Bank Credit Allocation in Nigeria – A Driver of Premature De-Industrialisation?


1.0 Introduction

Credit to the private sector is on the rise in advanced economies, and African countries which were believed to have undeveloped financial systems and consequently lower consumer credit, have not been left out of this trend. As obtains in advanced high-income economies of America, Europe and emerging Asia, where banking activities have long shifted away from traditional lending from savers to borrowers to extraction of income from households (Allen and Santomero, 2001), with ever increasing income from net-interest spread, especially for the poor (Bazot, 2013), banking operations in Africa show similar trends (Griffith-Jones and Karwowski, 2013). Also, while banking in Africa is being re-focused towards more complex technology-driven products designed to extend financial services to more of its growing population (Dos Santos and Kvangraven, 2017), lending to productive activities or the real sectors is declining – a phenomenon characteristic of advanced capitalist economies.

This paper illustrates how the case of the Nigerian financial system tows the above path, particularly, the expansion of bank credit in the financial sector, together with the implications of this development on output growth. It shows that while banks have recorded enormous deposits, high net interest spreads, growing rentier income from speculative activities, the economy has seen a remarkable decline in income and investment in the real sector. This dysfunction in the Nigerian banking system is manifested in many ways. One of these is the disproportionate growth in bank deposit relative to bank credit. Also, the disproportionate sectorial allocation of bank credit to services and oil and gas sectors at the expense of agriculture and manufacturing is telling of this development.
A consequence of this shift in bank credit allocation is the increasing removal of the financial sector from the real economy, evident in the decline in real output and worsening economic conditions in the country. Therefore, the concentration of credit in the oil and gas sector is argued to be, in part, responsible for Nigeria’s recent poor economic performance, especially the recent 2015 economic recession, albeit generally attributed to only a slump in global commodity prices. While no causal relationship has been established in this paper, it opens the conversation on the role of bank financing for manufacturing, and sets the agenda for more rigorous empirical studies for establishing causality in future research.

The disproportionate allocation of bank credit to the private sector to the services sectors is further analysed as a case for premature de-industrialisation, in which developing countries transition to more services sectors without industrialising (Rodrik, 2015; Tregenna, 2016). In this paper, I locate the diminishing share of manufacturing value-added (MVA) in total output in the disproportionate allocation of bank credit to sectors of the economy other than manufacturing, especially services and oil and gas in the case of Nigeria. The discussion on the causes of de-industrialisation recognises its non-exhaustive or context-specific forms, as such, gives room for teasing out the different causal factors depending on the context (Rowthorn and Coutts, 2004; Tregenna, 2016). In short, Rowthorn and Coutts nuance the idea of disproportionately lower allocation of investment to manufacturing as a causal factor of de-industrialisation by arguing that it may arise from a declining rate of investment in the share of manufacturing value added in GDP and employment. This is similar to the argument made here. Also, the link made between premature de-industrialisation and the disproportionate allocation of bank credit to the oil and gas sector resonates with Palma’s (2005) location of the causal factors of de-industrialisation around the discovery of significant amount of natural resources.

The implications of a de-industrialising economic structure for Nigeria, or re-structuring of its economy, as fondly labelled in the Nigerian policy space, are teased out, with lessons that other African countries may learn from. The rest of this paper is organised as follows: section 2 is a discussion of some theoretical underpinnings of the conceptualisations of credit and why it may tend towards negative rather than positive effects. It discusses briefly the limitations of mainstream economic theory to credit and touches on alternative approaches. Section 3 analyses developments in the Nigerian finance sector, starting with an overview of the Nigerian economy and drawing on developments in this sector to show expansion of finance in the economy and its penetration into households, with the attendant implications. This leads to
discussions around credit allocation by banks, with data to tease out the structure of such allocation in Nigeria. Section 4 delves into the literature on de-industrialisation and the shortcomings associated with this phenomenon. A brief conclusion with policy direction is put forward in section 5.

**2.0 Some Underpinning Theoretical Considerations**

Loanable funds in the mainstream economic literature is understood as generated from savings by households and allocated by banks to the most “efficient” investments. This process, supposedly underpinning money creation, has been criticised for many shortcomings, not least the ambiguity associated with the prominent role ascribed to interest rates, including little consideration of the effects of interest rates on household consumption and aggregate demand. It is also notably deficient in that it has no consideration for rising levels of debt independent of increase in savings (see Krugman, 2012 for a critique). Alternative theory, put forward by the Post-Keynesians allows money creation to be realised through credit generated by banks and other financial institutions, and not necessarily a function of savings. This theory has been called “endogenous money”. This process has been confirmed by the Bank of England as the channel through which money is created in practice (McLeay et al., 2014), by showing that the money supply in the economy increases whenever credit is created by deposit banks. Here, increasing (credit-financed) spending will cause increase in savings, and not the other way around.

One implication of endogenous money creation is its potential to increase debt build-up in the economy as more and more credit is created by banks (See, Moore, 1979; Minsky, 1980 and Graziani, 1989, from whom this argument originates). Keen (2014; 2015b) shows that when endogenous money goes into circulation, aggregate demand or income (or capital gains, as the case may be) increases by an equivalent amount. So, depending on how credit is allocated, it may boost demand and growth and further reduce unemployment, especially in a recession or capacity under-utilisation, as Keynes puts it (Keynes, 1973), or fuel the debt level in the economy. The potential of credit to boost household income and increase demand is further enhanced when it is channelled appropriately to the most productive sectors of the economy, not when allocated for speculative purposes or proliferation of financial asset.

A differentiation between credit flows that speculatively inflate the value of financial asset prices and credit that contributes to growth in the real economy is therefore necessary. An appropriate distinction will show that credit to the real sector directly translates into growth
while financial credit, allocated to the finance, insurance and real estate (FIRE) sectors, does not. Although an important distinction in the real estate sector needs to be made, between the financing of new versus existing buildings, with the latter inclined towards speculative purposes. Credit to FIRE has been regarded as the economy’s net build-up of debt, and the cause of financial fragility and instability. For example, “prolonged booms in mortgage flows and excessive consumer lending tend to create larger net debt burdens than lending to non-financial businesses” (Bezemer, 2013, p. 4).

As such, it matters how credit is created, which sectors it accrues to, how it is redistributed and where the spending power of an economy lies. The sectoral allocation of bank credit in Nigerian economy therefore comes to the fore, taken up below. This will be seen to be rather detrimental as opposed to driving economic development, due largely to the sectors which it has targeted.

3.0 Brief Overview of the Nigerian Economy

Nigeria’s total GDP amounts to $405.10 Billion at 2010 constant prices. Although this fell from an all-time high of $568.50 billion in 2014, Nigeria’s GDP which makes up 0.65 percent of World GDP and remains the largest in Africa. The current economic situation in Nigeria shows modest recovering from a two-year recession, with a current GDP annual growth rate of 1.4 percent at the end of 2017, from an average annual growth rate of 3.91 percent between 1982 and 2017. Figure 1 shows that growth rate reached an all-time high of 19.17 percent in 2004 in the wake of an unprecedented expansion in the financial sector, and an all-time low of -7.81 percent in 1983, when the country experienced its first major oil price slump. Unemployment rate continues to rise and currently stands at 18.80 percent as at 2017. Youth unemployment in particular, lags behind and stands at a towering 33.10 percent, and real wages are at its lowest in 25 years.
Services is now the largest sector of the Nigerian economy, contributing about 50 percent of the country’s total GDP. Among the fastest growing segments in Services are Information and Communication, which together account for about 10 percent of total GDP. The contribution of manufacturing share to total output has seen a consistent decline from around 10 percent in the 1970s and 7.82 percent in 1982 to about 4 percent in 2012. Rebased GDP figures however suggest that manufacturing sector reached about 9.03 percent of real output in Nigeria. Also, there has been a decline in value added in agriculture, which now contributes about 23 percent of GDP, from over 50 percent before the 1980s. Following a resurgence of the oil sector with a 25.89 percent year on year growth, Crude Petroleum and Natural Gas contribution amount to 11 percent of total GDP, while retaining its place as the country’s main export. Industry and Construction account for the remaining 16 percent of Nigeria’s GDP (National Bureau of Statistics, 2017).

At the crux of the matter is the monolithic economy in Nigeria which continues to depend on oil as its main source of revenue. Oil export contributes about 90 per cent to the country’s revenue. Although, many analysts are of the notion that the global slump in oil prices, Nigeria’s main source of revenue, underpins the recent economic slowdown of 2015, I argue that despite fluctuation in oil prices, insufficient credit growth to the real sectors has been the main driver of economic recession in Nigeria. This argument is located on the belief that Nigeria’s
monolithic economy would have been successfully diversified by now had the financial sector effectively assumed its role of channelling resources to the most productive sectors of the economy.

However, this is not to absolve successive Nigerian governments of the short-sightedness with which the economy has been managed and the deficient political vision to create an effective business environment that incentivises banks to target the manufacturing sector. The recent simplistic attempt at currency manipulation in which exchange rate was pegged for select investors and certain goods (comprising raw materials and cheap manufactures) banned from being imported into the country is evidence that the country lacks a coherent industrial policy or effectiveness to persuade banks to target the manufacturing sector. Banks were seen to further advance their rent-seeking activities through currency speculation and round-tripping, taking advantage of the thriving dual foreign exchange market in the country (see Nweze, 2017), propped up by deficient government policy. The arbitrage opportunity that emerged from this currency manipulation was significantly enough to discourage any long-term investor or even banks from investing in the manufacturing sector.

3.1 Some Historical Background on Nigerian banks

The establishment of the African Banking Corporation in 1892, among other foreign banks, was the advent of modern banking in Nigeria (Beck et al., 2005). Several domestic banks were established in the 1930s, leading to a surge in banking activities. As became necessary, the Banking Ordinance came into effect in 1952 to boost depositors’ confidence. The Central Bank of Nigeria (CBN) was later created in July 1959 to regulate the banking industry, as the country prepared for its independence from the colonial government. From here, banking was heavily driven by public ownership in the post-colonial period of the 1960s and 1970s.

Major privatisation reforms were carried out in the Nigerian banking system from the early 1990s, particularly through interest rate liberalisation, credit loosening and reduction in entry requirements in an overarching liberalisation agenda of the Structural Adjustment Programme (SAP). According to Beck et al (2005), this involved the divestment of government shareholding of over 50 per cent of total banking assets, in eight commercial banks and six merchant banks by 1992. This privatisation of government equities triggered the entry of new banks into the Nigerian banking system. The surge in banking activities within this period led to the establishment of the Nigerian Deposit Insurance Corporation (NDIC), which was tasked with the objective of insuring depositors and boosting public confidence in the banking sector.
However, the financial boom in the Nigerian banking industry following privatisation, saw a rise in rent-seeking and arbitrage activities, as opposed to traditional banking activities of savings and loans, which prompted the government to re-nationalise the banks in a bid to clean up the industry. A failed bank decree was then established for prosecuting banking misconduct (Beck et al., 2005). After the country’s transition to a democratic rule in 1999, many of its bureaucrats and politicians alleged that the failure of Nigerian banks to perform efficient intermediation service was due to their low capitalisation, as such, demanding that Nigerian banks increase their capital base.

As such, another banking consolidation process was embarked upon between July 2004 and December 2005, with the objective of strengthening domestic banks to finance large long-term capital projects. The banking consolidation process in this period required each bank, through a combination of mergers, acquisitions and initial public offers to recapitalise to the tune of N25 billion (approximately $200 million). The directive for recapitalisation of all Deposit Money Banks (DMBs) in Nigerian saw a 1250 per cent rise in paid up capital, causing a shrinking in the number of commercial banks in Nigeria from 89 to 25. This capitalisation achieved in the 2004-2005 banking recapitalisation exercise in Nigeria was high even by advanced economy standards (Griffith and Karwowski, 2013, p. 22-23).

Following the recapitalisation exercise of 2004 in Nigeria, the expansion of finance increased the penetration of finance into households and other non-financial corporations. There was an explosion of bank borrowing such as credit cards, consumer loans and financing of private and corporate purchase of assets from the Nigerian Stock Exchange (NSE). Commercial banks provided loans of up to 300 percent equity contribution to customers buying shares from the primary and secondary capital markets. Strikingly, banking halls in Nigeria became platforms for trading all kinds of financial and non-financial instruments as commercial banks engaged in trading forex (both on-site and online), mobile phone top up cards and other speculative instruments. The sale of mobile phone top-up cards in banking halls was later stopped by the CBN, they continued to be traded online to this day, among other merchandise. Banks concentrated heavily on foreign exchange dealings discussed above, with the country’s multi-tiered foreign exchange market presenting significant arbitrage and rent-seeking opportunities for banks to declare enormous profit and grow without necessarily investing in productive investments.
The availability of domestic bank capital, due largely to the successful recapitalisation exercise in the Nigerian banking sector alongside rents from rising oil prices, led to a boom in credit creation at alarming rate in the Nigerian economy. Domestic credit to the private sector rose sharply in absolute terms, and grew even more by almost five times in real terms, in the period leading up to the GFC in 2008, as shown in figure 2. As shown in figure 3, private credit tripled from 12 percent to 36 percent between 2006 and 2009. Despite a dip between 2014 and 2015, due to economic recession in the country, credit to the private sector has exceeded previous years and continues to grow significantly.
Consequently, there was a steep rise in non-performing loans (NPLs) as percentage of gross loans grew from 9.5% in 2007 to about 30% in 2009. Non-performing loans saw a corresponding spike in the period leading up to and preceding the GFC. Although the percentage of non-performing loans to gross loans decreased massively in the period 2011-2015, it has shown an upward trajectory since 2015. This is depicted in figure 4.
The sharp rise in credit is believed in this paper to contribute significantly to the systemic banking crisis experienced in 2009, in which nine banks were bailed out by the CBN at the cost of $4 billion. Today many Nigerian banks have grown into regional banks dominating the African banking system, and expanding their branches across Europe and the USA. In addition to being listed on the NSE, some are on (raising capital) stock exchanges abroad, such as the London Stock Exchange (LSE) and the Johannesburg Stock Exchange (JSE).

### 3.2 Divergence Between Bank Deposit and Loan Disbursement in Nigeria

Following the 2004-2005 recapitalisation exercise, Nigerian banks could expand their branches to cover previously unbanked, mostly rural, not least through deployment of ATMs and mobile payment systems. This brought to the fore another deficiency of the Nigerian banking system: the expansion of its financial system did not necessarily increase traditional banking activities of allocating finance to the most productive areas of investment, nor was there any efficiency in allocating credit. Remarkably, there has been a disproportionate growth in bank deposits relative to loans. Table 2 shows that while bank deposits increased steadily in Nigeria, albeit at decreasing rates, bank loans on the other hand did not experience equivalent increase in the same period. Despite a sharp rise in 2013, the poor performance in bank loans is evident in the
negative changes in 2011 and 2012, and displaying extremely high fluctuations between 2010 and 2015.

Table 1: Bank Loans and Deposit in Nigeria (2010 – 2015)

<table>
<thead>
<tr>
<th>Year</th>
<th>Bank Loans (N’ million)</th>
<th>% Change in Bank Loans</th>
<th>Bank Deposit (N’ million)</th>
<th>% Change in Bank Deposit</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>8,658,028.87</td>
<td></td>
<td>9,945,435.16</td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td>8,092,234.32</td>
<td>-6.5</td>
<td>11,927,978.06</td>
<td>20</td>
</tr>
<tr>
<td>2012</td>
<td>7,806,034.58</td>
<td>-3.5</td>
<td>13,871,090.19</td>
<td>16.2</td>
</tr>
<tr>
<td>2013</td>
<td>10,315,312.66</td>
<td>32</td>
<td>15,517,105.71</td>
<td>11.9</td>
</tr>
<tr>
<td>2014</td>
<td>12,936,210.64</td>
<td>25</td>
<td>16,944,109.82</td>
<td>9.2</td>
</tr>
<tr>
<td>2015</td>
<td>13,120,470.00</td>
<td>1.4</td>
<td>17,175,887.47</td>
<td>1.5</td>
</tr>
</tbody>
</table>

Source: National Bureau of Statistics, and Author’s Computation

The disproportionate growth in bank deposit to credit in the table above is depicted in the graph below, with the area of the former not only larger, but showing increasing divergence from the latter in the post-crisis period. The deficiency in loan disbursement is in part driven by high interest rates. Like other developing countries, interest rates in Nigeria are high, preventing borrowing by businesses. In short, only commercially crude and unsophisticated business, such as trading (especially short-term), can borrow at such high interest rates and still be in business. Sophisticated businesses with robust operations are usually unable to borrow with these rates. And innovative start-ups fall in this category.
Dysfunction in the Nigerian financial sector is not limited to disproportionate growth between deposits and bank lending. Divergence between growth in stock market capitalisation relative to capital formation of real investment can be observed between 1981 and 2017 in figure 6 below, similar to what obtains in financial markets in advanced capitalist economies. The rate of change of gross capital formation as percentage of GDP in Nigeria has remained largely unchanged and even declining for most part of the 1990s and into 2000s until the bank recapitalisation exercise was completed in 2005. While a disproportionate increase in market capitalisation may not directly portend negative implications, the dominance of banking, insurance and oil and gas stocks in the Nigerian capital market makes its growth problematic. Market capitalisation of listed domestic companies as percentage of GDP is also seen to exhibit significantly larger volatility than capital formation, with sharp rises in the 1990s and the period preceding the GFC.
3.3 The Role of Bank Credit in Nigeria’s Premature De-Industrialisation

Data on the sectorial allocation of credit by banks in Nigeria as complied by the country’s National Bureau of Statistics is relatively new, (and may in fact be insufficient to draw conclusions on the nature of bank financing in the country). However, it is helpful for observing bank financing within a given period for which data has been made available, and inference made on the nature of Nigerian banks in general. Some modest analyses may therefore be derived from it.

A look at value added by industries shows that finance increasingly contributes more to output or gross value added in Nigeria than manufacturing in figure 7. While these proportions were relatively consistent in the early to mid-1990s, the decline in manufacturing value added in the late 1990s, although marginally, established the divergence between finance and manufacturing value added. This divergence has been gradually increased since the 2000s with financial sector seen to contribute more to Nigeria’s gross value added.
In addition to the decline in accumulation of real investment, a corresponding disproportionate accumulation is seen to occur between manufacturing and the services sector. This is depicted in figure 8, which shows a divergence between value added of manufacturing and services. These trends also show that value added in services relative to manufacturing has not only diverged but the proportion of this divergence has been on the increase since the post-crisis period of 2009. Therefore, disproportionate allocation of credit to services is telling of the nature of accumulation in the Nigerian economy, including the implications for labour and wages. For labour and wages, it is necessary to understand that the non-material productivity in the services industry (except for construction and tourism) makes it unable to absorb the residual low-wage labour that arises from a decline in the manufacturing sector (Hallward-Driemeier and Nayyar (2017). In Nigeria, unemployment rate has been on the rise and is seen to have increased steadily from 6.4 per cent in January 2015 to 18.8 per cent at the end of 2017 (National Bureau of Statistics, various years), a reflection of the structure of the concentration of value added in its economy.
In addition, the disproportionate growth in services in Nigeria can be linked, at least in part, to an underpinning disproportionate allocation of bank credit to the private sector as a percentage of GDP to the services sectors relative to manufacturing, agriculture and other materially productive sectors. Figure 9 is a graphical representation of bank credit allocation. Quarterly data for the period 2015-2017 is used in this analysis due to the unavailability of annual data before this period. From 2015Q1-2017Q3, allocation to services has been in the range of five times that of manufacturing, at about 60 percent of total credit by banks. Services is followed by the oil and gas sector as second highest recipient of bank credit. Notably, this reflects the contribution of different industries to Nigeria’s GDP. Bank credit to these two sectors is evidence of the financial sector’s preference for high yield and non-productive investment.
<table>
<thead>
<tr>
<th>Quarter-Year\Sector</th>
<th>Agriculture</th>
<th>Mining &amp; Quarrying</th>
<th>Manufacturing</th>
<th>Oil &amp; Gas</th>
<th>Power &amp; Energy</th>
<th>Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1 2015</td>
<td>466,381.34</td>
<td>222,303</td>
<td>1,878,091.98</td>
<td>2,153,166.81</td>
<td>282,697.75</td>
<td>8,354,461.31</td>
</tr>
<tr>
<td>Q2 2015</td>
<td>484,947.80</td>
<td>17,937.35</td>
<td>1,909,491.64</td>
<td>2,058,656.54</td>
<td>353,910.83</td>
<td>8,608,481.37</td>
</tr>
<tr>
<td>Q3 2015</td>
<td>469,924.38</td>
<td>12,142.76</td>
<td>1,958,451.18</td>
<td>2,241,331.26</td>
<td>359,567.76</td>
<td>7,972,463.73</td>
</tr>
<tr>
<td>Q4 2015</td>
<td>449,307.29</td>
<td>11,714.18</td>
<td>1,736,192.99</td>
<td>2,272,812.29</td>
<td>340,308.57</td>
<td>8,275,869.60</td>
</tr>
<tr>
<td>Q1 2016</td>
<td>485,639.22</td>
<td>11,336.49</td>
<td>1,862,589.07</td>
<td>2,237,712.11</td>
<td>357,587.99</td>
<td>8,252,739.06</td>
</tr>
<tr>
<td>Q2 2016</td>
<td>480,639.22</td>
<td>16,328.38</td>
<td>2,058,036.94</td>
<td>3,366,153.62</td>
<td>447,228.40</td>
<td>9,169,067.19</td>
</tr>
<tr>
<td>Q3 2016</td>
<td>491,282.18</td>
<td>27,282.41</td>
<td>2,130,441.30</td>
<td>3,647,251.14</td>
<td>428,448.59</td>
<td>9,460,398.61</td>
</tr>
<tr>
<td>Q4 2016</td>
<td>525,945.19</td>
<td>21,283.46</td>
<td>2,215,741.07</td>
<td>3,587,904.75</td>
<td>432,293.83</td>
<td>9,334,117.20</td>
</tr>
<tr>
<td>Q1 2017</td>
<td>556,544.59</td>
<td>8,229.26</td>
<td>2,142,390.15</td>
<td>3,575,664.85</td>
<td>472,083.75</td>
<td>9,247,574.16</td>
</tr>
<tr>
<td>Q2 2017</td>
<td>501,088.16</td>
<td>11,417.18</td>
<td>2,216,749.95</td>
<td>3,528,162.53</td>
<td>466,086.89</td>
<td>8,987,006.01</td>
</tr>
<tr>
<td>Q3 2017</td>
<td>491,496.69</td>
<td>11,761.54</td>
<td>2,267,425.12</td>
<td>3,542,289.06</td>
<td>459,248.46</td>
<td>9,053,078.04</td>
</tr>
</tbody>
</table>

Source: Author’s Compilation from National Bureau of Statistics (NBS) and Central Bank of Nigeria (CBN)

Note: ‘Services’ in Bank credit to the private sector as categorised by the Nigeria Bureau of Statistics (NBS) comprises construction, trade/general commerce, government services, real estate, finance, insurance and capital market, education services, oil and gas, power and energy services, information and communication, transportation and storage, general services and others.
Source: Author’s Compilation from National Bureau of Statistics (NBS) and Central Bank of Nigeria (CBN)

Note: ‘Services’ in Bank credit to the private sector as categorised by the Nigeria Bureau of Statistics (NBS) comprises construction, trade/general commerce, government services, real estate, finance, insurance and capital market, education services, oil and gas, power and energy services, information and communication, transportation and storage, general services and others.

Suffice to point out that credit allocation by banks in Nigeria has been a main driver of the country’s dysfunctional economic structure. Even, within the allocation of bank credit to services, a closer scrutiny reveals that FIRE attracts the largest proportion of about an average 18 per cent of total allocation to services, and 10.6 per cent of total bank credit to the private sector. This further disproportionate allocation of bank credit to the FIRE sectors points to the growing influence of finance in the economy, and a point of departure for analysing financialisation in Nigerian (taken up elsewhere).

The combination of these factors; decline in credit in real investment, lop-sided allocation of credit to services and oil and gas sectors relative to manufacturing, clearly make Nigerian banks liable in some ways. There is a possibility that the uneven allocation of credit to non-manufacturing sectors may in fact, be a major determinant to the decline in the productivity in the manufacturing sector. Where there is insufficient allocation of credit to manufacturing, the obvious implication is a decline in productivity and a consequent reduction in the share of
labour employed by the manufacturing sector. Suffice to say therefore, that were credit (efficiently) available to the manufacturing sector, the economy may not have slumped, or at least, to the extent that it did when oil prices crashed in 2015. The manufacturing sector would have served as a buffer for the crash in commodity prices, including oil prices. As such, the one-sided focus of Nigeria’s economy on the oil sector has been detrimental to development for the country, and banks have been accomplices in this deficiency, through their pursuit of short-term profit in services and oil sectors.

4.0 Premature De-industrialisation

Notably, developing countries have turned to the services sectors instead of manufacturing, a trend that is seen in Nigeria. This is also the trend in the rest of Africa, where services share of GDP is growing while agriculture and manufacturing share is declining. The idea that economies can skip manufacturing without first realising the benefits of developing their productive base and where industrialisation is no longer the key route for convergence with advanced countries is gradually being accepted in the mainstream literature. For example, IMF’s position is expressed in the most recent edition of its flagship report “World Economic Outlook, 2018” and summarised by Gruss and Novta, (2018) in the blog titled “The Decline in Manufacturing Jobs: Not Necessarily a Cause for Concern”. Such acceptance of services as a necessary way forward may be due in part, to changes in technology in manufacturing and effects of globalisation manifested in global value chains and production networks. In light of these, many analysts have pointed out that the efficacy of manufacturing is waning given the rise of Artificial Intelligence (AI), uncompetitive labour cost and unbridgeable infrastructure gap that is the bane of developing countries. As a result, there is less enthusiasm around manufacturing as a driver of development in Africa.

Given the above reality, a shift towards certain services has been recommended, especially FIRE and telecommunications, as the viable alternative, in the absence of a rise in manufacturing in these countries. Canuto (2018) even recommends adopting a model of productivity that merges services with manufacturing, strategizing on elements that merge both physical and non-physical goods. But it is difficult to understand how the practicalities of this model will play out, and whether the kind of products to be created will overcome the challenges faced by the domestic services sectors in the global market. Even the recently flaunted “interconnected manufacturing” by Hallward-Driemeier and Nayyar (2017), which simply recommends interconnection between machinery and the internet, still demands that the
levels of automation are raised and adequately linked to domestic production to boost capabilities. And so, the question remains whether such products deriving from the said melding of services and manufacturing will be as tradeable and competitive in the global market to the extent that they generate foreign currency to adequately absorb the legion of low-skilled labour in the domestic economy.

This brings to the fore the fundamental deficiency of a service-based economy. For it is not that services are in themselves detrimental to the economy or are unable to absorb labour. In fact, they emerge to absorb the residual labour force in the absence of a large manufacturing sector, and can generate some income for the economy. This fact is corroborated by the high net contribution to Nigeria’s revenue derived from services. However, the problem remains around legitimate concerns of higher inequality due to poor remuneration for low- and middle-skilled workers in the services sectors. Inequality increases in countries experiencing de-industrialisation because the manufacturing sector has historically been the best safeguard of employment of the labour force (Rodrik, 2013). Most importantly, the non-material forms of most services make them less tradable in the global market to earn foreign currency for the country. For developing countries like Nigeria, services have been found to emerge around low capabilities, as such, remain uncompetitive abroad.

The term ‘premature de-industrialisation’ was first used by Dasgupta and Singh (2006) to describe the above phenomenon, in their finding that manufacturing share of output started to shrink in developing countries at income levels significantly lower than observed for advanced economies. As argued by Rodrik (2015), this phenomenon has been largely obscured by the focus on output growth, especially when analysed by nominal figures of manufacturing sector's contribution, which neglects changes in income and population growth. He shows that this phenomenon becomes glaring when employment share of manufacturing is used to measure sectoral contribution. Rodrik further shows that the substitution effect of this phenomenon is a reduction in the share of manufacturing output (which is said to experience more rapid productivity growth than the rest of the economy) and labour employed by the manufacturing sector, when the elasticity of substitution between manufacturing and other sectors of the economy is less than 1. This decline in manufacturing sector contribution is attributed to factors such as worsening trade deficit for developing countries within the global economy, general secular shift away from manufactures (or the displacement of unskilled labour force due to technological progress in the case of advanced economies).
The critical survey by Tregenna (2016) associates premature de-industrialisation with low levels of per capita income, and largely attributed it to policy changes by way of trade and financial liberalisation and austere monetary policies. These set of policies were markedly adopted in Nigeria (as with other parts of Africa) in the 1980s and 1990s. It is therefore unsurprising that the short-term focus of the (liberalised) financial sector in Nigeria disproportionately allocates credit to services and oil and gas relative to manufacturing. One implications of premature de-industrialisation, is a reduction in aggregate demand as employment in manufacturing falls, and consequently reduction in the possibility of convergence with advanced economies.

5.0 Concluding Remarks

The preferential allocation of credit to the services and oil and gas sectors therefore has been a fundamental driver of pre-mature de-industrialisation, with short-term profit motive of banks at the heart of this phenomenon. It is necessary to understand that the flow of credit in an economy is crucial in determining its economic structures. The state of the Nigerian economy shows that disproportionate credit allocation to services has damaging effects on its development. It is therefore necessary to re-visit the economic structures of the Nigerian economy if the country is to achieve sustainable development. At the core of this matter is that there is no alternative to industrialisation, albeit with consideration for the type of products around which manufacturing and industrialisation are to emerge. The services that emerge around these must be do so with strategic positioning on the Global Value Chains. Whichever route Nigeria chooses to development, productive capabilities must be developed, from which manufacturing and industries will emerge organically. There is huge potential wealth to be tapped from developing the manufacturing base for Nigeria’s large market.

Ultimately, it is necessary to understand the conditions within which manufacturing was made successful in today’s industrialised economies, not least the level of wages that ensured manufacturing thrived and maintained output growth, as opposed to its complete abandonment. This would mean revisiting the issue of distribution that ensures the income of the teeming low- and middle-skilled labour force can be boosted through labour policy reforms to continue to sustain aggregate demand. A redistributive taxation policy, especially on all forms of wealth, holds the key to balancing the disruption that technology poses to labour. While developing an effective tax system for Nigeria may seem independent of the current shift from manufacturing to services, these issues not independent. An effective industrial policy is one that ultimately recognises the interconnectedness of these factors, usually taken apart and analysed as such.
There is need to bring these issues together in the search for sustainable growth strategies in Nigeria, and indeed, the rest of Africa. The state of economic development in Nigeria should cause other African countries to rethink the quest for bank credit expansion with policies that will ensure its pitfalls are avoided.

References


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