Impact Assessment of Globalization and Capital Flow on the Nigerian Economy

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Abstract. This study examines the impact of globalization and capital flow on Nigerian economy during the period of 1983-2019. The variables used include trade openness, government expenditure, money supply, exchange rate and capital were analyzed using co-integration and error correction model to understand the relationship between the variables mentioned. Result shows that the variables are co-integrated. Globalization has a negative and significant association with capital inflows in the short run. In addition, the relationships between globalization and capital inflows is positive and significant in the first lag. The Johansen test found that the variables in the model on the effect of globalization on capital outflows are co-integrated. Globalization has a favorable and strong relationship with capital outflows in the short run, both in the current time and one year afterwards. The study recommends among other things that Nigeria's business environment should be well-developed in order to attract both domestic and foreign investors to the economy.

Keywords: Globalization, Capital Flow, Co-integration, ECM and Economy

Introduction

Globalization is the process of bringing national economies together through commerce and financial exchange. It entails the cross-national movement of commodities and services. Globalization includes cultural, political, and technological dimensions, according to (Agbarha & Peter, 2017). Globalization has shown to be the most often used strategy for addressing economic development, enhancing state social welfare, and establishing political ties between countries over time (Nsehe, 2017). It has been going on for centuries, from the colonization of the world's inhabited areas to the emergence of nations, from conquests to independent countries, from sailboats and caravans to steamboats, truck fleets, and cargo planes, from trade in a few commodities to global production and distribution networks, and finally to the current explosion of international flows.

Globalization has a long and illustrious history. Although globalization is widely regarded as a modern phenomena, historians recognize that it is not new in several crucial ways. The present period of globalization, according to economic historians, began around 1870. For decades, developing countries have desired money as a supplement to local savings for growth and development. This is fueled by the need to bridge the gap between savings and investments to maintain economic growth, as indicated by the focus on attracting foreign money as a key source of filling the savings-investment gap in most resource-scarce economies, particularly in emerging countries (Gabriel, John & Baryl, 2019). Long-term development of a growing economy like Nigeria would necessitate consistent and significant investment expenditures sufficient to meet the country's critical capital needs. Due to the dynamism of the underlying economic underpinnings, many avenues for achieving these aims are always being investigated. One of the measures is to open up trade between countries and to speed up the flow of foreign direct investment (Gabrie *et al.*, 2019). Foreign capital flow is a factor for economic growth and development, according to the current reforms implemented in most developing countries' economies, such as Nigeria's, which cover the financial, public, and private sectors.

Capital inflow is very desirable, having played a significant role in both the development of less developed economies with insufficient domestic resources (Nwokoma, 2013) and the

development of industrialized economies. He further shows that through capital inflow, recipient economies can finance developmental projects that will ensure growth and eradicate poverty, while capital outflow smooths the donor countries' consumption patterns, assisting them in achieving higher consumption in the long run (Ikpesu, 2019).

Capital inflow was essential to offer the necessary growth for developing countries to achieve economic take-off. This means that the ability of emerging economies to join the global production web through capital inflow is inextricably linked to their ability to boost productivity, technological transfer, effective competition, and economic growth. As a result, private capital inflows have increased dramatically over the decades, owing to a variety of local and external variables that have contributed to the region's (ECOWAS) appeal to global investors (Orji, Uche & Ilori, 2014).

When intended investments exceed actual savings and investments with extended gestation periods that create monetary returns, as well as expanding government expenditure that is not tax supported, capital is required (Balogun *et al*., 2019). Capital inflow has been seen to signify additional resources that a country requires to strengthen its economic performance and give employment opportunities. As a result, developing economies around the world, particularly Nigeria, have realized that local resources alone are insufficient to finance investment and accelerate growth, luring international investors to invest in the country. The issue at this time is that the government has not been able to create an enabling climate that will encourage skilled foreign investors to invest actively in the country. Because of the continuing issues of corruption, instability, and policy inconsistency, the government's efforts to improve the industrial sector through luring foreign investment have clearly failed. However, these difficulties have resulted in a steady reduction in foreign capital inflows and industry performance in Nigeria (Olunkwa, 2018).

Literature Review

Globalization is a multi-dimensional notion since it encompasses a wide range of topics, including economics, politics, and social issues. Because of its multi-dimensional complexity, it is extremely difficult for multiple definitions to agree on what the notion actually implies. As a result, globalization is defined in a variety of ways by various individuals and organizations. Although these definitions have a lot in common in terms of meaning, they have a lot of variances in terms of what they cover, therefore it's impossible to give an accurate description (Kilic, 2015).

Nigeria, Africa's colossus, has long embraced globalisation as a strategy of achieving rapid economic growth. Surprisingly, despite having abundant natural resources, 53.5 percent of Nigerians live in abject poverty (World Bank, 2009), and the country's human development index is ranked 152nd (United Nations Development programme, 2016). Given these figures, Nigeria is clearly one of the most disadvantaged countries participating in globalisation, given her high unemployment rate, vulnerable economy, bad policies, unfavorable investment climate, high level of indebtedness, and corruption.

Globalization, according to Mutascu and Fleischer (2011), has both beneficial and bad consequences. Increased national income through comparative advantage, access to global finance, the spread of technology, opportunities for individuals, and the spread of human rights are only a few of the beneficial benefits. The ability to weaken the position of those lacking skill or capital, the problem of economic openness in weak states, exploitation of works in poorer countries, destabilizing global capital markets, loss of cultural integrity, an undermining of national economic autonomy, and so on are some of the negative effects.

Capital Flows

Capital inflows and outflows are two types of capital flows.

Capital outflows have been seen as a major contributor to the foreign debt crisis and a barrier to growth in the developing nations. The massive quantity of capital outflows faced by LDCs, as well as their effects on national economies, have piqued the interest of many economists in recent years. Various risk perceptions, exchange rate misalignment, banking sector limitations and repression, fiscal deficits, poor institutions, macroeconomic policy distortions, corruption, and unusual access to government funds are among the causes of capital outflows, according to Ajayi (2012).

Foreign capital inflow has been identified as an important mechanism for expanding the supply of money for local investment, according to Orji, Uche and Ilori (2014). Africa and other emerging economies require significant inflows of capital to close savings and foreign exchange deficits, as well as to boost capital accumulation and development, which are required to alleviate widespread poverty. As a result, the relative benefit(s) of foreign capital influx as a productivity-enhancing package is now widely recognized, especially in light of recent financial crises.

Capital flows are caused by savings/investment imbalances between countries, resulting in the transfer of real resources via trade or current account transactions. They react to economic fundamentals, government policies, and flaws in the financial markets. However, assessing the impact of these policies and distortions is particularly difficult since they frequently overlap, generating both barriers and stimulus to capital movements. Capital transfers to developing countries are hampered by a number of causes. Liquidity, market size and concentration, little trading volume, weak capacity to enforce regulations, country and regulatory hazards, and exchange controls are only a few of them. Taylor and Sarno (1997) identified two categories of factors that influence capital flows. The first type of pull factor is country-specific, which reflects domestic potential and risk. Capital (bond and stock) flows are projected to become a more important source of external finance as developing countries' creditworthiness improves. Equity-related capital flows, for example, might be quite big, according to them, and could take the shape of either Foreign Direct Investment (FDI) or portfolio investment in shares. The opportunity to use local raw resources or use local labor force may entice FDI. Other important factors of capital flows include rates of return, credit ratings, and secondary-market pricing of sovereign debt, which represent the opportunities and hazards of investing in the country.

Globalization in Nigeria

International interactions and contacts are not a new occurrence. It began during the Mercantilist era, which lasted from the sixteenth through the middle of the eighteenth century. They crisscrossed the globe in search of valuable metals, partitioning and colonizing every continent in the process. Even in the Classical era, the law of comparative advantage encouraged the interchange of goods and services. This was made feasible by the existence of comparative advantage, which is defined as a situation in which one country has a comparative cost advantage over another in the production of an item.

Furthermore, throughout the twentieth century, Neo-classicists saw the potential for international trade and exchanges. This was made possible by the fact that different countries had varied proportions of production elements. As a result, countries have been encouraged to develop and export commodities in which they have a plentiful supply of production factors. As a result, globalization has a long history. Trade, exchanges, inter-country movements, travels, and migration were all used to accomplish this. The global economy has become extremely dynamic, with tremendous growth potential. Technological, financial, and information technology advancements, among other disciplines, have offered a plethora of chances for generating economic growth and advantages (Tonuchi, 2015).

Capital Flows in Nigeria

Some scholars suggest that capital inflows in the form of aid disbursements/FDI to developing nations are a major driver of capital flows because capital inflows and outflows occur at the same time (Adekunle *et al.*, 2020). The availability of foreign exchange raises the possibilities for bribery and corruption in cases involving public sector borrowing. According to anecdotal evidence, major portions of assistance inflows controlled by the Nigerian government have resulted in around half of the aid amounts reaching the intended beneficiaries, while the other half has been 'lost' within the official institutions.

Countries that have recently witnessed significant levels of capital movements are expected to see higher capital outflows in the coming years (Epstein, 2012). This is primarily due to the momentum generated by capital outflow. In most circumstances, the presence of substantial capital outflow for a given level of government expenditure may lead private actors to expect higher tax rates as a result of the consequent lower tax base. As a result, the resulting drop in expected after-tax profits discourages domestic investment and encourages private agents to look for higher returns elsewhere. Furthermore, capital outflows may become habitual, making it difficult for investors to respond quickly to any changes in the investment climate (Epstein, 2012).

Capital outflow can happen in a variety of ways. There are so many conduits that compiling a complete list of them is nearly impossible. The most important channels for Nigeria are discussed in this section. To begin with, transfers can be made using cash or monetary instruments. These are typically in the form of international or domestic currency, traveler's checks, or other types of checks. Stories abound from the early 1970s of Nigerian cash being transported out of the nation and exchanged legally for foreign currencies at current market prices in major financial centers such as London and New York. Despite the current economic situation, the naira is still exchanged for other currencies in the course of trade in various African countries.Second, capital flight can occur through bank transfers from a foreign institution's local affiliate to a targeted beneficiary abroad. This is possible at the market rate, with no limits or constraints in place. In the face of currency regulations, transfers may still be possible, although at a less favorable rate. The existence of local affiliates of foreign banks may be seen throughout the history of banking in Nigeria. It is undeniable that transfers of the type described have occurred in Nigeria. However, it is logical to assume that such transfers will not be available for illegally created income

The black market, which was formerly a major source of transporting funds outside, is a fifth means of transferring money abroad. It's difficult to quantify how much money has been transmitted this way. Commissions and agents' fees, which are paid by foreign contractors into the foreign bank accounts of residents, are a sixth way for capital to be transferred overseas.

According to Umoru (2013), an analysis of UNCTAD data shows that global foreign direct investment (FDI) outflows increased at an annual average rate of 13% between 1980 and 1997, which was significantly higher than the annual growth rates of 7% reported for world GDP at current prices and world export of goods and non-factor services (IMF, 2007). Between 1987 and 1996, private capital reached a total of US$40 billion, with Nigerian residents accounting for $17.5 billion and the Sudan for $7.0 billion (Epstein, 2012). Over the same period, residents of Sub-Saharan African countries increased their unreported foreign asset holdings by US$132.0 billion. Nigeria accounted for approximately US$11.7 billion, while Sudan accounted for approximately US$7.2 billion.

Comparative Advantage Theory

This is because trade as a phenomena is usually pursued by economic agents since it is a profitable means of doing business. To ensure that the process of lucrative trade takes place, various abilities and resources are frequently pooled. People frequently find it more beneficial

to trade goods they already have in great amounts relative to their tastes or requirements in exchange for things they urgently want since it is difficult for humans to meet all of their basic demands; hence, the concept of comparative advantage.

According to the comparative advantage hypothesis, countries should specialize in exporting items that they can produce at the lowest relative costs under competitive conditions. David Ricardo proposed this hypothesis. The argument is based on the fact that equivalent items in various countries have varying production costs. Due to geographical division of labor and specialization in production, production costs vary widely between countries. A country can produce one commodity at a lesser cost than the other due to differences in climate, natural resources, geographical location, and labor efficiency. As a result, each country focuses on producing the commodity with the lowest comparative cost of production. As a result, when a country engages in commerce with another country, it will export commodities with the lowest comparative cost of production and buy commodities with the highest comparative cost of production.

The Investment Diversion Theory

This theory claims that because of the macroeconomic and political uncertainty in developing countries, as well as the availability of better investment opportunities in advanced countries, such as high foreign interest rates, a diverse range of financial instruments, political and economic stability, a favorable tax climate, and account secrecy, some unscrupulous corrupt leaders and bureaucrats usually take advantage of these opportunities. As a result, these funds are unavailable for investment at home, resulting in a drop in aggregate investment, low economic growth, and, as a result, a drop in employment, an increase in dependence ratio, and a high death rate. These unfavorable macroeconomic repercussions on these countries may need borrowing from outside in order to resuscitate the home economy, which can lead to greater external dependency and debt.

If the authorities operate a floating exchange rate system, the liquidity constraint could lead to a depreciation of the domestic currency (Ramasamy & Yeung, 2005). At this point, attempting to preserve the exchange rate will result in a loss of international reserves. One of the well-known negative effects of capital outflows in the nations affected is the investment diversion concept. However, by itself, it only explains a portion of the economic effects of capital flight.

Ndubuisi and Abdul (2018) studied Nigerian capital flows and industrial performance between 1980 and 2016. In addition, the study employs the VEC Model, while the granger causality test is used to investigate the causative relationship between capital flow components and industrial performance as measured by industry value added. The findings show that there is a long- and short-run relationship between capital flow components and industrial performance, and that there is no causality between workers' remittance, official development assistance, and industry value added, though there is unidirectional causality between foreign capital inflow and industry value added. Furthermore, the paper recommends that the government solve the issue of insecurity and policy inconsistency as soon as possible in order to ensure free flow of capital, workers' remittance, and foreign investors' confidence in the country.

Balogun *et al.* (2019) use data from the Central Bank of Nigeria to look at the impact of capital flows on economic growth in Nigeria from 1981 to 2016. In order to estimate our given model, we used the method of error correction model framework and autoregressive distributed lag. Capital flows have a considerable impact on Nigeria's economic growth, according to our estimated model. As a result, the study suggests that strong, robust, and energetic economic policies be developed solely for the goal of attracting and bringing money into the country,

thereby assisting in the bridge-building of capital required for Nigeria's economic growth and development.

From 1986 through 2016, Danladi *et al.* (2021) looked at the impact of capital flight on Nigeria's economy. The endogenous variables employed were Real Gross Domestic Product and Capital Flight, while the explanatory factors were others. The Statistical Bulletin of the Central Bank of Nigeria (CBN), the World Bank Development Index, the Economic and Financial Crimes Commission Bulletins, the Tertiary Education Trust Fund Publications, and the Federal Ministry of Information Annual Briefings and Extracts were used to compile data for these variables (various editions). The variables were discovered to be mixed order integrated, thus we used the Bounds test to confirm the long run relationship between them. A negative and significant association exists between capital flight and economic growth, according to the simultaneous equation model. Domestic Investment and Interest Rate Differential have both been found to have positive and significant effects on Real GDP, whereas Political Instability, looted Funds, Expenses on Foreign Education, and Medical Services have all been found to have positive and significant effects on Capital Flight. These findings suggest that capital flight has harmed Nigeria's economic progress, with foreign education and medical expenses, as well as looted funds, being the main conduits through which large sums of money leave the nation. Our educational and health-care infrastructures should be sufficiently funded and maintained, according to the recommendations.

Globalization and Economic Growth: Evidence from Nigeria, observed Maduka, Madichie, and Eze (2017). To analyze the influence of globalization on economic growth in Nigeria, the study employs modern econometric approaches such as co-integration and error correction mechanisms within the context of the Pesaran *et al.* (2001) ARDL model. The study finds that trade openness, financial integration, and foreign direct investment all have a significant beneficial impact on Nigeria's economic growth, using annualized secondary time series data from 1970 to 2015. As a result, proper mechanisms should be put in place to ensure that globalization achieves the required economic growth rate.

Between 1981 and 2016, Ikpesu (2019) intends to determine the growth benefits of capital inflows in Nigeria utilizing investment as a transmission channel. To analyze the data, the researchers used least square regression. Capital inflows have a beneficial and considerable impact on the growth of the Nigerian economy, according to the findings of the study. This indicates that infusions of foreign capital have aided the country's economic development. Domestic investment has a good and considerable impact on Nigerian economic growth, according to the research findings. The study's findings suggest that capital inflow and domestic investment have aided Nigeria's economic growth. This study's conclusions provided important policy guidance. To begin, the study stressed the importance of the government and policymakers attracting more foreign capital into the country, but the negative effects of large capital inflows into an economy must also be recognized. Second, the government should figure out how much capital should come in to help the country develop and thrive.

For the years 1981 to 2016, George-Anokwuru (2018) looks at the impact of globalization on Nigerian economic growth. Imports, Exports, Foreign Direct Investment, and Gross Domestic Product are all investigated in this article. For the research period, the paper uses limits cointegration tests and the Autoregressive Distributed Lag (ARDL) test. The model's short and long run forms show that import is adversely associated to GDP but has a considerable impact on growth, whereas the short and long run impact of export on GDP is positive and significant, showing that export enhanced Nigeria's GDP growth by 10.98 percent. Foreign Direct Investment (FDI) has been demonstrated to have a negative impact on GDP. This conclusion implies that FDI is ineffectual in propelling Nigeria's economic growth. Nigeria is not yet reaping the full benefits of globalization, according to the results of this article. This paper suggests that Nigerian authorities should develop and implement policies to

reduce import levels, as well as policy measures and reforms, as well as sound macroeconomic policies, to create a more stable and conducive environment for investment and economic activity.

Methodology

The data used in this study included time series data from 1983 to 2019. It is based on secondary data from the World Bank Development Indicators, the National Bureau of Statistics, and the Nigerian Central Bank's statistics bulletins.

Model Specification

$$CF = F(CI, CO) \quad (1)$$

Where CI = Capital Inflow (represented by FDI inflow)
CO = Capital Outflow (represented by FDI outflow)
CF = Capital Flow

$$CI = F(GLO, GEX, MS, EXR) \quad (2)$$

Where; GLO = Globalization (represented by Trade Openness)
GEX = Government Expenditure
EXR= Exchange Rate
MS= Money Supply

$$CI = \alpha_0 + \alpha_1 GLO + \alpha_2 GEX + \alpha_3 MS + \alpha_4 EXR + \mu$$

Where αo is the intercept when the explanatory variables are equal to zero and α1, α2, α3, α4 are the coefficients or parameters attached to the explanatory variables. μ is the error term.

Results and Discussion

The results of the ADF unit root test revealed that all variables are stationary only at first difference, implying that the variables are integrated of order one. This is because the ADF test statistic values are more than the MacKinnon critical value at the 5% significance level and the probability values of the ADF test statistics are less than 0.05.

Johansen Co-integration Test

The Johansen cointegration test was used to determine whether the variables utilized in this study have a long-term relationship. The presence of co-integration indicates that the variables are in a long-run equilibrium relationship. This means that if a set of variables is co-integrated, the effects of a shock to one of them spread to the others, sometimes with time lags, preserving the variables' long-run link.

Table 1. Johansen Co-integration test

Series: LNCI LNGLO LNGEX LNMS LNEXR				
Unrestricted Cointegration Rank Test (Trace)				
Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None *	0.665695	78.66775	69.81889	0.0083
At most 1	0.447351	38.12681	47.85613	0.2965
At most 2	0.212831	16.18464	29.79707	0.6993
At most 3	0.160215	7.330088	15.49471	0.5396
At most 4	0.023227	0.869525	3.841466	0.3511
Trace test indicates 1 cointegrating eqn(s) at the 0.05 level				
Unrestricted Cointegration Rank Test (Maximum Eigenvalue)				
Hypothesized No. of CE(s)	Eigenvalue	Max-Eigen Statistic	0.05 Critical Value	Prob.**

None *	0.665695	40.54094	33.87687	0.0069
At most 1	0.447351	21.94217	27.58434	0.2234
At most 2	0.212831	8.854553	21.13162	0.8440
At most 3	0.160215	6.460563	14.26460	0.5548
At most 4	0.023227	0.869525	3.841466	0.3511
Max-eigenvalue test indicates 1 cointegrating eqn(s) at the 0.05 level				

Source: Computation from E-views (2021)

The Johansen cointegration test for the capital inflow found that the variables used in this study are cointegrated. The presence of one cointegrating equation is indicated by the Trace test, and similarly, the presence of one cointegrating equation is indicated by the Max-Eigenvalue test. This means that the variables are cointegrated and that there is a long-term relationship between them.

Error Correction Model (ECM)

The Error Correction Mechanism is the most appropriate strategy to apply when they all the variables were stationary at first difference and co-integrated. The short-term dynamics of a variable around its stationary equilibrium value are detected using an error correction model (ECM).

Table 2. Error Correction Model

Dependent Variable: D(LNCI)				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.066599	0.118037	-0.564223	0.5781
D(LNCI(-1))	-0.007841	0.309754	-0.025313	0.9800
D(LNCI(-2))	0.164640	0.195383	0.842653	0.4081
D(LNGLO)	-0.313339	0.142629	-2.196888	0.0406
D(LNGLO(-1))	0.326421	0.080168	4.071702	0.0003
D(LNGEX)	0.671688	0.083681	8.026739	0.0000
D(LNGEX(-1))	0.126940	0.268748	0.472338	0.6411
D(LNEXR)	0.911857	0.086526	10.53854	0.0000
D(LNEXR(-1))	0.586716	0.052856	11.10031	0.0000
D(LNMS)	0.316170	0.727088	0.434844	0.6677
D(LNMS(-1))	0.220104	0.740748	0.297137	0.7690
D(LNMS(-2))	0.217967	0.081397	2.677831	0.0116
ECM(-1)	-0.879904	0.376831	-2.335009	0.0286
Squared 0.723145 F-statistic 3.036668 Adjusted R-squared 0.522271 Prob(F-statistic) 0.00015 Durbin-Watson stat 1.985167				

Source: Computation from E-views (2021)

In the table above, the ECM result on the effect of globalization on globalization is shown. The R squared value is 0.723145, indicating that the model is well-fitting and that changes in capital inflows can be attributed to changes in the independent variables by about 72%. The F statistic's probability value of 0.00015 indicates that all of the independent variables used in this study have a significant impact on capital inflows. The Durbin Watson statistic is greater than the R squared statistic, indicating that there is no spurious regression. At the 5% level of significance, the ECM coefficient is negative, less than one, and statistically significant.

Capital inflows in the first lag have a negative relationship with current-period capital inflows, whereas capital inflows in the second lag have a positive relationship with current-period capital inflows. In both the first and second lags, this association is minor. Globalization has a negative and significant association with capital inflows at the moment. This is due to the fact that Nigeria's business climate and economic performance are unappealing to investors, and as a result, capital flows into the country will decline. However, in the first lag, this relationship is positive and significant, implying that a 1% increase in globalization will result in a 33% increase in capital inflows. Government expenditure has a positive relationship with capital inflow in both the current and one-year lagged periods. It means that when government spending rises, capital inflow rises with it. In both the current period and a one-period lag, the exchange rate has a positive and significant association with capital inflows. This means that as the currency rate falls, capital inflows rise. In the current era, as well as the first and second lags, Nigeria's money supply shows a positive connection with capital inflows.

Conclusion/Recommendation

Globalization has a negative and significant association with capital inflows in the short term. However, the relationship between globalization and capital inflows is positive and significant in the first lag. The Johansen test found that the variables in the model on the influence of globalization on capital outflows are co-integrated. Globalization has a favorable and strong relationship with capital outflows in the short run, both in the current time and one year afterwards.

Globalization has a negative link with capital inflows in the short run, according to the research. This suggests that when globalization improves this year, capital inflows from foreign direct investment will decrease. When it comes to capital outflows, globalization has a favorable correlation with them. Nigeria's business environment should be well-developed in order to attract both domestic and foreign businesses. Macroeconomic stability, particularly exchange rate stability, must also be achieved. A stable exchange rate regime or system encourages international investment while also protecting the local currency's value. Governments and policymakers must work to improve the performance of all sectors that have been badly impacted by globalization. Economic diversification in the oil sector, which has been the country's major contributor to GDP in recent years, should be encouraged, and investments in other sectors such as manufacturing, agriculture, and solid minerals should be made.

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