

Investment Climate Reform in Nigeria: Challenges and Prospects

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This paper reviews the issues, challenges and prospects of investment climate reforms in Nigeria towards achieving faster growth. Specifically it reviews issues of governance, infrastructure, human resources, international integration, access to finance, microeconomic and gender issues. The challenges to investment climate reforms in Nigeria include restraining rent-seeking, establishing credibility, fostering public trust and legitimacy, human resources, infrastructure, shallow financial markets and overwhelming dependence on oil revenue. To address these challenges, the paper recommends electoral reforms, standardization of contract execution, stronger institutions including educational institutions, the use of credit bureaux and stricter surveillance of the nation's international borders. The paper concludes that a good investment climate is key to growth and poverty reduction. Government policies and behaviours shape investment climate and in the process play out over a wide field. However, no country has a perfect investment climate and perfection is not a prerequisite for reaping the benefits of good investment climate. Firms should be the starting point of reforms as they generate incomes and employment and indeed growth.

Keywords: Investment, Economic Growth, Poverty Reduction

JEL Classification: O16, O31

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I. Introduction

Developing countries especially in Sub-Saharan Africa have launched aggressive economic reforms in a bid to revitalize their economies that have hitherto suffered from structural imbalances and inappropriate policies (Magbagbeola, 2004). These imbalances are prominently manifested in monolithic and monocultural production bases. In Nigeria, the effects of structural imbalance are typified in the total dependence on agricultural production from the 1960s to the exclusive reliance on oil and gas since the early 1970s. Thus, the national economic development aspiration has remained that of altering the structure of production and consumption activities so as to diversify the economic base, reduce dependence on oil and on imports in the bid to return the economy on the path to self-sustaining growth (Ajakaiye, 2001). Consequently, the country has pursued economic reforms from the Structural Adjustment Programme (SAP) of the mid-1980s to the 1990s to the National Economic Empowerment and Development Strategy (NEEDS) of the 2000s. The

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NEEDS, however appears the most robust of the reforms so far and its articulation and implementation are the most deliberate and concerted. This is for several reasons including the fact that it was home grown and demand-driven.

So far, positive results have been identified since the enthronement of NEEDS, but the yet observed weakness in investment levels, including foreign direct investment (FDI), has triggered concerns about the quality of the “investment climate” in Nigeria. With regard to domestic investment, the critical question relates to why most wealthy Nigerians prefer to invest outside Nigeria. For foreign direct investment, one may want to know why foreign non-oil investors prefer to invest in other countries despite the huge human and material resources in Nigeria. Answers to these questions rest in the quality of investment climate in Nigeria.

Investment climate refers to the environment in which firms of all types and sizes invest and grow. Determinants of this environment can be classified into macroeconomic factors, governance issues and infrastructure (Bangladesh Enterprise Institute and the World Bank, 2003) Given the heterogeneity of firms' behaviour, investment climate reform has also a micro dimension and so covers in addition issues critical to the growth of individual firms. These include human resources, access to finance, among others (Caves, 1998; Bartelsman and Doms, 2000; Ahn, 2000).

Investment climate reform, therefore, refers to the provisioning of the enabling environment for investment and operational competitiveness of economic agents. It is a deliberate and concerted effort at removing obstacles to investment and growth of firms. The objective of this paper, therefore, is to review the issues, challenges and prospects of investment climate reforms in Nigeria towards achieving faster growth. In particular, the issues reviewed include governance, infrastructure, human resources, international integration, microeconomic factors, gender and overreliance on the petroleum sector. The importance of the paper is further amplified by the fact that Nigeria has initiated series of reforms and an investment climate reform at this time would maximize as well as sustain the gains therefrom.

The rest of the paper is in five sections. Following the introduction, section two treats the conceptual and theoretical issues while section three reviews the relevant literature. Section four overviews the Nigerian investment climate and section five deals with the challenges and prospects of investment climate reform

in Nigeria. Section six discusses the policy implications and proffers some recommendations while section seven summarizes and concludes the paper.

II. Conceptual and Theoretical Issues

Investment climate is about the environment in which firms and entrepreneurs of all types- from farmers and micro-enterprises to local manufacturing concerns and multinationals- have opportunities and incentives to invest productively, create jobs and expand (The World Bank, 2005). It consists of location specific factors that shape the enabling environment for firms to invest productively and grow (Smith and Hallward-Driemeier, 2005).

In Keynesian terminology, investment refers to real investment which adds to capital equipment. It leads to an increase in the level of income and production by increasing the production and purchase of capital goods. Investment, thus, includes new plants and equipment, construction of public works, net foreign investment, inventories, and stock and shares of new companies. In the words of Joan Robinson, "by investment is meant an addition to capital, i.e. making an addition to the stock of goods in existence. To be more precise, investment is the production or acquisition of real capital assets during any period of time". Thus emphasis on investment used to mean advocating greater quantities of investment, under the assumption that a financing gap was a barrier to development (Bangladesh Enterprise Institute and the World Bank, 2003). Recent research, however, focuses on the quality and not the quantity of investment (Easterly 1997; Soludo, 1998; The World Bank, 2005). They focus on the institutional and policy environment that determines whether investments pay off in greater competitiveness for firms and in sustained growth for the economy. After all, higher productivity in individual firms culminates in higher rates of growth of the gross national product (GNP). Therefore, though, the policy areas covered by investment climate is broad, the performance of individual firms is at the heart of the policy and micro-level data provide useful insights into how firms assess the package of policies and government behaviours using such criteria as risks, costs and barriers to competition. At the firm level, uncertainty about the content and implementation of government policies are of important concern. In developing countries, policy inconsistency is very rampant and inefficient implementation of policies sometimes occasioned by corruption and nepotism is a common feature of government business relationship. Poor policy design and weak institutions exacerbate macroeconomic instability, arbitrary regulation and weak protection of property rights. All these cloud business opportunities and chill incentives to invest productively.

Policy-related costs constitute a high percentage of firms' operational costs. These arise from outmoded and ill-conceived regulations. In addition to these are costs associated with infrastructure failure such as power outages, poor road network, crime and corruption. Together with weak contract enforcement and onerous regulation, these costs can amount to over 25 percent of sales or more than three times what firms typically pay in taxes (Smith and Hallward-Driemeier, 2005).

Firms naturally prefer less competition to more but discriminatory incentives in favour of one firm deny opportunities to others. However, competitive pressures drive firms to innovate, improve productivity, and share the benefits of higher productivity with consumers and employees. Economies of scale, market size and openness to trade can enhance competition but government influences competitive pressure through the regulation of market entry and exit and by its reaction to monopolistic behaviours.

The on-going liberalization and globalization have entrusted the private sector with the economic role of wealth creation and employment generation. In line with this goal, one cardinal thrust of economic reforms is growing the private sector to become the engine of growth and prosperity. For the private sector to play this role effectively requires the competitiveness of enterprises. Since enterprises operate in national environments which enhance or hinder their domestic or international competitiveness, business environment is inevitably of important policy concern. Poor business environment tends to increase the cost of doing business, which in turn, retards economic competitiveness. In the same vein, bad business environment negates firm-level productivity and efficiency of resource use. Theory and evidence underscore the inverse relationship between international competitiveness of nations and domestic cost of doing business. Notwithstanding the efficiency and cost effectiveness of firms, overall performance can still be undermined by difficult operating environment (Eifert et al, 2005). Other factors held constant, countries with stable, relatively lower-cost business climate are more likely to secure competitive edge in world markets. This is why nations today strive to ease domestic conditions for business and investments through investment climate reforms.

Given the foregoing analysis, some authors (Stern, 2002; World Bank and Bangladesh Enterprise Institute and the World Bank, 2003 and World Bank, 2005) have identified the perspectives of investment climate to include macroeconomic factors, governance, infrastructure, international integration, access to finance, human resources and microeconomic factors. In developing

countries especially in Africa, the exclusion of women from most economic, commercial and legislative matters has implications for investment climate. For this reason, this study also looks at gender issues. In all these, the expectation is that the relationship between these variables and the investment climate is positive.

III. Literature Review

Literature on investment climate reform is scanty. This is mainly because it was not until recently that policymakers and multilateral organizations began to emphasize the need for sound investment climate for promoting economic growth in developing countries (Stern, 2002). Earlier on, emphasis on investment as an engine of growth focused on the quantity rather than quality of investment under the assumption that a financing gap was the barrier to growth. This view has been criticized as too simplistic (Bangladesh Enterprise Institute and the World Bank, 2003). Indeed recent research shows little correlation between investment levels and growth rates at least in the short run (Easterly, 1997). Soludo (1998), concludes that for Nigeria, investment is negatively associated with growth. Pindyck (1990) argues that if the goal is to stimulate investment, stability and credibility could be much more important than tax incentives or interest rates.

Caballero and Corbo (1988) conclude that a major cost of political and economic instability may be its depressing effect on investment. This is likely to be important for less developed countries as investment level at any point in time is reflecting past behaviour of some uncertainty variables like inflation, terms of trade, etc.,. The authors recommend that relevant authorities must strive to reduce macroeconomic policy uncertainties if private investment is to grow. Government policies and behaviours shape opportunities and incentives facing firms and investment climate reforms are about shaping government policies and behaviours.

Mallon (2004) reports that the net impact of the investment climate reforms in Vietnam was the simplification of procedures for registering new businesses, and for operating and expanding these businesses. This resulted in a dramatic increase in the number and total registered capital of new private enterprises following the enactment of the Enterprise Law in January 2000. Up until the end of 1996, only 190 joint-stock companies, 8900 limited liability companies, and 21,000 private enterprises had registered under the 1990 Company Law and Law on Private Enterprises. This increased to 524 joint stock companies, 15,310 limited liability companies, and 29,135 private enterprises under the 1990 Company Law and Law on Private Enterprise by the end of 1999. Following the enactment of the

Enterprise Law of 2000, there were more than 70,000 newly registered companies by the end of 2003 including 6,791 joint-stock companies. This reflected in an increasing contribution of private business to GDP. In a similar study focused on the Peru Urban Land Reform, Endo (2004) reports that between July 1996 when the reform implementation started, and 2002, 1.3 million titles to individuals were produced and title formalization time was reduced from 7 years to 45 days. The 2005 World Development Report, with the theme "A Better Investment Climate for Everyone", analyzing data from the World Bank Investment Climate Survey, which cover more than 26,000 firms in 53 developing countries, and the Doing Business Project, which benchmarks regulatory regimes in more than 130 countries, concludes as follows:

- that investment climate is central to growth and poverty reduction;
- that reducing unjustified costs is critical but policy-related risks and barriers to competition also need to be tackled;
- that progress requires more than changes to formal policies; and
- that investment climate improvement is a process, not an event.

Pomeleano (2000) concludes *inter alia* that there were clearly micro excesses within a disciplined and benign macro financial context. He added that his results support Krugman's hypothesis that crony capitalism, and the supportive and necessary poor policies designed to "aid and abate" poor credit decisions lead to poor investment and misallocation of resources.

Investment climate is the location specific factors that shape the opportunities and incentives for firms to invest productively create jobs and expand (World Bank, 2005). Stern 2002 defines investment climate as "the policy, institutional and behavioural environment, both present and expected that influence the returns and risks associated with investment" The author identified three perspectives of investment climate: macroeconomic factors, governance and infrastructure (Bangladesh Enterprise Institute and the World Bank, 2003). Macroeconomic factors are exemplified in fiscal, monetary, exchange policies, political stability among others. Governance refers to government interactions with business and manifests in forms of regulations and corruption both of which affect the cost of doing business, risks and competition. Infrastructure refers to the quantity and quality of physical infrastructure such as power, transport and telecommunications as well as financial infrastructure such as banking or access to finance generally. The World Bank and Bangladesh Enterprise Institute 2003 in addition to these recognized international integration and human resources as further perspectives of investment climate. The central role of individual firms in

development has turned the attention of researchers and policymakers to micro-level-evidence in articulating investment climate policies. Thus, the sixth perspective of investment climate is the microeconomic environment which refers to how individual firms are encouraged through the provision of opportunities and incentives to increase their productivity, develop, adapt, and adopt better ways of doing things and respond to consumers (World Bank, 2005). In developing countries especially in Africa, the exclusion of women from most economic, commercial and legislative matters has implications for investment climate. In view of this, this study also looks at gender issues.

There has been a lack of consensus regarding the measurement methodology of investment climate. Firms evaluating alternative investment options, governments interested in improving their investment climate and researchers seeking to understand the role of different factors in explaining economic performance- all have attempted to define and measure investment climate. These attempts have expanded the variables available. The World Bank World Development Report 2005, identified five main challenges to the measurement of investment climate as

- The multidimensional nature of the concept being measured;
- The inherently difficult measurement of some dimensions;
- Differences in perspective across firms and activities;
- Differences between locations even in one country; and
- The experience on ground does not always reflect formal policies.

IV. Overview of Investment Climate in Nigeria

Investment climate in Nigeria is dominated by yet undefined set of relationship between the pervasive public sector and the incumbent firms, as well as public sector interference in private sector activities (Shiells, 2003). Government's extensive regulation manifested in the form of business registration and certification, combined with low disposable incomes of workers, weak institutional framework, incoherent and uncoordinated government policies among the three tiers of government, multiple taxation, provide incentives for rent-seeking to public officials. In turn, barriers to entry and competition, ineffective bankruptcy laws and procedures as well as weak corporate governance and inappropriate pricing mechanisms allow inefficient incumbent enterprises to remain in business.

With this general statement, this section discusses the investment climate in Nigeria under the following sub-headings: governance, infrastructure, access to

finance, international integration, human resources, microeconomic issues and gender.

Governance: A country's general structure of governance and the institutions that govern interactions between business and government determine the burden that firms face in complying with government regulations, the quality of government services and the extent to which corruption is associated with the procurement of those services.

The military occupied power for almost 30 out of the 40 years of independence before 2000. In these years the country was a pariah state and transparency and good governance were not serious issues of policy consideration. Traditionally, military regimes lack accountability as well as checks and balances, as they are constructed on a command structure. Given the preponderance of oil resources in Nigeria, national institutions were weakened to promote corruption. The collection and allocation of oil rents was according to the caprices of a few military officers and their cronies. This created a horde of rent entrepreneurs; that is, "Big Men" without any productive source of livelihood except proximity to state power (Soludo, 2005). In the circumstance, merit suffered as there were no standards of performance and accountability.

Government grew in size as the major source of employment. Citizens expected government as the "Giver" to provide everything free for them. In the face of huge oil revenue, tax collection was downplayed and Nigerians abandoned their civic responsibilities. Government on its part became less and less accountable and transparent, while the people remained in the delusion that there was no link between their taxes and government expenditure.

The link between government and the private sector also got broken. Before the military intervention into government and the oil sector dominance of the economy, the government was under pressure to provide the enabling environment for businesses to thrive because businesses in turn provided employment and generated revenue for the government. Because of oil wealth and the lack of accountability of military governments, government did not need the private sector revenue, nor was it under pressure to please the voters.

Of course, the inevitable consequence of the foregoing scenarios was waste, weak institutions, corruption and failure of public policies. Informal interpersonal networks and relationships replaced formal institutions and rules of procedure. Arbitrariness and private interest took over at the expense of public trust and

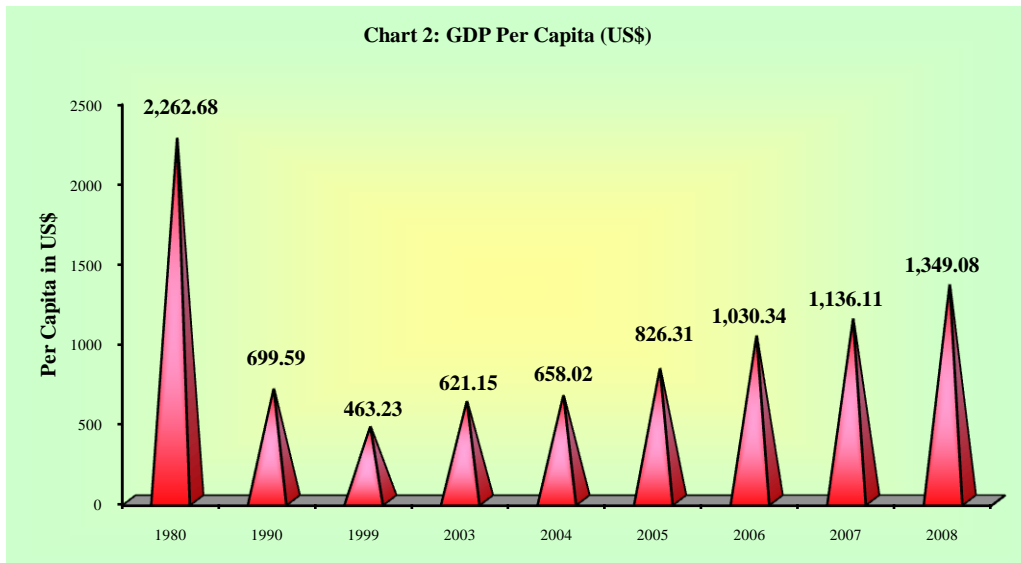
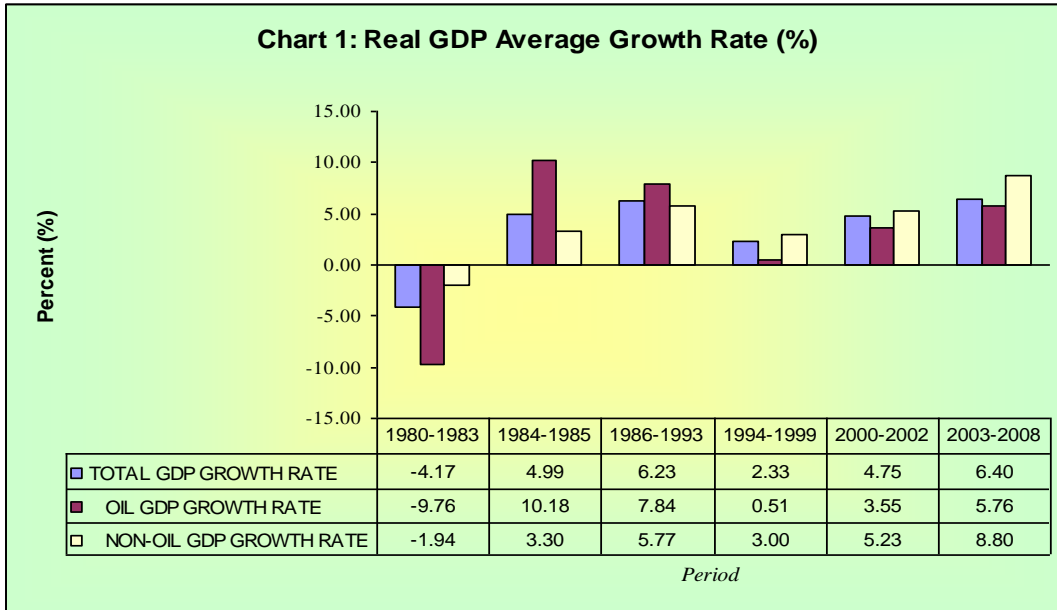
legitimacy. Corruption blossomed with resultant underdevelopment. The world looked away from Nigeria.

The return of democracy in 1999 ushered in some degree of transparency and accountability in the system. This was as a result of the many reforms undertaken by the civilian administration. The principal reforms included:

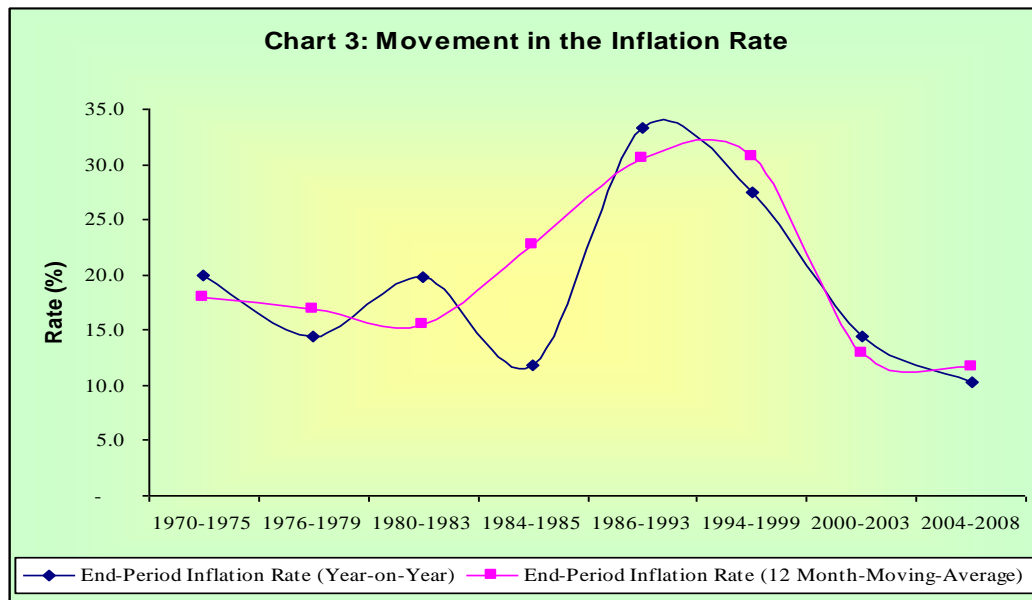
- De-militarization and reforms of the military by which the government began to remove the military from government and to refocus it to its core mandate of defending the territorial integrity of the nation.
- Re-building basic institutions of the state. The collapse of most state institutions led to the dilapidation of legal and regulatory functions of the government. The new democracy, therefore, needed strong institutions to enable it enforce its principles. Therefore the police force was strengthened by about four times. The Independent Corrupt Practices Commission and the Economic and Financial Crimes Commission were established to fight corruption. A new procurement process, emphasizing due process, was introduced to promote value for money. Democratic institutions, the legislative and judiciary were not left out.
- As the business environment also suffered in the hands of the rentier class with costs and risks of doing business rising astronomically while competitiveness dwindled, the programmes of liberalization and privatization was undertaken. The telecommunication sub-sector was liberalized and most of the ailing government enterprises were privatized. Attempts were made to rebuild the power sector, roads and airports that decayed over the years.

An Economic Team was set up to aid the government through advocacy and evidence-based advice to manage the economy. There was greater coordination of monetary and fiscal policies leading to robust macroeconomic outcomes. The banking and financial sector reforms were also undertaken, a significant phase of which was the Bank consolidation of 2004-2005. Exchange rate and foreign exchange management was also reformed. Nigeria also adopted the Common External Tariff.

Attempts were made to break up public monopolies such as the energy and telecommunication sectors.



The reforms further impacted positively on the economy resulting in higher GDP growth rates, higher GDP per capita and lower inflation rate, among others.



Despite all these, the position of Nigeria among some West African Countries with respect to some investment climate indicators remain poor as is found in the table below.

Table 1: Nigeria's Ranking on the Global Competitiveness Index 2005/6

Country	Global Competitiveness Ranking		Business Competitiveness Index	Quality of the National Business Environment
	2005	2006		
Nigeria	88(3.23)	101(3.45)	76	79
South Africa	42(4.31)	45(4.36)	28	30
Botswana	48(4.21)	81(3.79)	55	50
Mauritius	52(4.0)	55(4.20)	52	49
Ghana	59(3.82)	- -	45	47

Figures in parenthesis are scores

Source: Global Competitiveness Report 2006-2007, WEF.

Nigeria ranked 88 in 2005 and 101 in 2006 in the Global Competitiveness Ranking while Botswana ranked 48 and 81 and Mauritius 52 and 55 in the same period; Ghana ranked 59 in 2005. Ghana ranked 45 against Nigeria's 76 under the Business Competitive Index in 2005. Under quality of National Business Environment, Nigeria was ranked 79 while Ghana was ranked 47. This could

explain the departure of Dunlop and Michelin from Nigeria to Ghana in the last two years. Governance and transparency issues are still replete with poor investment climate attributes. There is yet no coordination between the three tiers of government. Most of what progress is observed in the country at this time is at the instance of the Federal government while the States and the local governments are still insensitive to the need for improved investment climate in their jurisdictions, in particular, and the nation, at large. The opaque administrative methodology especially in the two lower tiers of government still continues unabated with attendant corruption. The adverse effects of this malaise have manifested in the lack of clarity in government policies resulting in uncertainty and confusion among prospective and even incumbent investors.

Infrastructure: Infrastructure and firm performance interact in several ways. Established firms already connected to utilities are affected by the quality of the service while new firms or those hoping to expand are concerned with the difficulties in connecting to utilities. In Nigeria, infrastructure provision has been the preserve of the government until very recently. The government provides water, electricity, roads, petroleum products, telecommunications, etc. All these relied on government subvention for funding and so the disposition of the government in power was of critical importance to the performance of the various infrastructures. During the military regimes, the provision of infrastructure suffered neglect resulting in the decay of most of the facilities. For example, the Turn-Around-Maintenance of the refineries were done according to the whims and caprices of the dictators and not in line with technical prescription. When it was to be done, it was contracted to the cronies of the powers that be and not to experts. This same attitude pervaded road construction, rail construction, the power sector, indeed all facets of infrastructure. The few democratic regimes that intervened during the prolonged military era were not much different as they could not repair the damages of one military regime before another took over power. The civilians on their part given the insecurity of their tenure were highly corrupt and so had only little money left for infrastructure development. Worse still, given the low technological base of the country, most of the infrastructure was provided by foreign firms on turn-key basis with implications for local content and cost.

In the democratic dispensation since 2000, efforts have been made, therefore, to privatize the agencies saddled with the provision of infrastructure. Some success has been achieved in this regard but much still remain to be done. The telecommunications liberalization has been accomplished to the applause of many but the main gateway is yet to be privatized. This has to do with the poor

state of the facility which has limited the price offered by core investors. The refineries are also in this state. The government contemplated refurbishing them before sale but the cost of doing so was huge. It therefore decided to dispose of it as is but the next government felt the price was too low for such a facility and reversed the action with implications for credibility. Attempts were also made to unbundle the National Electric Power Authority. Thus far, this has remained inconclusive and it appears to many that the government is even going back on the programme. The attempted unbundling of the Nigerian National Petroleum Corporation (NNPC) is also yet to be completed. Road maintenance was sometime privatized through the installation of toll gates on most major roads in the country.

Overnight these gates were dismantled and the Federal Road Maintenance Agency was established. The poor power supply in Nigeria has for a long time held down industrial and, indeed, business development. It is the most critical constraint to enterprise competitiveness across Nigeria states. The African Institute of Applied Economics, (2007) shows that seven of the 36 states of the federation including the Federal Capital Territory have an average of below two hours of public electricity supply per day while 27 states have 2 to 7 hours of public electricity supply per day. Only two states have an average of 8 to 13 hours per day while no state has above 13 hours of public electricity per day. UNIDO Manufacturing Enterprise Survey 2004 found that firms have only 2.98 days of public electricity in a week. The World Bank Investment Climate survey, 2002 found that 97.4 per cent of firms have self-provisioned electricity to tide over inadequacies in the public supply. Skoup and Company survey of Industrial clusters in Eastern Nigeria reported that 92 per cent of firms in the region perceive electricity shortages as their biggest production problem.

In terms of petroleum products supply, the pricing and supply of products have haunted the energy sector particularly the transportation sub-sector. Inappropriate pricing of energy (petroleum products, electricity) serve as implicit subsidies especially to energy-intensive enterprises while at the same time corruptly enriching ordinary petrol station attendants with consequent abuse of moral values. The problem was exacerbated by the government's insistence on the removal of subsidy on the products. The government claims that it spent N1.2 trillion on petroleum products price subsidy between 2007 and 2009. Labour unions, however, perceive the matter of subsidy as a mere hoax arguing that the government has no reason not to refine sufficient products for domestic consumption - a situation that would have reduced the price of products drastically. They also argue that Nigerians have a right to subsidized consumption

of petroleum products as free gifts of nature to the country. At the micro –level, therefore, only in two of 36 states of the federation do prices conform to the official ones. In 17 states, price variation range from 1-10 per cent and in 14 states it varies from 11-20 per cent. In 3 states, the variation is above 20 per cent. In terms of availability of products, 28 states have products available 100 per cent of the time while 8 states have it only 50 per cent of the time (BECANS, 2007).

Another important challenge to both corporate and individual citizens is the inadequacy of water supply. UNIDO Manufacturing Enterprise survey in 2004, indicates that firms that rely heavily on water for their production such as food, beverages, chemicals, cosmetics and foam industries had especially reduced their dependence on public water supply. The CBN 2004 Baseline Survey of Small and Medium Enterprises found that public water supply is a big bottle neck to enterprise performance and competitiveness. The study of industrial clusters in Eastern Nigeria (Skoup and Company Ltd, in collaboration with the International Finance Corporation and the World Bank, 2003) reported that 85 per cent of the respondent firms perceive inadequate water supply as their greatest constraint and so more than 50 per cent of the studied firms had bore holes. Daily per capita water supply in Nigeria was 20 liters in 11 of 36 states, but between 14 and 20 liters in 4 states, and below 2 liters in 7 states. In 3 states of the Federation, the average price of 20 liters of private water supply was below N5 and between N5 and N7 in 7 states. It was between N8 and N10 in 15 states and above N10 in 11 states. BECANS Business Environment Reports show that in 23 states of Nigeria, there was less than 1 post office per 100,000 persons and only 12 states have between 1 and 2 post offices per 100,000 persons. In 2 states, there was 70 per cent incidence of ownership of mobile telephones, 9 states with between 31 and 50 per cent, 14 states with between 11 and 30 per cent and 11 states with between 10 per cent and below.

Access to Finance

Economic theory suggests that businesses will invest in projects where the expected benefits exceed the cost of investment. This efficient outcome, however, can be achieved only when entrepreneurs face no credit constraint unrelated to their own performance. Financial intermediation for investments especially by small and medium enterprises (SMEs) is limited by underdeveloped money and capital markets. Moreover, weak property rights, contract enforcement and bankruptcy procedures present obstacles to further strengthening of the banks. Financing of investment by the formal financial institutions is mainly restricted to very large enterprises with credible track records and not for up and starting projects no matter how viable. In Nigeria as in other

developing economies, access to formal finance is a critical constraint to business and enterprise operations and growth. However, in Nigeria, studies have shown that there is a low amount of domestic investment through loans vis-à-vis some comparator countries and the Eurozone. For example, Oyelaran-Oyeyinka, (2007) shows that in 2006 total loans as per cent of GDP was only 19.7 while it was 47.2, 54.3, 94.0 and 104.1 in Kazakh, Egypt, South Africa and Eurozone. The paper went further to show that majority of the loans were made to large corporations while the SMEs were denied facilities. Given the problems encountered by firms in obtaining finance from the formal banking sector, especially after the bank consolidation of 2005, efforts have been intensified towards providing finance outside the formal banking sector. This has led to the strengthening of some financial institutions. These include five development finance institutions (Bank of Industry, Federal Mortgage Bank of Nigeria, The Nigerian Export Import Bank, the Nigerian Agricultural, Cooperative and Rural Development Bank (now Bank of Agriculture) and the Urban Development Bank) as at 2009. There are also 709 microfinance banks, 5 discount houses, 112 finance companies, 93 primary mortgage institutions and 703 bureaux-de-change

The CBN also guarantees loans for agricultural development under the Agricultural Credit Guarantee Scheme Fund (ACGSF). As at end-2007, a cumulative 540,925 loans valued at N19, 34 billion had been guaranteed by the Bank for the development of various sub-sectors of agriculture. In addition, the Small and Medium Enterprises Equity Investment Scheme was set up in 2001 by the CBN in collaboration with the Bankers' Committee. The scheme covenants that banks in the country invest 10 per cent of their profit before tax in industries. The list of ventures covered by the scheme was later extended and further reform of the scheme made it voluntary to the banks. As at 2007, notwithstanding the dilution of the provisions of the scheme, the cumulative sum set aside by the banks stood at N42.02 billion. The cumulative investment by banks was N24.7 billion in 327 projects.

International Integration

Research has shown that countries that aggressively pursued integration with the global economy (such as Brazil, China, India, Malaysia, Mexico, the Philippines, and Thailand) grew more quickly in the 1990s than those that did not. Indeed, many studies find that openness to trade and foreign direct investment accelerates growth (Dollar and Kraay, 2001; and Frankel and Romer, 1999). Sachs and Warner (1995) find that openness is a highly significant determinant of growth and when combined with property rights, might even represent a sufficient condition for growth in poor countries. External sector reforms included the pursuit

of debt relief and exit from the Paris club, as well as the submission of the Nigerian nation to assessment by international rating agencies to promote competitiveness. Some of the efforts in this regard included: Policy Support Instrument (PSI) with the IMF, Standard and Poor/ Fitch ratings, New Partnership for African Development (NEPAD) Peer Review Mechanism. Openness measured as the ratio of total trade (imports and exports) would provide different effects if the country in question is a price taker from if it is a price giver. Nigeria is an oil exporter. It is, however, a price taker as well as a primary exporter implying that the local content of the exports is small and the measure of international integration based on ratio of trade and GDP, overestimated. Moreover, Nigeria is an import-dependent country especially of finished goods. This also adds to trade and openness. A more realistic measure of openness especially in the context of investment climate should rely on the net flow of foreign exchange into the country.

Human Resources

The availability of inputs is a critical element of the investment climate. For human resources, this implies more than just an abundant supply of workers. It also implies workers with sufficient education and technological know-how. Ezekwe, (1994) states that it is not the lack of investment in physical capital alone, which prevents poor countries from catching up with rich ones. Educational attainment and public spending on education are correlated positively with economic growth. Moreover, import of physical capital is less costly than the domestic development of human capital and technical expertise. In Nigeria, given the poor engineering and scientific-culture, most of the production processes are based on imported technology. Also, as many key projects in the past were executed on turn-key basis, most inputs and intermediate products are sourced from external supplies. The low technological base is further compounded by inappropriate science education and poor attitude to research and development (R&D) to facilitate the adoption and adaptation of ideas developed in other jurisdictions. For instance in 1980-1992 allocation to science and technology in Nigeria was 0.1 per cent of GDP while in Tanzania, Taiwan, India, South Korea, Malaysia and Japan, it was 1.5-3.5 per cent, 2.0 per cent, 2.0 per cent of GDP and 0.6-1.0 per cent of GNP and 2.8 per cent of GNP, respectively. (Ezekwe, 1994).

In Nigeria, especially from the colonial era to the early 2000s, organized human resource development was principally undertaken by the government and some religious organizations through the provision of formal education. In this era, the federal and state governments built schools from primary to tertiary levels and ran them and any person who dropped out of any such school stood the chance of

not receiving any patronage, including jobs, from the government. However, as the country grew both in population and economic activities, there was an explosion in the need for formal education to the extent that the government felt incapable of providing the services alone. More recently, therefore, private proprietors were allowed and schools of all sorts and cadres are established and run by private entities along side the government. As at 2007, of the 36 states in the country including the Federal Capital Territory, Abuja, the average pupil teacher ratio stood at 30 and below in 12 states, 31-40 in 11 states, 41-50 in 4 states and 50 and above in 9 states. With respect to funding, only six states had education share of capital budget of 20-26 per cent, 3 states had 16-20 per cent, 11 states had 11-15 per cent, 14 states had 5-10 per cent and 2 states below 5 per cent (African Institute of Applied Economics, 2007). Also only an average of 13 per cent of state's capital budgets was devoted to healthcare. Specifically, 5 states devoted between 10 and 14 per cent of their annual budgets to the health sector and 20 states between 5 and 9 per cent. Eleven states devote 5 per cent and below of their capital budgets to health. In terms of entrepreneurship promotion, policy on entrepreneurship exists only in 14 of the 36 states of the Federation and awards for deserving entrepreneurs exist in only one state. More recently, entrepreneurship promotion was undertaken by the Central Bank of Nigeria in the six geopolitical zones of the country aimed at developing entrepreneurial skills of young men and women across the country. In all of this, however, little attention is paid to vocational training. Training of artisans (bricklayers, carpenters automobile mechanics, etc) is still a private sector concern. In this regard, no enforceable standards are in place to promote high quality output. Thus, costing of jobs is difficult as standards vary and there is no difference between a master and an apprentice.

Microeconomic Issues

The Federal Government of Nigeria has made some selective interventions to the benefit of particular firms and sectors of the economy. This became necessary to complement the progress made at the macroeconomic frontier. Such initiatives focused on removing factors that limit the accelerated growth and development within the microeconomy and as such it focused on key cross-cutting areas including technology, human resource development, and access to finance for the SME subsector among others. Key input sectors such as transport, telecommunications, and energy have also been targeted to improve microeconomic competitiveness. Key microeconomic reforms to date include: the various federal government initiatives on agriculture, the establishment of microfinance banks in the country, the setting up of the Small and Medium Enterprises Equity Investment Scheme, the Agricultural Credit Guarantee Scheme

Fund, the Trust Fund Model, The Automobile Development Fund, the Development Finance Institutions and the Mass Transit Scheme, among others. In addition, the Nigeria Import Export Bank was set up to help the export subsector.

Gender Issues: The various ethnic groups in Nigeria traditionally limit the role of the women in the economy to mere water fetching and wood hewing. Though this attitude is changing across the country for the better, it is still prevalent in some parts of the country. One of the critical consequences of this is the exclusion of girl children from schools. Boys are preferred to girls as candidates for school enrolment while the girls are made ready for marriage. For example in 1996/7, literacy rate for males in the country was 58.2 per cent while for women it was 41.0 per cent. In some parts of the country it was 32.2 per cent for men and 14.7 per cent for women. In the same period, 35.2 per cent of Nigerian women married before age 15 (Federal Office of Statistics 1996/7). With this background, women were excluded from economic/commercial, contractual as well as legislative activities. A woman cannot rent a shop or a living room on her own unless she is supported by a man. A woman is cannot take a suspect on bail or stand surety or enter into a contract. She cannot buy or sell land and is not entitled to freedom of association. As abhorrent as this attitude is most women appear to have accepted it to the extent that they cannot stand on their own. They clamour for concessions even in environments as competitive as holding political offices. In work places, it is common to hear such utterances as "we need men in this office". The law, however, fails to protect the women in any way. On marital matters, the man is absolute. Only a few women would seek legal redress in case of marital abuse. For this reason many women are intimidated and are not empowered. The society as a whole, therefore, loses the potential contribution of women to growth and development. As they cannot give what they do not have, the children are hardly brought up beyond the level of their mothers.

V. Challenges and Prospects to Investment Climate Reforms

Improvement in investment climate offers faster growth and poverty reduction. Despite the many benefits, investment climate reforms are slow and difficult. This is because of a number of challenges that countries have to face in the process of improving the investment climate. More countries are improving on their investment climate and are reaping the fruits of faster growth and less poverty despite the challenges. This is to say that there is no perfect investment climate and that perfection even on one dimension is not a prerequisite to growth and poverty reduction. It is, however, important that the concept is understood and accepted and that a deliberate and concerted effort is made in a sustainable

way towards improving the investment climate. Nigeria's prospect in investment climate reforms is bright. This section deals with some of the various challenges Nigeria faces and the prospects it can leverage on in the process of improving on the investment climate. At the government level, three challenges stand out. These include restraining rent seeking, establishing credibility and fostering public trust and legitimacy.

Restraining Rent Seeking

Rent seeking behaviour has been ingrained in the Nigerian public life. The huge petroleum rent and the prolonged military regime both nurtured the rent-seeking behaviour of the people to the extent that the challenge for the government is to restrain it in order to improve on the investment climate. On the one hand, rent seekers would fight to retain the status quo while on the other hand efforts are needed to bring about a paradigm shift from rent-seeking to productive enterprise. Already, given the length of time during which rent-seeking has thrived in Nigeria, a large proportion of Nigerians rely on it for their wealth and livelihood and this further strengthens the opposition to change. Nevertheless, the Independent Corrupt Practices Commission (ICPC) and the Economic and Financial Crimes Commission (EFCC) have been set up by the government to fight corruption and financial crimes. The government in power has also pledged to respect the rule of law. These are merely dealing with the symptoms of rent seeking and not with the root cause of it. To deal with rent seeking itself, a complete overhaul of the system is required.

Establishing credibility

While the military lasted in power, and rent seeking remained the main business formula, government lost credibility both at home and abroad. Government policies were reversed indiscriminately and even those that were not reversed were allowed through non-implementation to die off naturally. Now that the military has gone, the people need to be roused to the realization that things have changed. This is a great challenge as the people still attribute obnoxious motives to government pronouncements. Actions of government ten years after the demise of military regime are attributed to ethnic, religious, political, even cultural motivations.

Investment is forward-looking and so relies heavily on government policies which decision makers believe are certain. Therefore, policies that lack credibility are unlikely to elicit the intended investment response. But a legacy of political, economic, cultural and even religious instability undermines the credibility of policy. As democracy firms up in the polity and the electoral process becomes

more capable of producing credible law makers and executives, credibility would return gradually. This is an evolutionary process that can be engineered for greater and speedier returns.

Fostering public trust and legitimacy

Business transactions are enhanced by trust and trust among market participants nurtures productive exchange and reduces the burden on regulation and contract enforcement. In Nigeria, the lack of trust among market participants is manifested partly in the extent to which transactions are cash-based, banking is viewed with suspicion and price gains by listed companies at stock exchange are regarded as a hoax. So while the citizenry doubts the government, one government doubts another just as one political party does not believe the other and firms doubt one another. This scenario constitutes a brick wall on the way to better investment climate in Nigeria. All these have to be resolved by the government in order to attract and retain public trust and legitimacy and move forward to improve on the investment climate. Public trust can return through a reformed democratic process. The process has to be seen to persevere in doing the right things. The caliber of corporate governance especially in the organizations that hold the assets of the nation in trust is an indicator of the speed at which trust is re-established in the country. Some of these organizations include the deposit money bank, the stock exchange, insurance companies, etc.

Human Resources

Government capabilities to monitor and improve on investment climate are priority as officials should be able to improve on policy articulation and implementation. The regulatory framework also needs constant fine-tuning. But the many years during which the political class was excluded from political activities and the civil service was rendered redundant by the military have nurtured an inept civil service and a political class devoid of ideology and decorum. Thus, one critical challenge to improving the investment climate in Nigeria is the lack of necessary government capabilities to articulate and implement policies. The officials of the government are part of the decadent society and this state reflects in the performance of their duties. To succeed in improving the investment climate, this situation should be reversed and that is a great challenge to the government. The Nigerian private sector is still fragile and inexperienced. This is due to poor human capability in the sector. The challenge flows from directing the attention of the youth to vocational education as a means of leading them to successful business life. Nigeria is blessed with a huge young population that is interested in learning given the high demand for opportunities in the educational establishments. The number of the

establishments is also increasing particularly with the liberalization of the sector. The globalization process through the information and communication technology is an added advantage to the development of education and, indeed, human capacity in Nigeria. In spite of these, the challenge of quality remains.

Infrastructure

Infrastructure connects firms to their customers and suppliers and helps them to take advantage of modern production techniques. However, challenges under infrastructure flow from market power associated with economies of scale. As the number of consumers increase, supply is often drowned especially in a developing country like Nigeria, where the population growth rate often outstrips the growth rate of the economy. In Nigeria the age-long government involvement in infrastructure provision has inadvertently laid the foundation for inefficiency both in the provision and consumption of utilities as well as the unwillingness to pay service charges. Bills collection by the various government agencies responsible for infrastructure provision is lax and the people over the years come to believe that the government is a free giver. To be able to sustain infrastructure provision, there has to be a paradigm shift. How could the government change this long-standing pattern is a huge challenge. In addition to this, is the problem of corruption. Government contracts are poorly executed and in some cases are not delivered on at all. On many occasions, the perpetrators were not prosecuted and it was almost becoming the normal trend. To bring government functionaries to respect instructions of the government to the extent of religiously rendering value for money is a huge challenge. However, the successful implementation of the amnesty programme in the Niger Delta leads one to believe that the dream of 10,000 megawatts of electricity in the near term would be realized. If commensurate addition is made to the transmission and distribution infrastructure, power supply in the country would improve. The law enforcement agencies in the country as well as the judiciary have demonstrated some effectiveness and efficiency in recent times and this is expected to impact inversely on corruption thus engendering more effective contract execution.

Financial markets

When functioning well, financial markets connect firms to lenders and investors willing to fund their ventures and share some of their risks. But the underlying challenges with finance flow from information problems, which are often exacerbated by insecure property rights. Land and even houses for example, cannot easily be used as collaterals due to the insecurity of property rights. Worse

still, there is hardly unique identification of persons. Names of persons can change either by changing the sequence of the surnames with that of the forenames or vice versa. This is because there is no single way of recognizing a person. Therefore, information on persons is vague and can hardly be used for contracts. But efficient financial markets operate in a transparent environment. The challenge here, therefore, is how to ensure that both corporate and individual citizens are uniquely recognized for contractual purposes. However, the National Identity Card Programme has attempted to deal with this challenge of identification of persons and is, indeed, one of the most reliable ways to handle it. Property rights documentation is slow and that appears to discourage people from seeking to document their properties. Otherwise, the banks would accept land and houses as collaterals if the documentation and the location are acceptable.

The literature shows that big banks are more likely to lend to large firms relative to small and medium ones (Berger and Udell, 2002; Craig and Hardee, 2004). Nigeria has recently concluded a bank consolidation exercise. The challenge is that given that most firms in the country are small and medium, credit to the core private sector has since declined. The Central Bank of Nigeria proactively went ahead to promote the microfinance banks. This is working but is yet to show up in the level of credit to the targeted group. The challenge is that in the era of globalization, how firms would attract funds from banks for investment at affordable rates of interest.

Microeconomic Issues

Going beyond the basics, the government sometimes intervenes in specific sectors or firms. Success in these initiatives is dependent on the level of knowledge of the sector or firm in which the intervention is to take place. Thus, the challenge flows from the lack of adequate information on the micro entity's operational circumstances. Coupled with this are budgetary issues that touch on the choice of a particular industry or sector in preference to others. Empirical studies can be undertaken on the firms or sectors of interest and based on the results of such studies, interventions can be carried out to the benefit of all. Budgetary provisions for interventions can form part of the appropriation bill for a particular year, thus enabling the government to intervene in sectors that are in need accordingly.

International integration

This exposes the country to foreign influences and checks and balances. The challenge, however, is that policy flexibility is lost and sometimes sovereignty

appears compromised. Membership of international organizations has been of some benefit to Nigeria. What is important is that the protocols and agreements are properly examined before they are signed. This again calls for knowledgeable and dedicated civil servants. Even of greater importance is the issue of loss of policy flexibility which makes greater demand on the policy makers to avoid reversals

The overwhelming dependence on the oil revenue

The Nigerian economy has relied on the oil revenue since the 1970s and this has limited government's attention to the non-oil sector especially the individual micro-level operators. The oil revenue also has encouraged rent-seeking in the economy and, this has withheld trust and consensus among market participants. It has also exacerbated the problems of economic management in Nigeria as government agencies are not committed to best practices since the oil revenue would flow whether the domestic economy works optimally or not. The oil industry also has a negative impact on public institutions by weakening them. The challenge flows from the need to strengthen the institutions in the face of the oil industry. These and many more problems of the oil revenue must be resolved for the investment climate reform to succeed. The oil revenue, however, provides the funds for running the country and places Nigeria on the list of countries considered for foreign investment. The challenges of rent-seeking and "Dutch Disease" are consequences of bad management of oil revenue. Sustained democratic governance holds the prospects of resolving these challenges.

The exclusive regime for women

This is gradually giving way for a more inclusive one. There are still challenges that are traceable to tradition and, sometimes, religion. This is, therefore, a serious problem as the government would be very careful in dealing with religious matters in a multi-religious country like Nigeria. But the consequences of delay are huge as a delay of one year affects a generation of Nigerians. Here lies the dilemma. However, globalization and, indeed, information and communications technology have opened up the world for Nigerians to see the growth potentials of girl children. Democratic governments in the country have also seen that much depends on them to reverse the trend of girl exclusion from school and economic activities to that of inclusion. In Nigeria too, given the increasing mobility of persons from all parts of the country, cultures are gradually streamlining and the walls of extremities are caving in. Women are now members of the National Assembly and belong to various professions and work in various establishments in the country and abroad. At least those women that have the opportunity of participating in these endeavours would not let their girl children

stay out of school or after going to school not put their knowledge into practice. The prospects are, therefore, bright for women to take their pride of place in Nigeria.

The dualization of the economy into formal and informal has grave adverse implications for economic policies. Improved investment climate for informal sector firms would imply addressing the constraints they find most binding and reducing the barriers to becoming formal. Rural firms too, though may be formal, suffer from the same constraints as the informal firms. Improved investment climate would unleash the growth potential in these firms and thus integrate them into the mainstream economy. These are the firms that could locate side-by-side with the oil firms in the rural environments of the oil-producing areas and offer services to the multinational oil companies, thus, increasing the local content of the Nigerian oil industry.

Presently there are many opportunities for firms in the industrialized countries but only those firms with the appropriate investment climate can take advantage of such opportunities. The African Growth Opportunity Act (AGOA) of the United States of America is one of such opportunities. To benefit from this opportunity, a firm has to produce the required goods at competitive prices and quality and export them to US markets. Improved investment climate would enhance the competitiveness of firms and so increase their chances of benefiting from AGOA. The New Partnership for African Development (NEPAD) is another opportunity and Nigeria would benefit from these only if the investment climate is appropriate.

Nigeria is endowed with material and human resources. There is, therefore, a plethora of incentives to grow industrially. The raw materials are there and the Nigerian market is large. Nigeria also has reach advantage over the West African market. On the other hand, owing to the policy of trade liberalization, the Nigerian market can be flooded by foreign goods thus making the country a mere consuming nation. To turn the situation to Nigeria's advantage, investment climate should be persistently improved upon. Once the existing institutions are sensitized to their responsibilities regarding investment climate and the firms are carried along, competition would drive the process while the government merely regulates, monitors and fine-tunes the climate to the benefit of all.

VI. Policy Implications/Recommendations

Investment climate is critical to growth and poverty reduction. Nigerian governments have already recognized this fact and have consequently put in place several measures aimed at improving the investment climate. However, there are still challenges. For purposes of policy, the implications of our analysis include:

Rent-seeking remains the most damaging challenge in Nigeria's economic and social life. Efforts at restraining it, thus far, have only dealt with the symptoms and not yet with rent seeking itself. To tackle the problem, there is need for reforms. The Constitution needs a review to limit the powers of some functionaries that promote rent-seeking. There is need for electoral reforms, stiffer sanctions for errant persons or institutions, standardization of contract execution, among others.

In order to establish credibility, reforms have to be sustained and deepened. Government functionaries should persevere in doing the right things. Right things have to be done persistently to convince all and sundry that, that is the only way to do it.

Public trust has diffused because corporate governance was lax both in the public and private sectors of the economy. There is need, therefore, to strengthen corporate governance especially in those institutions that hold public assets in trust (the banks, the stock exchange, insurance companies, the national and state assemblies, etc).

Even if there are opportunities for every Nigerian in tertiary institutions, not all Nigerians would complete the primary and secondary education. Provision should, therefore, be made for school drop outs. School drop-outs or even those that have not attempted at all should be given vocational training supervised by the government just as is the case with formal education. Apprenticeship is a form of education and government should be involved in it to ensure that the apprentice receives standard training. The curricula should meet the skill needs of firms. Given adequate incentive, the private sector can undertake such training under government supervision.

Rent-seeking and corruption are the major challenges to infrastructure provision. Corruption thrives in opaque environments and contract awards should be more transparent than hither to. Contracts should be standardized so that a prospective contractor knows what is expected of him/her and the details of the

contract are known to the public. Roads have life span and should the road collapse before the expected time, the contractor should be called to explain.

Financial markets rely on confidence for their functions. Market participants should be easily identified and recognized. The banks for example should demonstrate good governance while the customers should be known through adequate information. The use of credit bureaus has been recommended by some but that would work if there has been in place a means of identifying persons and corporate bodies uniquely. The National Identity Card project has to be revisited to ensure that every Nigerian acquires the card. Every other thing in the economy (registration at school, issuance of driver's license, etc) should take off from it. The Nigerian borders should be put under stricter surveillance to check the movement of illegal migrants.

Government intervention in the economy is unavoidable. However, the government should know where, when and how to intervene. This is the product of a micro level evidence which firm surveys would produce. Firms, therefore, should be surveyed regularly and the results of such surveys made public. Government intervention should be funded through budgetary provisions and not through ad-hoc arrangements.

International protocols and agreements compromise policy flexibility. However, in this era of globalization, autarky appears retrogressive. The protocols should be signed only after a close study of the situation by experts. There is need for selectivity. Participation at international fora makes or mars national reputation. So participation should be efficient and effective and not by anybody but the expert on the subject matter.

Some people including Nigerians have wished that the petroleum dries up. They claim that the existence of the resource has removed the thinking ability of Nigerians. The over-reliance on petroleum makes the resource a curse rather than a blessing. There is an urgent need to diversify away from petroleum. Promote industry and agriculture through not only more funding but also more extension services and better investment climate.

There is need for social reforms that would eliminate discriminatory practices especially between men and women, between the children of the rich and those of the poor. Let there be equal opportunities for everybody. This can be guaranteed by strong institutions (the judiciary, the police, the universities, the national/state assemblies etc).

VII. Summary and Conclusion

The paper has reviewed the concept of investment climate and the challenges and prospects of improving it in Nigeria. The challenges include the basic tension of spreading resources between social and economic infrastructure, restraining rent-seeking, fostering public trust and legitimacy and establishing credibility, among others. The prospects include the fact that Nigeria already has the necessary framework for an investment climate reform, improved investment climate would integrate informal firms into the formal economy, it would also integrate rural firms into the mainstream and unleash the growth potential of smaller firms. Based on these, some recommendations were made prominent among which are an upward review of the conditions of service of civil servants, the conduct of investment climate survey on a regular basis, making the firm the starting point of reform framework and the establishment of an industrial extension team.

Investment climate is key to growth and poverty reduction. Government policies and behaviours shape investment climate and in the process play out over a wide field, from contract enforcement and business regulation to the provision of infrastructure and labour market policy. No country has a perfect investment climate neither is perfection a prerequisite for reaping the fruits of investment climate. Nigeria already has the framework but the method still appears reactive and irregular. Nigeria has initiated several reforms and investment climate reform should be part of the whole reform programme. What it takes is to make the firm the starting point of the reform programme, conduct investment climate surveys regularly and base government industrial policies on the results of such surveys. Micro evidence has advantages over macro indicators but more work and discipline is demanded of the government and its officials.

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