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Capital Market and Economic Developments in Nigeria

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Abstract: Economic development is one the major goals of national policy in any economy. It controls the growth of any nation. This research looked at capital markets and its role on the economic developments in Nigeria. With the gradual shift from bank dominated credit to capital market enhanced funds, it has become obvious that the capital market is the key in achieving economic growth and development.

Key words: Capital market · Economic development · Bank and Nigeria

INTRODUCTION

Economic development is regarded as the major goal of national policy in any economy, while capital accumulation or formation is also seen as a potent factor in the process of economic development. It is regarded as the core process by which all other aspect of growth is made possible and feasible. However, the rate of economic development is always limited by shortage of productive factor and if any scarce factor associated with development should be singled out, it will be finance (capital) [1].

A major engine of economic growth and development of a nation is its capital. It impacts positively on the economy by providing financial resources through its intermediation process for the financing of long term projects. The projects could be promoted by government or private sector institutions. They are usually in such areas as infrastructure, agriculture, solid minerals, manufacturing, banking and other financial services and other real sector areas. Hence without an efficient capital market, the economy may be starved of the required long-term fund for sustainable growth [2].

In Nigeria, the capital market has over the years been performing its traditional role. However, the efficiency and effectiveness in this regard have greatly being limited by various factors notable among which is the structure of the economy; which is dominated by oil production. Yet the oil producing companies are not fully listed on the stock exchange. Also the capital market has been identified as an institution that contributes to the socio-economic growth and development of emerging and economies. This is made possible through some of the vital roles played such as channeling resources, promoting reforms to modernize the financial intermediation capacity to link deficit to the surplus sector of the economy and a veritable tool in the mobilization and allocation of savings among competitive uses which are critical to the growth and efficiency of the economy [3]. It helps to channel capital or long-term resources to firms with relatively high and increasing productivity thus embracing economic expansion and growth [3].

Ekundayo (2002), argues that a nation requires a lot of local and foreign investment to attain sustainable economic growth and development. The capital market provides a means through which this is made possible. However, the paucity of long-term capital as posed the greatest predicament to economic development in most African countries including Nigeria. Capital provides the impetus for the effective and efficient combination of factors of production to ensure sustainable growth and development. Moreover, it is the effective utilization of productive resources accumulated over time that will determine the pace of growth of an economy. Growth in productive activities and its distribution determines the social well-being of the population. Capital formation can only be achieved through conscious effort and savings mobilization and accumulation of resources by both public and private savers.

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The Nigeria capital market which is supposed to be an avenue for sourcing long-term funds to finance long-term projects is not as developed as her foreign counterpart. It has therefore not been able to judiciously perform its primary obligation of meeting long-term capital needs of the deficit sectors, through efficient accumulation of capital or mobilization of funds from the surplus unit of the economy and effectively channel mobilized funds for more economic use. A critical study of both the real and service sector will elucidate this fact [4].

Institutional frameworks of the capital market to effectively carry out its core purpose of its establishment have to be put in place to ensure that the expectations of both the lenders and users of funds are adequately met to induce savings and optimal investment necessary to economic growth and development. Emenuga (1998), for instance believed that the stock market is illiquid and blamed the ownership structure in the Nigeria stock market. He concluded that the stock market is small and has few listed companies, low capitalization and low volume of transactions. Ariyo and Adelegan (2005), contend that the liberalization of the capital market has contributed to the growth of the market, but that it impact has not been felt at the macroeconomic level of the nation.

Every nation view economic growth and development to be the focus of their government as no nation wants to be behind in terms of development pace. This is why all policies including fiscal and monetary centres on resource allocation distribution aiming at improving the channeling process of gearing savings into investment. Since the capital market is the medium for long-term fund acquisition, therefore its activities and performance requires stringent study to enhance improvement and encourage or foster economic growth and development.

In view of the above, the paper seeks to examine the effect of capital market reforms on economic growth in Nigeria. The study will be useful to scholars of financial discipline, the government of this nation, participants or operators in the capital market and other stakeholders as it will provide policy recommendations on the basis of its findings. The study is limited to Nigeria and spans for a period 1981 to 2009. Section two provides the review of relevant literatures, section three deals with the methodology, section four presents the data analysis and interpretation of results and section five provides summary, conclusion and recommendations.

The Nigeria Capital Market Reforms: Financial reforms and attendant policy prescriptions are aged long phenomena. They represent the various transformations and policies adjustments and overhaul that are directed at the art, practice and activities of financial institutions and market overtime in response to nominal need for operational improvement and growth of both the institutions and economy as a whole. They could be internal or external in nature, reflecting critical comprehensive amendment, restructuring and/or additions to the existing body of laws, guidelines and policies [4]. In Nigeria, the ability of the financial sub-sector to play its role has been periodically punctured by its vulnerability to systematic distress and macro-economic volatility and policy fine tuning inevitability (Kama, 2006). Consequently, the financial reforms were focused on further liberalization of banking business; ensuring competition and safety of the system and proactively positioning their interrelation with the capital market to boost financial intermediation with the hope to serve as a catalyst to economic growth and development.

In many emerging markets, including Argentina, Brazil and Korea, financial reforms have also become prominent as banks strive to become more competitive and resilient to shocks as well as reposition their operations to cope with the challenges of the increasing globalized banking system. Starting in 1986, Nigeria's financial system began to be deregulated and by 1992, substantial changes had taken place.

Capital market reforms are predicted upon the need for reorientation and repositioning of existing status quo in order to attain an effective and efficient state. Okeke (2009) posits that reforms are deliberate actions by the government to fast track, jump start and consolidate specified sector of the economy to achieve desired objectives.

Also, financial reforms, according to Ebong (2006) are deliberate policy response to correct perceived or impending financial crises and subsequent failure. Reforms in the capital market are aimed at addressing issues such as government, risk management and operational inefficiencies. Like other emerging economies, Nigeria has been involved in financial reforms on a regular basis aimed at responding to the challenges posed by some factors and developments such as system crises, deregulation, globalization and technological innovations [5].

In Nigeria, financial sector reform was a component of the Structural Adjustment Programme (SAP) which kicked off in 1986. The introduction of the programme was on the heels of the rejection of IMF loan packaged with conditionality, a decision that rejected the consensus of a national debate. Some of the reforms created for the money market indirectly affected the capital market activities simultaneously. These include deregulation of interest rates, exchange rate, entry/exit into the banking business, establishment of the Nigeria Deposit Insurance Corporation (NDIC) strengthening the regulatory and supervisory institutions, upward review of capital adequacy, sectorial credit guidelines, capital market deregulation and the introduction of direct monetary policies instruments (Nnanna, Englama and Odoko, 2004). Some of the reforms put in place by the Nigerian Government within the period covers by this study according to Nnanna 2002 are examined below:

Establishment of the Nigeria Deposit Insurance Corporation (NDIC): Deposit insurance systems are largely established to protect the banking system against possible bank run (unrestricted demand for cash savers) that can cripple the financial intermediation process, disrupt the payment system and have severe macro-economic effects (Mass and Tally, 1990). It establishment was informed by economic circumstances under SAP, especially policies relating to banks shareholders support and the bitter experience of previous bank failures in Nigeria.

The NDIC was established by decree no 22 of 1988 and charged with the following responsibilities:

- Insuring all deposit liabilities of licensed banks and such other financial institutions operating in Nigeria so as to engineer confidence in financial transactions
- Giving assistance in the interest of depositors such as taking over the management of a distress bank or by merging a distress bank with a strong one.
- Assisting monetary authorities in the formulation and implementation of banking policies so as to ensure sound banking practice.

Bank Consolidation Programme in 2005: The two major elements of the reform agenda are the requirement for Nigerian banks to increase their shareholders funds to minimum of N25 billion by the end of December 2005 and consolidation through merger and acquisition. The consolidation of the Nigerian banking system started after the announcement on July 6, 2004 Central Bank of Nigeria's 13 point agenda of banking sector reforms. This exercise led the numbers of banks in Nigeria from 89 to 25 banks; now 24 banks after the merging of Stanbic and IBTC. This affected dealings in the stock market as banks raised their required minimum capital through the capital market by issuing new securities.

Pension Reform: Prior to the pension reform act in 2004 and the setting up of the National Pension Commission (NPC), the situation was such that:

- There were significant outstanding pension liabilities
- Most scheme in existence were under-funded
- Majority of workers in the private sector were not covered by any retirement benefit arrangements.
- Establishment Of Debt Management Office (DMO)
- This was established to provide a one stop shop for clearing all Nigerian government debts
- To transfer Nigeria's portfolio into an asset for growth and development
- To build a world class DMO of making Nigeria's debt sustainable by 2006.

Anti-Corruption Drive: This reform focused on reducing the negative impact of corruption on the nation's economy. The government set up Economic and Financial Crimes Commission (EFCC) to tackle financial and related crimes while the Independent Corrupt Practices and other related offences Commission (ICPC) was set up to fight corruption in public office. Also the due process office was set up to oversee and demand that standard process be followed in the execution of government activities. This is to ensure the elimination of financial sharp malpractices in the capital market of Nigeria.

Establishment of Second-Tier Securities Market (SSM): This was established in 1985. The establishment of this market was essentially a deliberate attempt to streamline the role of the Nigeria Stock Exchange and adapt the market to cater for more of the prevailing institutional arrangements.

Primarily, it was intended to assist small and medium sized indigenous enterprise to gain access to the resources at the capital market for expansion and modernization.

The Central Securities Clearing System (CSCS): The central securities clearing system rests on the concept which provides an integrated central depository, clearing (electronic entry transfer of shares from seller to buyer) and settlement (payment for bought securities) for all stock market transactions. It was incorporated as a subsidiary of the Nigeria Stock Exchange to obviate the inherent bottlenecks in the transaction process in the capital market and commenced operations in 1997. To this end, the CSCS is to implement a computerized Stock Exchange Management System (SEMS), which emphasizes immobilization of share certificates in the central depository and elimination of the bottlenecks between registrars and company executives in issuing new certificates to investors. All securities listed on the NSE and their registers of members are under the custody of CSCS limited. This arrangement enables all securities transactions on the NSE to be processed and concluded within five (5) working days in electronic book entry form. In carrying out this important function, the CSCS limited constantly updates the register of members of all listed companies and issues statement on their holdings. Such updated registers are made available to the registrars of companies from time to time.

Establishment of More Discount Houses: In order to facilitate the development of a secondary market for government dependence on the CBN in terms of trading debt instrument, three discount houses were licensed in 1992. In addition to intermediating funds among financial institutions, the discount houses were also expected to promote primary and secondary markets for government securities.

The Nigeria Investment Promotion Commission in 1995: This commission among other things is charged with the responsibility of encouraging, promoting and coordinating investment activities in Nigeria. It was empowered to initiate and support measures which would enhance the investment climate in Nigeria for both citizens and foreign investors. The commission is also empowered to register any enterprise in which foreign participation is permitted and to allow foreign enterprises to buy shares of any Nigerian enterprises in any convertible foreign currency. Prior to 1995, non-Nigerians were prevented from investing directly in any sector of the Nigerian economy until the promulgation of Nigerian Investment Commission Decree (now Act), except on the list set out in section 31; production of arms and ammunition, production of and dealing in narcotic drugs etc.

The Foreign Exchange (Monitoring and Miscellaneous Provision) Decree: (now Act) was also promulgated in 1995 inter alia allowing the free importation and exportation of foreign currencies up to the sum of $5000. Sums above that were to be declared upon importation or exportation on prescribed forms ''for reasons of statistics only''. More importantly, section 15 of the law allows the investment of foreign currencies and capital in enterprises or securities in Nigeria, if the foreign currency or capital is imported through an authorized dealer. The legislation goes a step further in liberalizing transactions in foreign exchange. Any person may repatriate funds in a foreign exchange from the country without further approval, provided the funds are purchased from an autonomous foreign exchange market.

The Privatization and Commercialization Act of 1988: The Act defined privatization as the relinquishment of part or all the equity and other interests held by the Federal Government or any of its agencies in enterprises whether wholly or partly owned by the Federal Government. From the definition above, three things are clear. First for privatization to take place there must be in existence public enterprises. Secondly, there is the reasoning that private ownership or control or management would be better than public ownership. And finally, Privatization is premised on the fact that there is part and parcel of a reform agenda to turn around these enterprises so that they can deliver goods and services more efficiently and effectively.

Introduction of Structural Adjustment Programme (SAP) in 1986: In July 1986, Nigeria embarked on the Structural Adjustment Programme (SAP). Its major objectives were to stimulate domestic production, diversify the economic base, fiscal and balance of payments viability, reduce the size of government expenditure as well as improve its efficiency and enhance the growth potentials of the economy.

SAP was an international designed and endorsed economic reform package, which suffered from low degree of ownership and participation and has widespread public resistance. It is a neo-liberal development strategy devised by international financial institutions to incorporate national economics into the global market. One of the main objectives of SAP was therefore to pursue deregulation and privatization leading to removal of subsidies.

Translating Economic Reforms to Economic Growth: The positive changes in the capital market activities has also become noticeable on the increase yearly in the proportion of market capitalisation on Nigeria's gross domestic product as shown below;

Growth of market capitalisation as a percentage of GDP

Year	Percentage
1999	9.39
2000	9.77
2001	12.07
2002	14.0
2003	18.9
2004	29.1
2005	25.1
2006	28.4

Source: Financial Standard, July 2007

One of the evidences that an economy is growing is that the capital market is growing and till now this is the Nigerian experience.

However, it is instructive to state that other criteria by which the performance of the capital market is measured include:

- The volume or number of securities listed.
- Efficiency of the operational procedure vis a vis the rate at which transactions are concluded at the floor of the exchange and information dissemination efficiency.
- How efficient are the regulations and controls at the stock exchange.
- Market capitalization or size of the market.
- All share price index
- Allocative efficiency in respect of how resources are channelled to the most efficient users.
- Pricing efficiency as it concerns the interplay of demand and supply
- The number of new issues and the size of the new issues to gross fixed capital formation.

Problems Confronting Capital Market: The ultimate aim of the present reforms in the financial system is to achieve economic growth, however if the benefits of the operations of the capital market will translate into the much more desired growth many of the problems confronting the market should be addressed. These problems include:

- The unstable macro-economic environment and policy instability
- Insider abuse in the market
- Use of the market to launder funds abroad resulting in illiquidity
- Inadequate regulation and supervision
- Disincentive to foreign capital inflow due to interference with the price determination mechanism that infringe on the transaction of a free market framework
- Exorbitant cost of raising funds through the capital market arising from high fees paid to operators, professionals and regulatory bodies as well as to advertising cum marketing agencies.

Other related issues are that there must be a reliable legal institution that protects investments, a relatively stable currency, policy consistency and predictability, regulation and controls should be effective because the problem of inefficient capital allocation which is common to banks are a result of imperfect information is not supposed to be allowed in the capital market and capital market operators and participants must scale up their skills and competencies from time to time.

In addition to the aforementioned support factors, there is the need for private sector control with less undue government interference. The government is expected though to provide a good political and business climate for capital market activities.

The Imperatives of Capital Market Operations in Nigeria's Business Environment: Considering the needed magnitude of growth in real resources and their allocation within an economy, financial markets are germane to the quest for growth not minding the claim that sometimes asset valuation may not adequately reflect the rate of return in investment in productive capacity [7]. The fact is that the capital market cannot be overlooked nor wished away by any nation that is serious about achieving economic growth. The failure of state directed credit to achieve economic growth makes it imperative for the capital market to take the lead.

Also the fact that bank financial investment is often not enough makes the capital market important considering the quantum of funds in dollar conversion of what is needed for development projects after the naira devaluation and the global competitiveness of foreign direct investment quest by developing countries around the world. Moreover, retained profits are no more sufficient for expansion in the face of the present information technology revolution. The situation has been further worsened with the endemic crisis in the banking industry.

The capital market thus among others help in financing the savings-investment gap both domestically and internationally as well as finance other activities that can result in economic growth. Ordinarily the need for long term finance makes the capital market relevant to our development drive. It is common knowledge that in Nigeria in the last few years as a consequence of the liberalisation, privatisation and re-capitalisation policies of the government that has swept across the telecommunication, energy, manufacturing, banking and insurance sub-sector, the capital market has played enviable roles in the attainment of the objectives of the government in pushing up the growth figures and enhanced human welfare coupled with the redistribution of income and benefits within the Nigerian business environment.

CONCLUSION

With the gradual shift from bank-dominated credit to capital market enhanced funds, it has become obvious that the capital market is key in achieving economic growth and development. Irrespective of the argument put forward by respected scholars who subscribe to bank finance over capital market finance in Nigeria, contemporary issues and reality has made us realise that the capital market cannot be wished away if truly Nigeria desires enviable economic growth.

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