

Interest Rate Policy and Stock Market Capitalization in Nigeria

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Article History	Abstract
Original Research Article	<i>This study investigates interest rate policy and market capitalization in Nigeria. Data on time-series were obtained from the Central Bank of Nigeria Statistical Bulletin. The dependent variable (MCR) and the independent variables are also defined: the prime lending rate, savings rate, money market rates and monetary policy rate. Methods: Market capitalization and interest rate policy were estimated using descriptive statistics and multiple regression models. The analytical models include Ordinary Least Squares (OLS), Augmented Dickey-Fuller (ADF) test and Autoregressive Distributed Lag (ARDL). The estimated model showed that the variation of market capitalization ratio (MCR) was 99.8% jointly explained with independent variables included in the model. Monetary policy rate and prime lending rate did not have statistically significant positive but negative effect on the development financial sector measured by market capitalization. The finding of the study also established that interest rate policy is a significant factor affecting variation of stock market capitalisation in Nigeria. It suggested that monetary authorities should continue to promote lending at moderate rates which support borrowing for productive investment while avoiding excessive crowding out of low-risk borrowers. Additionally, the Central Bank of Nigeria must adjust interest rates in more gradual and nuanced ways so as not to stifle private-sector access to finance.</i> Keywords: Interest Rate Policy, Monetary Policy Rate, Prime Lending Rate, Savings Rate, Stock Market Capitalization.
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Copyright © 2026 The Author(s): This is an open-access article distributed under the terms of the Creative Commons Attribution 4.0 International License (CC BY-NC) which permits unrestricted use, distribution, and reproduction in any medium for non-commercial use provided the original author and source are credited. Citation: Ezema, Uchechi Anne & Dr. H.W Akani. (2026). Interest rate policy and stock market capitalization in Nigeria. UKR Journal of Economics, Business and Management, 2(9), 40-51.	

Introduction

To understand this idea, take a public company whose shares are traded in the stock market calculating the value of its shares and division among all those thanks to that gives us their total market capitalization. The stock market (or equity market) is a component of a financial market for the trading of company stock and derivatives at an agreed price; such as shares, which represent fractional ownership in a firm (debt securities are more properly known as bonds) (Osoro, 2013). According to Table A.21. 3 of the Central Bank of Nigeria Statistical Bulletin, market capitalization relative to GDP in Nigeria ranged between about 30% and 45 percent from 1985 to 2023. Economic literature has extensively covered the importance of market capitalization in economic growth, especially since it plays a vital role as an indicator of the ups and downs of capital markets. These variations are as a result of the price changes in stocks traded in market (Uremadu et al, 2019). This means that if the market capitalization is up, it tells that the market is doing well and stockbrokers can sell stocks profitably

unlike when the market capitalization is low it tells about a poor performance in the market thus reduced chances of making profits (World Bank, 2021). Market capitalization is the market value of a company measured by the firms' current stock price multiplied to the total number of shares outstanding (Shiller, 2015).

Interest rate deregulation was one of the key elements in Nigeria's financial sector reforms that began in the last quarter of 1986. The target was to keep interest rates positive (after inflation), since the large increase in inflation during the 1970s had made real interest rates negative, while rigid exchange and interest rate controls maintained low levels of direct investment. That was the position on the policy side, that interest rate liberalization would also improve other things like providing adequate funds to (over)investors especially manufacturers who were considered as being the leading agents of investment and therefore economic growth (WEA Doc: Odhiambo (2009).

Interest degrees include financial savings charges, lending charges Treasury bill fees and improve charge of interest. This policy was initiated to enhance efficiency in the financial part and advance financial deepening. Key to the transmission of interest rates is the adjustment of retail bank interest rates, both deposit and lending rates, to changes in policy rates, as well as money market rates. Transmission of changes in the policy rate to retail interest rates and money market rates is critical for monetary policy effectiveness. How effective this transmission will be, however, is largely determined by the stage of development of a given financial system. The expected evolution of the financial market is also accounted for with bank management models as financial markets tend to be characterized in terms of their size, liquidity and degree of access to financial services due both to internal strategic factors and external economic conditions.

In addition, Udoka (2012) noted that Nigerian interest rates were fully deregulated in 1986 but after this regulation was undone in January 1994 which pegged the lending interest rate at 21% per annum and deposit interest rate at 12% per annum. Interest rates were fully deregulated in October 1996, when it was permitted for banks, based on consultations with their customers to structure cornerstone interest rate. That said, we maintained that CBN retained its discretionary powers to intervene in the money market at any point it deems necessary with a view to ensuring orderly interest rate behaviour. And this deregulation framework has continued to function since 1997. Following the submission by Francis (2019) as quoted in Adebayo and Udofu (2021), despite retaining indirect regulation of interest rates via official monetary policy instruments, banks operate in a deregulated interest rate regime in Nigeria. Interest rates on deposits by Nigerian deposit money banks remain substantially influenced if not entirely driven by the Monetary Policy Rate (MPR), which is in turn set and controlled by the CBN. So higher MPR generally attracts high-interest rates and lower MPR meaning low interest (Francis, 2019).

Consequently, the Monetary Policy Rate (MPR) is defined as the prevailing policy interest rate set by the Central Bank of Nigeria and it is considered a benchmark for other rates in money market and economy. The MRR/MPR has not always been constant over the years; on the contrary, it has usually been varied upward and downward to conform to changing economic conditions in the country and as a benchmark rate of other market interest rates in the economy. The CBN cut the MPR to lend cheaply in support of economic activity (Olurounbi, 2020) from 12.50% to 11.50%. But after keeping the MPR at 11.5% for about two and a half years, Enyioko (2012) note that the CBN Monetary Policy Committee has fully reversed the biting

increase of benchmark interest rate from 11.5% to new heights of 13%, which they say was expedient as large scale inflationary pressure bears down on global economy. This was increased to 14% in July 2022 (Smith, 2021). This illustrates the fact that monetary policy can be volatile in Nigeria, which makes financial market performance quite difficult to predict since it is largely driven by interest rate movements. Given the above, this study is appropriate and pertinent to investigate how the behaviour of interest rates has affected market capitalisation.

Literature Review

Conceptual Reviews

Interest Rate Policy

According to Keynes (1936), savings are defined as income that surpasses consumption expenditure. In other words, savings are the share of disposable income over a period of time that is not used for consumption (Umoh 2003, Uremadu 2005). With income being equal to the value of current output and that current investment (gross capital formation) is graphically equal to this portion of current output not consumed, savings can be viewed as income less consumption. For Keynes, on an aggregate level more income than consumption (or savings) cannot be different from the increase in capital equipment or gross fixed capital formation or Gross-Domestic Investment. Hence, savings is residual and consumption of Invest — the decisions made aggregate expenditures during a certain period determine total volume of created national income? From this viewpoint, there will be an eventual rise in savings from higher income as long as it continues. Actually, there are two functions that would depend on income — saving and consumption; saving is considered to be a complement of the consumption function. The savings function does in fact stem from the simple linear consumption function where autonomous consumption expenditure has been separated (Umoh, 2003). But it was Keynes (1936) who brought in the opportunity cost variable, that is, interest rate — as classical economists viewed this as one of the most important factors determining savings (Olusoji, 2003; Chete, 1999; McKinnon, 1973; Shaw, 1973).

Lending Rate Policy

Lending interest rate: The lending interest rate is the level at which a financial institution provides credit to its client. The lending interest rate is classified by CBN (2016) into Prime lending and maximum lending rates. It is the rate at which deposit money banks (DMBs) are willing to lend credit to their most reliable customers and thus represents a minimum interest rate that can be used as part of the foundation for any lending rate across various sectors. To contrast that, the maximum lending rate is when customers perceived to be lower risk borrowers can borrow from a

DMB spread. In support of the position of CBN, Kagan (2020) further asserts that the lending interest rate is reported as a percentage for which a borrower will be charged for borrowing funds and represents income to the lender. The author's observation is that an interest rate will depend on the type of financing DOA you obtain and how qualified they are.

Savings Rate Policy

Also known as the deposit rate the savings interest rate is another of the significant variables necessary to reach the aims of this research work, which are usually contemplated in classifying market lending interests. According to Ogege (2019) savings interest rate is the cost that deposit-taking financial institutions incur while borrowing and in this case, mobilizing deposits which ultimately determine how much it would cost to lend these same funds. Therefore, higher savings interest rates imply that lending interest rates will also be high, and vice versa. A good savings interest rate leads to higher savings. Individuals save their idle funds if interest rates offered on savings are attractive. This raises the amount of loanable funds available to support economic activities and, as a result, help grow the economy. In the point of view of financial-sector performance, a higher interest rate on savings translates into better profitability for savers who earn greater returns on their deposits while things get more expensive for financial institutions, which have additional expenses relative to the deposits they mobilize.

Nonetheless, the short-term expense to financial institutions due to higher savings deposit rates could be alleviated over the long run due to greater revenues from an increased lending base. Increased deposit rates could be a carrot to urge the collection of deposits; this will also provide financial institutions with capital needed and that they can loan out to borrowers insistent on earning interest. On the other hand, money supply was made accessible in the market, as CBN last week reviewed downwards interest on savings deposits to a floor of 10 per cent a year for all banks from 30 per cent annually of the MPR before (Olurounbi, 2020). Interest rate spread is the difference between lending rate and deposit rate. Interest rate spread is an integral part of the saving-investment process and a gauge in assessing the functional efficiency of financial institutions in their function as intermediaries between savers and borrowers (Igbodika & Chukwununu, 2016).

Monetary Policy Rate

Until now, Nigeria's discount rate was called the Minimum Rediscount Rate (MRR). To enhance it anew as an effective tool for 'anchoring' market interest rates, the Monetary Policy Rate (MPR) replaced the MRR in December 2006 enabling it to serve as a benchmark that would be used to

determine other interest rates in the economy thereafter (Sanusi, 2004). Monetary policy is defined by the Central Bank of Nigeria (CBN, 2016) as the actions that the Central Bank takes to manage the money supply and interest rates in order to pursue objectives targeting economic growth, employment, price stability, or other macro-economic goals. The MPR is highly significant as it represents CBN policy rate and used primarily in terms of monetary policy transmission, serving basically as a benchmark interest rate for the entire money market and the economy at large. Changes in MPR have their impact on the price mechanism and various economic activities through different transmission channels. This is confirmed by the study of (Coronation Research, 2021) that statements regarding MPR influence public expectations and confidence likewise expectations on the future performance of the economy for several economic agents.

Likewise, MPR affects stock and other financial assets prices, exchange rates and saving and spending choices of economic agents. In this time, the MPR has varied significantly in response to changing economic conditions; inflation towards the top and stimulus urges at the other. MPR, 27.0% as of October 2025 (CBN, 2025). Thus, the MPR plays a fundamental role that forms the basis of our research focus as it is one of the key independent parameters for evaluating how interest rate policy may affect the market capitalization in Nigeria. This conforms to the submission of Igbodika and Chukwunulu (2016) which held that a higher monetary policy and savings rates raise borrowing cost for financial institutions and by implication affect living and economic activities.

Market Capitalization

Capital market capitalization is defined as the compounded value of a company's outstanding shares which are traded in the stock exchange. Often called the market capitalization or market cap, calculated by multiplying a company's total outstanding shares by its current stock price per share. The measure is used by the investment community to compare two companies in relative size instead of just total sales or as an alternative to a total asset value (Osinubi, 2004). In this study, the larger variable capital market capitalization is computed relative to broad money supply (i.e., consequently the percentage of broad money supply that has found its way into investing in Nigerian capital market).

Beck and Levine (2004) noted that theory on the way that share listing drives resource allocation – and thus economic growth – is not yet well developed. Also, following the arguments of Levine and Zervos (1998), market capitalization can not necessarily predict economic growth. Yet, according to Yartey (2008), this implies a different vision: higher overall market size is positively related to an

economy's ability to mobilize capital and diversify risk. Due to these opposing opinions, this paper uses a range of stock market development indicators such as: Market capitalization to GDP ratio; total value of shares traded ratio; turnover ratio etc. Secondly, this procedure also helps to get rid of multicollinearity in the model, which one can expect from Demirgüç-Kunt and Levine (1996), as all different measures of the development of stock markets are highly correlated.

The most widely used criteria for stock market size is to measure the ratio of Market Cap to GDP, which reflects the value of domestic shares in a country expressed as a percentage or fraction of that country's GDP. Two main reasons for the wide spread adoption of this indicator in the literature as a measure of stock market development. The first is a measure of size: the stock market capitalization, which is positively correlated with its ability to mobilize capital and diversify risk. Second, it is expected to represent the sum of companies accrued profits and future growth opportunity, so that a high market capitalization-to-GDP ratio could signal better growth opportunities (Zervos 1998b; Bekaert et al. 2001; Rajan & Zingales 2003). One of the primary shortcomings of this measure is that a high ratio can simply be a function of rapidly increasing share prices for just a handful of companies, with little to no increase in raised funds or breadth within the stock market itself. This might result in an overstatement of stock market developmental level (Adelegan, 2008).

Theoretical Review

Keynes Theory of Interest Rate

This hypothesis suggests an equilibrium with less than full employment in which both income and employment are variable. Interest is essentially a reward for forgoing liquidity. Interest rates are determined based on demand and supply of money. It is established that supply of money is largely controlled by monetary authorities and demand for money depends on income & interest rate. The liquidity preference theory of money, relating to the income for transactionary and precautionary motive is interest inelastic as well Reward Model.

The Keynesian hypothesis states that interest rate as piece of administered cost is detrimental to rise savings, and hence also investment demand at all. Those in favor of the theory emphasize that a higher real interest rate has strong positive effects on savings available for investment. This is because the high interest rate will prompt those with excess liquidity to save. So, banks will have lots of money available to lend to investors for investment purposes thus increasing the amount of productive investment undertaken. Finally, Keynes also emphasized the fact that interest rate is an entirely monetary phenomenon. This

theory introduced the concept of liquidity trap which is one such situation where low rate of interests discourages saving and hence interfere with investments because of lack of investable fund.

Loanable Fund of Interest Rate

The **Neoclassical or Loanable Funds Theory** explains the determination of the interest rate through the demand for and supply of loanable funds or credit. According to this theory, the interest rate represents the price of credit and is determined by the interaction between the demand for and supply of loanable funds. Prof. Lerner, as cited in Jhingan (1992), described the interest rate as the price that equates the supply of credit, comprising savings plus the net increase in the money supply during a period, with the demand for credit, consisting of investment plus net hoarding during the same period. The demand for loanable funds primarily originates from three sources: the government, businesses, and consumers. The government borrows funds to finance public works and other expenditures, while businesses borrow to acquire capital goods and finance investment projects. Such borrowing is generally interest-elastic and depends largely on the expected rate of return relative to the prevailing interest rate. Consumers also demand loanable funds to purchase durable goods such as houses and vehicles. Consumer borrowing is similarly interest-elastic, with the tendency to borrow generally increasing when interest rates are low and decreasing when rates are high.

Classical Theory of Interest Rate

The Classical Theory of Interest Rate states that the interest rate is determined by the interaction between the demand for and supply of capital. The supply of capital is governed by thrift or time preference, while the demand for capital is determined by the expected productivity of capital. Thus, the equilibrium interest rate is established at the point where the demand and supply curves for capital intersect at a given level of income (Younsi & Bechtini, 2018). The theory is regarded as a real theory of interest because it emphasizes real economic forces, particularly productivity on the demand side and thrift on the supply side, while largely disregarding monetary influences on the determination of interest rates. However, the theory has been criticized for treating money as merely a passive factor and for assuming full employment of resources. It also overlooks the influence of investment on income and, according to its critics, confuses the amount actually saved with the propensity to save (Taussig, 1998).

Empirical Review

David and Kofi (2025) explored the interactions of lending interest rates as well as loan portfolio structures, in Sub-Saharan Africa (SSA), on financial sector development. We

utilize two-step system Generalized Method of Moments (GMM) estimation techniques and fixed-effects regression models with panel data for 47 SSA countries over the period 2010–2023. The results showed that high lending interest rates negatively affected both loan portfolio quality and size. However, while the same credit aspect of financial development has been shown to negatively impact loan portfolio performance. More prominently, the interaction effect showed that strong financial access greatly dampens the negative impact of increasing interest rates on improving loan portfolio quality. Thus, the study underscored a crucial need to boost financial inclusion, deepen capital markets and foster institutional efficiency for sustainable credit systems as well as stronger resilience that are instrumental in Africa's development trajectory⁵².

Iriabije and Effiong (2025) studied the impact of financial sector development on Nigerian economic growth in the real sector between 1981 and 2022. The interest rate spread served as an indicator of the efficiency of financial intermediation and was used to measure financial sector development, while the growth rate of real gross domestic product (GDP) represented real-sector expansion. It used time-series data from the World Bank and the Central bank of Nigeria Statistical Bulletin, as well as the Autoregressive Distributed Lag (ARDL) model. The results showed that financial sector development hampers economic growth in the short run significantly and negatively, while its effect turns out to be positive and significant in the long run. The paper found that higher interest rate margin in developing economies is linked to high transaction costs due to insufficient infrastructure. It contended for a more responsive Nigerian financial system with a lower interest rate spread through infrastructure provision — to reduce transaction costs that would usually be embedded in lending rates.

Katembo (2024) examined how interest rate fluctuations impact stock market volatility in Congo using literature review methodology based on desk research—a secondary data from various published studies, reports, journals, and online sources. They proposed that fluctuations in interest rates carry the most weight in their impact on stock market volatility via investor sentiment and economic expectation. Higher interest rates usually cause borrowing costs to go up, which could hurt corporate profits and economic growth — in turn, making markets more volatile as investors re-evaluate stock prices. On the other hand, lower interest rates make borrowing cheaper which can benefit corporate profits and encourage economic growth, causing a preliminary drop in market volatility. Extended low interest rates however can also worry about overvaluing assets which will then amplify volatility in the market. It also added that fluctuations in interest rates are signallers of the

path of monetary policy and overall economic conditions, and they affect investor behaviour and stock market movements.

Kehinde (2024) examined the impact of financial deepening on stock market development in Nigeria within the mean for the period from 1981-2019. The Bound cointegration test within the ARDL framework was employed based on a strong belief that Nigeria's financial sector is still shallow and there isn't enough liquidity nor capital to help support developing a stock market. We then estimated short-run and long-run models after the Bounds cointegration test confirmed that a long-run relationship exists among all of these variables. Long-run empirical results showed that financial development, domestic savings as percent of GDP, broad money diversification and GDP were key determinants of Nigeria's stock market development. The implication of the study therefore is that financial deepening, domestic savings mobilization, monetary development and economic growth plays significant role in strengthening stock market in Nigeria.

Ogunlokun and Oguntuase (2023) used quantitative secondary data spanning the period 1987-2020, to assess the behavioural impacts of interest rates on growth in financial sector development in Nigeria. The study estimated financial sector growth, as a proxy normalised by real Gross Domestic Product (GDP) of the financial Institutions sector, against lending interest rate, deposit interest rate, monetary policy interest and Treasury bill rate. The different results obtained from the Phillips–Perron unit root test revealed that while; some variables were integrated $I(0)$, others at first-difference $I(1)$. Therefore, in order to examine both short- and long-run relationships between the variables under consideration, this study applied Autoregressive Distributed Lag (ARDL) model and bounds cointegration. Results confirmed that the variables interact in the long run. The most important factor for financial sector growth is lending interest age (coefficient -0.1391, p-value 0.0268 (<0.05)). On the other hand, deposit interest rate (coefficient = -0.0076; $p = 0.7410$), monetary policy rate (coefficient = 0.0077; $p = 0.2626$) and Treasury bill rates (coefficient = -0.3533; $p = 0.4889$) were statistically insignificant in the long run, but their short-run relationships are slightly different from that of long runs as well, The short-run dynamics estimated an error correction mechanism with a corrective speed of about 35 percent following each period deviation from long-run equilibrium. Post-estimation tests revealed that the residuals were homoscedastic and did not suffer from serial correlation. The study recommended that, considering the de-regulated nature of the financial sector, lending rates should be determined more efficiently by market forces of demand and supply rather than being artificially rigged up by banks

as it concluded that lending interest rate is a key driver for growth in the financial sector.

This study analysed the effect of monetary policy on financial sector development in Nigeria using financial data spanning the interval between 1981 and 2021 obtained from Central Bank of Nigeria, National Bureau of Statistic by Iwedi and Bekweri (2023). Unit root tests, cointegration analysis, regression techniques and Granger causality tests were used in the analysis of the data. The negative effects of the monetary policy rate and Treasury bill rate on the development of Nigeria's financial sector were particularly evident in the regression results. In contrast, Exchange rate and Inflation Rate have a positive impact on the financial sector development. The study then subsequently deduced that monetary policy variables such as money supply, Treasury bill rate, monetary policy rate and exchange rate are important factors on the development of financial sector in Nigeria. The results of the study suggested that in order to encourage economic growth, it is important for the government and monetary authorities to design effective exchange rate policies aimed at maintaining a stable and predictable exchange rate.

Obainoke et al. ADULMOTEN et al. (2023), studied the context of banking stone-development and stock market performance: evidence from Nigeria over a 29 years period; using data covering 1993–2021. Methods The Augmented Dickey–Fuller (ADF) unit root test, correlation analysis and Fully Modified Ordinary Least Squares (FMOLS) were used in the study. The development of the banking sector was evaluated through three indicators: private sector credit-to-GDP ratio (CPSG), banks' liquid liabilities-to-GDP ratio (BLIQR), bank assets-to-GDP ratio (BASSG). The results showed that private sector credit-to-GDP ratio and banks' liquid liabilities to GDP ratio significantly affected the stock market performance, while bank assets to GDP ratio did not have a significant effect. The study established the fact that banking sector development was one of the major determinants of stock market performance in Nigeria within the period under consideration. It had urged both the government and the Central Bank of Nigeria to pursue banking sector development, finance sector deepening by increasing access to credit for private-sector operators and expand Nigerian stock market performance. It observed that the bank system remains the final paying agent in any financial market and therefore recommend, among other things, efforts to strengthen monitoring frameworks on illegal conduct within banks — including effective measures against market malpractices and fraudulent activities but even sharp practices.

Literature Gap: These studies offer insights into the short-run and long-run effects of interest rate policy on market capitalisation . There remains, however, a conceptual

research gap in understanding the mechanisms that transform interest rate adjustments into market volatility. Specifically, there is a need for further research into the psychological and behavioural aspects of market players' responses to interest rate policy on stock market capitalisation in Nigeria.

Methodology

This study adopted an ex-post facto research design to investigate the relationship between bank management and loans to private sector in Nigeria. Data were assembled for the period 1990–2024 to encompass the period of interest. The data used in the study are annual time series data of the variables as described in the model. The secondary data approach was used in the study.

Model Specification

The theoretical framework presented showed how bank private sector credit. This study includes financial sector development variables as dependent variables bank management as independent variables.

$$MCR = f(PLR, SR, MTR, MPR) \quad (1)$$

The model can thus be presented as follows.

$$MCR_t = \gamma_0 + \gamma_1 PLR_t + \gamma_2 SR_t + \gamma_3 MTR_t + \gamma_4 MPR_t + \varepsilon_{5t} \quad (2)$$

Where:

MCR symbolized as Y_t is the market capitalization as percentage of gross domestic product

PLR_t - is Yearly prime lending rate data.

SR_t - is Yearly savings rate data.

MTR_t - is Yearly money market rate data.

MTR_t - is Yearly monetary policy rate data.

β_0 - is a constant

Where β_1 , β_2 and β_3 are the respective coefficients

All variables were converted to a percentage. Variable transformation to % is a typical practice in the literature (Bellemare & Wichman, 2020). It is done to make the interpretation process easier, make the relationship between the variables non-linear, normalize highly skewed data and reduce heteroscedasticity. This study uses the theory of the relationship of bank management presented by Dyvids (1983) on the link between bank management and private sector credit.

Unit Root Tests

To this end, we employ the Augmented Dickey-Fuller Test (ADF) and the Philips Peron test for unit root. Both tests are implemented in their three forms for dependable findings. The ADF was chosen because of the possibility to include

maximum lags of the dependent variable to account for autocorrelation in the error term. The most standard approach of testing for unit root was used to test for ADF in the following forms.

$$\Delta Y_t = Y_{t-1} + \sum \beta_t \Delta m_{t-1} Y_{t-1} + \mu_t \quad (3)$$

(none)

$$\Delta Y_t = \beta_1 + \beta_2 Y_{t-1} + \sum \beta_t \Delta m_{t-1} Y_{t-1} + \mu_t \quad (4)$$

(intercept)

$$\Delta Y_t = \beta_1 + \sum T + \beta_2 Y_{t-1} + \sum \beta_t \Delta m_{t-1} Y_{t-1} + \mu_t \quad (5)$$

(intercept and trend)

Where:

ΔY_t - is the variable of interest.

Y_{t-1} - is its one-period lag.

β_1 - is a constant and T is the time trend.

The null hypothesis of the variable's non-stationarity is evaluated against the alternative hypothesis of stationarity. The null hypothesis is rejected if the estimated t statistics is more negative than the crucial t statistics at 5% level (Gujarati et al., 2012). A rejection of the null hypothesis suggests that the variable is stationary.

Cointegration Analysis

The study used the autoregressive distributed lag model bounds testing technique to cointegration to assess the long-run relationship among variables. The ARDL models are recognised as better than other methods to examine long term relations between variables when the size is small like in this study.

$$PSC = \alpha_0 + \beta_1 CM_{t-1} + \beta_2 LM_{t-1} + \beta_3 CAM_{t-1} + \beta_4 IM_{t-1} \quad (6)$$

Here: Δ denotes the first difference operator

ε_t - is the random error term t is the time period.

α_0 - is the constant.

α_{1i} - is the coefficient of the dependent variable lagged from one.

α_{2i} to α_{4i} - are the coefficients of the independent variable.

β_1 to β_4 - are the coefficients of the level lagged value of the variables.

The other variables are as stipulated before. The appropriate values for the maximum lags are p , q_1 , q_2 and q_3 . These were established using the Akaike Information Criterion (AIC). The summation operator implies that in each case, summation ranges from 1 to p , 0 to q_1 , 0 to q_2 and 0 to q_3 , respectively. The null hypothesis of the F test is that there is no long run relationship between all the series, that is,

$$H_0: \beta_1 = \beta_2 = \beta_3 = \beta_4 = 0;$$

Against the alternative hypothesis that

$$H_1: \beta_1 \neq 0 \text{ or } \beta_2 \neq 0 \text{ or } \beta_3 \neq 0 \text{ or } \beta_4 \neq 0.$$

To test for cointegration, the obtained F statistics is compared to the crucial values given by Narayan (2005). If the calculated F statistics exceeds the upper critical values of Narayan (2005), then cointegration exists. If the F statistic is less than the lower critical value, the null hypothesis also is not rejected. If the F statistic lies between the lower and upper boundaries in Narayan (2005), the test is inconclusive. If there is cointegration, an error correction model shall be estimated to study the short-term dynamics of the model.

Long Run Model

After it has been found that variables are cointegrated, the long-run relationships between variables shall be examined using the ARDL approach based on the following long-run model.

$$MCR = \alpha_0 + \sum \beta_{1i} PLR_{t-i} + \sum \beta_{2i} SR_{t-i} + \sum \beta_{MTRi} MTR_{t-i} + \sum \beta_{MPRi} MPR_{t-i} + e_{it} \quad (7)$$

Where α_0 , is the constant and α_1 , σ_i and β_i are long run coefficients. A variable significantly impacts economic gross if its associated probability value is less than 10%.

Empirical Results

Table 1: Test of Stationarity

Variable	ADF Stat	MacKinnon @ 1%	MacKinnon @ 5%	MacKinnon @ 10%	Order of integration
MCR	-1.462393	-3.653730	-2.957110	-2.617434	1(0)
MPR	-3.110801	-3.046342	-2.954021	-2.615817	1(I)
MTR	-2.435161	-3.646342	-2.954021	-2.615817	1(0)
PLR	-3.737808	-3.646342	-2.954021	-2.615817	1(I)
SR	-3.134761	-3.646342	-2.954021	-2.615817	1(I)

Source: Author's Computation using E-view, 2026

The results obtained by E-view version 9.0 are presented above. The first Unit root test was Augmented Dickey-Fuller Test at Level for each variable. And the results as presented in the table above shows that the variables are stationary, because all the absolute values of the Test

statistics regardless of their signs were above than the values of 5% critical value. Thus, the variables are stationary at 1(0) and 1(I). We reject the null hypothesis of non-stationarity and conclude that stationarity in first difference exists.

Table 2: F-Bounds Test

		Null Hypothesis: No levels relationship		
Test Statistic	Value	Signif.	I(0)	I(1)
			Asymptotic: n=1000	
F-statistic	6.922438	10%	2.2	3.09
k	4	5%	2.56	3.49
		2.5%	2.88	3.87
		1%	3.29	4.37
Actual Sample Size	31		Finite Sample: n=35	
		10%	2.46	3.46
		5%	2.947	4.088
		1%	4.093	5.532
			Finite Sample: n=30	
		10%	2.525	3.56
		5%	3.058	4.223
		1%	4.28	5.84

Source: Author's computation using E-view, 2026.

From the ARDL bounds test result, it is clear that there is a long run relationship amongst the variables. This is because the computed F-statistic of about 6.922438 is higher than the upper critical bounds at 1%, 2.5%, 5% and 10% critical values. This provided evidence to reject the null hypothesis

of no cointegration at 5% and 10% significance level for the growth model. It can therefore be concluded from the ARDL bounds test that there is a long-run relationship among the variables.

Table 3: ARDL Short Run Model

Selected Model: ARDL(4, 1, 4, 3, 3)				
Variable	Coefficient	Std. Error	t-Statistic	Prob.*
MCR(-1)	0.938373	0.290487	3.230350	0.0090
MCR(-2)	-0.444704	0.428984	-1.036646	0.3243
MCR(-3)	1.366997	0.554677	2.464493	0.0334
MCR(-4)	-0.871416	0.345951	-2.518900	0.0304
MPR	-0.031857	0.010691	-2.979685	0.0138
MPR(-1)	0.021341	0.009855	2.165633	0.0556
MTR	0.057031	0.015217	3.747948	0.0038
MTR(-1)	-0.007108	0.010611	-0.669879	0.5181
MTR(-2)	0.024448	0.013471	1.814836	0.0996
MTR(-3)	-0.005208	0.011509	-0.452558	0.6605
MTR(-4)	0.012401	0.007275	1.704564	0.1191
PLR	-0.042562	0.012297	-3.461142	0.0061
PLR(-1)	-0.033462	0.014259	-2.346810	0.0409
PLR(-2)	-0.011248	0.010979	-1.024467	0.3298
PLR(-3)	0.009441	0.010296	0.916964	0.3807

SR	0.035702	0.017449	2.046129	0.0679
SR(-1)	-0.014811	0.021420	-0.691476	0.5050
SR(-2)	-0.067048	0.022807	-2.939752	0.0148
SR(-3)	0.027230	0.022499	1.210301	0.2540
C	1.000898	0.766260	1.306212	0.2207
R-squared	0.999368	Mean dependent var		8.607000
Adjusted R-squared	0.998168	S.D. dependent var		1.731143
S.E. of regression	0.074092	Akaike info criterion		-2.132296
Sum squared resid	0.054896	Schwarz criterion		-1.198165
Log likelihood	51.98444	Hannan-Quinn criter.		-1.833460
F-statistic	832.7081	Durbin-Watson stat		2.154791
Prob(F-statistic)	0.000000			

Source: Author's computation using E-view, 2026

The R^2 in the model is 0.998168; this means that about 99.8% of the variation of the dependent variable MCR is explained jointly by all the independent variables in the model. The explanatory power of the model is very high and is a good fit, leaving about 1% for the unexplained variable. The F- statistics of 832.7081 with probability of 0.000 is highly significant. This means that the independent variables in the model are jointly significant. Durbin Watson statistics of 2.154791 indicate that there is no autocorrelation, since the value 1.80 approximately is within the range of 1.8 and 2.2. It, therefore, implies that the result will be reliable for prediction and policy making.

The findings revealed that the monetary policy rate and prime lending rate had negative and non-significant effects

on market capitalization. However, the one-period lagged values of the savings rate and money market rate had positive and significant effects on market capitalization. These results indicate an inverse relationship between interest rate policy and market capitalization, suggesting that a unit increase in the monetary policy rate in Nigeria leads to approximately a 0.5% non-significant decrease in market capitalization. Similarly, the prime lending rate was inversely related to market capitalization, although the relationship was statistically insignificant. In contrast, the one-period lagged savings rate and money market rate exerted positive and significant effects on market capitalization, indicating that changes in these interest rate variables may influence stock market development with a time lag.

Table 4: ARDL Long Run Form and Bounds Test

Conditional Error Correction Regression				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.838323	0.423055	1.981591	0.0614
MCR(-1)*	-0.035307	0.029348	-1.203027	0.2430
MPR(-1)	0.001066	0.007589	0.140428	0.8897
MTR**	0.015326	0.009540	1.606592	0.1238
PLR**	-0.030003	0.008843	-3.392806	0.0029
SR(-1)	-0.006946	0.008441	-0.822828	0.4203
D(MCR(-1))	0.288978	0.174940	1.651866	0.1142
D(MPR)	-0.012379	0.008107	-1.526856	0.1425
D(SR)	0.027850	0.015738	1.769629	0.0920
D(SR(-1))	0.016549	0.013895	1.191048	0.2476
D(SR(-2))	-0.022493	0.016327	-1.377625	0.1835
Levels Equation				
Case 2: Restricted Constant and No Trend				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
MPR	0.030185	0.213604	0.141313	0.8890

MTR	0.434087	0.557618	0.778467	0.4454
PLR	-0.849785	0.631715	-1.345203	0.1936
SR	-0.196720	0.187801	-1.047491	0.3074
C	23.74410	9.261685	2.563691	0.0185
EC = MCR - (0.0302*MPR + 0.4341*MTR -0.8498*PLR -0.1967*SR + 23.7441)				

Source: Author's computation using E-view, 2026

Table 4 presents the ARDL long run results; the long run result shows that monetary policy rate and prime lending rate have negative long run effect on market capitalization ratio while savings rate and money market rates have positive effect on market capitalization ratio within the periods covered in the study.

Table 5: ARDL Error Correction Regression

ECM Regression				
Case 2: Restricted Constant and No Trend				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(MCR(-1))	0.288978	0.123415	2.341519	0.0297
D(MPR)	-0.012379	0.005207	-2.377303	0.0275
D(SR)	0.027850	0.010362	2.687785	0.0142
D(SR(-1))	0.016549	0.009902	1.671261	0.1102
D(SR(-2))	-0.022493	0.010442	-2.153997	0.0436
CointEq(-1)*	-0.035307	0.006509	-5.423862	0.0000
R-squared	0.647235	Mean dependent var		0.207097
Adjusted R-squared	0.576682	S.D. dependent var		0.118945
S.E. of regression	0.077389	Akaike info criterion		-2.107953
Sum squared resid	0.149727	Schwarz criterion		-1.830407
Log likelihood	38.67327	Hannan-Quinn criter.		-2.017480
Durbin-Watson stat	1.933949			

Source: Author's Computation using E-view, 2026

The co-integration equation has a value of -0.035307 with a corresponding probability value of 0.0000 which is statistically significance at 5%. This implies that there may be a distortion in short runs which will be corrected in the long run via adjustment mechanism. This indicates that short term distortions in the variables are of enormous importance in their long-term relationship and 3.5 % of this disequilibrium is corrected in the current period. The above results enable us to present the long run ARDL results.

Discussion of Findings

The results also exhibit that the independent variables together explain around 99.8% of the variation in a dependent variable (market capitalization ratio (MCR)). This model has very high explanatory power as nearly 100% of the variances can be explained by these variables leaving only 0.2% unexplained variance within the model (low overall model misfit). The financial policy rate and prime lending had insignificant negative effect on financial sector development denoted as market capitalization. Only the one period lags of savings rate and money market rate significantly developed the financial sector positively. This

could explain the very inverse relationship between money market and prime rates as compared to development in the financial sector, a measured by market capitalization (policymakers have quite large TEI). In particular, a unit increase in the monetary policy rate was associated with an approximate 0.5% statistically non-significant reduction of market capitalization. For the prime lending rate, there was also an inverse relationship with market capitalization; however, this variable was not statistically significant. Conversely, the one-period lagged savings rate and money market rate had positive significant impacts on market capitalization suggesting that changes in these rates might influence financial sector development with a time lag.

Findings corroborate with those provided by Toby and Zaagha (2020) on the empirical link between monetary transmission channels and funding of private sector in an evaluated country: Nigeria- as claimed in their paper where they employed Ordinary Least Squares (OLS), Augmented Dickey-Fuller test, Johansen cointegration test, normalized cointegrating equations relating to different shocks, a parsimonious Vector Error Correction Model pairwise

causality tests. These results are also consistent with the hands of Adebayo and Kolawole (2022), who stated that private sector credit is negatively influenced in the short run by three policy tools [monetary policy rate, cash reserve ratio, and repo rate], while broad money supply retains a positive long-run influence. A similar result is provided by Tobins and Mambo (2012) who report that a 1% tightening of monetary policy decreases investment by 2.63%, with an expansionary monetary policy having the opposite effect in a similar measure. These results are in line with those of Adelegan (2018), which demonstrated that the prime lending rate negatively impacted on output but were statistically insignificant. Similarly, in a study conducted by Ezeanyej and Okoro (2016), it was shown that even during periods of an expansionary monetary policy, SMEs continued to be rationed credit as a result of high perceived default risk due to inadequate collateral and poor credit history. Ajayi & Atanda (2019) further derived a statistically significant negative relationship between private sector credit and interest rates. There are some constancies in the ability of interest rates, lagged monetary conditions and one measure of financial sector activity to potentially exert influence over investment and credit allocation, however the extent and significance with which each can affect particular economic behaviour is delicate across different time periods and various indicators of financial market development.

Conclusion And Recommendations

Conclusion

This study examined the effect of interest rate policy and stock market capitalization in Nigeria findings revealed that found 99.8% of the variation in market capitalization was explained jointly by interest rates in the model. Monetary policy rate and prime lending rate had negative and non-significant impact on market capitalization. The study revealed that the one period lag of savings rate and money market rate had positive and significant impact on market capitalization, interest rate policy and by market capitalization from this result showed that they are inversely related pointing that a unit increase in monetary policy rate in the country causes about 0.5% non-significant decrease in market capitalization.

Recommendations

- i. Monetary authorities should encourage banks to sustain moderate lending rates that promote borrowing for productive investment without crowding out low-risk borrowers.
- ii. The study revealed that monetary policy rates had a negative and significant effect on private sector credit, meaning that tight monetary policies constrain lending.

- iii. The Central Bank of Nigeria should adopt a balanced approach to interest rate adjustments to avoid over-constraining private sector financing.

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