FINANCIAL INCLUSION AND MONETARY POLICY SHOCKS NEXUS IN NIGERIA: A NEW EMPIRICAL EVIDENCE

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Abstract

This paper empirically investigates the impact of monetary policy shocks on financial inclusion in Nigeria using the Vector Autoregression Model (VAR). Time series quarterly data were employed to conduct the analysis and the findings of the study reveal that shocks to minimum rediscount rate, interest rate, broad money supply and deposit rates of deposit banks all have significant impact on financial inclusion in Nigeria, however not at the same time and magnitude. Thus, the paper recommends the implementation of policies that will encourage innovations and competition in the banking industry. Also, there is need to adopt effective monetary policy measures that will increase financial inclusion in the country.

Contribution of the Study:
This is one of the pioneer papers that focused specifically on the impact of monetary policy shocks on financial inclusion in Nigeria using the Vector Autoregression Model (VAR). The paper makes some outstanding findings that can feed into monetary policy formulation in Nigeria. This is a major contribution to literature.

Keywords: Monetary Policy; Financial Inclusion; Shocks, Nigeria.
JEL Classification: E42, E51, E52, E58, G21, G23.

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1. BACKGROUND AND MOTIVATION

Recent discussions on monetary policy in Nigeria has been largely anchored on price stability and monetary targeting framework. This has also become the focus of monetary policy in recent times. This approach differs slightly from the earlier periods where the major focus of monetary policy was mainly on economic growth and employment. The special attention on price stability derives from new developments in monetary theories and empirical evidences which shows that sustainable growth can only be achieved when there is stability in the price level (CBN, 2017). Another issue that has also been a major concern to the monetary authorities is the relationship between monetary policy and financial inclusion.

The concept of financial inclusion has assumed greater level of importance in recent times due to its perceived usefulness in bridging the gap between the owners of investible funds and the users of such funds within the economy. Essentially, improving the mechanism through which access can be gained by hundreds of millions of men and women (all over the world) to relevant financial services and products would provide the possibilities for the creation of large depository of savings, investable funds, investment and therefore global wealth generation (CBN, 2014 and Anthony-Orji, Orji., Ogbuabor, and Nwosu 2019).

Mehrotra et al (2009), emphasized that access to financial services allows the poor to save money outside the house safely, and helps in mitigating the risks that the poor faces as a result of economic shocks. Hence, providing access to financial services is expected to have some far reaching social and economic implications. Again, the nexus between monetary policy and financial inclusion derives from the fact that to achieve economic prosperity in any nation, there is need for government to adopt monetary policy innovations and measures aimed at growing financial inclusion in such a country.

Prior to the recent effects to promote financial inclusion, the Nigerian economy was largely a cash-based economy with significant proportion of the narrow money stock in the form of currency outside the banking system. Although the average ratio of the currency outside the banking sector (COBs) to narrow money supply (M_1) tended downward from 61.1 percent in the 1960s to 44.3 percent in the 1970s and later to 40.9% in the 1980s, the value (in nominal terms) was still high considering the growth in the level of narrow money in the economy. This decline in the ratio was attributable to a combination of developments, including increased literacy rates and government policies directed towards encouraging financial sector growth. The CBN initiated the Rural Banking Programme directing banks to open branches in the rural areas, encouraging Nigerians to use financial institutions and their product more. In the 1990s the banking industry witnessed crisis which eroded the confidence of the populace in the industry. The problem was aggravated by the excessive spending of the political class leading to the increases in the level of currency outside the banking system. The ratio of the currency outside the bank system moved up to 47.7 percent by end of the 1990s. To forestall the damaging