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ANAYSIS OF INTEREST RATE SPREAD, FINANCIAL DEVELOPMENT AND FOREIGN CAPITAL INFLOW NEXUS IN NIGERIA

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ABSTRACT

The world has gone through various economic crises in the past century, and their effects have had varying implications on the economies of countries all over the world. In a bid to help stabilise economies all over the world, various measures have been put in place. Some of these measures include regulations and policies by the Bretton Woods institutions (World Bank and International Monetary Fund) and their agencies. The idea behind these measures is to ensure sustainable growth and development among member states and other countries of the world. Some of these policies include the privatization and liberalization policies of the Bretton Woods institutions as well as other policies bordering on such economic and social benefits for people all over the world. The Nigerian economy in our contemporary time can be described as passing through a rather 'volatile' phase with respect to interest rate, financial development and foreign capital inflow. Thus, this study investigated the impact of interest rate spread and financial development on foreign capital inflow in Nigeria. Several studies have been carried out using different methodologies, such as; co-integration equation, multivariate vector auto regressive (VAR) model and vector error correction technique. Each methodology used was in line with the objective of the research in question. However, to achieve its objective, this paper adopted the Classical Linear Regression Model. The results of the study showed that financial development has a positive impact on foreign capital inflow, while interest rate spread on the other hand, was also found to have a positive impact on foreign capital inflow. Other control variables such as market capitalization and treasury bills rate were also found to positively affect foreign capital inflow, while the all share index had a negative impact on foreign capital inflow. Some economists have opined that the Nigerian economy is currently going through a phase of slow economic growth. In order for large scale investments to be made within the country, there is a need for foreign participants to be attracted to the Nigerian economy and pull their resources, both financial and non-financial into the country (but, not without regulation). However, for these investors to have confidence to make investments in the Nigerian economy, there has to be a high degree of economic stability in the country. This can be supported by enacting and implementing policies that can enhance the quality of interest rates spread and financial development within the country. The policy implication of this study is that enhancing financial development through sound policies and adopting competitive interest rates, could increase the rate of foreign inflow into the economy. In view of this, it is also recommended that government policies should target interest rate competitiveness, financial and economic development as well as sustainability.

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INTRODUCTION

The world has gone through various economic crises in the past century, and their effects have had varying implications on the economies of countries all over the world. In a bid to help stabilise economies all over the world, various measures have been put in place. Some of these measures include regulations and policies by the Bretton Woods institutions (World Bank and International Monetary Fund) and their agencies. The idea behind these measures is to ensure sustainable growth and development among member states and other countries of the world. Some of these policies include the privatization and liberalization policies of the Bretton Woods institutions as well as other policies bordering on such economic and social benefits for people all over the world (Orji, Aza, Anthony-Orji, and Isaac, 2022).

The issue of foreign capital inflow came into play with the rising desire of many under-developed countries to break the chain of stagnancy in their economies and move to the league of developed or first world countries. These activities can be said to have started in the days of the colonial masters' rule. This is because the developed countries flocked to countries in Sub-Saharan Africa and Asia and offered them civilization for a 'price'. Many years later, some countries are still being held as economic slaves by the first world countries. This is in line with the saying 'all that glitters is not gold', as the terms of the grants and contributions given to them by these first world countries were not as rosy as they seemed during the planning stages.

Foreign capital inflow is more or less an umbrella name for all monetary inflows into a country. These inflows are made up of various components such as Foreign Portfolio Investment, Foreign Direct Investments, and Remittances amongst others. Inflow of funds like these were also used in western countries like London after the World War 2 (WWII). In those days, they were used to accelerate the growth rate of basic infrastructure and technology within the state (which had been destroyed during the war) and pave way for a robust production base in order to foster economic development. Just like other policies of its kind, a lot of factors tend to affect these compositions. These factors include the available market size in the receiving country, high government consumption, international remittances, agglomeration and huge national resource endowments amongst others. These inflows if effectively and efficiently managed by the Nigerian government can go a long way in ensuring that the country is economically stable and, in the long run, can lead to a high rate of economic growth and development (Orji, Ogbuabor, Nwosu, Anthony-Orji and Okpala, 2019).

The Nigerian economy in our contemporary time can be described as passing through a rather 'volatile' phase. For example, with the projected 2021 budget of N13.6 trillion which is higher by 26% from last year's budget (N13.6 trillion vs N10.8 trillion), bulk of the money to be used for funding the budget would be sourced through borrowed funds by the Federal Government. Specifically, there is increased borrowings, amid concern for high debt levels. New borrowings are 12% higher than 2020 levels, at N4.7 trillion. New borrowings are split into 50% each for domestic and foreign borrowings (NBS, 2021). The implication of this buttresses the rating of Nigeria as one of the greatest national debtors of our time. It might also pave the way for instability in various economic cycles, including interest rate spreads and financial development.