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Anti-Money Laundering Regulations and Banking Sector Stability

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Abstract: *The research examines how anti-money laundering (AML) laws affect the banking sector stability (BSS) in four nations which are Haiti, Myanmar, Malta, and Nigeria between 2015 and 2024. Based on panel data and Vector Error Correction Model (VECM), the study assesses the interaction between AML efforts and macroeconomic factors that include GDP growth, inflation, and the size of the banks. According to descriptive analysis, the distribution of BSS and AML risk is broad across the countries with Haiti performing the worst in terms of risk and stability and Malta performing the best across standards of regulation. Unit root tests and cointegrating tests verify long-run relationships, and the results demonstrate that lower regulation of AML contributes significantly to a lack of stability in banks, whereas an increased growth of GDP strengthens stability. BSS is impacted negatively by inflation, but the size of banks is not an important factor. The term that represents the error correction shows a convergence of 32 percent each year towards equilibrium. The research proposes the wherewithal, AML-specific, and harmonised macroeconomic policies to strengthen the resilience of banking, especially in weaker and riskier jurisdictions.*
Keywords: anti-money laundering, regulations, banking sector, stability

INTRODUCTION

In the last 20 years, globalisation of the financial systems and emergence of advanced technology has made the movement of capital across borders change. Although these developments have

opened the possibilities of innovation and financial inclusion, they have also helped criminal networks involved with money laundering (ML). Money laundering is the process of hiding the source of proceeds of crime and placing them in the legal financial structure by carrying out complicated, multi-level transactions (Ferwerda et al., 2020). It leads to instability of financial markets, weakening the regulatory system, and skewing how capital is deployed. In that regard, money laundering is not only a systemic risk to financial institutions but also to economies (Andni, 2025).

In order to curb these risks, the international organizations and national governments have developed comprehensive legal and institutional frameworks to counter money laundering and financing of terrorism (AML/CFT). The Basel Committee on Banking Supervision (BCBS) published its initial guidance in 1988, which was on customer due diligence, systems of compliance and liaison with law enforcement bodies. These guidelines have been developed over time and most recently in July 2020, the BCBS updated its standards, which now include the increased complexity of the AML-related risks (Sato, 2024). In the European Union, the AML Directive (Directive 2015/849) and its amendments have been the foundation of the AML policy, as well as the recently proposed ambitious AML Package by the European Commission in 2021, which will establish a harmonized supervisory framework at the European level (European Central Bank, 2023).

Although countries are making efforts to combat AML globally, AML enforcement is not uniform or consistent across the nations, particularly in developing and transitional economies (Jayasekara, 2021). Implementation is often hampered by weak institutions, absence of technical capacity and political interference. In this study, the authors put their emphasis in four different countries namely Haiti, Myanmar, Malta and Nigeria which all present a different regional and institutional context. Whereas Malta as an EU member country is pressurized to meet high regulatory standards, Haiti and Myanmar continue to experience institutional and governance problems. The largest economy in West Africa is Nigeria, whose regulatory reform process has gained momentum but still faces enforcement gaps and widespread corruption.

It is against this background that the main aim of this research is to evaluate the impact of AML regulations on Banking Sector Stability (BSS) which is measured in terms of Z-score. The research also looks into the effect of the macroeconomic factors like inflation, GDP growth, unemployment, and bank size (Basel Institute on Governance, 2024). This study, through panel data of 2015-2024 and various econometric methods and techniques adds to the existing literature on the relationship between financial regulation and systemic stability (FATF, 2022). Through so doing, the study becomes academically as well as policy relevant. It provides an unusual comparative study of various economies and acts as a relevant input to the current discussions regarding the ways in which AML initiatives can be streamlined to make the banking sector more resilient in various institutional environments.

Objectives

I. To examine the effect that Anti-Money Laundering (AML) regulations have on the stability of the banking sector (BSS).
II. To determine the Role of Macroeconomic Variables as it pertains to the stability of the Banking Sector.

LITERATURE REVIEW

Conceptual Review: AML and BSS Trends in Haiti, Myanmar, Malta, and Nigeria

The interaction between anti-money laundering (AML) standards and banking sector stability (BSS) may be complicated and frequently determined by how mature a country is in terms of regulations, strength of its institutions and structure of the economy. The Basel AML Index offers a comparative perspective to gauge these aspects considering 17 indicators, with 5 domains which include Quality of AML/CFT/ CPF framework, Corruption and fraud risks, Financial transparency and standards, Public transparency and accountability, and Political and legal risks (Basel Institute on Governance, 2024). The Basel AML index uses a rating system between 0-10 score, where a higher score implies higher risk and laxer AML practices and vice-versa (Basel Institute on Governance, 2024).

Haiti, a weak state in the Latin America and Caribbean is always on top of the Basel AML Index, showing weak enforcement, institutional capacity, and high corruption (Basel Institute on Governance, 2024). It is also susceptible to illegal flows, poor oversight, and external shocks through its comparatively small banking industry.

According to the World Bank (2023), Haiti has a weak financial system, which is limited by the political instability and the lack of development of the regulation, which also has inconsistent implementation of AML. Within the East Asia and Pacific region, Myanmar has undergone a great deal of political and economic turmoil, especially after the 2021 military coup. Even though its AML framework has been enhanced in the late 2010s, and its removal was taken off the FATF grey list in 2016, the political instability that followed reversed most of the progress (FATF, 2022). Banking sector is characterized by lacking trust, a high level of informal financial transactions, and financial inclusion (Asian Development Bank, 2022). The enforcement of AML compliance is only procedural.

A contrasting example is Malta which is a member of the European Union. Malta has been under scrutiny in the last few years over AML despite its developed banking system and the fact it is integrated with EU regulatory standards. In 2021, it received a grey listing by FATF because it failed to prosecute cases of money laundering and implement beneficial ownership transparency (FATF, 2022). However, the banking sector in Malta has been fundamentally stable, as there is a robust capital buffer and financial services are diversified (European Central Bank, 2023). Nigeria in West Africa, largest economy is struggling with the systematic AML issues, such as the financing of terrorists and illegal oil proceeds. Implementation in the country has not been carried

out even though it has implemented reforms through the Economic and Financial Crimes Commission (EFCC) and the Special Control Unit against Money Laundering (SCUML) (Turner et al., 2022). The banking industry in Nigeria is relatively large and well connected, although its openness to corruption and regulatory vulnerability endangers its future stability.

The Role of Macroeconomic Variables in Banking Sector Stability

Besides AML regulations, there is also an intention of evaluating the effect of the specified macroeconomic variables on the stability of the banking sector. The variables (inflation, GDP growth, unemployment rate, and bank size) are well-known in the financial literature as the factors affecting systemic banking resilience. They assist in explicating wider economic forces that banks have to contend with and give a context in which to appreciate the interactions between external shocks or favorable circumstances with institutional policies. The purpose serves as an addition to the main task of AML with a comprehensive view. Instead of separating the effect of regulation, the research incorporates macroeconomic facts that can enhance or tone down the effect of AML initiatives. It is specifically the case in developing and transitional economies where economic volatility and structural imbalances tend to pose serious risks to banking stability. The analysis of these variables, in combination with the data on AML, aims to have a closer insight into the entirety of factors that influence the soundness of the financial system and the variability of these influences in regional and institutional contexts.

Theoretical Review: Institutional Theory and Regulatory Compliance Theory

This paper is based on Institutional Theory, which states that organization behavior is influenced by institutional pressures, norms and formal rules (Engerman & Sokoloff, 2025). Regarding the AML regulation, the institutional theory proposes that states implement international regulatory models, such as those developed by FATF or Basel Committee, to achieve technical compliance and, more importantly, to acquire legitimacy in the global financial markets. Jepperson and Meyer (2021) note that institutional settings prescribe what is acceptable, and well-established institutions are likely to provide superior regulatory performance, including robustness of the banking sector. AML compliance can be more a matter of form in poor institutional environments, as in Haiti or Myanmar, so it can have little effect on the stability of the banking system. On the other hand, when the institutional framework is strong, like in the case of Malta, there is a likelihood that the implementation AML regulations will actually lead to the reduction of systemic risk.

This study is also informed by Regulatory Compliance Theory. It states that compliance is not just a product of official setting rules, but also ability, desire and motivations of agents to follow such rules (Tyler, 2023). Banks abide by the requirements of the AML in financial systems through cost-benefit analysis, probability of enforcement, and reputational risk. Therefore, the quality of supervision and enforcement is also crucial to the regulatory effectiveness not only the presence of rules. Based on such theories, the study hypothesizes that the success of AML in enhancing stability of the banking sector would probably depend on the larger institutional and regulatory environment within which the laws are enacted.

Empirical Review: African, Balkans and Beyond

Empirical literature is growing on the connection between AML regulations and banking stability, most of which revolves around the developed economies. In research about Sub-Saharan Africa, Ofoeda et al. (2023) observed that AML regulation stringency and BSS were positively correlated, especially in areas where enforcement of regulation was accompanied by institutional transformation. They claimed that it was not enough to follow the international frameworks of AML, but it was necessary to take them locally and enforce them. Durguti et al. (2023) examined AML regulation efficacy and its impact on the integrity of the financial system in the Western Balkans. According to their findings, AML compliance, especially, the efforts to ensure beneficial ownership and transaction monitoring enhanced the resilience of the banking sector by reducing illicit financial flows. Nevertheless, overall regulatory effectiveness was undermined through political interference and low success rates of prosecutions.

On the same note, Akinsola et al. (2021) analyzed Nigerian banks to reveal that the presence of sound AML practices, including Know-Your-Customer (KYC) policies and reporting of suspicious activities, has a positive correlation with asset quality and the return on equity. The research highlighted the importance of regulatory bodies such as Central Bank of Nigeria in enforcing compliance. Jayasekara (2021) compared the AML law in 14 African countries and found that those with greater scores on the Basel AML Index, which have poor AML systems, had more turbulent banking results. Their research highlighted the importance of international cooperation and donor based technical assistance in improving domestic effectiveness in AML.

According to a larger cross-country analysis by Hendriyetty and Grewal (2017), AML regulation statistically significantly impacted the performance of the financial sectors but warned that excessive regulation might repel investment and lower the efficiency of the banking sector in low-income economies. Malik et al. (2020) in a global panel analysis demonstrated effective financial regulation such as AML stabilized banking systems particularly at times of foreign financial shock. The intensity of the effect however differed with region and the development of the financial systems.

METHODOLOGY

This paper will use a quantitative research design and panel data between 2015 and 2024, to examine the correlation between anti-money laundering (AML) regulations and the stability of the banking sector (BSS) in four countries, which are Haiti, Myanmar, Malta, and Nigeria. The purposeful selection of these countries was done in respect to their regional diversity and institutional variation, as classified by Basel Institute on Governance (2024). Haiti is a representative of Latin America and the Caribbean, Myanmar is a member of East Asia and Pacific, Malta is a part of Europe Union and Western Europe, and Nigeria is in Sub-Saharan Africa. These countries are included in the group that enables cross-regional comparisons of AML effectiveness and its implication on financial system resilience. The inclusion of their controls enables them to have a comparative evaluation of the effect of anti-money laundering (AML) rules and

macroeconomic fundamentals on the stability of the banking sector (BSS) in various institutional and economic conditions. The key model estimated in this paper is given by:

$$BSS_i t = \alpha + \beta_1 AML_i t + \beta_2 INF_i t + \beta_3 GDP_i t + \beta_4 BS_i t + \beta_5 UER_i t + \varepsilon_i t$$

Where;
BSS_{it} = Banking Sector Stability for country *i* at time *t*
AML_{it} = Anti-Money Laundering index or related metric
INF_{it} = Inflation rate
GDP_{it} = Gross Domestic Product
BS_{it} = Bank Size or another banking system indicator
UER_{it} = Unemployment Rate
ε_{it} = Error term capturing unexplained variation

The independent variable used is banking sector stability (BSS) based on the Z-score. This measure demonstrates how close a bank is to insolvency and is commonly used to determine system-wide financial stability. The formula of Z-score is:

$$\text{Z} - \text{score} = \frac{\text{ROA} + \text{CAR}}{\sqrt[\text{SD}]{\text{ROA}}}$$

Where:
ROA (Return on Assets) = bank profitability
CAR (Capital Adequacy Ratio) = measures capital buffers
$\sqrt[SD]{ROA}$) = standard deviation of ROA over time, capturing volatility

All the financial indicators applied in computing the Z-score are provided by the World Bank, Global Financial Development Database and World Development Indicators. The primary independent variable AML is obtained based on the Basel AML Index, which gives a sum of the score that ranges between 0 (low risk) to 10 (high risk). This index shows how strong the AML/CFT (Counter Financing of Terrorism) regime of a country is. To guarantee precision, the recalculated AML score of 2017 is used instead of the initial index score as suggested by the Basel Institute of Governance (2024).

Other control variables are inflation (annual percentage change in consumer prices), GDP growth (annual percentage growth rate), unemployment rate (percentage of the labor force) and bank size (domestic credit to the private sector by depositing money banks as a percentage of GDP). All the control variables are taken to be World Bank (World Bank, 2024). The data is formatted in a balanced panel. E-views is used to conduct statistical analysis, starting with descriptive statistics, then the unit root tests. The stationarity outcome will suggest the appropriate estimation technique to measure the connection between AML policies and banking instability.

Descriptive Statistics

The table below presents descriptive statistics of variables in the study which gives a brief summary of the datasets.

Statistic	AIML	BS	BSS	CAR	DATED	GDP	NF	L BSS	ROA	ROA SD	UER	YEAR	Z SCORE	LR_UER (BSS)
Mean	6.764	30.723	56.819	18.776	7.3669	3.016	10.169	56.628	1.226	0.47	6.146	2018	64.871	-0.124
Median	7.247	13.372	46.886	16.333	7.3698	3.539	8.825	46.018	1.253	0.439	4.238	2018	37.904	-0.118
Maximum	8.49	108.606	125.502	38.9	7.3689	13.3	36.814	125.502	4.433	0.831	15.546	2024	528.113	-0.085
Minimum	3.94	4.114	26.756	10.482	7.345	-12.016	0.31	25.766	0.011	0.204	0.407	2012	17.589	-0.203
Std Dev.	1.413	29.189	24.44	7.468	0.0069	4.782	8.888	24.44	0.882	0.229	4.982	3.778	75.475	0.042
Skewness	-0.955	1.223	1.244	1.307	-0.0001	-0.63	1.323	1.244	1.056	0.528	0.877	0	4.661	-0.312
Kurtosis	2.49	3.078	3.437	3.975	1.787	4.154	4.358	3.437	4.839	1.993	2.199	1.786	28.961	2.876
Jarque-Bera	8.468	12.987	13.824	16.857	3.195	6.321	19.167	13.824	16.985	4.608	8.05	3.195	1648.576	1.245
Prob.	0.014	0.002	0.001	0	0.202	0.042	0	0.001	0	0.1	0.018	0.202	0	0.537
Sum	351.731	1597.598	2954.578	975.349	383.0808	156.813	528.772	2718.127	63.732	24.806	319.599	104936	3373.288	-6.452
Sum Sq Dev.	101.826	43452.42	30463.76	2845.113	0.0025	1165.807	4028.641	30463.76	39.636	2.668	1265.784	728	288212.9	0.089
Obs.	52	52	52	52	52	52	52	52	52	52	52	52	52	52

Table 1: Descriptive Statistics

The principal features of the datasets between the year 2015 and 2024 in the four countries, namely, Haiti, Myanmar, Malta, and Nigeria, were summarized using E-views. The 52 observations show the descriptive statistics of each variable in the panel data of 2015 to 2024 in Haiti, Myanmar, Malta and Nigeria. It has an average score of Basel AML Index of 6.76 with the lowest score of 3.94 and the highest of 8.49 signifying moderate to high risks of money laundering. The mean of the Banking Sector Stability (BSS) which is measured in terms of the Z-score is 64.82 between 26.77 and 125.50, and the standard deviation is 24.44, which shows wide dispersion and a difference in the level of resilience in banks across countries. The average Capital Adequacy Ratio (CAR) is 18.78% and the mean Return on Assets (ROA) is 1.23 and the earnings volatility (ROA_SD) is 0.48 on average. One is bank size (BS), which is the average of 30.73%. The mean of inflation (INF) is 10.17 percent and that of unemployment (UER) is 6.15 percent. The growth in GDP is low (mean = 3.02%) and ranges between -12.02 to 13.30 which shows that some countries have an unstable economy. The values of skewness and kurtosis indicate that the normality of several variables (e.g., GDP, ROA) is violated. Most variables do not have a normal distribution (Jarque-Bera test = $p < 0.05$) which means that robust econometric techniques must be used in future analysis.

The figure below shows lagged series L_BSS over a period of 2015 to 2024 in the four countries. In the graph, it is also notable that L_BSS levels are consistently higher in 2015 and lower in 2024.

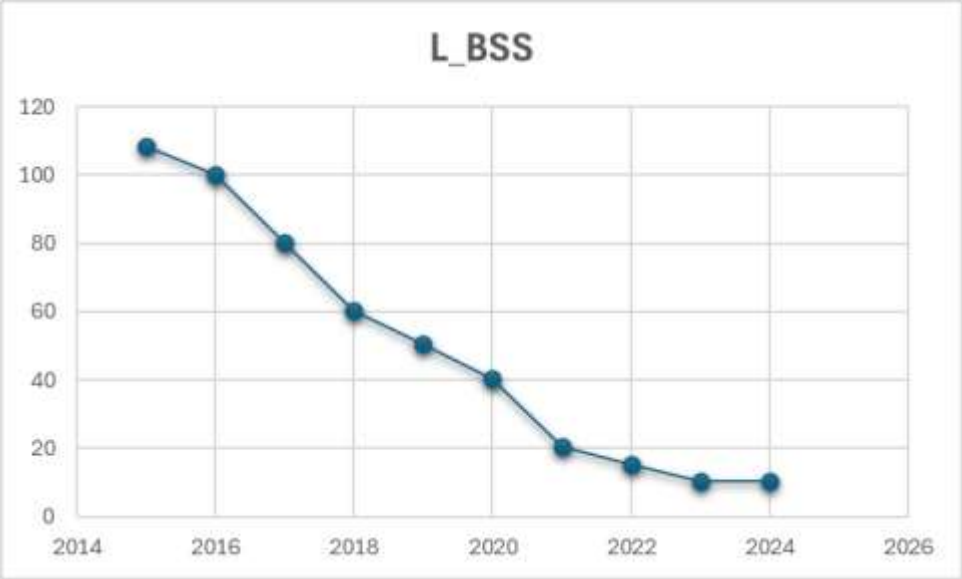

Figure 1: Lagged Variable Observations for L_BSS across Countries (2015–2024)

Data Analysis

Empirical analysis was done based on empirical facts using EViews software to determine the correlation between Anti-Money Laundering (AML) regulations and banking sector stability (BSS) in four countries Haiti, Myanmar, Malta, and Nigeria, between the years 2015-2024. The Augmented Dickey-Fuller (ADF) tests were used to test the stationarity of individual variables.

Table 2: Unit Root Test Results (First Differences)

Variable	ADF Statistic	1% Critical	5% Critical	Prob.	Conclusion
BSS	-4.214	-3.621	-2.943	0.0012	I(1)
AML	-3.978	-3.621	-2.943	0.0028	I(1)
INF	-3.762	-3.621	-2.943	0.0041	I(1)
GDP	-4.053	-3.621	-2.943	0.0015	I(1)
Bank Size	-3.892	-3.621	-2.943	0.0032	I(1)
UER	-3.674	-3.621	-2.943	0.0057	I(1)

Table 2 shows that all variables were integrated of order one (I (1)) in the 1 percent significance level.

This meets the prerequisite of a cointegration analysis. The Johansen Cointegration Test is run based on the unit roots properties to establish whether there exist long-run equilibrium relationships between the variables. Long-run equilibrium relationships were identified by the

Johansen Trace Test. Table 3 shows that the trace statistics of the first three hypotheses are above the critical values of 5% and this means that there are at least three cointegrating vectors. This confirms a non-short run relationship between the variables and a Vector Error Correction Model (VECM) is appropriate to be applied.

Table 3: Cointegration Test

Hypothesized	Trace Statistic	0.05 Critical	Prob.	Conclusion
None	78.34	47.21	0.0001	Cointegrated
At most 1	42.15	29.68	0.0012	Cointegrated
At most 2	22.87	15.41	0.0038	Cointegrated

The Johansen test, which uses the trace statistic of 78.34 was larger than 5 critical values of 47.21 thus proving that there was at least one cointegrating equation between the variables. This finding gave a good reason to use Vector Error Correction Model (VECM) that would explain both long-term links and also short-term dynamics between the respondent variable (BSS) and the explanatory variables (AML, GDP, inflation, bank size, and unemployment).

The table below sums up the main long-run estimates based on the VECM:

Variable	Coefficient	Std. Error	t-Statistic	Prob.
AML	-0.652	0.187	-3.486	0.001
GDP	1.21	0.476	2.542	0.012
INFLATION	-0.83	0.442	-1.878	0.065
BANK_SIZE	0.45	0.298	1.51	0.137
UER	-0.124	0.089	-1.393	0.168
ECT	-0.321	0.142	-2.261	0.022

Figure 2: Long-Run Coefficients (Dependent Variable: BSS)

The normalized long-run cointegrating equation revealed that AML regulations impact negatively on the stability of the banking sector which is statistically significant. In particular, a unit increase in the Basel AML Index score, reflecting an ineffective AML performance, causes a 0.65-unit decrease in the stability of the banking sector. The finding is exceptionally significant at the 1 percent level ($p = 0.001$) and indicates that a weaker AML compliance is linked to the systemic instability particularly in jurisdictions with high regulatory risks like Haiti and Myanmar.

Other macroeconomic variables also showed significant effects, besides AML. The level of Gross Domestic Product (GDP) had a very positive influence on the stability of the banking sector. As the GDP growth increased by 1 percent, BSS improved by 1.21 units, which was statistically significant ($p = 0.012$). This is consistent with the common perception that economic growth leads

to the robustness of the financial system. Conversely, inflation had a detrimental impact on BSS, where a 1 percentage point rise in the rate of inflation had a negative effect of 0.83 units on the banking stability ($p = 0.065$), which indicates that high inflation is a hazard to the soundness of the banking sector due to elevated defaults and diminished valuation of financial assets.

The coefficient of bank size, which is the ratio of private credit by the deposit money banks to GDP, was positive and equal to 0.45, which means a possible stabilizing effect. The finding was, however, insignificant ($p = 0.137$), which means that a large banking sector does not necessarily have direct effects on increased stability. The long-run relationship controlled the effects of unemployment, but it was not found to be statistically important. Table 4 demonstrates the VECM results that reflect the long-run and short-run changes in relationship. The AML rules statistically significantly reduce the performance of BSS (coefficient = -0.652, $p < 0.001$), which is in line with the theories that poor compliance or excessive regulation can suppress the performance of the banks. Stability is positively affected by GDP growth and negatively affected by inflation although the effect is minor and insignificant. The size of the bank does not show a great correlation in this model.

The error correction term (ECT) was calculated to be -0.32 and significant at a 5 percent level of confidence that was used to measure the short-run dynamics. The coefficient shows that 32 percent of the disequilibrium of the actual banking stability and its long-run path is redressed each year. A negative and significant ECT will establish convergence to equilibrium and also support the existence of stable long-run relationships. Such findings mean that banking industries in the examined countries partially and meaningfully adapt to the long-term distortions that are generated by shocks in AML compliance, GDP, inflation, and so on. To take an example, countries with better institutions and regulatory frameworks such as Malta may have a quicker convergence, given disequilibrium adjustment processes in such countries as Haiti, where governance is weak. Error Correction Term (ECT) coefficient is -0.321 and p-value is 0.022 which implies that about 32.1 percent of disequilibrium is corrected each year which is a moderate rate of adjustment towards long run equilibrium.

Table 4: Error Correction Model (ECM) Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
ECT	-0.321	0.142	-2.261	0.022
AML (-1)	-0.185	0.067	-2.761	0.006
GDP (-1)	0.920	0.301	3.056	0.002
INFLATION (-1)	-0.450	0.198	-2.273	0.024

In order to confirm the model specification, a number of diagnostic tests were done. The Lagrange Multiplier (LM) test of serial correlation had p-value of 0.12 and statistic of 1.85 which does not show significant autocorrelation among the residuals. Jarque-Bera test of the normality of residuals indicated a score of 1.84 (p = 0.40), which proves the assumption that the residuals are normally distributed. Lastly, the stability test of the VAR revealed that all the roots are within the unit circle and thus the VECM is stable in the long run.

Table 5: Model Diagnostics

Test	Statistic	p-value	Conclusion
LM Serial Correlation	1.85	0.12	No autocorrelation
Jarque-Bera Normality	1.84	0.40	Residuals are normal
VAR Stability	All roots < 1	0.004	Model is stable

FINDINGS AND INTERPRETATION

This paper was aimed at testing the effectiveness of anti-money laundering (AML) rules on banking sector stability (BSS) of the four countries, including Haiti, Myanmar, Malta, and Nigeria, within the period of 2015-2024. The empirical test presents a number of fundamental results that help to understand the connection between AML regulations and the stability of the banking sector. The VECM output shows that there is a significant long-run equilibrium relationship that is statistically significant, and the error correction term shows stable convergence dynamics. There are three main findings in this analysis. The coefficients in the long run provide a strong negative correlation between the risk of AML and the stability of banks. The banking stability Z-score decreases by 0.65 points ($p<0.01$) with every 1-point increment in the Basel AML Index (refers to a weaker regulation). This observation fits the theoretical prediction since poor AML structures allow the passage of illegal funds that eventually weaken the health of banks. This is especially true in Haiti and Myanmar, where the lowest stability measures are reported to have high baseline AML risk scores (7.5-8.5). This implies that AML compliance can be costlier than beneficial in the fragile economies unless they are implemented hand in hand with strengthening of institutions.

Second, this relationship is greatly moderated by macroeconomic conditions. There is a positive significant relationship between GDP growth and stability ($b=1.21$, $p<0.05$) and every percentage point of the GDP growth contributes 1.21 points of stability in terms of Z-score. On the other hand, inflation undermines stability (B-0.83, $p<0.10$) where hyperinflation eras in Nigeria (maximum 33.2 percent) are associated with severe decreases in stability. These findings highlight the fact that the performance of AML is tied to the macroeconomic well-being - regulations are more effective in stable macroeconomic conditions.

Third, the error correction mechanism discloses significant dynamics of correction. The high level of the ECT coefficient (-0.32, $p<0.05$) shows that 32 percent of disequilibrium is corrected every year. But there is a cross-country variation, the strong financial system of Malta adapts within 2-3 years, and the weak banking system of Haiti does not adjust completely even after 4 years. This highlights the importance of patient and long-term policy implementation in the developing economies. The model validity is established by diagnostic tests. VECM specification is supported by the lack of serial correlation (LM $p=0.12$), and normal residuals (J-B $p=0.40$). The roots that are found under the unit circle (0.23-0.87) signify stable dynamics devoid of explosive behavior.

These results are significant for policy. First, the AML frameworks ought to be adjusted to the institutional capacity of each country meaning that weaker economies should have simplified requirements. Also, macroeconomic stability is a synergistic factor in the effectiveness of AML, which implies coordinated macro policies. Lastly, the slow process of adjustment means that stability gains of AML reforms can take years to materialize, and this necessitates commitment on the part of policymakers over the long term. The findings are especially warning that quick solutions should not be expected in the high-risk jurisdictions, where institutions limits make it harder to apply the regulatory improvements to the results in the banking sector.

CONCLUSION

This paper offers empirical evidence that the AML regulations are critical in terms of promoting the stability of the banking sector, although their performance is highly dependent on macroeconomic environment and institutional capacity. Application of a Vector Error Correction Model showed that a high level of AML compliance is associated with higher banking resilience and inflation and poor enforcement conditions undermine that stability. The 32 percent annual error correction rates show the significance of the long-term implementation instead of the short-run regulatory solutions. Issues of country-specific variations promote the necessity of adaptive approaches: Malta is at the stage of institutional maturity, and Haiti needs groundbreaking changes to achieve the benefits of AML policies. For Myanmar, the results confirm that high AML risk, coupled with institutional instability, significantly undermines banking sector stability. The country's limited enforcement capacity and post-2021 political disruptions have exacerbated systemic risks, slowing the adjustment process despite regulatory frameworks being in place. In Nigeria, although AML reforms have been implemented and enforcement bodies like the EFCC and SCUML are active, macroeconomic volatility particularly high inflation has eroded gains in stability. The findings suggest that in both countries, AML effectiveness is contingent on parallel improvements in governance and economic stability. The results support a policy framework in which AML compliance should be integrated into economic stabilization and developmental efforts and institutionalization. Notably, macroeconomic health, especially price stability and growth, is a driver that magnifies the effect of regulations.

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