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COMPETITION IN THE BANKING INDUSTRY: IMPLICATION ON FINANCIAL SECTOR DEVELOPMENT

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***Abstract**: The objective of this work is to examine the consequence or implication of competition in the banking industry for financial sector development. Whereas, competition is good for individual banks, the customers, and the banking system, excessive competition has implications which should be carefully identified and accorded the necessary regulatory attention. To examine the consequence or implication for financial sector development, a blend of exploratory, investigatory and descriptive technique was used. These methods were employed in order to capture the competition in the banking industry in Nigeria and its effects on financial sector development. Some of the implications identified to have direct bearing on the system's stability are related to supervision, risk management, corporate governance, market discipline, and self-regulation. Notwithstanding the enormous challenges posed by the keen competition in the industry as a result of consolidation, there is no doubt that the regulatory authority have been proactive and put in place policies to guarantee safety and soundness of the banking industry. The study concluded that the reforms introduced in the banking sector in the late 80's, raised the degree of competition and improved the level of efficiency of the Nigerian commercial banks.*

***Keywords:** Banking, Competition, Efficiency, Financial sector, Development.*

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Introduction

The banking industry plays an essential role in the economy in terms of resource mobilization and allocation and, is by far, the most important part of the financial system in developing economies, accounting for the bulk of the financial transactions and assets (Moyo, Nandwa, Odour and Simpasa, 2014). In addition, banks have recently expanded in other activities such as securities markets, fund management, insurance, among others, blurring the distinction between banks and other financial markets. Accordingly, it is expected that through reforms (increased competition), banks can potentially be the main source of financial innovation and efficiency or, in a worst case scenario, as a source of systemic risk to the financial structure through contagion, thus engendering macroeconomic instability and diminished investment and growth. The latter phenomenon was aptly evidenced by the recent global financial crisis which had its origin in excessive risk-taking behavior through the use of leveraged asset-price derivatives by financial institutions, mostly banks.

Notably, in developing countries, lack of well-developed domestic capital markets and access to international capital markets makes the banking sector ubiquitous and, therefore, any systemic bank failures would have serious contagious repercussions in such economies.

Competition in the financial sector matters for a number of reasons. As in other industries, the degree of competition in the financial sector matters for the efficiency of production of financial services, the quality of financial products and the degree of innovation in the sector. The view that competition in financial services is unambiguously good, however, is more naive than in other industries and vigorous rivalry may not be the first best. Specific to the financial sector is the effect of excessive competition on financial stability, long recognized in theoretical and empirical research and, most importantly, in the actual conduct of (prudential) policy towards banks. There are other complications, however, as well. It has been shown, theoretically and empirically, that the degree of competition in the financial sector can matter (negatively or positively) for the access of firms and households to financial services, in turn affecting overall economic growth.

In terms of the factors driving competition in the financial sector and the empirical measurement of competition, one needs to consider the standard industrial organization factors, such as entry/exit and contestability. But financial services provision also has many network properties, in their production (e.g., use of information networks), distribution (e.g., use of ATMs), and in their consumption (e.g., the large externalities of stock exchanges and the agglomeration effects in liquidity). This makes for complex competition structures since aspects such as the availability of networks used or the first mover advantage in introducing financial contracts become important.

Not only are many of the relationships and tradeoffs among competition, financial system performance, access to financing, stability, and finally growth, complex from a theoretical perspective, but empirical evidence on competition in the financial sector has been scarce and to the extent available often not (yet) clear. What is evident from

theory and empirics, however, is that these tradeoffs mean that it is not sufficient to analyze competitiveness from a narrow concept alone or focus on one effect only. One has to consider competition as part of a broad set of objectives, including financial sector efficiency, access to financial services for various segments of users, and systemic financial sector stability, and consider possible tradeoffs among these objectives. And since competition depends on several factors, one has to consider a broad set of policy tools when trying to increase competition in the financial sector.

Received evidence shows that in developing countries with transparent financial regimes where financial sector reforms have been implemented, competition in the banking industry has generally improved2 compared to countries characterized by less transparent financial sector regimes

(Ariss, 2010; Beck, Demirguc-Kunt, & Levine, 2009; Claessens & Laeven, 2004). For instance in the East African countries, studies have shown that financial sector reforms stimulated competitive pressures in the banking industry (Yildirim & Philippatos, 2007; Berger, Klapper, & Turk-Ariss, 2009; Mugume, 2007). The results are robust to entry of foreign banks and bank privatization (Čihák & Podpiera, 2005).

However, this evidence is not uniform. Other studies on SSA have reported limited effects of reforms on competition (Saab & Vacher, 2007; Buchs & Mathisen, 2005), with liberalization in some cases leading to financial crises (Fowowe, 2013). Less established, though, is the evidence on the relationship between financial liberalization (competition) and stability/fragility in the banking industry in these economies, particularly in SSA countries.

In all, this means that competition policy in the financial sector is quite complex and can be hard to analyze. Empirical research on competition in the financial sector is also still at an early stage. The evidence nevertheless shows that factors driving competition have been important aspects of recent financial sector improvements. To date, greater competition have been achieved by traditional means: removing entry barriers, liberalizing product restrictions, abolishing restrictive market definitions, eliminating intra-sectoral restrictions, etc. Making in this way financial systems more open and contestable, i.e., having low barriers to entry and exit, has generally led to greater product differentiation, lower cost of financial intermediation, more access to financial services, and enhanced stability. The evidence for these effects is fairly universal, from the US, EU and other developed countries to many developing countries. As globalization, technological improvements and de-regulation further progress, the gains of competition can be expected to become even more wide-spread across and within countries.

Conceptual framework

After more than two decades of financial repression, financial liberalization offered an opportunity for a revival of the Nigerian banking industry. As part of the broader economic reform package, financial reforms were in recognition that a well-functioning and competitive financial system is critical to the country's overall economic development. By 2005, the Central Bank of Nigeria embarked on Banking

Consolidation exercise, a widespread strategy aimed at strengthening financial sector infrastructure to enable it support sustainable economic growth. The implementation of the consolidation has helped address key bottlenecks in the financial system, including improving corporate governance of the banking sector, after the crisis of the pre 2004.

In 2008, the existing 25 banks were further pruned down to 17 through a rescue exercise by the central bank of Nigeria. Out of these, seven were first generation banks and others were new generation banks. Majority of these banks were instructed to divest from non-banking activities and this led to the provision of a unique feature of ownership, encompassing foreign financial equity stake, domestic private sector participation and public sector interest. Nonetheless, management rights reside with Nigerians. However, the Nigerian banking industry continues to exhibit a high level of concentration as very few banks dominate the financial landscape. In terms of assets and deposits, five largest banks accounted for sixty six percent between 2004 and 2013. The other banks captured the remaining one third. As per profitability, the two traditional profitability measures of ROA and ROC are employed. However, these measures alone are no longer adequate to measure banks profitability performance as they do not adequately meet the needs of stakeholders. Nigerian banks have been vibrant and generated earnings from loans, bonds and treasury bills.

The increase in the number of new entrants in the late 1990s lent credence to this view. The profitability level of most banks however nosedived between 1998 and 2011 due to a number of factors including, inadequate risk management capacity, ethical issues and poor corporate governance. ROA averaged about 6% for this period, the regulatory authority had to intervene to acquire the non-performing loans of these banks by 2009. At the same time, this performance led to acquisition of five distressed banks, at a time the whole industry also experienced a squeeze in earnings due to the global financial crisis.

To reinforce the Nigerian economy, the central bank of Nigeria announced a new 13-point reform agenda in mid-2004. Overall, the goal of this agenda is to promote soundness, stability and enhance international efficiency of the Nigerian banking industry. The highpoint of this reform is that all banks in the country should raise their minimum capital base to N25 billion, with a compliance deadline of 18 months. The efforts of banks to comply with this directive triggered merger and acquisitions. This also led to the increase of the share of the industry in the Nigeria Stock capitalization from 24% to 38% between 2004 and 2006. At this end of this deadline, 25 banks made it through out of which nine were first generation banks. (CBN, 2008).In spite of these positive developments, a new set of challenges merged in 2008 and threatened the financial system, coinciding with the global financial crisis

Effects of Competition in the Financial Sector

As a first-order effect, one expects increased competition in the financial sector to lead to lower costs and enhanced efficiency of financial intermediation, greater product innovation, and improved quality. Even though financial services have some special properties, the channels are similar to other industries. In a theoretical model, Besanko and Thakor (1992), for example, allowing for the fact that financial products are

heterogeneous, analyze the allocational consequences of relaxing entry barriers and find that equilibrium loan rates decline and deposit interest rates increase, even when allowing for differentiated competition. In turn, by lowering the costs of financial intermediation, and thus lowering the cost of capital for non-financial firms, more competitive banking systems lead to higher growth rates. Of course, they are not just efficiency and costs, but also the incentives of institutions and markets to innovate that are likely affected by the degree of competition.

Access to Financial Services

As a first-order effect, greater development, lower costs, enhanced efficiency, and a greater and wider supply resulting from competition will lead to greater access. The relationships between competition and banking system performance in terms of access to financing are more complex, however. The theoretical literature has analyzed how access can depend on the franchise value of financial institutions and how the general degree of competition can negatively or positively affect access. Market power in banking, for example, may, to a degree, be beneficial for access to financing (Petersen and Rajan, 1995). With too much competition, banks may be less inclined to invest in relationship lending (Rajan, 1992). At the same time, because of hold-up problems, too little competition may tie borrowers too much to an individual institution, making the borrower less willing to enter a relationship (Petersen and Rajan, 1994; and Boot and Thakor, 2000). More competition can then, even with relationship lending, lead to more access. The quality of information can interact with the size and structure of the financial system to affect the degree of access to financial services. Financial system consolidation can lead to a greater distance and thereby to less lending to more opaque firms such as SMEs.

Theory has shown some other complications. Some have highlighted that competition is partly endogenous as financial institutions invest in technology and relationships (e.g., Hauswald and Marguez, 2003). Theory has also shown that technological progress lowering production or distribution costs for financial services providers does not necessarily lead to more or better access to finance. Models often end up with ambiguous effects of technological innovations, access to information, and the dynamic pattern of entry and exit on competition, access, stability and efficiency (e.g., Dell'Ariccia and Marquez, 2004, and Marquez, 2002). Increased competition can, for example, lead to more access, but also to weaker lending standards, as observed recently in the sub-prime lending market in the US (Dell'Ariccia, Laeven and Igan, 2008) but also in other episodes.

These effects are further complicated by the fact that network effects exist in many aspects of supply, demand or distribution of financial services. In financial services production, much used is made of information networks (e.g., credit bureaus). In distribution, networks are also extensively used (e.g., use of ATMs). Furthermore, in their consumption, many financial services display network properties (e.g., liquidity in stock exchanges). As for other network industries, this makes competition complex (see further Ausubel, 1991, and Claessens, Dobos, Klingebiel and Laeven, 2003).

Stability

The relationships between competition and stability are also not obvious. Many academics and especially policy makers have stressed the importance of franchise value for banks in maintaining incentives for prudent behavior. This in turn has led banking regulators to carefully balance entry and exit. Licensing, for example, is in part used as a prudential policy, but often with little regard for its impact on competition. This has often been a static view, however, Perotti and Suarez (2002) show in a formal model that the behavior of banks today will be affected by both current and future market structure and the degree to which authorities will allow for a contestable, i.e., open, system in the future. In such a dynamic model, current concentration does not necessarily reduce risky lending, but an expected increase in future market concentration can make banks choose to pursue safer lending today. More generally, there may not be a tradeoff between stability and increased competition as shown among others by Allen and Gale (2004), Boyd and De Nicolò (2005) and reviewed recently by Allen and Gale (2007). Allen and Gale (2004) furthermore show that financial crises, possibly related to the degree of competition, are not necessarily harmful for growth.

Theory of the Determinants of Competition

In terms of empirical measurement and associated factors driving competition one can consider three types of approaches: market structure and associated indicators; contestability and regulatory indicators to gauge contestability; and formal competition measures. Much attention in policy context and empirical tests is given to market structure and the actual degree of entry and exit in particular markets as determining the degree of competition. The general Structure-Conduct-Performance (SCP) paradigm, the dominant paradigm in industrial organization from 1950 till the 1970s, made links between structure and performance. Structure refers to market structure defined mainly by the concentration in the market. Conduct refers to the behavior of firms – competitive or collusive – in various dimensions (pricing, R&D, advertising, production, choice of technology, entry barriers, predation, etc.). And Performance refers to (social) efficiency, mainly defined by extent of market power, with greater market power implying lower efficiency. The paradigm was based on the hypotheses that i) Structure influences Conduct (e.g., lower concentration leads to more competitive the behavior of firms); ii) Conduct influences Performance (e.g., more competitive behavior leads to less market power and greater social efficiency). And iii) Structure therefore influences Performance (e.g., lower concentration leads to lower market power)

Theoretically and empirically there are a number of problems with the SCP-paradigm and its implications that, directly and indirectly, structure determines performance. For one, structure is not (necessarily) exogenous since market structure itself is affected by firms' conduct and hence by performance. Another conceptual problem is that industries with rapid technological innovation and much creative destruction, likely the financial sector, may have high concentration and market power, but this is necessary to compensate these firms for their innovation and investment and does not mean reduced social welfare.

Most importantly, and different from the SCP-paradigm, the more general competition and contestability theory suggests that market structure and actual degree of entry or exit are not necessarily the most important factors in determining competition. The degree of contestability, that is, the degree of absence of entry and exit barriers, rather than actual entry, matters for competitiveness (Baumol, Panzar, and Willig, 1982). Contestable markets are characterized by operating under the threat of entry. If a firm in a market with no entry or exit barriers raises its prices above marginal cost and begins to earn abnormal profits, potential rivals will enter the market to take advantage of these profits. When the incumbent firm(s) responds by returning prices to levels consistent with normal profits, the new firms will exit. In this manner, even a single-firm market can show highly competitive behavior.

The theory of contestable markets has also drawn attention to the fact that there are several sets of conditions that can yield competitive outcomes, with competitive outcomes possible even in concentrated systems since it does not mean that the firm is harming consumers by earning super-normal profits. On the other hand, collusive actions can be sustained even in the presence of many firms. The applicability of the contestability theory to specific situations can vary, however, particularly as there are very few markets which are completely free of sunk costs and entry and exit barriers. Financial sector specific theory adds to this some specific considerations.

While the threat of entry or exit can also be an important determinant of the behavior of financial market participants, issues such as information asymmetries, investment in relationships, the role of technology, networks, prudential concerns, and other factors can matter as well for determining the effective degree of competition (see further Bikker and Spierdijk, 2008).

Empirical framework

Erol, et al (2012) carried out an empirical assessment of the market structure and the competitiveness of the Chinese banking sector particularly in the wake of China's accession to the WTO by employing the Panzar-Rosse H-Statistic as a non-structural model over the period 2004-2007. The empirical findings indicate that the banking sector in China was monopolistically competitive for the specified period. They also find that the Chinese banks, which operate in more monopolistic environments, are less efficient. The findings reject the state of conjectural variation short run oligopoly or natural monopoly in the industry for the period under consideration.

Casu and Girardone (2007) investigated the impact of increased consolidation on the competitive conditions of EU banking markets by employ both structural (concentration ratios) and non-structural (PanzarRosse statistic) concentration measures. Using bank level balance sheet data for the major EU banking markets, in a period following the introduction of the Single Banking License (1997-2003), the results seem to suggest that the degree of concentration is not necessarily related to the degree of competition. They equally found little evidence that more efficient banking systems are also more competitive. The relationship between competition and efficiency is not a straightforward one. Increased competition has forced banks to become more efficient but increased efficiency is not resulting in more competitive EU banking systems.

Bikker and Haaf (2002) investigated the relationship between competition and market structure in the banking industry for all banks in their sample and estimate a regression model where competition measure is tested against market structure (proxied by concentration indices and the log of the number of banks in the markets) and a dummy for EU/non-EU countries. Overall, they find support for the conventional view that concentration impairs competitiveness.

The general contestability literature has suggested specific ways on how to go about testing for the degree of competition. Klein (1971), Baumol, Panzar, and Willig (1982) were the first to develop a formal theory of contestable markets. They draw attention to the fact that there are several sets of conditions that can yield competitive outcomes, even in concentrated systems.

Conversely, they showed that collusive actions could be sustained even in the presence of many firms. Their work has spanned a large empirical literature covering many industries.

Two types of empirical tests for competition can be distinguished since they have been applied to financial sector (and other industries). The model of Bresnahan (1982) and Lau (1982), as expanded in Bresnahan (1989), uses the condition of general market equilibrium. The basic idea is that profit- maximizing firms in equilibrium will choose prices and quantities such that marginal costs equal their (perceived) marginal revenue, which coincides with the demand price under perfect competition or with the industry's marginal revenue under perfect collusion.

The alternative approach is Rosse and Panzar (1977), expanded by Panzar and Rosse (1982) and Panzar and Rosse (1987). This methodology uses firm (or bank)- level data. It investigates the extent to which a change in factor input prices is reflected in (equilibrium) revenues earned by a specific bank. Under perfect competition, an increase in input prices raises both marginal costs and total revenues by the same amount as the rise in costs. Under a monopoly, an increase in input prices will increase marginal costs, reduce equilibrium output and, consequently, reduce total revenues.

Buchs and Mathisen (2005) examined the degree of bank competition and efficiency with regard to banks' financial intermediation in Ghana. In the study they applied panel data to variables derived from a theoretical model and find support for the presence of a noncompetitive market structure in the Ghanaian banking system, possibly hampering financial intermediation.

Weill (2004) investigated the relationship between competition and X-efficiency using stochastic frontier method. The study regressed efficiency scores on competition measure and a set of independent variables including: macro factors (GDP per capita and density of demand); an intermediation ratio (loans/deposits) and finally a dummy that corresponds to the geographical location. The author finds evidence of a negative relationship between competition and efficiency in EU banking.

Ajisafe and Akinlo (2014) examined the relationship between bank competition and efficiency in Nigeria for period of 1990-2009 using pooled least square and dynamic panel generalized method of moment estimation techniques with fixed effect for the

data collected for fifteen selected banks in Nigeria. The result of the study showed that there was a positive and significant relationship between the degree of competition and efficiency of commercial banks in Nigeria.

Bashorun and Ojapinwa (2014) investigated the effect of bank consolidation in Nigeria on the structural characteristics of the banking market. They established that there is substantial increase in concentration for the post consolidation period with very high tendency to gravitate towards becoming a moderately concentrated market according to the USA merger guideline. Also, there is the emergence in 2012, of eight top dominant banks controlling more than 75% of the Nigerian banking business especially in the total assets market. The implication of this finding is that there is the need to forestall collusive and anti-competitive practices by stepping up the oversight functions of the regulatory and supervisory agencies while reviewing periodically the hurdles for new entrants to the industry.

A number of papers have applied either the Breshnahan or the PR methodology to the issue of competition in the financial sector, although mostly specific to the banking system.

One of the first papers using the Breshnahan methodology for banks is Shaffer (1989). He applies the methodology to a sample of U.S. banks and finds results that strongly reject collusive conduct but are consistent with perfect competition. Using the same model, Shaffer (1993) studies the competition conditions in Canada and finds that the Canadian banking system was competitive over the period 1965-1989 although being relatively concentrated. He also finds that the degree of competition in Canada was generally stable following regulatory changes in 1980. Gruben and McComb (forthcoming) applied the Breshnahan methodology to Mexico before 1995 and find that the Mexican banking system was super-competitive; that is, marginal prices were set below marginal costs. One of the few studies that uses the Breshnahan model with a relatively large sample of countries is Shaffer (2001). For 15 countries in North America, Europe, and Asia during 1979-91, he finds significant market power in five markets and excess capacity in one market. Estimates were consistent with either contestability or Cournot type oligopoly in most of these countries, while five countries were significantly more competitive than Cournot. Since the data refer to the period befo re the European single banking license was adopted, the result may, however, not be reflective of the current situation. Shaffer (1982) was also one of the first to apply the PR model to banks. He estimated it for New York banks using data for 1979 and found monopolistic competition. Nathan and Neave (1989) study Canadian banks using the PR methodology. The results for Canada also reject monopoly power for the Canadian banking system. Some other studies have applied the PR methodology to some non-North America and non-European banking systems. For Japan, for example, Molyneux, Thornton and Lloyd-Williams (1996) find evidence of a monopoly situation in 1986 1988.

A number of papers have applied the PR methodology to European banking systems. These papers include Molyneux, Lloyd-Williams, and Thornton (1994), Vesala (1995), Molyneux, Thornton and Lloyd-Williams (1996), Coccorese (1998), Bikker and Groeneveld (2000), Bikker and Haaf (2001), De Bandt and Davis (2000) and Hempel

(2002). The countries covered, the time periods and some of the assumptions used vary between the studies. Although the findings varied somewhat, generally, the papers can reject both perfect collusion as well as perfect competition and mostly find evidence of monopolistic competition. (Bikker and Haaf (2001) summarize the results of some ten studies.) Bikker and Groeneveld (2000), for example, find monopolistic competition in all of the 15 EU-countries they study.

To date, tests on the competitiveness of banking systems for developing countries and transition economies using these models are few. Using the PR-approach, Belaisch (2003) finds evidence of a non- monopolistic market structure in Brazil.

Gelos and Roldos (2002) analyze a number of banking markets using the PR-methodology, including some developing countries. They report that overall banking markets in their sample of eight European and Latin American countries have not become less competitive although concentration has increased. They conclude that lowered barriers to entry, such as allowing increased entry by foreign banks, appeared to have prevented a decline in competitive pressures associated with consolidation.

Levy, Yeyati and Micco (2003) find similar results using the PR-methodology for their sample of Latin America countries and find that the process of consolidation in the 1990s, if anything, may have led to more, rather than less, competition.

Philippatos and Yildirim (2002) investigate 14 Central and Eastern European banking systems using bank-level data and the PR-methodology. They find, except for Latvia, Macedonia, and Lithuania, that these banking systems can neither be characterized as perfectly competitive nor monopolistic. They also conclude that large banks in transition economies operate in a relatively more competitive environment compared to small banks.

Methodology

Generally, secondary data were used in this work. These data were time series and cross section. The data reflected the Capital/assets (%), Liquid & trading assets/total short-term funding (%),Gross bad debt ratio (%), Net interest margin (%), Cost ratio (%) , ROE (%), ROA (%)of selected commercial banks in Nigeria The data were sourced and extracted from existing documents and materials. These include the Central Bank of Nigeria (CBN) statistical Bulletin, CBN Annual Report and Statement of Account, CBN Bullion, National Insurance Commission (NAICOM) Annual Reports, text books, journals, and internet sources, among others.

The data collected for this work were presented in tables indicating the series of observations, the trend and movement of the variables studied. Percentages (%ages), diagram and ratios were computed to analyze the characteristic trend of competition in the banking industry. These tools made it possible to carry out empirical analysis describing the trend in Capital/assets (%), Liquid & trading assets/total short-term funding (%), Gross bad debt ratio (%), Net interest margin (%), Cost ratio (%), ROE (%), ROA (%) of selected commercial banks in Nigeria. Thus, the tools used in the article were descriptive and inferential in nature.

Empirical details and analysis

The main focus of this work is to examine competition in the banking sector and its implication on financial sector development in Nigeria. As part of the broader economic reform package, financial reforms were in recognition that a well-functioning and competitive financial system is critical to the country's overall economic development. Therefore, this section is set aside to present and analyze the data on the key variables examined in the article including Capital/assets (%), Liquid & trading assets/total short-term funding (%), Gross bad debt ratio (%), Net interest margin (%), Cost ratio (%), ROE (%), ROA (%) of selected commercial banks in Nigeria.

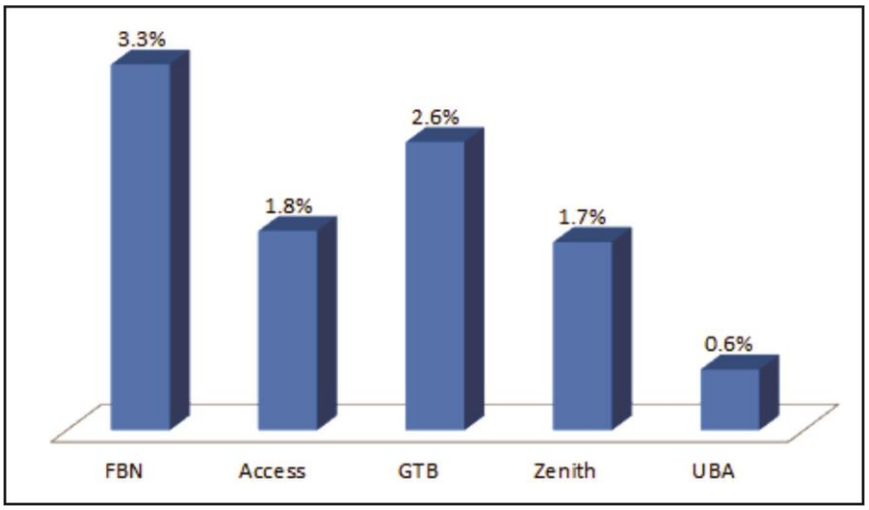
Table 1: Selected ratios of some commercial banks in Nigeria

Selected banks	First Bank	Zenith	UBA	Access	GT Bank
Year end 31 December 2012					
Capital (N'bn)	394.5	463.0	192.5	240.3	283.4
Total assets (N'bn)	3,079.8	2,566.1	2,260.2	1719.9	1,688.7
Net loans (N'bn)	1,563.0	989.8	687.4	608.6	783.9
Total comprehensive income (N'bn)	94.4	98.5	55.5	35.1	86.4
Capital/assets (%)	12.8	18.0	8.5	14.0	16.8
Liquid & trading assets/total short-term funding (%)	29.8	49.5	33.0	27.8	46.5
Gross bad debt ratio (%)	2.6	3.1	1.9	5.3	3.3
Net interest margin (%)	10.0	8.6	9.4	11.3	10.3
Cost ratio (%)	65.0	52.4	64.5	61.1	42.6
ROE (%)	24.5	23.0	32.3	16.2	33.6
ROA (%)	3.2	4.1	2.7	2.1	5.3

Source: Nigeria Bank Credit Rating Report (2013)

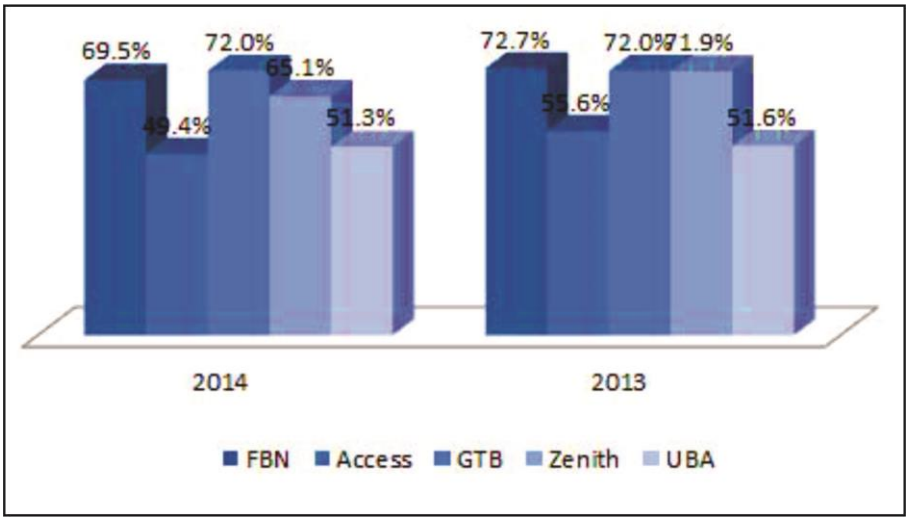
A care examination on the table above proved that there is a keen competition among the banks. In 2012, Zenith bank have N463b capital while first bank, UBA, Access and GT bank have a capital of N394.5b, N192.5b,N 240.3b and N283.4b respectively. Looking at the income of the banks under review, Zenith bank maintains the lead with N98.5b followed by first bank with N94.4b, GT bank N86.4b, UBA N55.5b and Access with N35.1b. The competition in the sector also reflects in the banks' returns on equity and assets. A close look at the table shows that there was a close margin in the returns of the banks. Return on equity was 24.5%, 23.0%, 32.3%, 16.2% and 33.6% for First Bank, Zenith, UBA, Access and GT Bank respectively. In the same manner return on assets shows 3.2%, 4.1%, 2.7%, 2.1%, and 5.3% for First Bank, Zenith, UBA, Access and GT Bank respectively. The information provided in the table above proved that there is actually a competition among the banks. Below are charts showing different indications of competition in different areas of the banks operations.

***Figure 1**: Non-performing loans to gross loans FY2014*



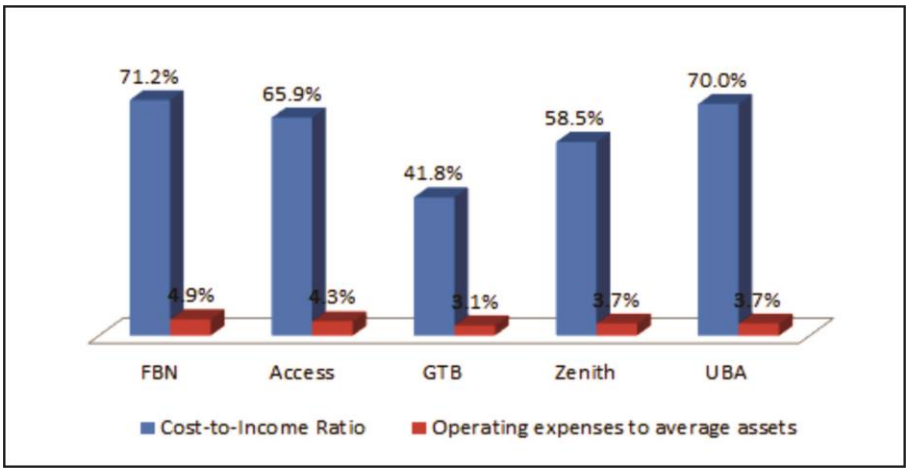
Source: Agusto& Co. (2015)

***Figure 2**: Net interest margin (FY2014)*



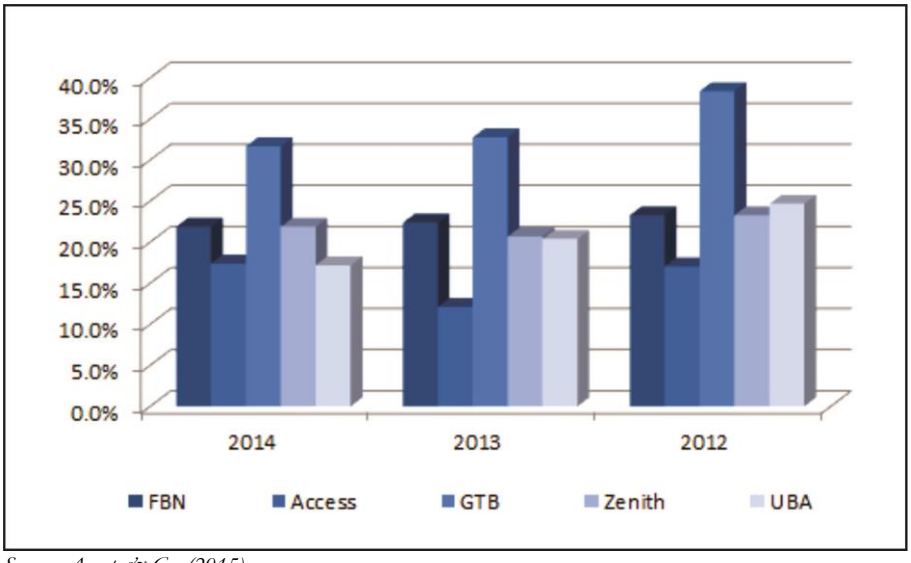
Source: Agusto& Co. (2015)

Figure: *Efficiency ratios (FY2014)*



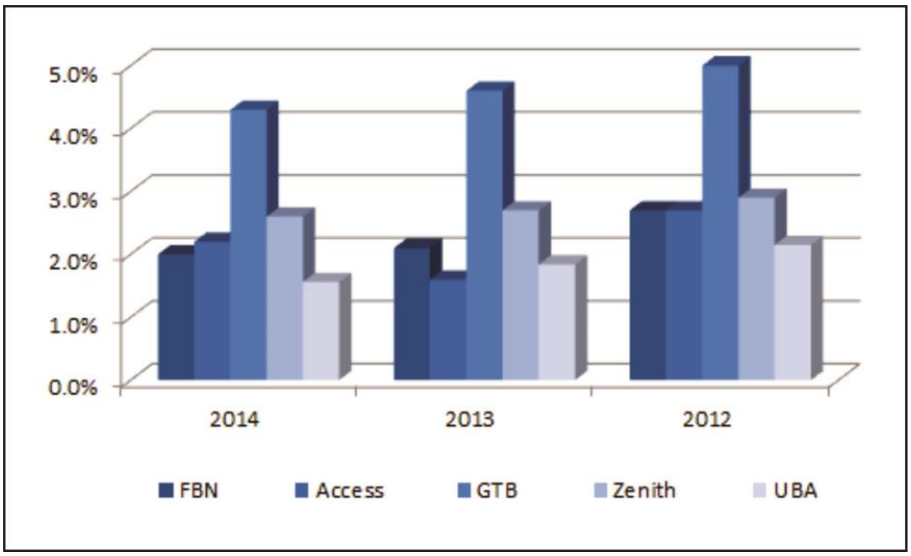
Source: Agusto& Co. (2015)

Figure 4*: Pre- tax return on average equity (ROE) FY2014*



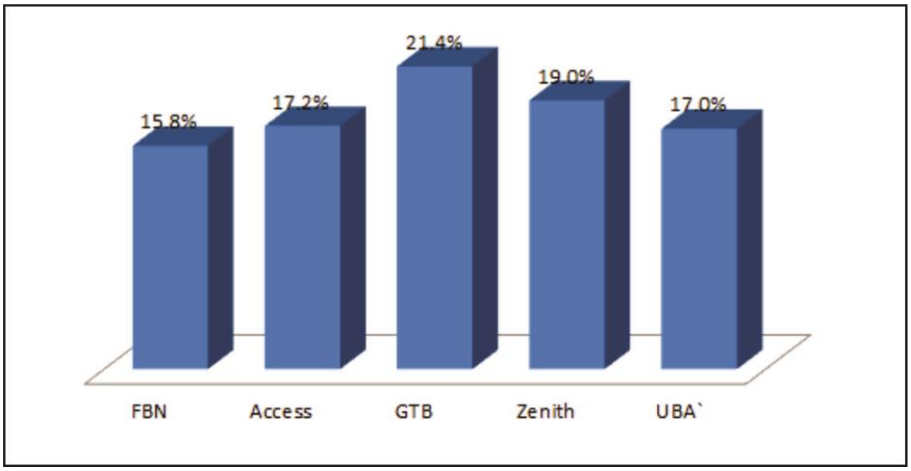
Source: Agusto& Co. (2015)

***Figure 5**: Pre-tax return on average assets (ROA) FY2014*



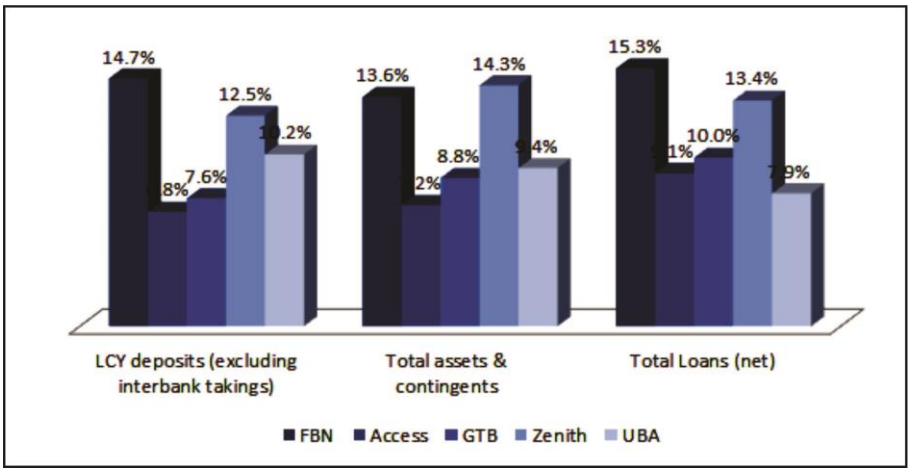
Source: Agusto & Co. (2015)

***Figure 6**: Basel II capital adequacy ratios (FY2014)*



Source: Agusto& Co. (2015)

***Figure 7**: Market share (FY2014)*



Source: Agusto & Co. (2015)

Discussion and conclusions

Discussion

Whereas, competition is good for individual banks, the customers, and the banking system, increased competition has implications which should be carefully identified and accorded the necessary attention. In a broad sense, some of the implications of increased competition in the banking industry which have direct bearing on the system's stability include the following, among others:

- Effective supervision;
- Effective risk management;
- Strong corporate governance;
- Market discipline;
- Self-regulation.

Effective Supervision

The current supervisory approach in Nigeria which is transaction- and compliance- and is narrow in scope and uniformly applied to all supervised institutions. With consolidation, there is the need to adopt a robust, proactive and sophisticated supervisory process that should essentially be based on risk profiling of the emerging big banks. In other words, the adoption of an appropriate risk-based supervisory approach is imperative with consolidation. The approach entails the design of a

customized supervisory programme for each bank and it should focus more attention on banks that are considered to have potentially high systemic impact. The approach should enable the supervisory authorities to optimize the utilization of supervisory resources. That necessarily requires that supervisors should have a clear understanding of the risk profile of the emerging big, and sometimes, complex banks. There is therefore, the need for capacity building – in this area.

Effective Risk Management Systems

Although effective risk management has always been central to safe and sound banking practices, it has become even more important in the post consolidation banking era than hitherto as a result of the on-going bank consolidation programme. It is important to indicate that the ability of a bank to identity, measure, monitor and control risks under the emerging banking environment can make the critical difference between its survival and collapse. For a bank to efficiently and effectively play its role under the emerging dispensation therefore, the deployment of an effective risk- management system with the following key elements is imperative:

- Active board and senior management oversight;
- Adequate risk-management policies, procedures and exposure limits;
- Effective risk identification, measurement, monitoring and control framework;
- Comprehensive management information system; and Efficient internal controls.

Strong Corporate Governance

While good corporate governance has remained imperative in the banking system, its importance in our nation's emerging banking environment is based on the fact that managements of most of the 'new' banks would be insulated from abusive ownership. Besides, there are many other stakeholders with goals, interests and expectations that do not necessarily coincide, and as a result, they constitute major areas of frictions. Corporate governance is about building credibility, ensuring transparency and accountability as well as maintaining an effective channel of information disclosure that would foster good corporate performance. It is also about how to build trust and sustain confidence among the various interest groups that make up an organization. Disclosure and transparency are key pillars of a corporate governance framework, because they provide all the stakeholders with the information necessary to judge whether or not their interests are being served.

Market Discipline

The current information disclosure requirements in the industry are grossly inadequate to effectively bridge the information asymmetry between banks and investing public that consolidation has inevitably created. Under the consolidated banking environment,

it is important that the accounting as well as disclosure requirements of the consolidated banks be reviewed. This has become necessary to ensure that business decisions by the investing public are well informed under the new dispensation. Adequate information disclosure requirement will make banks to pay greater attention to reputational risk that could result in loss of confidence as well as patronage.

Self-Regulation and Self-Discipline

This development has become necessary in view of the realization that self-regulation and self-discipline are critical to the promotion of a sound, transparent, accountable and efficient I financial market. Effective self-regulation requires probity, transparency and accountability, which are yet to be fully entrenched in the system. Necessary steps should be taken by the regulatory/supervisory authorities to encourage these virtues and operators also needs to comply with rules and regulations to promote healthy competition since self-regulation does not amount to elimination of regulatory controls and supervision.

Conclusion

In this paper, an attempt has been made to discuss the competition the banking industry and its implication on financial sector development in Nigeria. In the main, some of these implications identified to have direct bearing on the system's stability are related to supervision, risk management, corporate governance, market discipline, and self- regulation. Notwithstanding the enormous challenges posed by the keen competition in the industry as a result of consolidation, there is no doubt that the regulatory authority have been proactive and put in place policies to guarantee safety and soundness of the banking industry .

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