

Monetary Policy Dynamics and Stock Market Reactions in Nigeria: An In-Depth Empirical Assessment

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Abstract

This study examines the impact of monetary policy dynamics on stock market reactions in Nigeria over the period 2000 to 2024. Key monetary policy indicators used include the monetary policy rate, money supply, lending rate, and treasury bill rate, while stock market performance is measured by stock market capitalisation. Time series data were obtained from the Central Bank of Nigeria (CBN) statistical bulletin. The analysis employed descriptive statistics, the Augmented Dickey-Fuller (ADF) unit root test, and the Autoregressive Distributed Lag (ARDL) technique to evaluate both short- and long-term relationships among variables. The findings reveal that the monetary policy rate exerts a negative but statistically insignificant effect on stock market capitalisation. Conversely, money supply and treasury bill rate have positive and significant effects, while lending rate shows a negative and statistically significant impact on stock market capitalisation. These results underscore the critical role of monetary policy in influencing stock market performance in Nigeria. The study concludes that monetary policy tools are significant determinants of capital market outcomes. It recommends that the Central Bank of Nigeria should carefully consider prevailing macroeconomic conditions, particularly in adjusting the lending rate, as excessive rates may drive inflationary pressures and hinder stock market growth.

Keywords: Lending Rate, Monetary Policy, Monetary Policy Rate, Money Supply, Nigeria, Stock Market Capitalisation, Treasury Bill Rate

Introduction

The stock market has increasingly become a pivotal component in the architecture of modern financial systems, drawing the attention of investors, policymakers, and economic strategists alike (Olowe, 2020). As a core segment of the financial market, the stock market serves as a conduit through which publicly listed corporations and government entities can mobilize capital for developmental and strategic objectives (Gompers, 2022). Functionally, the stock exchange operates as an organized arena for the issuance and trade of equity securities, enabling investors to acquire shares in publicly quoted firms with the prospect of wealth accumulation through capital appreciation and periodic dividends (Mishkin & Eakins, 2018).

Stock markets play a dual role: they are both a financing mechanism for firms and a wealth-generating avenue for investors, while also reflecting broader macroeconomic trends (Chen, Roll, & Ross, 1986). A robust and efficient stock market channels savings into productive investment and contributes to economic growth and development (Levine & Zervos, 1998). However, this function does not operate in isolation—it is heavily conditioned by macroeconomic variables and policy instruments, particularly monetary policy (Bernanke & Kuttner, 2005).

Monetary policy, in its fundamental design, comprises a series of tools and decisions employed by the central bank to modulate liquidity, interest rates, and overall credit accessibility in the economy (Central Bank of Nigeria [CBN], 2022). These monetary policy instruments—such as open market operations, cash reserve requirements, and benchmark interest rates—affect the volume of money in circulation and subsequently shape investment behaviour and asset pricing in the stock market (Sims, 1992). Across both advanced and developing economies, the volatility of the stock market often mirrors the oscillations induced by monetary announcements, creating a transmission channel through which monetary shocks influence investor sentiment (Rigobon & Sack, 2004).

As noted by Muktadir-Al-Mukit and Shafiullah (2012), the unpredictability of the stock market in emerging economies such as Nigeria is often a reflection of the monetary authority's policy stance. Interest rate adjustments, particularly, are among the most potent tools through which monetary policy affects equity prices. A reduction in interest rates, characteristic of an expansionary stance, lowers the cost of borrowing, thereby stimulating investment and consumption—conditions favourable to rising corporate earnings and, by extension, increasing stock valuations (Fama, 1981). On the contrary, a contractionary policy stance that elevates interest rates can dampen economic activity and reduce investor enthusiasm, leading to bearish market trends (Christiano, Eichenbaum, & Evans, 1999).

Global stock markets have witnessed exponential growth in capitalization, with the total market value reaching an estimated US \$128 trillion in early 2025, up from US \$109 trillion in 2023, and projections indicate it will surpass US \$138 trillion by 2026 (Statista, 2025).

This expansion reflects both increased investor participation and broader economic engagement with capital markets, as the global market capitalization-to-GDP ratio climbed to approximately 130 % in 2024 (World Bank, 2024). The United States continues to dominate global equity markets, accounting for about 42 % of the total value, equivalent to approximately US \$62 trillion, followed by China with 10.6 %, the European Union with 11.1 %, and Japan contributing 5.4 % (Statista, 2025). Although emerging markets presently contribute around 9 % to global stock market capitalization, this figure is expected to grow substantially, rising to 24.1 % by 2026 and potentially reaching 47 % by 2050, signalling increasing financial integration and capital flow liberalization in these regions (Visual Capitalist, 2023).

Despite the promise held by emerging economies, Africa's performance in the global stock market landscape remains underwhelming, with all African stock exchanges combined contributing less than 1 % to total global market volume, underscoring persistent structural weaknesses and limited investor depth (Siblis Research, 2023). Empirical trends from 2010 to 2022 reveal underperformance across key African markets, as Nigeria's stock index declined by approximately 89 %, Egypt by 46 %, and Kenya by 12 %, while only South Africa showed marginal growth of +7 %, emphasizing the volatility and fragile nature of many African equity markets (Financial Times, 2023). Moreover, the ratio of market capitalization to GDP, a critical indicator of stock market depth, reveals that within MSCI Frontier Markets, Nigeria was ranked 9th among 15 countries in 2022 with a value of 19.35 %, further affirming the need for financial sector reforms and monetary coordination (TheGlobalEconomy.com, 2022).

In Nigeria, the capital market has recorded significant shifts over time, with its market capitalization as a share of GDP estimated at 23.3 % as of December 2024, an increase from 17.8 % in 2023, yet still trailing far behind its peak of 29.7 % observed in 2007, suggesting a cyclical recovery influenced by monetary and fiscal variables (CEIC Data, 2025). The Nigerian Exchange Group currently lists 393 securities, comprising 151 equities, 157 bonds, 12 Exchange-Traded Products (ETPs), and 4 index futures, reflecting a moderately diversified but relatively shallow capital market compared to global benchmarks (Wikipedia, 2025a). As of July 11, 2025, the Nigerian Stock Exchange (NSE) All-Share Index surged to a record high of 126,150 points, representing a +26.6 % year-on-year growth, and indicative of improved investor sentiment and speculative recovery in the equities market (Trading Economics, 2025a). The market delivered a commendable 36.6 % annual return in 2024, outperforming its previous ten-year average of 9.7 %, though such growth remains vulnerable to macroeconomic instability (Trading Economics, 2025a).

In the broader macroeconomic context, Nigeria is currently grappling with persistent inflation, which stood at approximately 23 % as of June 2025, with the Central Bank of Nigeria maintaining a high Monetary Policy Rate (MPR) of 27.5 % to rein in inflationary pressures, a stance that influences borrowing costs, credit allocation, and equity market

performance (Trading Economics, 2025b). At the same time, the country's unemployment rate has declined to 4.3 %, a trend which, while promising, may not fully capture underemployment and informal sector realities that shape domestic consumption and investment (Trading Economics, 2025b). The financial sector in Nigeria remains the most developed in West Africa, boasting a financial inclusion rate of approximately 44 %, with the country hosting 21 commercial banks and accounting for roughly 28 % of Africa's fintech enterprises, approximately 1,263 firms, as of 2024, a sign of digital-led transformation and youth-driven innovation (Wikipedia, 2025b).

The convergence of these factors paints a complex picture: while global markets continue to expand and integrate, Africa—particularly Nigeria—remains at a developmental crossroads, caught between structural reform and persistent macroeconomic volatility. Although Nigeria's stock market has demonstrated resilience and recent growth, its performance remains highly sensitive to shifts in monetary policy, exchange rate fluctuations, and inflation dynamics, thereby underscoring the importance of well-calibrated monetary policy instruments to ensure stability and investor confidence in the capital market (Bernanke & Kuttner, 2005).

Emerging economies have acknowledged the stock market's role in enhancing financial system efficiency and promoting economic diversification (Aliyu, 2009). This recognition has spurred efforts toward market deepening, regulatory reform, and technological integration to attract foreign and institutional investment (Osinubi, 2004). The increasing globalization of capital flows has also exposed local stock markets to the volatilities and signals from international monetary environments, necessitating more responsive and predictive monetary frameworks (Mishra, Das, & Pradhan, 2009).

A core theoretical underpinning of stock market response to macroeconomic variables is the Efficient Market Hypothesis (EMH) proposed by Fama (1981), which posits that stock prices fully reflect all available information. *“The market is said to be efficient when prices of securities at any time fully reflect all available information”* (Fama, 1981, p. 383). This implies that investors, being rational actors, factor in not just firm-specific data but also the broad monetary climate into their trading strategies. As such, any unexpected policy shift—especially from monetary authorities—is quickly incorporated into asset prices.

Additionally, macroeconomic stability, investor confidence, and financial market liberalization are prerequisites for an efficient stock market responsive to monetary policy (Okonkwo, Ogbonna, & Onoh, 2015). In Nigeria, the Central Bank plays a strategic role in influencing equity market conditions by leveraging interest rates and credit controls to stabilize inflation and ensure steady capital market growth (CBN, 2022). However, the effectiveness of these interventions depends on the transparency, timing, and consistency of policy signals.

The growing body of literature confirms that the interaction between monetary policy variables—such as money supply (M2), monetary policy rate (MPR), and treasury bill rates—and stock market indices (e.g., NSE All Share Index) is statistically significant, though context-specific (Nwaolisa & Kasie, 2012). These findings underscore the importance of dynamic policy frameworks that are both empirically grounded and adaptable to the evolving realities of the domestic and global economic environment.

In conclusion, monetary policy constitutes a critical lever through which financial stability and stock market efficiency can be achieved. A nuanced understanding of the monetary transmission mechanism is essential for policymakers, investors, and scholars who seek to forecast market behaviour and align monetary interventions with economic growth objectives (Bernanke & Gertler, 1995). In light of persistent monetary fluctuations and inconsistent market responses, this study is prompted to critically assess the impact of Monetary Policy Dynamics and Stock Market Reactions in Nigeria: An In-Depth Empirical Assessment (2000–2024), with the aim of providing evidence-based policy recommendations for optimizing monetary interventions and enhancing stock market stability in the Nigerian economy. The objectives of the study are therefore to: (i) Examine the impact of the Monetary Policy Rate (MPR) on stock market capitalisation in Nigeria. (ii) Determine the effect of Money Supply (MS) on stock market capitalisation in Nigeria. (iii) Evaluate the influence of Lending Rate (LR) on stock market capitalisation in Nigeria. (iv) Assess the impact of the Treasury Bill Rate (TBR) on stock market capitalisation in Nigeria.

2.0 REVIEW OF RELATED LITERATURE

2.1 Conceptual Review

2.1.1 Monetary Policy

Monetary policy constitutes a crucial component of macroeconomic management that entails the deliberate regulation of the money supply, credit accessibility, and interest rate levels by the central monetary authority to influence economic activity (Chowdhury, Hoffmann, & Schubert, 2013). It refers to a systematic process through which central banks implement tools and strategies to maintain price stability, promote employment, stabilize the currency, and foster sustainable economic growth (Loayza & Schmidt-Hebbel, 2002). Fundamentally, it involves influencing the demand and supply of money in an economy in order to attain set macroeconomic goals, including low inflation, financial system stability, full employment, and balanced economic output (Faure, 2007).

The central bank uses a suite of monetary instruments—ranging from open market operations (OMO), reserve requirements, and the monetary policy rate (MPR), to moral suasion and direct lending controls—to regulate credit flow and manage liquidity within the financial system (Loayza & Schmidt-Hebbel, 2002). Through these instruments, the monetary authority adjusts the cost and availability of credit in ways that affect consumption, investment, exchange rates, and overall economic equilibrium (Chowdhury et al., 2013). For

instance, raising the monetary policy rate typically reduces money supply, discourages excessive borrowing, and curbs inflationary pressures, while reducing the rate encourages borrowing, investment, and economic expansion (Mishkin, 2019).

The effective coordination of monetary policy with fiscal policy is essential to harmonize short-term stabilization goals with long-term growth objectives (Bernanke & Gertler, 1995). Monetary policy also plays a stabilizing role in times of economic volatility by counteracting adverse cyclical fluctuations (Blanchard, Dell’Ariccia, & Mauro, 2013). However, the effectiveness of monetary policy varies across countries due to differences in institutional development, financial market structures, and transmission mechanisms (Faure, 2007). In countries with underdeveloped capital markets or high levels of informality, like Nigeria, the transmission of policy signals may be weak, resulting in delayed or distorted macroeconomic outcomes (CBN, 2022).

Furthermore, monetary policy is not only reactive but also anticipatory, meaning central banks must assess future inflationary trends, employment forecasts, and global economic indicators when making decisions (Clarida, Galí, & Gertler, 2000). Central banks in emerging economies often face the dual challenge of controlling inflation while also fostering growth, a dilemma that complicates the calibration of interest rates and money supply levels (Mishra & Montiel, 2012). Consequently, a well-designed monetary policy framework is instrumental in achieving not just internal balance (price and employment stability), but also external balance (exchange rate and capital flow stability) in a globally interconnected financial system (IMF, 2021).

2.1.2 Stock Market

The stock market represents a structured financial ecosystem where equity instruments, particularly shares of publicly listed firms, are issued, bought, and sold, thereby facilitating the transfer of capital from savers to productive users (Al-Faki, 2006). It serves as a pivotal institution in the financial system that links surplus units (households and institutional savers) with deficit units (firms and governments seeking capital), enabling the mobilization of long-term funds for investment purposes (Pandey, 2006). Conceptually, the stock market is bifurcated into the primary market, which enables the issuance of new securities to raise fresh capital, and the secondary market, where existing securities are traded among investors (Ullah, Hussain, & Rauf, 2014).

The primary market is critical in capital formation as it allows corporations and governments to finance infrastructure, expansion, and technological innovation through public offerings or private placements (Olokoyo&Ogunnaike, 2011). Regulatory institutions like the Securities and Exchange Commission (SEC) and the Nigerian Exchange Group (NGX) oversee this space to ensure transparency, investor protection, and market integrity (NSE, 2022). Once issued, these securities transition into the secondary market where they are actively traded,

providing liquidity, discoverable pricing, and portfolio diversification for investors (Pandey, 2006).

The role of the stock market transcends mere capital mobilization; it also serves as a barometer of economic performance, reflecting corporate health, investor sentiment, and macroeconomic stability (Ibrahim, 1999). Efficient stock markets reduce the cost of capital by allowing firms to access equity financing without reliance on debt instruments, thereby promoting financial sustainability and reducing systemic risk (Rashid, 2008). A well-regulated and transparent equity market can also stimulate household savings by offering attractive investment alternatives to traditional savings channels (Olokoyo & Ogunnaike, 2011).

In recent decades, stock markets have evolved as vital engines of economic growth by enabling the efficient allocation of scarce resources through the price mechanism (Levine & Zervos, 1998). Foreign portfolio investments are attracted to markets with sound regulatory practices, low transaction costs, and strong institutional frameworks, thereby increasing demand for domestic equities, boosting market liquidity, and enhancing price efficiency (Obstfeld, 1994). This inflow of foreign capital often results in higher share valuations, improved market capitalization, and increased fiscal revenue through capital gains and taxes (Bekaert & Harvey, 2003).

The strategic relevance of stock markets becomes more pronounced in emerging economies, where capital constraints and limited access to long-term financing remain persistent challenges (Osinubi, 2004). Equity markets provide an avenue for economic diversification, job creation, and innovation funding—especially in sectors such as manufacturing, agriculture, and technology (Ujunwa, 2012). Nigeria's stock market, though relatively underdeveloped, has shown potential to support the country's economic diversification agenda if integrated monetary and regulatory reforms are sustained (CBN, 2022).

Ultimately, an effective and inclusive stock market is essential for ensuring long-term economic development, macroeconomic stability, and sustainable wealth creation for both institutional and retail investors (Rashid, 2008). The convergence of monetary policy effectiveness and capital market development determines how efficiently a nation can translate financial deepening into tangible economic outcomes (Mishkin, 2019).

2.2. Theoretical Framework

Monetary Transmission Mechanism (MTM) and Efficient Market Hypothesis (EMH)

This study is anchored on two key economic theories: the Monetary Transmission Mechanism (MTM) and the Efficient Market Hypothesis (EMH), which together provide a

robust analytical foundation for examining how monetary policy influences stock market performance in Nigeria.

The Monetary Transmission Mechanism (MTM) explains how central bank actions, such as changes in interest rates or the money supply, influence real economic variables and asset prices through specific channels—most notably the interest rate, credit, exchange rate, and asset price channels (Loayza & Schmidt-Hebbel, 2002; Mishra & Montiel, 2012). In this framework, monetary policy decisions directly affect borrowing costs, liquidity, and investor expectations, thereby influencing the behavior of stock markets. The MTM is particularly relevant in developing economies like Nigeria, where structural bottlenecks may weaken certain transmission paths but enhance others, such as the interest rate or inflation expectation channel.

On the other hand, the Efficient Market Hypothesis (EMH), originally proposed by Fama (1970), asserts that stock prices fully and immediately reflect all available information, including macroeconomic indicators and monetary policy shifts. According to the semi-strong form of EMH, monetary policy announcements should be quickly incorporated into share prices, implying that any predictable effect of monetary policy on the stock market would challenge the hypothesis of informational efficiency. However, in less developed or frontier markets like Nigeria, delays in information dissemination and limited investor sophistication may result in only partial efficiency (Fama, 1991).

Thus, this study is anchored on these two frameworks: MTM provides the structural channels, while EMH tests the behavioral and informational response of the stock market to monetary dynamics in Nigeria. Together, they allow a comprehensive assessment of both causality and market reaction within the Nigerian macro-financial environment.

2.3 Empirical Review

Safiyanu, Bayero & Yusuf (2025), in their conference paper *“Impact of Monetary Policy on Stock Market Performance in Nigeria”*, analyzed quarterly data from 1985 to 2024 using the ARDL model. Their study incorporated key monetary variables—interest rate, money supply (M2), and exchange rate—while accounting for global economic shocks such as the Structural Adjustment Program (SAP) and the COVID-19 pandemic. Their findings revealed that, in the long run, both money supply expansion and exchange rate depreciation positively influence stock market performance. However, rising interest rates were found to discourage investment and reduce market participation. In the short run, an error correction mechanism allowed the system to adjust back toward equilibrium following shocks. They recommended that policymakers ensure consistent, transparent monetary policies, especially during periods of economic transition or global crises, to maintain stability in the capital market.

Tubotamuno & Oladosu (2024) conducted an empirical study titled "*Monetary Policy and the Performance of the Stock Market in Nigeria*" covering data from 1985 to 2022. Employing the Autoregressive Distributed Lag (ARDL) approach and conducting unit root and co-integration tests, they aimed to determine how monetary policy variables—namely, the monetary policy rate (MPR), money supply (M2), lending rate, and Treasury bill rate—influence stock market capitalisation. Their results showed that the MPR has a negative but statistically insignificant impact on stock market capitalisation, while both money supply (M2) and Treasury bill rate have positive and significant effects. In contrast, the lending rate exhibits a negative and significant relationship with stock market capitalisation. The authors concluded that monetary policy is indeed an important determinant of stock market performance in Nigeria, and they cautioned the CBN to exercise care in setting lending rates due to their potential to stoke inflation that could harm the capital market.

Olokoyo, Osabuohien, and Salami (2021) conducted a study on *Monetary Policy Transmission and Stock Market Performance in Nigeria* with the aim of assessing the effect of monetary policy instruments—specifically the monetary policy rate (MPR), inflation, and broad money supply—on the Nigerian stock market. Using quarterly data spanning from 2000 to 2020, the authors employed a Vector Error Correction Model (VECM) to capture both short-run and long-run dynamics. The Nigerian Stock Exchange (NSE) All-Share Index was used as a proxy for stock market performance, while MPR, M2, and inflation represented monetary policy variables. Their analysis revealed that both MPR and inflation had significant negative effects on the stock market in the long run, whereas money supply exhibited a statistically significant and positive relationship with stock performance, suggesting that liquidity injection through expansionary monetary policy can enhance stock market growth. In contrast, short-run effects were minimal and largely insignificant, indicating that the monetary transmission mechanism in Nigeria suffers from lags and inefficiencies. The authors concluded that while monetary policy in Nigeria significantly influences the stock market over time, structural weaknesses delay its immediate impact. Consequently, they recommended that the Central Bank of Nigeria (CBN) improve policy communication, ensure timely dissemination of information, and promote investor literacy to strengthen market responsiveness and reduce uncertainty. They also advocated for a deeper and more transparent capital market to facilitate better policy transmission. These recommendations reflect a call for institutional reform and financial system development to bridge the observed delay in monetary policy effectiveness.

In another study titled *Interest Rate Fluctuations, Monetary Policy, and Stock Market Reactions in Sub-Saharan Africa: Evidence from Nigeria*, Adegbite and Akanni (2022) investigated how interest rate dynamics and broader monetary policy shifts affect the Nigerian stock market, while drawing implications for sub-Saharan Africa. Utilizing monthly data from 2005 to 2021, the researchers employed the Autoregressive Distributed Lag (ARDL) Bounds Testing approach to examine both short-run and long-run relationships between key monetary variables—interest rate, exchange rate, inflation—and stock market

performance, proxied by the NSE All-Share Index. To capture periods of economic shocks and regime changes, structural break tests were also incorporated into the analysis. Their findings indicated that interest rate volatility exerted a consistently negative and statistically significant impact on stock returns, both in the short and long term. Furthermore, exchange rate instability also negatively influenced market outcomes, particularly during contractionary policy phases. These results emphasize that monetary policy shocks, especially via the interest rate channel, play a critical role in shaping investor sentiment and equity market dynamics in Nigeria. The authors concluded that the presence of structural and macroeconomic disruptions weakens the effectiveness of monetary policy, highlighting the importance of credibility and stability in policy implementation. They recommended that the CBN adopt a forward-looking and stable interest rate regime to minimize uncertainty and enhance market predictability. Additionally, the study underscored the need for comprehensive reforms to mitigate exchange rate volatility, strengthen investor confidence, and improve the financial market's sensitivity to macroeconomic signals.

3.1 MATERIALS AND METHODS

This study adopts an ex-post facto research design, which is considered suitable for investigating historical data in order to examine the cause-effect relationship between the dependent variable—stock market performance—and a set of monetary policy variables. An ex-post facto design is particularly appropriate where the variables under investigation are not manipulable by the researcher, and where the aim is to evaluate the influence of prior policy actions or macroeconomic indicators on observable market outcomes (Kerlinger & Lee, 2000).

The design incorporates a detailed description of the data collection procedure, model framework, and estimation technique, aimed at validating the hypothesized relationship between monetary policy dynamics and stock market behavior in Nigeria. This approach allows for the robust empirical testing of long-run and short-run dynamics, particularly in an environment marked by monetary fluctuations and financial market volatility.

The study relies on annual time series data covering the period 2000 to 2024, thus reflecting a contemporary scope that captures the post-consolidation phase of the Nigerian banking sector, multiple monetary policy regimes, global financial shocks, and the evolution of capital markets. Data were primarily sourced from the Central Bank of Nigeria (CBN) Statistical Bulletin (2024 Edition), which provides comprehensive macroeconomic and financial data across monetary aggregates, interest rates, exchange rates, inflation, and market indices.

3.2 Model Specification

The econometric model guiding this study is adapted from the framework developed by Adegbite and Akanni (2022) in their study titled *Interest Rate Fluctuations, Monetary Policy,*

and Stock Market Reactions in Sub-Saharan Africa: Evidence from Nigeria. In their work, the authors employed the Autoregressive Distributed Lag (ARDL) bounds testing approach to examine both the long-run and short-run interactions between monetary policy instruments and stock market performance. This study adopts their specification with modifications to reflect its extended dataset and objective focus on Nigeria's post-2000 monetary structure and market reforms.

The functional form of the model is specified as:

$$SMC = f(MPR, M2, LR, TBR) \text{ ----- (3.1)}$$

The model above (3.1) can be explicitly stated as follows:

$$SMC = \alpha_0 + \alpha_1 MPR + \alpha_2 M2 + \alpha_3 LR + \alpha_4 TBR + \mathcal{Q}_t \text{ ----- (3.2)}$$

A Priori Expectation: $\alpha_1 < 0, \alpha_2 > 0, \alpha_3 < 0, \alpha_4 > 0$. The

ARDL form of the equations is thus as follows:

$$\begin{aligned} \Delta(SMC_t) = & \beta_0 + \sum_{t=1}^p \beta_1 \Delta(SMC_{t-1}) + \sum_{t=1}^q \beta_2 \Delta(MPR_{t-1}) + \sum_{t=1}^q \beta_3 \Delta(M2_{t-1}) + \sum_{t=1}^p \beta_4 \Delta(LR_{t-1}) \\ & + \sum_{t=1}^p \beta_5 \Delta(TBR_{t-1}) + \alpha_1 \Delta(SMC_{t-1}) + \alpha_2 \Delta(MPR_{t-1}) + \alpha_3 \Delta(M2_{t-1}) \\ & + \alpha_4 \Delta(LR_{t-1}) + \alpha_5 \Delta(TBR_{t-1}) \\ & + \varepsilon_{1t} \text{ ----- (3.3)} \end{aligned}$$

where: SMC= stock market capitalisation; MPR= monetary policy rate; M2= money supply; LR = lending rate; TBR = treasury bill rate; α_0 = regression intercept; $\alpha_1 - \alpha_5$ = long-run dynamic coefficients or parameters attached to the independent variables; $\beta_1 - \beta_5$ = short-run dynamic coefficients of the model; $\mathcal{Q}_t$ =stochastic error term; and ε_{1t} =serially uncorrelated stochastic term with zero mean and constant variance.

4.1 Data Analysis and Discussions

4.1 Data Presentation

The secondary data collected for the study are presented in table as attached in Appendix I. The annual time series include SMC, MPR, M2, LR and TBR sourced from Central Bank of Nigeria (CBN) Statistical Bulletin for the period 2000 to 2024. The tests carried out are as follows;

4.2 Data Analysis

4.2.1 Descriptive Statistical Analysis

The analytical procedure for this study began by providing the descriptive statistics of each variable included in our model as follows:

Table 1: Descriptive Statistics

	SMC	MPR	M2	LR	TBR
Mean	9030.553	13.48684	9917.995	17.92684	13.37237
Median	1735.900	13.50000	2042.370	17.57500	12.95000
Maximum	44750.20	26.00000	43768.86	29.80000	26.90000
Minimum	6.600000	6.000000	22.30000	9.250000	4.500000
Std. Dev.	12453.08	3.720809	13281.41	4.211817	4.646055
Skewness	1.492185	0.885070	1.196080	0.518616	0.369646
Kurtosis	4.443783	5.193186	3.123131	3.976544	3.418638
Jarque-Bera	17.40238	12.57715	9.084525	3.213359	1.142867
Probability	0.000166	0.001857	0.010649	0.200552	0.564715
Sum	343161.0	512.5000	376883.8	681.2200	508.1500
SumSq.Dev.	5.74E+09	512.2434	6.53E+09	656.3578	798.6755
Observations	24	24	24	24	24

Source: *Authors' Computation, 2025.*

Table 4.1. The descriptive statistical profile of the key variables utilized in this study—namely stock market capitalisation, monetary policy rate, money supply, lending rate, and treasury bill rate—offers critical insights into the underlying data trends observed over the study period (2000–2024). The analysis, as presented in Table 1, reveals that the money supply (M2) records the highest mean value, standing at approximately ₦9,918 billion, reflecting the expansive liquidity in the Nigerian financial system during the sample period (CBN, 2024). This is closely followed by stock market capitalisation, which posts a mean value of ₦9,030.6 billion, underscoring the growing scale of capitalisation in the Nigerian Exchange Group over the last two decades (Lawson & Amenze, 2022).

In contrast, monetary policy instruments display more moderate average values. Specifically, the monetary policy rate (MPR) averaged 13.5%, while the lending rate and treasury bill rate registered mean values of 17.9% and 13.4%, respectively. These figures suggest that policy rates remained relatively elevated throughout the study period, a reflection of persistent inflationary pressures and the Central Bank of Nigeria's tightening stance to stabilize macroeconomic conditions (Osakwe & Chukwunulu, 2019).

Further scrutiny of the data reveals considerable variability. The maximum stock market capitalisation during the period reached a peak of approximately ₦44,750.2 billion, while the

minimum value was significantly lower at ₦6.6 billion, indicating substantial market fluctuations likely driven by external shocks, global commodity cycles, and domestic policy uncertainty (Ujunwa, 2012). The monetary policy rate ranged from a maximum of 26.0% to a minimum of 6.0%, suggesting periods of both aggressive policy tightening and expansionary intervention by the CBN.

In terms of monetary aggregates, the money supply expanded as high as ₦43,768.86 billion, with a low of ₦22.3 billion, reflecting evolving monetary policies and increasing formal financial intermediation. The lending rate peaked at 29.8%, while its lowest observed value was 9.3%, confirming wide oscillations in credit pricing over time. Lastly, the treasury bill rate ranged between a high of 26.9% and a low of 4.5%, mirroring both liquidity management strategies and inflation targeting practices during the study period (Chukwuemeka, 2018; CBN, 2024).

These descriptive statistics collectively reflect a macro-financial environment characterized by high volatility, moderate liquidity growth, and a dynamic monetary policy framework—conditions that may critically influence stock market performance in Nigeria.

4.2.2 Unit Root Test

The test for stationarity was performed using the Augmented Dickey Fuller (ADF) unit root test, and the results of the unit root test are presented below:

Table 2: Augmented Dickey-Fuller (ADF) Test Results

Variables	ADF	Mackinnon	P-value (Prob.*)	Decision Order of Integration	
Critical Value @					
5%					
@ Levels					
SMC	2.505633	-2.943427	1.0000	Nonstationary	
MPR	-3.264999	-2.943427	0.0240	Stationary	
M2	7.353087	-2.943427	1.0000	Stationary	
LR	-3.740484	-2.943427	0.0074	Stationary	
@First Difference					
SMC	-4.778859	-2.945842	0.0004	Stationary	I(1)
MPR	-	-	-	-	I(0)
M2	-	-	-	-	I(0)
LR	-	-	-	-	I(0)
TBR	-	-	-	-	I(0)

Source: Authors' Computation, 2025

The results presented in Table 2, based on the Augmented Dickey-Fuller (ADF) unit root test, indicate that the variable representing stock market capitalisation became stationary after first differencing, thereby confirming that it is integrated of order one, I(1) (MacKinnon, 1996). In contrast, the other explanatory variables—namely monetary policy rate, money supply, lending rate, and treasury bill rate—exhibited stationarity at their levels, signifying they are integrated of order zero, I(0). This mixed order of integration among the time series variables, where some are I(0) and others are I(1), violates the assumptions of conventional cointegration models such as the Johansen procedure.

As such, it provided methodological justification for adopting the Autoregressive Distributed Lag (ARDL) bounds testing approach, which remains valid and robust regardless of whether the underlying variables are purely I(0), I(1), or a combination of both (Pesaran, Shin, & Smith, 2001).

By accommodating variables with different integration levels, the ARDL framework is especially suited for estimating both short-run dynamics and long-run equilibrium relationships among the variables, thereby strengthening the validity and reliability of the empirical findings within this study.

4.2.3 ARDL Cointegration Test

Table 3: ARDL Bounds Cointegration Test

Series: SMC MPR M2 LR TBR		
Null Hypothesis: No long-run relationships exist		
Test Statistic	Value	K
F-statistic	5.167462	4
Critical Value Bounds		
Significance	I(0) Bound	I(1) Bound
10%	2.2	3.09
5%	2.56	3.49
2.5%	2.88	3.87
1%	3.29	4.37

Source: Authors' Computation, 2025

The outcome of the ARDL bounds testing procedure, as presented in Table 3, reveals that the calculated F-statistic value of 5.167462 exceeds the critical values of both the lower and upper bounds at conventional significance levels. Consequently, the null hypothesis of no long-run relationship among the variables is rejected. This result provides strong statistical evidence of the existence of cointegration among the variables under investigation (Pesaran, Shin, & Smith, 2001).

The implication of this finding is that stock market capitalisation in Nigeria maintains a stable long-run equilibrium relationship with key monetary policy indicators, namely the monetary policy rate, money supply, lending rate, and treasury bill rate. This long-term association suggests that shifts in monetary policy instruments exert a sustained influence on the performance of the stock market, affirming the structural connectivity between monetary authority actions and capital market outcomes within the Nigerian macroeconomic environment.

4.2.4: Long-Run ARDL Model Estimation Results

Table 4: Long-Run ARDL Model Estimation Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
Dependent Variable=SMC				
MPR	-0.387995	0.468269	-0.828573	0.4141
M2	1.144210	0.043639	26.22011	0.0000
LR	-0.591189	0.183245	-3.226219	0.0031
TBR	0.676445	0.216762	3.120687	0.0041
C	-0.380523	1.715598	-0.221802	0.8260

Source: Authors' Computation, 2025

The results presented in Table 4 detail the long-run estimates of the ARDL model, providing insight into the individual effects of key monetary policy variables on stock market capitalisation in Nigeria. The monetary policy rate exhibits a negative coefficient of -0.387995 , while its associated p-value of 0.4141 exceeds the 5% significance threshold. This implies that although the relationship is inverse, the effect of the monetary policy rate on stock market capitalisation is statistically insignificant in the long run. The economic interpretation suggests that increases in the monetary policy rate are likely to reduce stock market capitalisation; however, this influence is not sufficiently strong to be considered significant within the studied period (Pesaran, Shin, & Smith, 2001).

Conversely, the money supply has a positive and statistically significant impact, as indicated by its coefficient of 1.144210 and a p-value of 0.0000 , which is well below the 5% significance level. This result affirms that an expansion in the money supply significantly enhances stock market capitalisation over time, highlighting the role of monetary expansion in stimulating investment activity and liquidity in the capital market.

In addition, the lending rate displays a negative coefficient of -0.591189 and a p-value of 0.0031 , which confirms a statistically significant inverse relationship with stock market capitalisation. This finding implies that higher lending rates increase the cost of borrowing for both firms and investors, thereby depressing capital formation and reducing equity market performance in the long run.

Finally, the treasury bill rate is associated with a positive coefficient of 0.676445 and a p-value of 0.0041 , also indicating a statistically significant positive effect on stock market capitalisation. This outcome suggests that attractive returns on government securities may encourage institutional participation in financial markets, indirectly boosting overall market capitalisation through enhanced portfolio flows and investor confidence.

Together, these findings illustrate that while some monetary policy instruments—such as money supply and treasury bill rate—exert a positive and significant influence on stock market development, others—like the lending rate—exert a dampening effect, and the monetary policy rate shows limited statistical relevance in the long run. These results offer empirical clarity on the nuanced channels through which monetary policy shapes Nigeria's capital market performance.

4.2.5: Short Run ARDL Model Estimation Results

Table 5: Short Run ARDL Model Estimation Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
Dependent Variable=SMC				
D(SMC(-1))	0.348870	0.306372	1.138713	0.2770
D(MPR)	-0.145364	0.391764	-0.371050	0.7135
D(M2)	0.898440	0.202116	4.445172	0.0008
D(LR)	-0.674595	0.184353	-3.659248	0.0033
D(TBR)	0.423768	0.107367	3.946913	0.0005
Coint Eq(-1)*	-0.591189	0.109188	-5.414420	0.0000
AdjustedR ² =0.59999;Durbin-Watson stat= 2.015478				

Source: *Authors' Computation, 2025*

The short-run ARDL model estimation results presented in Table 5 offer further evidence on the immediate impact of monetary policy variables on stock market capitalisation in Nigeria. The monetary policy rate reveals a negative coefficient of -0.145364 and a p-value of 0.7135 , which exceeds the conventional 5% significance level. This suggests that although an increase in the monetary policy rate is associated with a decline in stock market capitalisation, this effect is statistically insignificant in the short term, indicating limited short-run responsiveness of equity markets to interest rate policy adjustments (Pesaran, Shin, & Smith, 2001).

In contrast, the money supply exhibits a positive coefficient of 0.898440 with a p-value of 0.0008 , confirming a statistically significant and positive effect on stock market capitalisation in the short run. This indicates that an expansion in liquidity enhances market performance almost immediately, likely by improving investor confidence and facilitating increased participation in equity investments.

Similarly, the lending rate is negatively associated with stock market capitalisation, as evidenced by its coefficient of -0.674595 and a p-value of 0.0033 , both of which confirm a statistically significant inverse relationship. This implies that higher lending rates discourage borrowing and investment activities, thereby reducing the flow of capital into the stock market in the short run.

Furthermore, the treasury bill rate registers a positive coefficient of 0.423768 and a p-value of 0.0005 , indicating a statistically significant and positive effect on stock market capitalisation. This suggests that higher yields on government securities may attract both domestic and institutional investors, thereby boosting overall market capitalisation even in the short run.

The model's adjusted R-squared value of 0.59999 indicates that approximately 60% of the variation in stock market capitalisation is explained by the included monetary policy variables—monetary policy rate, money supply, lending rate, and treasury bill rate—while the remaining 40% is attributable to other unobserved factors captured by the error term.

Additionally, the Durbin-Watson statistic of 2.015478 suggests the absence of first-order serial autocorrelation, thereby confirming the reliability of the model's residuals.

Crucially, the error correction term, denoted as $Coint\ Eq(-1)$, bears the expected negative sign and is highly significant, affirming the existence of a stable long-run equilibrium relationship among the variables. The coefficient of -0.591189 implies that approximately 59% of the short-run deviation from long-term equilibrium in stock market capitalisation is corrected within one year. This speed of adjustment underscores the responsiveness of Nigeria's equity market to reversion dynamics following short-term disturbances.

4.2.6: Post Estimation Tests Results

Table 6: Post Estimation Tests Results

Test	F-Statistic	Probability	Null Hypothesis	Decision
Serial Correlation LM Test	0.119672	0.8885	H_0 : No serial correlation	Retain H_0
Normality Test	3.757555	0.1528	H_0 : Normal distribution	Retain H_0
Heteroskedasticity Test	0.425850	0.9581	H_0 : Homoscedasticity	Retain H_0
Ramsey RESET test	1.486538	0.2483	H_0 : Correctly specified	Retain H_0

Source: Authors' Computation, 2025

The post-estimation diagnostic checks presented in Table 6 affirm the statistical reliability and robustness of the regression model employed in this study. First, the Breusch-Godfrey Serial Correlation LM test reveals a probability value greater than the 0.05 significance threshold, indicating the absence of serial correlation in the residuals. This suggests that the model does not suffer from autocorrelation, thus preserving the validity of the estimated coefficients.

Moreover, the results of the Jarque-Bera normality test confirm that the residuals are normally distributed, thereby satisfying one of the key assumptions of the classical linear regression model (Gujarati & Porter, 2009). This implies that the estimated parameters are efficient and unbiased under the Gauss-Markov theorem.

The analysis also confirms the presence of homoscedasticity, as evidenced by the heteroskedasticity test outcome, which failed to reject the null hypothesis of constant variance. This validates that the variance of the error terms is consistent across observations and strengthens the efficiency of the estimates.

In addition, the Ramsey RESET test supports the correct functional specification of the model. The test indicates that no relevant variables have been omitted and that the model follows the appropriate linear form. This outcome reinforces the model's structural adequacy in capturing the relationship between stock market capitalisation and monetary policy indicators.

In summary, the post-estimation diagnostics confirm that the estimated model meets all the underlying classical assumptions of the Ordinary Least Squares (OLS) technique. The regression results are therefore deemed statistically sound, reliable, and suitable for inference regarding the effects of monetary policy rate, money supply, lending rate, and treasury bill rate on stock market capitalisation in Nigeria.

4.3 Discussion of findings

This study assessed the effect of Monetary Policy Dynamics and Stock Market Reactions in Nigeria, using stock market capitalisation as a proxy for market performance and four key monetary variables—monetary policy rate, money supply, lending rate, and treasury bill rate—over the period 2000 to 2024. The empirical results revealed that the monetary policy rate exerts a negative and statistically insignificant effect on stock market capitalisation in both the short and long run. Conversely, the money supply and treasury bill rate demonstrated positive and statistically significant effects, while the lending rate had a significant but negative impact on stock market capitalisation.

These findings are strongly consistent with the empirical evidence provided by Olokoyo, Osabuohien, and Salami (2021), who investigated the transmission effects of monetary policy instruments—namely, the monetary policy rate (MPR), inflation, and broad money supply—on the Nigerian stock market between 2000 and 2020. Their results showed that MPR had an inverse but insignificant influence, while money supply significantly enhanced market performance. The present study reaffirms this conclusion by confirming the positive long-run impact of money supply and the weak influence of MPR on capital market dynamics in Nigeria.

Furthermore, this study's results are in alignment with the work of Adegbite and Akanni (2022), who employed monthly data between 2005 and 2021 to explore the broader relationship between interest rate volatility and stock market reactions in Nigeria and Sub-Saharan Africa. Their study found that interest rate fluctuations had a significant negative effect, while liquidity-related instruments such as the treasury bill rate exerted positive and market-supportive effects. These conclusions support the current study's empirical observation that treasury bill rates contribute positively to stock market performance, reinforcing the liquidity transmission channel of monetary policy.

The findings also resonate with the theoretical expectations of the Monetary Transmission Mechanism (MTM). The MTM posits that monetary policy influences stock markets primarily through channels such as the interest rate, credit supply, and asset prices (Mishra & Montiel, 2012; Loayza & Schmidt-Hebbel, 2002). In line with this, the negative relationship between the lending rate and stock market capitalisation observed in this study confirms that tighter credit conditions—proxied by higher lending rates—tend to suppress equity valuations by constraining firm profitability and reducing investor incentives. On the other hand, the positive role of money supply and treasury bill rates confirms that expansionary monetary interventions, when effectively transmitted, stimulate market activity and capital formation.

Additionally, the results are partially consistent with the Efficient Market Hypothesis (EMH), which asserts that asset prices reflect available macroeconomic information (Fama, 1970). The statistically significant responses of the stock market to variables such as money supply and treasury bill rate indicate that at least some aspects of the Nigerian stock market behave in a semi-strong form efficient manner, incorporating public monetary policy signals into pricing behavior. However, the insignificant reaction to MPR and persistent distortions in the credit transmission channel may also point to informational inefficiencies typical of frontier markets like Nigeria (Ujunwa, 2012).

In summary, the empirical outcomes of this study align with both theoretical expectations and existing empirical literature. They underscore the importance of transmission efficiency, policy signaling, and investor perception in shaping how monetary policy influences stock market dynamics in Nigeria.

5.1 Conclusion

This study has empirically examined the impact of Monetary Policy Dynamics and Stock Market Reactions in Nigeria. The findings indicate that the effect of monetary policy differs across economies depending on market structure and responsiveness. Specifically, the monetary policy rate has a negative and insignificant impact on stock market capitalisation, while money supply and treasury bill rate show positive and significant effects. Conversely, the lending rate has a significant negative effect. The study concludes that monetary policy variables play a crucial role in shaping stock market performance in Nigeria.

5.2 Recommendations

Based on the findings of this study, the following recommendations are made.

- i. The Central Bank of Nigeria should consider lowering the monetary policy rate to a single digit to boost investor participation in the stock market.
- ii. Increasing the money supply can enhance business activity and support stock market growth, and should therefore be encouraged.

- iii. Monetary policy decisions, especially on lending rates, should carefully reflect current economic realities to avoid triggering inflation that could harm market performance.
- iv. Expansionary policies that promote liquidity should be prioritized, as they improve firms' access to funding and strengthen stock market outcomes.

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