Online ISSN : 2249-4588
Print ISSN : 0975-5853

Global Journal

of Management and Business Research: B

Economics and Commerce

Inflation and Economic Growth

Colonial Traces of Fractionalization

Highlights

Time Series Analysis

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Discovering Thoughts, Inventing Future

VOLUME 14 ISSUE 5 VERSION 1.0

Global Journal of Management and Business Research: B
Economics and Commerce

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Economics and Commerce
Volume 14 Issue 5 (Ver. 1.0)

Open Association of Research Society

Incorporation No.: 0423089
License No.: 42125/022010/1186
Registration No.: 430374
Import-Export Code: 1109007027
Employer Identification Number (EIN):
USA Tax ID: 98-0673427

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Wakefield MASSACHUSETTS, Pin: 01880,
United States of America
USA Toll Free: +001-888-839-7392
USA Toll Free Fax: +001-888-839-7392

Offset Typesetting

Global Journals Incorporated
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Pin: CR9 2ER, United Kingdom

Packaging & Continental Dispatching

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200 USD (B/W) & 250 USD (Color)

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Contents of the Volume

Global Journal of Management and Business Research: B
Economics and Commerce
Volume 13 Issue 5 Version 1.0 Year 2014
Type: Double Blind Peer Reviewed International Research Journal
Publisher: Global Journals Inc. (USA)
Online ISSN: 2249-4588 & Print ISSN: 0975-5853

Colonial Traces of Fractionalization: The Possibilities of Africa Moving Beyond the Walls to a Sustained Growth

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Abstract - While fractionalization had long been debated as one of the devastating economic factors on the African continent, there is much to believe that some important factors are responsible not only for its increasing growth and adverse effects, but also its perpetuation over the continent. This paper asserts that, colonial rule, among others, is to blame for the difficulties involved in dealing with the seemingly invincible effects of linguistic fractionalization and makes a recommendation that could help assuage the situation. The results are robust to alternative specifications including OLS, a simultaneous equation model and a spatial econometric model.

Keywords: fractionalization, institutions, trade, colonial rule, homogeneity, spatial dependence.

GJMBR-B Classification: JEL Code: M59

COLONIALTRACESOFFRACTIONALIZATIONTHEPOSSIBILITIESOFAFRICAMOVINGBEYONDTHEWALLSTOASUSTAINEDGROWTH

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Keywords: fractionalization, institutions, trade, colonial rule, homogeneity, spatial dependence.

I. Introduction

Though many factors have been found to account for the underdevelopment of African countries, fractionalization has been gaining increasing attention in the development literature. For example, many researchers have explored the relationship between institutions, ethno-linguistic fractionalization and growth. This includes the indirect effects of colonial institutions on the ability of Africans to trade peacefully. Colonial institutions in Africa are found to have exacerbated fractionalization, which led to the poor growth of African countries. Alternatively, others find that good institutions mitigate fractionalization and this leads to economic growth. Some other findings are that ethno-linguistic fractionalization negatively impacts economic growth and policies in Africa, and this is responsible for poor growth in Africa (Leeson, 2005; Easterly, 2001; Easterly and Levine, 1997).

The relationship between linguistic diversity, political stability and democracy has also been investigated widely and researchers find that linguistic diversity has positive impact on political instability. It is also discovered that democracy eliminates the negative impact of ethno- linguistic fractionalization on growth. There is also an established positive relationship between ethnic homogeneity and trust, which reinforces the positive relationship between trust and economic growth (Collier, 1999; Knack and Keefer, 1997). Cunning and Fay (1993) also explore the relationship between long-run growth and ethno-linguistic fractionalization.

There is also a plethora of literature on the relationship between colonization and growth. European colonization, for example, has a negative impact on growth. Colonial heritage, measured as the identity of the Metropolitan ruler and the degree of Economic Penetration (GNP/GDP), is one of the reasons for low average growth rate of GDP per capita and the observed heterogeneities in Africa. This explains differences in investment output ratio, education attainment and the index of ethno-linguistic fractionalization. Other researchers have also established a negative relationship between the number of years of colonial rule and growth. Also, by exploring the effect of ethnic, linguistic and religious fractionalization on the quality of growth, other studies find that linguistic and ethnic (racial) fractionalization are strongly negatively related to growth, but religious fractionalization is not (Bertocchi and Canova, 2002; Grier, 1999; Alesina, Devleeschauwer, Kurlat, Easterly and Wacziarg, 2003). Some other works in the area of economics of language include the explanation of the evolution of languages, the investigation of the economic and demographic determinants of destination language proficiency among immigrants and the connection between trade and languages. These researchers show that trade requires language. (Rubinstein, 1998; Chiswick, 2008; Smith, 1776).

Most of these researches focus on fractionalization as an exogenous variable. In this paper, I empirically investigate the determinants of fractionalization and argue that it can be reduced. For example, while the main focus of Easterly and Levine (1997) and Leeson (2005) is that regardless of heterogeneity countries can realize gains from trade, this paper asserts that trade can reduce fractionalization society. In other words, if and as diverse individuals trade, the walls of linguistic fractionalization and ethno-linguistic fractionalization can eventually be lowered significantly if not utterly destroyed as a result of their interaction. The paper posits that if incidents and events such as colonial policies that sever the interaction of diverse individuals had not occurred, trade among African countries would have developed at a faster pace. This

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increased trade would then lead to declining fractionalization, paving the way for a faster growth in Africa.

Thus, though many papers have investigated fractionalization and its effects on growth and development few, if any, researchers have empirically endogenized fractionalization specifically in an African context. This paper fills the gap by providing an empirical analysis of linguistic using OLS, Seemingly Unrelated Regression (SUR) and Spatial Autoregressive model (SAR). The results suggest that, among other factors, the measures of colonization (the number of years of colonial rule, colonial history and colonial heritage) do affect the persistence of fractionalization in Africa. The paper also finds that linguistic fractionalizetion is spatially dependent (contagious) suggesting that the best ways to address fractionalization include steps that will reduce linguistic fractionalization.

The rest of this paper is organized as follows: in the following section the study examines the possibility of linguistic fractionalization decline in Africa, followed by what exactly transpired during colonial rule. It then continues with specification of the methodology, presentation of my results, robustness checks, and discussion of the possibility of linguistic fractionalization decline in Africa today.

II. The Possibility of Fractionalization Decline in Pre-Colonial Africa

a) *Pre-colonial Africa and the Decline of Fractionalization*

African countries are among the world's most ethnically diverse countries. According to Easterly and Levine (2001), African countries are among fourteen of the world's fifteen most ethnically heterogeneous societies, with Uganda being the world's number one. Other societies in the world have gone through a phase of fractionalization comparable to Africa but, unlike the rest of the world, fractionalization in Africa seems to have come to stay.

However, before colonization, though fractionalized, Africa was one big society with no official significant differences. In order to commute from one area to the other, people did not need any documents or permission as long as they had the means of transportation and travelled through other settlements peacefully. Though sometimes special gifts and offerings were given to the chiefs and fetish priests of other societies through which one travelled or undertook business transactions, movement as well as assimilation into other societies and cultures was very common. Outsiders wanting to join a particular community gave special gifts to the Earth's Priests and agreed to respect the community's rituals (as a signal of credibility) and, thus, were given the possibility of trading with the existing group members. (Leeson, 2005).

This is accentuated by the fact that some languages and cultures are common to a lot of ethnic groups across African countries today. For example, there are tribes in many African countries who speak same languages as some tribes in other African countries today. In other words, this shows that interaction of different societies through trade (free trade) was highly possible even in the face of fractionalization. Domestic, long distance and international trade developed in Africa with the resultant social interaction between different ethnic groups prior to European's arrival on the continent (Cohen, 1969: 6). There were also commercial interactions in pre-colonial Africa to the extent of creating homogeneity between different diverse people (Thornton, 1995: 194). Thus, without any interruption, there was the possibility that the walls of fractionalization might be lowered to their minimal levels if not utterly destroyed.

One way ethno-linguistic fractionalization could have declined in the absence of colonial rule is that, with time, some languages and cultures could become dominant over others in each society or a lingua franca could have evolved. In every society, each group is identified with a certain kind of occupation. Typical examples are farmers, (including shepherds who travel widely in search of pasture), and traders. The latter are very influential as they move from one place to the other and must interact with the indigenous people in order to transact business with them. Consequently, they tend to spread their language and culture from place to place. For example, commercial interactions help explain the great cultural similarities between many different peoples south of the equatorial forest (Vansina, 1968: 325). It is imperative to point out that most countries that have adopted one language today have gone through an evolution. This process of evolution from linguistic fractionalization as evident in other countries' experiences could have taken place in Africa too, but this was interrupted or slowed down, largely, as a result of colonization.

b) *Cost and Benefits of Learning a New Language in Pre-colonial Africa*

Language skill is human capital, since it satisfies the three requirements of a human capital namely productivity, costliness and embodiment in a person (Chiswick, 2008). The first two of these attributes imply that there is a benefit and cost associated with learning, adopting or developing a language that will serve the common good of a fractionalized society as Africa. If the cost is higher than the benefit, then the society or individuals who make up the society will stick to their different languages, instead.

One of the costs of learning a dominant language or developing a common language in pre-colonial Africa is time; it takes time for one to learn a new language, especially so for the old. It could also take time for parents and relatives to teach the young this new language, but in pre-colonial Africa where interacttion among diverse individuals was free the process could be much faster than it was under colonial rule. Exposure to the dominant language is another determinant of the cost of learning a new language. This exposure was much greater in the absence of colonial barriers and colonial immigration restriction policies. Similarly social distance, another cost of learning a new language, was smaller in pre-colonial Africa. For example, Leeson (2005) argues that pre-colonial agents used signals such as property usage, religious practices and the individual's relationship to authority to minimize the social distance between sender and receiver to send their credibility to outsiders they wanted to trade with.

Another factor that determines the cost of learning a new language is distance between one's mother language and the new (dominant) language. Though Africa has many languages, one thing these languages mostly have in common is their syllabus. You can almost write every language using a set of alphabets. There are many languages that have certain words in common as well. This means that it will be easy for a speaker of one African language to learn to speak another or most African languages.

There are also benefits associated with learning a new language. One of such benefits is productivity; language is productive in consumption activities. This implies that it will enable people find quality goods and services at lower prices. Trading in Africa, including today's, requires one's ability to negotiate prices, so the more proficient you are in a trade language the higher your chances of success. Not only would learning a dominant language in pre-colonial Africa enable people do well in the market, it would also make them find good jobs in the labor market. Learning a new language enables agents to execute their jobs efficiently. Other social benefits include one's ability to network and make a wide range of friends outside his linguistic enclave and the enhancement of civic involvement by gaining full political and economic rights of the new (dominant) spoken language community (Chiswick, 2008). In pre-colonial Africa, learning the larger society's language could be seen as a signal of credibility and could result in gaining access to full benefits of the larger society.

III. The Worsening of Fractionalization During Colonial Rule

Colonial rule seems to play a role that stymie the decline of linguistic fractionalization in Africa. Leeson (2005) explores the indirect effects of colonial institutions on the ability of Africans to trade peacefully. One of the findings includes how artificial colonial institutions such as forced allegiance to an authority disabled the signal that individuals look to when evaluating the credibility of outsiders to trade with, which resulted in the creation of smaller sub-groups among broader ones to eliminate the risk of interacting with those who were remotely unknown. Thus, this colonial distortion of trade further reduced social and commercial interaction that would expose individuals to and cause them to learn a dominant (trade) language.

Second, colonial rule inhibited free movement of individuals in Africa and this was no environment for cultural or linguistic convergence. As opposed to pre-colonial Africa where people could come and go as they pleased, so that it was possible for people to be members of multiple communities and hence exchange with a wide range of individuals, colonial land policy created noise in this signal used to convey credibility by legally requiring colonial agents to stay attached to their ruler-allocated areas of land. Such a colonial policy also restricted migration, as was the case of Basutoland in 1903 when colonial law forbade the provision of land to non- Basotho people (Leeson, 2005). Limited mobility under colonial rule was therefore one of the factors that reduced the need to adopt or learn the most widely spoken language(s) as the cost of doing so became more than the benefit, if any.

Another way colonization exacerbated linguistic fractionalization in Africa is that colonial masters separated African countries into territories that may never be reconciled to each other. The separation has far reaching ramifications of maintaining ethno-linguistic borders especially across countries. As mentioned above, walls of colonization have divided different African societies that had common languages and cultures. Societies that once saw each other as one though far apart, because of language and culture, now see each other as aliens. Even if the walls of ethno-linguistic fractionalization gradually break down in each colony (now country) it may never break down across countries, unless stringent measures are taken. This is because these colonies now see one another as different entities. For example, the people from the Volta region of Ghana speak the same language and have same culture as about half the population of Togo, a neighboring country, but are now considered aliens in Togo because of colonial walls. The same is true for tribes of many neighboring countries in Africa.

Moreover, colonization led to the proliferation of different institutions in Africa that made it difficult to reduce fractionalization. Colonial created institutions severed the communication mechanism between sociallly heterogeneous individuals in Africa by reducing the signals (pre-colonial institutions) that enabled communication and interaction as this increased the cost of commercial interaction. Legal systems of each colonial master were different and this made it difficult for Africa to adopt an institutional framework that supported continent-wide development initiatives such as free trade areas. These legal frameworks that distorted the already established ones before them helped prolong fractionalization in Africa. In addition, the division of colonies into regions and districts by some colonial rulers has huge ramifications. This was an attempt to facilitate colonial rule but now permanently left these internal groups at conflict with each other over lands, resources and domains. Colonial policy led to a break-down of the ability of African people to interact freely and, instead, led to a sharp increase in property disputes among Africans (Leeson, 2005).

One would think that the introduction of the language of the colonist should mitigate linguistic fractionalization but what happened was the exact opposite. Unlike societies such as Latin America where colonial masters introduce Spanish to the whole society, the colonial master's language was intended for only a few selected Africans, who helped in the facilitation of communication of the colonial masters with the rest of the African societies. If a larger population of each country were taught the colonial master's language, it could help promote homogeneity. Today, the colonial master's language is a luxurious commodity in Africa, and it is largely the rich consume it. In most cases, one could only learn this language (official language) through formal education, which is costly. Studies show that 90 percent of the population in most African countries does not speak the official language at home (Easterly and Levine, 1997). In other words, these official languages tend to add to linguistic diversity in Africa rather than help create homogeneity.

Coupled with above, the same master did not colonize all African countries, and that means ranging from English to Spanish, more languages were added to the several languages spoken in Africa rather than replace them (a situation that would have reduced fractionalization in Africa). If a greater proportion, if not all, of the population of Africa countries were able to speak its colonial master's language the outcome would have been close to desirable.

Post-colonial attempts to use the colonial master's language to reduce linguistic fractionalization in Africa did not succeed. Most African countries made it mandatory for every school going person to learn the official language (colonial master's language) of their neighboring African country. Due to these colonial walls that have now become official barriers, even if one learns the neighboring country's language he could do little with it (because hardly does anyone speak that language in the domestic country) and hence tend to forget it a few years after leaving school. If there were no official barriers and people could travel freely to neighboring countries to trade or undertake other commercial activities, continuous use of the neighbor's language could cause them to be proficient not only in their own official language, but also in the language of their neighboring countries. Canada is an example of the possibility of speaking a second official language in the absence of official barriers.

IV. Methodology

a) Data

This study estimates the impact of colonial rule (number of years of colonial rule) on fractionalization in Africa. The data comprises a cross-section of 49 African countries from 1980-2000. The list of countries is found in Appendix 2. Data on linguistic fractionalization is computed by Alesina, Devleeschauwer, Kurlat, Easterly and Wacziarg (2003). This variable is based on the shares of languages spoken as mother tongues. The reason for the choice of this variable is that it is entirely based on language and hence different from the effect of any racialor ethnic features.

Even though both linguistic fractionalization an ethnic fractionalization were used by Alesina, Devleeschauwer, Kurlat, Easterly and Wacziarg (2003), in most of their main regressions linguistic fractionalization does have a bigger effect (and higher level of significance) on growth than ethnic fractionalization. I thus employ only linguistic fractionalization in my regressions.

The population, GNP and GDP data are taken from the World Bank's databases. One of the measures of olonial rule, colonial penetration (also referred to as "drain") is the ratio of a country's GNP to GDP in 1960 as in Bertocchi and Canova (2002). The lower the value of GNP the higher the level of colonial penetration and the lower the ratio. They use this as a measure of colonial drain following the drain of wealth thesis. According to them this measure captures how Metropolitan countries further extracted colonial surplus by reducing indigenous capital accumulation through repatriation of profits, pensions, interest on loans and salaries. They argue that the impact of colonization may survive past political independence but those colonies kept paying the consequences of their history even after independence was achieved.

Institutional measures are taken from the International Country Risk Guide (ICRG). Data on colonial rule is taken from the World Fact Book. The length of colonization was compiled based on Barro (1991), which provides data including dates of independence. A detailed description of the data, together with summary measures is given in Appendix 1.

b) Model

Both OLS and a spatial econometric model, SAR (Spatial Autoregressive Model) are employed in the main regressions. A simultaneous equation model is also employed for robustness analysis. SAR specifies a country's linguistic fractionalization as a function of the weighted value of the linguistic fractionalization of its geographic neighbors. The models are specifiedbelow. OLS:

$$Elf = \alpha 0 + \alpha 1 Colrule + \alpha 2\ Institutions + \alpha 3 Colpen + \alpha 4 GDP + \alpha 5 Poltstability + \alpha 6\ Borderdummy + \eta \quad (1)$$

$$Trade = \alpha 0 + \alpha 1 Colrule + \alpha 2\ Institutions + \alpha 3 Colpen + \alpha 4 GDP + \alpha 5 Poltstability + \alpha 6\ Borderdummy + \omega \quad (2)$$

where, *Elf* represents linguistic fractionalization, *Trade* is the volume of bilateral trade between each country and all other countries in the study, *Colrule* is the number of years a country has been colonized, *Institutions* is an index of the quality of a country's institutions, *Britishdummy*, *Frenchdummy*, and *Belgiumdummy* are colonial history dummies for African countries colonized by Britain, France and Belgium respectively *Borderdummy* is a dummy created for countries whose post colonial borders existed before colonial rule, and η and ω are NX1 matrixes of *iid* random errors.. Colonial rule is expected to have positive impact on linguistic fractionalization and negative impact on trade. Equation (2) is only employed for robustness analysis.

SAR:

$$Y = \alpha + \rho WY + \beta X + \nu \quad (3)$$

where *X* is a vector of controls variables specified above, *Y* is an NX1 vector of measures of the dependent variables; ρ is the spatial autoregressive and spatial error coefficients (which represents geographic contagion in the dependent variable), and **ν** is an NX1 matrix of *iid* random errors. *W* is an NXN weight matrix for geographic neighbors.

For the geographic weight matrix a country gives a weight of one to every country it shares a border with (whether vertically, horizontally or at vertex contacts) and zero otherwise. The geographic weight matrix is row standardized. For example, if country A has 4 neighbors, then each of these countries is assigned a weight of ¼ by country A.

$$W = \begin{bmatrix} \frac{\mu_{1j}}{\sum \mu_{1j}} & \cdots & \frac{\mu_{1n}}{\sum \mu_{1j}} \\ \vdots & \ddots & \vdots \\ \frac{\mu_{nj}}{\sum \mu_{nj}} & \cdots & \frac{\mu_{nn}}{\sum \mu_{nj}} \end{bmatrix} \quad \text{for } j = 1, 2, \ldots n$$

$$\text{Where, } \mu_{ij} = \begin{cases} 1 & \text{if county } i \text{ and } j \text{ are neighbours otherwise} \\ 0 \end{cases} \quad (4)$$

This makes the weights given by each country to all others sum up to 1. This is represented in matrix notations above.

V. Results

a) Main Findings

The results suggest that the number of years of colonial rule in an African country affects a country's level of linguistic fractionalization.

Table 1 results show that without controlling for institutions the number of years of colonial rule is positive but insignificant. However, once I control for institutions both the number of years of colonial rule and institutions become significant. Similarly, other measures of colonial rule are also positive and significant in Table 1. Colonial Penetration is positive and significant in all regression while French Colonial Dummy is also significant but only when institutions are controlled for.

Table 2 reports the results for the SAR model. The main aim of this regression is to find out if there is a spatial dependence in the dependent variables; that is if countries that have low levels of linguistic fractionalization tend to be neighbors and vice versa. The results indicate that linguistic fractionalization is contagious. This is evident, as the coefficient, (rho), is significant. A possible reason explanation is that languages can be created, adopted, spread or dominated.

Controlling for spatial dependence also makes all the independent variables, except British and French colonial dummies, insignificant. This can be explained by the fact that all the independent variables are spatially correlated. All of them are measures of colonial rule. Thus the geographic weight matrix therefore captures and removes this spatial correlation making these variables insignificant. British colonial dummy is now significant and French colonial dummy is still positive and significant, still indicating the effects of British and French colonization on linguistic fractionalization.

b) Robustness Checks: Adding New Variables and Comparing Alternative Models (SUR and OLS)

While the above gives an indication that the length of colonial rule and colonization in general does have an effect on the fractionalization measure, the paper attempts to check the robustness of the results by including other independent variables, and a dependent variable (trade), to see if the results will change signifycantly. To do this, a simultaneous equation specification is also employed in addition to the OLS regression. The use of such a specification can improve standard errors as well. A seemingly unrelated regression (SUR) models are specified below based on equation (1) and (2) above:

SUR:

$$Elf = \alpha 0 + \alpha 1 Colrule + \alpha 2\ Institutions + \alpha 3 Colpen + \alpha 4 GDP + \alpha 5 Poltstability + \alpha 6\ Borderdummy + \eta \tag{1}$$

$$Trade = \alpha 0 + \alpha 1 Colrule + \alpha 2\ Institutions + \alpha 3 Colpen + \alpha 4 GDP + \alpha 5 Poltstability + \alpha 6\ Borderdummy + \omega \tag{2}$$

First, I estimate the impact of colonial rule on trade. Table 3 shows that there is a negative impact of colonial rule on bilateral trade between African countries (as seen in the OLS regression) and the results are significant at 5%-10% levels. However no other independent variable is significant in the OLS regression. Table 4 presents the results for SUR regression based on equation (1) and (2) above. The SUR result for linguistic fractionalization is still significant, but the trade result is no longer significant. In addition, the linguistic fractionalization regression gives a negative and significant coefficient of institutions. Thus there is a negative relationship between linguistic fractionalization and institutions. However, the results suggest that whereas colonial may have an effect on trade, institutions do not have an effect on trade.

VI. Is there a Possibility of Linguistic or Ethno-Linguistic Homogeneity in Post-Colonial Africa?

Though one cannot say for certain whether ethno-linguistic fractions can reduce enough in Africa, looking at what is going on other continents suggests that there is a possibility. Economic integration or political integration or both can help. For example, English is becoming a "lingua franca" in Europe following the reduction of legal barriers that now facilitates the movement of people and the removal of non-tariff and tariff barriers that facilitates trade (the free mobility of goods) across EU countries (Chiswick, 2008).

If this EU paragon could be applied in Africa, free trade and free mobility of economic agents could call for, if not result in, a lingua franca. This new language, which can be a widely spoken African language or one of the widely spoken languages introduced by colonial masters, would reduce linguistic fractionalizetion. When a big society speaks the same language, ethnic fractionalization will also dwindle, because it will become more and more difficult to tell ones ethnicity when everyone's name is in the same language. Governments can help fund the teaching of this language and make individuals view the speaking of such a language as a sign of demonstrating patriotism or nationalism. Creating the awareness of the effect of homogeneity on economic growth of Africa can help Africans embrace such policies. In other words there are benefits as well as costs associated with achieving linguistic and ethno-linguistic homogeneity now as, if not more than, it was in pre-colonial Africa.

VII. Conclusion

The findings of this paper show that while colonization worsened both linguistic fractionalization in Africa, its effect on effect is only significant by controlling for institutions. This is supported by the results of this paper, which show that the number of years a country was colonized, colonial penetration and colonial history do have a positive impact on linguistic fractionalization in Africa. It also shows that while both French colonial rule and British colonial rule exacerbated linguistic fractionalization, others did not. This may be due, for example, to colonial policies such as divide-and-rule practiced by Britain.

Also the results suggest that linguistic fractionalization is more adversely affected by colonialism than trade and that while colonial institutions have negative effect on linguistic fractionalization, it does not have any significant effect on trade. The results also support the view of Leeson (2005) that bad institutions worsen fractionalization and that this is one of the reasons for the increasing fractionalization and poor growth in Africa. Apart from the division of the continent into colonies, different foreign languages and institutions introduced by colonial rulers made it difficult for Africa to reduce its level of fractionalization. Therefore, policy recommendations for mitigating or eradicating the effects of linguistic fractionalization in Africa may include the introduction or emergence of a lingua franca.

Table 1 : Dependent Variable: Linguistic Fractionalization

Independent Variables	I	II
Constant	2.910** * (3.65)	1.626** (2.23)
Colonial Rule (no. of year)	0.003** (2.14)	0.0002 (0.25)
Institutions	-0.202 *** (-2.63)	
Colonial Penetration	-0.025*** (-3.21)	-0.013* (-1.73)
British Colonial Dummy	0.642** (1.99)	0.306 (1.03)
French Colonial Dummy	0.554* (1.78)	0.336 (1.13)
Belgium Colonial Dummy	0.338 (0.79)	0.263 (0.73)
Border dummy	0.030 (0.20)	-0.063 (-0.40)
R-Squared	0.35	0.15

*Notes: t-statistics in parentheses; asterisks indicate significance as follows: ***=1%, **=5%, *=10%. Variable description, descriptive statistics, and sources can be found in Appendix 1.*

Table 2 : Dependent Variables: Linguistic Fractionalization

Independent Variables	I	II
Constant	0.246 (1.595)	0.246* (1.710)
Rho	0.317*** (2.49)	0.312*** (2.424)
Colonial Rule (no. of year)	0.0005 (1.065)	0.0004 (1.081)
Institutions	-0.002 (-0.039)	
Colonial Penetration	-0.0004 (-0.400)	-0.0004 (-0.399)
British Colonial Dummy	0.210* (1.62)	0.209* (1.671)
Belgium Colonial Dummy	-0.028 (-0.146)	-0.028 (-0.144)
Border Dummy	0.027 (0.270)	0.027 (0.270)
R-Squared	0.17	0.17
Observations	49	49

*Notes: t-statistics in parentheses; asterisks indicate significance as follows: ***=1%, **=5%, *=10%. Variable description, descriptive statistics, and sources can be found in Appendix 1*

Table 3 : Dependent Variables: Trade

Independent Variables	I	II
Constant	23.861 (0.08)	98.928 (0.40)
Colonial Rule (no. of year)	-0.363* (-1.84)	-0.330** (-2.130)
Institutions	24.835 (0.59)	
Population	0.418 (0.65)	0.441* (0.69)
Political Stability	25.4031 (0.65)	22.753 (0.69)
Colonial Penetration		
GDP	0.00004 (0.30)	0.0001 (0.77)
Border Dummy	-48.513 (-0.747)	-48.513 (-0.747)
R-Squared	0.18	0.17
Observations	49	49

*Notes: t-statistics in parentheses; asterisks indicate significance as follows: ***=1%, **=5%, *=10%. Variable description, descriptive statistics, and sources can be found in Appendix 1.*

Table 4 : Dependent Variables: Linguistic Fractionalization & Trade

	Dependent Variables	
Independent Variables	Trade	Linguistic Fractionalization
Constant	165.912 (-0.37)	2.545** (2.41)
Colonial Rule (no. of year)	2.590 (1.34)	0.0051*** (3.21)
Institutions	-41.776 (-0.53)	-0.136** (-1.92)
Population	0.466 (1.23)	0.441 (1.41)
Political Stability	47.712 (0.79)	-0.0150 (-1.46)
Colonial Penetration		-0.0711 (-1.42)
GDP	-0.0004 (-1.02)	-0.00001** (-1.96)
Border Dummy	-15.432 (-0.12)	-0.009 (-0.09)
R-Squared	0.22	0.460
Observations	49	49

*Notes: t-statistics in parentheses; asterisks indicate significance as follows: ***=1%, **=5%, *=10%. Variable description, descriptive statistics, and sources can be found in Appendix 1.*

Appendix 1 : Variable Description, Descriptive Statistics, and Sources

Variable Name (source)	Description	Mean (Std. Dev.)
Dependent Variables:		
Linguistic Fractionalization (3)	Index of linguistic diversity (%)	0.623(0.291)
Ethno-linguistic Fractionalization(6)	Index of ethnic and linguistic diversity (%)	0.616(0.26707)
Trade (2)	A country's total volume of trade with each African country (US$)	237.111(253.877)
Independent Variables:		
GDP (1)	GDP (constant 2001 US$)	9.43E+09(1.99E+10)
Colonial Penetration(1)	GNP/GDP computed for 1960: The lower the value the higher the extent of colonial penetration.	98.993(4.341) 2.327(0.993)
Institution (5)	Index of institutional quality computed as an average of three variables (bureaucratic quality, risk of expropriation, and the risk of repudiation of contracts): (1-10); the higher the better.	
Colonial Rule (4)	Number of years a country has been colonized by all possible colonial Masters (years)	106.065(120.9877)
Political stability (5)	Index of political stability (1-10).	6.997(1.115)
Border dummy	A dummy specifying whether a country's borders were created by colonial masters	
Colonial Dummy	A dummy showing which colonial master colonized a country	
Population (1)	Total population of a country (millions)	13604971(17391899)

1. *World Development Indicator; The World Bank Databases. 2. Direction Of Trade; IMF Databases. 3. Alesina et al. (2003) Dataset. 4. CIA, The World Fact Book*
5. *International Country Risk Guide; ICRG Dataset 6. Elf Dataset*

Appendix 2 : List of Countries

Algeria	Egypt	Morocco
Angola	Equatorial Guine	Mozambique
Benin	Ethiopia	Niger
Burkina Faso	Gabon	Nigeria
Burundi	Gambia, The	Rwanda
Cameroon	Ghana	Senegal
Cape Verde	Guinea	Sierra Leone
Central African	Guinea-Bissau	Somalia
Repuclic	Kenya	South Africa
Chad	Liberia	Sudan
Comoros	Libya	Tanzania
Congo, Rep.	Madagascar	Togo
Of the	Malawi	Tunisia
Congo, Dem.	Malawi	Uganda
Rep. Of the	Mauritania	Zambia
Cote d'Ivoire	Mauritius	Zimbabwe
Djibouti		

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Global Journal of Management and Business Research: B
Economics and Commerce
Volume 13 Issue 5 Version 1.0 Year 2014
Type: Double Blind Peer Reviewed International Research Journal
Publisher: Global Journals Inc. (USA)
Online ISSN: 2249-4588 & Print ISSN: 0975-5853

New Characteristics in the Changing Psychological Contracts and Repatriation Success of Expatriates in Japanese Multi-National Corporations

ByYanghua Zhou
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Introduction– With more and more multi-national corporations in this globalization age, the research on effective expatriate utilization is attracting increasing attention. Because of the culture difference, the characteristics of expatriate in different countries have distinguishing charac-teristics. In this study, based on multi-dimension analysis of organization, individual, culture and institution, with cases from interview with expatriates, the new factors that influence expatriate repatriation success in Japanese multi-national corporations will be discussed..

Keywords: psychological contracts, expatriate,repatriation success, culture, institution.

GJMBR-B Classification: JEL Code: O10

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I. Introduction

With more and more multi-national corporations in this globalization age, the research on effective expatriate utilization is attracting increasing attention. Because of the culture difference, the characteristics of expatriate in different countries have distinguishing characteristics. In this study, based on multi-dimension analysis of organization, individual, culture and institution, with cases from interview with expatriates, the new factors that influence expatriate repatriation success in Japanese multi-national corporations will be discussed.

According to Yan (2002), expatriate repatriation success depends on psychological contracts of expatriate individuals and multi-national corporations. And Morishima (2000) did the research on psychological contracts of general employees in Japanese corporations and changes that have happen. However, how the psychological contracts of expatriates in Japanese multi-national corporations change in recent several decades, and what new characteristics influence their repatriation success is still open to further research.

Therefore, in this study, based on theoretic analysis and interviews with these expatriates in Japanese multi-national corporations, these topics will be answered and the propositions of Yan(2002) will be verified.

II. Literature Review

a) *The necessity of expatriate utilization in multi-national corporations*

According to Tan (2006), 'Expatriates are home-country nationals (i.e. citizens of the country in which the multi-national firm is headquartered) who are sent by the headquarters to the foreign positions' to accomplish the transference of technology or knowhow from the headquarters to subsidiaries and the subsidiary management within 3 or 5 years or longer period.

Many scholars analyzed why a multi-national corporation uses expatriates. In general, the utilization of expatriates mainly lies on 2 reasons. The first one is to reduce transaction costs between headquarters and subsidiaries. And the second one is the necessity of running internal labor markets of multinational corporations. From the viewpoint of agency and transaction costs theories, in a multi-national firm, there is principal-agent relationship between headquarter and its subsidiary. According to Tan (2006), using expatriates is a kind of governance aimed at offering managerial services in foreign branches, and this action is usually considered for reducing the agency and transaction economic costs from managers of foreign branches. Tan (2006) pointed out that the multi-national corporations have to reduce communication cost and asymmetric information problems between the headquarters and their foreign subsidiaries by sending expatriates to important positions in their foreign branches. From the viewpoint of transaction costs theory, multi-national corporations will assign expatriates to reduce bargaining problems of subsidiary managers to some extent. Because in a multi-national corporation, headquarter and its subsidiaries are in different countries, it takes a lot of time to observe and monitor managers' routine work situation across such a long distance. With an expatriate from the headquarter, it becomes much easier. The expatriate may observe and monitor the local branch every day and report to the headquarter timely.

Furthermore, Erdener (1999) pointed out that from the perspective of transaction cost economics, using expatriates may reduce culture frictions and risk so that multi-national corporations are able to get competitive advantage and improve their performance. In general, every country has its unique culture and business habits, therefore sometimes culture frictions occur. This is also a hard problem for the headquarters to deal with and it cannot be solved by money. If there is an expatriate who understands both the culture and coordinates between the two parts, the partnership will

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be more effective. Additionally, based on an empirical study of 145 Norwegian multi-national corporations, Gabriel (2005) stated that according to transaction cost theory, using expatriates may reduce transaction cost, especially when using experienced expatriates. He also observed that culture differences between host and home countries will influence the ex post transaction cost of multi-national corporations.

From the perspective of 'Multi-national Internal Labor Markets' theory (see Figure 1), Shiraki (2006) stated that sufficient basic human resource in subsidiaries of a multinational corporation is a necessary condition for the formation of Multi-national Internal Labor Markets. According to Shiraki (2006), Internal Labor Markets are those where workers are hired into entry level jobs and higher levels are filled from within. Without internal labor market in a multi-national corporation, human resource management may have some serious problems. For instance, if some foreign subsidiary of a multi-national corporation is in lack of knowhow or technology in some field, it can send an expatriate there to fill this gap soon. But if its internal labor market is not regular, it will take a lot of time to search such a suitable person to accomplish this job. Hence, expatriate assignment becomes an important part of international human resource management strategy. Discussed as above, both 'Multi-national Internal Labor Markets' theory and agency and transaction cost theory suggest that it is necessary for multi-national corporations to use expatriate assignment.

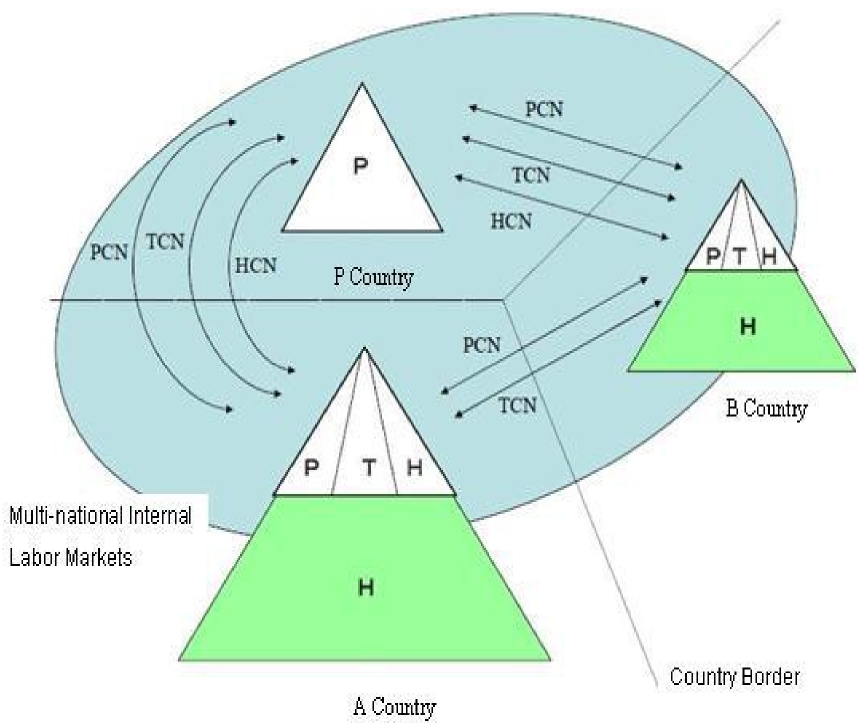

Figure 1 : Multi-national Internal Labor Markets

Source: Shiraki (2006), An analysis of International Human Resource Management: From the 'Multi-national Internal Labor Markets' Viewpoint, p28.

Note: PCountry represents parent company country. PCNs (or P) represents parent-country nationals, HCNs (or H) represents host-country nationals, TCNs (or T) represents third-country nationals.

b) Expatriation success and Repatriation success

In previous literature, an important concept related to expatriate utilization is expatriation success and repatriation success. According to Yan, A., Zhu, G., and May, D. (2002), the main contents of expatriation success and repatriation success of expatriates are defined in the following Table 1.

Table 1 : Possible Success Criteria for International Assignments

		Benefits	
		Individual	*Organizational*
Assignment stage	*Expatriation*	- Task performance - Skill building, learning, and growth - Job satisfaction	- Accomplishment of organizational tasks - Achievement of key organizational objectives
Assignment stage	*Repatriation*	- Continued development - Attractive future assignments - Promotion - Enlargement of responsibility	- Retention of repatriated employee - Utilization of new expertise - Transfer of expertise

Source: Yan, A., Zhu, G., and May, D. (2002): "International assignments for career building: A model of agency relationships and psychological contracts". Academy of Management Review, 7(3), pp. 373-386.

In Japanese multi-national corporations, many expatriates repatriates to their headquarters. The proposition of repatriation is much higher than other countries, such as America, Singapore, and China. But in recent years, the retention rate of these repatriated expatriates is not so high as the proposition of repatriation. That's to say, the degree of repatriation success is not so high. In the following analysis, this problem will be discussed.

c) *Psychological contracts related theory*

According to Yan (2002), an important factor that influences the success of expatriation and repatriation is psychological contracts. The concept of psychological contract means "employees' perceptions and expectations of the mutual obligations that exist between themselves and the employing organization." (Rousseau, 1989). And a psychological contract represents critical mutual expectations held by the two parties of individuals and their organizations (Schein, 1965).The expectations from individual to organization includes promotion, high salary, training, long-term employment, career development and other support. On the contrary, the expectations from organization to individual include overtime work, loyalty, good performance, contents unwritten in job description, capability of transfer, maintaining confidentiality, minimum years of service (Rousseau, 1990). Compared with paper-based contracts, psychological contracts have the characteristics of implicit, unwritten, and informal in most cases.

Through meta-analysis of the relationship between psychological contract fulfillment and its result, Zhao, Wayne, Glibkowski and Bravo (2007) suggested that psychological contract breach has negative impact on job satisfaction, organization commitment, resignation notion, organizational citizenship behavior and performance of an individual. Therefore, psychological contracts affect expatriates' career selection when they think of repatriation. They will consider whether they should go back to headquarters or quit to other multi-national corporations. Marius, Gudela, Christian, and Sabine (2012) also got a similar conclusion by an empirical study.

According to MacNeil (1985), psychological contracts are divided into two types: relational contracts and transactional contracts. Relational contracts refer to a long-term loyalty based expectation and transactional contracts refer to short-term job and project oriented expectation. Rousseau (1989) stated that relational psychological contracts have the characteristics of an indefinite duration and diffuse obligations. And the transactional psychological contracts are characterized by monetizable resources, short time frames, and specifically delineated obligations. Morishima (2000) also pointed out that relational contracts are often implicit whereas transactional contracts are explicit. Additionally, besides relational contracts and transactional contracts, other forms of contract are also possible, such as balanced contracts (Rousseau, 2000).

According to Yan (2002), the mechanism by which psychological contracts influence expatriate's success of expatriation and repatriation is shown in Table 2. Yan, Zhu & May (2002) proposed an Organization-Individual Alignment Matrix (as shown in Table 2) by analyzing psychological contracts (relational contracts and transactional contracts) of both organizations and individuals. And based on the psychological contract alignment, the degree of repatriation success was suggested. Therefore, there are different career patterns in expatriates' repatriation. Furthermore, because psychological contracts are easy to be changed, possible external causal factors in shift-in are also proposed in their paper. Through an empirical study, Arno and Chris (2009) also emphasized that during the repatriation period there is a stronger link between a perceived breach and turnover cognitions than at other times in the employment relationship.

Table 2 : Organization-Individual Alignment Matrix and summary of propositions

		Individual	
		Relational	Transactional
Organization	Relational	Cell I: Mutual loyalty - High organizational success in expatriation and repatriation (PI) - High individual success in expatriation and repatriation (P2)	Cell II: Agent opportunism - Moderate organizational success in expatriation but failure in repatriation (P3) - High individual success in expatriation but mixed success in repatriation (P4)
	Transactional	Cell III: Principal opportunism - Moderate organizational success in expatriation and low success in repatriation (P5) - Moderate individual success in expatriation but failure in repatriation (P6)	Cell IV: Mutual transaction - Moderate to high organizational success in expatriation and a better chance of organizational success in repatriation than that in the case of misalignment (P7) - Moderate to high individual success in expatriation and a better chance of individual success in repatriation than that in the case of misalignment (P8)

Source: Yan, A., Zhu, G., and May, D. (2002): "International assignments for career building: A model of agency relationships and psychological contracts". Academy of Management Review, 7(3), pp.373-386.

d) Career stage (age) and psychological contracts

According to Liu (2002), Employees in different career stages have distinct characteristics of psychological contracts. In the determining stage of one's career (from 30 years old to 45 years old), an employee views the relationship with his/her organization as transactional; in the maintenance stage (from 45 years old to 55 years old), an employee views it as balanced, and in the decline stage (>55 years old) an employee views it as relational. In this study, the age and career stage will be discussed as a factor that influences expatriates' repatriation.

e) Collectivism Culture and the employee's traditional psychological contracts in Japan

As Morishima (2000) stated, the culture characteristics in Japanese society is collectivism and there people emphasize the importance of 'belonging,' or being a member of a large entity such as a group or organization. Therefore, the traditional psychological contracts in Japanese companies are relational. Both individuals and organizations have high loyalty and the career employment system is the main employment style and it has lasted for a long time. Therefore, in Japanese multi-national corporations, many expatriates repatriated as scheduled, especially in the high level economic growth period.

Wang (2013) also argued that individual's culture characteristic can influence one's sense of value and then have impact on his/her psychological contracts. He pointed out that it is easy for employees in the culture that has individualism characteristic to have transactional contracts. And individuals in collectivism culture have the tendency of taking relational contracts. In this study, individuals and organizations in collectivism culture circumstance in Japan are the research objects.

f) Institution Change in Human resource management of Japanese corporations

From the view point of Institution Change Theory of Neo-Institutional Economics (Douglass C. North), institution is limited and will change with the outside environment because of the bounded rationality of human and the scarcity of resources.

According to Morishima (2000), Institution Change in Human resource management of Japanese corporations has happened. Career employment is the traditional employment style but in recent years, externalized employment and performance-based pay system have been introduced to Japan society. What caused this change? According to Institution Change Theory, it should be the environment. The most important reason should be the changing economic environment, from high level economic growth period to economic depression. The change of economic environment not only influences society institution but also has impact on psychological contracts between individuals and their organizations.

Morishima (2000) stated that the psychological contracts of Japanese employees have changed from relational to transactional because of her changing employment system. The collectivism culture in Japan is famous all over the world, therefore, in the past, career employment was very general and the psychoogical contracts between Japanese employees and organizations are mainly relational up to 1990s. But the introduction of externalized employment and performance-based pay system helped the psychological contracts change from relational to transactional.

III. Research Questions

The above researches are good references for us when considering the careers at repatriation of expatriates. But what new characteristics influence their repatriation success is still open to further research. In this new circumstance, what are the new characteristics of Japanese expatriates? What is the change of the mechanism that influence expatriate's success of expatriation and repatriation in recent years in Japan? Additionally, there is a lack of appropriate data in previous literature in that field. To answer these research questions, the author took interviews with some Japanese expatriates.

IV. Method

In this research, the method (Figure 2) is a kind of qualitative analysis used by Christensen (2009). Eizenhart (1989a) and Gilbert (2005) has also thought a great deal of that inductive theory development method. As is shown in Figure 2, first, some descriptive conclusions are extracted from data. Second, confirm these descriptive conclusions through collected data and revise them until they have good consistency. Third, based on the descriptive conclusions, some prescriptive theory are extracted and then confirmed. The above process will be checked and dittoed several times and finally, the prescriptive theory will be proposed.

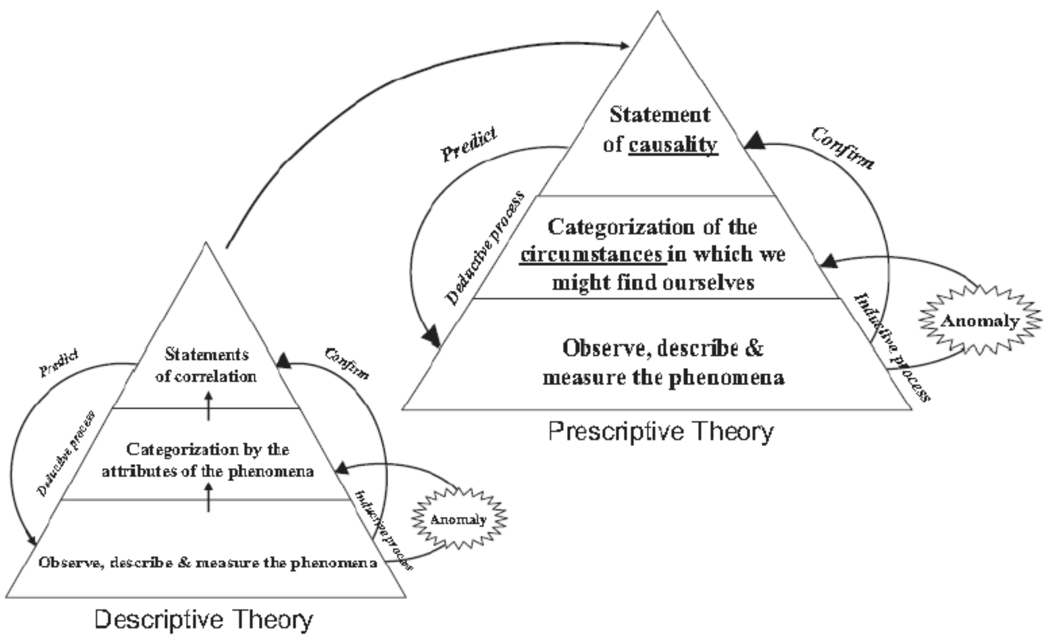

Figure 2 : The Transition From Descriptive Theory to Prescriptive Theory

Source: Clayton M. Christensen, Academy of Management Learning & Education, 2009, Vol. 8, No. 2, 240–251.Course Research: Using the Case Method to Build and Teach Management Theory.

V. Data Sources

In this study, data were mainly collected from interviews with Japanese expatriates, who worked overseas for once or several times. There are 9 in-person interviews in total and every interview is about 1-2 hours.

The expatriates are representative and are selected from different companies of different industries optionally, as is shown in Table 3. Most of them are managers and some are consultants and other staff etc. As industries, there are service industry, manufacture, Assurance Company and trade firm. Half of them worked as an expatriate in the high level economy growth period (before 1990s) of Japan and half of them worked after that, in the economic depression period. All of the expatriates in this study are male since female expatriates in Japanese multi-national corporations are very rare. The age range in interview is from 30 years to 78 years old. The work place includes China, India Sri Lanka, Saudi Arabia, Syrian Arab Republic, America and English. Some of them have been expatriated to different countries for 2-3 times. Every time they work about 1-6 years.

Table 3 : Data summary

Mr.	Frequency	Age	Year	Work place	Occupation	Career path after leaving for the new assignment	Industry
1	1	51-52	2007	China	GM	Removed from duty on the way	Service industry
2	1	55-56	2008	China	GM	Repatriated but left to another company a little later	Service industry
3	2	58-62	2007-2011	China	Chief consultant	Turned to work in another local Japanese company after the first term	Service industry
				America	HR Manager	Repatriated	Manufacture
4	1	32	2007-2011	China	Deputy GM	Repatriated	Service industry
5	1	30	2007-2011	China	Consultant	Repatriated	Service industry
6	2	46	1994	Saudi Arabia	Manager	Repatriated	Manufacture
		57-59	2005-2007	India	Manager	Repatriated and retired	
7	3	28-33	1964-1969	Saudi Arabia	Manager	Repatriated	Oil development
		58-60	1994-1996	Sri Lanka	Manager	Repatriated and retired	
		67-68	2003-2004	Syrian Arab Republic	Manager	Repatriated	Jetro
8	1	40-45	2005-2010	America	Staff	Repatriated but left to another company a little later	Assurance company
9	2	28	1961	English	Staff	Repatriated	Trade firm
		38-42	1971-1975	English	Manager	Repatriated	

VI. Analysis of Data

a) *The degree of expatriation success and repatriation success*

As Morishima (2000) stated, the culture characteristics in Japanese society is collectivism and there people emphasize the importance of 'belonging,' or being a member of a large entity such as a group or organization. Therefore, the traditional psychological contracts in Japanese companies are relational. The result of interviews with expatriates in this study shows the same trend. Before 1990s, in the high level of economic growth period, most expatriates repatriated to their headquarters and the retention rate of repatriated employee was higher than those after 2000s. After repatriation, these expatiates had attractive future assignments and at the same time, their job responsibility were enlarged, such as Mr. 4, 5, 7&9. Both the expatriates and multi-national corporations had high loyalty. The proposition 1&2 in Table 2 are proved basically.

On the contrary, after 2000s, because of the economic depression of Japan, most expatriates in Japanese corporations repatriated, but after repatriation, some of them have no fitful position and have to leave from the company after several years, such as Mr. 2, 6&8. The expatriates had high loyalty and wanted to serve for the company for a long time but finally they have to leave. The proposition 5&6 in Table 2 are proved basically. And in the case of Mr. 1, the expatriate had some problems in his health and he also had high loyalty. But he didn't have good work performance although he worked hard to some extent. Then after about 1 year, he was replaced by another expatriate from the headquarter. This case also reflected proposition 5 & 6 in Table 2.

On the other hand, some expatriates who are older than 50 years old did not repatriate as scheduled. Some of them leave to another local company after they finished the expatriation assignment, such as Mr. 3. The loyalty of expatriates and multi-national corporations is becoming low. It shows that the psychological contracts between expatriates and multi-national corporations have changed. It is different with what they were 20 years ago. The economic depression of Japan brings poor business performance to a part of corporations and many employees had their salaries cut down. Even some corporations have the plan of lying off employees. Therefore, the economic depression brings opportunistic behavior to both corporations and expatriates. The proposition 7&8 in Table 2 are proved.

Proposition 1

The economics of Japan determinates the Human resource system and makes it change from career employment to performance-based pay system. And in addition, the Human resource system influenced the psychological contracts between expatriates and Japanese multi-national corporations.

b) The effect of age and career stage to repatriation success

According to age and career related theory, one's age and career stage have influence on the psychological contracts between him or her and the organization. In the cases from interviews with expatriates in this research, in the economic depression period of Japan, almost all of the expatriates who are older than 50 years old are not able to serve in their Multi-national corporation continuously, such as Mr. 1, 2, 3 & 6. Besides the economical reason, their age is also an important factor that effects their leaving from the organizations.

For an employee who is over 50 years old, there are many problems that affect their job performance, such as health situation, communication problems, except that they are elites and will become managers of headquarters or subsidiaries. In this situation, it is easy for their organizations to take opportunistic behavior, especially in an economic depression environment.

As expatriates themselves, most of them understand the situation very well. They will also try to seek job chances outside the present multi-national corporation if possible. Therefore, as is shown in the interview data, some of them repatriated to Japan but leave the headquarters after one or two years. On the other hand, one of them did not repatriated as scheduled and turned to another local Japanese company. Therefore, in this age and career stage, both the expatriates and their multi-national corporations' psychological contracts are usually transactional.

Proposition 2

In the high level of economic growth period, age and career stage does not affect repatriation success so much. But in the economic depression period, one's age and career stage affect an expatriate's repatriation success highly.

c) The effect of families to repatriation

Besides the factors of economic environment and the age and career stage of expatriates, some other reasons affect an expatriate's repatriation success, such as family factor. According to the interviews with Japanese expatriates, parents' health problems, spouse related aspects and children education conditions effect their repatriation decision.

Some expatriates need to repatriate as scheduled but some of them repatriated before the termination of term. There are some family reasons, for instance, their parents have got some serious disease, their spouses are not used to the foreign life style in the local city, their children have to come back and attend elementary school. In such a case, expatriates would have to come back to work in their home country although maybe they have high loyalty and want to serve in the subsidiaries until the expiration of their term of service.

On the other hand, if an expatriate's spouse likes the local life very much and will not live in the home country any more, and if there are good job opportunities in the local country, the expatriate is more likely to stay with the spouse and refuse repatriation.

That's to say, the psychological contracts of expatriates will be changed although maybe they were relational if they have some serious family problems.

Proposition 3

In Japanese multi-national corporations, the family factor of expatriates, such as children's age, the spouse's willingness of departure for home and the health situation of parents will affect their repatriation timing and willingness.

d) The effect of job type to repatriation

As the agent of a multi-national corporation, expatriates' repatriation is also influenced by their job type. According to the interviews, many managers of overseas subsidiaries repatriated as scheduled. On the contrary, some senior engineers turn to other local companies or other countries where they can use their talent and get promotion and good working condition in the same time.

From the view point of psychological contract theory, employees expect ensured employment and good compensation through their hard work and organizations expect employee's hard work and good performance. And in Japanese multi-national corporations, employees who have good performance are considered as elites and will become managers or directors of the headquarters or subsidiaries. Additionally, every company has its unique enterprise culture, and the longer a manager works in the same company, the better he understand the enterprise culture. Therefore, it is very possible for managers to have a bright future in their present corporations. Furthermore, if they turn to other companies, their management experience about enterprise culture cannot be utilized in the same way as before.

On the other hand, senior engineers won't be so lucky as them because they have to face the threat of substitution of new technology. They have to keep learning hard rapidly. But it is difficult for an employee to accomplish this in a long term. Therefore, if they can't see a bright future in present company and at the same time someone outside the company offers a good job chance and compensation condition to them, they will choose to leave. Additionally, the technology they owned in the former company can still be utilized in the same way as in the next company although the outside work environment has changed. In this case, the organization has transactional psychological contracts and the individual also has transactional psychological contracts. If they receive the outside chance and leave the former company when the end of expatriate assignment period is coming, that is better than repatriation failure for both organization and expatriates. Proposition 7 and 8 in Table 2 refers to this case.

On the contrary, some senior engineers have excellent technology skills and can keep them change with practical needs rapidly. These elites always have chance to turn to other companies with better compensation conditions. In this case, the organization is very likely to have relational psychological contracts and the individual has relational or transactional psychological contracts. If the expatriate receives the outside chance and leaves the former company near the termination of expatriate assignment period, his or her psychological contracts are transactional. Therefore, this is the case of repatriation failure for the organization. In this case, Proposition 3&4 in Table 2 can be proved.

Proposition 4:

In Japanese multi-national corporations, job type is also an important factor that influences expatriates' repatriation success. Compared with senior engineers, managers are more likely to repatriate as scheduled.

VII. Discussion

While there are some theoretic and empirical studies on expatriation and repatriation, psychological contract related research in this area is insufficient. Based on psychological contract and other career theoretic analysis and interviews with expatriates from different Japanese multi-national corporations, this study offers a theoretical framework model with 4 propositions for future research on expatriate repatriation success. At the same time, the conclusions in previous literature can be proved by the data. According to theoretic analysis and interview data, it is shown that in Japanese multi-national corporations, expatriates' repatriation success is influenced by the psychological contract factor and the psychological contracts will be affected by several other factors, such as family reasons, job type, expatriate's age and career stage and the whole economic environment. Under the economic depression these years in Japan, the degree of expatriates' repatriation success is not so high as before.

As a human resource manager in a Japanese multi-national corporation, to raise the degree of repatriation success, he or she may take the following measures, for instance, considering family conditions and expatriates' age and career stage and doing long-term career plan, improving the compensation system and performing interviews with them on a routine schedule to increase expatriates' motivation, creating good training environment for expatriates to grow better. At the same time, if the careers of expatriates are well designed, the multi-national internal labor market will be stronger and the human resource mobility in a multinational corporation will be more active, which can enhance the corporation's efficiency and benefit its performance obviously.

As an expatriate in a Japanese multi-national corporation, to raise the degree of repatriation success, he or she may take the following measures, for instance, trying to increase job performance, performing interviews with the supervisor on a routine schedule to get a rapid feedback and propose some effective solutions etc.

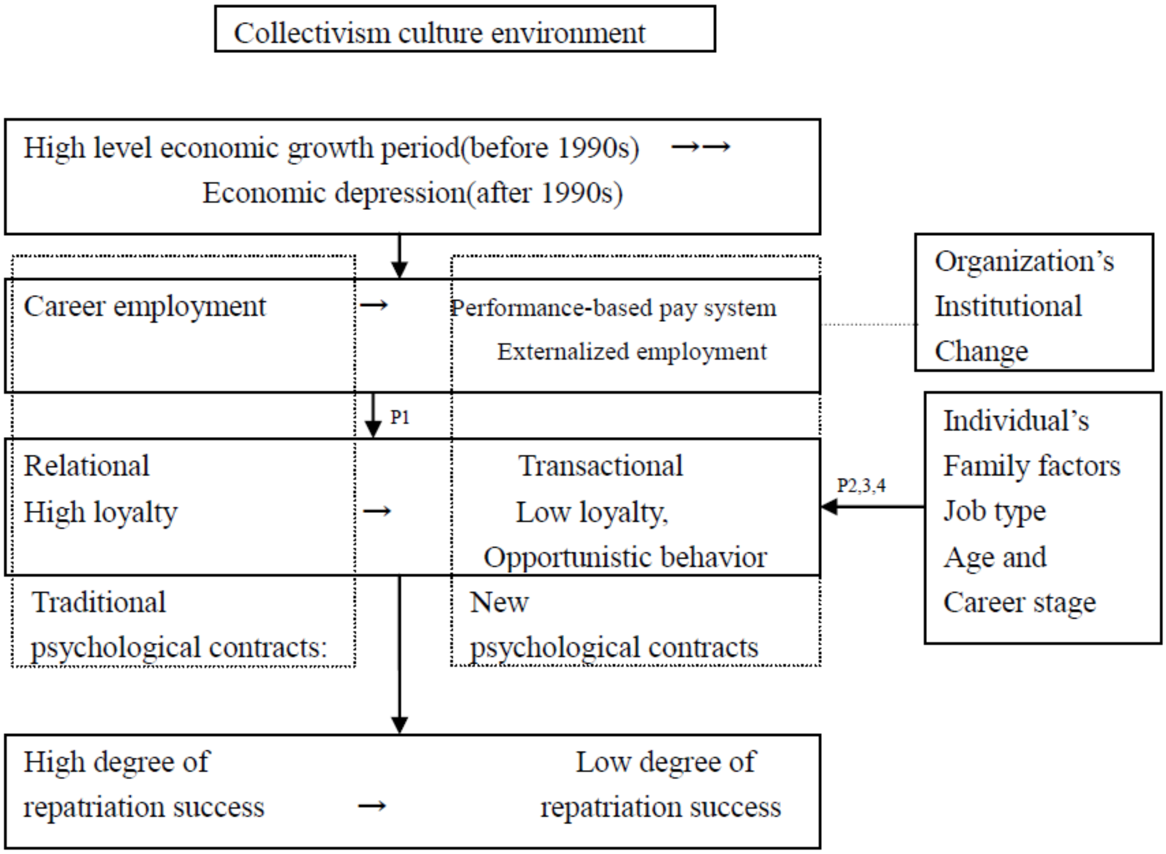

Figure 3 : Changes in Japanese expatriate's repatriation success and summarized propositions

VIII. Conclusion

The purpose of this research is to develop a general theoretic framework model (Figure 3) of expatriates' repatriation success in this new world by theoretic analysis and interview data from expatriates of Japanese multi-national corporations. The framework includes four aspects: the individuals, the organizations and the environment of culture, economy and institution change of Japan. Based on analysis of psychological contract theory, career related previous literature and the collectivism culture of Japan, the conclusion of this paper is as follows. In the high level economic growth period before 1990s, under the career employment system of a company and high loyalty of employees, the psychological contracts between individuals and organization were relational. Therefore, in that age, the degree of expatriates' repatriation success was high. After that, under the economic depression, performance-based pay system and externalized employment was inducted into Japanese corporations. This influenced the running of internal labor market in a multi-national corporation and opportunistic behavior happened in both individuals and organizations. Therefore, the degree of expatriates' repatriation success is lower than at that time. Beside the economical reason, family factors, job type and one's age and career stage also influence an expatriate's repatriation success of Japanese multi-national corporations.

IX. Limitations

However, this research is not perfect and some limitations are worth noting. First, there are some other factors that affect expatriates' repatriation success, such as business industry, enterprise performance, local human network etc. As the data of interviews is limited, these factors' impact should be discussed in future research. Second, the theoretic model and propositions are under the culture environment of collectivism. In other countries, there is different culture and concept of values and the model will be changed to some extent. There are more and more expatriates in this globalization world and I believe I can do better research in the future.

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Global Journal of Management and Business Research: B
Economics and Commerce
Volume 13 Issue 5 Version 1.0 Year 2014
Type: Double Blind Peer Reviewed International Research Journal
Publisher: Global Journals Inc. (USA)
Online ISSN: 2249-4588 & Print ISSN: 0975-5853

Pension Legislation for Federal Public Servants in Brazil

By Maria Chaves Jardim & Sidney Jard

Abstract– This paper addresses the creation of pension funds for federal civil servants in Brazil, analyzing the existing legislation and regulation on this issue. To this end, it takes off based on the genesis of the Brazilian private pension plans, logging the emergence of private funds as well as the existence of various laws and constitutional amendments prior to Law 12.618/2012, which provided for the pension funds system for Brazilian federal public servants. It also identifies proponents and opponents to the Foundation for Pension Funds of Federal Civil Servants (FUNPRESP), signaling the discursive construction of the pension fund schemes as central character in contemporary welfare capitalism. Finally, presents controversial aspects of the new pension fund law developments in Brazil.

GJMBR-B Classification: JEL Code: O40

PENSION LEGISLATIONFORFEDERALPUBLICSERVANTSINBRAZIL

Pension Legislation for Federal Public Servants in Brazil

Maria Chaves Jardim [α] & Sidney Jard [σ]

Abstract- This paper addresses the creation of pension funds for federal civil servants in Brazil, analyzing the existing legislation and regulation on this issue. To this end, it takes off based on the genesis of the Brazilian private pension plans, logging the emergence of private funds as well as the existence of various laws and constitutional amendments prior to Law 12.618/2012, which provided for the pension funds system for Brazilian federal public servants. It also identifies proponents and opponents to the Foundation for Pension Funds of Federal Civil Servants (FUNPRESP), signaling the discursive construction of the pension fund schemes as central character in contemporary welfare capitalism. Finally, presents controversial aspects of the new pension fund law developments in Brazil.

I. Introduction

On April 30, 2012, Bill No. 1992/2007 was transformed into Ordinary Law 12618/2012, whose main objective has been the implementation of pension funds for Brazilian federal public servants. The enactment of the new law represented a significant advancement in the implementation of the Constitutional Amendment 40/2003, sent exactly nine years ago to the Congress by the then President Luiz Inácio Lula da Silva (2003-2010). The new legislation has determined that the pension funds for public employees would be deployed as "defined contribution" and would be known as Foundation for Pension Funds of Federal Civil Servants (FUNPRESP). The main arguments made by advocates of the matter, in 2003 and 2007, as well as in 2012, pervade the social security crisis, excessive privileges of the public sector, and the quest for greater equity between public and private pension benefits.

In order to provide an understanding, even if provisional and exploratory of a theme as relevant (and current) for the economy, politics and society as this one, we present in this paper a critical discussion on the topic. The text is based on literature review, analysing of bills and constitutional amendments, and finally, collecting of material in the press seeking to outline proponents and opponents to the pension funds for civil servants in Brazil.

This reflection is motivated by previous studies, in which were showed the consolidation of pension funds as a central character in the Brazilian contemporary capitalism (Jardim 2007; Jardim, 2009; Jardim, 2010). Therefore, it is an extension of efforts to understanding the finance capitalism and its related characters (pension funds, insurance market, manag-ers, union pension funds, etc.). At the theoretical level, this text allows us to reflect on the similarities and differences between State and market institutions in the provision of social security welfare.

The text is divided as follows: it starts with the emergence of private pension plans in the Brazilian social security system, then it shows the various reforms (laws and contitutional amendments) leading to the creation of pension funds for servants and finally, in the last part, we analyse the discourses of opponents to and advocates who stand by the issue, as well as the controversies surrounding the pension reform in Brazil.

II. Creation and Regulation of Pension Funds in Brazil

The regulation of private pension plans in Brazil began during the military regime in 1972, stepping up from 1974 on. This debate appeared in Congress for the first time in 1976, when an Interministerial Commission drafted a preliminary bill to be sent by the Executive to the Legislature. This project was processed and approved by Congress during the Geisel Government in 1977 when the private pension activities in Brazil were institutionalized.

Therefore, the private pension formally came into existence in Brazil, with the enactment of Law 6435 of July 15, 1977. This law established that the activities of private security should be regulated and controlled by the State. Until then, entities operating in the market existed without any monitoring by the state and worked in isolation, without organization or dialogue among operators in the market. From the creation of Law 6.435/77, the pension market was expanded, and the private pension expression began to be used in Brazil. Before the 1977 law, entities that operated open private pension plans were called "montepios", whose origin dates back to the period of the Empire.

Law 6435 of July 15, 1977 set a maximum date for the regulation of existing private pension entities. Those who did not meet the standards of this law would be excluded from the market. This is the case of the montepios, many of whom were deposed by the National Superintendence of Private Insurance (SUSEP), which alleged irregularities in these institutions. The

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montepios approved had to be restructured to fit the new rules set forth by SUSEP. Menicucci (1994) reports that 180 montepios attended SUSEP for regulatory purposes, and of those, 120 were approved. Those approved had their old pension plans blocked and were forced to create new ones.

The pension funds of state enterprises that emerged in Brazil in 1977 had the following characteristics:

- strongly inspired by the pension funds of the United States;
- under the Government's interest and not the workers';
- in order to strengthen the capital market (stock exchange);
- strongly founded on public companies;
- modeled in Defined Benefit Plans.

To Menicucci (1994), through the 1977 legislation, the government made it clear that its goal was to gradually eliminate from the market the nonprofit organizations, represented by traditional montepios, and open space for profit organizations, encouraging mergers and acquisitions. Menicucci (1994) argues that the State saw in the private pension an instrument for capturing savings, i.e., it aimed to start in the country the internal logic of capital accumulation from funding through private pension. The savings generated by private pension funds would be invested in the economy.

In addition to the private pension model featured above, Law 109/2001 (replacing the 1977 Law) authorized the existence of a new device called plan "Institutor". Approved in 2001, in the government of Fernando Henrique Cardoso (1995-2002) and regulated in 2003, in the Government Luiz Inacio Lula da Silva (2003-2010), this device enables the creation and management of pension funds through unions, professional organizations, and others. Moreover, the pension reform of 2003 allowed the adoption of a pension fund for civil servants, the FUNPRESP, which is the subject of this text.

Therefore, since its regulation in 1977, the private pension has undergone significant changes throughout its history. Open and closed entities move together 25% of Brazil's GDP, and of this amount 18% of closed private pension and the remaining 7% of the open private pension (represented by the insurance industry). In turn, the market of pension funds has a total of 368 entities, which move the amount of 565 billion dollars. See the table below:

Table 1 : Number of Closed Supplementary Pension Entities - CVET by predominant type of sponsorship

Patrocínio	Quantidade de Entidades *	%
Instituidor **	18	4,9%
Privado	266	72,3%
Público	84	22,8%
Total	**368**	**100,0%**

*Number of Entities**
*Founder***
Source: Consolidado
Estatístico, junho de 2011.
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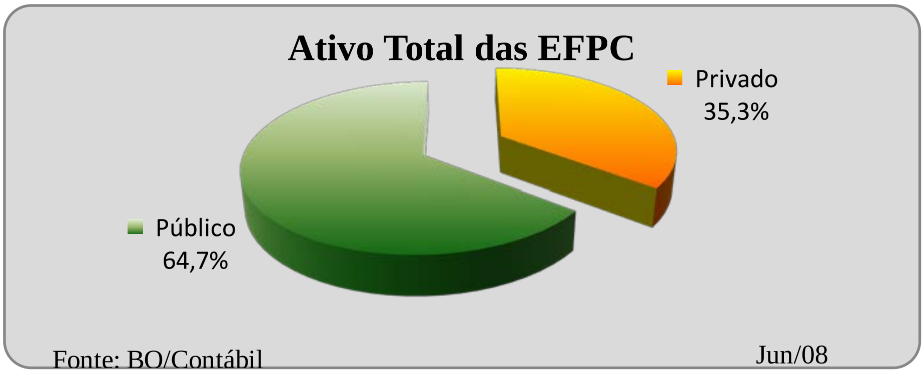
It is worth pointing out that even if the table shows a greater amount of privately sponsored entities (266), public sponsorship funds are the ones holding greater economic, political, and symbolic power in the social space of pension funds.

The following graph shows the total of assets controlled by public and private funds.



Graph I : Total assets of pension funds

Source: BO/Universo Cadastro, 2008

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Based on the graph above, it is possible to verify the superiority of public sponsorship funds (64.7%) over private sponsorship funds (35.3%), which hold greater symbolic power in the closed pension plan in Brazil. As per Jardim (2010), the funds of public patronage actively participate in the Growth Acceleration Program (PAC).[1] It is in the management of those funds that labor union members can be found, coming from the banking and oil industries, which greatly influence the investment portfolios of the pension fund market, to forge new forms of investment with sustainability criteria and strengthening institutional designs such as Investment Funds holdings (FIPs), also known as private equity.

From this context, we affirm that the private pension institution has existed in Brazil since the Empire, in the form of montepios. However, during the 1970s, these entities had the image worn by irregularities and possibly fraud committed by such institutions. This led many montepios bankrupt and as a result, consumers lost money and began to mistrust pension funds.

Distrust of Brazilian society in relation to pension funds began to turn in 2000, when it ceased to be associated with the image of bankruptcy, failure, and corruption to be associated with the development of Brazil. More specifically, the savings of those funds was (partially) used for the implementation of new projects in the Lula government, such as construction of dams, roads, railways, public housing, hospitals, etc.

Finally, in 2012, the market for private pension gained a new product, the pension fund for public employees. If we consider the rich market moved by pension funds, it is clear that over the coming years, the fund will be subject to great political and financial disputes.

Below, we discuss the legal transformations of the social security system for the public civil servants.

[1] The Growth Acceleration Program (PAC) was implemented in 2007 by Lula government and includes the budgets of the Union, states and municipalities and resources from private companies.

III. Legal Framework of the Brazilian Pension System

Since the Constitution of 1988, the pension system has undergone reforms, especially regarding the civil service. We present in this topic, the laws that sparked the emergence of pension funds to the public servants in Brazil. We shall begin with a table that summarizes the legal framework for the pension funds of public employees sector. These laws / amendments are detailed in the following pages.

Law/year	Details
Law No. 9.717 of November 27, 1998	The General Pension Law in the public sector imposes general rules for the organization and operation of specific social welfare regimen of civil servants of Federal, State, and Local Governments. It was determined that the RPPS were organized based on general standards of accounting and actuarial, with actuarial valuations and assessments to review plans and costing. In Article 1, it was established that funding systems themselves should use funds from Federal, State, and Local Governments and contributions of civil and military, active, inactive and retiree to their respective regimes. In Article 2, the Law set forth that the employer contribution may not be less than the employee contribution, or double that, leaving the Federal, State, and Local Governments responsible for covering the financial shortcomings of their own arrangement stems, a consequence to the payment of pension benefits.
Constitutional Amendment No. 20, December 15, 1998	It was sent to Congress for the 1st time in 1995 in order to cut costs. It was only approved in 1998 and it brought the following changes: the minimum age for full retirement based on time of contribution was increased to 60 for men and 55 for women; minimum of 10 years of public service and 5 years in office to enable programmable retirements, end of accumulation of retirement and the possibility of increased income in the passage to inactivity; extinction of proportional retirement and special retirement of teachers; replacement of retirement for length of service and time of contribution.
Constitutional Amendment No. 41, of December 19, 2003	End of parity between the adjustments in wages and social security benefits, passing the latter to be adjusted based on the inflation; pension became in full up to the RGPS and reduced to 30% for higher values; social security contribution on retirement and pensions higher than the RGPS limit; institution of time of service allowance equivalent to the amount of the contribution for service of the servant, who, although allowed to retire, can continue in activity. The possibility of Federal, State, and Local Governments establishing the maximum level for the benefit of the general social security scheme, for the value of pensions to be granted by the schemes, was instituted as long as they create complementary pension systems to their respective servants. It established the end of the parity and completeness.
Bill No. 1992/2007	Attempts to deploy a pension fund for civil servants (Funpresp). Based on this Bill, the person who goes into public service after the creation of the fund will have to contribute to it, if they want to retire earning more than the limit that already exists for the private worker at INSS, that is, 3.600 monthly in 2012. According to the 2007 Bill, the servants who enter public service after the initial operation of the Foundation for Pension Plans of the Federal Civil Servants (FUNPRESP) are subject to the maximum benefit. The participant's contributions should focus on that part of the proceeds that exceed the ceiling of the General Scheme, at a rate set by the participant, limited only by the regulation of the benefit plan. This means that, provided any new constraint to be adopted in the benefit plan, it is possible to contribute to the entire portion of the earnings that exceed the RGPS ceiling.

Source: Research data

Figure : Laws that promotes changes in the pension system

a) Law 9.717 of 1998

In November 1998 it was established Law 9717, which provides for the organization of Special Social Security Scheme (RPPS) for servants of the different government levels in the country (federal, states, and municipalities). Such schemes would be independent of the General Social Security System (RGPS), maintaining specific standards for servants (IPEA, 2011).

With the establishment of the RPPS, states and municipalities started to separate their pension accounts from other elements of income and expense in their budgets, and they were granted the possibility of accumulating financial reserves through investments in the capital market.

According to IPEA (2011), data for 2009 indicated 2,236 municipal RPPS(s) and 26 state RPPS(s). The Federal Government, however, have not unified until 2012, the pension management of their servants, whose management remains in charge of the various organs and powers that are linked to more than one million civil servants.

The following law, of December that year, further details the legal provisions brought by Law No. 9,717.

b) Constitutional Amendment No. 20 of 1998

Constitutional Amendment No. 20 of 1998, determined that the federal, state, and local governments should set up pension funds and that they could fix the ceiling of the RGPS for pensions to be granted to their servants. The law determined that the employer's contribution should not be less than the employee contribution, or double that, leaving the federal, state, and local governments responsible for covering the financial shortcomings of their own regime, due to the payment of social benefits.

Constitutional Amendment (CA) No. 20, introduced other changes in the pension system for civil servants, such as the determination that their regimes were contributory and funded by federal agencies as employers; to maintain financial and actuarial balance; and that it would submit to the supervision and control of the Ministry of Social Security (MPS).

Moreover, the same amendment imposed stricter conditions on retirement of servants; stipulated a ceiling to their remuneration (valid for pensions); extinguished the modality of special retirement for academics and forbade the accumulation of retirements within the same scheme (CA No. 20/1998, Federal Constitution of 1988, Article 40).

In the regulatory framework of pension funds of the servants, we cannot forget Complementary Laws No. 108 and 109 of 2001, which will be discussed next.

c) Laws 108 and 109 of 2001

The supplementary pension servants must necessarily be in accordance with Complementary Laws No. 108 and 109, 2001. According to the 2001 legislation, the creation of pension funds is optional, being the federal institutions authorized (not required) to establish complementary social security. In this case, the condition is setting the value of pensions based on the ceiling of the RGPS.

d) Complementary Law No. 108 of 2001

This Law regulates the restrictions on the relationship between state-owned enterprises, as sponsors of pension funds, and their closed private pension entities. These restrictions are in addition to the general rules to be observed by all the private pension system, whether in the sphere of public sponsors, whether in the private sphere. In addition to rule items to reduce the overhead of the state in funding closed pension entities, the law improves the means of supervision and imposes rules to ensure the financial stability of these entities.

e) Complementary Law No. 109 of 2001

This Law provides for the general rules for the system of private pension and replaces Law No. 6.435, of July 15, 1977. It can be argued that this law establishes essential conditions to "modernize" the system of private pension in Brazil, giving it greater flexibility, credibility, and transparency and strengthens the capacity of regulation and supervision by the state. It was through this law that labor unionists became part of the management boards of the pension funds of state enterprises (Jardim, 2007).

f) Constitutional Amendment No. 41 of 2003

As we have seen, the possibility of creating pension funds for civil servants was created in Constitutional Amendment No. 20 of 1998. But it was the end of parity and integrity brought by Constitutional Amendment No. 41 of 2003 that gave grounds to the interest in pension funds.

Therefore, the rights and criteria for access to retirement benefits and pensions of public servants were defined by Amendment No. 41 of December 2003. From this Amendment, the Ministry of Social Security (MPS) would make a pact about the pension adjustment of states and municipalities, which was done through the Support Program for Reform of State Security Systems (PARSEP) that provided support (including financial) for municipalities and states to organize pension funds. It is worth noting that states and municipalities are not required to maintain a RPPS. The federal entity can choose between having a RPPS or bind to the RGPS (IPEA, 2011).

In addition, the Amendment predicted the end of integrity of the value of pension benefits of public employees, as well as the end of parity between benefits and wages of active personnel. It also established an extra pension contribution (11%) for retired servants and pensioners whose earnings were above the RGPS ceiling (Brazil, 2009).

Based on this Constitutional Amendment, the servants who join the public service and want to get above the ceiling of ten minimum wages, may join the fund, collecting monthly from 6% to 9% of their gross salary. The amendment also adds that the funds raised must meet the following characteristics: be organized autonomously in relation to their own pension scheme; keep the membership of the servants optional; be governed by the principle of capitalization; allow full access to management information by the participants; make the contributions by the public entity equal to that of the participating servant (never higher). Finally, according to Constitutional Amendment 2003, only the executive branch can take the initiative to establish a supplementary pension system.

The approval of the CA brought the expectation that in the future the RPPS will coexist with FUNPRESP, intended for the retirement of servants. Discursively, the goal that motivated the government in creating the supplementary fund was seeking to balance the deficit of social security and the reduction of early retirement in the federal system.

g) Bill No. 1992 of 2007

The Project continued questions brought by CA 2003. However, it was "forgotten" during the last years of the Lula government and was only retaken in the spotlight of power in 2011, when President Dilma Rousseff claimed urgency in tackling the issue and project approval.

The intent of the Dilma government to take the matter further was explained when she triggered Mr. Silvio Costa (PTB-PE), chairman of the Committee on Labor, Public Service, and Administration of the House, to request priority to vote on the proposal. Within three weeks, Costa decided that he himself would be the reporter of the project, analyzed it, and presented a favorable opinion, approving it.

Specifically, Bill No. 1992 of 2007 aimed to create a supplementary pension for civil servants who hold effective positions of executive power, including its agencies and foundations, as well as members of the judiciary, public prosecution office, and the Court of Auditors.

According to the bill, the benefits to the new servants and members who join the public service would be limited to the ceiling of the General Board, which in 2012 amounted to 3.6 billion dollars. Remember that membership was not compulsory. By the rules established in Bill No. 1992 of 2007, the servants who join the public service until the day before the beginning of the operation of the entity responsible for the private pension, may join the pension funds system, being limited to the ceiling of their general scheme benefits but also being entitled to a special benefit.

The scheme will be offered by public-character closed private pension entities, which shall offer to its participants, benefit plans only in the form of "defined contribution”.

Under current pension rules of the servants, possible shortcomings of cash for the payment of benefits are covered with resources from the treasure of several governing levels to which the beneficiaries are bound. As public revenue comes from taxation, the whole society is responsible when the government needs additional resources to finance the pensions of their servants. So, if defined benefit plans were adopted, the same situation would remain as before, in the sense that the costs of any solvency risks of these plans would also be transferred to the company as a whole (IPEA, 2011).

The bill states that FUNPRESP must be fully maintained by their revenues, arising from contributions from participants, beneficiaries, and sponsors; the financial results of its applications and donations and bequests of any kind. That is, the value that will be received by the person retired in the public sector will depend on the contributions collected during activity and how these funds were invested in the financial market. In this sense, the risk is all on the insured.

However, the servant will have a portion of their pension benefit categorized as "defined benefit". It's limited to the RGPS ceiling value because, regardless of the existence of capitalization or not, the government will ensure that value to the retired civil servant. In this case, the risk is all on the employer, i.e., the government.

Therefore, the design of pension plans for public service provides a guaranteed income, which assures the minimal standard of living of the insured, via public security, while offering the possibility of complementation, which in turn depends on the individual accumulation of each person, via pension fund.

The bill also adds that the administration of the fund shall be held by institutions authorized by the Brazilian Securities Commission (CVM). The sole paragraph of Article 4 provides that FUNPRESP should be structured in the form of foundation with legal personality under private law enjoying administrative, financial, and managerial autonomy and headquartered in Brasilia.

Regarding its organizational structure, this will consist of the governing board, supervisory board, and executive board, respecting the laws No. 108 and 109 of 2001. On investments, the bill proposes that this be done pegged to indexes of market references, within the guidelines and limits of prudence established by the National Monetary Council to closed private pension entities.

Regarding contributions, the Bill proposes that the contribution of the participant should be decided by them, and the Sponsor’s contribution shall be equal to the participant’s, up to the limit of 7.5% (the government has studied the possibility of meeting the claim of social movements, increasing this ceiling to 8.5%).

The federal government, as well as the sponsor, appoints the majority of members in the administration of the fund. The monitoring will be the responsibility of the National Treasury, the Central Bank, and the Ministry of Planning. The fund will be capitalized by the defined contribution system (instead of the defined benefit system).

One last issue refers to portability, i.e. the bill allows the insured to bear or carry their capital to other supplementary pension institution. Portability is an institution already existent in the current pension funds (Jardim, 2009).

Finally, we affirm that Laws No. 108 and 109 of 2001, as well as Amendment No. 41 of 2003 and Draft Law No. 1992 of 2007 (processed at Annual Law 12618 of 2012) are part of a political context of dominance of finance, discourse of social security crisis, and political, economic and social implications for the creation of pension funds, considered the central character in contemporary capitalism (Orléan 1999; Farnetti 2005; Chesnais 2005 Aglietta, 2009) and important struggles in creating domestic savings (Aglietta, 2009).

In the next section, we will highlight the controversial aspects of the reform.

IV. Controversial Legal Aspects: Private Pension and Public Nature

In accordance with Law 12.618 of 2012, FUNPRESP is a foundation of private law but public nature (Michelon, 2011). Constitutional Amendment of 2003 provides the requirement that all entities of pension funds, which may be created by federal agency, must have characteristics of "public nature". To wit:

Article 40, Section 15. The supplementary pension scheme in § 14 shall be established by an act of the respective executive branch, subject to the provisions of Article 202 and its paragraphs, where applicable, through closed pension funds of public nature, which offer to their participants benefit plans only in the form of defined contribution. (Maimomi, A, 2004).

On the occasion of the 2003 pension reform, the Brazilian newspaper Folha de São Paulo brought the following criticism of the pension reform text:

The pension reform text passed in the House may limit the performance of pension funds that will be created to supplement the pensions of future servants and still allow governments, especially those of states and municipalities, to use the resources of those entities to invest in projects of public interest. (*Folha de São Paulo*, 08/08/03).

Likewise, the former Secretary of Social Welfare of Fernando Henrique Cardoso Government highlighted criticisms to the "public nature" of pension funds. According to him, thanks to the "public nature" characteristic federal, state, and local governments can use these resources in private interest investments. For the foregoing secretary, the "trend is that this occurs primarily in states and municipalities, where the control of resources is less strict." (*Folha de São Paulo*, 08/08/03).

It is worth noting that there is no clear definition in the legal debate about what a public nature pension fund of private law means. This can create statutory questions about the pension funds of public servants that may be imposed.

According to Meneguin (2011), the most reasonable interpretation of what the expression public nature means is in line with those who argue that the closed supplementary pension entity of the servants is of public nature for the quality of its participants (servants), the need to transparency in the management of assets and liabilities, inspection by the public sponsor, and accountability to society. Dal Bianco, Oliveira, Lima, and Cechin (2009) continue this argument emphasizing the fact that even though the participants are civil servants and the sponsors are public entities, it does not cause the accumulated assets to become public, nor that there is any subsidiary or joint liability of the public body for the maintenance of the social security scheme.

The arguments assume that the public nature of the regulatory instruments that shape this entity would be in conflict with each other (IPEA, 2011). On one hand, CA No 41 of 2003 provides that FUNPRESP have a "public nature" legal personality, on the other hand, Law 12.618 of 2012 determines that such a foundation is organized based on Complementary Laws No 108 and 109 and Article 202 of the Constitution, which provide that the closed private pension funds are governed by private law. That is, apparently, based on the Constitution, the expression "public nature" could not be understood as meaning "legal personality under public law".

In this sense, IPEA (2011) argues that the pacification of the conflict would be in the own text of Law 12.618 of 2012, Article 8, since it provides that the public nature of closed entities, referred to in Article 40 of the Constitution, consists of:

I. submission to the federal legislation on procurement and public contracts;
II. conducting public tender for hiring staff;
III. published annually in the official press or public administration official site digitally certified by accredited authority for that purpose under the Infrastructure Brazilian Public - ICP - Brazil - their accounting, actuarial, financial statements and benefits without prejudice to the provision of information to the participants and beneficiaries of the benefit plan and the regulatory and supervisory body of the closed private pension entities, in the form of complementary Law No. 108 and 109 of 2001. (IPEA, 2011).

V. Fragmentation of Pension Law: Three Power and Three Funds

Supplementary pension fund for civil servants should avoid the segmentation of assets among participants of executive, judiciary and legislative branches. This would undermine the effectiveness of the plan. First, because the greater the mass of resources applied, greater profitability, and second, because the operation of the pension fund involves administrative costs, which can also be greater if there are several entities. In this sense, IPEA (2011) argues that one should consider the union of the three powers in the same fund, as well as the possibility of participation of states and municipalities in the scheme. So the new pension fund would be provided with scale economy.

Throughout the voting process of Bill No. 1992 of 2007, this idea was shared by the federal government. However, the decision to create only one pension fund under the three powers created a controversial debate among the future categories of participants in pension system. Contrary manifestations by civil servant unions and the Senate itself took place since the government suffered a constant pressure to decentralize FUNPRESP, creating a fund for each power.

In March 2012, the government backtracked on the idea of creating a single fund for all three branches of government - Executive, Judicial and Legislative. In this perspective, the project was redesigned and there will be a unique fund for each power, which means higher expenses for the government. As per the statement of the Minister of Welfare, Garibaldi Alves, on the theme: "All claims of the parties were served, as well as of the trade unions. All that emerged was clarified and answered. There is nothing pending". [2]

Besides agreeing with the creation of a pension fund for every power, the Minister added that these will be administered by the participants themselves, not by a third party, as provided in the initial design. He also noted the possibility of contribution of 8.5% to Federal funds (and not only 7.5% as originally proposed). [3]

Regarding the criticism that the plan will come out more expensive, the Minister replied that: "It will be more expensive because of administration costs. But this is a claim of sectors, especially the Judiciary". [4]

By indulging and allowing the creation of three pension funds, the government also eliminated another controversy of the law, namely, the administration of the fund, as entities linked to the Executive, Judiciary, and Legislative since civil servants were complaining about lack of representation in the Board of Directors of FUNPRESP.

VI. Opponents and Supporters of the New Law

The theme has instigated several controversies, especially about its subtext of privatization of social security, the social security deficit, and the public nature of pension funds. Public servants have been reticent to that proposal and have been organized from the National Federation of Federal Public Servants (COND-SEF). Campaigners against the reform claim that FUNPRESP will create legal uncertainty in the category. To wit:

> This project represents the death of the pact between generations in public service. It will create three categories of servants: those who have already retired and those who are expected to retire, and in theory still be entitled to full pension and those who come after regulation of complementary retirement, which will no longer have this right. There are also those who entered after 2003, which will fall in a legal vacuum that nobody knows what will happen. This creates considerable legal uncertainty in the category. (3rd Meeting of Retirees and Pensioners DS Campinas/Jundiaí, Speech made by the Auditor Mr. Marcelo Lettieri Siqueira, from DS Ceará *"Previdência Social: a importância do pacto entre gerações)"*.

The argument of breaking the solidarity pact promoted by social security, and the destruction of social security, was also cited.

> The leading thread of this model is the dismantling of the social welfare model based on solidarity between generations. Thus, Social Security is now regarded as a burden that costs money (...) New generations who did not live long periods of social instability are more sensitive to this speech. The reasoning is that it will be able to fund their own retirement fund and there is no reason to fund those already retired. (3rd Meeting of Retirees and Pensioners DS Campinas/Jundiaí, Speech made by the Auditor Mr. Marcelo Lettieri Siqueira, da DS Ceará *"Previdência Social: a importância do pacto entre gerações)"*.

To defend their arguments, opponents militants are inspired by bankrupted examples, as Chile's.

> In Chile, the pension fund for civil servants lost 48% of its revenues and had to increase the amount of contributions, taxing retirees and reducing the value of pensions. In the state of Michigan (USA), the pension fund for civil servants lost 80% of its reserves and pensions were reduced to ¼ of the value. (3rd Meeting of Retirees and Pensioners DS Campinas/Jundiaí, Speech made by the Auditor Mr. Marcelo Lettieri Siqueira, da DS Ceará *"Previdência Social: a importância do pacto entre gerações)"*.

On the other hand, advocates of pension funds for servants, also use international experience to support their arguments. Meneguin (2011) shows that in the 1980s, the pension system for civil servants of the United States worked as defined benefit and showed severe imbalance. To remedy the problem, the government proposed a major reform, which was passed by Congress in 1986, creating the pension scheme of federal civil servants in the United States, known as Federal Employees Retirement System (FERS). This plan is mandatory for new servants that were employed after the publication of the law and optional for all others. [5]

According to the Ministry of Social Welfare, in 2010 the Brazilian government spent U.S. $ 51 billion to cover the difference between what they earned in pension contributions from public workers and what it paid to 950,000 retirements of the category. It meant that there was, on average, a monthly allowance of R$ 4,300.00 for each inactive public servant. To the Minister of Social Security: "If we do not stop this bleeding (from the security of servants), Social Security will pay significantly. Incidentally, it is already paying[6]".

[2] http://g1.globo.com/politica/noticia/2011/12/fundos-de-pensao-para-servidores-e-icms-sao-prioridades-diz-mantega.html

[3] http://g1.globo.com/politica/noticia/2011/12/fundos-de-pensao-para-servidores-e-icms-sao-prioridades-diz-mantega.html

[4] http://g1.globo.com/politica/noticia/2011/12/fundos-de-pensao-para-servidores-e-icms-sao-prioridades-diz-mantega.html

[5] The author informs us that FERS is a pension plan that provides benefits from three different sources: a plan of the public social security system (standard for all U.S. workers), a defined benefit plan, and a supplementary defined contribution plan (Thrift Savings Plan – TSP).

[6] http://www.previdencia.gov.br/arquivos/office/3_110610-160738-086.pdf.

IPEA (2011) has also used efforts on the subject and stood in favor of the creation of FUNPRESP. According to the arguments made by IPEA, the introduction of pension funds for civil servants, with the consequent imposition of a ceiling on benefits in their own schemes, has the virtue of promoting greater equity among various sectors of the population. By establishing the maximum benefit, it promotes horizontal equity between servants and private sector workers, since the RGPS, which caters to the latter, already practices the maximum benefit by referring to the supplementary pension plan to workers who rely on income higher on retirement.

On the other hand, the measure will also promote greater vertical equity, since it will prevent the entire society to bear the costs of sometimes excessive retirement benefits and pension, generated by higher-income strata of civil servants.

For the IPEA (2011), the reform will reduce the "fat" existing in the civil service sector. According to the defenders of the existence of privilege in the public sector, despite constitutional reforms already undertaken, the pension rights of public servants and private sector employees remain quite distinct, being public servants in significant advantage, especially with regards to the expected values for retirement benefits and pension.

Despite the discourse statements of "successful" experiences, the critical wing of the project looks at the proposal with suspicion. In the opinion of Lettieri, for example, Bill 1992 of 2007 represents a serious risk to public servants and to the Brazilian society, since it is an ongoing policy of dismantling Social Security[7].

In this context, CONDSEF met with the Ministry of Planning and claimed the development of "workshops" with the economic and political areas to discuss the issue. "We do not agree with the assumptions of the government. He says that there is a deficit in the pension plan of the servants, but there is contribution evasion of the Executive, who does not collect what it should" [8].

VII. Final Provisions

As we see throughout the text, the possibility of creating pension funds for civil servants is present in the Brazilian legislation since Constituional Amendment No. 20 of 1998. From that date until 2012, 26 states and the Federal District have established their own benefit plans (pension funds).

However, the possibility of pension funds to the servants became more concrete since 2003, when we had the approval of Constitutional Amendment 41, which authorized the creation of FUNPRESP. The project was resumed in 2007 with Bill 1992, which provided for the deployment of funds. But it was only in 2011, during the government of President Dilma, that the theme occupied again the headlines and the discussions in the National Congress. On April 30, 2012, nine years after the welfare reform initiated by the Lula government, the private pension scheme of federal civil servants was finally established by Law 12,682.

The discursive production around the theme signals the existence of opponents and advocates, who are fighting for the approval or not of the fund, as well as the beliefs that comes along with it. In this sense, the content of the discourse litigation signals that the purpose of the creation of the fund is to reduce the social security deficit, with a solidarity contribution between the various participants, the servant, and the Federal Government, as well as reduce the privileges of the civil service, responsible for the social security crisis.

Therefore, the social security crisis was used by defenders of public employees pension funds as justification for the creation of private pension. However, studies indicate (Duval, 2007; Jardim 2002) that the debate on the social security system crisis is more a social construct imbued with ideologies, than an actual reality.

Regarding the reasons that influence the advocates of pension funds, these are political, but also economic. That is, considering the recent economic and social performance of the pension funds of public companies in Brazil (Previ, Petros, Funcef), as well as the quality and quantity of their domestic savings, the implementation of a pension fund for the servants is quite seductive. The formation of a pension plan is a powerful tool in raising money to invest in areas that the government considers important, such as infrastructure and financing of public debt.

As the public sector wages are higher than the private sphere, the amount of funds to be administered will, in relatively short time, even exceed the assets of the pension fund of Banco do Brasil (Previ), totaling in 2012, R$ 139 billion. It is possible that this perspective causes an extensive dispute among various groups of servants as well as a strong political interest, as observed in the management of pension funds of state enterprises.

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[7] http://www.dscampinasjundiai.org.br/site/documento_618_0__artigo:-estariamos-perdendo-a-fe-no-atual-sistema-de-financiamento-da-previdencia--por-marcelo-lettieri.html

[8] http://www.previdencia.gov.br/arquivos/office/3_110610-160738-086.pdf).

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Global Journal of Management and Business Research: B
Economics and Commerce
Volume 13 Issue 5 Version 1.0 Year 2014
Type: Double Blind Peer Reviewed International Research Journal
Publisher: Global Journals Inc. (USA)
Online ISSN: 2249-4588 & Print ISSN: 0975-5853

The Nature of Shareholding in Nigeria: Evidence from the Banking Crisis

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Introduction– When investors decide to buy shares or stocks in any company, there is the initial presumption that the company would in turn make profits which would then be delivered to them based on their investment. However, more often than not, there are cases where investors are faced with the situation whereby their investments could go down the drain due to bad corporate governance practices of the company-ies in which the investments are made. Bad corporate governance practices and indeed control fraud have led to insider abuse whereby directors have failed to perform their fiduciary duties in proper management of the companies' assets.

Keywords: corporate governance, corporate fraud, shareholder activism, banking crisis, corruption, Nigeria.

GJMBR-B Classification: JEL Code: E59, G29

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Strictly as per the compliance and regulations of:

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Simisola Iyaniwura [α] & Wole Iyaniwura [σ]

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I. Introduction

When investors decide to buy shares or stocks in any company, there is the initial presumption that the company would in turn make profits which would then be delivered to them based on their investment. However, more often than not, there are cases where investors are faced with the situation whereby their investments could go down the drain due to bad corporate governance practices of the company-ies in which the investments are made. Bad corporate governance practices and indeed control fraud have led to insider abuse whereby directors have failed to perform their fiduciary duties in proper management of the companies' assets.

These problems could be further compounded by the ignorant or complacent nature of shareholders with regards to their rights and responsibilities. In Nigeria, it can be said that shareholders are mainly faced with the problem of ignorance and in cases where they are actually aware of their rights; there is a passive nature of inexperience as to best approach possible in the circumstances.

That notwithstanding, the recent banking crisis in Nigeria which is the subject matter of this paper has created a lot of awareness relating to shareholder activi-sm in the country. These are seen in forms of Policies, Regulations and Scholarly Articles aimed at educating shareholders of their rights and responsibilities in the company.

In view of this, it is the focus of this chapter to examine the extent to which shareholders can be said to have contributed to the banking crisis in Nigeria, taking into account the first five banks declared by the CBN as financially unstable. These are Oceanic Bank, Interconti-nental bank, Union bank, Afri bank and Finbank. The paper will commence with an analysis of the concept of ownership and control, examining the agency problem associated with director-shareholder relationships. This will then be followed by an investigation of the legal position of shareholders rights and responsibilities in Nigeria, using the Companies and Allied Matters Act, 1990 (CAMA) and the SEC Code for Shareholders, 2007. There will be a discussion of shareholder meetings and voting rights, following which the nature of Share-holder activism in Nigeria will be explored. The paper seeks to argue that apart from ignorance and illiteracy on the part of the shareholders, the general state of corporate governance practice in the country has been influenced by institutionalised political corrupt-tion, corporate fraud and regulatory manipulation to which shareholders are victims.

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II. Separation of Ownership and Control: The Agency Problem

Generally, an organization is more likely to survive when it produces goods to customers at the lowest price possible while still covering costs.[1] Fama and Jensen[2] examines the separation of risk bearing and decision functions observed in large corporations, otherwise known as ownership and control respectively and argue that the contract structures of organizations generally tend to separate the ratification and monitoring of decisions from the initiation and implementation of the decisions.[3] This hypothesis will be analysed in detail below.

They start by referring to the definition of an organisation as posed by Jensen and Meckling[4] to the effect that an organisation is made up of a totality of contracts, whether written and unwritten, among owners of factors of production and customers. According to them, these contracts are the 'rules of the game' and would specify two things: the nature of residual claims and the allocation of the steps of the decision process among agents.[5]

The nature of contract of organisations usually tend to limit the risk borne by most agents; and this is achieved by specifying fixed promised payoffs and incentives that are attached to measures of performa-nce. The risk of the probability of cash flows to promised payments to agents (otherwise known as the residual risk), is borne by another set of agents identified by Fama and Jensen as the residual risk bearers or the

[1] This will be analysed subsequently in detail.
[2] Fama, E.F., Jensen, M.C. 1983. "Separation of ownership and control", *Journal of Law and Economics*, 26, 301-25.
[3] Fama and Jensen *supra* at p. 302.
[4] Jensen, M and Meckling, W. (1976) Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure. *Journal of Finan-cial Economics,* 3, 305-360.
[5] Fama and Jensen *supra* at p. 302.

residual claimants.[6] However, mention must be made of the fact that most agents' contracts explicitly provide that the agent consents that in the exchange of a specified amount, the resources he provides can be used to satisfy the interests of the residual claimants.[7]

The effect of having most of these risks borne by the residual claimants would create a survival value whereby lesser costs would be incurred to monitor contracts with the other group of agents. Furthermore, it would lead to more production at lower costs which would not only increase net cash flows, but also contribute to organisation's survival.

They then examined the way organisations allocate the various steps of decision process across agents as a vital element of survival for the organisation.[8] They explain this through four steps of decision processes. First is the initiation stage which, to them involves the series of proposals which are utilized for structuring of the contracts; this is then followed by the ratification stage where the choice of decision initiatives to be implemented is made. The third stage involves the actual implementation and execution of the decisions so ratified; while the last stage involves monitoring, that is, the measuring the performance of the decision agents and implementation of rewards.[9] They further group the initiation and implementation stage as being performed by the same agents and therefore termed *decision management* while the ratification and monitoring stage is known as *decision control*, performed by another set of agents. These two serves as components of an organisations decision process.

At the end, their analysis produced two complementary hypotheses about the relationship between decision systems and residual claims:

1. Separation of residual risk bearing from decision management leads to decision systems that separate decision management from decision control:
2. Combination of decision management and decision control in a few agents leads to residual claims that are largely restricted to these few agents.[10]

The above led them to conclude that where decision management and decision control functions effectively in one or more agents, it becomes effective in controlling agency problems that could arise between residual claimants and decision makers because the residual claims are restricted to the decision makers.

This agency problem identified by Fama and Jensen is in relation to 'costs' and is analysed below.

Tricker considers Agency relationship through the lens of the agency dilemma whereby directors seeking to maximize their own personal benefit, take actions that are advantageous to themselves but detrimental to the shareholders.[11] An important element in any agency relationship is trust. Tricker defines trust as an agreement between parties with asymmetrical access to information.[12] This is premised on the fact that directors are well knowledgeable in the conduct of business activities and are professionally trained to do so; therefore the shareholders must trust them to do their job.

Jensen and Meckling[13] define agency relationship as a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent. If both parties to the relationship are utility maximizers, there is good reason to believe that the agent will not always act in the best interests of the principal.[14] They further examined the ownership structure of a corporation, taking into account how the equity ownership by managers can be said to align their interests with that of the owners.

According to them, the principal is able to limit divergences from his interest through the creation of various incentives to which the agent can benefit from and engaging in monitoring costs aimed at limiting future deviant activities of the agent.[15] For example, providing bonding costs for the agent to guarantee that he will not harm the principal, and where this happens, ensuring that the principal is compensated. However, more often than not, there will be a discrepancy

[6] These are persons who contract for the right to net cash flows and can be said to be shareholders. See Fama and Jensen *supra* at p. 303

[7] Fama and Jensen *supra.*

[8] Fama and Jensen *supra* at p.303.

[9] See Fama and Jensen *supra.*

[10] Residual risk bearing is otherwise known as 'Ownership', while decision management refers to 'control'. See Fama and Jensen *supra* at p. 322-323.

[11] Bob Tricker, Coporate Governance, Principles and Practices, 2009 Oxford University Press, P. 219.

[12] Bob Tricker *supra.*

[13] Jensen, M and Meckling, W. (1976) Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure. *Journal of Financial Economics,* 3, 305-360.

[14] Jensen, M. And Meckling, W. (1976) *supra* at p. 310. It can be said that agency theory developed within economics and has since served as a foundation for most scholarly research in corporate governance and has provided foundation for a more powerful approach to theories of corporate governance. See Clarke, T. (ed) Theories of Corporate Governance: The philosophical foundations of Corporate Governance, 2004 Routledge, Robert A.G. Monks, Nell Minow: Corporate governance - 2nd ed. Oxford Blackwell Business, 2001, Eisenhardt K.M. , Agency Theory, An Assessment and Review, (1989) *Academy of Management Review,* Fama, E.F., Jensen, M.C. 1983. "Separation of ownership and control", *Journal of Law and Economics*, 26, 301-25, Jensen, M and Meckling, W. (1976) Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure. *Journal of Financial Economics,* 3, 305-360. As a theory, the principal-agent relationship lends more insight to shareholders and boards as entities. Also, as identified by Tricker (*supra* at p.220), activities and relationships within the board are treated as a black box and most research based on agency theory involved readily available data such as financial statements and director reports.

[15] *Supra* at p.310.

between the agents' decisions and decisions that would serve to optimize the interest of the principal. This is because it is generally not feasible for either the principal or agent to ensure that the agent will make vital decisions in the interest of the principal at no cost; generally, monitoring and bonding costs are usually incurred.[16]

Agency costs is defined by Jensen and Meckling to include monitoring expenditures incurred by the principal, bonding expenditures incurred by the agent, as well as residual loss.[17]

Going back to Fama and Jensen, organisations that tend to separate residual risk bearing from decision management are generally complex in nature because valuable information are then diffused among many agents of the organisation, therefore what we have in most complex organisations is a sort of 'part' separation because effective decision systems are diffuse. This is because where there are many residual claimants, it becomes a costly exercise for all of them to be involved in decision control; hence, the separation of residual risk from decision control, and this, no doubt creates agency problems residual claimants and decision agents. The separation of decision management and control at all stages in the organisation would ultimately help to control possible agency problems. This is because it would limit the power of individual agents to expropriate the interests of residual claimants.[18] Thus, the separation of decision management and control would be effective in complex organisations as they would both allow relevant applicable knowledge to be utilised as and at when due because they help to control the agency problems that is posed by diffuse residual claims. Furthermore, in decision control systems where decision agents bear little or no share of the cost effects of their decision, what is seen is a multiple-member board of directors that tend to ratify and monitor important decisions as well as choosing, rewarding and dismissing important decision agents.[19] This would then make it difficult for any form of collusion between decision management at the top and control agents; and this is what makes separation of ownership (residual risk) and control (decision management) a vital decision of an organisation.

[16] Otherwise known as pecuniary and non-pecuniary costs. See Jensen and Meckling *supra*.

[17] It is important to note that monitoring goes beyond measuring and observing the agents behaviour from time to time, it also includes practical efforts of the principal to 'control' the behaviour of the agent, such as operational rules, policies, and the likes. Residual loss refers to agency costs incurred despite appropriate monitoring. See Jensen and Meckling *supra* at p.310-311.

[18] Jensen and Meckling *supra* at p.323.

[19] Jensen and Meckling *supra*.

III. Nature of Shareholding Practice and Structure in Nigeria

As the most populated country in West Africa with natural resources ranging from crude oil to agriculture,[20] Nigeria has one of the largest Stock Exchange Markets in Africa, known as the Nigerian Stock Exchange (NSE).[21]

The Stock Exchange is a self regulating entity set up to support the SEC in supervision of its activities within the security market. The purpose of the NSE is to monitor compliance with the financial requirement of listed companies on behalf of the SEC.[22] In effect; this requirement measures the level of good corporate governance in any company. It seeks to protect shareholders interest by requiring prior approval of making annual report available to shareholders before the annual general meeting and this approval may be withheld in case of discrepancies in the report in which case it is subject to correction.[23]

The NSE started operations in 1961 with 19 securities listed for trading. The requirement for shares to be quoted on the market initially received a lazy response and as at 1970, only 20 companies had their shares quoted in the market, even though there were about 2000 foreign owned enterprises in Nigeria at the time.[24] However, today there are 260 Securities listed on the Exchange, made up of 10 Government Stocks, 55 Industrial Loan (Debenture/Preference) Stocks and 195 Equity / Ordinary Shares of Companies, all with a total market capitalization of N875.2 billion.[25] Most of the listed Companies in Nigeria have foreign affiliations and cuts across various sections of the economy ranging from Agriculture to manufacturing and services. The largest Plc listed on the exchange, Dangote Cement has an asset value of $2.1 Billion and a Market value of $12.5 Billion. Being the richest company in Nigeria, it ranks 1434 position in the list of the World's Biggest Public Companies.[26]

[20] The 2009 estimates revealed that the country's total population is in excess of 154 million, The Nigerian economy is largely based on Oil production which accounts for about 80% of its Gross Domestic Product and more than 90% of its exports. See http://www.Mbendi.com.energysector.html Last accessed 06.08.13.

[21] Formerly known as the Lagos Stock Exchange, the Nigerian Stock Exchange is the second largest stock market in Africa The first being the Johannesburg Stock Exchange (JSE): http://www.advfn.com/StockExchanges/about/JSE/JohannesburgStockExchange.html Last assessed 27.08.11.

[22] Source: NSE Website available at: http://www.nse.com.ng/AboutUs/Pages/The-NSE.aspx last accessed 20.10.13.

[23] NSE Website *supra*.

[24] Elewechi N. M. Okike, Corporate Governance in Nigeria: the status quo, 2007 *Volume 15 Number 2 March* p.173 – 193.

[25] Figures as at 2003. Source: The Nigerian Stock Exchange available at: http://www.nigerianstockexchange.com/quoted_companies.jsp Last Accessed 06-08-2011.

[26] See http://www.forbes.com/global2000/#p_144_s_acompanyRankOverall_All_All_All Last accessed 06.08.2011.

What is known as the Federal Republic of Nigeria was a former colony of Britain. The first companies to operate in Nigeria therefore were British Companies Chattered in England. Foreign companies had foreign ownership status that granted them absolute rights and privileges associated with it. Legal activities began in 1876 when Lagos, the then Federal Capital Territory was ceded to the British Crown. Following the amalgamation of the Northern and Southern protectorates in 1914and the establishment of a Supreme Court for the whole country, an Ordinance was also promulgated for the whole country. Section 14 of the new Ordinance provided that:

'Subject to the terms of this or any other Ordinance, the Common Law, the Doctrines of Equity and the Statutes of General Application which were in force in England on the 1st of January 1900, shall be in force within the jurisdiction of the court'.

The above provision laid the foundation of Company Law in Nigeria as the English Common Law and Doctrines of Equity as it applied to English Company Law became applicable to Nigeria. The Companies Ordinanceof1912 was the first Company law in Nigeria, based on the English Companies (Consolidation) Act of 1908.

The independence of the country in 1960 necessitated the need for local control of public infrastructure. In this regard, the government effected a major change in ownership and control structure of Nigerian corporations prohibiting absolute ownership by foreign investors.[27] The activities of the government in the encouragement of local participation in economic activities led to the enactments of various Acts from 1962 to 1977. Two major legislations passed to this effect were the Foreign Exchange Act of 1962 known as the FX Act and the Nigerian Enterprises Promotion Decree (NEPD) No. 4 of 1972, often referred to as the Indigenization Decree. The purpose of these Acts was to reserve for Nigerians those areas where they had the experience and capital to run. The FX Act prohibited the transfer of security or interest of security outside Nigeria without the permission of the Minister of Finance. The NEPD on the other hand, in a bid to restrict foreign ownership created three types of enterprises[28]. First, there are enterprises exclusively reserved for Nigerians, which basically was a reflection of the Nation's economic, financial and corporate needs at the time. There were also enterprises in which Nigerians are not allowed to own more than 40% of shares in which case foreign companies had the opportunity to invest in the country, generating foreign capital and managerial expertise for Nigeria. The third sector was enterprises in which foreigners were not allowed to own more than 60% of shares and this included capital – intensive enterprises.[29]

The ownership structure of the country prohibiting 100% of foreign ownership made a lot of foreign corporations to divest their shares. However, due to lack of local investment funds at the time, government became the major shareholder of the divested shares, although few local investors bought a small percentage of the shares.[30]

Subsequently, the government became actively involved in the production sector of the country, either solely or as joint ventures with the foreign or local investors. In reality, the government policy on prohibition of absolute foreign investment in the country only operated to empower foreign investors as major partners with the government, leaving local investors as the minority. This, no doubt created abuse of minority rights as majority shareholders had control. Conflict between majority and minority shareholders remain a dominant problem of most developing countries with concentrated ownership structure.[31]

The independence of the country further envisioned the need to provide a more comprehensive legal framework that better meets the development needs of the country, particularly the promotion of indigenous companies. This necessitated the establishment of a Law Reform Commission to make recommendations on the future of the country's corporate sector while protecting the interest of investors, the general public and the nation as a whole.

The recommendations of the Law Reform Commission saw the birth of the Companies and Allied Matters Decree (now Act) 1990.[32] Part 1 and 2 of the Act provides that it shall apply to all companies formed and registered under it, as well as all existing companies, all companies formed or incorporated under other enactments and also all unregistered companies.

IV. Shareholders Rights and Responsibilities under Nigerian Law

Generally speaking, a shareholder is a part owner of any company who is also entitled to take part in the decision making of the company.[33] SEC provides

[27] Boniface Ahunwan 'Corporate Governance in Nigeria 2002 *journal of Business Ethics* 37: 269-287.
[28] Ss 4, 5, and 6 of the NEPD.
[29] Orojo, J. O.: 1992, *Company Law and Practice in Nigeria* Mbeyi and Ass. Lagos.
[30] Akinsanya, A. A.: 1983, '*State Strategies towards Nigerian and Foreign Businesses*', in L W. Zartman (ed.). *The Political Economy of Nigeria* (Preager, New York), p. 169.
[31] La Porta, R., F. Lopez-de-Silanes. and A. Shleifer:1996, 'Lavv and Finance' (National Bureau of Economic Research, Inc.) *Working Paper 5661* (1996).
[32] It can also be rightly said that CAMA is largely based on the UK Companies Act of 1948.
[33] See the Securities and Exchange Commission (SEC) Shareholders Rights and Responsibilities. p.7 Available at www.proshare.com. Last accessed 17.10.13.

that the shareholder is also entitled to access information regarding to performance or otherwise of the company as it is contained in its yearly annual report. There is no doubt that a shareholder benefits favourably in form of turnovers and profits, otherwise known as dividends whenever the company is doing well.[34]

CAMA provides for basic rights relating to shareholders which are highlighted below:[35]

1. The right to attend general meetings in accordance with Section 81 of the Act[36]
2. Right to speak and vote on any resolution
3. Right to vote in person or in absentia. Likewise, equal effect shall be given to votes whether cast in person or in absentia
4. Right to be furnished with sufficient and timely information regarding the date, location and agenda of the general meetings, as well as full and timely information regarding the issues that will be discussed at the meeting.
5. Right to ask questions from the board and to place items on agenda at the general meeting, subject to reasonable limitations
6. Right to be informed of any resolution appointing or approving the appointment of a director for the purpose of Section 256 of the CAMA[37]
7. Right to sue for dividends in accordance with Section 385 of the CAMA[38]
8. Right to have a copy of the Memorandum and Articles of Association, if any and a copy of any enactment which alters the memorandum in accordance with Section 42 of the CAMA
9. Right of a preference share to more than one vote in accordance with Section 143 (1)(3) of the CAMA
10. Right to conveying or transferring shares
11. Rights of sharing in the residual profits of a company
12. Rights to bonus and rights issue of a company
13. Right to inspect the register of members of the company
14. Right to be issued a share certificate within three months of the close of the offer pursuant to Section 146(1&2)
15. Right of shareholders vis-a-vis a prospectus that is being issued in an offer for subscription of shares by an issuer
16. Right to be represented in an audit committee of the company
17. Right to seek remedy in the case of aggrieved shareholders.[39]

SEC, in the 2007 Code for Shareholders Rights and Responsibilities further sets out basic principles developed to promote shareholder voting rights and to help enhance shareholder value in Nigeria. These principles are discussed below:[40]

To start with, as explained above, there exists a distinct relationship between shareholders and directors. This relationship is distinguished from normal contractual relationships with contractual protection.[41] Ordinarily, shareholders do not have contractual protection of their interests, but rather 'rely' on their elected board of directors and it is their responsibility to monitor and oversee the conduct of this board. As agents of the company, each director represents all shareholders and shareholders are entitled to expect that each director is acting in the interest of all shareholders and not in the interest of any majority shareholder or dominant stakeholder. Shareholders should be able to develop and maintain effective communication with directors through formal means. The board in turn, is responsible for representing the interest of the shareholders and when the board of directors fail to fulfil this fundamental obligation, shareholders are entitled to challenge the board based on this.

Flowing from the above, it can be rightly said that there exists a stewardship relationship between the board and shareholders. This relationship is based in accountability of directors on their performance and conduct in the company and use of company's assets and resources, although the articles of association usually reserves powers to the board of directors in the fulfilment of their duties. The collective responsibility of enhancing effective corporate governance lies in the hands of the board and this would normally mean a form of balancing relationship between the board, shareholders and stakeholders of the company.

An important and fundamental measure of the stewardship role of the board lies in the company's annual financial statement, which is simply an account of the financial performance of the company and management of its assets. Statutorily, all directors of quoted companies are required to provide annual financial statements.[42] It must be mentioned that the board and

[34] This is in the form of capital appreciation when the shares are actually worth more than when they are bought by the shareholders.

[35] See generally part IV, V and VIII of the CAMA. These are also highlighted in the SEC Shareholders Rights and Responsibilities *supra*

[36] Section 81 of the Act provides that every member of the company shall have the right to attend general meetings and vote provided that all sums payable with respect to their shares have been fully paid.

[37] Section 256 of the Act gives a restriction on the age of directors to 70, failing which a special notice is required of any resolution appointing a director above the age of 70.

[38] This defines dividends as special debts due to and recoverable by shareholders within 12 years and which is only actionable when declared.

[39] Remedy can be sought through the Investment and Securities Tribunal (IST) and the Administrative Proceedings Committee (APC) of the SEC.

[40] See SEC Shareholders Rights and Responsibilities *supra* at p.13-14

[41] For instance, customer-supplier relationships.

[42] See Section 331 -334 of CAMA.

not the external auditors is responsible for ensuring that the financial statements give a 'true' and 'fair' view of the company's financial situation for the year in question.[43] The board should therefore ensure that copies of the financial statements are sent to every shareholder and persons entitled to it.

Furthermore, there is the principle of one share to one vote with regards to shareholders.[44] This would mean that every member shall be entitled to vote on proportion to their economic stake and each share of ordinary stock should have one vote. In like manner, shareholders should be able to vote by proxy in an independent and confidential manner; this is to protect them from any possible undue influence and control. It is worth mentioning, that, although shareholders are very well entitled to proxy votes as an important tool by which they can perform their role in the governance of the company, where institutional investors have been entrusted with the investment funds of others, it is appropriate that they become active shareholders and help enhance effective corporate governance in the company in the exercise of their rights. As stated by SEC, institutional investors should also ensure that the internal corporate governance practices of the company come to terms with the global standards of accountability, transparency and judicial responsibility.[45]

Also, SEC provides for the principle of simple majority which applies to mean that shareholders should have the right to approve matters brought before the meeting by a simple majority of the shares voted. The procedure for voting is provided for in Section 224 of the Act, and is generally made with a show of hands.[46] The board is not ordinarily expected to impose super majority voting requirements unless this is done where there is a dominant shareholder in order to protect the interest of the minority shareholders. Voting should be made on each and every issue and done separately; the board is not to combine lump issues to be presented for shareholders' single vote. Also, approval of increase in the authorized number of shares shared should be brought before shareholders who are to ensure that such increases are made with their corporate interests in mind.[47]

V. Shareholder Meetings

One avenue where shareholders can exercise their rights especially when acting as a group is in a meeting. Shareholders' meetings are generally classed as 'General Meetings' to which all shareholders have the right to attend and vote.[48] CAMA identifies three types of meetings which are the Annual General Meetings (AGM)[49], the Extraordinary General Meeting (EGM)[50] and the Class meeting (CM).[51]

It is important to note that only persons with requisite authority can convene a meeting, without which a meeting would be said to have been convened in error, and the notice issued for such meeting would be said to be invalid, while the resolution passed would be said to be null and void.[52] The authorised persons that could convene a meeting include the board of directors, two or more shareholders with not less than 10 percent of the issued share capital of the company, shareholders with not less than 10 percent of the paid up share capital of the company and also any director in the case of an Extra Ordinary General Meeting upon requisition.[53]

By section 18 of the Act, the issuance of a notice is fundamental prior to the holding of any meeting and this is to be sent to all shareholders within 21 days from the date of the meeting. service of the notice can be done personally or by post to their registered adderss.[54] It is also paramount to state that for shareholders entitled to receive additional notice, it is the duty of the company to make sure that such notice is given to them and by Section 222 of the Act, additional notice must be given via 2 daily newspapers at least 21 days before any

[43] Section 335 of the Act. It is worth mentioning that financial statements and accounts were discussed in detail in the preceding chapter.

[44] See SEC *supra* at. P.11.

[45] See SEC *supra* at p.12. Institutional investors are financial intermedia-ries between lenders and borrowers charged with the role of acting as highly specialized investors on behalf of others. They include banks, insurance companies, pension funds and mutual funds. See http://www.investopedia.com/terms/i/institutionalinvestor.asp Last accessed 17.10.13.

[46] By Section 224 (2), unless a poll is demanded, upon declaration by the chairman that a resolution has, on a show of hands been carried unanimously, or by a particular majority shall be conclusive evidence of the face, without proof of the number of proportion of the votes recorded in favour of, or against the resolution.

[47] See generally Section 224 of the Act.

[48] Section 213 of the Act.

[49] Section 213 (1) of the Act provides that the AGM must be held each year, in addition to any other meeting in that year within a company's first 18months of incorporation, following which it must be held once a year, in mot more than 15months after the last AGM or not more than 6 months after the end of its financial year.

[50] The EGM's are specially convened meetings designed to discuss matters that are too urgent to wait till the next AGM. By Section 215 (2) of the Act, an EGM may be requisitioned by any shareholder(s) holding at the date of the requisition not less than one-tenth of the paid up capital of the company as at the date of the deposit carrying the right of voting, or in the case of a company not having a share capital, shareholders of the company representing not less than one-tenth of the total voting rights of all the shareholders having at the said date a right to vote at general meetings of the company.

[51] Class meetings refer to meetings held by holders of a particular class of shares, for example income shares, preference shares, etc and they are basically held with regard to the variation of rights that are attached to the class of shares.

[52] Failure to give notice of any meeting to any person entitled to receive it, invalidates such a meeting, unless such failure is based on an accidental omission. See generally Section 221 of the Act.

[53] See Section 215 of the CAMA.

[54] Registered address refers to any address which the shareholder has supplied for notice to be served to him. (Section 220 (5) of the Act). Where a notice is sent by post, by the provision of Sub Section 2 of the Section, this service is effected by properly addressing, preparing and posting the letter of service in the ordinary course of post, which is then deemed to have been effected after the expiration of 7 days.

general meeting.[55] Section 18 of the Act also specifies the content of the notice which must include the name, type of meeting, place of meeting, date and time of the meeting, as well as an overview of the nature of business to be discussed in the meeting so as to enable the shareholders to decide whether or not to attend, and in the case where a special resolution is to be considered at the meeting, the terms of this resolution shall be set out in the notice.[56]

It is important to also state that attendance of annual general meeting is to be taken rather seriously by the shareholders as this responsibility creates an avenue for shareholders to exercise their rights. The responsibility of the shareholders to act as watchdogs over the directors and managers of the company as a means to safeguard their investments is exercised through attendance of meetings where questions can be raised.

It is also worth noting that the shareholders are to ensure that the necessary quorum of meetings is attained and appropriate resolutions are passed during the meeting.[57] Section 233 of the Act distinguishes an ordinary resolution from a special one when it states that an ordinary resolution is one passed by a simple majority of votes cast by such members of the company that are being entitled to do so and who have voted either in person or by proxy at a general meeting. A special resolution on the other hand, is one that has been passed by not less than three-fourth of the votes cast by every member of the company entitled to do so, either in person or by proxy at a general meeting to which 21 days notice was adequately given, specifying the intention to propose the resolution as a special resolution.

Every meeting is to be presided over by a chairman who is to oversee the smooth conduct of the meeting.[58] The chairman is to act in the *bona fide* interest of the company, ensuring that the true intentions of the meeting are carried out with regards to all the issues raised before it.[59] The chairman has the power to adjourn a meeting pursuant to Section 239 (1) of the Act.[60]

VI. The Banking Crisis, Shareholders and the CBN

The global financial crisis in Nigeria which began in mid-2008 saw an adverse effect on all sectors of the economy, particularly the banking sector and Nigerian Capital Markets.[61] Subsequently, there was an immediate deterioration in value of assets owned by banks which posed liquidity issues across the affected banks. This led the CBN to conduct special investigations on all the 24 banks in the country at the time. It was not surprising that the investigations of the CBN confirmed peculiar challenges in the capital base requirements of these banks, owing to fraudulent practices and bad corporate governance.[62] The CBN also injected a total of N420 bn ($2.8m) of government funds into the five banks for stabilisation and finally nationalised some of the banks in 2011.[63] The nationalisation saw the acquisition and birth of new banks while the CBN delisted the old banks from trading at the NSE. The result of this created panic and distress on the part of the shareholders as some of them merely woke up, only to realise that the banks have been acquired with new names of management and boards announced and as a result, many shareholders were left putting up their shares for sale. The NSE claimed that the CBN had not consult the Exchange at any point during the recapitalization and takeover. It also expressed concern on the fact that the decision of the CBN did not take into account neither of majority or minority shareholders' interests who were gravely affected by the sudden takeovers.[64] Treats were being made by shareholders to sue the CBN for their action and also the NSE for not fighting to protect their interests, therefore making their shares worthless.

[55] Failure to give additional notice to such members that require it shall also invalidate the meeting as provided for in Section 221 above.

[56] The term 'special resolution' is defined subsequently in the course of the chapter.

[57] By Section 232 (1), unless otherwise provided in the Articles of Association, no business is to be transacted at any general meeting unless a quorum of members (i.e. shareholders) is present at the beginning of the meeting and throughout such meeting. Furthermore, the quorum of the meeting shall be one third of the total number of members of the company or 25 members, (whichever is less) present in person or by proxy (Subsection 2), and where there is a quorum at the beginning, but no quorum at the end due to any of the shareholders leaving for whatever reason, the meeting shall be adjourned for a week to the same place and time, and if there is no quorum still at the adjourned meeting, the members present then shall be the quorum and any decision made at the adjourned meeting shall bind other shareholders and where only one member was present, he may seek the direction of the court to take a decision. (S. 232(5)).

[58] See generally Section 240 of the Act. Where the chairman is not present within one hour of the meeting or where he is unwilling to act, the directors shall choose one of its members to act as chairman and in case where no director is present within one hour of the meeting or where none is willing to act, the shareholders are entitled to choose one of them to preside over the meeting as the chairman.

[59] Duties of the chairman also include: ensuring that proceedings are conducted in a regular manner as well as making sure that all issues brought before the meeting are promptly decided. See Section 240 (3) (a-e) of the Act.

[60] This is done with the consent of members present at the meeting which must also be in a quorum. See Subsection 1-4 of Section 239.

[61] Another major sector affected was the Oil and Gas sector.

[62] Details of the investigation have been explained in previous chapters. However, for the purpose of illustration, relevant aspects will be utilised to explore shareholders' activities as it affects the banks in question.

[63] Source: http://www.thenigerianvoice.com/nvnews/57904/1/nationalised-banks-shareholders-to-sue-cbn-ndic-am.html. last accessed 18.10.13.

[64] Source http://www.thenigerianvoice.com/nvnews/57904/1/nationalised-banks-shareholders-to-sue-cbn-ndic-am.html Last accessed 18.10.13.

Series of opinions were given in reaction to the issue. Notably, the MD of Resource Trust and Company Limited (RTC)[65] explained that the NSE had failed in its fundamental duty of protecting investors, concluding that the NSE could, indeed be said to be complicit in the series of events that have led to the banks' abuses and problems that created the nationalisation of these banks.

The ultimate losers in the banking crisis were investors who lost significant amount of money at the NSE on a weekly basis. In one day, investors lost N141.96 billion as the total value of all the shares listed at the Exchange dropped from 7.203 trillion from N7.345 trillion to 7.203 trillion. Furthermore, the All Share Index dropped from 22,963.11 points to 22,519.32 points, a decline of nearly 1.93 per cent. The NSE Banking index also declined by 4.22 per cent; from 317.33 points to 303.93.[66] This decrease was brought about by the massive decline in the share price of majority of the banks.

The question which then comes to mind is whether or not one or more of the shareholders could have been part of the activities that led to the banking crisis and problems in the NSE. Evidence published by the CBN reveals that companies and individuals owe the five banks a total of N348.409 billion.[67]

It is important to emphasize that many of these non performing loans were granted to companies, some of which were wholly or partly owned by the CEO's themselves and the rest by customers of the banks. There is no evidence on the list published by the CBN to suggest that individual shareholders were part of the debtors.[68] It therefore suffices to say that majority of the non-performing loans were granted to customers and CEO's of the banks (In the name of their companies), who, by all indication would have been part of the ongoing control fraud.

What is also not surprising is that the CBN published list of debtors includes names of renowned dignitaries, top politicians and business men across the country. However, what is shocking is the revelation of two presidents of the Nigerian Stock Exchange as major debtors in these banks. First is Forbes rated richest man in Nigeria and the then NSE president, Aliko Dangote[69] who, according to the CBN has a non-performing loan of N2.5 billion with oceanic bank which was secured through Dangote Industries Limited;[70] Second is Mr Oba Otudeko, an immediate past president of the NSE owes N1.6 billion to Oceanic bank through his company, Honeywell Group.[71]

Questions that would come to mind at this stage is: How come the shareholders did nothing to stop the fraud? One possible answer would be that they were probably ignorant of these frauds. As the banks showed no apparent sign of distress, publishing financial statements that suggested economic boom, it is possible that the shareholders were indeed unaware of the insider abuse. However, it remains to be said whether they their ignorance is due to their passive nature where they were unaware of their rights and responsibilities.

The revelation of the CBN upon its special examination of these banks triggered questions by the shareholders to the CBN, NSE, directors and management of these banks, demanding that due process be followed to ensure that the relevant persons are held accountable for their actions.

One case is that of Afribank, now known as Mainstream Bank Limited.

Upon the initial sacking of the CEO's of the five banks in 2009, a number of Afribank's shareholders, namely; Igbrude Oke, Rasak Mumuni, Akinsanya Sunday, Suleiman Babatunde and Igba Olatomide, in a bid to request for the result of the special examination, had, on behalf of themselves and other shareholders of the bank[72] challenged the CBN's action at the Federal High Court in Lagos where the Trial Judge, Justice James Tosho, held in a ruling that the CBN did not have the absolute power to hire or fire bank directors without disclosing findings of the so called 'special examination' conducted into the financial statements of these banks and their affected directors.[73] The court further held that although he CBN had power to regulate and control the business activities of these banks under Section 35 of

[65] The RTC is a company that helps to provide support and advisory services to Market clients within various sectors of the economy. See http://www.resourcesandtrust.com/services.html last accessed 15.10.13.

[66] Figures of the 9th of August 2011. Source: http://www.thenigerianvoice.com/nvnews/57904/1/nationalised-banks-shareholders-to-sue-cbn-ndic-am.html Last accessed 18.10.13.

[67] Source: CBN list of debtors available at: http://www.cenbank.org/Out/publications/pressRelease/GOV/2009/ADVERTORIAL2.pdf last acessed 15.10.13.

[68] See the CBN list of debtors *supra.* It is important to state that the CBN had identified most of these debtors as Shareholders and Directors of the companies by which they borrowed these monies and most of these companies were owned by CEO's and employees of the banks. Others were monies borrowed by customers.

[69] See http://www.forbes.com/global2000/#p_144_s_acompanyRankOverall_All_All_All Last accessed 06.08.2013.

[70] http://www.vanguardngr.com/2009/10/cbn-releases-fresh-list-of-bank-debtors/ last accessed 10.10.13. see also the CBN publication *supra.*

[71] Other top bad debtors listed by CBN include Mr. Femi Otedola, N12.8 billion (Intercontinental Bank) through his company, African Petroleum Plc and another N6.2 billion is owed Union Bank through his Zenon Oil; and Mr. Jimoh Ibrahim, N14.78 billion (Oceanic Bank), through Global Fleet Industries Limited. - Source: http://www.vanguardngr.com/2009/10/cbn-releases-fresh-list-of-bank-debtors/#sthash.NMrZTvFW.dpuf Last accessed 17.10.13.

[72] See http://www.vanguardngr.com/2012/07/shareholders-appeal-afribanks-liquidation/ last accessed 15.10.13 http://www.vanguardngr.com/2012/07/shareholders-appeal-afribanks-liquidation/#sthash.8Km8U27a.dpuf

[73] Source: http://www.vanguardngr.com/2011/12/cbn-frustrating-our-case-afribank-shareholders Last accessed 17.10.13.

the BOFIA, disclosure should and must be made when such powers would substantially affect interested parties as in this case.[74] However, an appeal was launched by the CBN and its governor contending the decision, with a motion for stay of proceedings pending the determination of the appeal. However, while the matter was still pending in the appeal court, the CBN, in collaboration with the Nigerian Deposits Insurance Commission (NDIC) and the Asset Management Corporation of Nigeria (AMCON) nationalised Afribank.[75] The shareholders then filed a motion to nullify the nationalisation, claiming that it was done pending an appeal and also in disrespect to the court and that the CBN had filed the motion for stay of proceedings in order to frustrate the diligent prosecution of the case.

The above scenario was further compounded when the CBN filed another suit at the Federal High Court in Lagos, winding up the bank. Justice Charles Archibong, in his decision, wound up Afribank on the ground that the bank had been delisted by the CBN and therefore had no licence to continue to operate.[76] Further efforts of the shareholders to challenge the decision have proved abortive till date.

From the above, it can be said that the shareholders of Afribank were ignorant of the insider abuse and control fraud in the bank and the revelations of the CBN triggered their demand for questions. However, these attempts of shareholders to demand for answers have been frustrated and while it can be rightly said that the CBN acted ultra vires its powers in sacking the CEO's without publishing the results of its special investigations, and subsequently winding up the bank, the judiciary is also to blame for turning a deaf ear to all the cries of the shareholders and ultimately carrying out a grave miscarriage of justice. The shareholders argued through their counsel, Mr Onyebuchi Aniakor, that the winding up order was made by Justice Archibong when the matter was stated for mention and not hearing.[77] Furthermore, upon the winding up petition brought by the CBN, the shareholders had made a preliminary objection to the petition, claiming that there was a pending suit before Justice Tosho of the same court and also arguing that the winding up petition is a calculated effort by the CBN to overreach the pending suit. What is surprising is that this preliminary objection was struck out by the court. A number of issues would arise, questioning the independence of the judiciary and the power and manipulation exhibited by the CBN.

However, in the case of Oceanic Bank Plc, now known as Ecobank, the shareholders, in an Extra-Ordinary General Meeting held with Ecobank on 23rd December 2011 approved the proposed resolution to merge both banks, transferring all assets, liabilities and undertakings of Oceanic bank, including real and intellectual property to Ecobank Nigeria. In consideration for the transfer of all assets, liabilities and undertakings of Oceanic Bank to Ecobank, the shareholders of Oceanic Bank are to receive a total of 16,111,111,111 billion new shares in Ecobank Nigeria, credited as fully paid-up; and N2, 600,000,000 to be credited to Oceanic Bank shareholders as deposit for shares in Ecobank Nigeria issued to Oceanic Bank shareholders as equity at N2.34 per Ecobank Nigeria share at a date to be mutually agreed by the shareholder of both banks.[78]

Perhaps what is seen in the case of Oceanic bank is management agenda control where the incentives offered for the merger led to its approval. However, what is seen is a situation where the shareholders were given an opportunity to vote for or against the resolution at the EGM, as opposed to the imposition of a decision.

VII. Shareholder Activism in Nigeria

Corporate governance embodies the totality of systems by which companies are directed and controlled[79] and this involves promoting fairness, accountability and transparency within the organisation, the frictions that arise due to this are sometimes expressed through shareholder activism.

Following the banking crisis in Nigeria, coupled with the activities of CBN, CEO's and the threat of collapse of the Nigerian Stock Exchange, shareholders have been awakened to their rights and responsibilities in Nigeria. A number of shareholder associations have been developed by shareholders as avenues for exercising their rights as a group. These include Proactive Shareholder Association, the Nigerian Shareholders' Solidarity Association and the Independent Shareholders' Association of Nigeria.

Adegbite and Amao consider the extent to which a country's local shareholder activism is a reflection of its brand of politics.[80] They describe shareholder activism as a corporate governance accountability mechanism, whether at the managerial or board level.[81] Shareholder activism consists of a variety of activities through which shareholders influence the management

[74] See http://ngrguardiannews.com/index.php?option=com_content&view=article&id=51578:court-dismisses-sanusi-others-objection-to-afribank-shareholders-suit&catid=1:national&Itemid=559 last accessed 12.10.13.

[75] The nationalisation of Afribank was done with two other banks: BankPhB and Spring Bank which saw the birth of Mainstreat Bank, a newly formed bank.

[76] Source: Vanguard news.16th July 2012 Available at: http://www.vanguardngr.com/2012/07/shareholders-appeal-afribanks-liquidation/ last accessed 19.10.13.

[77] See Vanguard News, 16th July 2012 *supra.*

[78] Source: http://www.vanguardngr.com/2011/12/ecobank-oceanic-shareholders-okay-merger/ Lass accessed 17.10.13.

[79] This definition is generally attributed to Sir Adrian Cadbury.

[80] Adegbite, E. And Amao, K. 'The Politics of Shareholder Activism in Nigeria' (2012) *Journal of Business and Ethics* 105: 389-402.

[81] Adegbite, E. And Amao, K. *supra* at p. 391.

and board. This can be in form of meetings, letter writing or associations as the case may be.[82] Gillian and Starks considers a shareholder activist as an investor who, thorough his voice, endeavours to change situations of concern, while not necessarily resulting to change in the firms control.[83]

There is no gainsaying that shareholder activism is peculiar to target firms and rationales for shareholder activism differ according to countries. However, contrary to the general view that shareholder activism is driven by the desire to maximize shareholders' wealth; there is evidence to suggest the need for responsible ownership as inclination to shareholder activism.[84]

Having said that, it follows that shareholder activism in Nigeria has been influenced by the political culture of the country. Corruption has mainly been a drawback for Nigeria since Independence and seemed to have eaten deep into as spheres of the economy, including the corporate sector. Adegbite and Amao, in their survey of the politics of shareholder activism in Nigeria, also considered the link between politics and pursuit of corporate interests and found that companies bidding for government contracts are forced to play by the rule of politicians.[85] The success of any business is therefore dependent upon its level of political will and support. Going back to the case of Afribank's shareholders, the level of political and power influence utilised to frustrate shareholder activism is shocking. While shareholders are constantly demanding accountability and transparency of directors, management and regulatory bodies, their activities are constantly undermined even at the judiciary l level where justice is meant to be done.

That notwithstanding, there is also a fundamental problem of misconception and misuse of shareholder activism by members to the extent that they are gradually being conceived as a threat to the organisations' day to day management.[86] This is based on the manner by which shareholder associations tend to comport themselves in the exercise of their rights, such as bullying and boycotting of AGMs. Commenting on this, Adegbite and Amao noted that some members of shareholder associations have expressed their concern on the way some of their members conduct themselves through negative publicity arising from threats and disruptions of meetings.[87] Perhaps this action is triggered out of frustration and as a means of cry for help, but to whom?

VIII. Conclusion

This paper examined the Nigeria's shareholding structure and investigates the activities of shareholders in the banking crisis. It can be said that although adequate legal provisions exists in the CAMA and SEC Code for Shareholders as to educate shareholders of their rights and responsibilities, it was not until the crisis that shareholders actually started exercising these rights. They can therefore be said to have been passive and more concerned with the financial turnovers of the company as opposed to activities of the board, thus, providing a perfect environment for control fraud.

Black identifies legal rules, conflicts of interests and manager agenda control as factors that can create shareholder passivity.[88] According to him, many institutional investors depend on the management and board for the business of the company; they therefore face conflicts of interests if they monitor corporate managers. Managers, on the other hand, mostly control shareholders' voting agenda especially on decisions that can have substantive outcomes.[89]

Despite the legal rules in place emphasizing shareholders' voting rights and also prohibiting management agenda control, shareholder activism in Nigeria is still emerging and it can be said that under a more facilitating regulatory and judicial environment, associations might do much more.

In view of this, some shareholder associations have developed a list of problems encountered by shareholders which can be said to be contributory factor to the crisis experienced in the corporate economy.

Their findings were published by the House of Representatives Report of the Ad-hoc committee on the investigation into the near collapse of the Nigerian Capital Market, most of which are highlighted below:[90]

- Manipulation of the market using delisted companies
- Regulatory failure of the financial sector regulators
- Sensitive banking reforms
- Investors' ignorance
- Lack of co-ordinated relationship between shareholders and the SEC

[82] See Becth et al. (2009). Returns to Shareholder Activism: Evidence from a clinical study of the Hermes UK Focus Fund. *The Review of Financial Studies* 22 (8), 3093-3129.
[83] Gillian, S.L., and Starks, L. T. (1998). A survey of Shareholder Activism: Motivation and empirical evidence. *Journal of Corporate Finance* 12(3) 275-305.
[84] See Hendry, J., Sanderson, P., Barker, R., and Roberts, J. (2007). Responsible Ownership, Shareholder value and the new Shareholder activism. *Competition and Change,* 11(3), 223-240, See also Sarkar, J., and Sarkar, S. (2000). Large shareholder activism in corporate governance in developing countries, Evidence from India. *International Review of Finance*, 1(3), 161-194.
[85] Adegbite and Amao *supra* at. P. 396.
[86] Adegbite and Amao *supra.*
[87] Adegbite and Amao *supra.*
[88] Bernard S. Black. Agents watching Agents: The Promise of Institutional Investor voice. *UCLA Law Review* Vol 39: 811-893 at 814.
[89] Black, *supra.*
[90] See the Report of the Ad-hoc committee on the investigation into the near collapse of the Nigerian Capital Market. P.11-14 Available at: www.proshare.com Last accessed 18.10.13.

- Corporate failure in the institutional and governance structure of the Securities and Exchange Commission
- The Nationalisation of Shareholders Investments in Afribank, Bank PHB and Spring Bank.
- Enforcement failure

The Committee, while evaluating the above issues raised by the associations, noted that ignorance of the investors provided a vacuum for the board of directors, managers and regulators to effect a sustained control fraud. Corruption and incompetence remains apparent in the financial system and capital markets with the government a mere observer.[91]

Although, it can be said that effective shareholder activism can promote effective corporate governance, in Nigeria, while shareholder activism tends to be emerging and should be encouraged, the level of corruption and power influence exhibited during the banking crisis suggests a more institutionalised problem in the country.

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Global Journal of Management and Business Research: B
Economics and Commerce
Volume 13 Issue 5 Version 1.0 Year 2014
Type: Double Blind Peer Reviewed International Research Journal
Publisher: Global Journals Inc. (USA)
Online ISSN: 2249-4588 & Print ISSN: 0975-5853

Impact of Inflation and Economic Growth on Unemployment in Sri Lanka: A Study of Time Series Analysis

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Abstract - This paper examines the effect of inflation and economic growth on unemployment in Sri Lanka for the period 1990-2012. To achieve this objective, secondary data has been taken from Central Bank annual reports for the above period. To test unit root or stationary, Augmented Dickey Fuller Test was used. In addition to that, ordinary least square technique and to determine the causality among the above variables Granger Causality test also were applied. Results of the unit root test indicate that only Gross Domestic Product (GDP) has stationary and unemployment and inflation have unit root problem or non- stationary at level. But when these two variables are tested at first difference then the problem of unit root has disappeared and hence they have become stationary at first difference.

Keywords: rate of unemployment, gross domestic product, inflation, granger causality test, economic growth.

GJMBR-B Classification: JEL Code: O40, O49

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Keywords: rate of unemployment, gross domestic product, inflation, granger causality test, economic growth.

I. Introduction

Sri Lankan economy since the political independence in 1948 has undergone fundamental structural changes in various aspects in the country. Inflation, economic growth which is measured by gross domestic product and unemployment, are the significance variables in any macroeconomic decision making and they are subject of social and economic life of every country. In case of Sri Lanka unemployment was 15.9 percent in 1990 and it has decreased continuously until 2001 and achieved to 7.9 percent in 2001 and after that it started increasing until 2003 and again from 2004 it started to declining and recorded 4 percent in 2012.

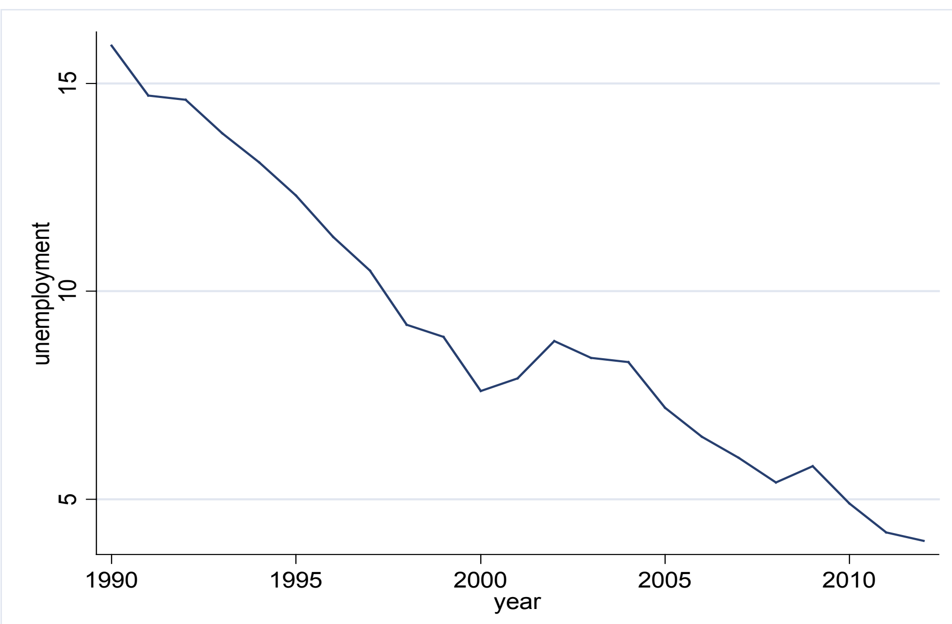

Figure 1 : Trend of unemployment, 1990-2012

Source : Central Bank annual reports, 1990- 2012

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Besides unemployment, inflation which was measured by gross domestic product deflator (GDP deflator) is another macroeconomic problem hurts both economic and social indicators in the country. Sri Lankan economy has also come across with this macroeconomic problem and the inflation rate was 56.3 percent in 1990 and after that it has increased continuously and reached to 398 in percent 2012.

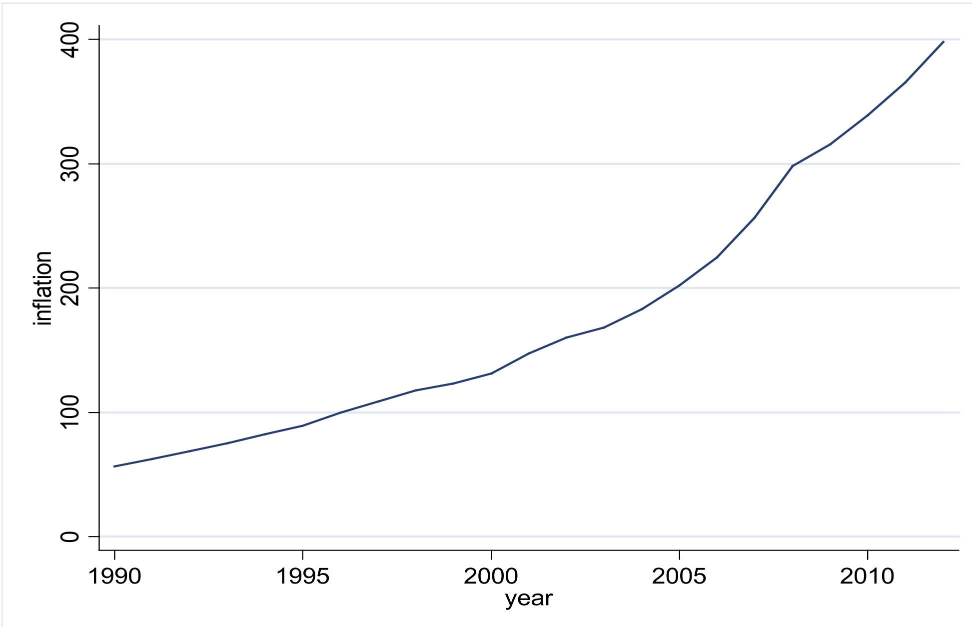

Figure 2 : Trend of inflation, 1990-2012
Source : Central Bank annual reports, 1990- 2012

Gross domestic product growth rate is used as proxy for economic growth in this study and it is generally perceived that when economic growth takes place in the country, it increases the pace of economic activity in the country, due to the employment increases. The increase in employment opportunities will enhance the purchasing power of the people in the country and as a result, consumption increases which leads to raise aggregate demand and hence inflation in the country. In case of Sri Lanka, GDP growth rate is recorded 6.2 percent in 1990 and it was negatively grows at 1.5 percent in 2001. It recorded 6.4 percent in 2012.

Figure 3 : Trend of gross domestic product growth rate, 1990-2012
Source: Central Bank annual reports, (1990-2012)

Objectives of this study are to identify the effect of inflation and economic growth on unemployment and also to determine the causality among the above variables in Sri Lanka.

II. Theoritical Framework and Literature Review

Tahir Mukhtar and Sarwat Rasheed (2010), testing the relationship between exports and imports: evidence from Pakistan using quarterly data for the period 1972- 2006. The econometric frame work such as Johansen maximum likelihood co-integration technique was used in the study. The findings show that there is a long run relationship between exports and imports and the Granger causality test it has found that there is a bidirectional causality exports and imports in Pakistan.

A Study was carried by Asoluka Njoku and Okezie A. Ihugba (2011) has examined the unemployment and Nigerian economic growth for the period 1985-2009. The study recommends that the agricultural sector as a medium of reducing unemployment in Nigeria should be harnessed and advises that Government and all relevant stakeholders continue in their quest towards reducing unemployment, as well as give their support in ensuring that the agricultural sector is not downtrodden but embraced in this task.

Mahmoud Ali Jaradat(2013) has analyzed impact of inflation and unemployment on Jordanian GDP from (2000-2010) and the results of the study indicate that there is a negative relation between unemployment and GDP, and there is a positive relation between Inflation and GDP.

Muhammad Umair and Raza Ullah (2013) have analyzed the impact of GDP and inflation on unemployment rate of Pakistan Economy in (2000-2010) and their study concluded that inflation has a role which influential but for GDP and unemployment with insignificant levels in the macroeconomics factors of Pakistani economy.

Ayesha Wajid (2013) empirically analyzes the impact of inflation and economic growth on unemployment by using time series evidence from (1973 – 2010) in Pakistan.

This study used Augmented Dickey Fuller (1981) test to test unit root problem and in order to find out the long run relationship among unemployment, inflation, economic growth, trade openness and urban population he applied Johansen – Juselius (1990) Maximum Likelihood Approach. This study concludes that inflation significantly increases unemployment in the long term; economic growth has a significant adverse impact on unemployment in the long run and in the short run respectively, and the impact of trade openness on unemployment is positively and insignificant in the long run but this impact becomes significant in the short run.

Karaçor, Zeynep, (2013), have analyzed the causal relationship between unemployment, inflation and the minimum wage: Case of Turkey from (1987 to 2010). Their study has found that the level of minimum wages and inflation variables is Granger reason for the unemployment in short period.

Another study carried out by Auwal Abubakar Muhammad, (2013) analyzed the effect of unemployment and inflation on wages in Nigeria using Ordinary Least Square (OLS) method, Augmented Dickey-

Fuller (ADF) technique and Granger causality test. The result of the regression revealed that the coefficient of unemployment is positive and statistically significant influence wage rate whereas inflation is positive but has no significant effect on it. Moreover, result of the unit root indicates that all the variables in the model are stationary while, the result of causality test suggests that unemployment Granger causes wage rate and not inflation.

III. Hypothesis Formulation

This study tries to identify the effect of inflation and economic growth on unemployment and also to determine the causality among the unemployment, GDP growth rate and inflation in Sri Lanka. Based on the objectives, the following hypotheses were developed.

a) Hypothesis 1

$H1_0$: Inflation has positive impact on unemployment in Sri Lanka.

$H1_1$: Inflation has negative impact on unemployment in Sri Lanka

b) Hypothesi 2

$H2_0$: GDP has positive impact on unemployment in Sri Lanka

$H2_1$: GDP has negative impact on unemployment in Sri Lanka

c) Hypothesis 3

$H3_0$ = there is unidirectional granger causality exists between inflation and unemployment

$H3_1$ = there is bidirectional granger causality exists between inflation and unemployment

IV. The Research Methodology

The model of this study contains the variables of GDP and inflation which are affecting on unemployment in Sri Lanka. The annual data for unemployment rate as the dependent variable and other independent variables such as, economic growth and inflation which were measured by gross domestic product and gross domestic product deflator respectively was taken from Central annual reports for the period (1990-2012).

To find out the impact of independent variables on dependent variable, Ordinary Least Square (OLS) method was used and the model is written as:

$$Y_t = \beta_0 + \beta_1 X_{1t} + \beta_2 X_{2t} + \varepsilon_t$$

Where,

t = 1, 2, 3,………….. 22 (time period is from 1990 – 2012)

Y = Rate of unemployment,

X_1 = Gross domestic product,

X_2 = Rate of inflation and

ε = Error term.

Because of the nature of the time series nature of the data initially, the unit root problem is tested by using Augmented Dickey Fuller (1981) for all three variables at the level and in case of non- stationary variables they were tested at first difference and thereby they became as stationary. Thus, unit root tests are important to test the integration between the variables involved in the study.

Maximum lag length for the model was estimated by using Vector Autoregressive (VAR) Model and afterwards, the long run relationship among the variables is tested by using Johansen co – integration test. This approach comprises of two test statistics such as Trace Statistic and Maximum Eigen – Value Statistic. Long run relationship among the variables is confirmed if the calculated value from the both test statistics is greater than their respective critical values. The following equations were used to estimate these test statistics:

$$\lambda_{\text{trace}} = L_A - L_0$$

$$\lambda_{\text{max}} = - \text{Tlog}\,(1- \hat{\ }\lambda_{r+1})$$

To find out the dynamic relationships among the variables Vector Error Corrected Model (VECM) also used and it will use full where the existence of co- integration is established. Finally, to determine the causality among the variables and to verify whether change in any series is unidirectional or bidirectional, granger causality test was applied.

V. Results and Discussions

a) Hypothesis test results

Unit root problem is tested in each variable by using Augmented Dicky Fuller (1981) test and its results are given in Table 1. These results have shown that all variables are not integrated in the same order and fail to reject the null hypothesis of non- stationary of all variables used except GDP growth rate at levels in the study.

Thus, only GDP growth rate has stationary at level and other two variables have unit root problem when they are tested at level. But when these variables are tested at first difference then the null hypothesis is accepted and the problem of unit root has disappeared from them. Also, all the variables are now integrated of order one {*I* (1)} and the variables have become stationary at first difference.

Table 1 : Results of unit root test

Augmented Dickey Fuller Test											
At level						At first difference					
Variables	t-statistics	Critical levels			p-value*	Variables	t-statistics	Critical levels			p-value*
		1%	5%	10%				1%	5%	10%	
Unemployment	-1.60	-3.75	-3.0	-2.63	0.482	Unemployment	-4.44	-3.75	-3.0	-2.63	0.0002
GDP	-3.904	3.75	-3.0	-2.63	0.0020	GDP	-6.983	-3.75	-3.0	-2.63	0.0000
Inflation	6.325	-3.75	-3.0	-2.63	1.0000	Inflation	-5.342	-3.75	-3.0	-2.63	0.043

Source: Central Bank annual reports, 1990- 2012

**Mackinnon approximate p-value (5%)*

According to the above table, GDP has the p-value of 0.002 proves that only it has stationary at level and other two variables have unit root problem or they are non-stationary. To overcome this problem, these variables are tested at first difference then all the variables have become stationary.

After the unit root test, the maximum lag length of the model is found by using Vector Autoregressive (VAR) lag order selection criteria. The results are presented into (Table 2) and it has confirmed that the maximum lag length of the model is ‘1’ and it is selected on the basis of the minimum value of each criterion and based on that the maximum number of ‘lag 1’ was selected. The estimated results for lag length criteria are given in the below (table 2).

Table 2 : Results of lag length criteria

Selection-order criteria
Sample: 1994 - 2012 Number of observations = 19

Lag	LL	LR	df	p	FPE	AIC	HQIC	SBIC
0	- 180.01				46697.6	19.26	19.29	19.41
1	- 103.82	152.38	9	0.000	40.35*	12.19	12.29*	12.78*
2	- 97.34	12.966	9	0.164	57.54	12.45	12.63	13.50
3	- 86.75	21.166	9	0.012	62.12	12.29	12.54	13.78
4	-75.15	23.216*	9	0.006	83.01	12.01*	12.34	13.95

Source: Central Bank annual reports, 1990- 2012

Note 1 :

* indicates lag order selected by the criterion
Endogenous: unemployment, GDP growth rate, inflation
Exogenous: Constant
LL: Log L
LR: Sequential Modified LR Test Statistic (Each Test At 5% Level)
FPE: Final Prediction Error

Based on the selection criterion, maximum lag length 1 is selected and it was used in all model in the system.

Note 2 :

AIC: Akaike's Information Criterion,
HQIC: Hannan-Quinn Information Criterion,
SBIC: Schwarz's Bayesian Information Criterion.

To test the Johansen tests for cointegration, the variables must be non- stationary at level 1. But after converted them into first differenced, they become a stationary at first difference. This is the necessary condition for the Johansen tests.

As it has found that all variables have become free from unit root problem at first difference and thus, it is more suitable to apply Johansen Maximum Likelihood Approach (Year….). The estimated results of the Johansen cointegration test are illustrated in (Table3).

Table 3 : Results of Johansen test for co-integration

Maximum Rank	Parms	LL	Eigen value	Trace statistics	5% critical value
0	12	- 123.38	……..	33.85	29.68
1	17	-110.95	0.693	8.99*	15.41
2	20	-107.89	0.252	2.88	3.76
3	21	-106.45	0.128		
Maximum Rank	**Parms**	**LL**	**Eigen value**	**Trace statistics**	**5% critical value**
0	12	-123.38	……..	24.86	20.97
1	17	-110.95	0.69	6.10*	14.07
2	20	-107.89	0.25	2.88	3.76
3	21	-106.45	0.12		

**Source: Central Bank annual reports, (1990- 2012).*
*Note: *Refers that there is one co-integration exists among the variables at level (5%)??*

Trend: constant Number of observations = 21
Sample: 1992 – 2012 Lags = 2

The above results are based on two methods such as trace statistic and maximum statistic tests and both results are the same. Here, (0) means there is no co-integration among the variables and (1) means there is 1 co-integration among the variables and (2 and 3) are represents that there is (2 and 3) co-integrations among them. At zero, test statistic which is 33.85 greater than critical value which is 29.68 at 5% then rejects the null hypothesis (H_0 ?) and showed that there is a co-integration. Since the trace statistics is less than its critical value at 1, cannot reject the null hypothesis and accept the alternative hypothesis (H_1 ?) at 5% level is suggesting that there is one 1 co-integration exists among the variables. This implies that all the variables are co-integrated and also they have long run association ships. Also it means that, unemployment and other two explanatory variables moves together closely to achieve the long run equilibrium.

When the variables are co-integrated, proves that the presence of co-integration between variables and it suggests a long term relationship among the variables under consideration. In the presence of co-integration, the Granger causation test cannot be estimated in a simple VAR model but requires the model to be specified in the more restricted vector error correction (VEC) framework. Therefore, vector error correction model can be applied in this study.

Table 4 : Results of Vector Error Correction Model

Beta	Coefficient	Std. Err.	z	P>|z|	[95% Conf. Interval]	
Ce1						
Unemployment	1	------	------	---------	------	
GDP	-2.92	.474	- 6.17	0.000	-3.85	-1.99
Inflation	-.028	.009	3.15	0.002	.010	.046
Constant	-6.72	--------	--------	--------	--------	--------

Source: Central Bank annual reports, (1990 2012)

Based on the table, the long run relationship between unemployment, GDP and inflation in Sri Lanka for one co-integrating vector for the period (1990-2012) is displayed below.

$$\text{Unemp} = -6.72 - 2.92\ \text{GDP} - 0.028\ \text{Infl} \qquad (1)$$

The equation represents the normalized cointegrating coefficients of each explanatory variable and in the above (table 4) shows that, the equation consists of a trend value at (-6.72) and further it illustrates that the coefficient of GDP has statistically significant at 5% level in the long run relationship. The negative sign of the variable GDP which is 2.92 indicates that, every one unit increase in GDP, leads to reduce in unemployment by 2.92 units assuming the rate of inflation is constant.

On the other hand, inflation rate also has negative sign with statistically significant proves that one unit increase in inflation rate leads to a decrease in unemployment rate by 0.028 units keeping GDP is constant. The results of this finding which examine the relationship between unemployment and GDP and unemployment and inflation have supported to the hypothesis stated by the researcher by rejecting the null hypothesis and accepting the alternative hypothesis.

Rest of other parts of the vector error correction model was displaced in the following table.

Table 5

Equation	Parms	RMSE	R-sq	χ^2	P> χ^2
D_Unemployment	5	.503	0.654	30.368	0.0000
D_GDP	5	1.936	0.594	23.408	0.0003
D_Inflation	5	5.775	0.928	208.613	0.0000

Source: Central Bank annual reports, 1990- 2012

Note :

No. of observations = 21

AIC = 12.18615

Log likelihood = -110.9546

HQIC = 12.36966

Det (Sigma_ml) = 7.794931

SBIC = 13.03172

In the above table, three variables, such as unemployment, GDP and inflation automatically converted into first differences. That is represented by D_unemployment, D_gdp and D_inflation and they represent that three of them were considered as dependent variables with statistically significant at 5% level.

Table 6

	Coefficient	Std. Err.	z	P>|z|	[95%Conf. Interval]	
D_Unemployment						
Ce1						
L1.	.081	.0432	1.89	0.058	-.002	.166
Unemployment						
LD	-.438	.287	-1.52	0.127	-1.00	.125
GDP						
LD	.053	.076	0.70	0.485	-.095	.202
Inflation						
LD	.037	.015	2.43	0.015	.007	.067

LD	.037	.015	2.43	0.015	.007	.067
Constant	-.619	.252	-2.45	0.014	-1.113	-.124

Source: Central Bank annual reports, 1990- 2012

In the D- unemployment equation, the short run coefficient of GDP is not significantly different from zero while the coefficient of inflation is significantly different from zero. But in the D-GDP equation all short run coefficients are not significantly different from zero. In the D-inflation equation, short run coefficients for unemployment and inflation have positive but GDP has negative significant and thus they are significantly different from zero.

Table 7

D_GDP						
Ce1						
L1.	.207	.166	1.25	0.211	-.117	.533
Unemployment						
LD	1.791	1.104	1.62	0.105	-.373	3.957
GDP						
LD	-.094	.292	-0.32	0.747	-.667	.478
Inflation						
LD	.0106	.059	0.18	0.857	-.105	.126
Constant	2.687	.970	2.77	0.006	.786	4.589
D_Inflation						
ce1						
L1.	-1.692	.495	-3.42	0.001	-2.663	-.722
Unemployment						
LD	7.519	3.294	2.28	0.022	1.062	13.97
GDP						
LD	-2.078	.871	-2.38	0.017	-3.787	-.369
Inflation						
LD	.393	.1762	2.23	0.026	.047	.738
Constant	.300	2.89	0.10	0.917	-5.369	5.969

Source: Central Bank annual reports, (1990- 2012)

In the above (table 7), Ce1 represents the error correction term or speed of adjustment towards equilibrium and for each variable one lag has chosen. The coefficient of error correction term of unemployment has .081 with positive sign and statistically (L1=…..*, p<.05: Sig. 000), it is insignificant. It shows that the divergence from equilibrium will take place with the speed of 8.1% and thus unemployment is adjusted by 8.1% of the past years deviation from equilibrium.

The coefficient of error correction term of GDP growth rate has positive sign of .207 and it is not statistically significant which implies that divergence from equilibrium will take place with the speed of 20.7% of the past years deviation from equilibrium. The coefficient of the error correction term of inflation has negative sign of '1.692' with statistically significant at 5% level (L1=…..*, p<.05: Sig. 000), indicates that convergence towards the equilibrium path will take place with the speed of 169.2%.

If 'L1' is negative in sign and significant then we can say there is long run causality running from GDP growth rate and inflation to unemployment. Here 'L1' is positive and p value also greater than '0.05' (L1=…..*, p<.05: Sig. 000),. There is no long run causality running from independent variables such as GDP growth rate and inflation to unemployment meaning that GDP growth rate and inflation has no influence on unemployment in the long run. Similarly, L1 for D- GDP also has positive sign and p-value also greater than 0.05 (L1=…..*, p<.05: Sig. 000), indicates that, there is no long run causality running from unemployment and inflation to GDP meaning that unemployment and inflation has no influence on GDP growth rate in the long run. But in case of inflation L1 has negative with the significant p-value which is less than 0.05 (L1=…..*, p<.05: Sig. 000), shows that there is a short run causality running from unemployment and GDP growth rate to inflation meaning that unemployment and GDP growth rate has influence on inflation in the short run.

Finally, the short run causal relationship between unemployment, GDP growth rate and inflation for each equation has been tested using the VEC Granger causality. The χ^2 test statistics (p>.05: Sig. 000), and its significance were considered for the above lagged variables

Table 8 : Vector error granger causality test

Dependent variable –: D-unemployment		
Excluded	χ^2	probability
D-GDP	0.49	0.485
D-Inflation	5.91	0.0151
Dependent variable –: D-GDP		
Excluded	χ^2	probability
D- Unemployment	2.63	0.1048
D- Inflation	0.03	0.8565
Dependent variable –: D-Inflation		
Excluded	χ^2	probability
D- Unemployment	5.21	0.0225
D- GDP	5.68	0.0172

Source: Central Bank annual reports, (1990- 2012)

According to the table 8, it proves that unemployment granger caused by inflation while GDP does not granger cause unemployment. Unemployment and inflation both does not granger cause GDP growth rate but unemployment and GDP growth rate both cause inflation. So, there is bi- directional (H3) granger causality exists between inflation and unemployment while there is unidirectional granger causality exists between inflation and GDP in the economy of Sri Lanka. Thus, the above results indicate that two way causation flowing from inflation to unemployment and unemployment to inflation.

In case of GDP it concerned that both unemployment and inflation are not granger causing it. This implies that there is a one – way causation or unidirectional causality is running from GDP to inflation only. The above results have supported to reject the null hypothesis and accepted the alternative that is there is bidirectional granger causality exists between inflation and unemployment in Sri Lanka.

VI. Conclusion

This paper examines the effect of inflation and economic growth on unemployment in Sri Lanka for the period (1990-2012) using multivariate time series techniques such as Augmented Dicky Fuller test, Lag length criteria, Johansen test for co-integration, Vector error correction model and Granger causality test.

The results of the Augmented Dicky Fuller unit root test illustrate that all series are non- stationary except GDP at their levels but after they converted into their first difference then all became as stationary. For getting optimal lag length of this model, vector autoregressive lag model was used based on FPE, HQIC and SBIC criteria. These criteria suggested that optimal lag length as (1) and it was used for Johansen co integration test.

This statistic based on both trace and maximum statistic indicate that there is only one co-integrating relationship exists among unemployment, GDP and inflation. Then move forward by applying the Johansen multivariate co-integration test to investigate the long run relationship among the variables. The result implies that, the above three variables establish a long run steady state equilibrium relationship in Sri Lanka. Vector Error Corrction model estimated the normalized coefficients of the variables and it suggests that both GDP and inflation have negatively and significantly affect the unemployment in Sri Lanka. It is, therefore, concluded that both GDP and inflation have a role which influential significant levels in the macroeconomics factors of Sri Lankan economy.

Further, stability of equilibrium also tested by using vector error correction model and its results indicate that coefficient of the error correction term for lagged of unemployment and GDP have not statistically significant while inflation has negative sign but statistically significant at 1% level.

Finally, Granger causality test also examined based on vector error correction model and the results reveal that, there is bi-directional granger causality exists between inflation and unemployment while there is unidirectional granger causality exists between inflation and GDP in the economy of Sri Lanka.

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Global Journal of Management and Business Research: B
Economics and Commerce
Volume 13 Issue 5 Version 1.0 Year 2014
Type: Double Blind Peer Reviewed International Research Journal
Publisher: Global Journals Inc. (USA)
Online ISSN: 2249-4588 & Print ISSN: 0975-5853

An Assessment of the Economic Development Existence in Nigeria

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Abstract - Poverty incidence and unemployment rate of the developing countries have been increasing as they claimed development in their economies, the situation in which Nigeria is not an exception. Thereby, this study set to investigate whether economic development existed in the country in the past 27 years, covering the periods of 1986 – 2012. Likewise, to inform the decision makers and policy implementers about the appropriate usage of the words 'economic development', and as well portends its redefining and differentiation between 'GDP growth and GDP widening'. The study stipulated ideal methods of assessing the existence of economic development based on the extant definitions from the most relevant authors in the field of Development Economics.

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GJMBR-B Classification: JEL CODE: C13, O47, O10

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Strictly as per the compliance and regulations of:

An Assessment of the Economic Development Existence in Nigeria

Benedict N. Akanegbu [α] & Matthew Oladapo Gidigbi [σ]

Abstract- Poverty incidence and unemployment rate of the developing countries have been increasing as they claimed development in their economies, the situation in which Nigeria is not an exception. Thereby, this study set to investigate whether economic development existed in the country in the past 27 years, covering the periods of 1986 – 2012. Likewise, to inform the decision makers and policy implementers about the appropriate usage of the words 'economic development', and as well portends its redefining and differentiation between 'GDP growth and GDP widening'. The study stipulated ideal methods of assessing the existence of economic development based on the extant definitions from the most relevant authors in the field of Development Economics. More so, the study finds new ways of using time-series regression analysis in answering logic-form question of economic development, and this goes with variables' signing rather than contributions. Based on partial comparative statics analysis, the study finds that economic development only existed in the country in the year1988 – 1990, and 1994 fiscal years during the years in consideration. In addition, based on partial comparative dynamic analysis, the study finds that no economic development has existed in the last 27 years in the country.

Keywords: economic development, gross domestic products, poverty, and unemployment.

I. Introduction

Economic development is an invented compound concept for recognizing economically backward or lagging behind countries, compared to other countries who are topping in term of economic well-being of their citizens. Economic development is generally used in synonymous terms such as economic growth, economic welfare, secular change, social justice and economic progress, (Somashekar, 2003). Media circuses of economic development in the country, each fiscal year is not on a lighter mood, even though, it is development without trickle down effects towards masses.

However, from 20th century to date, only comparative statics perspective of economic development and growth has been under the limelight of economists, while an extensive part of its dynamic analysis is excluded and silent about with the exception of token aspect of 'economic development measurement'. Quah (2001) buttresses its empirical measurements, even though, painstakingly. Little wonder, that the use of the term economic development is losing grip and turning to be academic mess and political propaganda. Since, the masses could not witness any trickle down effects of the proclaimed economic development constantly sing by the government agents, especially, the policy-makers and implementers. The indigence has started seeing it as political brouhaha, cajoling, and hiding pillar for political leaders. This calls for a shift of economic development measurement from a mere comparative statics to a partial comparative dynamic measurement. This will help in differentiating between Gross Domestic Products (GDP) widening – increment in the size of Gross Domestic Products (GDP) warranted by increase in the number of people who are either producing or consuming- and economic development, which trickle down to reduce poverty incidence, unemployment, and inequality level in the society. Ultimately, it will be imperative to assess Nigeria's economic development in the light of new economic view of development by deviating from its traditional view, which has no impressing measurement, but ordinary figure statement of national outputs.

Historically, economic development and growth became a concern of the so-called developed countries, with the notion that 'poverty anywhere is a threat to prosperity everywhere', besides, it has been an arrow of the concerned-countries' leaders, in bid of breaking off the yoke of vicious cycle of poverty on their citizens which was not a flickering fire as it is today.

a) Objective

Universally, economists unanimously agreed that economic development bring about reduction and/ or elimination of poverty, inequality and unemployment. Nevertheless, myriads of journal articles experimenting on the country's data failed to relate the inconsistencies in the universal believe of the economists. This study tends to bridge the gap between the general believe of the economists and the happenings in Nigeria, with respect to the indigent population. On this backdrop, the study sets to answer this question, 'Does economic development in Nigeria implies reduction and elimination of poverty, inequality and unemployment? More so, the following are the specific objectives of the study:

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i. To investigate the existence of economic development in Nigeria between the periods of 1986 - 2012.
ii. To correlate existence of growth in figure wise with/ to its impact on the country's teeming population.

This research article would help in informing decision makers and policy implementers about what they might probably need to do, in ensuring economic development translation from figure to reality in betterment of the citizens and society. More so, it will portend whether growth exist or not.

The study is structured into five sections. Section I, which is the introductory part, and study objective inclusive. Section II covers the background information about the operational concept of the study and its overall observed performance in the country. Section III covers the model specification and methodology, and Section IV deals with estimation of results and analyses, while Section V concerns with conclusion and policy recommendations.

II. Literature Review

According to Schumpeter (1934), economic development is a discontinuous and spontaneous change in the stationary state, which forever alters and displaces the equilibrium state previously existing. While economic growth is a gradual and steady change in the long-run, which comes about by a gradual increase in the rate of savings and population.

Robbins (1968) accepted the concept 'development' in terms of increases in income per head or capacity to produce that income, as his working definition. However, cautioned about the narrowness of the concept, and chose to define it (economic development) in terms of increasing real income per head or increasing potential to produce such income. Detailed technicalities of the concept 'economic development' needs being overlooked and conceived it in relation to comparatively long periods (Ibid.)

Seer (1969) defined development as the occurrence that goes with reduction and elimination of poverty, inequality and unemployment within a growing economy. Furthermore, to sufficiently determine what economic development means, he asserted:

The questions to ask about a country's development are therefore: What has been happening to poverty? What has been happening to unemployment? What has been happening to inequality? If all three of these have declined from high levels, then beyond doubt this has been a period of development for the country concerned. If one or two of these central problems have been growing worse, especially if all three have, it would be strange to call the result "development" even if per capita income doubled.

UN Rio Declaration (1992) defined sustainable development to be development that meets the needs of the present without compromising the ability of future generations to meet their own needs. Sen defined development to consists of the removal of various types of unfreedoms that people with little choice and little opportunity of exercising their reasoned agency (Corbridge, 2002), which is still on the same page with other definitions.

In generic understanding, economic develop-ent refers to the problems of underdeveloped countries and economic growth to those of developed countries (Jhingan, 1997).Thorough observation of situation in some of the third world countries, especially, Nigeria accentuate the fact that economic development are directly proportion to poverty, inequality and unemployment. Meanwhile, the relationship supposed to be inverse.

Table 1 : Showing relationships among variables of interest

Year	GDP Growth rate	Poverty Incidence (%)	*Population in Poverty (Million)	*Change in Indigent Population (%)	Unemployment Rate (%)	Life Expectancy at Birth (Years)
2008	6	54.0	80.78		14.9	54
2009	7	54.0	83.32	3.05	19.7	54
2010	8	69.0	109.91	24.19	21.4	54
2011	7.4	71.5	120.04	8.44	23.9	47.6
2012	6.6	72.0	121.17	0.93	25.7	47.6

Source: Central Bank of Nigeria(A) (2012), with the exception of the asterisked columns, which are authors' calculations.

In addition, with this development, there is need to ascertain whether the country is really experiencing economic development. As this study would relate to the academic world what the happenings are, and re-orientate the populace about the nature and circumstances surrounding the acclaimed economic development, which the indigent population have termed to be political jamboree. Recently, CBN's annual report confirmed economic growth for the year 2012 to be 6.6 per cent, while NBS confirmed poverty rate to be 72 per cent.

a) *Economic Growth and Development*

The concepts become important as it is used to determine progress in its core values. It is relevant because it is used to evaluate the following according to Todaro and Smith (2011):

i. *Sustenance*

The ability to meet basic needs: economic development takes account of how much people are becoming more capable in providing for their basic needs in term of goods and services, such as food, clothing, and shelter, which are the least things to survive.

ii. *Self-esteem*

This is simply feeling of worthiness that a society enjoys. This point is so cogent that 'a just and egalitarian society' was entrench as number one objective in the national education policy.

iii. *Freedom*

This stands for ability of having a number of alternative means to satisfy wants, that is, people especially the indigent are not constraint with the choices available to them in satisfying their wants.

When the three items explained briefly above are taking place in a society, it is assumed that such society is actually experiencing economic development. But is very unfortunate that majority of the developing countries leaders and policies managers there found a common ground in hiding their non-performance toward steering economic development parse. Considering economic growth rate figure or increment in Gross Domestic Products (GDP) figure without given its life transformation and betterment effects heavier weight, it will not be worthy to account such increment as development.

b) *Factors of Economic Development*

Economic development could mean sustained increase in welfare of an economy – nation, region, and city – as well as the ongoing changes in that economy's industrial structure; public health, literacy, and demography; and distribution of income (Quah, 2001). Economic theory settled on three factors in broad categorization as the determinants of economic development, which are: (i) the progress of science and productive knowledge; (ii) the growth of individual skills; and (iii) incentives (Ibid). Economic development rests on joint existence of these determinants, and availability of both economic and non-economic factors. Whereby, the country is abundance of these, especially, economic factors.

Economic development is not in a utopian notion but pragmatic and usually stimulated by the presence of some economic factors in which Nigeria as a country is fully endowed with. Although, the utilization and maximization of these factors, non-economic factors inclusive; may not be encouraging but much can still be done to bring its maximization into point of satiety. Those factors as pointed out by Jhingan, (1997) and Somashekar, (2003) are:

i. *Land*

This include natural resources in the earth itself and this is the principal factor among others. It include quality of the soil, forest wealth, good river system, minerals and oil-resources, good and bracing climate. A country may actually be backward in economic progress if people are indifferent about the resources, which means the presence of this resource is not serving as silver bullet to economic development.

ii. *Capital Formation*

This is the stock of physical reproducible factors of production. Capital formation works out through sound financial system, which further extends to financial deepening and intermediation. Over the years, the country had actually shown reasonable improvement in terms of capital accumulation; in the year 2010 it increases by 79.93 per cent appropriately, compare to the year 2005 figure.

iii. *Technological Progress*

It is equally referred to as widening of capital, and in a very simple term, technological progress is in place because capital accumulation is not possible without technical progress, (Somashekar, 2003).

Other factors such as human resources, population growth, social overheads and transformation of agricultural society. Statistically, the country is fairly playing in respect to all of these factors. population growth is relatively stable over the past period up till 2011 at 3.2 per cent until it fell to 2.3 per cent in the year 2012 (Central Bank of Nigeria (A), 2012). A reasonable part of the country's budget over the years now, goes to social overheads. In addition, the services sector growth rate of 13.2 in the year 2011, which is the highest growth rate in the real sector, as it was in the past years pointed at the transformation of agricultural society to service sector (Central Bank of Nigeria (A), 2012).

c) *Measurements of Economic Development*

According to the United Nations Expert Committee as cited in Somashekar, (2003), "Development concerns not only man's material needs but also the improvement of the social condition of life. Development is, therefore, not only economic growth, but growth plus change – social, cultural and institutional as well as economic". On this note, proxy for economic develop-pent, which is commonly taking as GDP will be considered jointly with the development variables. Robbins (1968) was sceptical about measuring economic development and sees it as trying impossible but still believed that measurement can be carried out on partial basis and not absolutely. Quah, (2001) exhibits a parallel ideal with Robbins, by asserting, that entertaining this kind of measurement cannot be possible without guidance about what can be parsed away and what is essential.

Measuring economic development from GNP per capita according to Meier and Baldwin (1957). It is defined 'as the process whereby the real per capita income of a country increases over a long period of time – subject to the stipulations that the number of people below an 'absolute poverty line' does not increase, and that the distribution of income does not become more unequal.' Although, going with real per capita income as measurement of development had been defined as narrow view of the concept with the experience in 1950s and 60s.When few countries reached their targeted, economic growth rates without changing the levels of living of the masses (Todaro & Smith, 2011); it was around the same time that one of the prominent economists asserted the spread out of economic development analysis.

From various authors' definitions of economic development as exhibited in some extant studies, the following conditions can be deduced for ascertaining economic development:

First Condition:- $\mathrm{GDP_t} - \mathrm{GDP_{t-1}} = \Delta\mathrm{GDP} > 0$

(Where GDP is the national outputs)

Second Condition:-$\mathrm{PovInc_t} - \mathrm{PovInc_{t-1}} = \Delta\mathrm{PovInc} < 0$

(Where PovInc stands for Poverty Incidence)

Third Condition:- $\mathrm{Unemp_t} - \mathrm{Unemp_{t-1}} = \Delta\mathrm{Unemp} < 0$

(Where Unemp stands for Unemployment rate)

and/or $\mathrm{GiniC_t} - \mathrm{GiniC_{t-1}} = \Delta\mathrm{GiniC} < 0$

(Where GiniC stands for Gini Coefficient)

In the light of the Meier, Seer, and Sen's definitions, if the conditions specified above were not met; it is better for a country to say that, she had actually increase GDP due to widening effect but she could not witness economic development. As masses have taken government declarations in this respect, to be bunch of lies, since they could not witness the trickle-down effects of the claimed economic development in the country. However, if all the three conditions specified above were met at a time, then, it is worthy of concluding that there is economic development. If condition one and any of two or three are satisfied, it may be concluded that economic development is in process.

III. Model Specification and Methodology

Method of analysis adopted was based on series of definitions as put forward by Somashekar, (2003), Meier, (2001), Seer (1969), Todaro and Smith (2011) among others. First, the examination of existence of development was based on comparative statics analysis rooted in the conditions developed under the measurements as sub-heading. Moreover, this shown whether there is existence of economic development on yearly basis or not. Simply by working on the first difference of the selected appropriate variables (Seers, 1969). According to Meier and Baldwin (1957), time series of national interest should not be less than 25 years since a major business cycle covers normally 6 to 13 years. The second approach was based on time series regression analysis, covering the period of 27 years ranging from 1986 – 2012. The interpretation of which is different from the conventional time-series regression interpretation. Since, the major question, this study is trying to answer is in logic form, variables' contribution are useless but their signing, significant level and their joint significant. Central Bank of Nigeria Statistical bulletin and annual reports various issues are the source of data used.

The time-series regression model adopted is:

$$\mathrm{GDP_t} - \mathrm{GDP_{t-1}} = \alpha_0 + \gamma_1(\mathrm{Unemp_t} - \mathrm{Unemp_{t-1}}) + \gamma_2(\mathrm{PovInc_t} - \mathrm{PovInc_{t-1}}) + \epsilon_t$$

Where t stands for the present year and t-1 stands for the immediate previous year, ϵ_t stands for the error term.

a) A priori

It is expected that change in Gross Domestic Products (GDP) should be positive, that is, greater than zero. While, the two independent variables according to the econometrics term are expected to be negatively signed, that is, less than zero.

IV. Estimation of Results and Analyses

Table 2 : Showing analysis outputs on yearly basis

year	dgdp	dPovInc	dUnemp	Comparative Statics Analysis Note
1987	-1164.9	-0.6	1.7	No economic development
1988	15069.09	-0.4	-1.7	There was economic development
1989	16853.95	-0.5	-0.8	There was economic development
1990	30820.41	-0.5	-1	There was economic development
1991	-2170.8	-0.5	-0.4	No economic development
1992	5986.38	-1.1	0.3	Economic development at the process
1993	3467.77	6.6	-0.7	Economic development at the process
1994	617.27	5.7	-0.7	Economic development at the process
1995	5956.84	5.3	-0.2	Economic development at the process
1996	12337.98	5.6	1.6	No economic development

1997	8277.1	0.4	-0.2	Economic development at the process
1998	8867.57	2	0	No economic development
1999	1293.43	1	-0.2	Economic development at the process
2000	16995.26	1	1.7	No economic development
2001	27815.52	0	-1.1	Economic development at the process
2002	76209.25	-15.6	8.6	Economic development at the process
2003	44329.47	15.6	2.6	No economic development
2004	50043.06	-15.6	-1.4	There was economic development
2005	34355.35	26.8	-1.5	Economic development at the process
2006	33890.22	-27.2	1.8	Economic development at the process
2007	38429.53	0	0.9	Economic development at the process
2008	37951.41	0	0.3	Economic development at the process
2009	46774.78	0	4.8	No economic development
2010	57354.88	15	1.7	No economic development
2011	57829.62	2.5	2.5	No economic development
2012	54731.17	0.5	1.8	No economic development

Source: Authors' Analysis Outputs

The analysis in the Table 2 above takes care of the study second specific objective and shows that economic development only take place in the year 1988 to 1990, and in the year 2004. While, there were no economic development in the year 1987, 1991, 1996, 1998, 2000, 2003, and 2009 to 2012. However, in the years, there were widening of Gross Domestic Products (GDP) with exception of the year 1987 and 1991. However, for the other years, economy was in the process of growth or development but the expected conditions could not be attained concurrently on the two variables taking as independent as per econometrics concern.

Table 3 : Showing Outputs of Partial Dynamic Analysis (Log of d_GDP as Dependent Variable)

Variable	Coefficient	S.E	P-Value	Remark
Const	0.0495539	0.00840561	<0.00001	Significant at 1 per cent
d_Unemp	0.00915969	0.00368904	0.02076	Significant at 5 per cent
d_PovInc	-0.000500755	0.000815163	0.54505	Not statistically significant
R-squared	0.255449			≈ 26 per cent
F-statistics	3.945551		0.033635	Significant at 5 per cent
LM statistics	0.675435		0.713397	No serial correlation
x^2 *Normality*	0.730373		0.694067	Normally distributed

Source: Extracted from Econometrics Software Output

Table 3 above satisfies the quest of first specific objective. Also from the table, the origin, which is constant, is statistically significant at 1 per cent- the result is 99 per cent not because of chance; then positively signed. First difference of unemployment rate was positively signed and statistically significant at 5 per cent. First difference of poverty incidence is rightly signed in consonance with a priori expectation but not statistically significant, therefore, it becomes irrelevant for decision. The regression line only explain approximately 26 per cent of change in the gross domestic product, the study mute about this because running the time series regression without differencing would indicate high R-squared (92 per cent) and having all the independent variables as Econometrics concerned, positively signed and statistically significant. Since, the main objective here was to answer logic form of question; less should the bothering about detail, which did not affect validity of the study's findings.

The F-statistics value of 3.945551 with p-value of 0.033635 shows that the variables in the model specified are jointly significant, that is, there is no misspecification in combining those variables used together. LM statistics with high p-value signifies absence of serial correlation, by implication past error value did not affect present error value, and thereby, constant variance exists. Chi-square test statistics value for normality test indicates that error is normally distributed.

V. Conclusions and Policy Recommendations

On a yearly basis, starting from 1986 down to 2012 economic development only existed in some past years, precisely, 1988 – 1990, and year 1994 in Nigeria. However, economic development was in process in the year 1992 – 1995, 1997, 1999, 2001 -2002, and 2005 – 2008, which means increase in the Gross Domestic Products, had either reduced or kept static one of the poverty incidence or unemployment rate in the country. However, there was no economic development in the other years within the range of years in consideration but not mention.

Going by the variable that is statistically significant between the difference of unemployment rate and poverty incidence, for the period of 1986 – 2012, the study finds that there is no economic development but widening of the Gross Domestic Products.

The study equally finds that starting point of the years in consideration might affect the yearly basis (simple comparative statics analysis) decision of whether economic development existed or not.

The study therefore concludes that following the partial dynamic analysis of existence of economic development, that there is no economic development existed in the country between the periods of 1986 to 2012 fiscal years. This implies that over the years in consideration, the indigent population, which is over seventy (70) per cent of the population, were not able to meet their basic needs, faced with limited means of satisfying their wants, and ultimately, lost a sense of worthiness in the society (Todaro & Smith, 2011).

Based on this major conclusion, government agents would need to adjust in their usage of the word 'economic development' by trying to differentiate development from mere widening of national products. Reasonable enough to know that increase in population goes with shift in population pattern, thereby, resulted to increase in size of each of the population classification. Because of this, ordinarily, Gross Domestic Products should increase because as population increases people produced more and consumed more as well. Therefore, it is not necessarily mean that increment in the Gross Domestic Products implies economic development. Economic development would reduce poverty incidence, unemployment rate and, inequality.

If the poor countries do not want to remain poor, appropriateness in their definition of terms, need to be taken into consideration. So that development variables can be rightly targeted, since the poor countries were poor and remained poor because of inappropriate and damaging government policies (Meier, 2001), and calling Gross Domestic Products widening as development is a tantamount inappropriateness that actually encourages damaging of government policies.

Developing countries need to start using appropriate concept in the light of this study to express their figures, so that, the masses can confide in the government policies and declaration once again; and even help in targeting towards the right variables, realising that economic development has not been in place. This study recommends further investigation by assessing the impact of unearned income, which may make a country to widening her GDP without economic development when the income circulation is restricted systematically.

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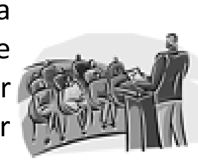

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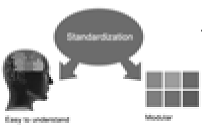

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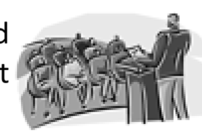

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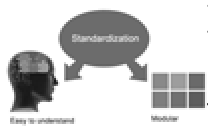

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	A-B	**C-D**	**E-F**
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Introduction	Containing all background details with clear goal and appropriate details, flow specification, no grammar and spelling mistake, well organized sentence and paragraph, reference cited	Unclear and confusing data, appropriate format, grammar and spelling errors with unorganized matter	Out of place depth and content, hazy format
Methods and Procedures	Clear and to the point with well arranged paragraph, precision and accuracy of facts and figures, well organized subheads	Difficult to comprehend with embarrassed text, too much explanation but completed	Incorrect and unorganized structure with hazy meaning
Result	Well organized, Clear and specific, Correct units with precision, correct data, well structuring of paragraph, no grammar and spelling mistake	Complete and embarrassed text, difficult to comprehend	Irregular format with wrong facts and figures
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ISSN 9755853