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EFFECT OF GLOBALIZATION IN A CORRUPT ECONOMY: EVIDENCE FROM NIGERIA

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ABSTRACT

This study explores the channels through which globalization engender corruption an acts as an impediment to achieving the economic growth in Nigeria. The Structural Vector Auto Regression (SVAR) estimation technique is used to test this relationship. The variables used include Gross Domestic Product (GDP) growth rate, Openness (proxy by index of export plus index of import divided by GDP and corruption perception index. The scope covers the period 1970 to 2010. It was discovered that globalization engender corruption which in turn impacted negatively on economic growth. The impulse response results indicate that globalization accounts for negative shocks in the economy via its effects on corruption, while the Forecast Variance Decomposition show that corruption accounts for a substantial portion of the variance decomposition of the variables under study. Hence, there is need to tackle corruption seriously if the country must achieve the essential benefit of globalization.
Keywords: Globalization, Corruption, Corrupt Leaders, Openness and Growth Rate

INTRODUCTION

Since the 1980s, globalization has changed drastically both negatively and positively the life of millions of people around the world, and most developing countries has not escaped this change. Globalization is not new, it "can be traced back at least to the 15th century, with the genesis of the capital world economy and the geographic expansion of division of labor, access to raw materials, industrial production, and the circulation of capital. However, in the last 30 years, the process of a globalization has increased in an unprecedented speed, and today, it involves so many reforms that simply some governments are unable to adjust themselves to these policies, and as a result governments see their sovereignty and power vanish away (Sicha, 2008).Today, corruption is internationally recognized as a major problem in the society, one capable of threatening social, economic and political development and undermining the values of trade and democracy. This holds true at both the domestic level and the international level. Indeed, with the growing globalization of markets of services, goods and people accompanied by the internationalization of illegal activities, the international dimension of corruption gains its significance. Shang –Jin (2009), opined that more corrupt countries receive less benefits of globalization. As a result, reducing corruption becomes a priority at both the national and international levels and requires concerted efforts, exchange of experience and a certain degree of standardization. Research in the mid-1990s however, showed that corruption is a hindrance to economic growth. Corruption is a major problem in Nigeria today. World Bank studies states that corruption accounts for up to 12% of the GDP of nations like Nigeria (Nwabuzor, 2005). This paper reviews the fact that

Nigeria with a high level of corruption will find it difficult to achieve the gains of globalization which resultant effects will lead to fall in the economic growth. The paper is motivated by the observation that Nigeria appears stuck in a vicious circle of widespread corruption and low economic growth despite their involvement in international trade. Apart from the introduction, the rest of the paper is organized as follows. Section 2 present literature review associated with causes of corruption and its effects on economic growth. Section 3 presents the empirical model, model specification and describes the data which are employed in the study. Section 4 presents the empirical results. Finally, Section 5 draws the main conclusions and possible recommendations of the paper.

LITERATURE REVIEW

Conceptualizing Corruption

It is very easy for every one to talk about corruption, but like many other complex phenomena, it is difficult to define corruption in concise and concrete terms. Corruption is one of the many unresolved problems that have critically hobbled and skewed development (Ayobolu, 2006, Obayelu, 2007). It remains a long-term major political and economic challenge for Nigeria (Sachs, 2007). It is a canker worm that has eaten deep in the fabric of the nation. It ranges from petty corruption to political / bureaucratic corruption or Systemic corruption. World Bank studies put corruption at over $1 trillion per year accounting for up to 12% of the Gross Domestic Product of nations like Nigeria, Kenya and Venezuela (see, Nwabuzor, 2005). Corruption is efforts to secure wealth or power through illegal means for private gain at public expense; or a misuse of public power for private benefit. Corruption like cockroaches has coexisted with human society for a long time and remains as one of the problems in many of the world's developing economies with devastating consequences. Corruption as a phenomenon, is a global problem, and exists in varying degrees in different countries (Agbu, 2001). Corruption is not only found in democratic and dictatorial politics, but also in feudal, capitalist and socialist economies. Christian, Muslim, Hindu, and Buddhist cultures are equally bedeviled by corruption (Dike, 2005). Corrupt practices are not an issue that just begins today; but the history is as old as the world (Lipset and Lenz, 2000).

In Nigeria, it is one of the many unresolved problems (Ayobolu, 2006) that have critically hobbled and skewed development. It remains a long-term major political and economic challenge for Nigeria (Sachs, 2007). It is a canker worm that has eaten deep in the fabric of the nation. It ranges from petty corruption to political / bureaucratic corruption or Systemic corruption (International Center for Economic Growth, 1999). World Bank studies put corruption at over $1 trillion per year accounting for up to 12% of the Gross Domestic Product of nations like Nigeria, Kenya and Venezuela (Nwabuzor, 2005). Corruption is endemic as well as an enemy within (Agbu, 2003). It is a canker worm that has eaten deep in the fabric of the country and had stunted growth in all sectors (Economic and Financial Crime Commission (EFCC), 2005). It has been the primary reason behind the country difficulties in developing fast (Independent Corrupt Practices Commission (ICPC), 2006). This is evident in Transparency International's has consistent rating of Nigeria as one of the top three most corrupt countries in the world (Ribadu, 2003).

Concept of Globalization

Much of the talk of 'globalization' is confused and confusing. 'Globalization' has become a buzzword - and those using the term often have contrasting understandings of what it means. Obadan,(2006) define globalization as a process which integrates world economies, culture, technology and governance. To Scholte (2000), 'globalization' refers to 'a process of removing government-imposed restrictions on movements between countries in order to create an "open", "borderless" world economy'. Those who have argued with some success for the abolition of regulatory trade barriers and capital controls have sometimes clothed this in the mantle of 'globalization'. Economic globalization can be defined as the process of increasing economic integration through trade, financial flow, exchange of technology and information, and movement of people (see Obadan, 2004 and 2005 Moghadam, 2005, D .Vani, 2004). Kinnvall and Jonsson (2002) present globalization in a very broad context suggesting that the concept is rather difficult to give a precise meaning noting that it is an all enveloping catchword of our times. This can be seen from the number of issues that it covers and the disciplines, which are addressing globalization. Snyder (2002) conceptualises globalization as an aggregate of multifaceted uneven, often contradictory economic, political, social and cultural processes, which are characteristic of our time. Findlay (2000) views globalization in a social context as the progress towards one culture on the planet— a single society. In this definition, Findlay envisages globalization as a social process whereby the constraints of geography on social and cultural arrangements recede and people become increasingly aware of this recession.

EMPIRICAL REVIEW

Many non-economists expect the costs associated with globalization to exceed its benefits. Fears of an erosion of social and environmental standards, high poverty rates in less developed countries and ever higher frequencies of financial crisis resulted in protests like that in Seattle in 1999. Quite the contrary, most economists strongly believe the net effect of globalization to be positive. Apart from economic theory, this optimism is supported by empirical studies as well. To measure globalization, most of these studies employed proxies like trade and capital flows or openness to these flows. Using these proxies, Beer and Boswell (2001) examined the consequences of globalization on inequality. Li and Reuveny (2003) analyzed their effects on democracy. As Heinemann (2000) shows, more globalized countries have lower increases in government outlays and taxes. Vaubel (1999) found them to have lower government consumption. The effects of globalization on growth have also been frequently analyzed with these measures. Until most recently, however, most studies examined them employing cross sections only. For example, Chanda (2001) uses an index of capital account openness to show that more developing countries have suffered from globalization than not, while Rodrik (1998) as well as Alesina et al. (1994) found no effect of capital account openness on economic growth.1 With respect to foreign direct investment (fdi) there is evidence of a positive growth-effect in countries which are sufficiently rich (Blomström et al. 1992) and a negative one in low income countries (Garrett 2001).2 Among others, Dollar (1992) analyzed the relationship between economic performance and openness to trade, Frankel and Romer (1996) those between growth and actual flows. Their results show that both openness to trade and actual trade flows are robustly related to growth. All of these studies present, however, only cross sectional estimates. Moreover, they do not adequately control for endogeneity. Their results might therefore reflect unobserved characteristics which do not vary over time instead of being the consequences of globalization or might reflect reverse causality. Aware of the shortcomings of the cross-section approach, some recent studies use panel data to examine the relationship between some dimensions of globalization and growth. Among them, Dollar and Kraay (2001) found that an increase in trade flows and foreign direct investment resulted in higher growth rates. Greenaway et al. (1999) also report a strong relationship between trade and growth. With respect to fdi, Borensztein et al. (1998) provide evidence of a positive growth-effect – given a minimum threshold stock of human capital. A detailed analysis of the impact of several indicators of financial integration and growth is provided by Edison et al. (2002a). Their results show that no robust relationship exists.

Causes of Corruption in Nigeria

There have been a lot of factors identified as instrumental to enthroning corrupt practices in Nigeria. These include, briefly, the nature of Nigeria's political economy, the weak institutions of government, and a dysfunctional legal system. Absence of clear rules and codes of ethics leads to abuse of discretionary power make most Nigerian vulnerable to corrupt practices. The country also has a culture of affluent and ostentatious living that expects much from "big men," extended family pressures (Maduagwe, 1996), village/ethnic loyalties, and competitive ethnicity. The country is also one of the very few countries in the world where a man's source of wealth is of no concern to his neighbours, the public or the government. Once a man is able to dole out money, the churches, the Mosques pray for him, he collects chieftaincy titles and hobnobs with those who govern. The message to those who have not made it is clear: just be rich, the ways and means are irrelevant (Ubeku, 1991). Low civil service salaries and poor working conditions, with few incentives and rewards for efficient and effective performance, are strong incentives for corruption in Nigeria. Other factors are: less effective government works with slow budget procedures, lack of transparency, inadequate strategic vision and weak monitoring mechanisms make Nigeria a fertile the environment for corrupt practice. Informal rules are found to supercede formal ones, thereby making stringent legal principles and procedures to loose their authority. Hence, bribery and corruption are taken by many Nigerians as norm even in the face of anti-corruption crusades intended to support clean governance.

Impact of Corruption on the Economy

There is no clear estimate of the global cost of corruption. However, In terms of the evaluation of the economic consequences of corruption Gupta et al (1998) examine the impact of corruption upon the distribution of income in 37 countries. They discovered a positive association between corruption and income inequality (measured by the Gini coefficient) and a negative impact of the growth of corruption upon the income growth of the bottom 20% of the income distribution. Other studies have focused upon the influence of corruption on the level of GDP per capita (Kaufman et al (1999)) and upon the rate of growth of GDP. Keefer & Knack (1995), Poirson (1998) and Leite & Weidmann (1999) all confirmed the significance of corruption levels for growth rates. Mauro (1995) identified reduced investment as the mechanism whereby growth was reduced by the influence of corruption. Utilising data from Business International for the period 1980-85 for 58 countries Mauro employed nine country assessment categories, grouped into indices of bureaucratic efficiency, political stability and overall institutional efficiency, so as to reduce measurement error. The bureaucratic index consisted of assessments of the efficiency of the bureaucracy, judiciary and of the incidence of corruption. Both the bureaucratic index and corruption alone were found to be negatively correlated with the rate of investment, even while controlling for other significant variables. To test for the endogeneity of these variables Mauro employed a measure of national linguistic homogeneity (Ethnolinguistic Fractionalisation), confirming the causal relationship. As investment is an important determinant of growth Mauro proceeded to examine the relationship between corruption and growth. Both the corruption index and the bureaucratic efficiency index were significantly related to per capita GDP growth over the period 1960-85, although the results were less robust than in the case of the relationship to investment. But more importantly once investment was introduced into the growth equations the bureaucracy and corruption indices became insignificant. Ades and Di Tella (1997) also examined the impact of corruption upon investment and found that it reduced the positive impact of interventionist policies upon investment by between 16% and 72%. A number of other studies, using different indexes of corruption, have confirmed these results (eg. Keefer & Knack 1995; Benno and Piatti (2010)). This suggests that the primary economic impact of corruption may be as a deterrent to investment rather than in reducing the productivity of capital once an investment is made.

Government Efforts at Combating Corruption in Nigeria

Nigeria remains mired in corruption, crime, poverty, and violence despite the promulgation of several laws like in other countries as the principal mechanism for curbing corruption. The legal instruments used to fight corruption in Nigeria include the Criminal Code, Code of Conduct Bureau, the Recovery of Public Property Act of 1984 and the newly formed commissions (the EFCC and the ICPC). Prior to 1966, the Criminal Code was the primary source of law dealing with corruption in Nigeria. But due to the narrow nature in dealing with corruption such as only criminalizing the conduct of bribe-taking public servants leaving the private, it was replaced by Criminal Justice (Miscellaneous provision) Decree in 1966. This however failed to stem the tide of corruption. The rules were confusing, thus leaving open the livelihood that guilty persons might escape punishment on technical grounds. The code of Conduct was thereafter formed in the 1979 Nigeria constitution where complaints on corrupt practices are referred to Code of Conduct Bureau Tribunal. The Bureau forbids public officers from simultaneously receiving remuneration of two public offices and from engaging in private practices while in the employment of government, the code bar public servants from accepting gifts or benefits in kind for themselves or any other person on account of anything done or omitted to be done in the discharge of their duties. It prohibits public officers from maintaining or operating foreign bank accounts. Public officers are required to declare their assets and those of their families immediately after taking office, at the end of every four years in office, and at the end of their terms. Due to the non inclusion of the private sector which are also corrupt in all these laws, In year 2000, the Independent Corrupt Practices and Other related Offences Act was promulgated which eventually gave birth to the ICPC and the EFCC charged with the responsibility of investigating, arresting and charging any offenders with corrupt practices either economic or financial crimes in Nigeria to court.

METHODOLOGY

This paper is based on a vector autoregression model as most empirical work make use of the Ordinary Least Square methodology and game (see for example Laffont 1991 and Murphy 1993). The vector autoregression however, is used along with the impulse response functions and the variance decomposition. The variables of interest are ordered as follows, Gross Domestic Product (GDP) growth rate (GR), Openness (Index of import + Index of export/ GDP) and corruption (COR) corruption perception index . All data are obtainable from the CBN statistical bulletin and the Transparency international and authors computation.

The VAR model is presented below

$$y_t = c + \sum_{i=1}^{n} \varphi_i y_{t-i} + Z_t + E_t \quad (1)$$

Where $y_t$is (3 x 1) vector of endogenous variables c is the (3 x 1) intercept vector of the VAR, φ_i is the (3 x 3) matrix of autoregressive coefficients, and E_t is the (3 x 1) generalization of a white noise. The VAR system can be transformed into its moving average representation as

$$y_t = \mu + \sum_{i=0}^{\infty} y_i + Z_t + E_t \ldots\ldots \quad (2)$$

Where y_t is the identity matrix while μ is the mean of the process. Equation two is used to obtain the forecast error variance decomposition and the impulse response function. The variance decomposition shows the proportion of the unanticipated change of a variable that is attributed to its own innovations and shocks to the variable in the system. The impulse response functions measure the response of each variable to a shock to itself and other variables.

EMPIRICAL RESULTS

Vector Auto Regression Result

Results obtained from the vector autoregression results indicate that the coefficient of determination R^2 is highest for GLO and COR with about 82% and 68% except for GWR which set for only 22%. The F – statistics result also indicates that only GWR was not been overall significant. The difficulty in interpreting vector auto regression results however makes it imperative to move straight to interpreting the impulse response functions and the variance decomposition.

IMPULSE RESPONSE FUNCTION

Except for COR and GLO, GWR variable respond to one standard deviation (SD) by converging to equilibrium by the tenth year. Response of all the variables to one another shows that they diverge from their equilibrium. Globalization and corruption diverge and also with its response to economic growth. The positive response of globalisation to corruption indicates that with increase in globalization in the country, corruption also increased and policies imposed by the government may not be able to solve the problem of corruption which will have allow the country achieve the gains of globalization. However, all results that may later converge shows that the convergence is gradually which shows that even if policies will work, it will be gradually which may not be achieved for a shorter period.

VARIANCE DECOMPOSITION RESULT

Result from the variance decomposition indicates that for globalization, globalisation accounts for 100% of itself with no other variables explaining it in the first year. However, in the second year as openness of the country is reducing corruption also was reducing, while growth in the economy was rising. The result shows that openness does not engender growth in the Nigeria content this may be as a result of its effects on corruption. By the tenth year however it is clear that corruption accounts for about 4%. The outcome of the result shows clearly that corruption has positive relationship with openness hence the more openness (globalization) of the economy, the more corrupt practice increase and this in turn slow down economic growth. For corruption it was found that openness accounts for it right from the first year. The implication of the result shows clearly that globalization and corruption works hand in hand in the Nigeria context. For the growth result also, it was found that an inverse relationship exist between growth and globalization, this no doubt will be as a result of corruption. The result from the first year shows that as economic growth is falling, globalisation is rising with corruption. This postulate the fact that globalisation pave way for corruption and is in turn reduces growth.

CONCLUSIONS AND RECOMMENDATIONS

This study on the effects of globalization in a corrupt economy evidence from Nigeria was carried out using a Vector Auto Regression (VAR) model with the impulse response functions and the variance decomposition. Findings show that globalization engender corruption which in turn reduces the level of economic growth. Corruption explains low growth more than growth explains corruption and that Globalization has been the leading avenue for corruption in the country of which all the governments from the top to the toe are fully involved this inturn reduces economic growth. The paper recommends that efforts be made at increasing the rate of economic growth, investing in human capital especially those that improve the well being of the people and a strong monitoring of the trade between the country and rest of the world. The local, State and Federal Government can achieve this, when they also try to ensure adequate reduction in the alarming rate of corruption. These are to be done on the basis of need and not for greasing the pockets of a few select people.. Conditions of service especially in the public service and living and economic conditions should be improved also. There should be less reliance on imported goods, as they have not contributed significantly to growth but have created room for rent seeking and siphoning of the country's revenue. The big government has provided opportunities for corruption and so they should divest from providing services to being a regulatory body so as to meet with the benefits of globalization. Howbeit, this can only be achieved when there is increased accountability, transparency in government and the public – private sectors of the country. If all these are well monitored and put in place, no doubt that the thought of the country in achieving positive gains from globalization will be ascertained.

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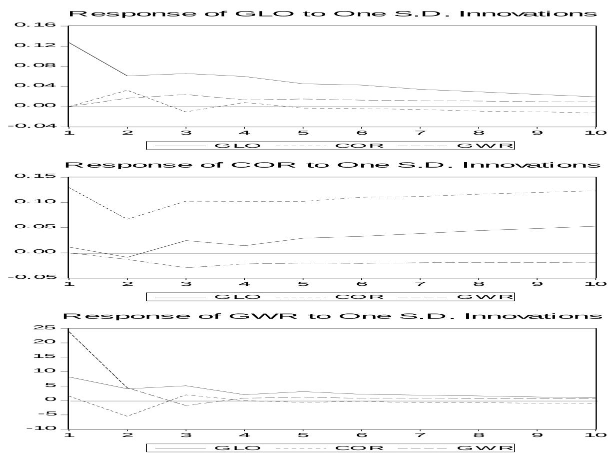
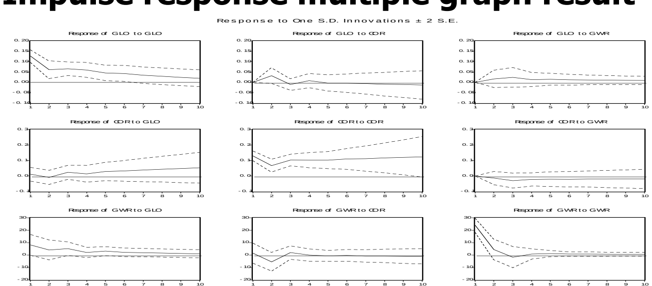
Impulse response combined graph result **APPENDIX I**



Impulse response multiple graph result



VARIANCE DECOMPOSITION RESULT **APPENDIX**

II Variance decomposition on: GLO

Period	S.E.	GLO	COR	GWR
1	0.127037	100.0000	0.000000	0.000000
2	0.145566	93.69636	4.985505	1.318138
3	0.161769	92.28102	4.453895	3.265082
4	0.173182	92.44448	4.113154	3.442371
5	0.179673	92.25540	3.849230	3.895373
6	0.185186	92.18366	3.668862	4.147477
7	0.188790	91.99155	3.626370	4.382082
8	0.191588	91.67557	3.742215	4.582212
9	0.193649	91.30253	3.951651	4.745822
10	0.195265	90.80782	4.302233	4.889949

COR

Period	S.E.	GLO	COR	GWR
1	0.130093	0.776756	99.22324	0.000000
2	0.147030	0.976893	98.21700	0.806106
3	0.183219	2.383096	94.47553	3.141372
4	0.211351	2.234190	94.31003	3.455778
5	0.237379	3.261364	93.25645	3.482191
6	0.264565	4.156280	92.41182	3.431904
7	0.290313	5.189156	91.49714	3.313705
8	0.316448	6.300530	90.52336	3.176111
9	0.342272	7.373269	89.59844	3.028295
10	0.368086	8.443843	88.67400	2.882159

GWR

Period	S.E.	GLO	COR	GWR
1	25.31737	10.43991	0.363439	89.19666
2	26.58674	11.78647	4.591465	83.62207
3	27.19552	14.77497	4.897333	80.32770
4	27.28173	15.22512	4.866913	79.90797
5	27.48654	16.26644	4.854421	78.87914
6	27.58474	16.77041	4.831818	78.39777
7	27.66975	17.12067	4.887424	77.99190
8	27.73264	17.36827	4.938777	77.69295
9	27.78264	17.49717	5.038076	77.46476
10	27.82625	17.56893	5.166332	77.26474

Vector Autoregression Results

R-squared	0.681242	0.827062	0.217368
Adj. R-squared	0.612937	0.790003	0.049661
Sum sq. resids	0.564841	0.592347	22433.92
S.E. equation	0.142031	0.145448	28.30568
F-statistic	9.973489	22.31789	1.296120
Log likelihood	22.55193	21.71985	-162.7650
Akaike AIC	-0.888681	-0.841134	9.700858
Schwarz SC	-0.577612	-0.530065	10.01193
Mean dependent	0.437650	1.006571	21.30267
S.D. dependent	0.228293	0.317397	29.03584