks in Nigeria.

The study examined the effect of bank size on the financial performance of Union Bank of Nigeria. The results showed that bank size had a weak positive effect on the financial performance of commercial banks. Thus, the study concluded that bank size affects the financial performance of firms in Nigeria.

# Recommendations

Based on the findings made in this study, the following recommendations have been made to address some of the problems discovered:

1. The study recommends that commercial banks should put more emphasis on the internal factors to financial performance.
2. These internal factors include capital adequacy, asset quality, management efficiency, earnings ability and liquidity management.
3. Monetary policy tools effect will be handled by the management through risk management policies for the bank.
4. The study further recommends that while bank size was found to lead to better financial performance, it is important that banks understand the source of its funds and the costs associated with the funds.
5. Findings emanating from the empirical analysis of this study proffered that monetary authority; the Central Bank of Nigeria (CBN) should adjust the monetary policy rate by reducing the cash reserve ratio which will increase liquidity to enable the commercial banks to discharge their lending and investment duties effectively to the public.
6. It is important that monetary and fiscal policies be complimentary and not working at variance. The co-intergration tests which show a disquilibrium by 41% which suggest that the level of cohesion in harmonizing policies are not adequate. The CBN and the Ministry of finance should work more closely to objectively articulate policies in the same economic direction.
7. The CRR should be complementing the Open Market Operations (OMO) in ensuring that excess liquidity or lack of it in the banking system is minimized, that way Money Supply (M2) will be more effective as a tool on measuring other performance indicators.
8. From the findings, the Liquidity Reserve Ratio (LRR) tends to impact more on bank turnover ratio. Because monetary effects of CRR changes are hard to be isolated from those of other policy measures. It means that the constraint of higher reserve requirements on bank lending seems more binding when initial excess reserves shrink below some threshold, restraining the subsequent loan expansion while leading to higher, more volatile market interest rates. The CBN should carefully and thoroughly consider the turnover effect in deciding the LRR..

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# APPENDIX

# SECTION A

This is purely an academic exercise and every information contained, shall be treated as confidential. So respondents are employed to be truthful and sincere as possible.

1. Sex: Male [ ], Female [ ]

2. Age: 20 – 30 [ ], 31 – 40 [ ], 41 – above [ ]

1. Marital Statius: Single [ ], Married [ ]
2. Educational Qualification: OND/NCE [ ], H.N.D/B.Sc. [ ], MSC/MBA [ ], Others [ ] 5. Years of Experience: 0 – 5 [ ], 6 – 10 [ ], 11 – 15 [ ], 16 and above [ ]

# SECTION B

***Instruction:*** Please tick ( ) in the appropriate box to signify your choice of answer

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **S/N** | **ITEMS** | **SA** | **A** | **SD** | **D** |
| 1 | Is there any effect of monetary policy on the financialperformance of deposit money bank in Nigeria? |  |  |  |  |
| 2 | Does your deposit money bank protect the helplessdepositors? |  |  |  |  |
| 3 | Does deposit money bank put inflation into check? |  |  |  |  |
| 4 | Does Central Bank Rate (CBR) have effect on thefinancial performance of commercial banks in Nigeria? |  |  |  |  |
| 5 | Does deposit money bank create sustainable friendlybanking environment in Nigeria? |  |  |  |  |
| 6 | Does deposit money bank impose or prescribe penaltyon any defaulting financial institution? |  |  |  |  |

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| 7 | Does deposit money bank policy affect banking operations in its bid to regulate money supply in the economy with particular reference to deposit andcredit creation? |  |  |  |  |
| 8 | Does Reserve Ratio Requirement have effect on thefinancial performance of commercial banks in Nigeria? |  |  |  |  |
| 9 | Has central bank of Nigeria gone far in itsachievement of regulating money supply? |  |  |  |  |
| 10 | Do you think monetary policy has improved theindustries in Nigeria as a whole? |  |  |  |  |
| 11 | Is there any impact of exchange rate on theperformance of deposit money bank in Nigeria? |  |  |  |  |
| 12 | Are there importances of monetary tools in achievingthe desired control through bank operations? |  |  |  |  |