Capital Market Operation and Nigeria's Economic Growth

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Abstract

This study empirically assessed the impact of capital market operations on Nigeria's economic growth from 1999 to 2021. The study was carried out to demonstrate the importance of effective capital market operation in the country's economic growth. The study used Ordinary Least Squares (OLS) methods to empirically examine the effect of market capitalization, total new issues, and transaction value on GDP. We tested and validated the hypothesis that capital market operations have a significant impact on Nigeria's economic growth. As a result, the study recommended that the government step up efforts to create a conducive business environment that would allow domestic and foreign investors to invest in the Nigerian capital market, thereby accelerating the country's economic growth.

Keywords: *capital market; economic growth; market capitalization; value of transactions; gross domestic product.*

JEL Classification: *I15; O40; O49.*

Introduction

Due to the inaccessibility of long-term finance, the majority of Nigerian businesses have relied on short-term financing such as overdrafts to finance even long-term projects over the years. To support this point of view, Ajibola (2017) argued that in Nigerian history, businesses rise and fall for a variety of reasons, including a lack of long-term finance. Using short-term funds to pursue long-term capital projects can cripple any business or project because most financial institutions in Nigeria operate on the match maturity concept, which ensures that loans given and debts incurred mature at the same time. However, according to Binuyo, Oluwatimilehin, Ehy-Ewoh, and Binuyo (2019), the capital market is very important in the economy because capital is a very important factor of production without which economic transactions cannot take place. The ability of a nation to mobilize savings and convert such savings into investment is dependent on the type of capital market that exists at a given time. Since the establishment of the Nigerian capital market, various challenges have been discovered, including but not limited

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to poor economic development that hinders conducive investment environment to sustain vibrant capital market and the challenges of buy-and-hold strategy, that is, stocks are being held for a long period of time.

According to Idris (2020), given the decline in economic performance exacerbated by the Covid-19 pandemic, individuals and businesses require more long-term capital to sustain their business growth; thus, the capital market is expected to intervene and mobilize their required capital as a government intervention fund. Given the market's low absorptive capitalization, low market capitalization, misappropriation of funds, and illiquidity, timely intervention and support may be difficult to provide. According to Binuyo et al. (2019), studies on the capital market have received a lot of attention in the finance and economics literature because of its important role in providing long-term, non-debt financial capital that helps companies avoid over-reliance on debt financing, thus improving corporate debt-to-equity ratio and mobilizing resources for economic growth and development. Idris (2020) argued that, aside from a lack of financing for the productive sectors of the economy, the impact of the capital market in Nigeria has not been thoroughly investigated, and that, while the correlation between the capital market and economic growth in Nigeria may be beneficial to policy-analysis, there is still a lack of sufficient studies to explore this research domain. As a result of the foregoing, the goal of this study is to use the Ordinary Least Square (OLS) regression technique to investigate the impact of the capital market on Nigeria's economic growth between 1999 and 2021.

Empirical Literature

The capital market is defined as a network of specialized financial institutions, as well as a series of mechanisms, processes, and infrastructure that facilitate the gathering of suppliers and users of medium to long-term capital for research and economic development projects in various ways (Al-Faki, 2006 in Binuyo et al., 2019). According to Nwankwo (1991), the capital market provides a variety of financial instruments that allow economic agents to pool, price, and exchange risk. It promotes financial savings by utilizing assets with appealing yields, liquidity, and risk characteristics. For the government and other long-term funding institutions, this is critical. According to Ajibola, a developed and efficient credit market encourages savings, allocates efficient investible funds, and promotes capital accumulation (2017). Countries with an effective credit market, such as the United States and the United Kingdom, have less severe business cycles, less output contraction, and a lower likelihood of an economic downturn, which directly or indirectly boosts private investment behavior in the economy.

According to Agu (2018), economic growth is an increase in an economy's capacity to produce goods and services from one period of time to the next. It refers to the process by which a country's wealth grows over time. The gross domestic product is the most commonly used indicator of economic growth (GDP). GDP, as defined by Adolphus and Dibiah (2021), is a monetary measure of financial development that can be expressed in ostensible terms that include expansion or in genuine terms that account for swelling. Long-term GDP is concerned with the expansion of a pattern or expected pattern, whereas transient GDP is concerned with the yearly change in genuine public yield. In close examinations of various nations with varying population sizes, GDP per capita is frequently used. Similarly, Gbadamosi (2017), as cited by Agu (2018), defines economic growth as an increase in per capita GDP or other aggregate income measures, which is typically reported as the annual rate of change in real GDP. Increased productivity, which means producing more goods and services with the same amount of labor, capital, energy, and materials, is the primary driver. Economic growth, according to Antwi, Mills, and Zhan (2013), is an increase in a country's labor and product yield or the actual expansion of the country's economy. Alhassan and Islam (2019) define economic growth as an increase in an economy's capacity to deliver labor and goods over an unspecified time period. The nature of capital market development and how it affects the real sector of the economy has

received little attention in Nigeria, resulting in numerous controversies. To determine the link between capital market development and economic growth, more research on the nature of the relationship between the financial sector and economic growth is required.

The establishment of the Lagos stock exchange market in 1960 boosted Nigeria's capital market and overall economic growth. The capital market has been identified as an institution that significantly contributes to the socioeconomic growth and development of both emerging and developed countries. The creation of liquidity is the primary channel through which the stock market influences economic activity. Many profitable businesses require long-term capital, but investors are frequently hesitant to give up control of their savings for long periods of time. As a result, the stock exchange market has faced challenges as a viable avenue for investors and businesses to achieve their goals over the years. The market enables the government and industries to raise long-term capital for new projects as well as to expand and modernize industrial operations. Aside from creating liquidity, the stock market aids in risk diversification, allowing it to stimulate economic growth through the process of international integration. By facilitating risk diversification, the stock market encourages a shift to high-return projects. As a result, both direct and indirect activities of the stock exchange market contribute to economic growth. By becoming the first port of call for domestic savings and foreign investors, the Nigerian stock exchange must play a critical role in enabling Nigerian economic transformation. The most significant impediment to economic growth in most African countries, including Nigeria, has been a lack of long-term funds.

Several authors have attempted to link capital market operation and economic growth. The relationship between capital market development and economic growth has frequently sparked heated debate among analysts studying developed and emerging markets, according to Kolapo and Adaramola (2012), cited in Agu (2018). The effectiveness with which the capital market performs its allocative functions determines an economy's growth. Okpoto (2015) also argued that, in addition to the social and institutional factors impeding Nigeria's economic growth, the bottleneck caused by scarcity in the economy is a major setback, thus evaluating the Nigerian capital market to determine its impact on the country's economic growth. Furthermore, Idris (2020) argued that, aside from a lack of financing for the productive sectors of the economy, the decline in economic performance was exacerbated by the Covid-19 pandemic, which affected the entire world. The impact of the capital market on economic growth in Nigeria has not been thoroughly investigated, resulting in a gap in the literature and a lack of sufficient studies to investigate the relationship between capital market performance and economic growth in Nigeria.

A developed stock market, according to Levine (1991), reduces businessmen's liquidity and productivity shocks to investment funds while also increasing the economy's production capacity, resulting in higher economic growth. Capital market development, according to Oladipo and Tunde (2013), promotes economic growth. Lenine and Zervos (1998) investigate whether there is a strong empirical relationship between stock market development and long-run economic growth using pooled cross-country time series. According to the study's findings, the GDP per capita growth rate was regressed on a number of variables designed to control for initial conditions, political stability and human capital investment, macroeconomic conditions, and the stock market development index. Authors such as Ewah et al(2009), Osho (2014), Yadirichukwu and Chigbu (2014), Costkun et al (2020), and others have reported a bidirectional relationship between capital market operation and economic growth.

Levine and Zervos (1998) examined the relationship between financial deepening and economic growth in 41 countries from 1976 to 1993 using regression analysis. One of the financial deepening indicators used in the analysis was the level of development of the stock exchange, as measured by a composite index combining volume, liquidity, and diversification indicators. In contrast, the real growth rate in per capita GDP was chosen as an economic growth indicator. Their findings show a very strong positive correlation between stock market development and

economic growth. The most intriguing aspect of the study was the decrease in statistical significance of other financial deepening variables after including the stock market development index in the regression equation. According to the authors, this demonstrated that stock market development had a greater impact on economic growth than other financial deepening indicators.

According to Binuyo et al., Obamiro (2005) investigates the role of the Nigerian stock exchange in economic growth (2019). He proposed that the government create a more conducive environment for stock market efficiency and, as a result, higher economic growth. Ezeocha et al. (2009) investigate the nature of the relationship between Nigerian stock market development and the level of investment flows. The authors discovered that stock market development encourages domestic private investment flows, implying an increase in the economy's production capacity as well as a boost in national output growth. Their research, however, discovered that the growth of Nigeria's stock market has not been able to encourage the flow of foreign private investment. Financial markets will develop if borrowers and lenders are willing and able to enter into contracts, and liquidity providers find favorable conditions for trading financial instruments, according to Chami et al (2009). They also stress the importance of regulatory structure in removing barriers that make potential borrowers, lenders, and liquidity providers unwilling or unable to play their roles, as well as creating an appropriate incentive for each agent to fulfill their end of the bargain.

Adolphus and Dibiah (2021) investigate the relationship between capital market development and economic growth in Nigeria from 1981 to 2017 using the vector Auto Regression (VAR) estimation method. The work of stock proportion and baking framework capitalization proportion, according to the study, are insignificant in determining Nigeria's GDP. Okpoto (2015), on the other hand, investigated the impact of capital market performance on Nigerian economic growth from 1980 to 2013 and discovered that the Nigeria capital market and economic growth are co-integrated. This meant that Nigeria's capital market and economic growth were in long-run equilibrium. Olawoye (2011), as cited in Adolphus and Dibiah (2021), employs multiple regression analysis to determine whether capital market indices have a significant impact on Nigerian economic growth as measured by GDP. The study discovered a positive relationship between the capital market and economic growth, and the author suggests that declining market capitalization could be improved by encouraging more foreign investors to participate in the market, preserving cutting-edge technology such as automated trading and settlement practices, electronic fund clearance, and eliminating physical share transfers, and restoring market confidence. According to Adjasi (2007), political risk and institutional quality are strongly related to stock market capitalization growth. According to their findings, the establishment of high-quality institutions can play a significant role in the development of stock markets. Institutional factors that influence stock market development include law and order, democratic accountability, and bureaucratic quality. Furthermore, Pagano (1993) observes that regulatory and institutional factors can influence the efficient operation of stock markets, as cited by Okpoto (2015). Regulations that increase investors' trust in brokers, for example, may increase stock market investment and trading.

Adam Smith's Growth Theories, which he proposed in 1776, were used in this study. The theory investigated the Nature and Causes of National Wealth, which did not provide a well-defined definition of theory of development, but the leading theme has been that of economic growth. According to Smith's theory, if individuals are free to maximize their personal wealth, the economy's aggregate wealth will also be maximized. This theory presumes that institutional, political, and natural factors remain constant. Labor is the most important factor driving economic growth; with labor division, labor productivity will rise. This is due to an increase in overall worker skill level. We will concentrate on capital accumulation, which is central to Smith's theory; he saw capital accumulation as a necessary condition for economic growth and

development. The higher the rate of savings in the economy, the higher the rate of investment, it is believed (Anyanwaokoro, 2008).

Methodology and Model Specification

This study examined and measured the impact of capital market activities on Nigeria's economic growth in order to establish a correlation between the two variables. The Ordinary Least Squares regression technique was used to test for stationarity in the time series, while the Unit Root and Johansen co-integration techniques were used to correct autocorrelation when necessary. GDP was used as the dependent variable in our model, and capital market indicators such as market capitalizations (government and industrial securities) were used as the independent variables, or explanatory variables. The model is specifically specified in functional form as follows:

$$RGDP = f(MCAP, TNI, VLT) \qquad (1)$$

Where:
RGDP = Real Gross Domestic Product;
MCAP = Market Capitalisation;
TNI = Total New Issues ;
VLT = Value of Transactions.

The model is further specified in linear form as follows:

$$LRGDP = \beta_0 + \beta_1 MCAP + \beta_2 TNI + \beta_3 VLT + Ut \qquad (2)$$

Where:
β_o = Intercept of the entire regression model;
β_1 = Slope of *MCAP;*
β_2 = Slope of *TNI;*
β_3 = Slope of *VLT;*
Ut = Stochastic error term.

The a priori expectations of the model are $\beta_1 > 0$, $\beta_2 > 0$, $\beta_3 > 0$. This shows that the set of regressors are assumed to be directly related to the gross domestic product (GDP). All the variables are in their natural logarithm form. The data used in this study were obtained from Central Bank of Nigeria Statistical Bulletin, the Nigeria Stock Exchange and the Security Exchange Commission fact book and relevant journals. The data set spanned a period between 1999 and 2021, which is a period of twenty-two (22) years.

Results

The analysis was done with the statistical package for social sciences (SPSS). Table 1 shows the results of ADF unit root test of stationarity of the variables. The model revealed that all the variables are I (1) order of integration where the absolute values of the t-test exceeded the 5% values. This indicates that there was no possibility of the spurious result.

Table 1. Unit Root Test Result

S/N	Variables	ADF t-test	5% critical value	Order of Integration	Trend
1	GDP	-7.260575	-3.440813	I(1)	S
2	MCAP	-5.722093	-3.583736	I(1)	S
3	TNI	-3.491038	-3.583736	I(1)	S
4	VLT	-4.668372	-3.590188	I(1)	S

Source: E-views Computation.

Table 2 displays the Johansen co-integration estimate used to establish a long-run correlation between the variables. The trace statistics values exceeded the 0.05 critical values, demonstrating the existence of co-integration. The findings revealed that the gross domestic product (GDP), which served as a proxy for Nigeria's economic growth, had an equilibrium relationship with the other regressors (market capitalization, total new issues and value of transactions).

Table 2. Johansen Co-Integration Result

Series	RGDP, MCAP, TNI, VLT			
Lags Interval (in first differences): 1 to 1				
Hypothesized No of CE(s)	**Eigen value**	**Trace Statistic**	**0.05 Critical value**	**Prob.****
None*	0.820634	90.12480	34.31162	0.0003
At most 1*	0.611743	58.70045	28.58098	0.0108
At most 2*	0.402600	25.50911	19.70295	0.0001
At most 3*	0.192406	14.37230	11.53371	0.0953

Trace test indicates 2 co-integrating equ. (s) at 0.05 levels of significance

Source: E-views Computation.

Table 3 displays the estimation results of the error correction model. The F-statistic of 6.281077 indicates that all regressors are jointly significant in determining the dependent variable, with a probability of the F-ratio of less than 0.05. Since the prob. values from the table are less than 5%, the results are statistically significant. Because the ECM coefficient is well behaved, the model is dynamic. Although it is negative, it is statistically significant. This means that the rate of adjustment from short-run to long-run equilibrium is only 50.96%. According to the model, all of the regressors had a significant impact on Nigeria's economic growth. The model was also free from autocorrelation, making the mode appropriate for policy prediction.

Table 3. Error Correction Estimation Result

Variable	Coefficient	Std. Error	t-statistic	Prob.
C	2.618463	0488117	3.535801	0.0009
D(MCAP)	2.298342	0.401658	3.604008	0.0005
D(TNI)	-0.420196	0.230114	-2.984506	0.0205
D(VLT)	0.060075	0.065881	5.100047	0.0010
ECM(-1)	-0.509622	0.020406	-3.411631	0.0125
R-Square	0.875319	Mean dependent var	5.187406	
Adjusted R-square	0.883142	S.D. dependent var	0.304250	
S. E. of Regression	0.173560	Akaike into criterion	-3.120007	
Log likelihood	27.13003	Schwarz criterion	-2.833264	
f-statistics	6.281077	Hannan-Quinn criter	2.505380	
prob (F-statistic)	0.000130			

Dependent variable: (GDP);
Method: Least Square;
Date: 24/04/2022;
Sample (adjusted): 1999 2021;
Included observations: 21 after adjustments.

Source: E-views Computation.

Discussion

We empirically verified the effect of capital market operation on Nigeria's economic growth in this study. According to the data analysis presented above, market capitalization and value transactions have a positive and significant impact on Nigeria's economic growth. The total number of new issues discovered to have a negative but significant impact on Nigeria's

economic growth. Furthermore, the research found that the regressors had an equilibrium relationship with Nigeria's economic growth. This implies that measures to increase capital market operation benefit Nigeria's economic growth. This means that market capitalization, total new issues, and transaction value have the potential to contribute to Nigeria's economic growth in the long run.

As a result, efficient capital market operations have the potential to significantly boost Nigeria's economic growth.

According to the preceding result, an increase in Nigerian capital market activity, as measured by market capitalization, total new issues, and transaction value, would significantly boost the country's output. This is because a large capital market broadens the prospect for growth as well as the stock of government development if investments are made and government spending is directed toward profitable sectors with high growth potential. Because increased activity in the Nigerian capital market will significantly increase investor confidence, the Nigerian government should intensify efforts to restore trust in the market by demonstrating genuine commitment and sincerity, enhancing fundamental infrastructures that will facilitate transactions between market participants (issuing houses, stock brokers, local and foreign investors), and encouraging the private sector to participate.

Conclusion

The capital market is a highly specialized and organized financial market and a crucial driver of economic growth because of its capacity to facilitate and mobilize saving and investment. This study calculated how sensitive the Nigerian economy was to the functioning of the capital markets between 1999 and 2021. The results of the study showed that efficient capital market operation continues to be one of the mainstays in every economy with the power to affect economic development and growth. As a result, it is anticipated that this study will support the government's and policymakers' attempts to revive Nigeria's capital market and win back the confidence of investors and other market participants. A thriving and well-developed capital market is expected to attract foreign investors and contribute to the country's faster economic growth. Throughout the investigation, the model demonstrated a positive relationship between the dependent variable and the independent factors (repressors). The study's findings led to the recommendation that favorable investment-friendly regulations be developed and implemented in order to attract potential investors to the Nigerian capital market. Furthermore, the stock exchange market must be expanded to accommodate more securities and to increase the value of the stocks traded there.

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