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Capital Flight and Domestic Investment in Nigeria

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ABSTRACT
This study examined the effect of capital flight on domestic real investment in Nigeria. The purpose was to examine the relationship between capital flight and domestic real investment. Time series data were sourced from Central Bank of Nigeria Statistical bulletin and publications of Nigeria Bureau of Statistics from 1986-2019. Domestic real investment was modeled as the function of external debt servicing, value of import, profit repatriation, Nigeria investment abroad and depreciating naira exchange rate. Ordinary least square methods of cointegration, granger causality test, unit root test and Vector error correction model. The study found that capital flight measures as formulated in the regression model explain 44.4 percent of the variations in domestic real investment. The estimated beta coefficient proved that, external debt have positive and no significant effect on domestic real investment. Importation has positive and no significant effect on domestic real investment. Profit repatriation negative positive and no significant effect on domestic real investment, Nigeria investment abroad have positive and no significant effect on domestic real investment while depreciating naira exchange rate have positive and no significant effect on domestic real investment. The study conclude that, capital flight have moderate effect on domestic real investment in Nigeria. We recommend that fiscal responsibility must be proper integrated in the process of external debt servicing, there need for economic diversification to reduce the growing importation to the country and The domestic economy should made more attractive for the investors by creating a wider menu of domestic financial assets on which domestic capital.
Keywords: Capital Flight, Domestic Investment, Nigeria external debt

INTRODUCTION

Investment is component of aggregate demand. It is the most volatile component of aggregate demand and fluctuation in its level is highly correlated with fluctuation in Gross National Product known as business cycle (Iyoha, 2004). Real investment can be private or public, while public investment is autonomous; the private investment is determined by monetary and macroeconomic variables in the economy. Unlike financial investment that is an avenue to increase wealth, real investment increases the productive capacity of the economy, create employment and expand production beyond national consumption, a prerequisite for economic growth, full employment, price stability and external balance. Domestic investment is a tool for measuring the level of Gross Domestic Product (Amer, Umer and Muhammad, 2014). Investment play key role in increasing capital formation and brings about long-run economic growth (Lucky and Kingsley, 2017). Through the control of monetary policy targets such as the price of money (interest rate both short term and long term), the quantity of money and reserve money amongst others; monetary authorities directly and indirectly control the demand for money, money supply, or the availability of money and hence affect output and private sector investment (Tobias and Mambo, 2012).

Investment is one of the leading factors that promote economic growth and development in developing countries like Nigeria. Long-term solutions to poverty and unemployment may be reached through investment. Conversely, capital flight shrinks the available capital for investment purpose in the economy

therefore lowering investment. Deprivation of capital in Africa through capital flight has witnessed increasing attention from policy makers and researchers including Ajayi (1997), Boyce and Ndikumana (2012), and Yalta (2010) among others. The striking paradox is that despite having massive capital inflows, the continent ranks high in capital flight.

Nigeria is trying to realize an increased and sustained level of growth and development has to have access to sufficient capital. There is a general consensus that the shortage of capital is a major impediment for the development of the African continent. The lack of sufficient domestic capital emphasizes the need of having a source of capital for Nigeria to fill the resource gap it faces (Olugbenga & Alamu, 2013). The low level of saving in Nigeria has meant that developmental objectives for them have been and are continually being funded externally (Al-Refai, 2015). Fofack (2009) argued that this need for capital has left no other alternative but the accumulation of huge sums of external debt. The existence of this external debt has been shown to have a compelling relationship with capital flight.

Capital flight affects private investment in various ways as noted by Ndikumana (2014). The leakages cause a depletion of private savings which reduces capital formation. Uncertainty in macroeconomic indicators causes high levels of capital flight by as private agents assume macroeconomic policy economic regulation failure by government. The loss of funds through capital flight minimizes the domestic tax base; as a result, it affects the redistribution of income. It negatively affects the country's balance of payment since the outflow tends to become export income affecting the current account. A negative effect on the current account is enough to cause a devaluation of the currency and a budget deficit that affect the domestic real investment.

The Nigerian capital market which is supposed to be an avenue for sourcing of long-term funds to finance long-term project is not developed as her foreign counterpart thereby increasing the rate of capital flight. It has not also been able to judiciously perform its primary obligation of meeting long-term capital needs of the deficits sectors through efficient accumulation of capital or mobilization of fund from the surplus units of the economy and effectively channel mobilized funds for economic use (Ojo, 2012) for instance the Nigeria capital market is very illiquid, few listed companies with low volume of equity transaction with low market capitalization. There has been a decline in the value of shares resulting from the global financial and economic crisis. This has equally reduced the propensity to invest in the sector thereby, affecting the rate of domestic investment in Nigeria. The poor functioning capital markets deter foreign and domestic investors because the markets are illiquid and trading is expensive (Geert, 1997). Nigeria's real domestic investment can adversely affect by high the factors affecting the financial market. From the above, this study examined the effect of capital flight on domestic real investment in Nigeria.

LITERATURE REVIEW

Capital Flight

Capital flight is as a term that is digested differently by academia and policy makers. It is therefore important to point out that because of this; the term is yet to be attached to a universally accepted definition. The elusiveness of its conceptualization is because it is not precisely clear what distinguishes capital flight from normal capital flows (Uguru, et al., 2014). This paradox has consequently lead to different measures and therefore different estimates of capital flight. The lack of cohesion in identifying a universally accepted definition is due to the asymmetry that exists between the ways the term is interchangeably used around the world. Some intellectuals consider outflows from developed countries as foreign direct investment, while the same activity is called capital flight when it is carried out by residents in a developing country (Ajayi, 1995).

This dichotomy is because outflows are seen as a portfolio decision involving rational investors. The view is that investors in developed countries are seeking better returns abroad, while investors in developing countries are fleeing the risk of capital loss due to macroeconomic mismanagement and the political instability that is consistent with most developing countries. 8 The fact that capital flight can manifest itself as both licit and illicit is also one of the reasons why it is inter alia perceived in different ways (Epstein, 2005).

Capital flight is considered to be licit when the transactions are reported and recorded accurately according to their fair value on the Balance of Payments statistics. On the other hand, it becomes illicit when flows are not recorded or are intentionally misquoted on the balance of payment with the sole purpose of hiding the origin, destination and the ownership of the flows. The norm in literature is for capital flight and illicit financial flows to be used synonymously.

Nigeria's External Debts

Nigeria is reported to have incurred her first official external debt, when she borrowed the sum of US$28million from the World Bank in 1958 for her railway lines extension programme. As the foreign exchange positions of the country worsened during the era of the international monetary crisis of the 1970s and the 1980s Nigeria had no other options than to obtain trade credits and medium-long-term capital from the world money and capital markets to proceeds with her development programmes. The foreign exchange problems of the Nigerian economy can be traced to 1964, when Nigeria's balance of payments position began to flash warning signals in the current account. This led CBN, for the first time into imposing qualitative and quantitative import restrictive measures in order to conserve foreign exchange (Onoh, 2007).

The adverse balance of payments position was worsened by the Nigerian-Biafra war, which lasted from July 1967 to January, 1970. During the war period exports of palm produce and crude oil, the major export products of the war-torn area were drastically reduced. As the balance of payments worsened, so also did the external reserves position. Reserves were partly applied to support normal imports and partly to finance the importation of arms. The depletion of the foreign exchange reserves coupled with the abolition of the convertibility of the Nigerian currency by Decree No. 51 of 1968, shook international confidence in the Nigerian economy and the currency. By 1968, the external reserve level of 1960 had dropped to 1/3. With the abolition of the convertibility of the Nigerian currency, international payments were settled at the CBN level only and deferred payments were imposed on all imports. With the end of the war in January, 1970, oil production resumed. It reached its peak production level by 1973, and at a time the barrel price of crude oil rose in the world oil market. The Israel-Arab war of 1973, which led to the boycott of oil exports to the western countries, accused by the Arab countries of complicity with Israel during the war.

Exchange Rate

Exchange rate arrangements in Nigeria have transited from a fixed regime in the 1960s to a pegged regime between the 1970s and the mid-1980s and finally, to the various variants of the floating regime from 1986 with the deregulation and adoption of the structural adjustment programme (SAP). A managed floating exchange rate regime, without any strong commitment to defending any particular parity, has been the most predominant of the floating system in Nigeria since the SAP.

Following the failures of the variants of the flexible exchange rate mechanism (the AFEM introduced in 1995 and the IFEM in 1999) to ensure exchange rate stability, the Dutch Auction System (DAS) was re-introduced on July 22, 2002. The DAS was to serve the triple purposes of reducing the parallel market premium, conserve the dwindling external reserves and achieve a realistic exchange rate for the naira. The DAS helped to stabilize the naira exchange rate, reduce the widening premium, conserve external reserves, and minimize speculative tendencies of authorized dealers. The foreign exchange market has been relatively stabilized since 2003.

As indicated by Mordi (2006), The conditions that facilitated the re-introduction of DAS in 2002 included, the external reserve position which could guarantee adequate funding of the market by the CBN; reduce inflationary pressures; instrument autonomy of the CBN and its prompt deployment of monetary control instruments in support of the DAS as well as the bi-weekly auctions as against the previous fortnightly auctions, thus assuring a steady supply of foreign exchange.

Domestic Investment

Domestic investment can generally be referred to as the investment in the companies and products of one's own country rather than in those of foreign countries. Domestic investment comprises of private and public investment. Private investment can be defined as investment by private businesses for the motive of generating profit whiles public investment refers to investment by the government sector primarily, but

not exclusively, on social and core economic infrastructure (Matsila, 2014). Domestic investment is one of the most important components of economic growth that countries consider as the main engine of the economic cycle. Recent theories on the nee-classical growth model as well as theories of endogenous growth has emphasized the role of domestic investment in economic growth such as capital spending on new projects in the sectors of public utilities and infrastructure like roads projects, housing, electricity extensions, as well as social development in the areas of health, education, and communication projects among others.

The determinants of investment are much clearer with the empirical literature than when theoretical arguments are postulated on investment in many countries including Nigeria. Nnanna *et al* (2004), authoritatively posit that the main determinants are in two forms: the finance and investment model. The finance model was however employed in the regression estimates carried out. The investment model starts with Cobb-Douglas production function measures capital or investment in physical assets first. Then it was specified to include the distortions and accompanying shocks, constraints and exogenous shocks in the macro economy as follows:

$$Y = f(A, K, L) = A, L \quad (1)$$

Where *Y* represents output, *K* is the capital stock, L labour supply and A the total factor productivity

$$K\ f(r\ pscner\ Y): \quad (2)$$

Where *r, psc, ner* and *Y* represent prime lending rate, (PLR), credit to the private sector, nominal exchange rate and national income respectively. The finance model of determinants of investment in Nigeria could be seen to be mainly from debt and non-debt sources that could be domestic or foreign with the following model

$$PSC\ f(SAVS, INV), \quad (3)$$

Where, *PSC, SAVS* and *INV* represent private sector credit, National Savings, and Investment respectively (Investment is divided into two parts namely *PUV* Public and Private Investment).

Theoretical Review

Theories of capital flight can be credited to the work of Pastor, (1989) and (Ajayi, 1992) who together have identified four main theories. These theories are namely the investment diversion thesis, debt-driven capital flight thesis sometimes called the debt overhang thesis, tax depressing thesis and austerity generating thesis.

The Investment Diversion Thesis

The investment diversion theory suggests that the existence of capital flight is due to the existence of macroeconomic and political uncertainty that occurs in developing countries at the same times as the existence of superior investment opportunities that exists abroad. These better opportunities may include higher interest rates, a wider variety of financial instruments to explore, political and economic stability, better tax rates and the ability to have secret accounts to store wealth. It is often the case that some of the dishonest and corrupt leaders who are in government often siphon the already scares capital from their countries to the more advanced countries. These funds become unavailable for the funding of investment projects in their resident 18 countries which leads to a decrease in investment spending, low economic growth and therefore a decline in employment, increase in the dependency ration and a high death rate. These factors often lead to the need to acquire external funding in order to boost the domestic economy. These borrowed funds are sometimes also wasted which creates a further dependency on foreign countries. The liquidity constraint (crowdingout effect) may also result in deterioration of the local currency if a floating exchange rate system is in use (Ajayi, 1992).Any attempts to protect the exchange rate leads to a loss in foreign exchange reserves. This theory therefore gives the one of the well-known negative consequences of capital flight.

The Debt Driven Capital Flight Thesis

The debt driven capital flight thesis is a continuation of the investment diversion theory. The thesis holds that countries that have a presence of huge sums of external debt give reason to its residents to move their resources outside to foreign countries. This theory postulates that external debt can be considered to be a fuel of capital flight and thus reduces the incentive for saving and investing inside the country. The

position taken here is that the existence of large sums of external debts creates an expectation of exchange rate devaluations, fiscal crisis, and the expropriations of assets in order to finance debt and the crowding out of domestic capital. So according to this theory capital flights results in sluggish growth, which creates the need to borrow in order to stimulate growth, the borrowing in turn leads to more capital flight and this cycle is perpetuated (Ajayi, 1992). The theory puts forward that a correlation between growth, capital flight and external debt exists.

The Keynesian Theory of Investment

In the General Theory, Keynes (1936) emphasized the central role of investment as the driving force of influencing aggregate output, employment, and short run fluctuations in economic activity. The theory emphasizes that investment is the result of firms harmonizing the expected return on new capital, referred to as the marginal efficiency of capital (MEC), and with the cost of capital, which depends primarily on the real interest rate. The financially viable while higher interest rates lead to some projects being postponed or cancelled since the cost of borrowing to finance investment become higher. To the Keynes since investment is volatile and dependent on firms expectations of the profitability of investment, so long as the expected yield on their investment exceeds the real interest rate, new investment will take place. Keynes rejected the notion that investment was based exclusively on technological conditions of capital productivity, but emphasized monetary factors and finance and uncertainty as the basic determinants of investment (Fazzari, 1989).

Empirical Review

Oyieke (2011) studied the correlation between private investment financing and public investment for Kenya using time series data from 1964 - 2006. The findings of the study were that local debt causes a significant negative effect on investment. Whereas, agricultural investment has a positive and significant effect on private investment. Other factors significant include; real exchange rate, depreciation, Investment in infrastructure Political risk, and tax (Oyieke, 2011). Kingori (2015) established that in the long run real GDP and trade openness were the core factors affecting private investment while in the short run, real GDP is an important variable in explaining disparities in private investment. Trade openness was no significant, inflation which was found to be significant (Kingori, 2015).

Altaleb and Alokor (2012) analyzed the trends and determinants of investments for the period 1980- 2010 in Jordan. The study concludes that private investments are significantly determined by exports and GDP. There exists a mixed impact of Gross Domestic Product on private investment as established by Oshikoya (1994). This is because the relationship between private investment and GDP in African countries is positive since slow economic growth discourages private investment. The outcome is in line with studies by Blejer and Khan (1984), Serven and Solimano (1992) who found that gross domestic product is the most important determinant of private investment. Using structural vector auto-regressions modeling techniques and time series data from 1965 to 2007.

Ndiaye (2011) found that an increase in one dollar of capital flight lowers domestic investment by 4.5 cents. The study suggests that repatriation of capital flight back to the country of origin will boost domestic investment. Kehinde (2012) established that public investment crowds in private investment. For instance a growth in public investment by ten per cent, private investment will rises by two per cent. Additionally, bank credit availability remains a major limitation to private investment in developing countries.

Mbaye (2012) on factors influencing domestic private investment in Kenya using data covering 1970-2010 established that there is a negative and significant influence on private investments. Conversely, real public debt, inflation, public investment, deposit rates, financial liberalization and foreign exchange reserves have a negative and insignificant impact on private investments.

Njuruet., et al (2013) looked at the impact of taxation on private investment from1964 to 2010. The results concluded that value added tax (VAT) and income tax have an adverse effect on private investment (Njuruet.,al 2013). Weeks (2015) examinied the impact of Capital Flight in Sub Saharan Africa for the period 1970 to 2005 found that in a situation of bad institutional quality and of poor governance, revenues, natural resources, aid and external debt are used in part to finance capital flight.

Similarly, a study on how capital flight affects current account sustainability in SSA established that corruption, macroeconomic instability, political instability, interest rate differentials, degree of financial market deepening, exports and debt-creating flows are the most significant determinants of capital flight.
Gankuo et al (2016) investigated the revolving door theory for Cameroon from 1970 to 2010 found that for every dollar rise in external debt causes a rise in capital flight by 47–62 cents. Further, institutional and political stability supports alleviation of illegitimate capital outflows caused by a rise in external debt. Similarly, external borrowing fuels capital flight. Salandy& Henry (2013) used two estimation techniques for econometric analysis. The Vector Error Correction (VECM) for the short-run and long run analysis and the Generalized Method of Momments (GMM) with an observation period of 1971-2008. Their results show that there is a negative relationship between capital flight and their two variables which are economic growth and investment. Their recommendation is that policy that is done with the aim of reducing capital flight will have a positive effect on domestic investment which would result in a positive and increased trajectory in economic growth.
Ifedayo & Olawale (2015) studied the impact of capital flight on economic growth in Nigeria for the period 1980 to 2012. This study employs the estimation techniques: co-integration, ordinary least squares (OLS) and error correction mechanisms (ECM). Their tests show that capital flight, foreign reserves, external debt, foreign direct investment and the current account balance co-integrate with Gross Domestic Product (GDP) in their study period. Their OLS and ECM results reflect that capital flight had a negative impact on the economic growth trajectory of Nigeria and advice that government should foster an environment that is conducive for profitable investments, and should also have an incentive attracting foreign investors to counter act the prevalence of capital flight in order to create sustainable growth and development in Nigeria.
Mohamed & Finnoff (2015) estimate the extent of capital flight for the period 1980 to 2000.They do so by adopting an indirect approach called the residual or broad measure. This technique estimates capital flight based on a comparison between the sources and uses of foreign exchange. Although the general perception is that political and economic instability may lead to capital flight, they find the contrary is true for South Africa. Their study shows that during the more politically and economically instable period (1980-1994) South Africa has a lower degree of capital flight than in the more politically and economically stable period (1994-2010). They suggest the easing of capital controls by the democratic government to reintegrate South Africa into the global economy, the lack of trust in the government by the wealth holders: which is fuelled by the persistently high levels of inequality and poverty could explain the paradox of a relatively higher degree of capital flight post democracy. Mohamed &Finnoff also point at the structural setting of the 28 economy being one of the other reasons why wealth holders would rather keep money abroad than invest it locally.
Ajayi (2014) employed a broad perspective on the analyses and implication of capital flight on economic growth and development in Africa. The study takes off by providing an overview of why capital flight limits and destabilizes economic growth and development in Africa because it creates a resource gap which aggravates sustainable growth and development. The analysis distinguishes between economic growth and development and dwells deeper on social development issues which is measured by the Human Development index (HDI) and economic transformation. The study goes further by dealing with the implications of inequality and poverty on development policy. His findings are that Africa has a substantial resources gap that needs to be closed to create an environment that is conjunctive for sustained growth and development. He also finds that because Africa is looking outside for resources it has become a net creditor to the rest of the world.
Boyce & Ndikumana (2012) investigated the determinants of capital flight using 30 sub-Saharan African countries, 24 of which were classified as severely indebted low-income countries for the period 1970-1996. Their empirical findings show that to a large extent capital flight shows a significant positive relationship with external borrowings in the Sub-Saharan region, their estimates show that for every dollar that a country received 80% of it flowed back as capital in the same year. Their study also finds that the presence of capital flight showed a likelihood of an increase in capital flight in the future. Another

empirical finding was that the growth rate differentials between an African Country and its OECD trading partners were negatively related to capital flight.

Ellyne & Mbewe (2015) study the role of exchange rates on capital flight using South Africa, Zambia and Nigeria as a case Study for the period 1970 to 2010. The Granger causality test is used to determine causality, The Johansen Co-integration test is Co-integration test is employed to determine whether a long run relationship exists and finally a Vector Error Correction Model (VECM) to establish the short run dynamics between capital flight and the real exchange rates. Their main finding was that in the larger economies of Nigeria and South Africa, the expectation of currency depreciation was a driver for capital flight. In Zambia however the opposite is true as the expectation of an appreciation in currency is the driver of capital flight. Macro-economic errors such as the unpredictability of inflation and foreign direct investment have an influence. Last but not least political factors are also found to have a contributory factor in all three countries.

Vukenkeng and Mukete (2016) investigated the relationship between capital flight and economic development using Cameroon as a case study. The observation period is 1970 to 2013 in order to evaluate capital flight in pre-debt crisis which was characterized by heavy borrowing and also during the debt relief. The technique of choice for calculating capital flight was the residual method. Their model of choice was the Fully Modified Least Squares technique which showed that capital flight had a significant negative relationship with economic development in Cameroon over their observation period. Explanatory variables such as exports and external debt also exhibited a negative relationship with economic development. The other explanatory variable which was the real interest rate was observed to have a positive relationship with economic development.

Ndiaye (2014) studied the impact of capital flight on economic growth in the Franc Zone. His observation period was for the period 1970 to 2010 where he uses the residual and the Morgan Guaranty Method as a measurement technique for capital flight. Capital flight was estimated to be in the 30 region of US$86.8 billion with the Residual method and US$80.1 billion with the Morgan Guaranty Method. This meant that capital flight represented 122.1% or 112.6% of GDP and was 5.3 or 4.9 times the amount of domestic investment. His econometric model shows capital flight to have a negative impact on economic growth in the Franc Zone. Capital flight was found to have reduced economic growth significantly and was thus a huge threat to the growth trajectory of these countries. His results show that domestic investment, credit provided to the private sector, the quality of regulatory institutions and domestic savings where important factors in explaining the extent of capital fight's influence on economic growth. The where seen as the important channels that affected the growth effect of capital flight in this zone. His view is that if capital flight was combated, there would be a significant increase in investment, credit to the private sector, the quality of the institutions, and domestic savings. His final recommendation is therefore that Combating capital flight in the Franc Zone would result in sustainable increases in economic growth for these countries.

Lucky and Kingsley (2016) examined factors that determine Nigerian capital formation. The objective was to test Jhingan's propositions for sources of capital formation in Nigeria. Time series data were sourced from Central Bank of Nigeria (CBN) Statistical Bulletin. Nigerian Gross Fixed Capital Formation (GFCG/GDP) was modeled as the function of Broad Supply (M2/GDP), Credit to Private Sector (CPS/GDP), Gross National Savings (GNS/GDP), Commercial Banks Lending Rate, Exchange Rate (EXR), Inflation Rate (INFR), External Debt (EXTD/GDP), Public Expenditure (PEX/GDP), Government Revenue (GR/GDP), Terms of trade (TT/GDP) and Operating Surplus (OPS/GDP). Cointegration Test, Augmented Dickey Fuller Unit Root Test, Granger Causality Test and Vector Error Correction Model were used to test the dynamic relationship between the variables. Findings proved that M2/GDP, GNS/GDP, EXR, EXTD/GDP, TT/GDP have negative and insignificant effect on capital formation while CPS/GDP, LR, INFR, PEX/GDP, GR/GDP and OPS/GDP have positive and insignificant effect. The model summary revealed 86.0% explained variation and f-statistics 12.38458 probability of 0.000004. The study concludes that the variables have significant impact on Nigerian Gross Fixed Capital Formation and confirm the Jhingans proposition.

Adesoye & Balogun (2015) examines the effect of exchange rate volatility on investment and growth in Nigeria over the period of 1986 to 2014. The vector error correction method, impulse responses function, co-integration and Augmented Dickey Fuller (ADF) test for stationarity were employed to capture the interactions between the variables. The results confirm the existence of long run relationship between exchange rate, investment, interest rate, inflation and growth. Finally the results show that exchange rate volatility has a negative effect with investment and growth while exchange rate volatility has a positive relationship with inflation and interest rate in Nigeria.

Akeju (2014) examined the impact of real exchange rate on terms of trade and economic growth which relies on cointegration techniques and error correction model using annual data covering from 1980-2012. It was revealed that a real exchange rate moves along the same direction with terms of trade in the long run. Rasaq (2013) examined the impact of exchange rate volatility on the macro economic variables in Nigeria and findings shows that exchange rate volatility has a positive influence on GDP, FDI and trade openness with a negative influence on the inflationary rate in the country. Ndikumana (2014) searched the implications of monetary policy for domestic investment through its impacts on bank lending to the private sector and interest rates in sub-Saharan African countries, the study based on a sample of 37 sub-Saharan African countries over 1980- 2012, the study found that monetary policy affects domestic investment negatively indirectly through the bank lending or quantity channel, as well as directly through the interest rate or cost of capital channel.

METHODOLOGY

This study is designed to examine the impact of capital market on capital formation in Nigeria. The research design adopted in this study is the descriptive research method which is largely quasi-experimental. Documentary data has been collected via Central Bank of Nigeria (CBN) Statistical bulletin.

Data Analysis Procedure

The main tool of analysis is the Ordinary Least Squares (OLS) using the multiple regression method for a period of 34years, annual data covering 1986– 2019. Statistical evaluation of the global utility of the analytical model, so as to determine the reliability of the results obtained were carried out using the coefficient of correlation (r) of the regression, the coefficient of determination (r^2), the student T-test and F-test.

(i) **Coefficient of Determination (r^2) Test:** This measure the explanatory power of the independent variables on the dependent variables.R^2 gives the proportion or percentage of the total variation in the dependent variable Y that is accounted for by the single explanatory variable X. The higher the R^2 value the better. For example, to determine the proportion of monetary policy to private sector funding in our model, we used the coefficient of determination. The coefficient of determination varies between 0.0 and 1.0. A coefficient of determination say 0.20 means that 20% of changes in the dependent variable is explained by the independent variable(s). Therefore, we shall use the R^2 to determine the extent to which variation in monetary policy variables are explained by variations in private sector funding variables over the periods covered in this study.

(ii) **Correlation Co-Efficient (R):** This measures the degree of the relationship between two variables x and y in a regression equation. That is, it tries to establish the nature and magnitude of the relationship when two variables are been analyzed. Thus correlation co-efficient show whether two variables are positively or negatively correlated. That is, it takes the value ranging from – 1, to + 1.

(iii) **F-Test:** This measures the overall significance. The extent to which the statistic of the coefficient of determination is statistically significant is measured by the F-test. The F-test can be done using the F-statistic or by the probability estimate. We use the F-statistic estimate for this analysis.

(iv) **Student T-test:** measures the individual statistical significance of the estimated independent variables. This is a test of significance used to test the significance of regression coefficients

(Gujurati, 2003). Generally speaking, the test of significance approach is one of the methods used to test statistical hypothesis. A test of significance is a procedure by sample results are used to verify the truth or falsity of a null hypothesis (Ho) at 5% level of significance.

(v) **Durbin Watson Statistics:** This measures the colinearity and autocorrelation between the variables in the time series. It is expected that a ratio of close to 2.00 is not auto correlated while ratio above 2.00 assumed the presence of autocorrelation.

(vi) **Regression coefficient:** This measures the extent in which the independent variables affect the dependent variables in the study.

Model Specification

From theories, principles and empirical findings, the model below is specified in this study.

DRI = f (EXDS, IMP, PR, NFIA, NER) (5)

It is empirically stated as

DRI = $\beta_0 + \beta_1 EXDS + \beta_2 IMP + \beta_3 PR + \beta_4 NFIA + \beta_5 NER + + \mu$ (6)

Where

DRI	=	Domestic real investment proxy by gross fixed capital formation to gross domestic products
EXDS	=	External debt servicing as percentage of gross domestic product
IMP	=	Import measures as balance of trade as percentage of gross domestic product
PR	=	Profit repatriation as percentage of gross fixed investment
NFIA	=	Nigeria investment abroad as percentage of gross domestic products
NER	=	Nigeria naira exchange rate
β_0	=	Regression Intercept
β_1 - β_6	=	Coefficient of the independent variables to the Dependent variable
μ	=	Error term

Estimation Procedure

Unit Root Test

Most of time series have unit root as demonstrated by many studies including Nelson and Plosser (1982) Stock and Watson (1988) and Campbell and Peron (1991). Therefore, their means of variance are not independent of time. Conventional regression technique based on non-stationary time series produce spurious regression and statistic may simply indicate only correlated trends rather true relationship Granger and Newbold (1974). Spurious regression can be detected in regression model by low Durbin Watson and relatively moderate R^2.Therefore, to distinguish between correlation that arises from share trend and one associated with an underlying causal relationship; we use the Augmented Dickey fuller (Dickey and Fuller, 1979, 1981)

$$X_t = \mu + \Theta X_{t-1} + \varepsilon_t \quad (7)$$

The null hypotheses for the ADF statistic test are H_0.

Non stationary (unit root) and H_a: Stationary respectively

Co-integration

To search for possible long run relationship amongst the variables, we employ the Johansen and Juselius (1990) approach. Thus, the study constructed a p-dimensional (4x1) vector auto regression model with Gaussian errors that can be expressed by its first differenced error correction form as

$$\Delta Y_t = \Gamma_1 \Delta Y_{t-1} + \Gamma_2 \Delta Y_{t-2} + ... + \Gamma_{k-1} \Delta Y_{t-k+1} - \Pi Y_{t-1} + \mu + \varepsilon_t \qquad \textbf{(8)}$$

Where Y_t are the data series studied, ε_t is i. i. d, N(0,$\sum$) Γ_i + -1 + A_1+A_1 + A_2 + A_3 + ……. + A_i for i = 1,2,3……..,k-1, $\Pi = I - A_1 - A_2$ - ……-A_k. The Π matrix conveys information about the long term relationship among the Y_t variables studied. Hence, testing the co-integration entails testing for the rank r of matrix Π by examine whether the eigen values of Π are significantly different from zero.Johansen and Juselius (1990) proposed two tests statistics to determine the number of co-integrating vectors (or the rank of Π), namely the trace and the maximum eigen-value (λ-trace) is computed as;

$$\lambda trace = -T \sum_{j=r+1}^{n} In(1 - \lambda_j) \qquad (9)$$

The trace tests the null hypothesis that "at most" r co-integration vector, with "more than" r vectors being the alternative hypothesis. The maximum eigenvalue test is given as:

$$\lambda_{\max} = -TIn(1 - \lambda_{r+1}) \qquad (10)$$

It tests the null hypothesis of r co-integrating vectors against the alternative hypothesis of r + 1 co-integration vectors. In the equation (3) and (4), is the sample size and λ is the largest canonical correlation.

Granger Causality

In case we do not find any evidence for co-integration among the variables, the specification of the Granger causality will be a vector autoregression (VAR) in the first difference form. However, if will find evidence of co-integration, there is the need to augment the Granger-type causality test model with a one period lagged error term. This is a crucial step because as noted by Engel and Granger (1987).

$$\boldsymbol{Y_t = \alpha_o + \sum_{i=1}^{n} \alpha_1^{y} Y_{t-1} \sum_{i=1}^{n} X_{a1} X \mu} \qquad (11)$$

and

$$\boldsymbol{X_t = \beta_o + \sum_{i=1}^{n} {}^{y}_{\beta 1} Y_{t-1} \sum_{i=1}^{n} X_{\beta 1} X Y_t} \qquad (12)$$

Error Correction Model (ECM)

Co-integration is a prerequisite for the error correction mechanism. Since co-integration has been established, it is pertinent to proceed to the error correction model.

A-Priori Expectation of the Result

The explanatory variables are expected to have positive and direct effects on the dependent variables. That is a unit increase in any of the variables is expected to reduce domestic real investment. This can be express mathematically as $a1_,$ a_2, $a_{3,}$ $a_{4,}$ $a_5 > 0$.

ANALYSIS AND DISCUSSION OF FINDINGS

Table 1: Presentation of Unit Root Test at Difference

Null Hypothesis: D(DRI) has a unit root		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-8.927857	0.0000
Test critical values:	1% level	-3.653730	
	5% level	-2.957110	
	10% level	-2.617434	
Null Hypothesis: D(EXDS) has a unit root			
Augmented Dickey-Fuller test statistic		-8.521190	0.0000
Test critical values:	1% level	-3.653730	
	5% level	-2.957110	
	10% level	-2.617434	
Null Hypothesis: D(IMP) has a unit root			
		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-7.645480	0.0000
Test critical values:	1% level	-3.661661	
	5% level	-2.960411	
	10% level	-2.619160	
Null Hypothesis: D(NER) has a unit root			
		t-Statistic	Prob.*
Augmented Dickey-Fuller test statistic		-4.953322	0.0003
Test critical values:	1% level	-3.653730	
	5% level	-2.957110	
	10% level	-2.617434	
Null Hypothesis: D(PR) has a unit root			
Augmented Dickey-Fuller test statistic		-6.764556	0.0000
Test critical values:	1% level	-3.653730	
	5% level	-2.957110	
	10% level	-2.617434	
Null Hypothesis: D(NFIA) has a unit root			
Augmented Dickey-Fuller test statistic		-6.428630	0.0000
Test critical values:	1% level	-3.653730	
	5% level	-2.957110	
	10% level	-2.617434	

Source: Extracts from E-Views 9 Output

Using the Augmented Dickey Fuller test, the results of the stationarity tests for all the study variables are presented in table 1 above presents the stationarity test results of the study's time series data. It indicates that the absolute values of the ADF test statistics for all the study variables are higher than their corresponding Mackinnon's critical values at 1%, 5% and 10% respectively. All the study variables are integrated of order I(1) and as such, deemed fit for employment in subsequent econometric estimations.

Table 2: OLS Regression Results

Variable	Coefficient		Std. Error	t-Statistic	Prob.
EXDS	0.006813		0.022481	0.303058	0.7641
IMP	0.175593		0.128545	1.366001	0.1828
NER	0.011043		0.018677	0.591254	0.5591
NFIA	6.665783		0.169649	3.072286	0.0047
PR	-4.002220		0.088813	-0.978822	0.3360
C	22.54468		0.928112	3.803012	0.0007
R-squared	0.444727	Mean dependent var			35.90518
Adjusted R-squared	0.345571	S.D. dependent var			4.112319
S.E. of regression	3.326734	Akaike info criterion			5.400644
Sum squared resid	309.8805	Schwarz criterion			5.670002
Log likelihood	-85.81095	Hannan-Quinn criter.			5.492503
F-statistic	4.485128	Durbin-Watson stat			2.268233
Prob(F-statistic)	0.003974				

Source: Extracts from E-Views 9 Output

To capture the short run relationships and the percentage of variation accounted for by the variations in the predictor variables in the short run, the Ordinary Least Squares test was implemented, the results of which are shown in table 2. The R^2 value of 0.444727 from the effect of capital flight on domestic real investment implies that variations in all the explanatory variables account for 44.4 percent of the variations in domestic real investment. The short run the probability of f-statistics is significant at 0.05 level (0.003974<0.5) for both models which implies a good line of fit while the Durbin-Watson value of 2.268233 proved the presence of serial autocorrelation among the variables in the time series.

Table 3: Presentation Co-integration Test

Series: DRI EXDS IMP NER NFIA PR

Unrestricted Cointegration Rank Test (Trace)

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05Critical Value	Prob.**	
None *	0.768118	119.8041	95.75366	0.0004	
At most 1 *	0.671947	73.03532	69.81889	0.0271	
At most 2	0.567868	37.36877	47.85613	0.3303	
At most 3	0.212425	10.52003	29.79707	0.9716	
At most 4	0.085811	2.878533	15.49471	0.9721	
At most 5	0.000236	0.007547	3.841466	0.9303	
Unrestricted Cointegration Rank Test (Maximum Eigenvalue)					
None *	0.768118	46.76880	40.07757	0.0076	
At most 1 *	0.671947	35.66655	33.87687	0.0303	
At most 2	0.567868	26.84874	27.58434	0.0619	
At most 3	0.212425	7.641493	21.13162	0.9243	
At most 4	0.085811	2.870986	14.26460	0.9550	
At most 5	0.000236	0.007547	3.841466	0.9303	
Normalized cointegrating coefficients (standard error in parentheses)					
DRI	EXDS	IMP	NER	NFIA	PR
1.000000	-0.783987	8.556499	1.022777	-74.26802	222.4927
	(0.23859)	(1.16753)	(0.20814)	(18.5448)	(34.8247)

Source: Extracts from E-Views 9 Output

The results of Johansen Co-integration tests for all the time series variables of this study are presented in table 3, the Johansen's co-integration results confirm the prevalence of one (1) co-integrating equations, thus indicating the prevalence of a significant long run relationship among the time series variables under study, in which case we proceed to correct for errors between the long and short run variables.In the long run model one found that all the independent variables have positive long run effect on domestic real investment except external debt servicing and Nigeria investment abroad that have negative long run relationship with domestic real investment.

Table 4: Presentation of Estimated Error Correction

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.908119	0.586500	1.548370	0.1399
D(DRI(-1))	-0.566164	0.301973	-1.874885	0.0781
D(DRI(-2))	-0.837038	0.218845	-3.824797	0.0014
D(EXDS(-1))	0.001123	0.018817	0.059691	0.9531
D(EXDS(-2))	-0.052912	0.025715	-2.057620	0.0553
D(IMP(-1))	-0.181152	0.115324	-1.570802	0.1347
D(IMP(-2))	0.137224	0.130105	1.054717	0.3063
D(NER(-1))	0.006167	0.025438	0.242421	0.8114
D(NER(-2))	0.002667	0.026925	0.099057	0.9223
D(NFIA(-1))	0.716245	2.411085	0.297063	0.7700
D(NFIA(-2))	3.087808	1.971688	1.566073	0.1358
D(PR(-1))	-1.107026	5.014947	-0.220745	0.8279
D(PR(-2))	3.667172	5.467620	0.670707	0.5114
ECM(-1)	-0.019538	0.413028	-0.047305	0.9628
R-squared	0.772506	Mean dependent var		0.285161
Adjusted R-squared	0.598539	S.D. dependent var		4.179670
S.E. of regression	2.648278	Akaike info criterion		5.088148
Sum squared resid	119.2274	Schwarz criterion		5.735755
Log likelihood	-64.86630	Hannan-Quinn criter.		5.299252
F-statistic	4.440546	Durbin-Watson stat		1.973817
Prob(F-statistic)	0.002508			

Source: Extracts from E-Views 9 Output

To evaluate and correct for the errors existent between the long and short run dynamics in the study, the error correction estimation was executed. The results are shown in table 4 above. From the table, the ECM coefficient stands at stands at -0.019538from with the expected negative sign, which implies that approximately 0.9 percent disequilibrium in domestic real investment is offset within the year. On the other hand, the coefficient of determination (R^2) of 0.772506indicates that about 77 percent of the variations in dependent variables the long run is accounted for by variations in the study's explanatory variables. The profitability of ECM f-statistics of 0.002508confirms its goodness of fit and its Durbin-Watson value of 1.973817within acceptable range also.

Table 5: Granger Causality Test

Null Hypothesis:	Obs	F-Statistic	Prob.
EXDS does not Granger Cause DRI	32	0.70677	0.5021
DRI does not Granger Cause EXDS		0.20525	0.8157
IMP does not Granger Cause DRI	32	0.22126	0.8029
DRI does not Granger Cause IMP		5.76559	0.0082
NER does not Granger Cause DRI	32	1.03236	0.3698
DRI does not Granger Cause NER		0.96440	0.3940
NFIA does not Granger Cause DRI	32	0.00317	0.9968
DRI does not Granger Cause NFIA		0.96866	0.3924
PR does not Granger Cause DRI	32	3.53478	0.0433
DRI does not Granger Cause PR		3.00608	0.0463

Source: Extracts from E-Views 9 Output.

The output of the Pair-Wise Granger Causality tests is presented in table 5, the results shows the Pairwise Granger Causality Output of employed variables of the study, the results provide compelling evidence to conclude the prevalence of causality between the dependent and the independent variables.

DISCUSSION OF FINDINGS

The objective of research question one and hypothesis was to examine the relationship between capital fight through debt servicing and domestic real investment in Nigeria. The results presented in table 1 found that capital flight measured by external debt servicing have positive and no significant effect on Nigeria domestic real investment. The estimated model as presented in chapter three of the study indicates that a unit increase in capital flight measured by external debt servicing increases domestic real investment by 0.06 percent. Theoretically we expected a negative relationship between capital flight measured by external debt servicing and domestic real investment, therefore the positive effect of external debt servicing on domestic real investment in Nigeria contradict our a-priori expectations. The positive effect of external debt servicing on domestic real investment could be traced effectiveness of debt management policies or to macroeconomic and financial sector reforms directed toward attracting foreign domestic and real investment. Empirically, the positive effect of external debt servicing confirm the findings of Oyieke (2011), Kingori (2015), Blejer and Khan (1984), Fofack, and Ndikumana (2014), Ghura and Goodwin (2010).

The results found that capital flight measured by importation have positive and no significant effect on Nigeria domestic real investment. The estimated model as presented in chapter three of the study indicates that a unit increase in capital flight measured by importation increases domestic real investment by 0.06 percent. Theoretically we expected a negative relationship between capital flight measured by importation and domestic real investment, economic theory considers import as a leakage in the income stream, therefore the positive effect of importation on domestic real investment in Nigeria contradict our a-priori expectations. The positive effect of importation on domestic real investment could be traced to macroeconomic and financial sector reforms directed toward attracting foreign domestic and real investment. Empirically, the positive effect of importation confirm the findings of Oyieke (2011), Kingori (2015), Blejer and Khan (1984), Fofack, and Ndikumana (2014), Ghura and Goodwin (2010).

The results found that capital flight measured by profit repatriation have negative and no significant effect on Nigeria domestic real investment. The estimated model as presented in chapter three of the study indicates that a unit increase in capital flight measured by profit repatriation reduces domestic real investment by 4 percent. Theoretically we expected a negative relationship between capital flight measured by profit repatriation and domestic real investment, therefore the negative effect of profit repatriation on domestic real investment in Nigeria confirm our a-priori expectations. Empirically, the negative effect of profit repatriation contradict the findings of Oyieke (2011), Kingori (2015), Blejer and Khan (1984), Fofack, and Ndikumana (2014), Ghura and Goodwin (2010).

The results found that capital flight measured by Nigeria investment abroad have positive and significant effect on Nigeria domestic real investment. The estimated model as presented in chapter three of the study indicates that a unit increase in capital flight measured by between capital fight through Nigeria investment abroad and domestic real investment in Nigeria increases domestic real investment by 6.7 percent. Theoretically we expected a negative relationship between capital flight measured by importation and domestic real investment, therefore the positive effect of Nigeria investment abroad on domestic real investment in Nigeria contradict our a-priori expectations. The positive effect of importation on domestic real investment could be traced effectiveness of debt management policies or to macroeconomic and financial sector reforms directed toward attracting foreign domestic and real investment. Empirically, the positive effect of importation confirms the findings of Altaleb and Alokor (2012), Oshikoya (1994), Karumba (2009), Ndiaye (2011), Kehinde (2012) and Mbaye (2012).

The results found that capital flight measured by depreciating naira exchange rate have positive and significant effect on Nigeria domestic real investment. The estimated model as presented in chapter three of the study indicates that a unit increase in capital flight measured by depreciating naira exchange rate increases domestic real investment by 0.01 percent. Theoretically we expected a negative relationship

between capital flight measured by depreciating naira exchange rate and domestic real investment, therefore the positive effect of depreciating naira exchange rate on domestic real investment in Nigeria contradict our a-priori expectations. The positive effect of depreciating naira exchange rate on domestic real investment could be traced effectiveness foreign exchange policies and financial sector reforms directed toward attracting foreign domestic and real investment. Empirically, the positive effect of importation confirms the findings of Altaleb and Alokor (2012), Oshikoya (1994), Karumba (2009), Ndiaye (2011), Kehinde (2012) and Mbaye (2012).

CONCLUSION

The study found that capital flight measures as formulated in the regression model explain 44.4 percent of the variations in domestic real investment. The model was statistically significant when judged by the f-statistic and probability while the Durbin Watson statistic proved the absence of serial autocorrelation. The Augmented Dickey Fuller test, proved that variables were co-integrated of order I(1) and as such, deemed fit for employment in subsequent econometric estimations.

from the findings, the study conclude that, there is positive but no significant relationship between external debt servicing and domestic real investment in Nigeria, the null hypothesis not rejected.There is positive but no significant relationship between importation and domestic real investment in Nigeria, the null hypothesis not rejected.There is negative but no significant relationship between profit repatriation and domestic real investment in Nigeria, the null hypothesis not rejected.There is positive and significant relationship between Nigeria investment abroad and domestic real investment in Nigeria, the null hypothesis rejected and there is positive but no significant relationship between depreciating naira exchange rate and domestic real investment in Nigeria, the null hypothesis not rejected.

RECOMMENDATIONS

From the findings, the researcher makes the following recommendations:

1. Fiscal responsibility must be proper integrated in the process of external debt servicing and economic reforms must target macro-economic stability, removal of structural distortion and creation of conducive environment for enhancing domestic production capacity such as anti-inflationary policies like non – expansionary monetary and fiscal policies to attract domestic investment.
2. There need for economic diversification to reduce the growing importation to the country and government should provide an attractive and conducive environment for investors who will enable them to stay back in Nigeria and invest more.
3. The domestic economy should made more attractive for the investors by creating a wider menu of domestic financial assets on which domestic capital can be assessed and invested at a lower rate compared to foreign financial instruments, this will encourage domestic investment and reduce profit repatriation.
4. Profits from Nigeria international investment should be properly accounted for and well utilized to offset the effect of capital flight on the domestic economy.
5. Furthermore, a more stable exchange rate policy should be pursued. In addition, trade liberalization should also be encouraged by dismantling import and export restrictions.

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