Do financial stability and institutional quality have impact on financial inclusion in developing economies? A new evidence from Nigeria

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Abstract: This paper investigates the empirical linkages among financial stability, institutional quality and financial inclusion in Nigeria using quarterly data from 1986–2013. For empirical analysis, the study applies the autoregressive distributed lag model based on unrestricted error correction model (ARDL-UECM). First, the results show evidence that financial stability has significant impact on financial inclusion in the long run period but not in the short run. Second, the study reveals that institutional quality has significant impact on financial inclusion in the long run period and in the short run. Having found that financial stability and institutional quality are positively related to financial inclusion in the long run, the study therefore recommends that the government and policymakers pursuing the agenda of financial inclusion should pay attention not only to the financial and economic indicators but also to institutional factors existing in the country since they interact in creating a harmonised and sustainable developmental trajectory. In a country where the economic, legal, judicial and political institutions are very weak, many households (savers) and firms (borrowers/investors) may not be protected when there are issues of financial contract enforcements or breaches within the economy.

Keywords: financial stability; institutional quality; financial inclusion; autoregressive distributed lag; ARDL.

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1 Introduction

The issue of financial inclusion and financial stability has become a subject of debate in many developing countries' literature. Thus, following the Maya Declaration on financial inclusion which was launched in 2011 at the Global Policy Forum (GPF) in Riveria Maya, Mexico, the Federal Government of Nigeria in 2012, inaugurated the national financial inclusion strategy (NFIS) in Abuja in a bid to encourage financial inclusion in the country. Nigeria committed to financial inclusion development in the Maya Declaration and commitment was to develop and pursue a financial inclusion strategy that would reduce the adult financial exclusion rate from 46.3% in 2010 to 20% by 2020. According to the Central Bank of Nigeria (CBN, 2012), the National Financial Inclusion Strategy was launched with specific targets for financial products, including savings, payments, credit, insurance, and pensions, as well as commercial bank branches, microfinance bank branches, automated teller machines (ATMs), point of sale (POS)