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# Effect of Globalization on Growth and Development of Capital Market in Nigeria

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***Abstract:*** *In this paper, we investigated the likelihood that capital market development in the emerging market like Nigeria is affected by financial openness and visible trade relationship. The paper aimed to examine how the capital market responds in terms of the market size and the market liquidity proportion when financial openness and trade integration indicators are endogenously determine by FDI and Export/Import volume. The main finding is that capital market growth and development is positively affected by integration of the world economic activities. The result suggest that the regulators most especially in emerging market, should encourage more liberalization of the financial market as this will bring about an increase in investors, financial securities, dynamic and quality of financial products and as well as quality and uniformity in accounting standard.*

***Key words:*** *Globalization; capital market development; liberalization; financial openness; trade integration; Nigeria*



## I. INTRODUCTION

Globalization involves liberalization of economic activities. The process of globalization is an intercontinental economic arrangement which has lead to the integration advancement of the world economy through the pulling the difficulty of trade and greater mobility of finance, labor and ideals. Popularly known as liberalization of trade through which economic of scale can be attained. The elements of globalization include free movement of goods and services, flow of capital movement of labor and the transfer of technology (Amit & Almas, 2005). Developing countries through liberalization and increased openness to trade have benefitted from the process (Amit & Almas, 2005). Thus, the second capital market development program addressed structural deficiencies in Bangladesh's capital markets by boosting economic growth and deregulating the financial system to better support the real economy by promoting private sector investment (Syed, 2016). So, globalization indicators (capital inflow, capital market capitalization, export volume, import volume etc.) have implication for economic development among other variable, hence, stimulate the increase in financial infrastructure development in developing economy. The efficiency and activity of capital market depend on many factors. These are; legal, tax, and economic environment, the availability and dependability of information, the behavior and knowledge of participants of the market, competitiveness with other market, the depth and liquidity of the market, globalization, and many more (Pocius, Stunguriene, & Paskevicius, 2013).

Thus, globalization has an indisputable effect on the financial market growth and development, having note that globalization caused improvement in product quality, information and communication, technology, regulation, deregulation, competition and integration of local market to other developed market all over the world. The advancement of economic globalization and integration of capital market stimulate the introduction of a single set of internationally harmonized accounting standard. Empirically research provides some evidence that international financial reporting standard (IFRS) adoption contributed positively to progression of (EU) capital market (Prochazka & Pelak, 2015). Globalization and financial crisis make policy-makers to rethink whether they know what they think they know about how economies work and what the proper economic policy responses should be to prevent and mitigate such crisis (Gallagher & Tian, 2017). Globalization also implies the internationalization of production distribution. As the benefits of globalization are revealed it as well has great positive effects on domestic economic financial crisis due to exposure to the global world. So, financial crisis in a foreign country can easily be transfer to the home country, hence, crisis in wake of globalization has ripple effect that extend itself into the economy at large. Financial globalization can lead to financial crisis that cause much economic hardship (Mishkin, 2018).

However, Liberalization of capital market opens vast possibility for companies to attract capital. The growing Chinese economy increases the demand to strengthen its securities market by opening it to foreign investors and issuers (Pocious, Stunguriene & Paskevicius, 2013). Openness leads to better convergence (Cheng & Mittelhammer, 2018). As many developing countries, such as China and India, have shown rapid economic growth and poverty reduction as a reduction of their pen economic policies since the 1990s (Cheng & Mittelhammer, 2018). Consistent growth and development of the general economy will improve the activities of financial market in advancing its growth and development.

Stock market development generally lowers the cost of equity by improving liquidity provision, information, production, risk diversification and external monitoring (Kim et al., 2015). Globalizations (financial liberalization) facilitate the access of investors to external financial resources and foreign investment and stimulate the unification of financial market products and regulation globally (Ball, 2006). Therefore, financial system integration of capital market reduces transaction costs and improves the allocation of resources, which ultimately results in capital market growth. The challenge for most African stock markets is to increase liquidity, expand access and reduce the cost of capital (Sunil, 2017).

However, there have been considerable improvement, rapid growth and liberalization in a number of Africa countries market (Allen et al., 2011). Without financial globalization, developing countries will not be able to realize their potential (Pocious, Stunguriene & Paskevicius, 2013). Since, the major engine and growth for any economy is the capital market which accommodates certain institute for the creation, custodianship, distribution and exchange of financial assets and management of long-term liabilities (Oluwole, 2014). The financial system in emerging economy must be more tightly integrated with those in the developed countries in order to partake in the benefit of financial flows, the lifeblood of the industrial world (Mishkin, 2018).

Since the deregulation of the Nigeria economy in 1986 and the subsequent liberalization of the capital market, the domestic markets have been greatly linked with the rest of the world markets , thus, overtime more than 70 percent of capital importations are into equity portfolio investment in Nigeria and record show that between March, 2012 and September, 2013, Capital Importation from Kenya, South Africa, China, United State and Germany constitute an average of 72.02 percent of the total (Uyaebo, Atoi & Usman, 2015). Globalization promotes regional and global integration of Nigeria stock market while trade liberalization had a significant impact on the growth of Nigeria stock market (Oluwole, (2014). However, Nigeria capital market is recovering from crisis because the index measure of the market direction grew by 34.5 percent in 2012 (Adediran, Adeyemi & Alalade, 2015). Then capital market capitalization, which opened trading for the year at N8.98 trillion, grew by 3.41 trillion to close at 37.97 percent (Adediran, Adeyemi & Alalade, 2015). The effectiveness and growth of capital market in Nigeria economy is a problem that has assumed of resent an intractable dimension (Nwankwo, 1991).

Addressing the issue of globalization and capital market development have increased rapidly in the past few years, but the theoretical ad empirical evidence did not conclusively resolve the issue. Further, most of the studies are centered on globalization and general economic growth and development and very limited done on globalization and capital market development in developing economy like Nigeria the situation thus, creates research gaps on the study of globalization and growth and development of capital market in emerging market. Hence, focusing on Nigeria capital market, the aim of this paper is to examine the impact of some selected globalization factors on capital market development indicators. The organization of this paper as follows; section II reviews of related literature; section III Theoretical Framework; section IV methodology used in the study; section V, findings and section VI, conclusion.

## II. REVIEW OF THE RELATED LITERATURE

Ross, & Sara, (1998) studied capital control liberalization and stock market development, two question was addressed, “what happen to stock market size, liquidity, volatility, and international integration following capital control liberalization in 6 emerging market economies”? Second, “what is the empirical relationship between stock market size, liquidity, volatility, and international integration and regulations concerning information disclosure, accounting standards and investor protection”? Using correlation analysis the findings revealed that stock market tend to become larger more liquid more volatile and mire integrated following the liberalization.

Stulz, (1999) examined the impact of globalization on the cost of equity capital. There are two main channels through which this reduction in the cost of capital occurs. The first channel is that globalization reduces the discount rate investors charge. The second is that globalization increases the cash flows investor expect to receive by increasing the monitoring of management and controlling shareholders. Using correlation analysis to estimates of the cost of capital due to globalization, the findings showed that globalization have a significant impact on cost of capital but small.

Stiglitz, (2003) analyzed globalization and growth in emerging markets and the new economy. The study tried to set forth some of the reasons why globalization, when managed well, may actually be adverse to overall economic growth. Concluded that countries that have managed the globalization process well has showed that globalization can be powerful force for economic growth.

Kilic, (2015) studied the effect of economic, social and political globalization on the growth level of developing countries and causality relationship between the variables between 981-201. Using fixed effets least squares method and Granger causality test developed by Dumitresu-Hurlin (2012) for 74 developing countries. The result indicated that economic growth levels of selected developing countries were positively affected by the economic and globalization whereas social globalization affected economic growth negatively. Causality test however showed that there are two way causality relationships between political and social globalization and the economic growth and one way causality relationship between social globalization and economic growth.

Nwakanma, & Ibe (2014) examined the causal relationship between globalization and economic growth in Nigeria from 981 to 2012. Using cointegration, regression and granger causality analysis, the cointegration results revealed the existence of long-run relationship, regression results showed a positive and significant relationship between financial integration, human resource development and trade openness while gross fixed capital formation was negative and insignificant. Granger causality showed a unidirectional causal relationship between financial integration and gross fixed capital formation and also a unidirectional causality between trade openness and gross fixed capital formation.

Goel, & Gupta (2014) examined the impact of globalization on stock market development in India using commonly recognized indicators to test this impact spanning from 1990-2007. The indicators used were good test market development and Deeping (i.e. market capitalization, liquidity and volatility). Using correlation analysis the results indicated that all selected indicators showed significant improvement in stock markets of India.

Mete , Olusi, & Ayodel (2006) examined the effect of globalization of economic growth in Nigeria for the period 1986-2003. Using Error Correction Modeling (ECM) and the result showed that trade openness has significant positive effect on economic growth in Nigeria. The findings revealed that Nigeria could benefit more from globalization if the economy could fully integrated with the rest of the world.

Amit, & Almas, (2005) analyzed the measurement of globalization and its variations among countries, regions and over time. The study attempted to measure globalization y using parametric and non-parametric approaches, data covering a wide range of industrialized transition and developing countries on bases of their international integration. Using correlations analysis the findings identified that the factors influencing globalization among the countries in the form of economic integration, personal contact technology and political engagement.

Sunil, (2017) analyzed the extent of stock market integration in Southern Africa Development Community with data obtained on daily stock market index data (closing values), covering the period 1999 to 2011. By analyzing beta and sigma (SADC) a convergence and then using cointegration analysis and the findings observed beta convergence but not sigma convergence; though the sigma values are falling for most of the SADC countries.

Kim et al., (2015) examined the relation between province-level financial development and the cost of equity in China ranging from 998-2011. Using OLS regression analysis, the result showed that stock market development reduced the cost of equity in general and banking development only marginally lowers the cost of equity.

Hamid (2018) examined the impact of information and communication technology (ICT) and financial development on developing economies of the petroleum exporting countries (OPEC) for the period 2002-2015. Using a panel of GMM type of growth model and the results revealed that the financial development index and ICT variables have impact on economic growth.

Prochazka, & Pelak (2015) studied the development of capital markets of New EU countries in the IFRS era, the particular focus was on the capital market size measured by a simple criterion, number of listed companies and its changes in transition and post-adoption period. using data of tab.2, they calculated the relative change in equity instruments traded in each country for two periods and the result revealed that the process is associated with relatively high benefits n some countries and relatively significant cost in other countries.

## III. THEORITICAL FRAMEWORK

### Globalization and Capital Market Growth and Development

What eventually matters for policy makers and economics alike is whether globalization affects economic development and if so how? As observed from the previous literatures, globalization or internationalization of stock market increases listing, capital raising and trading abroad in domestic market (Olowole, 2014). And in his work on globalization and capital market growth and development, a positive relationship was observed between globalization and capital market growth along with negative intercept.

Also, according to Adediran, Adeyemo & Alalade, (2015) the traditional growth in theoretical literature was not suited to explore the relationship between financial intermediation and economy because it focused on steady-state level of capital stock per worker to exogenous technical progress. They identify a positive relationship between globalization capital market and development in Nigeria along with negative interception. Thus, the globalization of capital markets and the development of trade will help to create new surpluses which could meet the world demand for capital (Adediran, Adeyemo & Alalade, 2015). Obviously, the Nigeria stock market must have a good reputation domestically, before it can favorably be view abroad and vital that the market is developed to cope with the problem that may likely arise from full integration of Nigeria s' stock market into global network (Adediran, Adeyemo & Alalade, 2015).

Moreover, countries that have managed the globalization process well have showed that globalization can be a powerful for economic growth (Stiglitz, 2003). International trade is playing a major role in economic growth of Nigeria total export indicated a positive and significant effect on economic growth (Adeleye, Adeleye & Adewuyi, 2015). Economic integration measured by trade openness bears a significant positive effect on the level of economic growth, hence, give the extent of trade economy is gaining from globalization and its policy of financial integration (Feridun, Olusi & Folorunso, 2006).

Regarding stock market development, liberalization increases the pool of capital available to local firms and broadens the investor's base. This is pool of capital available to local firms and broadens the investor's base (Oluwole, 2014). More so, Nwakanma & Ibe (2014), granger causality test identified a unidirectional causal effect from financial integration to gross field capital formation and also from trade openness to gross field capital formation. According to Ross & Sara, (1998), the data suggested that stock market become larger, more liquid, more internationally integrated and more volatile following the liberalization of restriction on capital and dividend flows.

Open trade in financial markets offers unambiguous gains relative to a closed economy and such trade permit insurance and the smoothing of shock, allow capital to seek out it highest rewards, implying the usual gain-from-trade result (Mourice & Alan, 2003). Guel & Gupta,

(2011) selected indicators showed positive effect in stock market of India, as globalization reform brought about improvement in market efficiency, transparency and preventing unfair trade practices; study showed that the stock markets in India have experienced exponential growth over the study period. The development of stock market is mainly influenced by such factors as the GDP growth, the bank sector development, market liquidity, fiscal behavior, overall geographical and economic environment have positive impact on securities market capitalization (Pocious, Stunguriene & Paskevicius, 2013).

## IV. DATA AND METHODOLOGY

### Data and Sample

Data on both dependent and independent variables come from bureau statistics database. The study covers the aggregate value of the capital market development indicators and as well as, the globalization measuring indicators in Nigeria over the 1990-2016 periods. That is, few years after structural Adjustment Program (SAP) this brought about financial system liberalization in Nigeria in 1986.

### The Dependent variables

To measure capital market development, we adopt value-based and liquidity-based measures for capital market development and growth (kim et al., 2015). ( i) Capital market size (the ratio of total market value of all shares listed on NSE at the end of a year to GDP in the same year denoted by MKTCAP) the higher the number of shares listed, the larger the market size. (ii) For market liquidity, value of traded ratio are used (this is equal to the ratio of total value of traded share in the stock market divided by GDP). Liquidity is the ease and speed at which economic agents can buy and sell securities. The more liquid the stock market, the larger the amount of savings that are channeled through the stock market, also liquidity is key to a successful securities market (Kavita & Rakesh, 2011 ).

### Independent variables

In measuring the effect of globalization (integration) our explanatory variables according to Feridun, Olusi & Folorunso, (2006); are (i) Sum of export and imports to GDP = Total integration (tangible goods) and (ii) Financial integration (Monetary movement) = foreign capital inflow and outflows ‘Financial Openness’ (FDI), these proxies were used to measure the level openness in order to determine the extent of integration.

### Control variables

Our control variables include interest rate, real exchange rate, inflation rate and GDP growth to neutralize the effect of some systematic factors.

### Description of Variables

| Dependent Variables | Description |
|---|---|
| Market Capitalization = Market size | Share price times the number of shares outstanding |
| Market Traded Value = Market Liquidity I | Total number of shares traded both domestic and foreign, multiply by their respective matching pries |

| **Independent Variables** | |
|---|---|
| Net foreign direct investment = Financial Openness/Integration I | Foreign capital inflow and outflows |
| Export and Import Value = Total Integration II | Total Exports + Total Imports |
| **Control variables** | |
| Inflation rate | Inflation as measured by consumer price index |
| Interest rate | Lending Rate |
| Exchange rate | The exchange rate determined by national authorities (local currency units relative to the U.S. dollar). |
| GDP growth | |

**The Model**

MKTSIZE = $b_0 + b_1$ (EXPIMP) + $b_2$ (FDI) + $b_3$ (INT) + $b_4$ (GDPG) + $b_5$ (EXCH) + $b_6$ (Infla) + e……………………………………………………………………I

MKTLIQ = $b_0 + b_1$ (EXP) (IMP) + $b_2$ (FDI) + $b_3$ (INT) + $b_4$ (GDPG) + $b_5$ (Infla) + $b_6$ (EXCH) + e…………………………………………………………………..II

Where, MKTSIZE and MKTLIQ are the dependent variables (i.e. market capitalization and value of traded share in the market respectively) measuring the capital market development. EXPIMP and FDI (i.e. sum of export/import and foreign direct investment respectively) indicators to measure extent of integration. (INT)Interest rate, (GDPG) GDP growth and (EXCH) real exchange rate and Inflation rate are important macroeconomic factors used for systematic control. $b_1$ is the slope of the equation, and $b_0$ is the point of intercept where; $b_1$, $b_2$, $b_3$, $b_4$, $b_5$ and $b_6$ are equal to zero. While 'e' is the error term that takes care of the unobserved factors that can cause capital market development.

**Hypotheses Tested**

Based on previous studies, the relationship between globalization and capital market development can be hypothesized as follows:

$H_1$: There is no positive and significant impact of export/Import value (EXPIMP) on Capital Market size in Nigeria.

$H_2$: There is no positive and significant 'impact of export/Import value (EXPIMP) on stock traded value in Nigeria.

$H_3$: There is no positive and significant impact of Foreign Direct Investment on Capital Market size in Nigeria.

$H_4$: There is no positive and significant impact of foreign direct investment (FDI) on stock traded value in Nigeria.

## V. FINDINGS AND DISCUSSION

### Correlation Analysis

| | MKTCAP | STV | NETFDI | EXPIMP | INT | INFLA | GDPG |
|---|---|---|---|---|---|---|---|
| MKTCAP | 1.000000 | 0.680838 | 0.316064 | 0.187818 | -0.383565 | -0.106080 | -0.023364 |
| STV | 0.680838 | 1.000000 | 0.168883 | -0.035908 | -0.512955 | -0.304394 | 0.284558 |
| NETFDI | 0.316064 | 0.168883 | 1.000000 | 0.212335 | 0.352111 | 0.515256 | -0.083725 |
| EXPIMP | 0.187818 | -0.035908 | 0.212335 | 1.000000 | 0.263406 | 0.057354 | 0.105660 |
| INT | -0.383565 | -0.512955 | 0.352111 | 0.263406 | 1.000000 | 0.357744 | -0.143871 |
| INFLA | -0.106080 | -0.304394 | 0.515256 | 0.057354 | 0.357744 | 1.000000 | -0.395653 |
| GDPG | -0.023364 | 0.284558 | -0.083725 | 0.105660 | -0.143871 | -0.395653 | 1.000000 |

The results showed that the linear relationships between the independent variables are minimal. In other words the variables are not highly correlated (no multicolineality).

## REGRESSION ANALYSIS

### Table 2

Dependent Variable: MKTCAP

Method: Least Square

Sample: 1990 - 2016

Included observation: 27

| Variable | Coefficient | t-Statistic | Prob. |
|---|---|---|---|
| C | 24.21730 | 3.702987 | 0.0013 |
| NETFDI | 2.778349 | 3.232846 | 0.0040 |
| EXPIMP | 0.136166 | 1.538332 | 0.1389 |
| INT | -1.361594 | -3.363554 | 0.0029 |
| INFLA | -0.159241 | -1.520085 | 0.1434 |
| GDPG | -0.484393 | -1.191752 | 0.2467 |

Significant at 1%, 5% & 10 level

R Square 0.500970

Adjusted R Square 0.382153

F –Statistics 4.216327

Prob (F statistics) 0.001245

The two indicators of globalization (NETFDI and EXPIMP) have a positive and significant impact on capital market size. Net Foreign Investment is highly significant than Export and Import value. The result indicated that the level of financial integration has a strong impact on capital market development. Generally, the liberalization of the economic activities in Nigeria promotes the growth and development of capital market. Interest rate as well has a negative strong impact on capital market growth; the decrease in the rate of interest charged promotes the activities of capital market. The equation was able to explain 50% of change in the general market capitalization in Nigeria. The remaining 50% goes for the factors that are not observed, for this reason $b_0$ is positive and strongly significant. Indicating that in absence of the tested factors, capital market capitalization size will still be positive. The F-statistic is 4.216327 (p-value = 0.001245 < 0.05), indicated that generally, equation model was appropriate for the analysis. Therefore, the entire independent variables used were good factors in explaining the change in the dependent variable.

**Table 3**

Dependent Variable: MKTCAP

Method: Least Square

Sample: 1990 - 2016

Included observation: 27

| Variable | Coefficient | t-Statistic | Prob. |
|---|---|---|---|
| C | 4.304485 | 3.045629 | 0.0061 |
| NETFDI | 0.558604 | 3.007680 | 0.0067 |
| EXPIMP | 0.000523 | 0.027347 | 0.9784 |
| INT | -0.293990 | -3.360574 | 0.0030 |
| GDPG | 0.059459 | 0.676921 | 0.5058 |
| INFLA | -0.039206 | -1.731793 | 0.0980 |

Significant at1%, 5% & 10% level

R Square 0.52236

Adjusted R Square 0.408680

F – Statistics 4.593887

Prob (F statistics) 0.005482

The results in the table 3; indicated that the two indicators of integration have positive but only the Net Foreign Direct Investment has a significant impact on total trade value in the stock market in Nigeria. Therefore, financial integration is a vital factor that increases the level of liquidity in the market. Total integration (export/import values) is positive though not significant. GDP growth also has a positive and significant impact on total market traded value; the growth in GDP will increase the income of the investors. Also inflation rate has a negative and significant impact on total market traded value in Nigeria. Decrease in the rate of inflation will leave more money in hand of the investors. While the decrease in the rate of interest will leads to diversification. The independent variables explained 52% in variation of dependent variables. The remaining 48% is the unobserved factors which also contribute positively to the activities of the market. This might be some market specific factors. Besides, the whole equation model was an appropriate model in examining the impact of globalization on capital market development.

## VI. CONCLUSION AND RECOMMENDATION

### Conclusion

Our empirical results indicated that capital market growth and development are positively influenced by integration of the world economic activities. Therefore liberalization of financial and commodity market activities will promote the growth and development of the Nigeria capital market. This supported the argument that globalization will contribute positively to capital market development.

### Recommendation

On the basis of our findings, the contribution of financial integration (FDI) is very high, so the regulators most especially in emerging market, should encourage more liberalization of the financial market as this will bring about an increase in investors, financial securities, dynamic and quality of financial products and as well as quality and uniformity in accounting standard. Thus, unfairness of the market and the cost of information will relatively decrease.

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