The Effect of Global Financial Crisis on Nigerian Economy

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Abstract
The recent global financial crisis, which was triggered by the credit crunch from the sub-prime mortgage market in the United States, had a contagious effect. Against this background this study makes an attempt to examine the impact of the recent global financial crisis on Nigeria economy in terms of selected economic and financial indicators. Some of the indicators include; market capitalization, commodity prices, exchange rate, foreign direct investment, trade flows etc. Market capitalization which stood at N13.3 billion in 2007 and fell to N9.6 billion in 2008 and also declined to N7 billion in 2009, while the All Share Index grew by 74.73 percent in 2007 and fell by 45.8 percent in 2008 and also declined by 33.8 percent in 2009; the crude oil price declined sharply from US$147 per barrel in July 2008 to $37 per barrel in January 2009, leading to a decline in external reserves and hence accruable revenue. The debt profile was also at increase. Foreign portfolio investors have withdrawn over $15 billion, while remittances and official development assistance (ODA) fell greatly from 2008 to 2009. Unemployment and inflation rate increased from 6.6 percent and 12.70 percent in 2007 to 15.1 percent and 14.90 percent in 2008, respectively. Government projects were affected with less budgetary allocation, thus, leading to instability in the Nigerian economy. In responses to the crisis government initiated measures which include; reduction of the Monetary Policy Rate (MPR) from 10.25 percent to 9.75 percent, reduction in Cash Reserve Requirement (CRR) from 4.0 percent to 2.0 percent, expansion of leading facility to banks up to 360 days and reduction of liquidity ratio from 40.0-30.0 percent. These measures were required to stop liquidity in the economy and stabilize it. However, Nigerian economy showed an evidence of rapid recovery after the periods of the set back, 2008-2009.

Key words: Global financial Crisis, Contagion, Inflation, Unemployment, Capital Market, Foreign direct investment, Exchange rate and Trade flows

JEL Classification: E31, E24, F31, F18, F21 G01, O55

1 Introduction
The term financial crisis refers to the loss of confidence in a country's currency or other financial assets causing international investors to withdraw their funds from the country. Financial crisis means a sudden
change in the financial stability in the country, a situation where some of the huge financial institutions suddenly lose a large part of their assets. It could be a situation of slow down or decline in economic activities. Also, it is a lull in an economy, characterized by recession or depression. It could be local when it affected only a handful of countries in a region/geographical area or global when it is more pervasive and affects many countries.

Historically, the global economy has witnessed several financial crises in the past. Some of it were experienced in 1830s, 1930s and recently, 2008. The most severe was the great depression of the 1930s. And the Asian financial crisis in the latter part of 1990s, all these recessionary trends had been accompanied by shocks to the economies of one or more markets. The 1830 depression affected land speculators in US where farmers lost their farms through mortgage, many construction works stopped, banks faced crises, unemployment rose and prices due to wave of speculations rose. The 1930 depression was very vicious where securities sold fifty times their earning power with dividend earning rising from $40 to $50 per share. Before 1930, from 1925-1929 the market value of US securities tripled from $27billion to $87billion as a result of high wave of speculations. But by the end of 1929 the market began to weaken resulting in the 1930 great depression. The recent, 2007-2008 financial crisis can be said to be global in nature as it affected almost all the economies of the world. 2007-2008 crisis is the crux of the subject matter.

The 2008 financial disruption triggered by the US sub-prime mortgage market led to a global financial crisis, which simultaneously affected major economies, such as United States of America, European Union, China and Japan. This global crisis threw all these economies and many more into recession by the end of 2008. According to IMF(2009), many countries in sub-Saharan Africa experienced robust economic growth in recent years that boosted their balance sheet. Enjoyed favorable external balance and increased external support in form of debt relief and high capital inflows. African economies greatly differ in relation to financial market development, linkages to global financial markets and instructions, initial adequacy of their financial systems, and their capacity to absorb or respond to external shocks flexibly. Hence, their exposure to the crisis also varies. The better positioned countries with adequate financial system, substantial reserves, and fiscal surpluses are linked to global markets and speedily they feel the contagion effects. And also, can absorb shocks better and, mitigate the effects more effectively(Kiyota, 2009).

With this background, this paper attempts to assess the effect of the recent global financial crisis on the Nigeria’s economy and lessons to learn. In this regard, the paper is organized in five sections. Following this introduction is section II, which contains overview of Nigerian economy prior to the global financial crisis, section III presents Africa’s exposure to shocks, section IV deals with the effect of global financial crisis on Nigerian economy. Section V examines the lessons to be learned from the crisis while VI concludes the paper.

II Overview Of Nigerian Economy Prior to the Global Financial Crisis

Prior to the global financial crisis in 2007 Nigerian economy performed below projected target, with an estimated GDP growth of 6.5 percent. This figure, though below the set target of 10 percent, was still higher than the 6.0 percent recorded in 2006(see table 1 below). This growth was driven primarily by the non-oil sector, which grew by 9.5percent (CBN, 2008), largely attributable to the agricultural sector, which grew by 7.4percent, led by crop production, livestock and fishing. The agricultural sector, on the other hand, contributed almost half of the GDP growth rate of 6.2 percent (Ajakaiye and Fakiyesi, 2009).
Table 1: Nigeria Sectoral Shares of Output (%) and Socio-economic Indicators, 2004-2009

<table>
<thead>
<tr>
<th>Nigerian Key Indicators/Year</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP at current market price (N trillions)</td>
<td>11.41</td>
<td>14.57</td>
<td>18.56</td>
<td>22.91</td>
<td>24.30</td>
<td>24.79</td>
</tr>
<tr>
<td>Real GDP growth rate (%)</td>
<td>6.58</td>
<td>6.51</td>
<td>5.63</td>
<td>6.45</td>
<td>5.98</td>
<td>6.96</td>
</tr>
<tr>
<td>Oil sector GDP growth rate (%)</td>
<td>3.30</td>
<td>0.50</td>
<td>(4.51)</td>
<td>(5.1)</td>
<td>(4.5)</td>
<td>0.45</td>
</tr>
<tr>
<td>Non-oil sector GDP growth rate (%)</td>
<td>7.82</td>
<td>8.6</td>
<td>8.59</td>
<td>9.8</td>
<td>9.5</td>
<td>8.32</td>
</tr>
<tr>
<td>Export of Goods and services(% of GDP)</td>
<td>-</td>
<td>4.7</td>
<td>-</td>
<td>-</td>
<td>42</td>
<td>37</td>
</tr>
<tr>
<td>Import of Goods and services(% of GDP)</td>
<td>-</td>
<td>31</td>
<td>-</td>
<td>-</td>
<td>29</td>
<td>29</td>
</tr>
<tr>
<td>Agriculture</td>
<td>390375</td>
<td>477319</td>
<td>564023</td>
<td>675786</td>
<td>798139</td>
<td>919385</td>
</tr>
<tr>
<td>Industry</td>
<td>461008</td>
<td>609489</td>
<td>748874</td>
<td>808538</td>
<td>971951</td>
<td>797249</td>
</tr>
<tr>
<td>Manufacturing capacity utilization (%)</td>
<td>55.7</td>
<td>54.80</td>
<td>53.30</td>
<td>53.38</td>
<td>53.84</td>
<td>-</td>
</tr>
<tr>
<td>Services</td>
<td>124672</td>
<td>162011</td>
<td>214348</td>
<td>250283</td>
<td>278565</td>
<td>310682</td>
</tr>
<tr>
<td>Oil Revenue(N million)</td>
<td>3,354,800</td>
<td>4,762,400</td>
<td>5,287,567</td>
<td>4,462,950</td>
<td>6,530,630</td>
<td>3,191,938</td>
</tr>
<tr>
<td>Total Revenue (N million)</td>
<td>3,920,500</td>
<td>5,547,500</td>
<td>5,965,102</td>
<td>5,715,500</td>
<td>7,866,590</td>
<td>4,057,499</td>
</tr>
<tr>
<td>Non-Oil Revenue (N million)</td>
<td>565,700</td>
<td>565,700</td>
<td>565,700</td>
<td>565,700</td>
<td>565,700</td>
<td>565,700</td>
</tr>
<tr>
<td>Total population (millions)</td>
<td>129</td>
<td>134</td>
<td>140</td>
<td>144</td>
<td>149</td>
<td>150</td>
</tr>
<tr>
<td>Unemployment rate (%)</td>
<td>11.80</td>
<td>11.90</td>
<td>5.30</td>
<td>12.70</td>
<td>14.90</td>
<td>19.70</td>
</tr>
<tr>
<td>Inflation rate (year-on-year) %</td>
<td>10.00</td>
<td>11.60</td>
<td>8.50</td>
<td>6.6</td>
<td>15.1</td>
<td>12.00</td>
</tr>
<tr>
<td>Inflation rate (12-month average) (%)</td>
<td>15.00</td>
<td>17.90</td>
<td>8.20</td>
<td>5.4</td>
<td>11.90</td>
<td>12.40</td>
</tr>
</tbody>
</table>

Source: CBN(2009), FSDH Research(2012), NSEC(2010), IMF World Economic Outlook (WEO), October 2010, World Development

Industrial output fell by 3.5 percent in 2006, attributable mainly to the 5.9 percent drop in crude oil production occasioned by the Niger Delta crisis in 2006 (Ajakaiye and Fakiyesi, 2009). As shown in table 1, manufacturing capacity utilization dropped from 55.7 percent in 2004 to 53.30 percent in 2006, owing to the difficult operating environment. In 2003 Foreign Direct Investment (FDI), Aid and Remittance stood, at US$6,409 million and 2.587 percent of Gross Domestic Product (GDP) and rose to US$11,428 million and 3.737 percent of the GDP in 2006 respectively. In the financial sector, the market capitalization was N2,112.5 billion in 2004 and rose to N5,121.0 billion in 2006 (see table 1 and 3). Unemployment rate stood at 18.40 percent in 2003 and declined to 5.30 percent in 2006 while inflation stood at 10.00 percent in 2004 and declined to 8.50 percent.
III Africa’s Exposure to Shock
As the financial crisis erupted in United State financial markets in September 2008 and quickly spreading to affect financial institutions in Europe, has its causes in a combination of factors. These include easy and cheap credit, a bubble in house prices, excessive deregulation and inadequate supervision of financial institutions, rapid innovation in highly leveraged financial derivative instruments that only few persons understood, expansion of sub-prime mortgage lending through skewed incentives, etc. these encouraged inappropriate risk-taking by financiers and traders as well as inappropriate ratings of securities. The Review and Analysis of what caused the crisis are contained in Morris(2008) and Taylor(2009).
Initially, because of various factors, many hoped that African countries, Nigeria not excluded, might be spared from the consequences of the crisis. These factors include, that the crisis originated in the financial sector of the United State(US) where African banks had limited exposure to US-originated securities, second, that the initial expansionary fiscal and monetary policies implemented by US and European Union were sufficient to stimulate their economies to prevent a slump in demand and a decline in aid to Africa, and third, that given the expansion of trade between Africa and Asia in recent years, there might be some disconnect of the dependency of African growth rates on US and European Union(Fosu and Naude,2009). Conversely, there was a growing awareness that Africa’s financial markets would not escape the evil hand of the crisis and that the effect would be more subtle and may be longer in duration.
As bailout and stimulus plans failed to stem the decline in the world trade and finance, there was fear for foreign aid to African countries to decline. Surprisingly, Africa’s growth rate and expected future growth pattern came down speedily after the crisis erupted in September 2008(Fosu and Naude 2009). It thus became obvious that African countries did not escaped the global financial crisis. In the next section we specifically discussed the effect of financial crisis on Nigerian economy.

IV Effect OF THE GLOBAL FINANCIAL CRISIS ON NIGERIAN ECONOMY
The extent to which Nigerian economy is at risk from the effects of global financial crisis depends on, first, how vulnerable the country is to external trade and financial shocks and second, how resilient she is in terms of coping with the effect of the crisis. The vulnerability to trade and financial shock is determined by Nigeria’s high dependency on exports, undiversified exports commodity, external financial inflows and rapid expansion in private sector credit. On assessing the effect of global financial we looked at its effect vis-à-vis on banking sector, capital market, oil sector, foreign exchange rate, capital flows, unemployment and inflation and trade flows.

Table 2: Nigeria’s Financial Indicators, 2004-2009

<table>
<thead>
<tr>
<th>Nigerian Key Indicators/Year</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inflation rate (year-on-year) %</td>
<td>10.00</td>
<td>11.60</td>
<td>8.50</td>
<td>6.6</td>
<td>15.1</td>
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<td>17.90</td>
<td>8.20</td>
<td>5.4</td>
<td>11.90</td>
<td>12.40</td>
</tr>
<tr>
<td>Credit to the private sector (N billions)</td>
<td>1,507.87</td>
<td>1,950.38</td>
<td>2,490.38</td>
<td>4,600</td>
<td>7,400</td>
<td>10,206</td>
</tr>
<tr>
<td>Net domestic credit (N billions)</td>
<td>2,020.2</td>
<td>2,313.4</td>
<td>753.8</td>
<td>2,212.7</td>
<td>5,391.8</td>
<td>7,903.8</td>
</tr>
<tr>
<td>Banks total assets (N billions)</td>
<td>3,392.9</td>
<td>4,389.3</td>
<td>6,738</td>
<td>10,431</td>
<td>17,031</td>
<td>15,851</td>
</tr>
<tr>
<td>Banks Non-Performing Loan (%)</td>
<td>21.60</td>
<td>18.12</td>
<td>8.76</td>
<td>8.44</td>
<td>28.00</td>
<td>35.00</td>
</tr>
<tr>
<td>Total banks deposits (N billions)</td>
<td>1,623</td>
<td>2,478</td>
<td>3,441</td>
<td>5,072</td>
<td>8,274</td>
<td>8,680</td>
</tr>
<tr>
<td>Exchange Rate (N/US$1),</td>
<td>133.3</td>
<td>131.60</td>
<td>127.00</td>
<td>116.80</td>
<td>131.25</td>
<td>148.10</td>
</tr>
</tbody>
</table>

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4.1 Effect On Banking Sector

In a globalised world, transactions are carried out in different countries in integrated markets. The world has over the past two decades headed towards liberalization and deregulation, with the goal of integrating world markets. Nigeria’s low level of banking sector integration meant that Nigerian banking sector was not affected directly by global financial crisis. On like Ghana, Angola, Botswana that have 65, 53, and 77 percent of their share of banking assets held by foreign banks. This shows how high the banking sector of these economies are linked to external source. The gravity and depth of the crisis in the banking sector was not fully evident until 2009. The main component considered is Non-Performing Loans (NPLs) as a percentage of total commercial bank loans. As shown in table 2 above, the NPLs reduced from 21.60 percent in 2004 to 8.3 percent in 2007 and increased to 35.0 percent in 2009. This increase in NPLs was as a result of maturity of loans granted in 2008 which falls due in 2009. Some of these are consequent to the activities of the stockbrokers in the use of margin loans in funding their capital market activities, as well as those who received loans to finance share purchases when their prices were still high. These became problematic when stocks prices tumbled. Margin lending allows money to be borrowed using existing shares, managed funds or cash as securities. Nigeria’s banking sector felt the contagion effects of the crisis through its margin loans to private individuals and stock broking firms that are into speculations. At a time, banks were financing about 65% (N1 trillion) of the Nigerian capital market.
through margin facilities (Olisaemeka, 2009) which represents 20% of total credit. And this represents total exposure of banks to capital market in term of trapped funds. However, table 2 shows that credit to private sector increased from N1,507 billion in 2004 to N4,600 billion in 2007 and later rose to N 7,400 billion and N10,206 billion in 2008 and 2009 respectively.

Figure 1 depicts that in 2007 when the world economy started experiencing financial crisis Nigeria’s banking sector was yet to experienced the full impact because the margin loans were still performing until 2008 when the margin loans became doubtful and toxic. Before then the Nigerian capital market had experienced 45.77 percent fall in its All Share Index. This resulted banks being violent on the borrowers of funds (investors and stock broking firms) used to acquire shares. These made banks to bring about suicidal pressure on these borrowers, compelling them to sell their shares at any price, just to have a moment of respite. Hence, the prime lending rate moved from 16.46 percent in 2007 to 19.03 percent in 2009. This further increased the supply of shares at ridiculous prices, leading to greater market crash. The rising interest rate is an indication of fewer funds to lend out.

4.2 Effects On Capital Markets
The contagion and interdependence significantly affect financial markets. The All Share Index (ASI) and the Market Capitalization (MC) of listed equities capture activities and performance of the Nigerian Stock Exchange (NSE). The index grew over the years from 18.91 percent in 2004 to 74.73 percent in 2007 and fell by 45.77 percent in 2008 and latter fell to 33.78 percent in 2009 while the market capitalization was about N2,111.5 billion in 2004 and increased to N13,294.4 billion in 2007, after which it fell precipitously to N9,562 billion in 2008 and further fell to N7,030.8 billion because of the meltdown (see Table 2 above).
The global crisis also induced massive withdrawal of foreign investors portfolio investment from the Nigerian financial system in order to service financial problems at the foreign investors’ home. Table 2 shows that portfolio investment stood at N23,541 million in 2004 and rose to N360,292 million in 2007 and fell to N157,157 million in 2008 and further fell to N107,837 million in 2009. According to Ajakaija and Fakiyesi, (2009), evidence on the foreign portfolio withdrawals shows that the total financial inflows to Nigeria from 2007 and 2008 increased by 21%, while between 2008 and 2009, it fell by 38.6%.

4.3 Effect On The Oil Sector In Nigeria
Oil sector have been one of the main drivers of growth in Nigeria. Strong growth in Nigeria has been an important factor of the increase in the prices and demand for oil. The changing international oil market posed grave concerns for Nigeria’s fiscal outlook. The global financial crisis led to slow growth in Nigeria, resulted from lower demand for oil from US and Europe. As a country whose earnings and expenditures are tied to the prospects from oil, how can we say that the financial crisis has not and will not affect Nigeria? As observed from table 3 below, the price of crude oil was $37 per barrel in 2004, in 2007 it was $64 per barrel, 2008 it sold for $97 per barrel and moved as high as hitting $147 per barrel the same year. Consequent upon the global financial crisis, oil price declined to as low as $40 per barrel in the month of December, 2008 and later fell to $35 per barrel in 2009. The global economic crisis resulted in about a 71% decline in basket price of crude oil prices. Hence, government projects financing were in a state of limbo with a deficit financing of $12.7 billion(N1.9 trillion) for 2009 budget. Also this impacted on the contribution of oil sector to economic growth(GDP) of Nigeria. As shown in table 1 above, oil sector contribution to GDP stood at 3.30 percent of the total real GDP before the crisis and declined by 5.1 percent in 2007 and later fell by 4.5 percent in 2008 in the wake of the crisis. Consequently, this led to a fall in real GDP growth, from 6.58 percent as it were in 2004 to 6.45 percent in 2007 and later declined to 5.98 percent in 2008.

4.4 Effect On Foreign Exchange Rate
In most countries, the impact of the financial crisis can manifest itself through currency fluctuations, especially against the US dollar or the Euro. A reflection of the crisis period can also be seen in the depreciation of the Nigerian naira. Table 2 above reveals that in 2004 the exchange rate stood at N133 per dollar and dropped to N116 per dollar in 2007. This shows that the Naira appreciated from 3.03 percent in 2004 to 8.03 percent in 2007. Also, from 2007 to 2008 the exchange rate moved to N131 per dollar and
moved further to N148 per dollar. This depicts that naira depreciated from 12.37 percent in 2008 to 12.84 percent in 2009. There is no doubt that the depreciation of Nigeria currency is attributable to the impact of the financial crisis on commodity(oil) prices and the decline in foreign exchange reserves, which dropped from $52.00 billion in 2007 to $42.41 billion in 2009. The depreciation of Naira as a result of the global financial crisis imposed higher importation cost on manufacturing and was worsened by high cost of production as a result of lack of basic infrastructures like good roads, power supply. This rising production cost in Nigeria was eventually passed on to the consumers as prices increases thereby fueling inflation and unemployment in Nigeria (see table 1 and 2). An evidence of employment crisis that resulted from the global financial crisis are the case of many quoted and unquoted companies like Dunlop Nigeria Plc and Michelin Nigeria. These companies closed down due to high cost of doing business compounded by the financial crisis. Dunlop Nigeria PLC, manufacturers of tires with a staff strength of over 5,000 closed down in 2009 due to financial losses in operation, the decline in activity in the manufacturing sector has caused large job losses with damaging effects on living standards, leaving the faith of these worker in state of sixes and sevens. According to ILO(2009), economic and financial crises are detrimental for both women and men, whether they are at work, looking for work or outside the labour force.

4.5 Effect On Capital Flows
Official Development Assistance (ODA) as Aid, which have become a major source of external financing for Nigeria, has been adversely affected by the slowdown in developed countries. The total volume of aid to Nigeria stood at US$6,409 million in 2005 and fell to US$1,956 million in 2007 and later fell to US$1,290 million in 2008. This is attributed to aid donors budget decrease. The decline in the volume of Aid had a direct negative impact on the nation since it is used for education and healthcare improvement.

Table 3: Nigeria’s External Indicators

<table>
<thead>
<tr>
<th>Nigerian Key Indicators/Year</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Export of Goods and services (% of GDP)</td>
<td>4.7</td>
<td>-</td>
<td>-</td>
<td>42</td>
<td>37</td>
<td></td>
</tr>
<tr>
<td>Import of Goods and services (% of GDP)</td>
<td>31</td>
<td>-</td>
<td>-</td>
<td>29</td>
<td>29</td>
<td></td>
</tr>
<tr>
<td>Current Account (% of GDP)</td>
<td>-</td>
<td>32.84</td>
<td>23.47</td>
<td>18.78</td>
<td>15.43</td>
<td>13.65</td>
</tr>
<tr>
<td>External reserves (US$ billions)</td>
<td>16.96</td>
<td>28.29</td>
<td>45.01</td>
<td>52.00</td>
<td>52.82</td>
<td>42.41</td>
</tr>
<tr>
<td>Aid Flow (US$ million)</td>
<td>-</td>
<td>6,409</td>
<td>11,428</td>
<td>1,956</td>
<td>1,290</td>
<td>1,657</td>
</tr>
<tr>
<td>Oil Price (US$)</td>
<td>37</td>
<td>50</td>
<td>58</td>
<td>64</td>
<td>45</td>
<td>35</td>
</tr>
<tr>
<td>Foreign direct investment(N)</td>
<td>248,224</td>
<td>654,193</td>
<td>624,520</td>
<td>759,380</td>
<td>650,431</td>
<td>861,636</td>
</tr>
</tbody>
</table>

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Nigeria is considered as one of the promising and fast growing economy in the world. Due to the liberalized rules for Foreign Direct Investment (FDI) in Nigeria, the telecommunication, services, construction activities, oil and gas etc have become very attractive investment avenues for both the domestic as well as foreign investors. The overall foreign investment in Nigeria met slight setback during the crisis. Table 3 shows that the foreign investment in Nigeria grew at a faster rate since 2004. However, 2008 was slightly hit by the crisis, the foreign investment declined to N650,431.55 million in 2008 from N759,380.43 million in 2007.

Remittances, which have become a major source of external financing for African countries, have been adversely affected by the slowdown in developed countries. Nigerian economy experienced constant increase in the workers’ remittance, prior to 2008 when workers’ remittance-to-GDP ratio slightly declined from 5.557 percent in 2007 to 4.818 percent in 2008 (see table 3).

### 4.6 Effect On Employment And Inflation

According to International Labour Organization (ILO)(2009), economic and financial crises are detrimental for both women and men, whether they are at work, looking for work or outside the labour force. Also, that over 51 million people throughout the world have been fired as at 2008 due to the economic and financial crisis and additional 40 million people are at risk of being out of job in 2009. From table 1 above, it is evident that employment crisis was compounded by the global financial crisis. Unemployment stood at 11.80 percent in 2004 and rose to 12.70 percent in 2007 and thereafter rose to 14.90 percent in 2009. In the same vein inflation rate in 2004 stood at 10.00 percent and declined to 6.6 percent in 2007 and later rose to 15.1 percent in 2008 (see table 1).

### 4.7 Global Financial Crisis and Trade Flows

The global financial crisis will adversely impact on the flow of goods and services. The global economy has recorded a decrease in volume and value of tradable goods and services. Indeed, world trade in volume increased by 6.3% in 2007, by 4.4% in 2008, and by only 2.1% in 2009. Trade was part of the main drivers of growth in Nigeria. Due to the economic downturn of 2007 and 2008 in the industrialized countries and lower primary commodity prices, Nigerian trade (export and import) was slightly hit. As seen from table 3, Nigeria’s average export-to-GDP ratio was 47 percent in 2005 and fell by 42 percent in 2008 and later fell by 37 percent in 2009. This is attributed to the downturn in advanced economies where major percent of Nigerian exports are destined for. Furthermore, Nigerian exports tend to be concentrated in commodities with oil, minerals and agricultural commodities. Commodity prices were in a boom phase in the pre-crisis period, reaching record levels by June 2008. Having benefited from the primary...
commodity boom, the prices dropped hastily since then. Between January 2003 and July 2008, energy, food and mental price indices rose, by 329, 102 and 230 percent respectively and then fell by 64, 30 and 46 percent respectively between June 2008 and February 2009 (IMF 2009a). However, within the same period import-to-GDP witnessed a fall between 2000 and 2008 by 31 and 29 percent respectively. Losses in export growth rates are not compensated for by decreasing import growth rates in value terms, implying that the trade balance deteriorated.

Under the effect of the crisis, current account dropped since 2006. From an overall current account position of 32.84 percent of GDP in 2005 to 18.78 percent of GDP in 2007 and also fell to 13.65 percent of GDP in 2009 (see table 3). This is a direct result of the decline in oil revenue occasioned by the crisis.

In 2009, Nigeria was faced with current account and budget problems. This is because exports fell more than imports (causing current account drop) while governments try to keep up with expenditure levels in the context of declining revenue. Thus, Nigeria was faced with the threat of structural macroeconomic imbalances in the medium term of the crisis persists.

V GOVERNMENT RESPONSES TO THE EFFECTS OF GLOBAL FINANCIAL CRISIS IN NIGERIA

The world Bank Group extended its helping hand in solving the problem posed by the financial crisis by increasing lending for crisis hit developing countries, from US$13.5 billion in 2008 to US$35 billion in 2009. Also, grants and interest free long term loans were granted to 78 world’s poorest nations out of which 39 are in Africa.

In response to the challenges posed by the crisis, Nigerian government initiated a lot of policies to reduce the effects of the crisis. Some of which are; the inauguration of Presidential Steering Committee on Global Economic Crisis on January 16, 2009, setting up of the Presidential Advisory Team on Capital Market in August 2008 which deliberated on measures to reverse the declining fortunes of Nigeria capital market. The regulators (Security Exchange Commission (SEC) and Nigerian Security Exchange (NSE)) of Nigerian capital market and its operators reduced fees by 50 percent; 1.0% maximum downward limit on daily price movement and 5.0% on upward movement were set. And was harmonized to 5% either way from end-October 2008; Strict enforcement of NSE’s listing requirement with zero tolerance for infractions; NSE reviewed the trading rules and regulations and de-listed about 9 NSE moribund companies. Some other measures include; reduction of the Monetary Policy Rate (MPR) from 10.25 percent to 9.75 percent, reduction of Cash Reserve Requirement (CRR) from 4.0 percent to 2.0 percent, reduction of Liquidity ratio from 40.0 percent to 30.0 percent, expansion of lending facilities to banks up to 360 days, introduction of an expanded discount window facility as well as stoppage of liquidity mopping up in 2008.

As rightly stated by CBN, these policy adjustments were designed to inject about N150 billion into the system and improve the liquidity in the economy. These were all part of the government’s initiative to forestall any unforeseen development in the domestic economy, in view of the high degree of uncertainty believed to be emanating from the global financial markets.

VI LESSONS OF THE FINANCIAL CRISIS

The following are some of the key lessons Nigeria should learn from the recent global financial crisis:

- It is very clear that countries which themselves to capital inflows become more vulnerable to large capital outflows when investor sentiment becomes unfavorable. This could result in sharp currency depreciation, financial instability and severe recession. Therefore, capital account liberalization needs to be done in an orderly and properly structured way;
The development of a sound financial system is indispensable to the effective management of capital inflows. Therefore, signs of banking system distress must continuously be addressed promptly and firmly;

It is necessary to watch the composition of capital inflows, including the currency composition and the balance between FDI and portfolio flows and the extent of short-term borrowing. To this end, it is desirable to encourage long-term inflows such as FDI in particular. Policies should, therefore, aim to shift the structure of capital inflows in favour of high quality FDI, and gain the confidence of long-term investors;

Short-term capital flows (bank loans and portfolio flows) are, or can become very volatile and vulnerable to reversals. Therefore, as the country takes measures to internationalize the domestic money and capital markets, it is desirable for it to avoid giving too much exposure to foreigners in the economy, especially in large holdings of short-term treasury bills and similar financial instruments. Such exposures create potential vulnerability both for government finance and, especially the balance of payments;

Efficient debt management is indispensable in the management of capital inflows. Thus, the example, long-term investment cannot indefinitely be financed with short-term capital without resulting in mis-investment, high speculation and eventual crisis in the domestic financial system;

The management of capital inflows has to be an integral part of macroeconomic management. Sound macroeconomic policies are required to ensure safety, viability, soundness and efficiency of the financial sector;

Exchange rate arrangement need to be flexible, given the recent context of economies open to capital inflows moving at high speed from country to country. Exchange rate flexibility can help to discourage excessive reliance on short-term foreign borrowing, unlike the case under exchange rate peg and high nominal interest rates which encourage large short-term capital inflows in to an economy. The exchange risk associated with greater nominal exchange flexibility can play a useful role in moderating the volume of short-term capital flows. The benefits of exchange rate flexibility can, however, be realized only with advance planning, and not through sudden introduction in a setting where banks and corporations are already burdened by heavy debts denomination in foreign currency;

In a world of financial openness and potential capital reversals, a higher level of reserves is needed as a buffer against sudden financial shocks and invariably, as a bolster to investors confidence. Also, enough reserves will give a country enough time to adjust to domestic and international pressure without unduly jeopardizing economic growth;

There is a compelling need for Nigeria to minimize its vulnerability to external shocks and shifts in investor sentiment, which is worsened by large capital inflows. In this regard, Nigeria should watch out for early warning signals for possible currency or financial crisis and address them with appropriate macroeconomic policies to prevent loss of reserve. Such signals include overheating of the domestic economy, as manifested by high inflation, appreciation of the real exchange rate, widening of current account deficit, rapid expansion of domestic credit, and inflation of asset prices;
• The vulnerability of Nigerian economy should be weighted against its resilience, that is, its coping ability or capability to recover from shock. Resilience can be nurtured and depends among others; on good economic management and good governance. On the issue of economic management, it is measured with fiscal and current account balances. The country should have a leeway to use countercyclical fiscal and monetary policy. While that of good governance looks at improved governance. The evidence points to a considerable improvement in political governance as a result of entrenchment of democracy in Nigeria. This has a powerful positive effect on the growth-enhancing policies;

• Regulating Inconsistencies and Pronouncements that is capable of provoking panic selling of stocks among investors. This contributed to the crash of the market;

• Lack of Infrastructure and High Production Costs leads to the crash of the share prices. Evidently, high production costs reduce profitability or increase loses which also impact negatively on the share prices;

• There is an inherent danger in letting capital flow as it will. This derives from the upward pressure that capital inflows exert on a country’s currency. This is not a problem if economic growth keeps up with that pressure. But this is often not the case and so the country’s currency becomes overvalued and its economy lose its competitiveness. This means that at some point, capital flows must reverse and exchange rate must fall and this seldom happens smoothly. Therefore, an appropriate policy response to capital inflows is necessary; and

• Financial and capital account liberalization has to be predicated on meeting the prerequisite of macroeconomic stability, adequate prudential supervision and regulation of domestic financial institutions and markets; adequate disclosure practices in financial and corporate sectors; and avoidance of implicit government guarantees that encourage excessive and unsustainable capital inflows. Even then, capital account liberalization should be done gradually and in a sensible manner, reflecting appropriate timing, speed and scope.

VII CONCLUDING REMARKS
The global financial crisis had a significant impact on Nigeria economy, although Nigeria’s growth outlook was still commendable compared to some industrialized countries. The financial crisis affected all the drivers of Nigerian growth: prices and demand for primary commodities, capital flows, especially foreign direct investment. And also the country faced the risk of current account and budget problems. With the fall in the price of crude oil, to about US$35 per barrel in 2009, some of the government projects financing were in the state of sixes and sevens with a deficit financing of US$12.7 billion(1.9 trillion) built into 2009 budget. The fall in oil price led to naira depreciated by 12.37 percent in 2008, which in turn led to rising production cost and was eventually passed on to the consumers as price increase thereby fueling inflation. The market capitalization nose-dived from an all time high of N13.3 billion in 2007 to N7 billion in 2009 and besides, the All-Share Index plummeted by 45.8 percent in 2008 and later by 33.78 percent in 2009. Had it being that the crisis were to last beyond 2009, it could have threaten the gains achieved in the last decade.

References


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