Contextual Factors of Innovation for Improving Commercial Banks' Performance in Nigeria

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Abstract : The banking system in Nigeria adopted innovative banking, with the aim of enhancing financial inclusion, and making financial services readily and cheaply available to majority of the people, and to contribute to the efficiency of the financial system. Some of the innovative services include: Automatic Teller Machines (ATMs), National Electronic Fund Transfer (NEFT), Point of Sale (PoS), internet (Web) banking, Mobile Money payment (MMO), Real-Time Gross Settlement (RTGS), agent banking, among others. The introduction of these payment systems is expected to increase bank efficiency and customers' satisfaction, culminating in better performance for the commercial banks. However, opinions differ on the possible effects of the various innovative payment systems on the performance of commercial banks in the country. Thus, this study empirically determines how commercial banks use innovation to gain competitive advantage in the specific context of Nigeria's finance and business. The study also analyses the effects of financial innovation on the performance of commercial banks, when different periods of analysis are considered. The study employed secondary data from 2009 to 2018, the period that witnessed aggressive innovation in the financial sector of the country. The Vector Autoregression (VAR) estimation technique forecasts the relative variance of each random innovation to the variables in the VAR, examine the effect of standard deviation shock to one of the innovations on current and future values of the impulse response and determine the causal relationship between the variables (VAR granger causality test). The study also employed the Multi-Criteria Decision Making (MCDM) to rank the innovations and the performance criteria of Return on Assets (ROA) and Return on Equity (ROE). The entropy method of MCDM was used to determine which of the performance criteria better reflect the contributions of the various innovations in the banking sector. On the other hand, the Range of Values (ROV) method was used to rank the contributions of the seven innovations to performance. The analysis was done based on medium term (five years) and long run (ten years) of innovations in the sector. The impulse response function derived from the VAR system indicated that the response of ROA to the values of cheques transaction, values of NEFT transactions, values of POS transactions was positive and significant in the periods of analysis. The paper also confirmed with entropy and range of value that, in the long run, both the CHEQUE and MMO performed best while NEFT was next in performance. The paper concluded that commercial banks would enhance their performance by continuously improving on the services provided through Cheques, National Electronic Fund Transfer and Point of Sale since these instruments have long run effects on their performance. This will increase the confidence of the populace and encourage more usage/patronage of these services. The banking sector will in turn experience better performance which will improve the economy of the country. Keywords: Bank performance, financial innovation, multi-criteria decision making, vector autoregression,

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