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CALMING THE TIDE: PRIVATE INVESTMENT AND MACROECONOMIC UNCERTAINTY IN NIGERIA

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ABSTRACT

This study is undertaken to determine the relative impacts of the uncertainty of macroeconomic variables on investment and make policy recommendations that may help dampen their fluctuations. In the study, generalized autoregressive conditional heteroscedasticity (GARCH) model was applied in the estimation of uncertainty of the macroeconomic variables. In the analysis of the data, econometric results were obtained from cointegration test and ordinary least squares. Thus, the study revealed the following: (1) existence of long run relationship between some of the macroeconomic variables and investment, (2) possibility of convergence of the variables from the short run to the long run with slow speed of adjustment and (3) the uncertainty of most of the macroeconomic variables impact negatively on investment in Nigeria. The study recommends the use of appropriate policy instruments that will bring about macroeconomic stability which provide conducive and enabling environment for private investment to thrive.

Keywords: Private Investment; Volatility; Inflation, Exchange rate; Economic Growth

JEL Classification: B22, E22, F41, G31, R42

INTRODUCTION

Theoretically and empirically, the concept of investment and uncertainty has attracted reasonable attention in macroeconomic literature. Investment is the most volatile of the major components of aggregate expenditure. After consumption, investment constitutes one of the most important and

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yet unstable part of total demand in every country, which is considered as one of the causes of cyclical fluctuations. Most of the relevant theories point to the instability of this variable on the one hand, and on the other hand, they emphasize the undeniable impact of this parameter on economic growth (Rexford, 2012; Leila et al. 2012 and World Bank, 2012). Dornbush et al. (1996) were of the view that investment spending is usually volatile, because it depends on multiple factors, and is responsible for much of the fluctuations of GDP over the business cycle. The instability of investment led Keynes, (1936) to conclude that the economy is inherently unstable, and there is need for government intervention to activate and regulate the saving and investment behavior of the society. The great depression of the 1930s left in its wake, the break-down of autarky and subsequent global financial liberalization. Demir, (2009) found that, in most developing countries, financial liberalization processes gradually led to sharp fluctuations in key macroeconomic indicators, over the years. NBS, (2004) asserts that Nigeria's macroeconomic indicators have been fluctuating since 1980. From early 1980s to the second half of the 1990s, annual inflation has averaged around 30 percent. Subsequently, average inflation came down to one –digit rate. However, since 2001, inflation is back in the two-digit domain, with an average of about 18 percent within 2000-2002. While, average inflation between 2004 and 2008 is about 10 percent.

When we take a cursory look at the performance of the Nigerian economy vis-à-vis other economies, we see some puzzling outcomes. For instance as presented in Table -1, available statistics reveal that averagely, interest rate, inflation rate , exchange rate and GDP growth volatilities are lesser in developed economies but more severe in emerging economies. Also, we see on the average, lower GDP growth rate and higher inflation rate among the emerging economies. As it were, when compared with some other emerging and developed countries, Nigeria's data show serious volatilities of some macroeconomic variables like exchange rate and inflation rate. Although, within the period under review, GDP growth rate and interest rate variability in Nigeria is lower than that of Chile, Brazil and South Africa, inflation rate in Nigeria, on the average is the fourth highest among the emerging countries with Hungary, Mexico and Columbia, taking the lead. That notwithstanding, among the emerging economies, Nigeria recorded some appreciable levels of GDP growth rate, coming second only to Poland, Mexico and South Korea which all grew around 4 per cent a year between 1997 to 2002 on the average. The statistics below therefore shows that as an emerging country, Nigeria' s macroeconomic environment (at least in terms of Inflation and exchange rates) is more volatile than say South Africa, Brazil and Chile. This further corroborates the words Batini that "emerging market economies like Nigeria face more volatile macroeconomic environment, and typically have weaker institutions that enjoy less credibility than their developed economies counterparts". It has also been observed that some aggregate macroeconomic variables in Nigeria such as real exchange rate (RER), government revenue and spending and terms of trade (TOT), were among the most volatile in the developing world between 1980-2002 (NBS, 2004). This has made the economy to be in a low growth trap, made up of low savings-investment equilibrium. Hence, our economy is still far below the minimum investment rate of about 30