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Gulf Journal of Advance Business Research
FE Gulf Publishers.
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Social Finance Model and the Banks' Financial Stability in Nigeria: Emphasis on Depositors' Safety Net Banking Scheme

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Volume No: 2	Issue No: 2	Page No: 140-150
Received: 15-01-24	Accepted: 25-02-24	Published: 27-03-24

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Abstract

This study examined the effect of social finance model affects the Nigerian banks' financial stability from 2001 to 2021 with emphasis on depositors' safety net banking scheme. The depositors' safety net banking scheme was measured by insured number of depositors, liquidation dividend, total bank deposits and total bank insured premium while bank z-score served as measure of banks' financial stability. The study covered all the 23 quoted DMBs in Nigeria as at 31st December, 2021. Data for the study were sourced from both the Central Bank of Nigeria (CBN) Statistical Bulletins and the Nigeria Deposit Insurance Corporation financial reports for the period of this study from 2001 to 2021. The Robust least square estimation technique was used to run the analysis. The study reported that, both number of deposits insured and the premium paid by banks for the insurance of their deposits improved banks' financial stability meaningfully while total bank deposits only improve banks' financial stability minimally. However, liquidation dividend reduced banks' financial stability significantly throughout 2001 to 2021. Hence, the paper concludes that the NDIC has been very effective in ensuring increase in the number of depositors insured and has ensured prompt remission of premium by banks. As such, the NDIC should extend their coverage to non-bank financial institutions as this will ensure overall stability of the financial system. The study is the first of its kind in the Nigerian context to analyze the effect of NDIC operations on the financial stability of DMBs in Nigeria.

Keywords: Depositors' Safety Net Banking Scheme, Banks' Financial Stability, NDIC Operations.

INTRODCUTION

One of the central goals of policy makers globally is to ensure that the banking system is relatively stable. This is because, if the banking industry is not relatively stable, the whole economic activities would be greatly affected (Onuarah, Arubayi, & Olannye, 2020; Erhijakpor, Enakirerhi, & Eferakeya, 2020). One attempt to make the banking industry to be relatively stable was the introduction of depositors' safety net scheme popularly termed Nigerian Deposit Insurance Corporation (NDIC). This is built on the four hall mark of financial intermediation which is cost, convenience, confidence, and consistence. In the case of Nigeria, the NDIC was established on the 15th day of June, 1988 following the report made by the committee which was set up by the apex bank (CBN) in 1983 to establish a depositors' trust fund saddled with the sole responsibility of examining both bank operations and at the same time ensuring that, depositors' funds are safe should a bank liquidates. For purposes of regulatory concerns, NDIC kicked off formally in 1989.

According to the NDIC report (2023), the establishment of the NDIC was one of the major reform measures carried out by the apex bank to restore confidence in the banking industry, strengthen the banking sector's safety net consequent upon its liberalization policy alongside the introduction of the Structural Adjustment Programme (SAP) in 1986. The rationalization was that, though, the introduction of the SAP in 1986 led to the increase in the numbers of Nigerian banks from 40 to 120 between 1986 and 1992 respectively, it led to various sharp cases most of which include the following: enthronement of inept manpower, enthronement of people of questionable characters, increased unhealthy competition in the Nigerian banking industry. Hence, NDIC was established to carry out both routine and special examinations on all licensed Nigerian banks alongside the CBN. Another rationale while NDIC was established according to the NIDC report (2022) was that, avoid the untold hardship recorded when 21 banks out of the 25 banks liquidated in the 1950s. Again, since Czechoslovakia being the first country in the world to adopt this banking model in 1924 used the scheme/model to revitalize the country's banking system after the First World War and that, cases of bank collapse and panic withdraw in the US stop due to the establishment of the Federal Deposit Insurance Corporation (FDIC) in 1933, Nigerian government also followed suit to adopt her own deposit scheme.

Furthermore, informed by the unwillingness of the Nigerian government to let Nigerian banks failed since the government are major stakeholders of most of these banks, the NDIC was established to build a reliable banking system and guarantee higher returns to investors, CBN and NDIC was given the statutory duty to supervise banks activities in Nigeria (Osuji, 2019). Notwithstanding the NDIC's enforcement oversight, banks have persisted in facing difficulties, leading to the majority of them merging in order to achieve stability and consolidation. For example, Prudent Bank, Bond Bank, Reliant Bank, and Corporative Bank combined to establish Sky Bank in order to avoid impending failure (Onuorah, 2020). 2019 saw the name Sky Bank being changed to Polaris Bank. In an attempt to prevent complete bank bankruptcy, First Inland Bank rebranded as First City Monument Bank (FCMB) in 2008. It was previously doubted if the NDIC could successfully oversee and regulate the activities of the banking industry when Intercontinental Bank amalgamated with Access Bank, which then combined with Diamond Bank to avoid collapsing owing to protracted distresses (Olaruwaju, 2016). This made some

wonder how effective NDIC supervision has impacted on the Nigerian banking industry's financial stability.

It is also depressing to note that, despite the large number of studies on Deposit Insurance Schemes (DIS), most earlier researches focused primarily on developed economies in Latin America, Great Britain, the United States, and the European Union (Alyeksyeyev & Mazur, 2018; Jameaba, 2018), with relatively few empirical studies on economies in Sub-Saharan Africa (Ani & Ogar, 2018; Onuorah, 2020; Ebiaghan, 2019; Jeroh & Ebiaghan, 2018). Therefore, by objectively evaluating the impact of NDIC activities on the financial stability of deposit money banks in Nigeria, this study seeks to close this information gap. The following hypotheses were generated for the study;

Ho_1: Total numbers of depositors insured does not affect Nigerian banks' financial stability significantly

Ho_2: Liquidation dividend does not affect Nigerian banks' financial stability significantly

Ho_3: Total bank deposits do not affect Nigerian banks' financial stability significantly

Ho_4: Total bank insured premiums do not affect Nigerian banks' financial stability significantly

LITERATURE REVIEW

Conceptual Linkages

Social Finance Model: Depositors' Financial Safety-Net and Financial Stability

The depositors' financial safety net, as defined by Anginer and Demirgüç-Kunt (2018), is a crucial banking model (social finance model) that most governments provide in an effort to save their own banking systems. According to Ani and Ogar (2018), the term "depositors' financial safety-net" refers to the financial guarantee that has been put in place by the relevant authorities expressly to safeguard depositors by ensuring the stability and security of the nation's whole banking system. Depositors are therefore guaranteed the security of their money and that the collapse of one bank does not imply the failure of every other bank in the system thanks to the implementation of DIS (Ehiedu, 2022; Ani & Ogar, 2018).

The idea of "financial stability" is not easy to grasp. This is a result of its complex character. Financial stability may be defined as the lack of financial instability. Stated differently, it is a state in which monetary policy and macroeconomic shocks are not easily absorbed by the financial system, comprising of institutions, markets, and intermediaries. A financial system is considered stable, according to the World Bank Group (2016), if it can dissipate financial imbalances that arise naturally or as a result of notable unfavorable (negative) economic conditions. Financial stability, according to Erhijakpor et al. (2022), is the state in which the financial market, institutions, and infrastructure are able to withstand challenging economic situations. As such, a robust banking sector can withstand both typical and unusual financial loss shocks, the author continued (Onuorah, 2022).

From the standpoint of the chosen variables—the total number of bank deposits covered, the total amount insured, the total bank issued premium, and the percentage of liquidation dividend provided to customers—it is possible to relate deposit insurance activities to the stability of the bank. Below is an explanation of these relationships:

i. The likelihood of bank stability increases with the total volume of insured bank deposits.

ii. The chance of bank stability increases with the entire amount insured.

iii. A lower liquidation dividend value raises the risk of bank instability. iv. A lower total bank insured premium value raises the risk of bank instability.

Theoretical Review

The Hands-on theory and the Regulatory Restraint theory served as the foundation for the article. In order to safeguard its interests, the insurer, according to the Hands-on principle, should first require covered banks to keep their portfolios at a risk level that corresponds to the cost of deposit insurance. The present improvements to bank regulations are based on the hands-on principle. The "traditional" theory of moral hazard, which holds that moral hazard, may be mitigated by varying insurance premium prices for various insurers based on the risk that each insured poses to the insurer, is the source of inspiration for the variable premium theory. Meanwhile, the regulatory restraint theory (RRT) stresses that, deposit insurance is unnecessary as the costs associated with moral hazard outweigh the benefits (Ebiaghan, 2019). The idea that insured deposits should only be accepted at distinct institutions that hold government securities portfolios and do not take uninsured deposits is supported by the segregation hypothesis. This idea has a lot of appeal since it would remove the moral hazard associated with deposit insurance.

Empirical Studies

Since the advent of the NDIC, there seems to be few empirical investigations on their activities. Recently, Onuorah et'al (2020) examined the relationship between bancassurance and insurance Firms' income in Nigeria from 1996 to 2017. Error correction model (ECM) results suggested that Bancassurance Convergence (BANS), Interest on Credit facilities (INTR) and Total Investment (TINV) improved insurance Firms' income in Nigeria from 1996 to 2017 significantly.

Ebighian and Jeroh (2020) assessed the extent Deposit Insurance Funds (DIF) has affected the quality of Nigerian banks' asset base. They focused on entire 15 listed DMBs while their data coverage spanned from 1989 to 2017. The ARDL model was used. They evidenced that, the volume of total deposits and total loans and advances of DMBs have long run negative and statistically significant relationship with DIF. Conversely, the quality of Nigerian banks' asset base improved minimally with the target reserve ratio of DMBs.

Nwanyanwu, Igbara, and Njoku (2020) investigated the nature and the extent of the impact of Nigeria Deposit Insurance Corporation activities on performance of banks in Nigeria from 1990 to 2018. Secondary data were sourced from NDIC, CBN and Statistical Bulletin of various years covering the period 1990 to 2018. OLS method was adopted to estimate the model parameters and test the hypotheses. The results revealed that total depositors insured have a significant relationship with banks' returns on assets while liquidation dividends paid to the banks' shareholders reduced banks' returns on assets.

Ebiaghan (2019) investigated the nexus between the moral hazard hypothesis and the adoption of the DIS in Nigeria. Using the secondary data sourced from the NDIC annual reports and accounts, the Generalized Method of Moments (GMM) was used for the analysis. The study revealed that the asset quality indicators of Nigerian banks improved due to deposit insurance fund.

Osuji (2019) did an explorative on the origin, evolution, and contributions of the NDIC on the financial stability of deposit money banks in Nigeria. The study adopted the documentary

approach. The study reaffirmed that, apart from insuring the deposit liabilities of all licensed banks, the establishment of NDIC has no doubt, generated the required stability and confidence through its activities in the Nigerian Financial System

Bonfim and Santos (2019) examined the Portuguese depositors' attitudes. After the adoption of deposit insurance in Cyprus, they discovered that the insured Portuguese depositors exhibited an inclination to reduce their savings in smaller, less profitable banks.

In their study comprising a relatively large sample of countries, Calomiris and Chen (2018) discovered that the introduction of deposit insurance orchestrated higher debt-to-equity ratios and higher loan-to-asset ratios, which resulted in incessant bank defaults as a result of higher leverage and asset risk.

A similar view was canvassed in the research study conducted by Ngalawa, Tchana and Viegi (2016) who argued that the costs imposed by moral hazard far outweighed the perceived benefits of deposit insurance.

In their study, Sahadewo, Purwanto and Pradiptyo (2018) simulated laboratory experiments, involving actual bankers to assess the impact of the implementation of a differential premium regime on the bankers' attitude and found no significant relationship between the deposit offer rate and the coverage limit regimes. Equally, they found out that the coverage limits for the deposits had smaller banks to take on more risky projects, thus evidencing moral hazard especially within small banks.

Chang (2018) employed a comprehensive data set covering 189 countries from 1960 to 2015, and a Heckman two-step selection model to investigate determinants of deposit insurance coverage. The study finds that that there may be higher banks' risk-taking incentives in developing countries after setting up explicit deposit insurance system.

Leepsa and Singh (2017) did a case study on the contribution of bancassurance strategy on the performance of axis bank because it acquired stack in the Max New York Life Insurance Co. Ltd. The study revealed that, the acquisition of the stake in Max New York Life Insurance by axis bank improved it performance. However, the acquisition does not yield any impact on the stock market return on the short-run.

In Nigeria, Ume, Oleka, and Obasikene (2017) carried out a theoretical review on the phenomenon of moral hazard and harped on the necessity to institute deposit insurance as a financial safety net; those efforts, however, should be intensified so as to mitigate the untoward consequences of moral hazard, which is an unintended offshoot of the DIS implementation.

De Caux, McGroarty and Brede (2017) analyzed the long-term costs and benefits of bailout strategies in banking systems. They found that bailouts serve as effective tools that limit the occurrence of bank failures in the short-run. However, inappropriate intervention strategies hearten risk-taking, which renders bailouts inefficient and disadvantageous to long-term system stability.

Deli and Hasan (2016) examined the effects of bank capital regulation on loan growth by using bank-level data from 125 countries within the period of 1998 to 2011. The results indicated that capital regulation only has a weak negative effect on loan growth. Moreover, the effect is entirely offset when banks hold moderately high levels of capital. However, they found that the components of capital requirements that have the most significant negative effect on loan growth

are those associated with the prevention of banks to utilize as capital borrowed funds and assets other than cash or government securities.

Nwakoby, Onwumere, and Ibe (2016) evaluated the effect of a deposit insurance scheme on bank intermediation in the Nigerian banking industry. Using the OLS regression, they confirmed that, NDIC operations have impacted meaningfully on the Nigerian financial intermediation process.

Peng, Jeng, and Wang (2015) examined the whether the bank performance and efficiency of banks are enhanced by bancassurance business in Taiwan from 2004 to 2012. The study adopted the multivariate regression approach. The reaffirmed that, banks that adopt bancassurance tend to accrue greater risk-adjusted returns that banks that does not.

METHODOLOGY

The study adopted the ex-post facto and analytical research designs. The choice hinged on two reasons. Firstly, the study relied on data obtained from the Central Bank of Nigeria Statistical Bulletin and Nigeria Deposit Insurance Corporation financial reports, as such, the events under investigation have already taken place and the researcher does not intend to control or manipulate the variables. Since both the sample size of 21 Nigerian banks equals with the population, the census sampling technique was considered. The study extracted data from the CBN Statistical Bulletins and the Nigeria Deposit Insurance Corporation financial reports from 2001 to 2021, processed the data, collated the data and discussed the data using E-Views 9.0. The Robust Least Square Estimate was used for the analysis. This study adapted the models of Nwanyanwu, Igbara, and Njoku (2020). Unlike their models that captures the effect of NDIC operations on bank performance; our model captures the effect of NDIC operations on the financial stability of DMBs in Nigeria. Hence, the modified model is stated as:

$$FIST = \beta_0 + \beta_1 TNDI + \beta_2 TBIP + \beta_3 TBDS + \beta_4 LIQD + \beta_5 EXCR + \beta_6 INFR + \mu_{it} \text{----------(1)}$$

β_0 = Constant Value

$\beta_{1-} \beta_6$ = Parameter Estimates

Table 1

Analysis of Study Variable's Aprioiri (Economic) Expectations

Denotation	Study Variable	Description	Nature of Variable	Aprioiri Expectation
FIST	Financial Stability	Z-score	Dependent	Nil
TNDI	Total numbers of depositors insured	Volumes of Total numbers of depositors insured	Independent	+
LIQD	Liquidation dividend	Volumes of liquidation dividend	Independent	+
TBIP	Total bank insured premiums	Volumes of total bank insured premiums	Independent	+
TBDS	Total bank deposits	Volumes of total bank deposits	Independent	+
INFR	Inflation Rate	Consumer Price Index	Control	-
EXCR	Exchange Rate	Naira to US Dollar	Control	-

Source: Researcher's Compilation (2023)

RESULT AND DISCUSSIONS

Data Analysis

Prior analyzing the sourced data, the study used the descriptive statistics to explain the behaviours of the study variables. The result is therefore presented thus:

Table 2
Descriptive Statistics

Variables	Mean	Maximum	Minimum	Std. Dev.	Observations
FIST	15.47962	20.06930	11.16120	2.650616	21
TNDI	9965.091	37613.04	499.1615	10419.38	21
TBIP	32419.91	456352.0	520.9500	98669.81	21
TBDS	243869.9	535815.0	38687.00	113634.7	21
LIQD	34.40405	116.2580	3.130000	32.22206	21
EXCR	193.6067	414.0000	111.9400	90.75765	21
INFR	17.28524	24.85000	11.55000	2.735591	21

Source: E-Views 9.0 2023

Table 2 revealed that the covered 21 observations which is the periods of 21 years (2001 to 2021). From the table, the mean and standard deviation for TBIP is ₦32419.91 billion and ₦98669.81 billion. The high standard deviation value indicates that TBIP deviated much away from the mean value. Meanwhile, it reported a maximum and minimum values of ₦456352.0 billion and N520.9500 billion respectively.

More so, TNDI, LIQD, TBDS, EXCR, and INFR reported average/mean values of ₦9965.091 billion, ₦34.40405 billion, ₦243869.billion, 15.47962 billion, ₦193.61, and 17.28% respectively. However, it deviated by ₦10419.38 billion, ₦32.22206 billion, ₦113634 billion, ₦2.65 billion, ₦90.75765, 2.74%. This reveals that, majority of the study variables clustered around their mean values. This signals that, the study variables a fit for parametric analysis. Again, they reported maximum values of ₦37613.04 billion, ₦116.2580 billion, ₦535815 billion, ₦20.06930 billion, ₦414, and 24.85% respectively but had minimum values of ₦499.1615 billion, ₦3.13 billion, ₦38687.00 billon, ₦11.16120 billion, ₦111.9400, and 11.56% respectively.

Consequent upon the above, the normality test for each of the study variables are presented in table 3:

Table 3
Normality Test Using Jarque-Bera

Variables	Jarque-Bera	Probability	Observations	Conclusion
FIST	0.898572	0.638083	21	Normally Distributed
TNDI	7.144777	0.028089	21	Departure from Normality
LIQD	2.299290	0.316749	21	Normally Distributed
TBDS	1.845276	0.397469	21	Normally Distributed
TBIP	251.5626	0.000000	21	Departure from Normality
EXCR	4.585917	0.100967	21	Normally Distributed
LER	3.602136	0.165122	21	Normally Distributed

Source: E-Views 9.0 2023

Table 4
Correlation Matrix

	FIST	TNDI	LIQD	TBDS	TBIP	EXCR	INFR
FIST	1.000000						
TNDI	0.705131	1.000000					
LIQD	0.602882	0.229557	1.000000				
TBDS	0.667876	0.232457	0.253423	1.000000			
TBIP	-0.245394	0.067606	0.205876	0.263328	1.000000		
EXCR	0.758305	0.150281	0.231111	0.181488	0.036502	1.000000	
INFR	-0.501645	-0.385840	-0.037787	-0.091829	-0.318835	-0.172423	1.000000

From the general correlation test result as shown above, the standard correlation between independent variables are very low, indicating that there is little or no chance of multicollinearity in the data. The correlation within Total numbers of depositors insured is the highest in the correlation matrix, with correlation coefficient value being (-0.385840) but this score for correlation is minimal and acceptable as a low level of correlation. The emphasis on correlation is because the presence of multicollinearity in a set of data forces the standard error to go up, and then in reverse, forces the t-statistics to be low. Hence, the lower the value of the t-statistics, the higher the probability value (i.e. P-value). To further buttress this, the variance inflation factors-VIF Values stated in table 5 evidenced that, the model is free from Multicolinearity problem since their VIF values are below 10.

Table 5
Variance Inflation Factors-VIF
Date: 03/03/23 Time: 05:40
Sample: 2001 2021
Included observations: 21

Variable	VIF
TNDI	1.157478
TBIP	1.451362
TBDS	1.344561
LIQD	1.258766
EXCR	2.457735
INFR	2.425515

Source: E-Views 9.0 2023

Result Presentation and Discussion

Since the Robust Least Square-RLS Estimation technique account for over parametization of study variable, the study adopted the RLS estimation technique. It is therefore estimated in table 6:

Table 6
Robust Least Squares Estimate
Dependent Variable: FIST
Method: Robust Least Squares
Sample: 2001 2021
Included observations: 21

Variable	Coefficient	Std. Error	z-Statistic	Prob.
C	8.009171	1.326653	6.037125	0.0000
TNDI	0.872084	0.317205	2.749276	0.0157
LIQD	0.025335	0.010966	2.310287	0.0366
TBDS	0.013261	0.064319	0.206174	0.8396
INFR	0.000706	0.016882	0.041799	0.9672
LER	-0.001849	0.003852	-0.480043	0.6386

.	Robust Statistics		
R-squared	0.861668	Adjusted R-squared	0.848890
Rw-squared	0.925073	Adjust Rw-squared	0.892961

Deviance	77.39627	Scale	2.060864
Rn-squared statistic	28.80806	Prob(Rn-squared stat.)	0.000000
Non-robust Statistics			
Mean dependent var	15.47962	S.D. dependent var	2.650616
S.E. of regression	2.380662	Sum squared resid	85.01326

Source: E-Views Version 9.0 (2023)

The study of the effect of NDIC operations and financial stability of DMBs in Nigeria has brought to limelight the extent to which the NDIC operations has helped banks in maintaining the financial stability of DMBs in Nigeria. The study reported that, on the overall, NDIC operations improve the stability of DMBs in Nigeria. Meanwhile, the R-squared, adjusted R-squared, Rw-squared, and Rw-squared values all evidenced that the model has a high predictive power.

Furthermore, the study shows clearly that the knowledge of the existence of the NDIC has helped to Nigerian banks to break even and enhance their limit of liability on insured amounts. By implication, the bank insured premium has also aided the banks to instill confidence in the banking industry. As a result, the higher the number of depositors' insured and total bank insured premium, the more stable/resilient the Nigerian banks become. This portends a significant safe banking practice in Nigeria so far since banks have found a balance between deposit premiums as well as their continued insurance of every depositor's funds in compliance with the NDIC Act 16 of 2006

Again, total bank deposits only improve banks' financial stability minimally. However, liquidation dividend reduced banks' financial stability significantly throughout 2001 to 2021. By implication, the more customers the bank gets, the more stable the banking industry becomes though it is still not significant enough at the moment. This is in tandem with Alyeksyeyev & Mazur, 2018; Jameaba, 2018; Onuorah et'al (2020); Ebighian and Jeroh (2020); Nwanyanwu, Igbara, and Njoku (2020) findings but is at little variance with Calomiris and Chen (2018); Ngalawa, Tchana and Viegi (2016); Sahadewo, Purwanto and Pradiptyo (2018) findings.

On the other hand, from 2001 to 2021, the liquidation dividend severely weakened the financial stability of banks. Negative indicators indicate that the NDIC will not pay the liquidation dividend and that the very low total amount of bank deposits was insufficient to support the financial stability of DMBs in Nigeria. On the other hand, the lack of significance of liquidation dividends indicates that Nigeria's deposit insurance program has not adequately protected shareholders in the event of partial or complete bank liquidation. It may also be noted that certain DMBs' failure to satisfy their deposit obligations to the Corporation and inadequate deposits with the NDIC are the reasons why this variable deviates from expectations..

CONCLUSION AND RECOMMENDATIONS

The establishment of a deposit insurance system can be more successful when a country's banking system is healthy. However, in order to make the banking system to be healthier, there is need for effective and efficient deposit insurance systems that will guarantee the safety of depositors' funds and in the same vein ensure the continued profitability of banks to meet up with shareholders expectations. Arising from the various findings of this study, the study

concludes that the NDIC has been very effective in ensuring increase in the number of depositors insured and has ensured prompt remission of premium by banks. This has in turn improved public confidence in the banking system and has made DMBs in Nigeria to be relatively stable over the periods studied. Hence, the paper made the following submissions:

i. The NDIC should extend their coverage to non-bank financial institutions as this will ensure overall stability of the financial system since the number of deposits insured improved Nigerian banks' financial stability meaningfully.
ii. The NDIC management should ensure that, banks pay more premiums since premium paid by banks for the insurance of their deposits is highly instrumental to their financial stabilities.
iii. To ensure that Nigerian banks are relatively stable, bank management must put in place aggressive deposit mobilization strategies
iv. The Nigerian banks should ensure that their deposit liabilities are adequately insured without cutting corners by under-valuing their liabilities.

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