THE RELATIONSHIP BETWEEN FINANCE AND DEVELOPMENT: TOWARDS NATIONAL DEVELOPMENT

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Abstract

The study assesses the relationship between finance and national development beyond 2020. It was discovered that, if financial security is sure for individual investors there will be increase in income this will also create happiness, satisfaction and self fulfillment to the individual investor .it reduces unemployment and social disorder among youths, promote enrolment in education as well as national development. In addition to increasing private income, economic growth also generate additional resources that can be used to improve social services. By generating additional resources for social services (such as education, health care, safe drinking water etc), unequal income distribution will be mitigated, hence social services are distributed equally across each community, thereby benefitting each individual. Concisely, the relationship between finance and development can be explained in three ways. Firstly, increase in average income leads to improvement in health and nutrition, secondly, it is believed that social outcome can only be improved by reducing income poverty, lastly, social outcome(education) can be improved with essential services such as education, health care and clean drinking water. It is recommended that government should encourage individual investors by making financial security sure.

Finance was originally part of economics, until recently finance became a separate subject of its own. Finance in itself is an academic discipline which is connected with the study of how funds are generated and expended in the modern day business. The role of finance manager is to keep accurate financial records, preparing reports, managing the firm's cash position, providing means of settling indebtedness, procuring additional fund externally. Recently other functions were added to the finance manager such as investment of funds, obtaining best mix of financing and valuation of the firm.

Economic development is the sustained, concerted actions of policy makers and communities that promote the standard of living and economic health of a specific area. Economic development can also be referred to as the quantitative and qualitative changes in the economy. Such actions can involve multiple areas including development of human capital, critical infrastructure, regional competitiveness, social inclusion, health, safety, literacy, and other initiatives. Economic development differs from economic growth. Whereas economic development is a policy intervention endeavor with aims of economic and social well-being of people, economic growth is a phenomenon of market productivity and rise in Gross domestic product (GDP).

The focus of this paper are to discuss the relationship of finance and national Development. The objectives of this study are to determine:

(1) The relevance of finance in an organization
(2) The significance of Economic Development
(3) The relationship of finance and development

Other parts of this paper are structured as follows: the relationship between finance and development and the conclusion of the study.

What is Finance?

Finance is a body of facts, principles and theories dealing with the raising and using of money by individuals, businesses, and governments. Finance is defined simply as Money, the management of money, and a scientific study of money. In essence finance is the hallmark of any business enterprise such as education.

Sources of Business Finance

The term sources of finance and investment may be used interchangeably. To clarify this it must be noted that a source of finance to an organization is also an investment to an investor. We are looking from the view point of the firm; therefore we are looking at sources of finance rather than investments in this aspect.

In general perspective, source of finance means the provision of fund in maintaining the organization goals. The various ways by which finance could be source include: Personal savings, subsidy, grant-in-aids, loans/borrowing, and overdraft facility,

court fines, royalty, rates and rents, taxes, Toll-fees, etc. Thus sources of finance are based in different angles namely: Long term, medium term and short-term. Their market value varies with current interest rates examples include debentures, preference shares, etc. Fixed Capital Investment, the investor deposits a sum of money, normally for a period of time, on which he receives interest. e.g. include commercial bank deposits, local authority loans, unquote government bonds, etc.

The major source of long-term fund includes: Ordinary shares, Preference shares and Long-term loan capital or debentures.

Medium-Term Capital: This means capital tied up for more than a year. Bank loans are an obvious source, usually it is related to the purchase of fixed assets, and can extend for as long as ten years. Overdrafts of any kind are given based on time frame on agreed limits.

Short term loans: Are credit facilities allowed to a customer for a period of one year. Short-term capital is used for such bridging purposes as mounting stocks in anticipating of seasonal demands. It may also be used for building up resources to invest in fixed assets at a later date.

By its very nature therefore, it is temporary finance and a useful tool for leveling out fluctuations in the required amount of working capital. Commercial banks are the first line of call through bank overdraft facilities with day-to-day interest (subject to a % base rate) on the outstanding balance. Loans for a definite period can also be arranged but with interest at a higher rate, over the full term. The amount borrowed basically depends upon the firm’s profit record, the collateral security offered and the cash-flow ability to repay the loan, with interest, on the agreed period.

Depreciation: Although not obvious at first sight, depreciation today is an important source of finance. All fixed assets (except land) tend to depreciate in real value and become obsolescent, thus, their provision has to be mindful for such depreciation annually out of the current profits.

However, depreciation is only a book entry not a payment of cash. When ascertaining cash flows from published figures, it is therefore usual to add back the amount charged for depreciation; basically it increases the firm’s cash flow.

For instance freehold building bought for ₦10,000 could be depreciated on a straight-line basis at ₦5,000 per annum over ten years reducing the book value to ₦5,000 at the end of that period. The current market value could by then be inflated to ₦14,000 thus (in money terms) giving an extra margin of ₦4,000 on which to raise finance. This ignores the quantitative aspects of rest terms as against money terms a problem that is dealt with in a different context.

Bills of Exchange: Bills of exchange are another source of finance. Usually it is self-liquidating over three months; these bills are, in effect short-term borrowing from merchant banks or financial institutions.

Trader's Credits: Is another accepted method for obtaining short-term funds, with the added advantage that no interest or dividend has to be paid. Every opportunity should be taken, therefore, to obtain maximum credit from suppliers; this has to be weighed, of course, in interest terms against any cash discounts offered from prompt payment. Suppliers of raw materials and services customarily offer credit facilities, payment to be made for example, one month after delivery.

Why Sources of Finance?
We source fund to
(a) Actualize the investment dream of an enterprise
(b) To create expansion path in business organization
(c) To embark on capital projects e.g. development of infrastructure
(d) Maintenance of economic standard
(e) To minimize risk concept in business

Debt Financing

Possible source of debt capital (borrowed fund) for the small scale business entrepreneur are commercial banks, vendors, equipment manufacturers and distributors, factors sales finance companies, insurance companies, private investors, small business investment corporations and the small business administration.

According to Okechukwu (2009), position of debt financing is very important in entrepreneurship business because of the lack of asset and fund, numerous factors hinders the source of debt capital such as:

a) The availability of external finance is crucial because those who set up business in deprived areas are less likely to be able to draw on internal funds for those in more developed areas.
b) Business in deprived areas tends to lack business experience including collateral and personal equity to access debt financing.
c) Business tends to be concentrated in sector subject to higher failure rates. They suffer from remoteness, small and localized markets and high crime rate.

Equity Financing

Equity financing is provided in a permanent nature as it is provided by the owner's of the enterprise.

Equity financing can come from various sources depending on the type of business entity. The equity financing on the type of business entity of a sole trader is usually sourced from personal savings and other sources as prescribed by the

entrepreneur. The equity financing of partnership business usually is being contributed by potential partners of the business. Actually equity financing are owner's capital investment in the business and other source known by the entrepreneur. It differs from other sources of financing of business entity. A shareholder of a public company that subscribe as an ordinary shareholder is a good example of equity capital investment because they are co-owners of the business essentially, reserve capital involves the long turn commitment of external equity to enable business not listed or listed in the stock exchange to grow and prosper. In becoming an equity partner, the venture capitalist will place more emphasis on realizing the final capital gain than regular cash flow. Typically the venture capitalist will also provide expertise, experience and contracts to help nurture the business.

Government Agencies Financing

The Nigerian small and medium enterprises investment and equity scheme (MEIES) initiative was set up by the banker's committee approved at the 24th meeting held on December 21, 1999. The initiative was in response to the Federal Government of Nigeria is concern and policy, for the promotion of small and medium enterprises (SME) business to cushion the unemployment problem and encourage rapid industrialization, sustainable economic development, poverty alleviation and employment creation.

The scheme, being a voluntary initiative requires that all financial institutions operating in Nigeria should set aside ten percent of their profit after tax for equity investment and the promotion of small and medium enterprises.

The ten percent profit after tax is set aside annually and is expected to be injected in the promotion of small and medium scale enterprises, serving as a banking contribution to the promotion of small and medium industry for the millennium goal of the federal government. The fund provided for this scheme is in form of equity finance to eligible businesses. The essence of this scheme is to reduce interest on loan and difficulties in securing loan from financial institution by the small and medium scale enterprises in Nigerian.

Finance Lease: A lease is a contract between the owner of an asset (lessor) and the user of the asset (lessee) granting the user the exclusive right to use the asset, for an agreed period in return for the payment of rent. This is different from hire purchase because there is no intention to transfer ownership of title to the user of the asset, the lease agreement only creates the right to use an asset for a definite period and at specified rent. The main advantage of leasing is the use of an asset without having to buy it. This conserves the entrepreneur funds. Leasing is usually popular when the cost of equipment is high. However, the lessee can elect to purchase the underlying asset at the expiration of the lease contract.

Financial Intermediary

Is a financial institution that connects surplus and deficit agents. The classic example of a financial intermediary is a bank that consolidates deposits and uses the funds to transform them into loans.

Through the process of financial intermediation, certain assets or liabilities are transformed into different assets or liabilities. As such, financial intermediaries channel funds from people who have extra money or surplus savings (savers) to those who do not have enough money to carry out a desired activity (borrowers).

A financial intermediary is typically an institution that facilitates the channeling of funds between lenders and borrowers indirectly. That is, savers (lenders) give funds to an intermediary institution (such as a bank), and that institution gives those funds to spenders (borrowers). This may be in the form of loans or mortgages. Alternatively, they may lend the money directly via the financial markets, which is known as financial disintermediation.

In the context of climate finance and development, financial intermediaries generally refer to private sector intermediaries, such as banks, private equity, venture capital funds, leasing companies, insurance and pension funds, and micro-credit providers. Increasingly, international financial institutions provide funding via companies in the financial sector, rather than directly financing projects.

Functions performed by Financial Intermediaries

Financial intermediaries provide three major functions: namely creditors (finance) risk transformation and convenience denomination,

1. Creditors (finance) provide a line of credit to qualified clients and collect the premiums of debt instruments such as loans for financing homes, education, auto, credit cards, small businesses, and personal needs. Converting short-term liabilities to long term assets (banks deal with large number of lenders and borrowers, and reconcile their conflicting needs).
2. Risk transformation Converting risky investments into relatively risk-free ones. (lending to multiple borrowers to spread the risk).
3. Convenience denomination Matching small deposits with large loans and large deposits with small loans.

Advantages and disadvantages of financial intermediaries

There are two essential advantages from using financial intermediaries:

1. Cost advantage over direct lending/borrowing
2. Market failure protection the conflicting needs of lenders and borrowers are reconciled, preventing market failure

The cost advantages of using financial intermediaries include:

1. Reconciling conflicting preferences of lenders and borrowers.
2. Risk aversion intermediaries help spread out and decrease the risks.
3. Economies of scale using financial intermediaries reduces the costs of lending and borrowing.
4. Economies of scope intermediaries concentrate on the demands of the lenders and borrowers and are able to enhance their products and services (use same inputs to produce different outputs).

Various disadvantages have also been noted in the context of climate finance and development Finance institutions. These include a lack of transparency, inadequate attention to social and environmental concerns, and a failure to link directly to proven developmental impacts.

Types of Financial Intermediaries

Financial intermediaries include:

- Banks
- Building societies
- Credit unions
- Financial advisers or brokers
- Insurance companies
- Collective investment schemes
- Pension funds

Economic Development

Finance facilitate economic development, is a term that economists, politicians, and others have used frequently in the 20th century. The concept, however, has been in existence in the West for centuries. Modernization, Westernisation, and especially Industrialisation are other terms people have used while discussing economic development. Economic development has a direct relationship with the environment. Alongside education; Development is brought about by education in the short-run in the long-run, education increases quantitatively and qualitatively through development.
Although nobody is certain when the concept originated, most people agree that development is closely bound up with the evolution of capitalism and the demise of feudalism.

Mansell and When (1998), also stated that economic development has been understood since the World War II to involve economic growth, namely the increases in per capita income, and (if currently absent) the attainment of a standard of living equivalent to that of industrialized countries. Economic development can also be considered as a static theory that documents the state of an economy at a certain time. According to Schumpeter (2003), the changes in this equilibrium state to document in economic theory can only be caused by intervening factors coming from the outside.

Growth and Development

Dependency theorists argue that poor countries have sometimes experienced economic growth with little or no economic development initiatives; for instance, in cases where they have functioned mainly as resource-providers to wealthy industrialized countries. There is an opposing argument, however, that growth causes development because some of the increase in income gets spent on human development such as education and health.

In addition to increasing private incomes, economic growth also generate additional resources that can be used to improve social services (such as healthcare, safe drinking water, etc.). By generating additional resources for social services, unequal income distribution will be mitigated as such social services are distributed equally or evenly across each community, thereby benefiting each individual. Concisely, the relationship between human development and economic development can be explained in three ways. First, increase in average income leads to improvement in health and nutrition (known as Capability Expansion through Economic Growth). Second, it is believed that social outcomes can only be improved by reducing income poverty (known as Capability Expansion through Poverty Reduction). Lastly, social outcomes can also be improved with essential services such as education, healthcare, and clean drinking water (known as Capability Expansion through Social Services).

Yet others believe that a number of basic building blocks need to be in place for growth and development to take place. For instance, some economists believe that a fundamental first step toward development and growth is to address property rights issues, otherwise only a small part of the economic sector will be able to participate in growth. That is, without inclusive property rights in the equation, the informal sector will remain outside the mainstream economy, excluded and without the same opportunities for study.

The Relationship between Finance and Economic Development

Economist Jayati Ghosh (2013), stated that it is necessary to make financial market in developing country more resilient by providing a variety of financial institutions. This could also add to financial security for small-scale producers.
Economic growth and development is two way relationship. The first chain consist of economic growth benefitting human development, since economic growth is likely to lead families and individuals to use their heightened income to increase expenditures, which in turn further human development. At the same time, with the increased consumption and spending, health, education, and infrastructure system all contribute to economic growth.

In view of Shaw (2004), competitiveness is the driving factor for successful economic development in government and industry. By addressing technology directly,

to meet customer's needs, competitiveness was fostered in the surrounding environment and resulted in greater economic performance and sustained growth.

Conclusion

If financial security is sure for small -scale enterprise, there will be increase in household income. This may further create happiness ,satisfaction and self fulfillment to the individual investors thus, removing individuals from psychological depression ,worries and sense of rejection by the society. As a result of having access to finance for investments, individuals investors are more likely to have better economic conditions and be able to afford most of the essential needs of the family and perhaps to invest more funds into their trades as well as education for future growth as found in the result of enterprise assets acquired which led to better living standard which will facilitate economic development, since economic development has a direct relationship with the environment, with the increased consumption and spending, health, education and infrastructure system and contribute to national growth.

Recommendations

Haven considered the place of finance in national development especially in Nigeria, the following recommendations should be put in place;

- government should encourage individual investors
- financial security must be guaranteed
- free interest loan should be provided for low income earners.
- Where interest rates are charged, they should reflect current market values.

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