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Stock Prices, Capital Market Development and Nigeria's Economic Growth

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Abstract
The objective of the paper has been to empirically investigate the influence of stock prices and capital market development on the level of economic progress in Nigeria. This becomes necessary due to the increasing role played globally by both stock prices and capital market in generating the desired the level of economic growth. The study used time series data that covered the period from 1980 to 2012. This includes the pre-Structural Adjustment Programme (SAP) and SAP eras. The cointegration test with its implied ECM was applied. The ADF unit root test indicates that all the variables are stationary at I(1). The Johansen cointegration test indicates a long run relationship among the variables. The short run dynamic result indicates that the level of market capitalization, new issues in the capital market, value of equities and government stock rate have positive signs and are statistically significant in explaining economic growth. Results revealed that government's policies on both stock prices and capital market have been beneficial in explaining the level of economic growth in Nigeria. The ECM shows a satisfactory speed of adjustment to equilibrium in the long-run. It is thus recommended that government should continue with her stock prices policies by further liberalizing the stock market and that the level of market capitalization should be further increased.
Keywords: Stock prices, Capital market development, Economic growth, Cointegration

Introduction

It is a generally held view by development economists and financial policy makers that a faster rate of economic growth and development can occur if there is a well- developed capital market. It is the expectation that such a market is capable of opening up avenues for financial resource mobilization by complementing bank financing, which in turn mitigates the risk of credit crunch and thus motivates entrepreneurs in order to accelerate their rate of investment and the pace of industrialization in a country. To do that, the economy needs an adequate flow of funds. The economy of every nation performs excellently well based on adequate mobilization of available financial and other resources and the ability of the financial resources to change hands from the surplus unit to the deficit unit. Many economists, decision makers and financial analyst have been familiar with the importance of this relationship as the basis for modeling an economy towards economic growth and ultimately culminating into a viable economy, characterized by sustainability over time. The capital market is thus recognized as the basis or the engine of economic growth (Levine & Zervos, 1998; Okereke-Onyiuke, 2000)). Countries with developed stock markets provide alternative sources of financing to companies thereby making them less dependent on bank financing, which in turn mitigate the risk of credit crunch. In this way, stock markets are able to positively influence economic growth by encouraging savings amongst individuals and providing avenues for firms financing (Levine and Zervos, 1998). As rightly pointed out, Okereke-Onyiuke (2000) observes that the cheap source of funds from the capital market remain a critical element in the sustainable development of the economy. Similarly, Eriemo (2013) also noted that fund mobilization which the capital market holds as one of its fundamental functions, creates funds facilities for continuous flow of exchange between the deficit and surplus units in the capital market. These roles are aptly played by the Nigerian Stock Exchange (NSE) formerly known as the Lagos Stock Exchange which was registered March1, 1959, incorporated September 15, 1960 but started business on June 5, 1961 with its functions stated inter alia: First is the enhancement of the liquid nature of shares and bonds by making them easily disposable and saleable; second, to provide and guarantee a free and continuous market for capital already invested, by facilitating the exchange of securities with minimum delay; third, to act as the country's barometers to the investing public through the trends it records in share /bonds prices and values, fourth, to provide the quoted securities with high ratings for the benefit of the business community through the stringent listing requirement; fifth, to provides adequate mobility of capital and directs the flow of funds to profitable and more successful industrial enterprises for development when there is market distortions and imperfections.

. In the past, availability of funds posed a serious problem to the capital market development and more to the small-scale industries which, for various reasons are completely unable to trade on the exchange. This is corroborated in a view by Akhamiokhor (1983) who noted that out of ninety-three companies listed on the exchange in 1983, only five of them are 100 percent indigenized and just one is wholly owned Nigerian promoted enterprise". Such a situation points a gloomy picture for the economy when it is known that small businesses are many in the country. This, no doubt calls for the development of policies that could take the capital market operations to greater heights. Capital accumulation in the form of inflows such as portfolio investment and foreign direct investment become very discerning.

Quite unquestionably, the Nigerian Stock Exchange has experienced increased performance in recent times yet its role as bulldozer to market capitalization and economic growth is superficial. The Nigerian Stock Exchange emerged when there was greater reliance on imported capital to implement Nigeria's development plan. At that time, much of the exchange activities were tied to the raising of funds for the Government development loans. Today its activities have gone numerous so that the scope in capital mobilization including new issues and securities and its activities have also attracted the connection with the emerging African Capital Markets using the European system. It is with a view to highlighting these laudable aspirations that informed the ideas of this paper; the approach here is to analyze how stock prices and capital market developments influence economic growth in Nigeria. Thus aside from this introductory episode, this paper is further divided into four distinct sections in sequence comprising theoretical underpinning and empirical literature, followed by methods and procedures, results and discussion; the paper ended with conclusion

Theoretical Underpinning and Empirical Literature

Interest in studies on stock market behaviours abounds but considering the crucial roles capital markets and their developments play in facilitating capital accumulation among nations of the world, researches relating to the thesis can never be emphasized. Available literature reveals that some examine the relationship between stock market development and economic growth, some examine stock prices and economic growth, and some others examine stock prices and market capitalization. Despite the varied approaches to the capital market analysis, views are similar, tending to pursue similar goals of enhancing the healthiness of the nation's investment drive. This stems from the generally held view that financial resource mobilization by capital markets as complement to fund-raising through commercial banks cannot be avoided if the economy is to meet its growth mission (Alile, 1999, Okereke-Onyuike, 2000, Osinubi and Amaghionyeodiwe,2003, Abu,2009, Adaramola,2011,Okey2012, Eriemo,2013,2014). Thus, a well developed stock market is crucial for the mobilization of financial resources for long term investment and thus constitutes one of the major pillars of economic growth. The stock market development is expected to accelerate economic growth by providing an avenue for growing companies to raise capital at lower cost..Although, the justification of these expectations has, in the past been provided by the works of well-meaning writers, the approach of this study differs slightly by the inclusion of government stock as a variable in the modeling.

Works of others in this theorizing include: Osinubi and Amaghionyeodiwe (2003) who examined the relationship between Nigeria stock market and economic growth during the period 1980-2000 using ordinary least squares regression (OLS) and reported a positive relationship between the stock market and economic growth and suggest the pursuit of policies geared towards rapid development of the stock market.. Ezeoha et al (2009) investigated the nature of the relationship that exists between stock market development and the level of investment (domestic private investment and foreign private investment) flows in Nigeria and concludes that stock market development promotes domestic private investment flows thus suggesting the enhancement of the economy's production capacity as well as promotion of the growth of national output. However, the results show that stock market development has not been able to encourage the flow of foreign private investment in Nigeria. This raises some doubts which this study is determined to provide answer to.

Further on this controversy, Abu (2009), examined whether stock market development raises economic growth in Nigeria, by employing the error correction approach and the econometric results of the study indicate that stock market development (market capitalization-GDP ratio) increases economic growth. He however, recommended the removal of impediment to stock market development which include tax, legal and regulatory barriers, development of the nation's infrastructure to create enabling environment where business can strive, employment policies that will increase the productivity and efficiency of firms as well as encouraging of the Nigerian Securities and Exchange Commission to facilitate the growth of the market, restore the confidence of stock market participants and safeguard the interest of shareholders by checking sharp practices of market operators.

Ewah et al (2009) appraised the impact of capital market efficiency on economic growth in Nigeria, using time series data on market capitalization, money supply, interest rate, total market transaction, and government development stock between 1961-2004 using multiple regression and ordinary least squares estimation techniques. The result of the study shows that the capital market in Nigeria has the potential to induce growth, but it has not contributed meaningfully to the economic growth of Nigeria because of low market capitalization, low absorptive capacity, illiquidity, misappropriation of funds

among others. (Chandra, 2004) opined that the growth rate of the Gross Domestic Product (GDP) and the growth rate of the economy have positive relationship. The higher the growth rate of GDP, other things being equal, the more favourable it is for the stock market. Equity prices may rise due to the potential for higher profits from a healthy business climate. Adaramola(2011) using stock prices, inflation rate, interest rate,

money supply, Gross Domestic Product, exchange rate, market capitalization and, volume of total transaction of the Nigerian stock exchange reported that macroeconomic variables except inflation rate and money supply,

have varying significant impact on stock prices of individual firms in Nigeria. In particular, Eriemo (2014) on empirical analysis of market capitalization determinants, observes that parsimonions ECM result indicates that the return on investment and value traded have the greatest influence on the level of market capitalization in Nigeria. The value of equity also exhibited positively and significant relationship with the level of market capitalization. The error correction showed a satisfactory speed of adjustment and so policies to improve the returns on investment, liquidity status and increase in the value of equity are thus recommended. In addition, the paper expressed the view that with concerted efforts aimed at developing the capital market and the pursuit of policies of deregulation already begun in the economy, the Nigerian stock price index would be a good instrument for measuring the pulses in the economy as is the case with the industrialized countries of the world judging from the robustness of the findings. .

Methods and Procedure

The cointegration technique with its implied Error Correction (ECM) technique was used for the analysis of the data and the interpretation of the empirical results. Because misleading results evolve from non-stationary data which are observed to produce spurious regression results, the unit root test was performed to confirm the stationarity of data using the Augmented Dickey-Fuller (ADF) unit root test. The cointegration technique with its implied Error Correction (ECM) technique was used for the analysis because it restricts the long run behaviour of the endogenous variables to converge to their cointegrating relationships while allowing for a short run adjustment (Gujaratti, 2003**).** The error correction mechanism shows the speed of adjustment of the dependent variable to changes in the independent variables. The decision rule is that the ADF test statistic value must be greater than the Mackinnon critical value at 5% and at absolute value. It is of the form:

$$\Delta y_t = \alpha\beta' y_{t-1} + \sum_{i=1}^{j=1} \Gamma_j \Delta y_{t-1} + \pi + \varsigma_t, t = 1, \dots, T$$

Where y_t = is a vector of endogenous variables which include Gross Domestic Product, value of equities, government stock rate, new issues in the stock market and market capitalization..

αs= parameters measures the speed of adjustment through which the variables adjust to their long run values and

β'= vectors which are estimates of the long run cointegrating relationships among variables in the model.

π= is the drift parameter and is the matrix of the parameters associated with the exogenous variables. The stochastic error term is also included in the specification.

Thus going from the above the model to be estimated in this study is thus defined below:

GDP bo + b1VEQ + b2GSR + b3NI + b4MCAP + Ut
b1, b2,b3, b4 > 0

where:

GDP	=	Gross Domestic Product
VEQ	=	Value of equities
NI	=	New issues in the stock market
MCAP	=	Market capitalization
GSR	=	Government Stock Rate

The data were collected from various issues of the Central Bank of Nigeria (CBN) statistical bulletin and various issues of the World Bank Indicators for Nigeria. The data covered the period from 1980 to 2012. This period included the contemporaneous behaviour of stock prices, capital formation and economic growth in both the pre Structural Adjustment Programme (SAP) adopted in Nigeria in the process of economic deregulation and post Structural Adjustment Programme

Results and Discussion

The Summary of descriptive statistics for the variables is shown in table 1 below:

Table 1: Summary of Results of Descriptive Statistics

	LGDP	LMCAP	LNI	LSMR	LVEQ
Mean	14.06494	5.241519	9.410119	2.349278	8.638811
Median	14.43420	5.570632	9.206784	2.420368	6.893555
Maximum	17.55145	9.495113	13.23433	3.292126	14.54597
Minimum	10.77100	1.609438	5.073923	1.609438	2.644329
Std. Dev.	2.251806	2.723726	2.741794	0.433930	3.378744
Skewness	1.009642	0.091372	1.063900	0.109141	1.379391
Kurtosis	2.651413	4.610205	1.461088	2.858915	2.777732
Jarque-Bera	2.501206	2.701771	3.278803	1.038223	2.845824
Probability	0.286332	0.259011	0.194096	0.595049	0.241011
Sum	464.1431	172.9701	310.5339	77.52619	285.0808
Sum Sq. Dev.	162.2602	237.3979	240.5580	6.025435	365.3091
Observations	33	33	33	33	33

The Skewness which is a measure of asymmetry of the distribution of the series around its mean have values greater than O except in two cases indicating skewness to the right. This implies that the distribution has a long right tail. The kurtosis which measures the peakedness or flatness of the distribution with an expected value of 3.0 shows that the value of equities, stock market rate and Gross Domestic Product satisfy the conditions. However, that of new issues is platykurtic (less than 3), while that of market capitalization is leptokurtic (greater than 3). The Jarque-bera test is used to test whether the random variables with unknownn means and dispersion are normally distributed. The Jarque-bera test has the null hypothesis of normally distributed residuals. The probability value indicates an acceptance of the null hypothesis that the errors are normally distributed. The next step is test for the stationarity of the variables.

The summary of the Augmented Dickey Fuller (ADF)unit root test is shown below:

Table2: Summary of AF unit root test result

Variables	**Level Data**	**First difference**	**Order of Integration**
VEQ	2.07	-6.13*	I(1)
SMR	-2.10	-5.25*	I(1)
NI	-0.15	-7.38*	I(1)
MCAP	-0.79	-4.89*	I(1)
GDP	2.60	-4.28*	I(1)

***** indicates significance at the 1 percent level

The ADF unit root test shows that all the variables were stationary after the first difference were taken. All the variables were stationary at the 1 percent level. This is an indication that all the variables are integrated of order 1, that is, they are I(1).

The result of the Johansen cointegration test is shown below. The Johansen cointegration test is preferable since amongst others, it allows for more than one cointegrating equations.

Table3: Summary of Johansen cointegration test result

Unrestricted Cointegration Rank Test

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	5 Percent Critical Value	1 Percent Critical Value
None **	0.739091	83.21257	68.52	76.07
At most 1	0.471356	42.90503	47.21	54.46
At most 2	0.396029	23.78181	29.68	35.65
At most 3	0.195364	8.654932	15.41	20.04
At most 4	0.068661	2.133967	3.76	6.65
Hypothesized No. of CE(s)	Eigenvalue	Max-Eigen Statistic	5 Percent Critical Value	1 Percent Critical Value
None **	0.739091	40.30755	33.46	38.77
At most 1	0.471356	19.12322	27.07	32.24
At most 2	0.396029	15.12688	20.97	25.52
At most 3	0.195364	6.520966	14.07	18.63
At most 4	0.068661	2.133967	3.76	6.65

The result of the Johansen cointegration test indicates a long run relationship among the variables. This is because both the trace statistic and the max-eigen statistic indicate one cointegrating equation each. These results permit us to estimate the parsimonious and overparameterize ECM model.

The result of the overparameterize ECM result is shown in table 4 below:

Table4: Summary of Overparameterize ECM Result: Modeling DLGDP

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DLMCAP	0.290419	0.501878	0.578664	0.5709
DLMCAP(-1)	0.908106	0.089434	10.15393	0.0000
DLMCAP(-2)	-0.499559	0.528763	-0.944769	0.3588
DLNI	0.333335	0.144167	2.312144	0.0344
DLNI(-1)	-0.102290	0.148753	-0.687651	0.5015
DLNI(-2)	-0.225750	0.167186	-1.350295	0.1957
DLVEQ	-0.117980	0.112578	-1.047984	0.3102
DLVEQ(-1)	-0.062900	0.102816	-0.611769	0.5493
DLVEQ(-2)	0.278391	0.107894	2.580236	0.0139
DLSMR	-0.209120	0.583491	-0.358394	0.7247
DLSMR(-1)	0.250679	0.063116	3.971709	0.0005
DLSMR(-2)	-0.477120	0.540031	-0.883504	0.3900
ECM(-1)	-0.691862	0.237988	-2.907125	0.0103
C	0.301830	0.241392	1.250375	0.2291

R^2= 0.68, Fstatistic = 18.62, DW= 2.12, AIC = 2.33, SC= 2.99

The overparameterize ECM result is made of two lags each of the independent variables. The Akaike Information Criterion (AIC), Schqarz Criterion (SC) were used to select the appropriate lag length. The summary of the parsimonious or preferred ECm result is shown in the table below

Table5: Summary of parsimonious ECM result modeling: DLGDP

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DLMCAP(-1)	0.483866	0.105695	4.577960	0.0001
DLNI	0.187952	0.048026	3.913570	0.0007
DLVEQ(-2)	0.576772	0.212428	2.715139	0.0112
DLSMR(-1)	0.416753	0.138104	3.017669	0.0047
ECM(-1)	-0.453696	0.077109	-5.883822	0.0000
C	0.079436	0.159754	0.497240	0.6235

R^2= 0.67, Fstatistic = 21.20, DW= 2.13, AIC = 2.10, SC= 2.38

The result indicates that the value of equities which is a measure of stock prices is statistical significant and have a positive linear relationship with the level of economic growth in Nigeria. This is an indication that stock prices in Nigeria have been beneficial to the level of economic progress in Nigeria. This is further supported by the relatively high elasticity. The result indicates further that the government stock rate which is another measure of stock process has a significant and positive relationship with the level of economic growth in Nigeria. This is symptomatic that the previous level of government stock rate has been beneficial to the level of economic

progress in Nigeria. This gives some level of credibility to the monetary authorities' policies on stock market prices. The immediate past level of market capitalization has a Significant and positive relationship with the level of economic growth in Nigeria. Since the level of market capitalization is an indicator of capital market development, the result suggests that the market in Nigeria has made important contributions to the level of economic progress in Nigeria. The result shows that an increase in the level of, market capitalization by 1 percent increased the level of economic growth by 48 percent. The statistical significance of the new issues which is another capital market development indicator which is also positively signed is an indication that the capital market development has been beneficial to the level of economic progress in Nigeria. The statistical significance of the ECM term which is also negatively signed is an indication of a satisfactory speed of adjustment. It suggests that about 45 percent of the errors are corrected each period.
The result of the stability test shown by the Cumulative Sum of Recursive Residuals (CUSUM) is shown below:

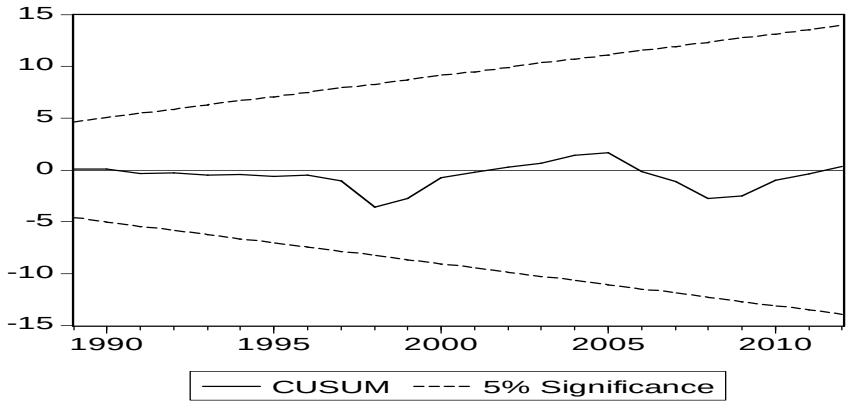

Figure1: CUSUM stability test
The result indicates that the residuals are stable. This is because the CUSUM line falls in-between the two dotted 5 percent lines.

Conclusion
The paper focused on stock prices, capital market development and Nigeria's economic growth**.** It is obvious from the study that the increasing attention paid to the stock prices and capital market development in both the developed and emerging economies of the world is an indication of the important role played by stock prices and capital market development in generating the desired level of economic growth. The last global financial crisis and the last European economic crisis were partly the consequence of flawed stock price policies and inefficiencies in the capital market. In Africa and Nigeria specifically, the reduced attention in stock price movements and the development of the capital market has hindered the level of economic progress. This is mostly due to corruption and bureaucratic interference in the operation of the capital market. The study commenced with the descriptive statistics which included the skewness, kurtosis and jarque-bera tests. The ADF unit root test indicated that the variables where I(1). The Johansen cointegration test indicated a long run equilibrium relationship among the variables. The result of the short run dynamic adjustment indicates that stock prices, government stock rate and new issues including market capitalization in the capital market have significantly and positively influenced the level of economic growth in Nigeria. The ECM indicates a satisfactory speed of adjustment hence the government should continue with her policies on capital market development and apply market principles to stock prices. .

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