GLOBAL ECONOMIC MELTDOWN AND THE NIGERIAN ECONOMY

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Abstract

The paper examines the global meltdown and its impact on the Nigerian economy. Through a historical excursion, it shows how the causes of the Great Depression and the current crisis are related. It situates the meltdown in the way America has tried to assert its hegemony in the global politics. This has resulted in the building of military complexes, the neglect of its productive and competitive sectors and its inability to meet its financial and trade obligations to the rest of the world. Other identified causes are the housing bubble and predatory lending by its financial giants. The crisis has inflicted so much harm on the Nigerian economy by resulting in reduction in foreign investment in the country, a fall in the value of the naira and a decline in government revenue and expenditure due to a fall in crude oil price among others. The paper therefore recommends some of the steps Nigeria should take to counteract the impacts as well as protect the economy from the measures taken by the developed countries to cushion their economies against the meltdown. Among its recommendations include the need to rely less on the advice of Bretton Woods Institutions and on the international currency exchange reserve system.

Key words: Economic meltdown, Globalization, Economy, Bretton Woods Institutes, Nigeria

Introduction

For the first time in recent years, the Nigerian economy, all through the last quarter of 2008 and first quarter of 2009, found itself engulfed in a vortex of local and external developments that created uncertainty and scars in their trail. Out of the blues came the global financial meltdown, marked by the collapse of hitherto revered and great financial institutions in major industrialized regions of the world. This has since transformed into a global economic crisis, with telling ripple effects in varying degrees on virtually all countries across the globe. Concomitant to this was a sharp and massive fall in the price of commodities, especially crude oil - the near–single foreign exchange earner for Nigeria. Consequently, the term economic meltdown (or downturn or crisis) has come to occupy a central place in global discourse in recent times. So what is it all about? How did it come about? How has it affected Nigeria? What does it portend for the country and what needs to be done? These and many more are pertinent questions that crave for answers. We will organize our responses by looking at the meaning of economic meltdown (crisis) in section two. Section three examines how economic crisis come about with emphasis on the current global economic meltdown. In section four we examine the impacts of the meltdown on Nigeria. Section five is our recommendations followed by some concluding remarks in section six.

Meaning of Economic Meltdown

In the simplest term, economic meltdown (or crisis) could be called economic ñgo-slowò which literarily makes an economy to recede as demand becomes sluggish, real output falling and unemployment rising. A recession is usually identified when real Gross Domestic Product (GDP) falls for two successive quarters (Black, 1997). During such period(s), there is scarcity of investible resources and inability of consumption to keep pace with production. There is also rising cost of production, a decline in investment and employment, a fall in the level of profits and strains in the stock market as well as in the banking system (Ohale and Onyema, 2001). If the economy experiencing the above is the largest in the world, the effects of its conditions will boomerang as the rest of the world catches cold. The crisis assumes a global proportion and hence the term global economic meltdown or crisis.

Origin of Economic Meltdown

The phenomenon of boom-burst-boom has been part of the history of human existence. Indeed it is an integral part of a market (capitalist) economy. Such periods of extreme prosperity and periods of major constriction are somewhat considered as normal behaviour of a market. From historical evidence, the economic crisis usually commences by rocking the financial sector and then ramifying to engulf the other sectors. The dominant position of America in the world economy has made it the source of major recessions in the global economy. For instance in October 1929, the first major depression in the history of the world occurred when the New York Exchange crashed. It has since been dubbed the Great Depression.

The Great Depression was an economic slump in North American, Europe and other industrialized areas of the world that began in 1929 and lasted until about 1939. It was the longest and most severe depression ever experienced by the industrialized Western world. Though the U.S economy had gone into recession six months earlier, the Great Depression may be said to have begun with a catastrophic collapse of stock market price on the New York Stock Exchange in October 1929. During the next three years stock prices in the United State continued to fall until late 1932 when they dropped to only about 205 of their value in 1929. Besides ruining thousands of individual investors, this precipitous decline in the value of assets greatly strained banks and other financial institutions, particularly those holding stocks in their portfolios. Many banks were consequently forced into insolvency. By 1933, 11,000 of the United States 25,000 banks failed. The failure of so many banks, combined with a general loss of confidence in the economy led to much reduced levels of spending and demand and hence of production, thus aggravating the downward spiral. The result was a drastic fall in output and a sharp rise in unemployment.

The Great Depression which began in the United States quickly turned into a worldwide economic slump owing to the special and intimate relationships that had been forged between the United States and European economies after World War I. The United States has emerged from the war as the major creditor and financer of postwar Europe, whose national economies have been greatly weakened by the war itself, by war debts, and, in the case of Germany and other defeated nations, by the need to pay war reparations. So once the American economy slumped and American investment credits to Europe dried up, prosperity tended to collapse there as well. The Depression hit hardest on Britain and Germany because they were heavily indebted to the U.S. In Germany, unemployment rose sharply beginning in late 1929 and by early 1932 it had reached 25% of the work force. Britain was less severely affected, but its industrial and export sectors remained seriously depressed until World War II. Many other countries were affected by the slump.

Almost all nations sought to protect their domestic production by imposing tariffs, raising existing ones, and setting quotas on foreign imports. The effect of these restrictive or protective measures was to greatly reduce the volume of international trade. By 1932, the total value of world trade had fallen by more than half as country after country took measures against the importation of foreign goods. This turned out to be a counterproductive measure.

At least in part, the Great Depression was caused by underlying weaknesses and imbalance within the U.S capitalist economy that had been obscured by the boom psychology and euphoria of the 1920s. The Depression exposed those weaknesses, as it did the inability of the American political and financial institutions to cope with the vicious downward economic cycle that had set in by 1930. Prior to the Great Depression, government traditionally took little or no action in time of business downturn but relied instead on impersonal market forces to achieve the necessary economic equilibrium. But market forces alone proved unable to achieve the desired recovery in the early years of the Great Depression, and this painful discovery eventually inspired some fundamental changes in United Statesô economic structure. After the Great Depression, government action, whether in the form of taxation, industrial regulation, public works, social insurance, social-welfare services, or deficit spending, came to assume a principal role in ensuring economic stability in most nations running market economies.

America again is at the center of the current economic meltdown. Available evidence shows that there are both remote and immediate causes of the present economic down turn in the globe.

Remote Causes of Economic Meltdown

There have been a lot of paternalistic platitudes and complicated jargons being passed around as reasons for the downturn in major industrial countries which in turn has affected the world. These are largely deceptive. The economic crisis largely has its origin in the emphasis by these countries, particularly the USA, in building and maintaining large but economically unproductive and expensive military complexes with which they have waged needless and unjustified wars around the globe. In pursuit of this, they have had to sacrifice the productive and competitive sectors of their economies. As American lagged behind competitively in economic production, so also is the deficit in its trade with the rest of the world which has come to rely on American market and the American dollar. For long the assumption was that being the most powerful economy in the world, America could print its way out of any economic problem. This hubris was given added fillip after the collapse of the Soviet Empire with a massive surge in American military production. Just as the American thought that it could print its way out of any economic deficit so also did the American leadership think America could bomb its way out of any dissenting views against its conduct in world affairs. For long, economists have cautioned about the overemphasis on military production at the expenses of more productive sectors where it has competitive edge. This made America less and less able to produce and compete in the world trade market which affected its ability to meet its financial and trade obligation to the rest of the World. It is the flipside of this dysfunctional economic emphasis that America and the rest of the world are experiencing today.

Immediate Causes of Economic Meltdown

The immediate causes of the current financial turbulence could be traced to the housing bubble, fueled by low interest rates, increased global liquidity and predatory lending by financial giants. In fact the saying ñEnjoy today and pay tomorrowò led most Americans into utilizing credit and gradually they started living above their means. Eberonwu (2009) states that ñthere is near unanimity that the current global economic imbroglio has its roots from the mortgage market crisis in the US which was riddled by óSubprimeô loans (Subprime loans are loans given out even when the borrower has not passed the necessary credit checks). This led to a lot of foreclosures and put strains on financial institutions which suddenly found themselves having a lot of real estate properties in their balance sheet. Prior to this, economic activity had been showing signs of decelerating even before the disruption in the credit and financial markets. While it is true that housing bubble is the primary source of weakness, the slow down in economic activity also started to spread beyond the housing sector. One of the main reasons behind the recent negative growth experienced by the US economy is the abrupt decline in the expansion of consumer spending, mounting job loses, fear of further economic meltdown and reduced access to credit. All these cumulatively compounded an already worse situation and hastened the occurrence of the recession. Other factors are greed. People were lured into acquiring life luxuries which their economic status would otherwise ill afford. Americans were living above their means. To worsen the situation, the Republican government of the day was not making things any easier. The government chose to fight a senseless war in Iraq that was costing the tax payers of United States whopping $1billion per day. No wonder President Barack Obama put most of the blame for the meltdown on the misguided policies of the past administration. The past administrationôs monetary policies allegedly encouraged speculative exuberance even as interest rates were at all time low and asset prices were spiraling out of control.

The big rating agencies also share part of the blame as they failed to be more rigorous in their risk assessment. Another contributory factor is the repeal of the Glass-Steagall Act (GSA) 1933, which had made a clear demarcation between general commercial banking on the one hand and investment banking activities on the other. The absence of such demarcation is underlined as one of the factors accounting from the speculative exuberance that led to the 1929 Wall Street crash and the current economic meltdown.

The Impact of the Global Economic Crisis on Nigeria

The current global economic crisis (meltdown), as we have shown, started in US with the melting of its financial system. This meltdown quickly reverberated across the globe. The Americans nay the developed world saw this meltdown early in 2008. They accepted the imperatives and the structural implications and immediately started taking bi-partisan actions to minimize its impact on their people and their economy. So apart from the direct impact the meltdown has on Nigeria and other developing countries, there are also the implications of the measures they are taking to cushion the consequences of their collapsing financial and industrial systems on us. Most Nigerians got the effect of the global financial crisis when the Nigerian Stock Market started to record massive losses in the value of shares of quoted companies. In 2008, the Nigerian Stock Exchange lost about N556 billion when foreign nationals who invested in the country pulled out their money from Nigeria due to the financial meltdown in their countries. Apart from the colossal losses by investors in the Nigerian Stock Market, the present economic crisis has also affected the country in the following areas.

1 Reduced portfolio investment; there is a reduction in foreign portfolio investments due to withdrawal and withholding of investment in order to service financial crisis at home (NSE All-share index went down by 38% by October 2008) as well as a reduction in foreign direct investment which affected investorsô confidence in Nigeria. This development has negative effect on the present Public Private Partnership (PPP) being used by the government to carry out project in power generation, rail, housing and road construction.

2 A drastic reduction in lending from financial institutions for businesses requiring short and long-term fund as well as inter bank lending. It is also now very difficult for businessmen to secure fresh loan from banks due to fear of inability of borrowers to repay such loans.

3 Declining infrastructural development.

4 Continuing decline of crude oil price which went down from the peak of US $148 per barrel in July 2008 to about US $48 per barrel. The Nigerian monocultural economy is badly hit by this development. Coupled with this is the reduction in the energy needs by the major buyers of Nigeriaĝs oil like USA as well as the interest in alternative energy source (wind, solar, bio-fuels) in developed countries. These led to the loss of billions of dollars in oil revenue and a reduction in government obligation to its people and infrastructural development. Table one shows that the

total statutory allocation to State and Local Governments declined from N128.5 billion and N68.5 billion in August 2008 to N69.6 billion and N36.6 billion in March 2009. These represent about 45.6% and 44.7% decline in States and local government revenue allocation respectively.

5 Depreciation of the naira; the Nigerian currency also sharply depreciated against the US dollar and other major currencies of the world. The fall in oil price put pressure on external reserves which further led to the depreciation of the naira.

6 Salary cut of public workers. The fall in the price of oil and the consequent reduction in the revenue earnings of the country also affected the revenue base of the central government and promoted a cut in the salary of public workers in the country.

Table 1: Summary of Statutory Allocation to States and Local Governments Council (August 2008 – March 2009 in N billion)

MONTH	TOTAL ALLOCATION TO STATES (N BILLION)	TOTAL ALLOCATION TO LOCAL GOVERNMENT	TOTAL ALLOCATION TO STATES AND LGAS
August 2008	128.5	68.5	194.4
Sept. 2008	115.7	61.0	174.3
Oct. 2008	109.6	58.7	159.9
Nov. 2008	101.0	55.1	147.5
Dec. 2008	109.9	57.3	158.5
Jan. 2009	101.9	54.8	147.9
Feb. 2009	73.3	40.1	104.8
March 2009	69.6	37.6	98.9

Source: *Revenue Allocation & Fiscal Commission; Abuja 2009*

America, Britain, France and Germany etc have evolved measures to cushion the consequences of their collapsing financial and industrial systems. Each of these governments is on record to have pledged billions of dollars to save banks and financial institutions from collapse. They also adopted far reaching measures including massive public works and infrastructural programs designed to create jobs and bring down unemployment in their countries. This prompts the question of where the money to fund all these programs will come from? It should be noted that even before the coming of the current global economic downturn, the economies of these countries were already running deficits collectively amounting to trillions of dollars. In the light of this, where did the additional money come from? Significantly, in the fundamental shift from economic philosophy and policy, government of these countries constituted themselves into economic war cabinets to directly prosecute the economic recovery programs rather than allow market forces to do the job. There can be no doubt that the massive bail out money needed to save the financial institutions and fund the stimulus package came from sources outside these countries. Already each of these countries tinkered with their monetary policies to achieve this goal. There is cuts in interest rates designed first to devalue foreign money held in the accounts of banks and secondly to lure yet more foreign money into their financial trap. Countries like Nigeria which have neither the industrial nor financial power felt the negative effects of these policies pursued by America, Britain and others. In the short term as a consequence of these policies, the value of our foreign reserves held and denominated in foreign currencies and banks have been on a free fall. The naira has continued to fall against major currencies while the prices of our export commodities particularly crude have been on a downward spiral.

The falling source of revenue is already been felt in the country with the looming massive cutback in government commitment to social goals. This has exacerbated social and political tensions in our fractious and fragile polity. Also in the long run as these countries try to shift emphasis from hydrocarbon to other energy sources, oil producers like Nigeria will certainly be left in the lurch. Not only will our income from oil become less and less but we will be compelled to source our energy requirement from the alternative energy sources developed by these countries with all the financial, economic and strategic implications to our country. We must resoundingly reject this grim and cruel fate being designed on the world by these countries.

Recommendations

Although the current crisis ravaging the global financial system is essentially economic in nature, the solution to them lies in the political realm. Hence faced with this tasking economic crisis, the Government of US, Britain, France etc have constituted themselves into an economic war cabinet not only to directly take over and manage their economies but also to set the stage for fundamental political paradigm shift to cope with looming political challenges. In United States spectacularly, this led to the emergence of Barack Obama with all symbolic hope he portends for the future of that country to re-discover America politically, economically and racially. Indeed as history teaches us periods of great economic challenges usually serve as opportunity to reset the clock of development. In this wise the economic cloud hanging over Nigeria also contains political silver lining which we as a people and nation must grab to make Nigeria a great nation. It should serve as the catalyst we need to energize our country for the greatness that we have long promised but failed to deliver. The road to this promise land must begin with a fundamental reordering of our economic engagement with the outside world. As a first step in this regard, we must consider seriously whether it will serve our long term economic interest to continue to engage wholesale the ideas and programmes of the Bretton Woods Institutions. Are the IMF and World Bank themselves not tainted by the crisis engulfing their principals? For the sponsor countries of these institutions have themselves proven to be inefficient managers of their economies. What rationale can there be for countries like ours to continue to accept economic advice from them? For there can be no question that the basis of enjoying economic seignorage by the IMF and World Bank and their principals have been laid hollow by the current economic downturn. It is all clear to see that Emperor has no clothes on and that indeed, his feet are of clay.

Secondly and critically, in the depressive economic situation such as we are now, we much rely less on the international currency exchange reserve system which has now all but collapsed, as a determinant of earnings. Money held in a reserve system that has no guarantee of solidity is at best a phantom. Instead we must place more emphasis on getting value for our resources and market potential through long term industrial development and market partnership with countries. Our position as regional market center in Africa should be fully tapped in this regard. The imperative of Nigeria to the world as the most populous black nation on earth endowed with more human and material resource potential than Britain, France, Germany and Italy put together, is to aim to be among the key nation helping to shape the coming global order. We are justified to play this role not only on the strength of our population size and resources, but more importantly on account of our divine ordination as the leader and spokesman of the worldôs people of African descent wherever they may exist. No other nation of the world is more favourable positioned to play this role than Nigeria. Thus when Nigeria speaks and acts, it should and must be on behalf of black people be they on the mother continent of Africa or in the Diaspora. Nigeria must hasten to acquire the necessary economic, political and diplomatic status to be able to do this. There can be no opportuned time to pursue this noble task than now as the world goes into flux. The decline levels of our infrastructure need to be urgently addressed. Government should in no distant time put up measures to improve power supply, road construction and provide effective transport system in order to stimulate investment, employment and growth in the country.

Finally, we have to review our value system. Corruption that has eaten deep into our lives has been attributed to our poor value system. The celebration of leaders and public officials that loot the public treasury has to be stopped. Also election of leaders to various political offices in the country has to be on merit and not on ethnicity, religion or other sentiments. The reorientation of Nigerians and a strict enforcement of severe sanctions to defaulters will help curb corruption and waste that characterize our present national life.

Concluding Remarks

We have to confess that we are not easily taken in by the report attributed to top government officials which declare our economy to be the safest in the world. As far as we know, our alleged safety derives from the paradox of marginality - to the simple fact that we are not deeply hooked in the global digital economy. It is fool hardy to behave like the proverbial ostrich when Rome is on fire and when the embers of financial contagion have been unleashed everywhere. We are constrained to note that we are yet to see a clear economic strategy around to anchor rational expectations and mobilize vast resources and energies of our people. Our leaders have all but forgotten the onerous task of nation building. The simple truth is that we are not yet a nation and we are far from having that spiritual bond and values which the British political philosophers, Sir Ernest Baker regarded as the most critical factor in the building of a united and prosperous country. Clearly, we have enormous work to do and several steep mountains to climb. At the global level, we would need to work with others to hammer out a brave new world in which the demands for equity harmonize with the imperatives of international solidarity.

For us in this benighted country, the current economic upheaval provides an opportunity to re-invent the country and to consolidate the foundations of democracy that would enhance peaceful and just development for our long-suffering people. After a millennium of hopelessness, our country may at last be coming to its own. Its foundations must be built on a sound public management. But we daresay that will not rise to the occasion until we have transformed our national mindset, reformed the way we do business and changed the structure of our politics and the very spirit of our constitution, leadership and nationhood.

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