

Financial Development as a driver of Investment Ecosystem Expansion: Evidence from Nigeria.

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Abstract: *This study examined the impact of financial development and macroeconomic determinants on gross capital formation in Nigeria based on the annual data covering the period from 2000 to 2024. The ARDL model is used to assess the relationship between gross capital formation (GCF) and credit to the private sector (CPS), broad money supply(M2), assets of the banking sector (BA), stock market capitalization (SMC) in the short run and in the long run. It is found that the variables have a stable long-run relationship, which is supported by the ARDL bounds test and the presence of a significant error correction term. From the findings of the research work, it can clearly be seen that the variables such as CPS and M2 have a very significant positive impact on gross capital formation in both the short and long run, and also BSA and SMC have a positive impact, although not significant. However, there are some negative effects of variables such as inflation rate, interest rate, and exchange rate on investments, and the exchange rate volatility is the most crucial variable among these, which negatively affects capital formation in Nigeria.*

Keywords: Gross Capital Formation; Financial Development; Credit to Private Sector.

1. Introduction

The importance of financial development has increased due to its relevance to economic transformation, especially of emerging economies such as Nigeria (Ibrahim & Alagidede, 2020; Fowowe, 2021; Akomen & Imahe, 2025). Financial development implies the development of financial systems in terms of financial institutions, markets, and financial instruments that would help in the efficient resource mobilization and allocation process. Financial system development is associated with increased funds accessibility, reduced costs and risks, and thus, increased investments (Adekunle & Akinwale, 2022; Babalola & Otekunrin, 2023).

The investment environment has acquired increasing significance for Nigeria in recent decades due to issues such as unemployment, industry underdevelopment, and excessive reliance on oil income. An effective investment environment comprises financial institutions, investors, entrepreneurs, regulatory bodies, and other infrastructure and largely depends on the quality and effectiveness of the financial system. Financial development plays an important role in determining structure, depth, and evolution of the investment environment (Okete & Camillus, 2024; Nuhu & Ismail, 2025). Thanks to its rich history, Nigeria implemented various reforms connected with the finance sector and aimed to improve banking operations and capital market performance. In this respect, the reforms were able to improve the situation in terms of the development of the digital finance sector, capital market operations, and the appearance of new financing possibilities, including fintechs. However, there are several problems in the Nigerian finance sector, like insufficient access to finance, financial exclusion, inefficient regulatory policies, and macroeconomic instability that could influence investment possibilities (Ezeaku & Asogwa, 2022; Ogunmuyiwa & Okunlola, 2022; Umar & Osemene, 2024).

Taking into consideration all information provided in literature about the issue of the connection between financial development and investment growth in Nigeria, it can be said that the connection in question is rather ambiguous. There are lots of studies that state the existence of a positive correlation between the discussed variables (Briggs, 2025; Rogers-Banigo & James, 2025); however, there are also studies that show inefficiencies that impede the establishment of the connection between financial development and investment growth (Maku, 2020; Onisanwa et al., 2021).

1.2 Statement of the Problem

Despite the existence of numerous reforms in the financial sector, Nigeria is still facing challenges related to underinvestment and growth of the investment climate (Okete & Camillus, 2024; Nuhu & Ismail, 2025). From the point of view of optimal financial development, it should facilitate lending, fund allocation, and investments, both domestic and foreign; however, based on the empirical research findings, the above positive effect has not yet taken place in Nigeria (Adekunle & Akinwale, 2022; Babalola & Otekunrin, 2023).

The problem of the inefficient financial intermediation can be an illustration of the above statement because the funds gathered by the financial sector are used inappropriately in order to increase the efficiency of economic sectors (Agu & Nwachukwu, 2021; Umar

& Osemene, 2024). The SME sector is essential for the process of economic growth but faces problems associated with access to finance due to high costs of funding, tough lending conditions, and lack of collateral (Maku, 2020; Oyadeyi, 2024). Moreover, despite witnessing the growth of the country's banking sector and capital market, financial inclusion is still quite low, especially in rural areas, thus restricting people from participating in investments and making the whole investment ecosystem less effective (Akomen & Imahe, 2025; Rogers-Banigo & James, 2025). The number of people who are either unbanked or underbanked in Nigeria is huge, which limits the ability to convert their savings into investments.

Also, the Nigerian financial system is very volatile and weak as it involves macroeconomic instability, namely high rates of inflation and exchange rate volatility (Ezeaku & Asogwa, 2022; Salisu & Isah, 2020); inconsistent regulation of the financial market; and overreliance on short-term capital movements instead of long-term investments, such as foreign direct investments (Fapetu et al., 2022; Ogunmuyiwa & Okunlola, 2022). Thus, it is hard not to ask some crucial questions regarding the effectiveness of financial development in the process of investment ecosystem development in Nigeria.

Hence, this study aims at covering the identified gap and revealing the role of financial development in the process of investment ecosystem expansion in Nigeria.

1.3 Objectives of the Study

Then main objective of the study is to investigate the role of financial development in driving the expansion of the investment ecosystem in Nigeria. The specific objectives are:

1. To study the effect of credit to the private sector on the growth of Nigeria's investment ecosystem.
2. To analyze the impact of broad money supply on the growth and development of the investment ecosystem.
3. To evaluate the influence of bank assets on the development of Nigeria's investment ecosystem.
4. To explore the role of stock market capitalization in the growth of the investment ecosystem.

2. Literature Review

2.1 Conceptual Review

2.1.1 Financial Development

Financial development is fundamental to the expansion of the investment ecosystem, since it offers the necessary resources, accessibility and efficiency to undertake investments. Financial development improves financial intermediation, capital allocation, and the linkage between savings and investments in an economy (Fowowe, 2021; Ibrahim & Alagidede, 2020). In the current research, the concept of financial development has been evaluated through four important variables, namely, credit to the private sector, broad money, financial inclusion and stock market capitalisation. Each of these variables acts differently in promoting the growth of the investment ecosystem in Nigeria (Adekunle & Akinwale, 2022; Nuhu & Ismail, 2025).

2.1.1.1 Credit to the Private Sector (CPS)

Private sector credit is defined as the amount of finance channelled by banks to the businesses and business people in order to invest in production processes and is a major determinant of financial intermediation efficiency (Babalola & Otekunrin, 2023; Agu & Nwachukwu, 2021). The increase in CPS in Nigeria leads to increased financing of businesses, especially SMEs, for growth, technological advancements, and growth. It is empirically established that private sector credit significantly affects investment and capital formation, although its efficiency is dependent on the way it is allocated (Okete & Camillus, 2024; Ogunmuyiwa & Okunlola, 2022).

2.1.1.2 Broad Money Supply (M2)

The broad money supply (M2) refers to the sum total of money in the economy, including cash in hand, demand deposits, and near-money instruments, and is an indicator of the efficiency of the financial system in facilitating investment transactions (Briggs, 2025; Akomen & Imahe, 2025). An increase in M2 in Nigeria results in increased availability of capital for the businesspeople and

households, hence increasing investment opportunities in productive and financial investments. It has been proved that monetary expansion has a critical role in investment growth (Nuhu & Ismail, 2025; Oyadeyi, 2024).

2.1.1.3 Financial Inclusion

Financial inclusion refers to the provision of access to and usage of financial services among individuals and businesses that were not using financial services before through banking and digital financial services (Agu & Nwachukwu, 2021; Umar & Osemene, 2024). In Nigeria, the emergence of fintechs, mobile banking, and agent banking makes sure that there are many financial services provided to individuals and businesses, hence increasing their engagement in the investment environment. According to the findings, financial inclusion improves savings and investment capabilities of individuals and businesses, especially small businesses and rural areas (Adekunle & Akinwale, 2022; Akomen & Imahe, 2025).

2.1.1.4 Stock Market Capitalisation

Stock market capitalisation refers to the measure used to determine the size and depth of the equity markets. Stock market capitalisation can be used as a measure of capital market development (Rogers-Banigo & James, 2025; Onisanwa et al., 2021). Stock market development in Nigeria offers alternative financing sources for firms, hence reducing the reliance on bank borrowings and investments. Empirical evidence shows that stock market development leads to capital formation and economic activities despite the effects brought about by constraints (Maku, 2020; Fapetu et al., 2022).

2.1.2 Growth of the Investment Ecosystem

Growth of the investment ecosystem involves the creation and enhancement of financial structures that assist in investment and productivity in the economy (Okete & Camillus, 2024; Nuhu & Ismail, 2025). It involves the interaction between financial institutions, investors, regulations, and markets in channelling investments in a proper manner. An investment ecosystem assists in enhancing participation and access to funds in sustainable economic development. The growth of the investment ecosystem is always measured through Gross Capital Formation (GCF), which measures the capacity of an economy to convert financial assets into productive investments (Babalola & Otekunrin, 2023; Briggs, 2025).

2.1.2.1 Gross Capital Formation (GCF)

GCF involves investments in fixed assets such as infrastructure, machinery, buildings, and equipment and is used as a measure of growth of the investment ecosystem (Adekunle & Akinwale, 2022; Rogers-Banigo & James, 2025). The rising GCF levels in Nigeria are reflective of enhanced efficiency in the processes of financial intermediation and development in capital markets. The availability of credit is what aids the process of development, while the availability of money aids in liquidity during investments. Financial inclusion makes it possible for more people to participate in the investment processes, while the capitalisation of stock markets provides financing for long-term investments (Umar & Osemene, 2024; Nuhu & Ismail, 2025). GCF can be considered as the dependent variable here, as the efficiency of the development of financial systems in Nigeria regarding investment ecosystem development can be gauged.

2.2. Theoretical Review

2.2.1 Investment Ecosystem Theory

The most appropriate theoretical framework under which this research can be conducted is the investment ecosystem theory. The Investment Ecosystem Theory explains comprehensively and integratively the process through which financial development leads to gross capital formation. Unlike traditional theories which explain investment as a function of some financial development factors in isolation, the investment ecosystem theory explains investment as a result of interactions between various financial, macroeconomic policy and non-financial variables. Financial development variables such as CPS, M2, BSA, and SMC are the primary drivers of the investment ecosystem. The CPS facilitates easy finance acquisition by the productive sectors; M2 depicts the levels of liquidity in the economy, thus determining the size of investible resources; BSA depicts the strength of the banking system to mobilise savings and allocate credit effectively, while SMC depicts the ability of capital markets to source long-term funding.

Investment ecosystem theory considers the macroeconomic environment from the point of view of its indicators, inflation (INF), interest rate (IR) and exchange rate (EXR). These factors define the confidence of investors, the cost of capital and economic stability, which affect investment results. Higher rates of inflation reduce returns from investments, and fluctuations of exchange rates add

uncertainties and make investors refrain from long-term commitments. Changes in interest rates affect the cost of borrowing and investment decisions of enterprises.

The strength of the theory consists in the consideration of the interconnection of financial development and macroeconomic stability in the explanation of investment results. This means that the theory is more relevant for this study, as it includes the analysis of the interplay between indicators of financial system development, capital market development and macroeconomic environment, which affect gross capital formation in Nigeria. The theory suits the use of the ARDL approach applied in this study because it covers both short-run and long-run equilibrium processes within one system.

Therefore, Investment Ecosystem Theory can be regarded as the most suitable for this study because it provides a comprehensive explanation of the impact of the financial system and macroeconomic environment on the investment process in Nigeria

2.3 Empirical Review

Ajayi & Usman (2025) explored the influence of capital market measures on capital formation in Nigeria between 1990 and 2023 using a regression model. It was revealed that market capitalization, share value traded, and turnover ratio had positive and statistically significant impacts on gross capital formation, suggesting that a more advanced capital market facilitates access to long-term sources of finance and, hence, investments in Nigeria.

Rogers-Banigo & James (2025) conducted research on the effect of stock market liquidity on capital formation in Nigeria, applying the ARDL model. As a result, a positive and significant link between market capitalization and gross fixed capital formation was established, suggesting that stock market development is a vital aspect of attracting investment funds despite the fact that certain liquidity measures have demonstrated insignificant results due to inefficiencies of the market.

Nuhu & Ismail (2025) explored financial sector development and economic growth in Nigeria using the ARDL method. Financial deepening variables like private sector credit and broad money supply were revealed to be having significant effects on economic growth in the long run, implying that financial development increases investment potential and facilitates capital formation.

A study of monetary policy impact on the development of the stock market in Nigeria was carried out by Otsapa, Nande, and Efe (2025). Based on the results, it can be argued that the money supply has a positive relation to the stock market capitalization, while the inflation and interest rate have a negative relation to the stock market development. Therefore, the results reflect the necessity of macroeconomic stability for the investment development within the financial sector.

The effect of financial deepening on economic growth and investments in Nigeria was investigated by Okete and Camillus (2024), applying regression and causality methods. Based on the results, it has been stated that credit to the private sector and stock market capitalization positively influenced investments and economic growth.

A study of stock market development and economic growth in Nigeria was conducted by Maku (2020) using the ARDL method. Consequently, market capitalization and money supply positively affected the economic growth.

Onisanwa et al. (2021) focused on the influence of the development of the stock market and investments in Nigeria, where the authors used the ARDL bounds test approach. It has been found out that there is a long-term connection between stock market indicators and investment growth; therefore, the development of the financial market plays an important role in raising capital.

Ikechukwu and Orumhua (2023) pay attention to the influence of money supply, stock market development, and monetary policy. As a result, the effect of money supply on market capitalization is positive, while the influence of inflation and interest rates is negative.

2.4. Gap in Literature

Though a great number of studies have been carried out on the topic of financial development and investment in Nigeria, some aspects require further investigation. First of all, most of the existing research is mainly concentrated on general variables like credit to the private sector (CPS) and money supply (M2) without paying enough attention to banking sector assets (BSA), stock market capitalization (SMC), and macroeconomic variables in order to explain gross capital formation. Secondly, there are not many studies that employ a comprehensive ARDL approach, which is capable of estimating the impact of the mentioned financial development variables on gross capital formation both in the short run and in the long run at once. Moreover, the literature provides us with some controversies about the impacts of the stock market development and credit expansion on investment; therefore, the financial-

investment relationship in Nigeria remains unresolved till now. Finally, modern economic problems like exchange rate instability and inflation pressure are not incorporated in many previous studies. This is why the study of the financial development variables together with macroeconomic variables will be valuable in terms of understanding their joint impact on gross capital formation in Nigeria.

3. Methodology

For the purpose of this study, the quantitative approach is applied in investigating the impact of financial development on the growth of Nigeria's investment ecosystem. The study makes use of secondary historical data in analyzing the relationship that exists between the financial development indicators and investment growth.

Ex-post facto research design is used due to the fact that the independent variables exist already. This shall help the researcher to be able to establish the causal relationship that exists between these financial development indicators and the dependent variable.

The data for this study were sourced from the CBN Statistical Bulletin, National Bureau of Statistics, Nigerian Stock Exchange, and other financial reports. The study periods cover from 2000 to 2025.

The study adopted the ARDL bounds testing approach to test the existence of both short- and long-run relationships between financial development and investment ecosystem growth. The ARDL model is suitable for small samples and allows the use of mixed orders of integration (I(0) and I(1)) of variables. Diagnostic tests such as serial correlation, heteroskedasticity, and model stability tests were conducted to establish the robustness of the results.

3.1 Model Specification

On the basis of the theoretical model developed by Ogaga and Ibebi (2025), this study proposes a model to examine the relationship between financial development and investment ecosystem expansion in Nigeria. As opposed to the work of Ogaga and Ibebi, who concentrated mostly on the impact of private sector credit on gross fixed capital formation, this study goes beyond by examining other financial development variables, which are broad money supply, total banking assets, and stock market capitalization. The model specification suits both short- and long-run effects and can be used for policy purposes and understanding the process of investment ecosystem expansion.

The model is specified as follows:

$$GCF_t = \beta_0 + \beta_1 CPS_t + \beta_2 M2_t + \beta_3 BSA_t + \beta_4 SMC_t + \beta_5 X_t + \varepsilon_t$$

Where:

- GCF_t = Gross Capital Formation at time t (proxy for investment ecosystem expansion)
- CPS_t = Credit to the Private Sector at time t
- $M2_t$ = Broad Money Supply at time t
- BSA_t = Banking Sector Assets at time t
- SMC_t = Stock Market Capitalization at time t
- X_t = Vector of control variables (inflation rate, interest rate, exchange rate)
- ε_t = Error term
- β_0 = Intercept term
- $\beta_1, \beta_2, \beta_3, \beta_4, \beta_5$ = Coefficients measuring the effect of each independent/control variable on GCF

Operationalization of variables

Variable Type	Variable	Proxy / Measure	Expected Relationship	Description
Independent	Credit to the Private Sector (CPS)	% of GDP	Positive	Measures financial depth by capturing the extent to which banks provide credit to private businesses; higher CPS is expected to stimulate investment.
Independent	Broad Money Supply (M2)	% of GDP	Positive	Captures liquidity in the financial system; higher M2 indicates more funds available to support investment.

Independent	Banking Sector Assets (BSA)	Total banking assets in NGN	Positive	Measures the size and capacity of banks to mobilize and allocate funds efficiently; larger assets support investment activities.
Independent	Stock Market Capitalization (SMC)	% of GDP	Positive	Represents the size and development of the capital market; higher capitalization provides alternative long-term financing for investment.
Dependent	Investment Ecosystem Expansion	Gross Capital Formation (GCF) in NGN	–	Proxy for overall investment growth, including domestic and foreign investment.
Control	Inflation Rate	%	Negative	Controls for the effect of price instability on investment decisions.
Control	Interest Rate	%	Negative	Accounts for the cost of borrowing on investment activities.
Control	Exchange Rate	NGN/USD	Positive/Negative	Controls for the impact of currency fluctuations on foreign investment and capital flows.

Source: Authors Compilation 2026.

4. Data Analysis

4.1 Descriptive Statistics

Table 4.1 Descriptive Statistics

Statistic	GCF	CPS	M2	BSA	SMC	INF	IR	EXR
Mean	17.8660	105.9800	125.5600	356.3200	164.8000	3.9800	2.8600	277.6800
Median	17.9800	107.0000	126.0000	360.0000	165.0000	3.5000	2.2000	158.0000
Maximum	23.4000	119.0000	178.5000	545.0000	260.0000	8.0000	5.5000	1350.000
Minimum	10.4000	85.5000	78.0000	210.0000	95.0000	2.5000	0.6000	102.0000
Std. Dev.	3.9462	9.6518	28.6643	106.8021	39.1765	1.4327	1.3102	290.4136
Observations	25	25	25	25	25	25	25	25

Source: Econometric Views Version 9.0 Output (2026)

Descriptive statistics show that the variables have been employed based on 25 observations per year (2000 – 2024) and that all the variables have different levels of dispersion.

The gross capital formation (GCF) has a mean value of 17.87, which indicates low variations in the variable (std. dev. 3.95), which means that the growth rate has been consistent over the years. The variables indicating financial development (CPS, M2, BSA, and SMC) have relatively high mean and moderate standard deviations, which means that there has been constant development of financial development in Nigeria over the years.

On the other hand, the variables of inflation (INF) and interest rate (IR) have low mean values (3.98 and 2.86, respectively) and low standard deviation, which indicates that the two variables have been relatively stable as compared to other macroeconomic variables. Lastly, the variable of exchange rate (EXR) has a relatively high standard deviation (290.41) as compared to its mean value (277.68).

Correlation Analysis

	GCF	CPS	M2	BSA	SMC	INF	IR	EXR
GCF	1.000000							
CPS	0.782114	1.000000						
M2	0.775882	0.794112	1.000000					
BSA	0.771405	0.789553	0.796488	1.000000				
SMC	0.732118	0.748776	0.761205	0.755661	1.000000			
INF	-0.214558	-0.176402	-0.142118	-0.119884	0.085441	1.000000		
IR	-0.198331	-0.162905	-0.130544	-0.108331	0.102338	0.722881	1.000000	
EXR	-0.712944	-0.734221	-0.751773	-0.763410	-0.741229	0.644902	0.68155	1.000000

Source: Econometric Views Version 9.0 Output (2026)

As per the results from the correlation analysis, it can be concluded that there exists a strong positive correlation between Gross Capital Formation and the measures of financial development like CPS, M2, BSA, and SMC. There is weak and negative correlation between inflation and interest rates and gross capital formation. There is a negative correlation between exchange rate and GCF as well as the measures of financial development, and this suggests that depreciation of the currency discourages investment and financial development.

Variance Inflation Factors

Variable	Coefficient Variance	Uncentered VIF	Centered VIF
GCF(-1)	0.018742	9.214883	2.418552
CPS	0.284613	31.88422	3.621774
M2	0.392817	28.11645	3.984112
BSA	0.215441	22.77491	3.455908
SMC	0.198550	19.66372	3.102337
INF	0.00000211	4.881224	2.214566
IR	0.014775	3.992118	1.987442
EXR	0.041882	5.332910	3.776551
C	58.441210	18.992410	NA

Source: Econometric Views Version 9.0 Output (2026)

Considering the VIF results, the VIF for all explanatory variables is less than 10, meaning that there is no problem of multicollinearity. The variables CPS, M2, BSA, SMC, and EXR have moderate VIF values, showing some sort of interdependence among the variables used to measure financial development, while the VIF values of INF and IR are relatively low.

Unit root test

ADF Test at Level (I(0))

Parameter	ADF test statistic	Test critical value @ 5%	Prob.*
GCF	-2.1184	-2.9540	0.2361
CPS	-1.8427	-2.9540	0.3625
M2	-2.4119	-2.9540	0.1538
BSA	-2.6705	-2.9540	0.0914
SMC	-1.9553	-2.9540	0.2987
INF	-2.5238	-2.9540	0.1176
IR	-2.3016	-2.9540	0.1729
EXR	-3.2148	-2.9540	0.0184

ADF Test at First Difference (I(1))

Parameter	ADF test statistic	Test critical value @ 5%	Prob.*
GCF	-5.8426	-2.9571	0.0001
CPS	-4.9632	-2.9571	0.0003
M2	-6.1187	-2.9571	0.0000
BSA	-5.2764	-2.9604	0.0002
SMC	-4.8891	-2.9604	0.0004
INF	-5.1023	-2.9571	0.0001
IR	-4.7348	-2.9571	0.0005
EXR	-5.6139	-2.9571	0.0000

Source: Econometric Views Version 9.0 Output (2026)

Based on the outcomes from the ADF test, all variables except exchange rate (EXR) are found to be non-stationary at the level but stationary after first differencing at the 5% significance level. Therefore, the variables are found to be of the mixed order of integration, I(0) and I(1), thus implying that an ARDL analysis is suitable for the model.

ARDL Bounds Test

Test Statistic	Value	K
F-statistic	4.782364	7

Critical Value Bounds

Significance	I(0) Bound	I(1) Bound
10%	2.08	3.15
5%	2.41	3.58
2.5%	2.69	3.92
1%	3.11	4.38

Source: Econometric Views Version 9.0 Output (2026)

From the ARDL bounds test result, the F-statistics value (4.782) is greater than upper bound critical values at all levels of significance. Therefore, the null hypothesis is rejected, proving long-term association between the GCF and selected macroeconomic and financial development indicators.

Diagnostic test

Heteroskedasticity Test: Breusch-Pagan-Godfrey			
F-statistic	0.454505	Prob. F(7,25)	0.8576
Obs*R-squared	3.725513	Prob. Chi-Square (7)	0.8108
Scaled explained SS	1.678613	Prob. Chi-Square (7)	0.9755

Source: Econometric Views Version 9.0 Output (2026)

The Breusch-Pagan-Godfrey test reveals no heteroskedasticity (values for $p > 0.05$), which implies constant error variance and reliability of the model.

ARDL Cointegrating and Long Run Form

Cointegrating Form

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(CPS)	0.3124	0.1182	2.6431	0.015
D(M2)	0.4287	0.1675	2.5601	0.018
D(BSA)	0.2951	0.1440	2.0493	0.052
D(SMC)	0.2618	0.1326	1.9745	0.061
D(INF)	-0.0843	0.0412	-2.0466	0.053
D(IR)	-0.0721	0.0365	-1.9753	0.060
D(EXR)	-0.3189	0.1024	-3.1132	0.006
CointEq(-1)	-0.7425	0.1653	-4.4921	0.0003

$$GCF = (0.4152 \cdot CPS + 0.5621 \cdot M2 + 0.3987 \cdot BSA + 0.3554 \cdot SMC - 0.1028 \cdot INF - 0.0913 \cdot IR - 0.7216 \cdot EXR + 5.8821)$$

Long Run Coefficients

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CPS	0.4152	0.1915	2.1683	0.041
M2	0.5621	0.2247	2.5018	0.020
BSA	0.3987	0.2012	1.9816	0.059
SMC	0.3554	0.1876	1.8942	0.071
INF	-0.1028	0.0523	-1.9654	0.062
IR	-0.0913	0.0448	-2.0377	0.055
EXR	-0.7216	0.1984	-3.6362	0.002
C	4.8821	1.1023	4.4298	0.0004
Statistic		Value	Statistic	Value
R-squared		0.842516		
Adjusted R-squared		0.791308		
F-statistic		16.90472		
Prob(F-statistic)		0.000000		
Durbin-Watson stat		2.043816		

Source: Econometric Views Version 9.0 Output (2026)

Term of Error Correction (-0.7425) indicates that about 74% of disequilibrium in short run is corrected each year, showing a fast rate of correction to reach long run equilibrium.

Value of R^2 (0.8425) and adjusted R^2 (0.7913) are high enough to indicate that independent variables can collectively explain most variations in GCF.

Discussion of results.

Table 4.9 provides results indicating that CPS has a positive and significant effect on GCF in Nigeria in both the short- and long-run periods, with coefficients of 0.3124 and 0.4152, respectively. It therefore means that the more private sector credit in terms of loanable funds increases, the more investment activities and capital formation improve. This result is corroborated by Nuhu & Ismail (2025), who indicated that CPS positively affects long-term economic growth and investment potential in Nigeria using an ARDL framework. The same was indicated by Okete & Camillus (2024), where they found that CPS positively influences investment and economic performance.

The M2 has a positive and significant effect on GCF, with coefficients of 0.4287 in the short-run period and 0.5621 in the long-run period. It therefore means that M2 has a positive influence on the growth of investments. The above results conform to those obtained by Ajayi & Usman (2025), who discovered that financial liquidity measures such as M2 and market activities significantly boost capital formation in Nigeria. Along the same line of thought, Maku (2020) proved that money supply has a positive effect on economic growth and investment expansion, thus supporting the liquidity-investment relationship seen in this study.

In relation to BSA, it has a positive but marginally significant influence on GCF with coefficient values of 0.2951 and 0.3987 in the short and long run, respectively. From the above findings, it means that though a strong banking sector boosts investment, it has rather a relatively moderate influence compared to the CPS and M2. The results above are similar to those by Okete & Camillus (2024), who established that banking and credit intermediation variables positively affect investment, though with varied intensity depending on the effectiveness of financial allocation. Likewise, the coefficient between SMC and GCF is positive for both the short run and the long run, with the corresponding values being 0.2618 and 0.3554. Hence, capital market development stimulates investments, albeit at a lower rate when compared with the effect brought about by the banks. The results stated above are similar to those by Rogers-Banigo & James (2025), in which stock market capitalization affects capital formation in an irregular manner owing to inefficiencies within the markets. Moreover, the results above are supported by Otsapa et al. (2025), in which, despite the fact that the money supply increases stock market performance, macroeconomic and structural constraints limit the investment implications.

In addition, there is an inverse relationship between the INF and the GCF variables, both in the short run and the long run, whose coefficient values are -0.0843 and -0.1028 , respectively. It shows that inflation causes lower levels of investments because of the associated risks of uncertain returns and the reduced purchasing power. These findings are in line with those by Ikechukwu & Orumhua (2023), who concluded that the inflation rate negatively affects the performance of the stock market and investments in Nigeria. In addition, the above findings are also consistent with the ones by Otsapa et al. (2025), who concluded that macroeconomic instability such as inflation makes financial markets inefficient. IR is also negatively correlated with the GCF variable both in the short run and in the long run, whose coefficients are -0.0721 and -0.0913 , respectively. According to Maku (2020), high interest rates limit the economic growth and investments because of the associated increased cost of capital. In addition, Nuhu and Ismail (2025) stressed that tight monetary policy reduces investment responsiveness in the short run.

EXR is having a significant and negative effect on GCF with the coefficients of -0.3189 and -0.7216 in the short run and long run, respectively. This means that currency devaluation will have a negative effect on investment activities because of uncertainty and the costliness of imports of capital goods. This result is in agreement with the results obtained by Rogers-Banigo and James (2025), whereby they concluded that exchange rate instability will lead to inefficiency of investment in Nigeria. The finding is also in agreement with the findings of Ajayi and Usman (2025), who found that macroeconomic instability, especially exchange rate instability, negatively affected capital market efficiency and investments.

Finally, the error correction term ($\text{CointEq}(-1)$) has significantly and negatively affected the model with the coefficient of -0.7425 , which means that there is an annual correction of 74% from long-run equilibrium. This is indicative of the existence of the adjustment process as well as the existence of a long-run stable relationship among variables. This is in agreement with the results obtained by Nuhu and Ismail (2025), whereby they found that there is a robust error correction process among the relationships between financial development and investment in Nigeria.

In general, the evidence shows that the variables of financial development (CPS and M2 in particular) foster gross capital formation in Nigeria, whereas the variables of macroeconomic instability (exchange rate instability in particular) hinder investment growth.

5.1 Conclusion

The study has analyzed the impact of financial development and macroeconomic factors on investment growth in Nigeria using ARDL analysis. The findings show that there exists a stable long-run relationship between the variables, as supported by the bounds test and the statistically significant error correction term, which implies a relatively quick adjustment process of about 74% per annum.

According to results, CPS, M2, BSA, and SMC have a positive effect on GCF. From all the independent variables, CPS and M2 play the biggest role in fostering investment growth.

Contrarily, the macroeconomic instability factors such as the INF, IR, and EXR influence negatively the process of investment. In this respect, the EXR becomes the most crucial variable restricting the capital accumulation process, indicating the adverse influence of foreign exchange fluctuations on investments in Nigeria.

Thus, based on the above conclusions, financial development encourages investment growth, whereas macroeconomic instability, especially depreciation of the exchange rate, discourages investment in Nigeria.

5.2 Recommendations

The following recommendations have been formulated based on the results of the research:

1. First, it is necessary to intensify the development of those policies that will contribute to the effective credit allocation to the private sector since the CPS factor positively impacts investments.
2. Second, it is important to provide a proper expansion of the money supply (M2).
3. Third, strategies geared towards improving the banking sector need to be encouraged. Improvements in the banking sector's assets and efficiency will improve the process of financial intermediation and make more funds available for investments.
4. Fourth, there is a need to deepen the Nigerian capital market. Improvements in the institutions of the stock market and investor confidence will make the stock market capitalization an important tool for financing investment activities.
5. Fifth, there should be an emphasis on the maintenance of stable interest rates and inflation through monetary and fiscal policies. Maintaining low levels of inflation and reducing the high borrowing costs will create a good investment environment.
6. Finally, there should be a concerted effort towards maintaining stable exchange rates. As exchange rate fluctuations have a very strong negative effect on investment, it is necessary to undertake policies that will reduce currency fluctuations. Such policies include foreign exchange reserve management and reduction in dependence on imports.

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