ASSESSING ECONOMIC FREEDOM, CAPITAL FLOWS AND ECONOMIC TRANSFORMATION IN NIGERIA

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Abstract

This paper contends that the challenges facing most African countries are how to attract increased Foreign Direct Investment (FDI). The purpose of the study is to examine the levels of business freedom in Nigeria, because business freedom can enable market incentives to operate effectively to the benefit of Foreign Direct Investment. Using descriptive and historical methods of research, the study observed that Nigeria ranked 33 among the worst performer since 1995 according to Heritage Foundation index of Economic Freedom in Africa. The paper concludes that robust capital flows is the key to economic transformation goals; and suggest that it is Nigeria's interest to continue on the path of great economic freedom, thereby exploiting the wider commercial benefit of globalisation. Therefore, the paper recommends that Nigerian should open-up more of its economy in the form of free market, reduce custom tariff, respect for property rights and rule law to attract private external investment.

Introduction

The past two decades have seen a process of almost continuous reform in public management in developing African countries and renegotiation of traditional relationship between state, economy and society. These changes have been expressed through market liberalization and deregulation policies in order to tune in better with the global economy and to attract private external investment. Economic liberties, in the form of free market and respect for property rights and the rule of law are more conducive to economic growth and Foreign Direct Investment.

The goals of capital flow and economic transformation in Nigeria are contingent on higher inwards direct investment. How to achieve that is the problem. The challenges facing most, if not all African countries are how to attract increased Foreign Direct Investment (FDI) i.e. money allocated to investment in risky Securities or speculative investment activities and reduce their heavy reliance of external aid.

According to World Bank, (2004) in recent years, official flows to the Sub-Saharan Africa have remained stagnant, at a low level, therefore, only foreign investment as well as other private capital flows can fill the current investment gap across the continent.

Defining Economic Freedom

The 2003 Economic Freedom of the World report compiled by the United State based Cato institute used five main criteria to measure the degree of economic freedom within a country, Moin Siddigi (2004:12). These are:

1. The size of government measured by public spending and state owned enterprises, relative to gross domestic product (GDP) and tax rates. The lower the taxation burden, the higher the country's score.
2. Freedom of trade and cross-border capital flows, assessed by the extent of import barrier/quotas, the level of import tariffs and abolition of capital controls. An open-economy that enables people and business to trade with overseas partners and move money in/out of the country promptly enjoy higher ratings.
3. Legal political structure by the degree of judicial independence, security of property rights and the degree of military influence in the political process. Military intervention in civil administration and poor legal systems hinder growth.
4. Access to sound money-measured by annual increases in consumer price inflation and money-supply growth as well as the freedom to hold foreign-currency banks account at home and abroad.
5. The state regulation of credit, business and labour. The first assesses whether banks are nationalised or privately owned. Whether foreign banks can serve local markets, and whether bank lending and interest rates are state controlled.

The second is business regulations – the degree of red tape affecting registration of new businesses and whether there are 'irregular payments' to officials, linked with business or import permits. The third is labour market regulations, i.e state controls, over hiring firing an minimum wage laws. Businesses prefer 'flexible' labour markets conditions where manpower costs are much lower compared with heavily-regulated markets.

The Institute's 2003 Economic Freedom of the World report, indicates that some African States – namely Mauritius, Botswana and South Africa are now boasting the same levels of business freedom as in matured economies like Germany, Japan, Norway, South Korea, Sweden and Taiwan, Moin Siddigi (2004:12). In similar case, index of Economic Freedom, co-published annually by the Heritage Foundation and the Wall Street Journal, ranks 155 countries (42 of them African) uses more detailed sits of economic variables, Anne Krueger (2004:12). They include:

1. The fiscal burden of government – public debts as a percentage of GDP, the top rate of income tax level upon the 'average' citizen and the top rate co-operation tax.
2. State participation in the economy, measured by the percentage of GDP contributed by monopolies and public bodies.
3. Trade openness-average tariff rates and extent of non-tariff barriers.

4. Monetary policy – the average inflation over a 10-year period and interest rates.
5. Capital flows and the hospitality of a country's Foreign Direct Investment regime – whether it permits majority foreign ownership of local companies and land, as well as equal treatment to domestic foreign investors in terms of fiscal incentives and taxation.
6. Governance issues – Corruption within the bureaucracy and red tape, i.e. whether regulations increase overall business costs.
7. Wages and price flexibility of labour marked (minimum, wage law) price controls and state subsidies.
8. The extend of formal (or black) marked activities – smuggling, trade in goods/services outside official channels and piracy of intellectual properly.
9. Banking/Finance – the number of nationalised banks and the degree of the States control over credit allocation.
10. The existence of a strong/independent judicial system – ensuring fair dispute settlement mechanism and respecting property right.

Review of Literature and Conceptual Framework

According to Moin Siddigi, (2005:12), Regional integration is seen as a means of promoting increased trade between member countries and securing economies of scale, as well as achieving industrialisation, thereby enabling African manufacturers to compete in competitive global markets. The author observed that successful regional integration is underpinned by three main criteria – reductions in trade costs (reflecting improved customs procedures, and covering non-trade invisible issues such as investment, services and labour. The author asserted an expanding invisible trade can, too, enhance member-countries' economic and national incomes.

The author noted that a surge in regionalism offers tangible benefits for African countries. He argued that enlarged markets facilitated by regional trade arrangements (RTA) encourage domestic competitor, larger production scales and greater specialisation, all of which underpin productivity and growth. RTA improves the foreign investments climate by creating wider selling opportunities across regional markets and increase Africa's collective bargaining power in international trade negotiations.

The author concluded that making regional trade integration work Africa has yet to fully develop intra-regional trade on a par with other regions such as North America, Western Europe.

According to James W. Watson, (1990), International Expansion is logical development for most growing businesses, but like all growth, needs to be carefully planned and controlled to be most effective. The author asserted that a business considering going international need to plan very carefully its approach, whether it chooses the franchise route or not. It is vital that its home business be soundly structured and mature, before looking overseas, regardless of how tempting it may appear. The author observed that there are major cultural differences, even across relatively short distances. For example, what is used as a general product description in the UK may only be sold by licensed pharmacies in Scandinavia. He added that attitudes to products and indeed to business ethics themselves have to be closely examined for international growth to be successful.

Brian A. Smith (1999), opined that the success of the franchise in the foreign market will depend not only on the development for the pilot operation and a team of supporting staff, but also building relationships between the franchiser and its accounts, lawyers and banks. The author asserted that all these professional advisers will be able to give the franchiser valuable information outside their own immediate area of activity.

The author argued that preparing a franchise for a foreign market requires careful preparation and planning. It requires a clear understanding of the market and environment in which the franchise will operate. He said its success depends on recognising the needs of the franchise and on continuous communication wherever these franchises are looked and whatever their language. The author concluded that although franchiser may be thinking internationally, it should be remembered that success in a foreign market depends on local knowledge and entails local action. Mark Abel (1993:46) observed that another route toward internationalisation is the acquisition of an existing network in the target territory. He asserted that this may be by way of a corporate acquisition or the acquisition of the rights to exploit a territory from an existing sub-franchiser or developer. The main problem in either case is locating a suitable target. The author said, this can be tackled by the use of contracts within the industry, published information and financial intermediaries such as merchant bankers, accountants, lawyers, etc. The author said that in some countries, however, there may be strong commercial and cultural tendencies against acquisitions especially by foreigners – Japan is a good example of this. This author concluded therefore, it is important for international expansion, to ensure that a full team of competent advisers is recruited, namely, a banker, lawyers (a local attorney from the franchisers own jurisdiction.

W. Seabrook (1998) tried to differentiate between globalisation and internationalisation. He argued that internationalisation is a more harmonious less violent version of promoting the image of a universal market. The other version of integration requires that only the powerless unite and that the disadvantaged combine in order to resist and make a common cause against what William Mans referred to as “the iron” rule of the world market.

Whichever way one wants to look at internationalisation, it entails the going beyond the border of anyone country to plan efficient production and distribution of goods and services, thus, it is at very core of economic globalisation. Internationalisation is spurred by a number of factors, which include:

1. improvement in transportation and communication, resulting in lower shipping costs and more feasible international trade.
2. the lowering of trade barriers designed to protect inefficient high costs of domestic manufacture goods caused by consumer's desire for low cost high quality products, and
3. firms wish to shift production to whenever costs are lowest. This is because a firm which operations are restricted to one country cannot compete unless cost in its home country happens to be low.

The study of internationalisation of business requires an understanding of the competitive forces of operating in the world market. These forces are concerned with inflationary trends and their monetary fiscal and wage policy determinations, productivity trends, wages and profits ratio, capital overhead, transportation costs, factors affecting investments climate, culture and other related variables.

Okelola (2000) noted that liberalisation increases the number of firms in an industry. This affect an increased in supply of goods sold and services rendered. The author said with demand remaining constant or at worst increasing at a lower rate (relative to supply) prices fall. The increase in business firms operating in the industry makes competition inevitable and consumers begin to consume higher quality commodities. Upon the liberalisation of an industry also rest a very high possibility of increased employment opportunities.

Obaseki (2000) observed that Globalisation is two main types. The types are: (a) Trade and Investment Integration and (b) Financial Integration. Globalisations of the World's goods are services through trade liberalisation and removal of all kinds of controls preceded financial market integration. The removal of barriers to worldwide trade by countries in the quest to operate within the framework of the multilateral trading system was a major impetus for the acceleration of global trade. The author noted that integration in global trade was followed and facilitated by foreign direct investment flows between countries that were involved in trade relations. The great multinational corporations, the original custodians of international monopoly capital, were the channels through which both international trade and Foreign Direct Investment (FDI) flows were made.

According to the author, the Foreign Direct Investment flows facilitate the growth in small companies, world trade, and global output by increasing the international mobility of capital and ensuring efficient use of technological and resources production process. This is the direction in which all companies are headed as the advantage of doing business anywhere; anything through any medium is possible for the entrepreneur and small companies as well. Information is power and as more information becomes available to companies through the global telecommunications system, they are empowered as never before.

The most re-occurent theme in this review of literature and theoretical framework is that economic liberties is the trend in the present external economic relations that no nation can ignore; it msut develop economically and otherwise. Globalisation has been derived from the globe and it connotes a world without national borders with particular reference to commerce which is the closer interaction between national economies through trade, investment and capital flows, is made possible by technological development and advancement in communication. This has increased global welfare and transformed the world into a global village. The big question is how far, has Nigeria faired in business economic freedom? The rest of this paper will examine this question.

The Purpose of the Study

The vast majority of Africa's 53 member-countries over the past decade have opened up their respective economies of international trade and inward foreign direct investment FDI – Economic Freedom in the form of free markets and respect for property rights and the rule of law are more conducive to economic and Foreign Direct Investment. The purpose of this study is therefore to examine the levels of business freedom in Nigeria, because business freedom can enable market incentives to operate more effectively to the benefit of Foreign Direct Investment (FDI).

Method and Procedure

This study is essentially descriptive and historical one. It is documentary and content analysis methodology. Materials were obtained from books and journals. The data were collected and tabulated into composite tables. The tables were clearly and honestly explained.

Data Presentation and Discussion

The above ten factors indicated in introduction by Heritage Foundation are rated from one to five, with one representing the best score and five being the worst. Scores are then average to produce the overall index score for economic liberalisation. Countries are classified by the foundation as being Free, Mostly-free, Mostly-unfree and repressed.

African Ranking

Africa falls into three categories (see table I). Nine countries are rated as mostly-free (scoring 2-2.99 points). In terms of the regional economic freedom index 1995 and 2004, Rwanda, Mozambique, Mauritania, Botswana, Senegal, Cape Verde, Burkina Faso, Chad, Madagascar, Ethiopia, Tanzania and Uganda all features in the list of most improved countries, on a level with several "old"

European Union Countries-Germany, Italy, Spain, Netherlands and Belgium on the other end of the spectrum – Nigeria, Niger, Mauritius, Zambia, Zimbabwe, Gabon, Namibia and Cameroon feature among the worst performers since 1995, according to Heritage Foundations findings.

However, 31 African nations are still ranked mostly-unfree with scores of 3-3.99, similar to China, Russia, India, Malaysia and Turkey. And two – namely Zimbabwe and Libya, are among the world's least-free and rightly repressed economies (scoring above four points).

Table I: Index of Economic Freedom in Africa

COUNTRY MOST FREE	SCORE	% CHANGE 1995-2004	GLOBAL RANKING 2000-20004	AFRICAN RANKING
Botswana	2.55	25.6	71 39	1
Uganda	2.70	13.0	74 48	2
South Africa	2.79	10.5	61 53	3
Copeverde	2.86	20.5	122 60	4
Morocco	2.93	3.3	49 66	5
Tunisia	2.94	1.1	74 67	6
Mauritania	2.94	25.1	127 67	6
Namibia	2.96	-5.7	61 70	7
Mauritius	2.99	-11.6	58 71	8
MOSTLY UNFREE				
Senegal	3.00	21.3	81 72	9
Madagascar	3.14	16.0	90 86	10
Swaziland	3.18	-0.6	74 89	11
Catedivoire	3.18	7.3	108 89	11
Djibouti	3.23	1.6	100 92	12
Guinea	3.24	1.5	84 93	13
Kenya	3.26	5.6	81 94	14
Mozambique	3.28	25.3	127 95	15
Egypt	3.28	11.0	Na 95	15
Burkina Faso	3.28	17.0	100 95	15
Tanzania	3.29	13.2	100 98	16
Algeria	3.31	10.0	108 100	17
Ethiopia	3.33	14.6	110 101	18
Mali	3.34	-5.4	102	19
Rwanda	3.36	27.0	139 103	20
Central Africa Republic	3.38	-2.1	Na 105	21
Ghana	3.40	4.0	84 109	22
Gabon	3.43	-7.5	84 111	23
Niger	3.43	-19.3	127 111	23
Benin	3.44	2.5	61 113	24
Malawi	3.46	7.5	120 114	25
Lesotho	3.50	7.4	115 118	26
Zambia	3.50	-11.1	61 118	27
Chad	3.54	16.7	127 124	28
Gambia	3.54	0.3	100 124	28
Cameroon	3.63	-3.4	100 127	29
Equatorial Guinea	3.69	13.4	144 130	30
Toto	3.73	10.0	127 134	31

Sierra Leone	3.73	4.3	127 134	31
Guinea Bisau	3.90	13.0	148 139	32
Nigeria	3.95	-15.1	94 142	33
REPRESSED				
Zimbabwe	4.54	-8.3	136 153	34
Libya	4.55	8.0	Na 154	35

Source: The Heritage Foundation/Wall Street Journal, Index of Economic Freedom (2004) in African Review of Business and Technology Pp.12-14

Nigerian Ranking

Nigeria ranking 33 among the worst performer since 1995 according to the Heritage Foundation is a significant revelation (see table I). The three man barriers to attracting increase in capital flows are: deficient public utilities, especially erratic power supply, unpredictable business environment, including insecure property rights, varioting, kidnapping, contract enforcement difficulties and corruption; and limited access to much needed capital (private-equity funds).

Economic liberalisation in the form of free market and respect for property rights and the rule of law, are more conducive to economic growth and Foreign Direct Investment (FDI). According to World Bank African Review (2004) regulatory burdens such lengthy and costly business procedures represent further impediments. In Nigeria, contract enforcement takes about 1,000 days compared to just 27 days in Tunisia according to the World Bank doing business report. In addition, small business enterpreneur lack skill and confidence to make effective use of domestic commercial bank while the banks generally lack the expertise to assess in meeting the credit needs of the Small Business Enterpreneur.

IMF urges improvement in public administration, legal/judicial systems, and, more generally in the enforcement of the rule of law. IMF research shows that annual GDP growth in sub-Saharan Africa countries could be two percent higher if the quality of their institutions were improved to the average of other regions. The government has ultimate responsibility for economic stability and infrastructure investments. Private sector growth cannot take off in climates of stagflation (Plunging output and Hyperinflation, coupled with depleting physical infrastructure.

In some countries, red tape remains a business impediment according to IMF, including complex sets of regulations, multi regulatory agencies, delays in clearing goods through customs, high market-entry transaction costs, and unreliable commercial court system. Foreign investors are often easy targets for extortion, bribery and other corruptive acts.

According to World Bank Study, (2004:13) there is a correlation between economic liberalisation and prosperity/self-sufficiency. Freer nation on average, enjoy superior growth and attract more Foreign Director Investment

(FDI), than reprosted economies. Business – friendly policies facilitate trade and promote entrepreneurial activity. This generates wealth-creation, creates jobs and raises living standards. But successful businesses require effective public-private partnership.

Conclusion

Robust capital flows is the key to economic transformation goals. Freedom from government interference can enable market incentives to operate more effectively, to the benefit of all in a competitive environment. In most cases, well regulated markets provide the right environments for efficient allocation of scare resources. Therefore, it is in Nigeria's interest to continue on the path of greater economic freedom, thereby exploiting the wider commercial benefits of globalisation.

Recommendations

For Nigeria to exploit the wider benefits of globalisation, Nigeria should open-up more of its economy in the form of free market reduce tariff, respect for property rights and the rule of law to attract private external investment.

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