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LENDING RATE AND FINANCIAL PERFORMANCE OF DEPOSIT MONEY BANKS IN NIGERIA (2008 – 2021)

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ABSTRACT

The study examined the effects of lending rates on banks' financial performance of Deposit Money Banks in Nigeria. Three deposit money banks listed on the Nigeria stock exchange between 2008 and 2021 were selected for this study. The lending rate was measured using CBN lending rates while banks' performance was measured with Profit After Tax, Return on Assets and Return on Equity. Three hypotheses were formulated based on the three performance variables and the models were estimated using Panel Least Square Regressing technique. Findings revealed that lending rate has a positive and significant effect on three banks' financial performance indexes. The study therefore recommends that the government should also make such monetary policies that will increase the profitability of banks.

Keywords: Deposit Rate, Financial Performance, Deposit Money Bank.

INTRODUCTION

Background of the Study

Determining a suitable interest rate is essential to attaining greater performance and fostering the growth of the banking industry. This is because when interest rates are high, the cost of borrowing money rises, which in turn slows down domestic investment, reduces aggregate demand, boosts unemployment, and slows down economic development. If the Nigeria banks and Nigeria economy must perform very effectively, the lending rate must be very fourable(Efanga, Hanson, Umoh&Umoh, 2020). The high lending rate from Nigeria banks has been a major concern to private sector businesses as they are unable to borrow at this high lending rate for production activities and still remain competitive. On the other hand, interest paid to depositors has been relatively low in Nigeria over the years resulting in a large spread between lending rates and deposits rate (Owusu-Antwi, Banerjee, &Antwi, 2017).

Money deposit banks would be interested in giving out loans and advances to their numerous customers bearing in mind that this will be the only way of increasing their interest income thus improving their profitability and performance. It is widely believed that fluctuations of market lending rates are a significant influence on the performance of money deposit banks. According to Samuelson (1945), under general conditions, bank performance increase with increase in profits and lending rates.He argued that the banking system as a whole is immeasurably helped rather than hindered by an increase in lending rates.The fact that banks serve as intermediaries in the process of resource mobilization and allocation is reflective of the fact that made to customers who borrow money from them. The need to enhance financial

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performance of the banks necessitated interest rate charges on loans. Financial performance is the measure of how well a bank can use its assets from its primary business to generate revenues. It can be measured by Return on Investment (ROI), Residual Income (RI), Earning Per Share (EPS), dividend yield, Return on Assets (ROA), growth in sales, Return on Equity (ROE) etc (Stanford, 2019).

The financial performance of deposit money banks is highly impacted by the interest spread, which is defined as the difference between lending and deposit rates. This is particularly true in terms of profitability. As a consequence of this, the interest rate is recognized as a crucial factor that contributes to the continued existence and successful operation of deposit money banks (Okoye&Eze, 2020;Ali-Momoh&Fajuyagbe, 2022). Deposit money banks also increased their lending rates in the business environment and to other borrowers. This resulted in fewer loans and advances and decreased the quantity of money in circulation throughout the economy. Individuals, businesses, and industries have been dissuaded from taking loans and advances as a direct result of the high interest rate, which has resulted in less money in circulation, a decrease in credit, and a fall in prices. Based on the above, this work focused on lending rate and financial performance of deposit money banks in Nigeria (2008 – 2021).

Statement of the Problem

Deposit money banks are always interested in interest rates by giving out loans and advances to their numerous customers. In this case, deposit money banks' decisions to lend out loans is basically influenced by the prevailing interest rate. However, deposit money banks in Nigeria were forced to restrict their borrowing after the Central Bank of Nigeria made the decision to raise the interest rate that banks pay to borrow money(Hassan, 2016). As a result, deposit money banks in Nigeria experienced a significant decline in both their overall operations and financial performance. This resulted in fewer loans and advances and decreased the quantity of money in circulation throughout the economy. Individuals, businesses, and industries have been dissuaded from taking loans and advances as a direct result of the high interest rate, which has resulted in less money in circulation, a decrease in credit, and a fall in prices (Akinwale, 2018).

As a consequence of this, deposit money banks are unable to create revenues related with borrowings, loans, and advances, which therefore has an effect on the financial performance of these banks(Hassan, 2016). The extent to which this has affected the financial performances of tier one banks in Nigeria is the focus of this study.

Objective of the Study

The general objectives of this study focused on lending rate and financial performance of deposit money banks in Nigeria (2008 – 2021).Specifically, the study is designed to:

1. evaluate the effect of lending rates on profit after tax of DMBs.
2. examine the effect of lending rates on return on asset of DMBs and

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3. evaluate the relationship between lending rates and return on equity of DMBs.

Based on the objective of the study, the following research questions were formulated to guide the study:

1. What is the effect of lending rates on profit after tax of DMBs?
2. To what extent has lending rates affected return on asset of DMBs?
3. What is the relationship betweenlending ratesand return on equity of DMBs?

In view of the above research questions and objectives, the following hypotheses were formulated to guide the study:

H_{o1}: There is no significant effect of lending rates on profit after tax of DMBs.
Ho_2: Lending rates has no significant effect on return on assets of DMBs.
Ho_3: There is no significant relationship between lending rates and return on equity of DMBs.

REVIEW OF RELATED LITERATURE

This section is organized under conceptual review, theoretical and empirical.

Conceptual Review

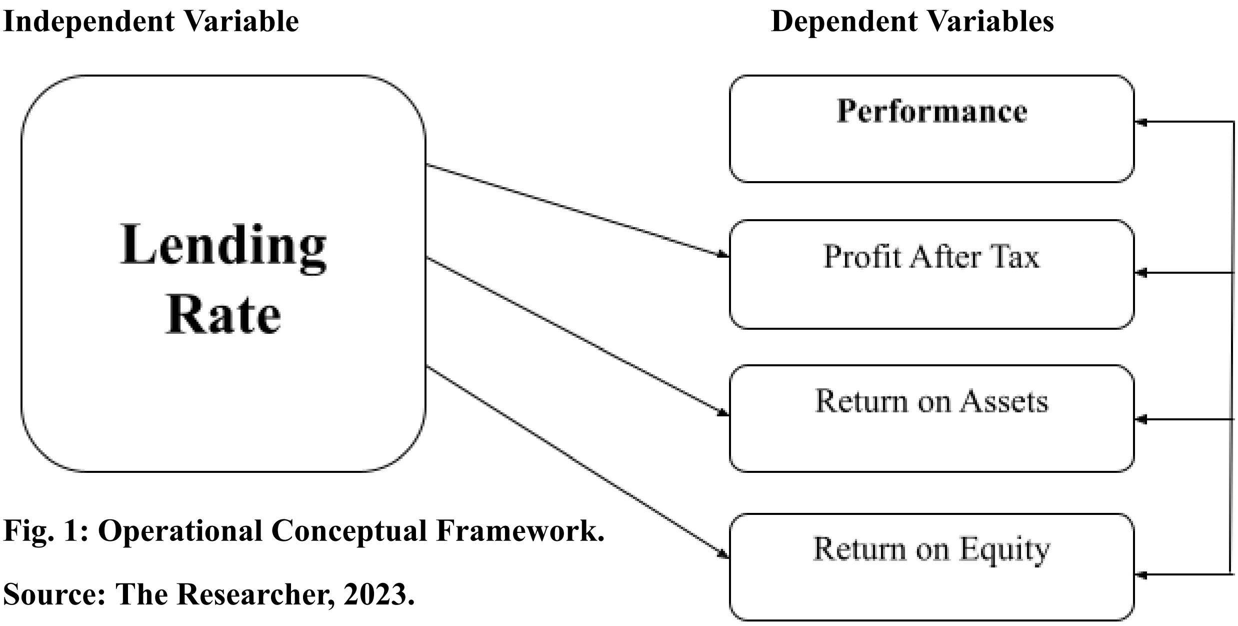

Fig. 1: Operational Conceptual Framework.

Source: The Researcher, 2023.

Interest Rate

Interest rate is the price a borrower pays for the use of money they borrow from a lender or fee paid on borrowed assets. Ngugi (2011) described interest rate as a price of money that reflects market information regarding expected change in the purchasing power of money or future inflation. Interest rates are important because they control the flow of money in the economy. High interest rates curb inflation but also slow down the economy. Low interest rates stimulate the economy, but could lead to inflation. In Nigeria, the increases in the

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nominal interest rate and inflation rate intensify the aggregate rates of failure or default of firms (Davis, 1995). Khan and Mahmood (2013) showed that the financial structure of some industries makes firms in that industry more susceptible to interest rate volatilities than others. The return or yield on equity, as well as the opportunity cost of delaying the use of money in the present in favour of a time in the future, are both components of the interest rate. The term "interest rate" refers to the sum of three separate rates: the loan rate, the saving rate, and the discount rate.

The price of credit, which is also known as the interest rate, is established by the competing forces of demand for and supply of loanable money in any given economy (Victor &Eze, 2013). The cost of taking out a loan or the return you get for keeping your money in the bank is both represented by an interest rate. It is determined as a percentage of the total money that is either borrowed or saved for a period of one year, or for any other length of time that the lender and the borrower agree upon at the time that the loan is contracted. To be more specific, the interest rate is the proportion of the principal that is paid as a fee over a certain amount of time. This charge is referred to as the "interest." It is also possible to think of it as the rental payments made by borrowers in exchange for the use of credit, and the return that lenders get for parting with their liquidity over time (Dhungana, 2016). In addition, interest rates may either be represented in nominal or real terms, depending on whether or not adjustments to the general level of prices (also known as inflation) are included into the calculations of either kind of rate.

In the event that the interest rate is not adjusted for inflation, the rate will be presented in nominal terms. A rate of interest that does not take inflation into account is referred to as a nominal interest rate (Owolabi, 2014). This is because inflation has a depressing effect on the purchasing power of the lender, which means that the lender will not be able to purchase the same quantity of goods or services with the money realized at payoff or maturity of the loan or investment in comparison to the time when they were secured (Ogunbiyi&Ihejirika, 2014)

Lending rates

Lending rate by money deposit banks determines the profitability and performance of banks among other factors (Gardner & Cooperman, 2018). High Lending interest rates have remained a macroeconomic problem that has been tricky to eliminate and thus hindering economic development. Banks play a critical role in the economic growth and development of the country, so, to uphold the economic growth of the country the banking sector must perform its task properly. Bold (2016) argued that lending rate spread remains a controversial area while some link it to market or individual banks inefficiency. There are other variables which are always being overlooked or not talked about like Cash Reserve Ratio (CRR), Monetary Policy Ratio (MPR), Total Deposit (TD) etc which contributed to the performance of the bank. Also, the ability of any bank to deliver credit to the real sector depends on a number of factors, the banks' operating in an inclusive environment, the operating business environment of most Nigerian banks has been identified as 'very harsh' and therefore very

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unfriendly (Beck &Hesse, 2016). These problems have been worsened by different forms of security challenges at almost every part of the country.

More so, most of the banks' capital base is so poor and the capital adequacy of a bank goes a long way to determine the ability of that bank to make loans available to the needy sectors. This is important because, the volume of loans that could be made to an individual or body corporate by law is determined by the single obligor limit, which is tied to the capital base (Sanusi, 2010). Lending which may be on a short, medium or long-term basis is one of the services that deposit money banks render to their customers. In other words, banks do grant loans and advances to individuals, business organizations as well as government in order to enable them embark on investment and development activities as a means of aiding their growth in particular or contributing toward the economic development of a country in general (Felicia, 2019). Deposit money banks are the most important savings, mobilization and financial resource allocation institutions. Consequently, these roles make them an important phenomenon in economic growth and development. In performing this role, it must be realized that banks have the potential, scope and prospects for mobilizing financial resources and allocating them to productive investments and in return promote their performance.

A more accurate measurement of how fluctuations in market lending rates affect banking firms largely depends on the sensitivity of banks' assets and liabilities. When lending rates fluctuate as a result of changes in monetary policy or general economic conditions, money deposit banks usually encounter a comparative change in the rate of return they earn on their assets. This occurs because banks hold many assets of relatively short maturity and the rates booked on short period loans fluctuate quickly when lending rates fluctuate Banks' investment portfolio components comprise of mortgage rates, business term loans, rates on bank credit card loans, and real assets such as rental offices, when lending rates decrease they do encounter rapidly falling yields. Consequently, even the longer period components of a bank's assets portfolio are susceptible to yield declines when market rates fall, although their yields fall more gradually than short period yields. In the short run, however, as general market lending rates descend, the market value of longer assets with fixed contractual terms will rise.

Therefore, no matter the sources of the generation of income or the economic policies of the country, deposit money banks would be interested in giving out loans and advances to their numerous customers bearing in mind, the three principles guiding their operations which are, profitability, liquidity and solvency (Okoye & Eze, 2020). However, deposit money banks' decisions to lend out loans are influenced by a lot of factors such as the prevailing interest rate, the volume of deposits, the level of their domestic and foreign investment, banks liquidity ratio, prestige and public recognition to mention just a few. Lending practices in the world could be traced to the period of industrial revolution which increased the pace of commercial and production activities thereby bringing about the need for large capital outlays for projects. Many captains of industry at this period were unable to meet up with the sudden

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upturn in the financial requirements and therefore turned to the banks for assistance (Akinwale, 2018). However, the emergence of banks in Nigeria in 1872 with the establishment of the African Banks Corporation (ABC) and later appearance of other banks in the scene during the colonial era witnessed the beginning of banks' lending practice in Nigeria.

Though, the lending practices of the then colonial banks were biased and discriminatory and could not be said to be a good lending practice as only the expatriates were given loans and advances. This among other reasons led to the establishment of indigenous banks in Nigeria. Prior to the advent of the Structural Adjustment Programme (SAP) in the country in 1986, the lending practices of banks were strictly regulated under the close surveillance of the bank's supervisory bodies. The SAP period brought about some relaxation of the stringent rules guiding banking practices. The Bank and Other Financial Act Amendment (BOFIA) 1998, requires banks to report large borrowing to the CBN. The CBN also requires that the total value of a loan credit facility or any other liability in respect of a borrower, at any time, should not exceed 20% of the shareholders' funds unimpaired by losses in the case of commercial banks (Felicia, 2019). For the banks to balance their main objectives of liquidity, profitability and solvency, lending must be handled effectively and the banks must behave in a way that their potential customers are attracted and retained.

Bank Financial Performance

Financial performance refers to analytical of the strength and weakness of a firm in relation to its balance sheet and profit and loss statement (Ndubuaku, Ifeanyi, Nse & Onyemere, 2017).In this study, financial performance of banks could be measured through dividend per share, return on asset, bank profit after tax and return on equity. They were discussed thus:

1. **Return on asset:** Return on Asset (ROA) is operationalized as the proportion of net income generated from the total assets of a company. It measures the naira earnings an organization derives from each naira of assets they control and utilize. It is useful for comparing rival companies in the same industry. ROA gives a manager, investor, or analyst an idea as to how efficient a company's management is at using its assets to generate earnings (Hargrave, 2019). Return on assets is displayed as a percentage. ROA, as an accounting-based measurement, gauges the operating and financial performance of the firm. The measurement is such that the higher the ROA, the effective is the use of assets to the advantage of shareholders. Higher ROA also reflects the company's effective use of its assets in serving the economic interests of its shareholders (Ibrahim & AbdulSamad, 2011).
2. **Bank profit after tax:**Profit After Tax refers to the amount that remains after a company has paid off all of its operating and non-operating expenses, other liabilities and taxes. This profit is what is distributed by the entity to its shareholders as dividends or is kept as retained earnings in reserves (de Wet &Toit, 2017). To him, it is the net amount earned by a business after all taxation related expenses have been

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deducted. Profit after tax (PAT) can be termed as the net profit available for the shareholders after paying all the expenses and taxes by the business unit. The business unit can be any type, such as private limited, public limited, government-owned, privately-owned company, etc. Tax is an integral part of an ongoing business. After paying all the operating expenses, non-operating expenses, interest on a loan, etc., the business is left out with several profits, known as profit before tax or PBT. After that, the tax is calculated on the available profit.

3. **Return on equity:** Return on Equity (ROE) is operationalized as the percentage of income generated as a return to shareholders on their capital investment in a company. ROE is calculated by taking the profit after tax and preference dividends of a given year and dividing it by the book value of equity (ordinary shares) at the beginning of the year (Orbunde, Lambe&Anyanwu, 2022). It measures the profitability of a business in relation to shareholders' equity, which is also known as net assets or rather assets minus liabilities.

Interest Rate charged on Borrowers

Banks cannot always set high interest rates. Banks should consider the problems of adverse selection and moral hazard since it is very difficult to forecast the borrower type at the start of the banking relationship (Stiglitz and Weiss, 1981 cited in Bikker&Vervliet, 2017). If banks set interest rates too high, they may induce adverse selection problems because high-risk borrowers are willing to accept these high rates. Once these borrowers receive the loans, they may develop moral hazard behaviour or so-called borrower moral hazard since they are likely to take on highly risky projects or investments (Chodecai, 2004). From the reasoning of Stiglitz and Weiss, it is usual that in some cases we may not find that the interest rate set by banks is commensurate with the risk of the borrowers. The cost of borrowing money, measured in naira, per year per naira, borrowed, is the interest rate. Interest rates differ mainly in term/maturity. When maturity and liquidity together with other factors are considered, many different financial instruments and so many different interest rates will emerge (Anyanwu, 1997 cited in Udude, 2015). Interest rates can either be nominal or real.

Nominal interest rate can be measured in naira terms, not in terms of goods. The nominal interest rate measures the yield in naira per year, per naira invested while the real interest rate is corrected for inflation and is calculated as the nominal interest rate minus the rate of inflation (Pandey, 2019). There are daily reports of how Nigerian banks rip off their customers through various charges and practices. Oftentimes, customers complain and cry out for appropriate regulatory intervention. Unfortunately, their complaints seem to fall on deaf ears, because they are unaware of any positive regulatory action in response thereto. Emboldened by regulatory inaction and indifference (which suggest tacit approval), many Nigeria banks now engage in more exploitative practices. The categories of such predatory bank practices unfold daily. Normally, when a customer secures loan from a bank, the latter fixes a negotiated lending rate based on the prevailing interest rate approved by the apex bank

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(Garr &Kyereboah-Coleman, 2021). Any change in the interest rate should be brought to the notice of the borrower except otherwise agreed.

In Nigeria, however, the lending rate is rarely negotiated and, when it is reviewed upwards by the Central Bank of Nigeria (CBN), the average bank automatically applies the new rate to the outstanding loan without notifying the borrower (Okafor, 2021). Ironically, the same bank hides the fact of any downward review of the lending rate from its mostly uninformed customer, thereby illegally subjecting the customer to a higher interest regime. Often, what the bank staff present to a prospective borrower during loan negotiations as the total charges become hydra-headed once he swallows the bait. While processing loans, Nigerian banks impose on borrowers both “processing” and “administrative” fees which are duplicates. Again, they charge borrowers and corporate customers higher than what they pay lawyers to conduct searches at land and company registries. We believe that the interest rates Nigerian banks display at their offices and report to CBN per Section 23 of the Banks and Other Financial Institutions Act (BOFIA, Chapter B3, Laws of the Federation of Nigeria 2004) are different from what most of them impose on customers. To verify this, CBN may wish to randomly obtain and examine depositors/ borrowers account statements from banks.

Theoretical Review

The theories used are the classical theory of the interest rate, liquidity preference theory,loan pricing theory, and credit market theory.

The Classical Theory of the Interest Rate

In 1945, Marshall and Fisher were the first to propose what is now known as the classical theory of interest rates. Because only real factors like productivity and thriftiness are taken into consideration in the process of determining interest rates according to this theory, it is also referred to as the "real theory of interest rates." This is due to the fact that monetary factors are not given any weight in the process. According to traditional economic theory, the level of interest rates is established by analyzing how demand for and supply of investment or capital interact with one another (Richard, 1979). Due to the fact that businesses borrow money in order to invest, the cost of investment is interest. Therefore, the interest rate is crucial to the decision to invest. The opposite is true as well: a high interest rate will result in a decrease in investment, while a low interest rate will stimulate more investment.

Therefore, there is a negative connection between investment and interest rates. People keep their money in the bank so they may earn interest on it. When interest rates are high, people save more money, but when they are low, they save less money (Okoye&Udeh, 2009; Uchendu, 2009). However, the interest rate has a direct bearing (or a positive influence) on the amount of money saved. The need that businesses have to invest is met by the savings that families have. Therefore, savings represent supply in the products market, whereas investment represents demand. Therefore, the level of interest paid on loans to finance the purchase of products is established at the point in the market where the supply of and demand

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for savings cross or intersect one another. The interest rate will change to maintain equilibrium in the products market as a result of saving and investment.

Liquidity Preference Theory

The liquidity preference theory was developed by Maynard Keynes in his book General Theory in 1936.The theory is based on the premise that people hold money for three motives: transaction motive, precaution motive and speculative motive. The theory posits that one needs money because one has expenditure plans to finance, or is speculating on the future path of the interest rate, or, finally, because one is uncertain about what the future may have in store so it is advisable to hold some fraction of one's resources in the form of pure purchasing power.

Keynes argued that, other things held constant, people prefer to hold cash (liquidity). According to the theory, interest rate was the reward of parting with liquidity (Lekachman& Keynes, 1964). The theory suggests that interest rates change with changes in demand and supply of money. The money supply is fixed by the central bank; the quantity of money supplied does not depend on the interest rate. According to the theory, there is one interest rate, called the equilibrium interest rate, at which the quantity of money demanded equals the quantity of money supplied.

Loan Pricing Theory

This theory was developed by Stiglitz and Weiss in 1981. To the theorists, banks cannot always set high interest rates. Banks should consider the problems of adverse selection and moral hazard since it is very difficult to forecast the borrower type at the start of the banking relationship (Stiglitz and Weiss, 1981). If banks set interest rates too high, they may induce adverse selection problems because high-risk borrowers are willing to accept these high rates. Once these borrowers receive the loans, they may develop moral hazard behaviour or so-called borrower moral hazard since they are likely to take on highly risky projects or investments (Chodecai, 2004). From the reasoning of Stiglitz and Weiss, it is usual that in some cases we may not find that the interest rate set by banks is commensurate with the risk of the borrowers.

Credit Market Theory

The theory was popularized by Ewert, Szczesny and Schenk in 2000.A model of the neoclassical credit market postulates that the terms of credits clear the market. If collateral and other restrictions (covenants) remain constant, the interest rate is the only price mechanism. With an increasing demand for credit and a given customer supply, the interest rate rises, and vice versa. It is thus believed that the higher the failure risks of the borrower, the higher the interest premium (Ewert, Szczesmy and Schenk, 2000).

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Empirical Review

Newman (2015) attempted to examine the performances of banks and macro-economic performance in Nigeria based on the interest rate policies of the banks. The study analyses published audited accounts of twenty (20) out of twenty-five (25) banks that emerged from the consolidation exercise and data from the Central Banks of Nigeria (CBN). This study used the regression and correction methods to analyze the relationship between interest rates and bank performance. They denote year 2004 as the pre-consolidation and 2005 and 2006 as post-consolidation periods for our analysis. We notice that the interest rate policies have not improved the overall performances of banks significantly and also have contributed marginally to the growth of the economy for sustainable development.

Garr and Kyereboah-Coleman (2021) researched macroeconomic factors, firm specific variables, and industry variables as possible determinants of interest spread in Ghana. The study was based on a sample of 33 banks spanning the years 1990 to 2010. The results of the study showed that Gross Domestic Product per capita, management inefficiency, government securities and bank ownership were positively associated with interest rate spread in Ghana. The results also showed that domestic banks have wider interest rate spread than foreign owned banks suggesting that the foreign banks are more efficient than the local banks.

Kanwal and Nadeem (2019) investigated the impact of macroeconomic variables on profitability of public Limited commercial banks in Pakistan for years 2001-2011. Pooled Ordinary Least Square (POLS) method is used to examine the effect of 3 major external factors, inflation rate, real Gross Domestic Product (GDP) and real interest rate on profitability indicators, Return on Assets (ROA), Return on Equity (ROE) and Equity Multiplier (EM) ratios in 3 separate models. The empirical findings indicate a strong positive relationship of real interest rate with ROA, ROE and EM. Secondly, real GDP is found to have an insignificance positive effect on ROA, but an insignificant negative pact on ROE and EM. Inflation rate on the other hand, has a negative link with all 3 profitability measures. Overall, the selected macroeconomic factors are found to have a negligible impact on earnings of commercial banks.

Ojeaga and Odejimi (2014) investigated the effect of interest rates on customer savings behavior in the Nigerian banking sector, after identifying host of factors that are likely to influence customer confidence in commercial banks such as average income, commercial lending, legal rights strength, central bank monetary policy and total annual commercial bank losses, using quintile regression estimation method, a non-parametric estimation process that is based on the premise that the sample median will tend to that of the distribution and addresses issues of heteroscedastic errors and data stringency associated with the data used in the study under question.They found that interest rates were probably increasing bank deposits while income was also found to affect bank deposits in general.

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Obidike, Ejeh and Ugwuegbe (2015) examined the impact of interest rate spread on the performance of the Nigerian banking industry for the period of 1986-2012. The study used the OLS method of estimation to analyze the data generated from CBN statistical Bulletin and World Bank online data base. Testing for the properties of time-series, ADF test indicates that all the variables are integrated of the same order 1(1). The co-integration test reveals that there exists a long-run relationship among the variables under consideration. The result shows that interest rate spread negatively and significantly impacts bank performance in the long-run. Exchange rate and GDP was found to be positively and significantly affecting bank performance in Nigeria at the long-run. The result of the ECM indicates that 23.37 percent of the disequilibrium in the model will be corrected annually. Moreover at the short-run interstate spread also negatively but insignificantly affect bank performance in Nigeria.

Musah, Anokye and Gakpetor (2018) measured interest rate spread using net interest income (IntSp) and Net Interest Margin (NIM) and bank profitability using Return on Assets (ROA) and Return on Equity (ROE). The study is based on a sample of 24 banks over a ten - year period using a panel data. Secondary data through regression was used. The results of the study show that there is a positive and statistically significant association between interest rate spread and bank profitability in Ghana. The findings could be interpreted within the context of the loan able funds theory to suggest that the demand for loans exceed the supply of same allowing banks to charge higher interest on lending relative to deposits to increase profitability. The results of the study have significant implications on research on interest rate spread and more especially on government policy to reduce interest rate spread in Ghana.

Akinwale (2018) examined the relationship between bank lending and economic growth in Nigeria between 1980 and 2016. Data sourced from the various issues of Central Bank of Nigeria Statistical Bulletin was analyzed through Dynamic Ordinary Least estimation technique. Data treatment was done through stationery and co-integration tests. The unit root test showed that the variables were integrated at order on 1(0) except rate of bank lending, inflation and real exchange were integrated at order on 1(1). The result of co integrated showed a long run relationship among the variables. The Results proved that a unit percent decrease in bank lending rate will bring about 118% increases in economic growth. Furthermore, the findings of Greenwood and Jovanovich Hypothesis established that as bank lending rate decreased, economic growth tend to increase and it is statistically significant at 1% level. The study concluded that a decreased in bank lending rate increased economic growth during the study period.

Mukolu and Adeleke (2020) examined the lending rate in the Nigerian money deposit banks and their effects on banks performance from 2001 to 2016. The study examined the correlation between the cash reserve ratio, lending rate, monetary policy rate, total deposit on return on asset and return on equity of money deposit banks in Nigeria. The study utilized secondary data and while unit root test, co-integration test, correlation analysis, and regression analysis were used as an estimation technique for the study. Multiple regression

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analysis was used to estimate the data for 21 commercial banks. The result confirmed that the lending rate has significant and positive effects on the performance of Nigeria money deposit banks. The implication of this is that monetary policy rate, lending rate, and cash reserve ratio have a positive impact on bank performance but they are not statistically significant.

Maigua and Mouni (2016) conducted research to determine the extent to which the performance of commercial banks in Kenya is affected by the factors that determine interest rates. The key economic elements that have the most significant impact on an economy's overall economic growth are interest rates. They are useful tools for bringing inflation under control and for fostering economic growth. Inflation rates, discount rates, exchange rates, and reserve requirements are some of the factors of interest rates that have been investigated in order to ascertain the effect that they have on the activities of financial institutions. The 43 commercial banks currently functioning in Kenya served as the study's primary population of interest. The size of the sample was determined to be 26 commercial banks that were randomly selected from the population. The method of analyzing the data that was used in this research was known as multiple regression analysis. On the other hand, higher levels of reserve requirement ratio lead to lower levels of performance in commercial banks in Kenya.

Oladele, Amos and Adedeji (2017) investigated how the current interest rate environment affects the profitability of deposit money institutions in Nigeria. During the years 2005 - 2014, data was collected from 21 different deposit money banks located in Nigeria. A regression analysis was carried out for the goal of their research in order to identify the nature of the connection that exists between the interest rate and the profitability of deposit money banks in Nigeria. The outcomes of their investigation indicated that there was a positive and statistically significant connection between the interest rates on loans and the profitability of the bank. There was a large and positive correlation between the interest rate that was being exchanged between banks and the profitability of the banks. The interest rate on treasury bills had a positive and substantial link with the profitability of banks, and the interest rate on monetary policy also shown a positive and significant association with the profitability of banks.

Kihara and Mirie (2017) analyze effect of interest rates on the financial performance of commercial banks in Kenya. The study adopted an explanatory research design. This study adopted a census research design; of all the 43 commercial banks in Kenya. The study also used secondary data. Multiple linear regression model was used to analyze the data using statistical package for the social sciences (SPSS) version 20. The study established that lending rate ratio influence the financial performance of commercial banks in a positive way. Deposit interest ratio on the other hand negatively affects performance of commercial banks. Liquidity management and liquidity management influence performance positively and negatively respectively. The study concluded that there is a positive significant relationship between lending rate ratio and financial performance of commercial banks. The study also arrived at the conclusion that deposit interest ratio negatively affects bank performance.

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Okoye and Eze (2020) examined the impact of bank lending rate on the performance of Nigerian Deposit Money Banks between 2000 and 2010. It specifically determined the effects of lending rate and monetary policy rate on the performance of Nigerian Deposit Money Banks and analyzed how bank lending rate policy affects the performance of Nigerian deposit money banks. The study utilized secondary data econometrics in a regression, where time-series and quantitative design were combined and estimated. The result confirmed that the lending rate and monetary policy rate has significant and positive effects on the performance of Nigerian deposit money banks. The implication of these is that lending rate and monetary policy rate are true parameter of measuring bank performance.

Ojeaga and Odejimi (2014) investigated the effect of interest rates on customer savings behavior in the Nigerian banking sector. It identified a host of factors that are likely to influence customer confidence in commercial banks such as average income, commercial lending, legal rights strength, central bank monetary policy and total annual commercial bank losses, using quantile regression estimation method, a non parametric estimation process that is based on the premise that the sample median will tend to that of the distribution and addresses issues of heteroscedastic errors and data stringency associated with the data used in the study under question. The work finds that interest rates were probably increasing bank deposits while income was also found to affect bank deposits in general.

Punita and Somaiya (2016) investigated the impact of interest rate on the profitability of banks in India between 1995 and 2010. It used regression through secondary data. The monetary variables used were Monetary Policy Rate (MPR), lending rate; cash reserve ratio and statutory ratio. These variables were regressed on banks profitability independently. Lending rate was found to exert positive and significant influence on banks' profitability, which indicates a fall in lending rate will reduce the profitability of the banks. Also, bank rate, cash reserve ratio and statutory ratio were found to have significant effect on the profitability of banks (negatively). It was also 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 instrument in the private sector.

Hughes, Lang and Moon (2018) examined the constrained implication of interest rate policy on bank lending in Ghana between 1998 and 2014. It used regression through secondary data. The study revealed that Ghanaian banks lending behavior are affected significantly by the country's economy and changes in money supply.

Efanga, Hanson, Umoh and Umoh (2020) empirically examined the impact of interest rate on commercial bank lending in Nigeria. Data was collected from the Central Bank of Nigeria (CBN) statistical bulletin, 2018. Multiple regression was used in analyzing the data. The Ordinary Least Square Regression (OLS) method was employed to ascertain the impact of interest rate on commercial bank lending in Nigeria. The result showed a negative relationship between commercial bank lending and lending rate, there existed also a positive

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relationship between gross domestic product and commercial bank lending. Since lending rate has a negative relationship with commercial bank lending, this study recommended that the CBN should reduce monetary policy rate (MPR) so as to reduce the high cost of borrowing.

Amidu and Wolfe (2018) examined the constrained implication of monetary policy on bank lending in Ghana between 1998 and 2014. It used regression through secondary data. Their study revealed that Ghanaian banks' lending behaviouris affected significantly by the country's economic support and change in money supply. Their findings also support the finding of previous studies that the central bank prime rate and inflation rate negatively affect bank lending. Prime rate was found statistically significant while inflation was insignificant.

Research Gap

Many studies have been done in related areas of this work. However, there exist subject, time series gap, geographical, content, indices, literature, and methodological research gaps. They are summarized thus:

a. **Period gap:** This work covered between 2008 - 2021 as its time scope. From the empirical studies, it could be seen that none of the past researches covered up to 2021. Which mean there exist time series gap which this work wants to fill.
b. **Geographical gap:** This work covers only banks in Nigeria. some of the previous researches were done using other countries of the work, not Nigeria. Some that covered Nigeria banks or the exact topic.
c. **Gap on the indices of measurement:** The indices of measurement used in most of the past studies differ from what was used in this work. The indices for this work islending rates. Others are return on assets, profit after tax, and return on equity. None of the past studies used the above indices, hence research gap.

In all there exists research gap which this study wants to fill. This study therefore focused on lending rate and financial performance of deposit money banks in Nigeria (2008 – 2021).

RESEARCH METHODS

Research Design

A research design is the set of methods and procedures used in collecting and analyzing measures of the variables specified in the research problem. In this study, the researcher employed quasi-experimental research design for the study. Quasi-experimental study examines how an independent variable, present prior to the study, affects a dependent variable. This will be used because the study focused on secondary data.

Secondary data sources were utilized for the study. The data were sourced from the three banks' annual reports between 2008 and 2021 (14 periods of 42 observations) and central bank of Nigeria statistical bulletin. The nature of the data is panel data. Banks performance

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was proxied with Profit after tax, return on asset and return on equity while lending rate was proxied with CBN approved lending rates.

Model Specification

The model used for this study was specified to show the functional relationship between interest rate and performance thus:

$$PAT = F(LendR) \ldots eq\ 1$$

$$ROA = F(LendR) \ldots eq\ 2$$

$$ROE = F(LendR) \ldots eq\ 3$$

The model can be specified econometrically as:

$$PAT_{it} = \beta_0 + \beta_1 LendR_{it} + \beta_1 Asset_{it} + \varepsilon_{it} \ldots eq\ 4$$

$$ROA_{it} = \beta_0 + \beta_1 LendR_{it} + \beta_1 Asset_{it} + \varepsilon_{it} \ldots eq\ 5$$

$$ROE_{it} = \beta_0 + \beta_1 LendR_{it} + \beta_1 Asset_{it} + \varepsilon_{it} \ldots eq\ 6$$

The model can be transformed to reflect its log form as follows:

$$logPAT_{it} = \beta_0 + \beta_1 log\, LendR_{it} + \beta_2 log\, Asset_{it} + \varepsilon_{it} \ldots eq\ 7$$

$$logROA_{it} = \beta_0 + \beta_1 logLendR_{it} + \beta_2 log\, Asset_{it} + \varepsilon_{it} \ldots eq\ 8$$

$$logROE_{it} = \beta_0 + \beta_1 logLendR_{it} + \beta_2 log\, Asset_{it} + \varepsilon_{it} \ldots eq\ 9$$

β_0 –slope of the model
β_1 – coefficients to be estimated
ε – stochastic error
i – Individual bank
t – Time period.

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PAT – Profit After Tax
ROA – Return on Assets
ROE – Return on Equity
Lend – Lending Rates
Asset – Control Variable

Method of Data Analysis

Panel Least Square Regression method of analysis was adopted for the model estimation. Some diagnostic tests such as normality test and dependency test were carried out to check the adequacy of the data and its appropriateness in fitting into the study model.
Decision Rule: Decision rule is based on 10% significant level.

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Data Analysis

Dependency Test

Table 3: Residual Cross-Section Dependence Test
Null hypothesis: No cross-section dependence (correlation) in residuals
Total panel observations: 42
Cross-section effects were removed during estimation

Test	Statistic	d.f.	Prob.
Breusch-Pagan LM	1.3011	3	0.4853
Pesaran CD	-0.6527		0.7412

Source: Researcher's Computation using E-views 7

Source: Researcher's Computation using E-views 9

One of the diagnostic tests carried out in this work is the dependency test, so as to confirm that the disturbances in panel data models are cross-sectionally independent. The study employed Breuch-Pagan (1980) LM and Pesaran (2004) CD dependence test to ascertain the presence of cross-sectional dependence in the residuals. Both Breusch-Pagan LM and Pesaran CD tests accept the null hypothesis at 0.05. Analysis shows that there is no cross-sectional dependence in the residual, hence the panel data is suitable for regression (P-Value 0.48 and 0.74 respectively).

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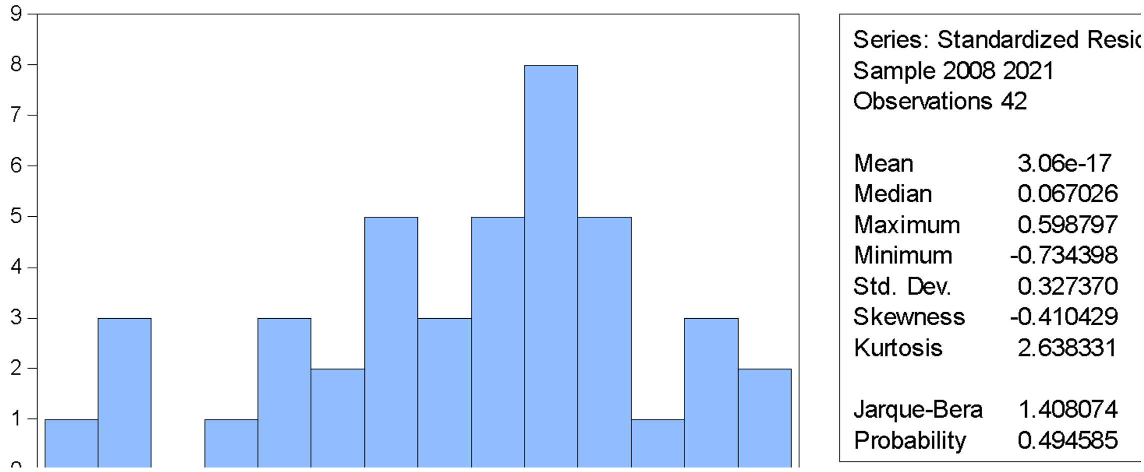

Figure 1: Test of Normality

Source: Researcher's Computation using E-views 9

To ensure that the data set had a normal distribution, a *normality test*was carried out. The test shows the aggregated averages of the mean, median, and standard deviation which are measures of spread and variation, skewness which looks at the symmetry, and Kurtosis which looks at the centrality of the peak. The overall Jarque-Bera statistics of 2.63 with a p-value of 0.49 accepts the null hypothesis that the data is normally distributed.

Panel Least Square Regression Result

The regression results as given in equation 7, 8, and 9 are presented below.

Table 4: Panel Least Square Regression Result for Equation 7

Dependent Variable: LOGPAT
Method: Panel Least Squares
Total panel (balanced) observations: 42

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LOGLENDR	2.683173	1.314118	2.041805	0.0480
LOGASSETS	0.243690	0.308638	0.789568	0.4346
C	-0.497047	1.199630	-0.414334	0.6809

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R-squared	0.356078	Mean dependent var	4.866289
Adjusted R-squared	0.323057	S.D. dependent var	0.355083
F-statistic	10.78319	Durbin-Watson stat	0.774001
Prob(F-statistic)	0.000187		

Source: Researchers' Computation

The coefficient of *LOGLENDR* shows that lending rateis positively and significantly related to banks profit after tax (*LogPAT*). Its coefficient of -2.68 shows that a unit increase in lending rate increases profit after tax by 2.68 units and this coefficient is significant as p value is less than 10 per cent (4.8%).

Table 5: Panel Least Square Regression Result for Equation 8
Dependent Variable: LOGROA
Method: Panel Least Squares
Cross-sections included: 3
Total panel (balanced) observations: 42

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LOGLENDR	2.301154	1.314090	2.341035	0.0527
LOGASSETS	-0.450205	0.308631	-2.954514	0.0189
C	1.741949	1.199604	1.252871	0.3277

R-squared	0.133607	Mean dependent var	0.349509
Adjusted R-squared	0.089176	S.D. dependent var	0.306111
S.E. of regression	0.292143	Akaike info criterion	0.445605
Sum squared resid	3.328563	Schwarz criterion	0.569724
Log likelihood	-6.357708	Hannan-Quinn criter.	0.491100
F-statistic	3.007095	Durbin-Watson stat	0.773989
Prob(F-statistic)	0.061016		

Source: Researchers' Computation

The coefficient of *LOGLENDR* shows that lending rateis positively and significantly related to banks return on asset (*LogROE*). Its coefficient of 2.30 shows that a unit increase in

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lending rate increases profit after tax by 2.30 units and this coefficient is significant as p value is less than 10 per cent (5.2%).

Table 6: Panel Least Square Regression Result for Equation 9
Dependent Variable: LOGROE
Method: Panel Least Squares
Total panel (balanced) observations: 42

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LOGLENDR	2.245724	1.195318	1.878767	0.0678
LOGASSETS	-0.445078	0.280736	-1.585398	0.1210
C	0.917684	1.091180	0.841002	0.4055

R-squared	0.083244	Mean dependent var	1.176971
Adjusted R-squared	0.036231	S.D. dependent var	0.270687
F-statistic	1.770658	Durbin-Watson stat	0.854715
Prob(F-statistic)	0.183631		

Source: Researchers' Computation

The coefficient of *LOGLENDR* shows that lending rateis positively and significantly related to banks return on equity (*LogROE*). Its coefficient of 2.68 shows that a unit increase in lending rate increases profit after tax by 2.68 units and this coefficient is significant as p value is less than 10 per cent (4.8%).

From the analysis so far, it evident that lending rate has a very significant positive effect on banks performance. All the three performance models employed in this study has the same outcome of significant relationship between lending rates and banks performance indices. These findings are in agreement with the study of Musah, Anokye and Gakpetor (2018) that there is a positive and statistically significant association between interest rate spread and bank profitability. It also correlates with the study of Garr and Kyereboah-Coleman (2021)in Ghana.

Summary of Findings

Lending rate and its effects on banks financial performance was critically examined in this study. The study proxied lending rate with lending rate issued to banks from the apex bank. WhileProfit after tax, return on assets and return on equity served as the measure for performance. Finding from the study shows that:

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i. lending rate has a significant effect on profit after tax in the Nigerian banks.
ii. lendingrate has a significant effect on return on asset in the Nigerian banks.
iii. lendingrate has a significant effect on return on equity in the Nigerian banks.

Conclusion

This research is conducted with the objective to examine the relationship between lending rate and financial performance of banks. In order to measure the profitability three dependent variables were taken; profit after tax, return on assets, return on equity. The independent variables were lending rate and total asset as a control variable. By considering the results of research we canconclude that profitability of banks is significantly affected by changes in the lending rate, though this does not mean that other variables that could affect banks performance were neglected such as deposits with otherbanks, investments and others.Return on assets is one of the critical factors which help us identify the profitability of banks. As banksincrease its deposits with other banks its return on assets decreases because it will decrease the value of totalassets. The study reviewed four important theories related to interest rates such as the Classical Theory of the Interest Rate, Liquidity Preference Theory, Loan Pricing Theory, Credit Market Theory. After a lot of empirical analysis, the study concludes that the lending rate has a positive and significant relationship with banks' financial performance.

Recommendations

The results of this research suggest that bankslending rate is an important function of their profitability. Through proficient and skilful regulation and administrative structure bank's lending rate polices can for formulated to benefit the banks more. Therefore, it is recommended that government should also make such monetary policies which will increase the profitability ofbanks.

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