OBAFEMI AWOLOWO UNIVERSITY

Capital Flight, Unemployment And Economic Growth In Nigeria (1980-2013)

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B. Sc. (Economics), Iwo

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CERTIFICATION

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DEDICATION

This thesis is dedicated to God Almighty for His Exceeding Grace, Favour and Strength throughout the course of this study.

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ABSTRACT

The study analyses the trend of capital outflow, unemployment and economic growth in Nigeria; and investigated the impact of capital flight on unemployment in Nigeria. It also analyses the relationship between capital flight and economic growth in Nigeria. These were with the view to determining the relationship among capital flight, unemployment and economic growth in Nigeria for the period 1980 to 2013.

Secondary data were used for the study. Annual data on gross domestic product, capital flight, unemployment, exchange rate and interest rate covering the period from 1980 to 2013 were sourced from the World Development Indicators (WDI) of World Bank. Data collected were analysed using descriptive statistics such as charts, tables and graphs; and econometrics techniques of vector auto-regression (VAR) and autoregressive distributed lag (ARDL) model.

The result shows that capital flight represented by outflows which shows a higher figure of ₦8 billion, ₦9 billion, ₦10 billion and ₦13 billion in 1998, 1990, 1993 and 2000 respectively, while there was drops in capital outflow in 2003, 2004, 2005, 2006 and 2007 which stood at ₦4.7 billion, ₦1.6 billion, ₦2 billion, ₦2.6 billion and ₦3.3 billion respectively. Similarly, from the trend of unemployment rate, it was revealed that unemployment rate increases as the population increases. The appraisal of economic growth shows that economic growth proxy by gross domestic product in Nigeria has witnessed an upward growth since 1980. In 1986, output growth recorded the least value of 1.8% due to SAP, output grew to 49% and 54% in 1987 and 1989 respectively immediately after SAP. The estimates reveals that capital flight had a significant and positive effect on unemployment ($t = 2.6$, $p < 0.05$). Similarly, exchange rate had a positive and significant effect on unemployment ($t = 3.35$, $p < 0.05$). On the other hand, the

study found that capital flight had a negative and significant effect on economic growth ($t = -6.7$, $p < 0.05$). Furthermore, unemployment had a negative effect on economic growth in Nigeria ($t = -4.9$, $p < 0.05$). Also, exchange had a negative and significant effect on economic growth in Nigeria ($t = -3.3$, $p < 0.05$).

The study concluded that capital flight and unemployment reduces economic growth in Nigeria.

CHAPTER ONE

INTRODUCTION

1.1 Background to the Study

Capital flight according to Schneider (2003) is the outflows of resident capital or resources which are motivated by economic and political uncertainties in the home country. Similarly, World Bank (1985) opines that capital flight is the change in a nation's foreign assets. Economic theory suggests that capital flight phenomenon is driven both by private actors and public authorities (Ndikumana and Boyce, 2003, 2008 and 2011b; Ajayi, 2007; Ndiaye, 2009a and 2014). The process of unrecorded accumulation of foreign assets by the private sector is referred to as "capital flight" which, especially after the debt crisis of the 1980s, has come to be viewed as one of the major economic problems in many developing countries. Macroeconomic uncertainty, political and institutional instability, less developed financial system, and higher rate of return differentials abroad are some of the factors that affect capital flight by private actors. These factors lead to increasing risks of losses in the real value of domestic assets of private agents, forcing them to shift their portfolio in favour of foreign assets. Similarly, public authorities can also contribute to capital flight under conditions of poor governance and bad institutional quality. In such a situation, corrupt public authorities take advantage of their favourable position to amass a personal wealth abroad (Boyce and Ndikumana, 2001). As these resources held overseas are domestic public resources, capital flight operated by public authorities' leads to a reduction in public resources, thereby causing a reduction in public investment, and increasing unemployment rate in these countries.

In recent times, capital flight from Latin America and African countries has been put at the forefront of the development policy debate. Furthermore, considerable attention has been drawn to the extent to which capital flight has a detrimental impact on economic development of African countries especially Nigeria which has the highest capital outflow in Africa (United Nation Development programme UNDP, 2011). The poor performance of the economy and the persistent negative trade balance recorded in most developing countries have been attributed to capital flight which has a direct link to unemployment in these countries (Ajayi, 1995). Indeed, the increasing levels of capital flight pose serious challenges for domestic resource mobilization in support of investment and growth in Africa (Fofack & Ndikumana, 2010). Inadequate financial resources for appropriate economic development has pushed most African countries including Nigeria into external borrowing to augment domestic resources in their quest for reduction in unemployment and increase in economic growth. Acquisition of foreign assets by residents has escalated even as developing countries search for external borrowing to boost capital inflow into the country.

International capital movements have grown in Nigeria since financial deregulation of the 1980s by African countries and the adoption of the Structural Adjustment Programme (SAP). Obiechina (2010) observed that the abrogation and subsequent entrenchment of certain laws of investment as well as the introduction of structural reforms facilitated the substantial flow of capital. Various macroeconomic policies by Nigerian government have been unable to achieve sustained price stability, reduction in unemployment and sustained growth. The fluctuations in the economy have confirmed the need to manage the economy effectively. The essence of macroeconomic management underlines the rationale of the government as a vital economic agent. However, it appears that government intervention has not been able to curb the increasing trend of capital flight that affects unemployment in the economy

1.2 Statement of Research Problem

In Nigeria, one of the unresolved and perturbing macroeconomic problems for the past three decades is the growing rate of capital flight and increasing unemployment, and the global financial crisis in 2005 and its generated problem of massive movement of funds out of the country. Statistics from the International Monetary Fund (IMF, 1996) showed that Nigeria suffered a deficit of $7,573 million between 1972 and 1989 to capital flight. Out of this total capital flight, the sum of US$7,362 million was lost between 1972 and 1978 against a capital inflow of $270 million within the same period. Corroborating this, International Financial Corporation in 1998 observed that Nigeria is among many African economies that have achieved significant lower investment levels as a result of capital flight. Such low level investment brought about by high rate of capital flight in Nigeria also has multiplier consequences on other aspect of the economy. These negative multiplier effects on Nigerian economy includes among others the alarming rate of unemployment as well as pronounced regressive effects on the distribution of wealth in Nigeria. In another related study carried out by United Nation Conference on Trade and Development (UNCTAD) in 2007, their report shows that around $13 billion per year have left the African continent in term of capital outflow between 1991 and 2004. This represents a large chunk of African continent total income, with Nigeria having the highest percentage of the total share. Furthermore, the total stock of illicit outflows from Nigeria between 2002 and 2011 was put at $142,274 million (Global Financial Integrity, 2013). In 2008, over $20 billion left the country as a result of capital flight. Capital flight has been regarded as one of the major factors contributing to the rising foreign debt and retarding development efforts of the economies of the third world countries. In addition to the continued increase in capital flight, Nigeria's unemployment rate increased to 23.9 percent in 2011 compared with 21.1