WWW.IJRPR.COM

International Journal of Research Publication and Reviews

Journal homepage: www.ijrpr.com ISSN 2582-7421

Effect of Capital Flight on Economic Growth in Nigeria

Okerekeoti, Chinedu U. & Emeneka, Ogochukwu L.

Department of Accountancy, Nnamdi Azikiwe University, Awka
Mail: nattyhoodz@yahoo.com; o.emeneka@unizik.edu.ng

ABSTRACT

The study examined the effect of capital fight on economic growth in Nigeria. *Ex Post Facto* research design was adopted for the study. The population of the study consist of all data on capital flight and gross domestic product from 1981 to the 2019 period in the Central Bank of Nigeria Statistical Bulletin. The Descriptive Statistics and Least Squares regression technique were used to analyze the data via E-view 9.0. The study found that the effect of current account balance on gross domestic product is negative and significant. This implies that increases in current account balance will have a significant negative impact on growth. In the light of the study findings, the recommended that while the findings shows that current account balance was deficit in the country's import. Government should address suit to ensure surplus position to improve in exporting goods and services more than is importing.

Keywords: Capital fight balance, Current account balance and Gross domestic product

Introduction

The primary focus of public authorities and other policymakers in Nigeria has been on macroeconomic policies regarding interest rates and other crucial indicators. Despite the fact that the economic reform policies implemented in the 1980s achieved a number of significant levels of success; However, despite the reforms to the financial sector's liberalization, there are still a number of obstacles to overcome. The interest rate's inefficiency has a devastating effect on borrowing costs and overall investment. Although a variety of expansionary monetary policies have been implemented to counter the destabilizing effect and further stimulate economic activity, the central bank has been required to raise interest rates due to the increased inflationary pressure on the economy. Consequently, the interest rate mechanism becomes contentious and does not align with other macroeconomic goals.

Even though there is a lot of research on this phenomenon, little has been written about how the real interest rate affects how productive a market-oriented economy like Nigeria's is.In addition, the empirical literature lacks a strong consensus regarding the direct or precise impact of the interest rate and its effects on other essential indicators. In addition, previous research on this phenomenon has largely ignored sub-Saharan Africa in favour of developed nations and other Asian economies. The effects of interest rates on long-term economic growth are at best inconclusive, even in such studies (especially those on the Nigerian economy).This is because of the Nigerian economy's recent recession, which reduced the country's productive capacity and made it possible for monetary authorities to restore stability. In addition, the devastating effects of global oil prices had an impact on the economy as a whole, as did a number of obstacles. According to Adegbite and Ayadi, this scenario has led to structural imbalances, which have affected the nation's capacity to mobilize revenue, its large and inefficient public sector, its inadequate capacity for savings and investment, and its persistently large fiscal deficits.

Monetary policy alone did not result in development, as stated in the Central Bank of Nigeria's Annual Report and Statement of Accounts for the year ended December 31, 2007.According to Mordi, Englama, & Adebusuyi (2010), Nigeria's economy appeared to be getting better in 2000, when the real GDP growth rate increased to 3.8%, up from 2.8% in 1999 and 1.8% in 1998, respectively.

After the oil price increased from $18 per barrel in 1999 to $28 per barrel in 2000, the positive terms of trade shock was largely responsible for the improved growth performance in 2000 (Abwaku, 2010).In addition, the economy is still largely beset by the large and ineffective public sector, low savings and investment rates, persistently large budget deficits, and inconsistent macroeconomic conditions (Eze, 2010).The expansion of the economy has been hampered by all of these (Sanni, 2006);and Nigerians continue to look forward to brighter times in which changes in interest rate management and the exchange rate could help the economy grow. According to Obansa, Okoroafor, Aluko, & Eze (2010), the observed effects of exchange rate and interest rate management on macroeconomic variables that would lead to economic growth are, however, sluggish, if not unsustainable.

Nigeria's gains from domestic investment and international trade do not match the reform that was put in place to achieve robust results. The economy's lending rate is still very high in comparison to the deposit rate, making it difficult to access funds for investment (Oweoye, 2007).The end result is that the Nigerian economy has not benefited significantly from nearly four decades of policy somersault, particularly in interest rate and exchange rate management (Onagowora, 2007).

As a means of closing the savings-to-investment gap, many developing nations have turned to borrowing from outside sources. However, it is paradoxical that wealthy residents and political officeholders of these debtor nations are diverting vast sums of money abroad despite the countries' lack of resources. With a loss rate of almost $10 billion annually due to capital flight, Nigeria leads the African League of Nations affected by this threat.

Others are Egypt, Algeria, Morocco and South Africa. It is against this backdrop that this study examined the effect of capital flight on economic Growth in Nigeria, using current account balance and gross domestic product.

Literature Review

Capital Flight in the Nigeria Economy

When compared to the amount of investment made in Nigeria during the same time period, the magnitude of capital flight from Nigeria in recent years is concerning. Additionally, this reduces the potential for economic expansion. For instance, estimates of Nigeria's capital flight in 2010 in dollars were $311,431.3 million, or roughly 158.2% of GDP. Indeed, Deppler and Williamson (1987) complain that Nigeria's economic growth is significantly slowed by an amount comparable to the magnitude of capital flight. This assertion is supported by current research (Lawanson, 2008; Adetiloye, 2012).
As politicians, corporations, and foreign investors massively move funds out of the country, the Nigerian economy is losing a lot of money. According to a survey of public payments made by the Central Bank of Nigeria (CBN), $22.1 billion left the country over the course of five weeks, or an average of $4.5 billion per week. Foreign exchange outflows increased to $5.35 billion for the week ending November 30, 2014, compared to approximately $3.083 billion for the week ending July 31, 2014 (CBN Statistical Bulletin 2014).The naira exchange rate, which had been stable prior to the 2015 elections, is said to have fallen as a result of capital flight. However the CBN has credited the breakdown of the naira to money examiners who purchase and hold cash to sell sometime not too far off at a higher rate to make gain, the development of assets out of the nation stops via Nigerian occupants purchasing up dollars with their naira and moving it seaward.
Nigeria's foreign reserves are said to have been depleted as a result of capital flight, weakening the naira. At $5.4 billion in 1999, Nigeria's foreign exchange reserves increased dramatically to $51.3 billion at the end of 2007 and $53.0 billion in 2008.However, the reserves fell further from $38.138 billion at the end of April 2014 to $33.04 billion in February 2015 due to the 2008 crash in the international price of crude oil and the global financial crisis that followed (World Bank, 2015).According to Ndikumana (2000), capital flight has led to significantly lower investment levels in many African economies, including Nigeria. According to World Development Indicators (2015), domestic investment in Nigeria totaled $43.8 billion in 1990.In 1992, this number fell to $37.3 billion, and it fell even further to $20.1 billion in 1995.The country saw a massive outflow of capital totaling over $900 billion between 2010 and 2015, compared to a relatively low level of domestic investment totaling approximately $134 billion. The multiplier effects on other aspects of the economy, such as the rate of unemployment and income distribution, with such levels of investment cannot help but raise questions.

Current Account Balance on Economic Growth

The current account balance is a measure of the inflow and outflow of goods and services, primary and secondary investment income, unpaid transfers, and employee compensation, typically in domestic currency. In the balance of payments account, it is one of the two major accounts (Sanni, Musa and Sani, 2019). The on going record balance reflects a country's exhibition in unfamiliar exchange labor and products and could be in excess or shortage. A country's surplus position indicates that it imports fewer goods and services than it exports; while a deficit indicates that a nation imports more than it exports from the outside world. The savings investment gap, or current account balance, is the difference between national savings and investment. As such, it is the distinction among pay and retention in the economy. A country is said to have a current account deficit if it absorbs more than it produces in this instance; indicating that foreign savings finance the majority of the country's investment. It indicates a low level of national savings, which causes the external reserves needed to finance economic activities to run out. A country, on the other hand, has a current account surplus if it produces more than it consumes. This demonstrates that national investments outnumber national savings. The current account balance is an important indicator of competitiveness (Sanni, Musa, & Sani, 2019).Creditors from other countries use the balance to assess an economy's creditworthiness. Non-residents' investment decisions are guided by it because it helps policymakers assess the economy's viability and the effectiveness of macroeconomic policies, particularly export promotion and growth-stimulating ones. In addition, it clearly identifies which economic sector requires attention. However, due to the unique characteristics of various economies, an evaluation based on the robustness of the current account position is necessary but not sufficient to determine sustainability. In some economies, what is sustainable may not be sustainable in other economies. Other indicators of sustainability, such as solvency and excessive current account balance, have been the subject of research (Aysu & Fazil, 2012).
However, the size and direction of an economy's economic growth—often expressed as a change in GDP over time—is the most important indicator of its overall health. The increase in the number of goods and services produced by an economy or nation over a specified or measurable time period is known as economic growth. It is a steady and positive rise in the total number of goods and services produced in an economy over a given time period. A proxy for economic expansion is the gross domestic product (GDP); The real GDP, which represents the value of all final goods and services produced in a nation, is what it is called when it is adjusted for inflation (Sanni, Musa, & Sani, 2019).

Empirical Review

Orji, Ogbuabor, Kama, and Anthony-Orji (2020) looked at how capital flight affected Nigeria's economic growth from 1981 to 2017.The study used the Autoregressive Distributed Lag (ARDL) bounds test method. According to the study, both short-term and long-term economic growth are significantly hampered by capital flight. Money supply, credit to the private sector, and domestic investment are additional variables that have been found to have a significant impact on economic growth. The work by Adedayo and Ayodele (2016) provides an empirical analysis of the impact that capital flight has on the economy of Nigeria. Secondary data from the National Bureau of Statistics and the Central Bank of Nigeria's Statistical Bulletin of various issues were used in the study. The sample period from 1980 to 2014 is the subject of the empirical measurement. The adopted variables, which include

Gross Domestic Product, Capital Flight, and Exchange Rate, were subjected to a comprehensive analysis using the Ordinary Least Square (OLS), Augmented Dickey-Fuller unit root test, and Co-integration test. The findings demonstrated that the variables have a significant positive influence. Bredino, Fiderikumo and Adesuji (2018) analyzed the effect of capital trip on financial development in Nigeria. Predicting the impact of capital flight on economic expansion has not been very successful using traditional methods. The combined global technique, Artificial Neural Network (ANN) as a predictive technique, and traditional methods like Ordinary Least Square (OLS) and co-integration/error correction methods were used to analyze the model, which was estimated to cover the years 1980 to 2012.According to the findings of the study, capital flight has a negative effect on GDP, while exchange rate has a positive effect on GDP, which is in line with expectations.Malaysia's macroeconomic factors of capital flight were empirically examined by Liew, Mansor, and Puah (2016).FDI, the stock market, external debt, political risk, and these other factors. The ARDL method, the KPSS stationary test, the bounds test for co-integration, and the ADF and PP unit root tests were all used in the study. Aside from that, the World Bank's measurement from 1985 was used to identify the factors that contributed to capital flight in Malaysia. According to the empirical findings, capital flight was inversely correlated with FDI, the stock market, and external debt, whereas capital flight was positively correlated with political risk. Between 1999 and 2015, Nwakoby, Ajike, and Ezejiofor (2017) looked at how Nigerian government financial incentives affected small and medium-sized businesses (SMEs) and economic growth. Using straightforward regression analysis, they found that SMEs' output had a significant impact on Nigeria's economic growth. The two variables used were loans to small and medium-sized businesses and the gross domestic product. Government spending, loans, and other forms of credit have a significant impact on the output of small and medium-sized enterprises (SMEs) in Nigeria as well as the expansion of the economy. Based on panel data from 58 nations from 2001 to 2013, Pyun and An (2016) calibrated the effect of financial integration on the economic growth nexus and capital flight. It demonstrated that the impact of capital flight responses, business cycle co-movements, local fundamental factors, and investment channels as factors that influenced capital flight was influenced by the global financial crisis and the high-level cointegration of global economies with the United States as the arrowhead. The study by Obidike, Uma, Odionye, and Ogwuru (2015) looked at how capital flight affected Nigeria's economic growth. It was decided to use the Autoregressive Distributed Lagged model (ARDL).Capital flight has a negative and significant impact on economic growth, as the Auto Regressive Distributed Lagged (ARDL) model revealed. The model's parameters were found to be stable over time in the CUSUM and CUSUMSQ tests. Between 1980 and 2012, Olawale and Ifedayo (2015) investigate the effects of capital flight on Nigeria's economic expansion. Co-integration, Ordinary Least Square (OLS), and Error Correction Mechanism (ECM) were the primary estimation methods utilized in the study. During the study year, findings showed that capital flight, foreign reserve, external debt, foreign direct investment, and current account balance all cointegrate with GDP in Nigeria. Additionally, it was discovered that the economy was adversely affected by capital flight. By focusing on the private sector's unrecorded accumulation of foreign assets, Yalta and Yalta (2012) used a panel causality approach to examine the impact of financial development and liberalization on capital flight. It used data from 21 emerging economies from 1980 to 2004 as its foundation. The study found that delayed capital flight values have a self-reinforcing characteristic. Financial liberalization policies were noted to have little or no effect on reducing capital flight. In a similar vein, the research that was carried out in China by Lan, Wu, and Zhang (2010) utilized the ARDL bounds testing method and annual data spanning the years 1992 to 2007.They discovered that capital flow would be affected by changes in the domestic economy and political environment. These included economic policy shifts and political instability like social unrest. For the empirical period from 1970 to 2006, Choong, Lau, Liew, and Puah (2010) investigated the relationship between debt and economic expansion in Malaysia. In addition, they used multilateral debt, long-term debt, short-term debt, total debt service, and other types of debt in addition to external debt. The empirical findings demonstrated that countries with stronger financial systems were better able to absorb private capital inflows than outflows and that an increase in the level of external debt had an effect on economic performance.

Methodology

The study employed a descriptive and time series research design, which is a very important in determining the relationship between time-series variables. The population of the study consist of all data on capital flight and economic growth from inception to the 2019 period in the Central Bank of Nigeria Statistical Bulletin. For the purpose of the research, a sample size from 1981 to 2019 is selected from the CBN Statistical Bulletin in order to determine the relationship between the variables. Data are quarterly data from 1981 to 2019 from Central Bank of Nigeria Statistical Bulletin.
The Descriptive Statistics and regression analysis were used to analyze the relationship between the variables via E-view 9.0. This is because it includes macroeconomic variables that determine the economic growth in Nigeria.

Model Specification

In order to achieve the broad objective of this study, the model of John (2016) was adapted.

The model was specified as:

NEG = CF …….. i

Where

NEG = Nigeria Economy Growth

CF = Capital Flight

NEG is measured by GDP and CF is measured by CAB.

The modified model where stated below;

GDP = f (CAB) …….. ii

$GDP = \mu_0 + \mu_1 CAB + \varepsilon t$

Where

GDP = Gross Domestic Product

CAB = Current account balance

μ_0 = Constant

μ_1 = Shift Parameters

ε = error term

Analysis of Result

Table 1: Descriptive statistics

	GDP	CAB
Mean	34690.67	6902.897
Maximum	71387.83	44731.2
Minimum	13779.26	-19488.7
Std. Dev.	20237.78	15066.28
Skewness	0.673787	0.895383
Kurtosis	1.880848	3.381349
Jarque-Bera	4.986242	5.447444
Probability	0.082652	0.06563
Observations	39	39

The mean for GDP was 34690.67 with standard deviation of 20237.78 and maximum and minimum values of 71387.83 and 13779.26. The standard deviation is large which suggest huge year on year fluctuations in GDP and the variable appears to be positively skewed (0.673). The p-value for the Jacque-bera statistics stood at 0.083 which indicates that the series is normally distributed and the presence outliers is unlikely. The mean for CAB stood at 6902.897bn with a standard deviation of 15066.3. The maximum and minimum values stood at 44731.20 and -19488.70 respectively and positively skewed (0.89). The p-value for the Jacque-bera statistics stood at 0.065 which indicates that the series is normally distributed and the presence outliers is unlikely. The p-value for the Jacque-bera statistics stood at 0.065 which indicates that the series is normally distributed and the presence outliers is unlikely.

Test of Hypothesis

H_{01}: There is no significant relationship between current account balance and growth of the Nigerian economy.

Table 2: Regression analysis between GDP and CAB using Fully Modified Least Squares (FMOLS)

Dependent Variable: GDP
Method: Fully Modified Least Squares (FMOLS)
Date: 07/07/21 Time: 14:01
Sample (adjusted): 1982 2019
Included observations: 38 after adjustments
Cointegrating equation deterministics: C @TREND
Long-run covariance estimate (Bartlett kernel, Newey-West fixed bandwidth = 4.0000)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
CAB	-0.276696	0.103281	-2.679065	0.0116
C	5756.477	3194.685	1.801892	0.0810

R-squared	0.922600	Mean dependent var	35202.05
Adjusted R-squared	0.910507	S.D. dependent var	20252.46
S.E. of regression	6058.607	Sum squared resid	1.17E+09
Long-run variance	62329825		

In Table 2, R-squared and adjusted Squared values were (0.922) and (0.911) respectively. The indicates that all the independent variables jointly explain about 91% of the systematic variations in gross domestic product over the thirty nine years periods (1981-2019). Table 2 reveals an adjusted R^2 value of 0.91. The adjusted R^2, which represents the coefficient of multiple determinations imply that 91% of the total variation in the dependent variable (GDP) in Nigeria is jointly explained by the explanatory variable (CAB). The value of adjusted R^2 of 91% also shows that 9% of the variation in the dependent variable is explained by other factors not captured in the study model. This suggests that apart from CAB, there are other factors that mitigate GDP in Nigeria.

The results in table 2 illustrated that current account balance (CAB) has a negative but significant relationship with gross domestic product measured with a beta coefficient (β_1) and t- value of -0.276696 and -2.679065 respectively and p- value of 0.012 which is statistically significant at 5%:
Based on the empirical evidence that suggests that current account balance has a significant negative effect on gross domestic product in Nigeria at 5% level of significance, thus, the alternative hypothesis of the study is accepted.

Conclusion and Recommendation

The study used current account balance to predict capital flight and looked at how current account balance affected Nigeria's economic growth.CAB has a negative and significant impact on GDP. This suggests that expansions in current record equilibrium will adversely affect development. In terms of driving growth, our exports' mono-product structure and import dominance present significant obstacles. The study concludes that Nigeria's economic growth can only be boosted by addressing capital flight. The study's findings suggested that, despite the fact that the country's imports were in deficit, the current account balance was in deficit. The situation must be addressed by the government in order for the surplus position to improve, with exporting goods and services outpacing imports.

References

Adedayo O. C. & Ayodele S.O. (2016). An empirical analysis of the impact of capital flight on Nigeria economy. *International Journal of Academic Research in Economics and Management Sciences*. 5(2); 1-4. http://dx.doi.org/10.6007/IJAREMS/v5-i2/2168

Adegbite, E.O. & Ayadi, F.S. (2011) The Role of Foreign Direct Investment in Economic Development: A Study of Nigeria. *World Journal of Entrepreneurship, Management and Sustainable Development*, 6, 133-147. https://doi.org/10.1108/20425961201000011

Adetiloye, K.A. (2012, February). Capital flight versus domestic investment in developing countries: An empirical analysis from Nigeria. *International Journal of Economics and Finance, 4*(2). https://doi.org/10.5539/ijef.v4n2p175

Ajayi, S.I. (2003). An Analysis of External Debt and Capital Flight in the Severely indebted Low Income Countries in Sub-Saharan Africa, *Research Department, International Monetary Fund Working Paper* 68 (Washington DC).

Bredino S., Fiderikumo P., Adesuji A. (2018). Impact of Capital Flight on Economic Growth in Nigeria: An Econometric Approach. *Journal of Business and Economic Development.* 3(1); 22-29. doi: 10.11648/j.jbed.20180301.14

Choong, C. K., Lau, E., Liew, V.K.S., & Puah, C.H. (2010). Does debts foster economic growth? The experience of Malaysia. *African Journal of Business Management*, 4(8), 1564-1575.

Deppler, M., & Williamson, M. (1987). Capital flight: Concepts, measurement and issues. *Staff Papers for the World Economic Outlook*. International Monetary Fund, Washington, DC.

Eze M. (2013) Percieved Relationship Between Exchange Rate, Interest Rate And Economic Growth In Nigeria: 1970-2010''. *International Journal of Academic Research in Business and Social Sciences.* August 2014, Vol. 4, No. 8

Lan, Y., Wu, Y., & Zhang, C. (2010). Capital flight from China: Further evidence. *Journal of International Finance and Economics*, 10(2), 13-31.

Lawal, A. I, Kazi, P. K., Adeoti, O. J., Osuma, G. O., Akinmulegun, S., & Ilo, B. (2017). Capital Flight and the Economic Growth: Evidence from Nigeria. *Binus Business Review*, 8(2), 125-132. http://dx.doi.org/10.21512/bbr.v8i2.2090

Lawanson, A. O. (2008). An econometric analysis of capital flight from Nigeria: A portfolio approach. *Africa Economic Research Consortium paper No. 166.*

Liew, S.L., Mansor, S.A., & Puah, C.H. (2016). Macroeconomic determinants of capital flight: An empirical study in Malaysia. *International Business Management*, 10(13), 2526-2534.

Mordi C.N.O., Englama A. & Adebusuyi B.S. (2010). The Changing Structure Of The Nigerian Economy. *Economics and Financial Review*, 48(3), 43

Ndikumana, L. (2000). Financial development, financial structure, and domestic investment: International evidence. *Working Paper Series*, No. 16, Political Economy Research Institute, University of Massachusetts Amherst.

Nwakoby, N.P., Ajike, A.K. & Ezejiofor, R.A. (2017). SMEs financing and economic development: Nigerian Government incentives (1999-2015). *Journal Scholars Journal of Economics, Business and Management. 4(8).* 548-554

Obansa S.A.J, Okoroafor D.O.K., Aluko O.O. & Eze M. (2010). Percieved Relationship between Exchange Rate, Interest Rate and Economic Growth in Nigeria: 1970-2010. *American Journal of Humanities and Social Sciences* 1(3)

Obidike P.C., Uma K.E., Odionye J.C. & Ogwuru H.O.R. (2015). *British Journal of Economics, Management & Trade*. 10(3): 1-13. DOI: 10.9734/BJEMT/2015/20122

Olawale O. & Ifedayo O.M. (2015). Impacts Of Capital Flight On Economic Growth In Nigeria. *International Educative Research Foundation and Publisher*. 3(8); 10-46

Orji A., Ogbuabor J.E., Kama K. & Anthony-Orji O. (2020). Capital Flight and Economic

Growth in Nigeria: A New Evidence from ARDL Approach. *Asian Development Policy Review*. 8(3); 171-184

Pyun, J. H., & An, J. (2016). Capital and credit market integration and real economic contagion during the global financial crisis. *Journal of International Money and Finance*, 67, 172193.

Sanni, G. K., Musa, A. U. & Sani, Z. (2019). Current Account Balance and Economic Growth in Nigeria: An Empirical Investigation. *Central Bank of Nigeria: Economic and Financial Review.* 57/2; 83-106

World Bank. (2015). *World development indicators 2015*. Washington, D.C.: World Bank.