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Institutional Qualities and Nigeria's Economic Growth Performance

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Abstract: African disappointing Economic performance has focused attention on the role of institutions in determining African economic growth. The role of institution for promoting growth in Nigeria has sparked a number of interests in recent years. The aim of this study is to examine institutional qualities and economic growth performance of Nigeria. This study employed two methods, the ARDL model approach to co integration and Causality, the second approach explore from the historical narratives how successful developers dealt with the problem of reverse causality. Whereas, filling the existing literature gap, this study found that higher sustainable improvement in good institutions is associated with rising growth and per capita income. Pertaining to the major area of dispute on the direction of influence, the findings of this study indicate that there is a reverse causality. Historical evidence reveals that a number of economies did not achieve significant improvement in good institutions before they began their economic transformations and Nigeria is no exception. This study suggests that the government needs to focus on development of critical sectors that may yield faster dynamic transformational change in Nigeria.

Key words: Institutions · Growth · Sustainable Development · Nigerian Economy

INTRODUCTION

The literature on Institutional approach to development stresses the importance of term "good institutions". The term is generally described as the traditions and institutions which explain the authority as applied in a giving country [1] matters for economic growth and poverty. This understanding surface from the earlier pioneering work of institutional economists such as [2] their pioneering works generated a wide spreads of cross-sectional empirical evidences, suggesting a positive relationship between institutional structures and economic growth, No wonder, in recent development a lot of agreement have been reached among growth economists, development specialists and international policy- makers that "good institutions" is considered as basic and necessary for economic growth and poverty reduction [3] and [4] Despite comparative literature on institutional structure and social determinants of economic growth and poverty, the institutions matters for development have been marred with a number of shortcomings. Various studies which to show that good institutions is important for economic growth have suffer a number of challenges for example the problems of reverse causality [5] Attempt to addressed causality problems has been marred with measurement error, [6], missing variables [7] conceptual vagueness [8].

The weakness of these types of cross-sectional regression exercise has been documented, by [1] in his famous work he pointed out that with regards to East Asia these cross-sectional studies have failed to capture the nuances of the interactions between governance and economic growth, because the governance measures were developed based on the implicit governance model which exists only in institutions available in Western advanced countries [1] his argument show that some of these successful Asian developers do not fare well in terms of conventional governance scores but yet they are superstars when it comes to economic growth performance, they created in a matter of short span of time a kind of growth and development miracles hitherto never expected in human history, conspicuous example here is China today occupying the second most enviable fasted growing economy in the World.

These curious arguments raised by Quibria find its way into Africa, building on the concerns of [9], in his famous works Understanding African poverty: Beyond the Washington Consensus to the Millennium

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Development Goals approach, he powerfully contested the argument that African failing to grow is the problem of either Macro economic mismanagement or constraints is the efficiency of private market, due to corruption and bad governance. Sach *et al*. explain that most of the poor counties especially in Africa experience have bad governance measures when compared to the developed countries.

This paper tackles the general questions of the role of institutions in achieving economic growth, treated among others by [10] and [9] On the contrary to these authors who were interested in the effects of institutional quality on the level of per capita income. This article is interested in the direction of influence from economic growth to institutions and whether institutional reforms are what are needed to address structural problems at an early stage of development.

Moreover, the studies [10] and [9] focus on political institutions and found positive and significant effects on growth. In contrast, this study is focusing on the quality institutional measures, in order to check the validity of the empirical evidences established through the use of these measures of institutional indicators, because these are the indicators used to show that institutions matters to Africa.

This study significantly differs from the study of [10] and [9] by complementing empirical evidences with historical evidences from the successful developing economies on whether institutions are necessary before a country can achieve economic development at an early stage of economic development.

Lastly, so far our knowledge goes beyond reasonable doubt, the existing studies [10, 9] did not solve the endogeneity problems in their studies, this paper aim to overcome this kind of shortcoming by using the ARDL Approach to Co integration and causality through the error correction analysis.

This signifies there is lack of clear understanding on the causal linkage between institutions and economic growth in Nigeria; hence, a thorough examination of the impact of institutions in specific to Nigeria is now imperative.

This study examines the qualities of institutions and economic growth performance using time series data for Nigeria because only limited studies investigated the relationship between institutional changes and economic growth over time in the same context. This study matters for Nigeria because time series outcomes may provide better understanding than cross- countries –section research, which combine every country together.

Following the introduction above the remaining section will be structured as follows; part two will focus on materials and method, while the remaining section will present results and discussion of the results.

MATERIALS AND METHOD

Theoretically, among the studies, that examine qualities of institutions the studies of [3] were the early study to emphasize on the role of institutions for an economy. North study was back up by the work [11] and [12]. The main idea behind the work of North is the importance of institutions public and private, as well as formal and informal, which include economic and social as well as political that determine how and economy functions. In fact he went further to described institutions as the set rules that determine how a society behaves in a particular setting. In his analysis he went further to explained that institutions encompasses taboos, customs and traditions as well as norms and values that hold the fibred of a society. He extended the definition to include formal written constitutions and laws governing economic, political and social interaction in the society.

Khan, [3] explained that the configuration of rules establishing institutions influence the incentives arrangement to which individual respond. [13, 14] have argued that institutions changes as the transaction costs of interaction changes, this is more obvious as the economy advance and technological advancement also improved. Equally institutions changes as the political and social forces within a society changes. [3, 11, 12] all have expressed the importance of property rights and contract enforcement in economic growth.

One of the good empirical efforts to examine the relationship between institutions and economic growth was conducted at World by the group of research [14] The findings of their studies reached to a conclusion that there is a bidirectional relationship between quality of institutions and economic growth and the influence is from institutions to growth.

Dollar, [14] and Kaufman, [15] they examined the direction of influence between governance and per capita 173 countries using data of over 300 indicators of governance selected from a large number of cross-country studies for the years 1997-98, the team developed aggregate indicators related to six governance indicators. The results of this study portrays that there is a significance positive relationship moving from good governance to economic growth. The study was backed up by subsequent studies by the same team [16, 17].

Other important case studies on Nigeria that emphasized on the role of institutions as a precondition of economic sustainability include the work of [10, 18] Other studies that indicated good institutions create higher income performance rather than the reverse causation include [11, 19, 20].

However, on the contrary, despite the proliferation of the above qualitative studies, there is a serious question emerged on the validity of the quality of institutional reforms both from within the main stream and heterodox economic studies. The fact remain that such types of empirical studies cannot precisely explain how institutions is necessary required for growth rather than the reverse causality, that is growth causing institutions For instance [9] demonstrated an econometric analysis that standardized the measurement of institutions by level of income and found that, in fact, a lot of African countries are properly govern based on the level of their income. Therefore, they reached a conclusion that there is a weak relationship between improvement in institutions and economic growth.

The general conclusions within the heterodox studies is that it is economic growth that influence institutions by improving higher income; this is clear in the case where growth was accompanied by greater need for higher good institutions (for example, desire for political institutions, which greater checks and balance). This is because institutions are desirable things to have but not a preconditions for development they can only be possess after certain level of economic prosperity is attained [21] A number of historical evidences suggest that rich countries possess most of the institutions in their economy, assume to be pre- requisites for economic development after they have achieved some level of economic prosperity not before the attainment of economic development such as democracy, rule of law and private property right.

On a general note, it is very clear that the literature on institutions and economic growth has not been settled on well accepted definition of institutions and concepts. Apart from that, it is also suffering from deficiency theory of how institutions themselves changes.

However, ignoring important possibility that economic growth changes institutions in the institutional policies discourse in poor countries, thus, make it imperative to conduct a case study of Nigeria in order to determine the direction of influence between institutions and economic growth.

Model Specification: We applied autoregressive distributed approach to co integration recently developed by [22], which is a breakthrough in the area of modeling time series data and the most simples' way of establishing the long run relationship among economic variables under investigation. Why we decided to adopt ARDL approach to our own study is because this approach enables us to investigate the long run relationship between governance, economic growth in Nigeria. One of the break though in the application of ARDL approach to co integration is how it side step the unnecessary difficulty of achieving the order of 1(0 and 1(1) as a condition of integrating order of our series (Pesaran and Shin, (1999). This approach appears to be more reliable better and more reliable when compared with [23, 24] approach to establishing co integration. One interesting thing with ARDL model is it provides avenue of using OLS estimation criteria for identification and estimation of certain variables under consideration (Lee, Pesaran, & Smith, 1998). The application of OLS into the long run relationship development is a breakthrough to ARDL approach, since reliable information can be generated and inferences are made possible out of the long run association established. If there is co – integration there must also be error correction representation which determine the direction of causation both in the short run and long run, therefore, in order to establish the direction of causation amongst variables in our model we took the next step of estimating the Error Correction Model (ECM) as suggested by PSS [25].

Moreover, after estimation, of the regression analysis under bound testing, we compare the F- test with critical values provided by [26] and the calculated F- statistics. If at the end of the exercise the F- test value is higher than the upper critical value the null hypothesis of F test value lies below the lower critical value, the null hypothesis is not rejected. Thus but in case where the F test falls between the upper and lower critical values the outcome results is inconclusive. It is should be noted that if the order of integration of the estimated series is satisfied or realized when the variables are achieve an I(1), the decision is decision is consider on the basis of upper bounds. On the contrary, if all the variables are I(0), then the consideration is based on the lower bounds. In every step in ARDL modeling selection of the lag order is a very important because the estimation is very sensitive to the lag order. Normally there are possibilities made available in selection of the lags order, where the minimum value is

considered under the Akaie Information criteria, (AIC) but in case where the maximum number of lags length is consider it is based on Schwartz-Bayesian Criteria (SBC).

A diagnostic test is performed in order to make sure that the model is well specified and it is free from any forms of disturbances or instability. The stability test is conducted by employing the cumulative sum of squares of recursive residuals (CUSUM) and the cumulative sum of squares of recursive residuals (CUSUMsq). This enables us to be certain of the error correction representation results.

We consider the standard practice in the literature following the work of Abdul jalil and Yig ma (2008), we modify and specified the model below:

$$\Delta InY = \beta 0 + \beta 1 \Delta InYt - 1 + \beta 2 \Delta XEt - 1 + \beta 3 \Delta BQt - 1 + \beta 4 \Delta ERt - 1 + \beta 5 \Delta Not - 1 + \beta 6 \Delta LGt - 1 + \beta 7 \Delta KKt - 1$$

$$\beta 8 InYt - 1 + \beta 9 XEt - 1 + \beta 10 BQt - 1 + \beta 11 ERt - 1 + \beta 12 Not - 1 + \beta 13 LGt - 1 + \beta 14 KKt - 1 + et - - (1)$$

The null hypothesis of no long run relationship is examined through F-test of the joint significant of the lagged level coefficient of equation (1).

Ho: β8, β9, β10, β11, β12, β13, β13, β14, β15, β16=0
Hi: β8□0, β9□0, β10□0, β11□0, β12□0, β13□0, β14□0, β15□0, β16□0

where InY is the dependent variable, InXE, InBQ, InER, InNO, InLG, InKK, are the log of Accountable executive, Quality of the bureaucracy, strong civic society, rule of law, competitiveness of political participation and control of corruption respectively and et is the white noise term.

Sources of Data: Data on GDP per capita Proxy as InY were collected from World Bank economic indicators and Central Bank of Nigeria annual statement of accounts various issues. Similar Data on inequality of Income were obtained from the various National Poverty Assessments Survey, various issues and Deininger square assembled data set on inequality of income for Nigeria.

Measurement of the indicators of governance is not an easy task considering the abstracts nature of the concepts, this made a large amount of these indicators in principle multi-dimensional. Considering this multi dimensionality of these indicators, we follow the work of [6, 27] to use different measures for each dimension of the indicators. We have no option other than to utilize the existing set of data that was made available.

For the purpose of this study, we follow the work of [28] and collected data from different various sources due to recent development in which data on these indicators are made available from the World Bank and other various data houses. We specifically collected data from World Wide Governance indicators, Country Risk Guide ICRG data house, Business Environment Risk Intelligence (BERI), Polity 11 data house, Freedom house data set, World Bank CPIA assemble data set.

We try to establish indicators from the data available in these mansion data sets. We start with Accountability of the Executive; we collect data from the Gurrs Polity 111 data set. To measure the quality of Bureaucracy which is the second indicator of governance, in our model, we collected data from ICRG data house and data from BERI data house. The rule law, which is another variable in our model, data was collected from ICRG indicators data were made available beginning from 1972- 2011. Data on Strong Civil liberties were found from the Gastil (now called freedom house indicators data set. Data on Competitive Political Participation, where sources from Gurrs Polity 111 data set, data on the control of corruption where also mad available from the transparency international and World Bank CPIA data set we collected these data set and used it for our purposes.

Considering the important attached to the concepts of governance poverty and economic growth in the international domain. We try to test the hypothesis underlying the concepts of governance, economic growth and poverty reduction to see whether relevant understanding can be provided from the econometric exercise coming from these set of data, or the econometric data may not be sufficient in identifying the specific institutional constraints of a particular country. The next step we take is examine to see whether our research objective can be investigated using these assemble data set, to do that we employ the ARDL approach to co- integration approach as a tool of our analysis.

RESULTS AND DISCUSSION

Since the data is a time series, we test stationarity in order to satisfy the assumption underlying classical regression which said that the variables in our model must be (covariance stationary). Using Units roots test to ascertain the stationary of our data.We employed Dickey Fuller test and PP test statistics, we run the test both in level and first differences

In Table 1, the results indicates that after differencing all the variables are stationary at 5% level of significance, implies that the computed Mackinnon statistics is greater in absolute value than the calculated statistics. However, from the result obtained in Table 2 the F statistics of all variables in the model with exception of InEX, have exceeded the upper critical value at 5% level of significant with these we can conclude that the null hypothesis of no long run relationship is rejected and also, since the F- statistics does not fall below the lower critical value, the null hypothesis is also rejected and conclude that there is long run relationship between the estimated variables in the model.

In order to determine whether good governance affects economic growth we measure economic growth variables against the explanatory variables, within the long run ARDL model. The answer is affirmative if the coefficient of the governance's indicators is positive and statistically significant. Therefore Table 3 above has estimated the long run coefficient of the ARDL. From the estimated results four out of the six indicators of good governance integrate with economic growth in the long run. Control of corruption appears with highest percentage, effects, which suggest any 1 percent changes in corruption in Nigeria will causes 21.5% changes in economic growth this indicate high level of endemic corruption in Nigeria, the negative sign in the case of corruption does not contradict the economic theory, because according to the economic theory, there is an inverse relationship between aggregate economic growth and corruption. Higher level of corruption implies lower level of economic growth, the channels through which corruption affect economic growth is an inverse one. For instance, through impacting investment and entrepreneurship, distorting markets and undermining productivity. These proposition are supported by a number of empirical evidences for example [29-31], that corruption can affect economic growth negatively because corruption hinder both internal and external productive investment, through tax and frustrating entrepreneur manpower development, which will in turn affect the quality of social infrastructures such as roads schools energy, telecommunication and others. Another possible channel is that corruption may lead lower level of investment and low level of output.

Table 1: The Augmented Dickey- Fuller (ADF) test and Phillips Perron test for a Unit root

	Critical val.		Critical Val.		Criticical Val.		Critical Val.	
Variables	ADF level	level	ADF first.Diff	first. Diff.	PP level	Level	PP first. Diff.	level
InY	-5.8258	3.661661	6.69156	2.967767	5.841001	2.960411	-32.241	-2.96397
InEX	-5.5678	-3.66166	-6.6916	-2.967767	-5.841001	-2.960411	-32.241	-2.96397
InBQ	-3.9863	-2.96041	-6.7587	-2.967767	-3.959514	-2.960411	-19.548	-2.96972
InER	-4.6583	-2.98104	-6.942	-2.963972	-2.997492	-2.960411	-7.4651	-2.96397
InNO	-2.3269	-2.96041	-8E+06	-2.963972	-2.165423	-2.960411	-8.1006	-2.96397
InLG	-2.6707	-2.96041	-8.3162	-2.963972	-2.639485	-2.960411	-14.706	-2.96397
InKK	-4.0272	-2.96041	-9.652	-2.963972	-4.02723	-2.960411	-18.215	-2.96397

Note: * ** *** indicate significant at 1% 10% 5% respectively thus all variables are significant at 5% level of significant Sources: the table is computed by the researcher using Microfit version 4

Table 2: Bound test for the existence of a long-run relationship

Test statistics		Bound testing critical value with no trend	
F- Statistics	Significance level	1(0)	1(1)
InY 11.9212	1%	5.754	6.483
InEX 3.6511	5%	3.993	4.533
InBQ 14.5386	10%	3.247	3.773
InER 8.5994			
InNO 21.1851			
InLG 23.5460			
InKK 16.3289			

Note: The critical values are extracted from Narayan (2005b), case11model with intercept and trend,

Table 3: Estimated Long Run Coefficient Taking Economic growth as a dependent variable

Regressors	Coefficient	T-Ratio
InEX	-1.3366	-0.86872
InBQ	4.2032	2.2337
InER	2.8094	2.409
InNO	1.5347	1.0401
InLG	-.0034831	-.44393
InKK	-21.4952	-2.3042

Diagnostic test

Serial Correlation χ^2 (1) = 11.6032= (0.031)

Functional Form χ^2 (1) = 2.5658 (0.109)

Normality χ^2 (1) = 3.7098 (0.156)

Heteroscedasticty χ^2 (1) = 0.41224 (0.521)

These statistics are distributed as chi-square variants, based on the following tests:

A:Lagrange multiplier test of residual serial correlation

B:Ramsey's RESET test using the square of the fitted values

C:Based on a test of skewness and kurtosis of residuals

D:Based on the regression of squared residuals on squared fitted values

Table 4: Dynamic Error correction representation, Economic growth as a dependent Variable

Regressors	DInY	dInEX	dInBQ	dInER	dInNO	dInLG	dInKK
dInY				0	-0.006589	0	0
				-0.024628	(-4.3886)	-0.14321	(-0.23613)
dInEX	-664.8581		-1.107	-0.020434	-0.25203	-0.21719	
	(-5.9948)		(-6.1523)	(-.65638)	(-5.2584)	(-6.5160)	
DInBQ	-11.1659	-312.343	-0.44724		-0.051542	-0.17804	-0.17031
	(-4.3977)	(-3.5152)	(-5.4065)		(-3.4582)	(-12.8109)	(-8.4933)
DInER	-24.8378	329.4836	-1.3815	-3.0362	-0.54949	-0.54949	-0.5784
	(-1.4498)	-4.5228	(-2.9263)	(-4.3246)	(-4.0124)	(-4.0124)	(-4.2401)
DInNO	-36.3609	129.1064	-2.3518	-4.9548		-0.77079	-0.88004
	(-2.3006)	-0.76597	(-5.2584)	(-12.4578)		(-6.4289)	(-7.8361)
DInLG	-70.6329	302.3322	-14.5971	-0.77079			
	(-4.7561)	-2.1599	(-8.4933)	(-6.4289)			
dInKK	23.9472	-1644.6	3.0689	3.0689			
	(.1.5667)	(-5.9572)	-4.0724	-4.0724			
ECM	-0.66143	-15886	-0.66143	-15886	-0.51555	-1.8492	-2.27801
	(-5.2971)	(-3.2882)	(-5.2971)	(-3.2882)	(-4.1019)	(-16.2732)	(-1.8417)

ARDL(1,1,0,1,0,0,1,1) selected based on Schwarz Bayesian Criterion

Accountable executive is statistically not significant; implying that it does not affects the level of economic growth in the long run. The Rule of law is statistically not significant indicating that it does not affect the level of economic growth in the long run. Competitive politic is statistically not significant meaning that it does not affect the economic growth in the long run. Table 4 presented the estimated results of the Error correction model, where the direction of causality is expected to appear, in the dynamic model. Economic growth was taken as the dependent variables and was regress against the lag values of the coefficient of the independent variables in the model. Error correction mechanism, which is the residual of the long run equation, is negative indicating a correct sign and statistically significant. Signifying long run relationship between economic growth and independent variables in the model and the dependent variables significantly affect the level of economic growth and there is one way causality from the independent variables to the dependent variables. In other words we may conclude that having ECM value of -1.5886 indicate that there is high speed of adjustment towards the equilibrium steady state of equilibrium. When we consider, the two models dynamic poverty, with that of dynamic economic growth, we realized a bidirectional causality relationship between poverty and economic growth in Nigeria.

To test for the fitness of the model a diagnostic test was conducted and Figure 1 provide the results of the test on the serial correlation, functional form, normality and hetroscidesticity related with the model underestimation. Figure 1 indicate that the null hypothesis of all coefficient in the given regression are stable cannot be rejected. However, when we observe the short run relationship, the coefficients of the lag value of the model appear with wrong so no serious claims can be made out of the short relationship.

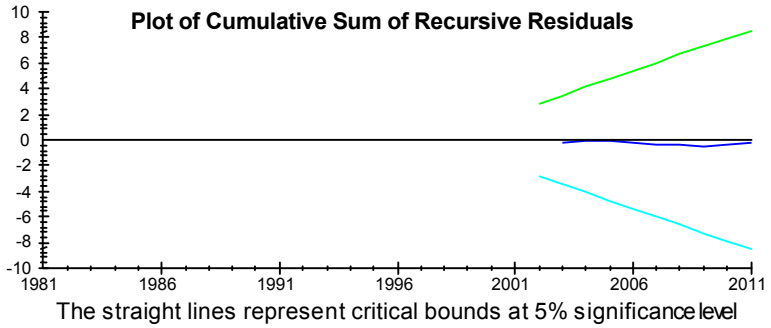

Fig. 1: Economic growth as dependent variable

When we take Accountability of the Executive as a dependent variable in the fourth model the results provides interesting information because the ECM which is the residuals of the long run relationship provide a statistically significant negative value of -1.8492 which indicate a long run relationship between Accountable executive and the rest of the independent variables in the model, one challenging information about the results is the bidirectional causality relationship between accountable executive and economic growth relationship because if we compare this with the results in the error correction representation model of economic growth where one way causality was achieved we can now safely concludes that another direction of causality is similar found here in this model moving from executive governance to economic growth, makes this findings seemingly paradoxical. This result seem quite consistent with the work of [6], who argue that the direction of the relationship between economic growth and Executive branch of government is bidirectional i.e economic growth also causes good governance. However our finding does not resolve the intense dispute on the direction of the relationship between governance and economic growth. A bigger understanding beyond the econometric data is necessary in order to figure out a clear understanding on the direction of the relationship which may require historical lesson from successful developers on how they were able to provide policy implication relevant to this type of analysis.

However, when we observe the short run relationship we found the coefficients of the lag value appear with a wrong sign as such serious claims cannot be made out of the results. However, one striking important in all the models was how the indicators of governance show a statistically significant relationship with economic growth. This indicates bidirectional relationship is established between economic growth and governance. This has suggested reverse causation on the direction of the relationship between governance and economic growth. This result seem paradoxical because contrary to the initial claimed by the classical economists and international donor agency that the relationship is one way and good governance is the necessary precondition for achieving economic growth, Our results suggest that economic growth also changes institutions. This study is entirely consistent with [32] who suggested that when initial incomes are taken into account (market improving) quality does not explain any significant part of growth difference in Nigeria. Similar conclusion is reached by Glaeser *et al*. (2004) in a wide ranging examination of governance indicators and economic performance.

CONCLUSION

The primary purpose of this study is to investigate the relationship between institutions and economic growth. However, the direction of the causality, remains to be established clearly and does have important implications for policy. We discussed the theory underpinning on the role of good institutions as it was developed, we test it plausible argument, using two methods of analysis. First, by using data for the period (1980-2011) with the sole aim of establishing the causal linkage among variables, the results suggest that the direction of causality remained indeterminate; as such issues of causality coming from these types of economic engagement need to be treated with caution. To understand why the difficulty of determining causality, we used historical narratives were history told us econometric data may not capture historical causality which demand understanding history. Looking at the historical wealth of evidences from the successful developers in Asia it was made clear that causality runs in two directions. Most countries, including the west do not have the existence of the good institutions at their early stage of development, until after they become rich.

But unfortunately compelling poor country to implement them at their early stage of development, no one is disputing the important of institutions they are desirable things to have but not at the early stage of development.

This study wraps up with some important policy implications for the Nigerian government. Nigerian government must pay attentions to the governance capabilities that would enhance economic growth, so that improved economic growth would lead to good institutions. Because, institutions improvement such as democracy, rule of law, anti-corruptions are very expensive public goods and they can only be achieved after certain level of economic prosperity is attained.

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