Balance of payments and policies that affects its positioning in Nigeria

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1 November 2016

TOPIC: BALANCE OF PAYMENTS AND POLICIES THAT AFFECTS ITS POSITIONING IN NIGERIAN ECONOMY

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Abstract

This study examines balance of payments (BOP) and policies that affects its position in Nigerian economy. The tariff, non- tariff and exchange rate policies were used as policies that affects the BOP. Various Proxies were used to explain the effect of these policies on the BOP. These includes; the indirect tax as a proxy for tariff policies, the money supply, export and interest rate as a proxy for non- tariff policies, and the exchange rate. This study employs the ordinary least square (OLS) methods of estimation and the heteroscedasticity and autocorrelation covariance (HAC) in order to avoid spurious regression results. The E-views 6.0 was employed in the regression analysis. In executing this study, the ADF (augumented dickey fuller) test and the Unit Root Test was carried out to test the stationarity of the variables. The result shows that the indirect tax, export and exchange rate satisfy the economic apriori expectation while the interest rate and money supply negates the apriori expectation. Using the t-test, it is revealed that only three (3) variables are significant in the explanation of the dependent variable (BOP) while the remaining two variables are insignificant. Recommendations are made to ensure that the balance of payments disequilibrium is resolved.

KEY WORDS: BALANCE OF PAYMENTS, TARIFF AND NON-TARIFF POLICIES, EXCHANGE RATE POLICIES.

1.0 INTRODUCTION

The increase in Nigerian's growth performance is attributed local production and consumption activities as well as foreign transactions in goods and services. It has been acknowledged that foreign trade is 'an engine of growth and development'. In an economy that is characterized by macroeconomic stability and favourable investment climate, attractive trade policies would encourage foreign investment, technological advancement and exports which will in turn attract massive inflow of foreign exchange. In order for a country to make international payments, foreign exchange is needed by the country involved. This foreign exchange is obtained in a variety of transactions namely; exports of goods and services, capital inflows from abroad, unilateral transfers receipt and gold exports. Foreign exchange obtained by this means is needed for paying for imports of goods and services, to finance capital outflows, unilateral transfers or transfer payments and gold imports. International monetary problem arises out of the relationship between the sources and uses of foreign exchange and their inter-connection with domestic, economic and monetary affairs. The starting point of the analysis of these problems is the BALANCE OF PAYMENTS (BOP).

1.1 STATEMENT OF PROBLEM

A common thought that has occupied the mind of economists and monetary authorities for decade is the case of disequilibrium in the balance of payments in Nigeria. The role Balance of Payments position play in the economy of any nation cannot be over emphasized and Nigeria is no exception. Every government regime desires a right balance of payments position. This has inspired every major turn of policy; setting of bank rates, changes in taxes, regulation of incomes, the restructuring of industry, introduction of export rebates, control of money supply and level of local government expenditure (Imoisi, 2012). The Current Account Deficit (CAD) in the balance of payments has been a problem for Nigeria because it adds to the already large indebtedness of Nigeria to the rest of the world and has become a barrier to the realization of government objectives. BOP disequilibrium is a reflection of disequilibrium in the money market (IMF, 2000). Monetary disequilibrium produces adverse effect on the aggregate expenditure for goods and services (absorption) in the sense that, if the public has an excess supply of money it gets rid of it by passing its excess cash balance to foreign countries in exchange for goods and services. If the public desires to keep more money than it has in stock, it achieves it by reducing absorption and ultimately passes goods and services on in foreign countries in exchange for money.

The disequilibrium in the country's balance of payments account have generated questions concerning the causes, its impact on social progress and what policies to adopt to achieve favourable balance of payments position. We recognize the fact that quite a lot of research has been carried out on the Nigerian BOP; Aniekan (2013), attributed the disequilibrium to disturbances in monetary variable, African research(2011),stated that improper allocation and the misuse of domestic credit, fiscal indiscipline and lack of appropriate expenditure control policies due to centralization of power in the hands of the government, Imosi (2012), attributed the disequilibrium in the balance of payments to the insignificant inflation rate, International Journal of Economics and Finance (2013), attributed the disequilibrium to the instability in the exchange rate. Most of these studies have been at the theoretical level, while others addressed the consequences of BOP deficit. None of these studies empirically modeled the tariff, non-tariff and exchange rate policies affecting BOP position. Effort will be made in this study to cover the gap.

1.3 LITERATURE REVIEW

Selected authors have been reviewed here to see their views concerning balance of payments and policies that affects its position in an economy.

Imosi (2012), carried out a multiple regression analysis using the ordinary least square method for linear and non- linear form. The log-linear form gave a better result and thus was adopted to ascertain the impact on this independent variable (exchange rate, inflation rate and interest rate) on dependent variable (balance of payments). The result shows that the independent variables appeared with the correct sign and thus, conforms to the economic theory but the relationship between balance of payments and inflation rate was not significant.

Odii & Onyemauwa (2010) analyzed how balance of payments management in Nigeria can be improved through agricultural earnings. The result of multiple regressions carried out indicates that exchange rates, interest rate, time factor, and foreign reserve are directly related to balance of payments while imports and exports were inversely related to the balance of payments.

Oladipupo, A. O (2011) investigates the impact of exchange rate on the Nigeria external sector using the **ordinary least square** (ols) method of estimation from periods 1970 - 2008. From his result, the exchange rate has a significant impact on the balance of payment position. The exchange rate position can actually lead to improved balance of payments positions if fiscal discipline is imposed. He also stated that improper allocation and misuse of domestic credit, fiscal indiscipline and lack of appropriate expenditure control policies due to centralization of power in government are some of the causes of persistent balance of payment deficits in Nigeria.

Imoisi (2013) examined the relationship between the Balance of Payments position in Nigeria and monetary policy adopted in the country. The research was conducted using an Ordinary Least Squares (OLS) technique of multiple regression models using statistical time series data from 1980-2010. The estimated result shows a positive relationship between the dependent variable (Balance of Payments) and the Independent variables (Money Supply, Exchange Rate and Interest Rate). Money Supply and Interest Rate had significant relationship with Balance of Payments, whereas Exchange Rate was not statistically significant.

1.4 RESEARCH METHODOLOGY

This work effectively captures factors that affect the balance of payment position in Nigeria. The OLS Method with the ADF Test was adopted for the unit root.

The framework of this study is based on the the modification of the work of Imoisi (2013) and Oladipupo (2011) and is specified thus;

Bop = $\boldsymbol{\beta 1 + \beta 2\ ind + \beta 3\ exp + \beta 4\ int\ rate + \beta 5\ m2 + \beta 6\ ex\ rate + \mu}$**………………………… *(1)***

From the modified model above, the indirect tax (ind) is used as a proxy for tariff policies which is imposed by the government of a country. The export (exp), money supply (m2) and the interest rate (int rate) is a proxy for the non-tariff policies. The exchange rate (ex rate) policy is a proxy of the exchange rate policy.

1.5 ECONOMIC A PRIORI EXPECTATION

This shows whether or not the explanatory variables conform to the postulations of economic theory in terms of their signs and magnitudes. According to economic theory, indirect tax, export and money supply has a positive relationship with balance of payments position while interest rate and exchange rate has a negative relationship with balance of payments position. If the estimates do not conform to what we have above then they must be rejected unless there are strong reason that will lead to their acceptance.

1.6 DATA SOURCES AND TYPES

Secondary Time Series data from 1981-2010 collected from the World Bank, Central Bank of Nigeria (CBN) 2010 statistical bulletin, will be used in this study.

1.7 THE RESULT

The result of the unit root test shows that the dependent and independent variable except for money supply is stationary at first difference. As a result, there is no need to perform co-integration test to check for long run relationship between the variables of the model.

The estimated result is shown below:

Result

Dependent Variable: BOP

Method: Least Squares

Date: 02/11/14 Time: 11:06

Sample: 1981 2010

Included observations: 30

White Heteroskedasticity-Consistent Standard Errors & Covariance

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-144290.2	118701.8	-1.215568	0.2360
IND	1.973183	2.203557	0.895453	0.3794
EXPORT	1.034025	0.095970	10.77442	0.0000
INTR	5641.571	9914.174	0.569041	0.5746
M2	-1.026292	0.137671	-7.454681	0.0000
ER	-12070.13	4498.384	-2.683214	0.0130

R-squared	0.814427	Mean dependent var	20871.55
Adjusted R-squared	0.775767	S.D. dependent var	1052452.
S.E. of regression	498370.8	Akaike info criterion	29.25293
Sum squared resid	5.96E+12	Schwarz criterion	29.53317
Log likelihood	-432.7940	Hannan-Quinn criter.	29.34258
F-statistic	21.06590	Durbin-Watson stat	2.143511
Prob(F-statistic)	0.000000		

The R2 shows that the explanatory variables employed explains 81.4% of the variations in the balance of payments position in Nigeria for the period under study. Export, Money Supply and Exchange Rate has a significant impact on growth given that it is correctly signed with a probability value of 0.0000 and 0.0130. Indirect Tax and Interest Rate on the other hand does not have significant impact on the variations in the balance of payments position in Nigeria given a probability value of 0.3794 and 0.5746.

The F-statistic of 21.06590 shows the overall significance of the model. The Durbin-Watson of 2.143511 shows the absence of first-order autocorrelation in estimated model.

1.8 CONCLUSION

Given the findings of this study, the following recommendations are made. The need for export diversification, since the prospects of traditional agricultural export products in the world market are not bright. Also, the government should create an incentive that would encourage investment in the country and also improve the balance of payments position. In addition to this, proper attention should be channeled on the yields from exportation to prevent mismanagement and embezzlement of funds and hence, balance of payments.

Lastly, all hands should be on deck by the Government and Central Bank Authorities to ensure stability in the exchange rate and interest rate.

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