

Capital Flight and the Nigerian Economy: An Empirical Reassessment

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ABSTRACT
The study empirically reassessed the impact of capital flight on the economic growth of Nigeria. The capital escaping from an economy is termed capital flight. This happens when capital escapes into safety or secrecy thereby depriving the source economy from its use. Reasons for this are poor economic situation, political crises, corruption, etc. Secondary data were collated from the publications of the Central Bank of Nigeria, Bureau- De-Change, and Global Finance Integrity to examine the relationship that exists between the Gross Domestic Product (GDP) of Nigeria and the Capital Flight from the country. The data covered a period of 20 years (i.e.1991-2010). The simple linear regression model was used to analyze the data. This was coupled with the F-ratio used to test the formulated hypothesis. It was discovered from the analysis that there exists a very high positive correlation between GDP in Nigeria and capital flight from the country. It was also found out that capital flight has a significant impact on the GDP of Nigeria. It was therefore recommended among others that the Nigerian economic and political environment should be made investment friendly by securing lives and property of present investors and would be investors. Government should also curtail the wind of corruption blowing across all the levels of government which has been aiding illegal transfer of capital from the economy. The economy would surely conquer the war against capital flight if the suggestions are implemented.
Keywords: Capital flow, Globalization, Gross Domestic Product

INTRODUCTION

Capital flight in Nigeria is adjudged to be more severe than it is elsewhere in other sub Sahara African countries. According to Ajadi (2008), this is due majorly to the political instability, unhealthy economic environment and the high magnitude of corruption at all levels of government in Nigeria.

The trend of capital flight in Nigeria was more noticeable between September and November 2009 when several billions of US Dollars were purchased through the banks and bureau-de-change. Within the period, a total of US $13.894 billion worth of (#2,153.57 billion) went out of the country. In 2010, by the records available at the Central Bank of Nigeria, between January 22 of year 2000 and March 5 of the same year, a total of US $6.734 billion (#1043.77 billion) went out of the country through banks and bureau-de-change.

The fundamental economic concern about capital flight is its tendency to reduce welfare in the sense that it leads to a net loss in the total real resources available to an economy for investment and growth. That is, capital flight is viewed as a diversion of domestic savings away from financing domestic real investment in favour of foreign financial investment. As a result, the pace of growth and development of the economy is retarded from what is otherwise would have been (Deppler et al, 1987).

Pastor (1990) and Ajayi (1992) have shown that developing countries' borrowings are substantially diverted into private assets abroad. Thus the paradoxical situation of accumulation of external debt by developing countries, and the corresponding acquisition of external asset by resident has been an additional force behind the problem of capital flight.

Also, capital flight encourages increasing demand for foreign currency which tends to exert pressure on exchange rate thereby increasing the rate. This can be explicitly viewed as one US Dollars being exchange for #70 currently in the parallel market in Nigeria as a result of high demand for dollars. These currency fluctuations in addition to aforementioned phenomena are things of concern, hence the paper is out to re assess the impact of capital flights on the Nigerian economy in the last two decades (from 1991 to 2010) and suggest ways of reducing the menace in Nigeria.

CONCEPTUAL FRAMEWORK

The concept of capital flight

Capital flight takes place through transferring a part of domestic private savings abroad, the persistence of which can lead to a serious decline in domestic savings and when this occurs, banks domestic resources in form of savings fall, thereby curtailing the bank's ability to provide credit. In developing countries, capital flight drains foreign reserves, heightens inflations, reduces tax revenue, cancels investment and undermines free trade.

Besides removing resources that could otherwise be used for poverty alleviation and economic growth, it tends to restrict the capacity and ability of affected countries to mobilize domestic resources and access foreign capital necessary to finance economic growth and development of developing countries like Nigeria.

According to Nwachuckwu et al (2009), when capital leakage occurs in an economy, much resource and opportunity for growth is lost. The processes of such movement are eased by the spate of globalizations sweeping through countries. Globalization itself has been held to enable efficient allocation of capital within the world economy. Flows and flight of capital occur to move capital from one economy to another and therefore have serious economic and financial implications in the countries suffering and benefitting from them.

The outflow of capital becomes capital flight when the GDP increases at a lower rate than capital outflow. This was corroborated by Ajayi (2000) as he stressed further that; capital shift out of developed countries is regarded as capital outflows, because the investors from developed countries are responding to investment opportunities while those from developing countries are said to be escaping the huge risk perceived at home, hence, regarded as capital flight in Nigeria.

Major causes and routes of capital flight in Nigeria.

Ajayi (2000) mentioned some various causes of capital flight in any developing economies like Nigeria as comprising the following.

1. Risk perception of investors---This factor goes with the theory of portfolio selection. Portfolio selection depends so much on the choice of investors who choose where to hold their wealth, either at home or overseas. The choice of either of this is influenced by the risk and return trade off and other considerations within the economy. A rational investor will usually invest where he/she can get a higher return on his/her investment. This has really eluded Nigeria due to the other factors to be discussed.
2. Exchange rate misalignment---This has encouraged the development of parallel market premium in the foreign exchange market and it usually exposes the wealth holder to capital losses should devaluation or depreciation happens. Fiscal deficit and macroeconomic distortions in the economy encourage flights of capital because of their attendant effect on the instability of exchange rate they bring about.
3. Financial sector constraints and repression---The financial market repression regulates the return on capital and does not allow the financial institutions to develop products and services that meet clients and customers needs, thus encouraging them to seek investment of their funds outside the shores of the country.
4. Corruptions by political leaders and extra ordinary access to government funds---These have led to unwholesome transfer of funds overseas from Nigeria for the main purpose of escaping sanctions and seizures by government that cares. Baker (1999) however, established the strongest link between capital flight and political corruption when he divided capital flight into two---legal and illegal. The legal aspect of capital flight covers the movement of capital out of the economy, which involves the proper transfer of after –tax profits, which is documented as it passes through the border and remains in the book of the entity from which it is transferred. On the other hand, the illegal component is tax evading and therefore illegal for the country from which it originates and thereafter disappears. All stolen monies by Nigeria political holders fall into this latter category and has really reduced the domestic investible funds drastically (Baker, 1999).
5. Economic instability---Economic indices such as inflation rate, depreciation of naira, civil unrest such as kidnapping, Niger Delta crises and "Boko Haram" problem have really sent away many investors

from the country to a saver economy where fortunes await their capitals. Other would -be investors around the globe think twice before investing in Nigeria.

6. Political crisis----The political scene of Nigeria lately has been bedeviled by the "do or die" syndrome. This phenomenon has sent wrong and terrible signals to the outside world. This always leads to insecurity of lives and properties; hence many investors attempt to transfer their life saving funds outside the economy especially around this time when Nigeria is preparing for another nationwide election.
7. Financial globalization----Capital flight being a challenge to domestic investment is exacerbated by the process of financial globalization that enables capital to move freely among countries. Since capital seeks the best avenue where it can earn the highest return given a level of assured risk, the domestic investment environment has not been attractive enough for investment.

   Financial globalization, in some cases has rendered some national governments monetary policies ineffective. Since financial globalization connotes the liberalization of the capital account, it enables capital to move in and out of the domestic economy which reduces the level of restrictions (Ojo, 2008). In fact, some foreign private banks even aid some corrupt Nigeria politician to save their loots, thereby draining the available fund for capital accumulation locally.
8. Poor infrastructural facilities--- As noted by Ojo (2007), Nigeria economy is presently overwhelmed with infrastructural deficit that has impeded the development of the country and its transformation into an industrial economy. Due to this, the economy has constantly lost resources to capital flights over the years. For example, Dunlop Plc left the country to Ghana due to epileptic nature of power supply in Nigeria. Many other investments have been lost as a result of the problem just mentioned above. Thereby resulting to higher exorbitant of money being spent on importation of goods and earn less on our few exports.

METHODOLOGY:

The data for the study covers the period of twenty 20years i.e. (1991-2010). Secondary data were used and were sourced from the publications of the Central Bank of Nigeria (CBN), National Bureau of Statistics (NBS) and the Global Finance Integrity.

The data are shown in the table below.

Table1. Capital Flight (KF) and Gross Domestic Product (GDP) in Nigeria.

YEARS	ADJUSTED KF IN #'MILLION	GDP AT FACTORS COST #'MILLION
1991	28,680.09	263379.1
1992	41,239.74	271,365.5
1993	36,922.73	274,833.3
1994	40,739.48	275,450.6
1995	236.41	293,745.4
1996	116.02	281,407.4
1997	59.10	302,022.5
1998	369.94	310,890.1
1999	1,113,345.94	312,183.5
2000	646,948.54	329,178.7
2001	611,584.19	356,994.3
2002	621,229.34	433,203.5
2003	1,261,337.62	477,533.0
2004	2,002,271.80	527,576.0
2005	2,466,275.81	561,931.4
2006	2,986,918.51	595,821.6
2007	4,104,917.11	634,251.1
2008	5,877,876.02	672,202.6
2009	8,344,151,56	716,949.7
2010	7,963,113,15	746,050.0

Sources: CBN Statistical Bulletins, National Bureau of Statistics and Global Finance Integrity (2010)

MODEL SPECIFICATION

The paper used quantitative method of analysis. A simple linear regression model and Pearson correlations were used to find the type of relationship and the magnitude of relationship that exist between the dependent variable (GDP) and the independent one (capital flight) in order to determine the impact of the latter on the former.

The F-ration was also used to test the overall significance of the model and hence used to test the formulated hypothesis. SPSS package was used for the calculations.

Mathematically, the model is given as follows:

$$Y= f(x)$$

Where y= GDP, and

x= capital flight

And the regression line is defined as:

$$GDP= B0 + B1Kf + E$$

Where GDP= Gross Domestic Product

Bo= intercept of the line/constant parameter

B1= slope of the regression line/coefficient of the regression

Kf= capital flight

E= stochastic term

Empirical Results.

Correlations

		GDP	KF
Pearson correlation	GDP	1.000	0.928
	KF	0.928	1.000
Significant (1-tailed)	GDP		0.000
	KF	0.000	
N	GDP	20	20
	KF	20	20

Model summary

Model	R	R-square	adjusted r-square	std. Error of the estimate
1	0.928[a]	0.860	0.853	64772.812

a. Predictor: (constant), KF

ANOVA

Model	sum of squares	DF	mean square	F	significance
Regression	465310069754.986	1	465310069754.986	110.906	0.000[b]
Residual	75519308824.256	18	4195517156.903		
Total	540829378579.242	19			

b. Predictors: (constant), KF

Coefficients

Model			standardized coefficient	t	significance
	B	standard Error	Beta		
(Constant)	319721.801	17974.911		17.787	0.000
KF	0.059	0.006	0.928	10.531	0.000

Source -table 1

The regression equation is given thus:

GDP = B0 + B1KF + E

GDP = 319721.801+0.059KF + E

SE = (17974.911) (0.006)

T = (17.787) (10,531)

INTERPRETATION OF RESULTS

From the analysis so far, the Pearson's correlation is very high at 0.98, meaning that there is exists a very high positive correlation between the two variables under discussion (GDP and capital flight). The regression result shows that, capital flight has a significant impact on the GDP of Nigeria. The coefficient of 0.059 indicates that a change of 10% in capital flight will lead to a change 0.59% in the economic growth (GDP) of the country.

The coefficient of determination (R square) and the adjusted R-square are both high at 0.860 and 0.853respectively, meaning that about 86% of economic growth can be explained by changes in capital flight while the remaining 14% can be explained by factors outside the model.

Test of hypothesis

The hypothesis formulated for testing is;

H0: Capital flight has no significant impact on GDP in Nigeria

H1: Capital flight has a significant impact on GDP in Nigeria

Using the data from the analysis, the F- calculated is 110.906 which is greater than F-table value of 4.41 at 0.05 significance level with (1.18) degree of freedom. Therefore, since the F-statistic of 110,906 is greater than the F-critical value of 4.41, we reject the null hypothesis (H0) and accept the alternative hypothesis (H1). Thus, upholding the statement that capital flight has a significant impact on GDP in Nigeria.

CONCLUSIONS AND RECOMMENDATIONS

The study empirically re-assessed the impact of capital flight on the economic growth of Nigeria. It was discovered that so much capital has fled the economy of Nigeria due to some factors such as exchange rate misalignment, financial sectors constraints and repression, macroeconomic policy distortion, lack of infrastructural development, corruption by political leaders and extra-ordinary access to government funds among others.

The capital flight menace over the years has drastically reduced the domestically investable funds thereby disallowing the economy to grow normally. Hence, Nigeria government continued to borrow from both internal and external sources with high interest rate and conditionality attached.

As a result of the above, the following recommendations were suggested:

(I). Nigerian government should pay serious attention to the provision of infrastructural facilities (e.g. regular power supply). This would encourage the national and foreign investors to invest in the country thereby increasing capital inflow to Nigeria and hence, leading to increase in production of goods and services within the economy.

(ii). Government should also find a way to eliminate the exchange rate misalignment to reduce flight of capital out of the country. The constant weakness of the naira against dollar has really discouraged many investors in keeping their money in naira form hence transferring such fund to outside the country.

(iii). Government should create an enabling environment for investment to reduce capital flight from the economy. The present government should as a matter of urgency curtail the "Boko Haram" insurgence which has destroyed so many lives and property in the northern part of Nigeria. When lives and property are not secured, investors flee to better environments.

(iv). Corruption should be checked in order to have a complete transparent process of fiscal management at all levels. The passing of freedom of information bill necessarily makes information available for all interested party needing it and must be fully utilized. Some studies have blamed the prevalence of capital flight on the seemingly intractable problem of corruption in Nigeria. One of the difficulties of measuring accurately the total value of capital flight is the illegal means of transferring ill-gotten funds overseas through bizarre processes. Capital will surely continue to flee if corruption is not checked in Nigeria as government decides not to be sincere about nipping the problem in the bud.

(v). Adequate penalties should be melted out to any national or expatriate illegally carting away capital from the economy. So much money is never accounted for within the political cycle of the country. Many of our bankers and politicians have illegally carted away peoples' deposits and funds meant for domestic development to acquire property worth billions of naira outside the country. This is a bad omen to the economic development of Nigeria.

Therefore, if the suggestions above are implemented, it is believed that capital flight from Nigeria would be curbed and hence, the economic would have access to enough investible funds locally instead of running after external debts with huge burden.

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