Financial Institutions' Operations & Capital Flight In Nigeria

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Abstract- *This study examines the impact of Financial Institution variables and operations on the level of capital flight in Nigeria for a period of forty two years. The financial institutions globally are expected to perform certain fundamental functions that are believed to the prerequisites for economic growth and stability. Required secondary data were sourced from the Central Bank of Nigeria statistical bulletin, the Nigeria Stock Exchange fact books and IMF financial reports while the Ordinary Least Square Method of Regression analysis and Co-integration Technique were employed to estimate and test the impact of selected economic and financial institutions' variables such as the prevailing Deposit Rate, Private Sector Credit, Change in Net Foreign Asset of Domestic Financial Institutions, Inflation Rate, Gross Capital Formation and Nigeria and U. S interest rate differentials on the level of capital outflow from Nigeria. With the World Bank and Erbe (1985) capital flight estimate, the findings reveal that all the explanatory variables are significance in explaining the behavior of capital. The results also show that each of the explanatory variables has specific impact on the dependent variable. Specifically,   high inflation rate induces capital flight, increase Gross Capital Formation (LGCF) reduces capital flight, and appreciable deposit rate on bank deposit encourages domestic savings while the Credit to Private sector has not brought about the desire expectation of improving and sustaining the domestic economy. The study recommends that government should provide an enabling environment that will enhance the ability of the financial institutions to perform their functions effectively and the private individuals to invest in the domestic economy profitably. While financial institutions managers and operators should adhere to the sound ethical practices and desist from shape practices that encourage illegal transferring of money.*

Keywords: *Financial Institutions; Economic development; Capital outflow; Ethical behaviors; financial operations*

1. INTRODUCTION

The banking system in any economy plays the important role of promoting economic growth and development through the process of financial intermediation. Development economists argue that the existence and evolution of financial institutions and markets constitute an important element in the process of economic growth. The banking system, in promoting economic growth, plays the following roles such as improving the efficiency of resource mobilization by pooling individual savings; Increasing the proportion of societal resources devoted to interest yielding assets and long-term investments, reducing the risk faced by firms in their production processes by providing liquidity and capital as well as enabling investors to improve their portfolio diversification by providing insurance and project monitoring. Thus, how well the financial institutions perform their expected roles will to a large extent determine the movement of capital among nations and as such affect the economic development of such nations.

Cuddingtom, 1987 asserts that the reasons for capital flight in developing countries include: level of risks and uncertainty, exchange rate misalignment, financial sector constraints, fiscal deficits and external incentives and external borrowing among others.

The bank deposit approach to capital flight define capital flight as the resident capital outflows which involves measuring the increase in recorded foreign bank deposits of a country's residents. Although this is a controversial measure since even if there are statistical sources which distinguish between official and private holdings; it cannot be argued convincingly that all private funds held abroad are recorded by the relevant authorities. Specifically, the difficulties in compiling the bank deposits data is compounded by the fact that some funds are deposited in bank which are not reported to the IMF or other relevant authorities while others may be held in non-bank foreign assets. Again, the depositors desire to conceal their nationality in order to minimize any potential risk they may perceive is another challenge. Consequently, foreign bank deposits owned by a country's residents are likely to under estimate resident capital outflows.

The Morgan Trust (1986) version of the residual a for estimating capital flight suggests that the balance of payments accounts is not sufficient to estimate resident

capital outflows, hence the need to adjusts the World Bank (1985) measure for changes in foreign assets held by domestic residents other than the banking system so as to reflect the increase in foreign assets of the Domestic Banking System. A significant increase in foreign assets of domestic banking system is an indication of capital outflow of capital which could have otherwise be used to develop the home economy to foreign economy. Thus the activities and operations of a country's financial institutions are expected to impact the level of capital flight. The study is set out primarily to examine how financial institution variables and operations impact capital flight as individual and

 as a whole

2. LITERATURE REVIEW

There has been rapid growth and mobility of international capital with some attendant risks and benefits to the World economic systems. One of such risks is that of fuelling capital flight. There exists no generally accepted definition of the term "capital flight". Most of   the time, this term is related to capital which is shifted out of developing countries. However, if capital shifts out of the developed country, it is usually referred to as capital outflow. Investors from developed countries are seen as responding to investment opportunities while investors from developing countries are said to be escaping the high risks they perceive at home (Ajayi, 1997). According to Cooper and Hardt (2000), capital flight entails the flow of financial assets resulting from the holder's perception that capital is subjected to inordinate level of risk due to devaluation, hyperinflation and/or political turmoil. The owners of funds in such hostile environment are seeking a safe haven for their funds. Ndikumana and Boyce (2003) defined capital flight as residents' capital out flows, excluding recorded investment abroad. It is important to note that when capital flows from a developed to a developing country it is not considered as capital flight. Also when capital flows a developing to developed countries through legal means and for investment purposes it is also not considered as capital flight. However, when capital flows from a developing to a developed country through illegal means it is capital flight. It is very difficult to measure illegal flows; however, the major means of measuring capital flight in this study is the difference between the sources and uses of funds. The main sources of capital to an economy are external borrowing and direct foreign investment while the uses of funds include financing of current account balance and external reserves, this difference constitute capital flight.

Basis for Capital Flight

Various issues have been identified as the basis or motivation for capital flight; some of these are briefly discussed below:

Investment Climate

A poor domestic   investment climate will affect the returns of domestic held assets while a good and favourable domestic environment will boost the returns on dometically held assets. A favourable domestic investment climate   will encourage capital inflows and a poor domestic investment enmvironment will encourage capital outflows. Various factors in turn affect the condition of the domestic environment. These include (Ali and Bernard Walters, 2011)

i. **Risks and Return Features-** The relative riskiness and profitability of domestic investments will determine whether or not capital will flow in or out of an economy. In decision making process, the wealth holder looks at the various risks confronting him. There are certain inherent characteristics of developing countries which make risks attached to investments larger than those of developed countries. An increase in risk in a rational expectation setting would tend to increase the outflow of private capital from the domestic economy into foreign countries where investment is less risky. Thus, domestic investors will prefer to transfer funds and hold foreign assets (Hermes andLensiink, 2001; Cerra *et al*, 2008).

ii. **Policy Distortions-** The specific macroeconomic policies a country pursues will directly affect the domestic climate. Macroeconomic instability such as high and volatile inflation rate will erode the real value of domestic assets and this will result in lower economic growth and lower returns to the investors. Apart from this currency, overvaluation has also been suggested as one important variable that is responsible for high rate of capital outflows from a country. This is because currency overvaluation will result in lower economic growth, higher probability of speculative attacks, increase current account deficits, shortage of foreign exchange, balance of payment crises and corruption flight (Frait *et al* 2006 , Rodic,2008).

iii. **Institutions and Political Instability-** Good quality financial institutions are very vital to ensure favourable domestic investment climate. The study of Acemoglu and Robinson 2001, Acemoglu *et al* 2005 show that institutions directly affect whether investors will engage in productive investments or not. Hence, the decision to invest locally or not depends on the availability or otherwise of investment-friendly financial institutions in the economy (North,1990).

iv. **Exchange Rate Misalignment-** The importance of this variable has amply been demonstrated in several empirical analyses including the studies by Dornbusch (1985), Cuddington (1986), Lessard and Williamson (1987) and Pastor (1989, 1990). The real exchange rate plays a significant role in the direction and magnitude of capital flight from highly-indebted developing countries. Under normal circumstances, if a currency appreciation is expected, domestic wealth owners would shift out of domestic assets into foreign assets. In general, it is difficult to measure precisely exchange rate expectations. It is safe, however, to assume that if a currency is overvalued, economic agents would expect the currency to be devalued in

the future. Holding firmly to this expectation would cause residents to avoid the potential capital loss by converting into foreign claims.

v. **Financial Sector Constraints-** It is well known that narrowness of the capital and money market is a feature of developing economies. Financial markets in these countries provide only a limited variety of financial instrument in which wealth can be held. There is also in many developing countries the lack of full or credible deposit insurance on assets that are held in the domestic banking sector. This deficiency is, however, being increasingly remedied by many developing countries. Additionally, there are extensive controls on interest rates and on other aspects of financial market behaviour in developing countries. Government policies in the financial sector have resulted in normal interest rates that are far below the rates on comparable foreign financial instruments. In most cases, the real rates of return on domestic financial assets are negative.

Financial Instability and Capital flight

Financial instability is often a consequence of fiscal deficits and exchange rate policies; it is a reflection of interest rate fixed below inflation rates, high legal reserve requirements of banks and the other institution imposed on financial systems by the monetary authority. Financial repression encouraged capital flight both by lowering returns on domestic investments and feeding overall financial instabilit (Adegbite and Ayadi, 2008).

In countries with more liberal financial systems such as market determined interest rates, large fiscal deficits and exchange rate over-valuation will result in high real domestic interest rates thus creating a different type of financial instability as firms and governments become highly indebted domestically. Domestic firms that hope to take advantage of relatively cheap foreign loan will t experience financial instability if corrective devaluations are implemented. Financial instability also activates what can be regarded as a secondary source of capital flight – the stock of assets held by residents abroad. Financial instability induced foreign asset holders to reinvest abroad the returns on their assets such as interest, dividends and capital gains. While policy distortions tend to have an immediate effect on capital flight, reversing them may only have positive results in the long run. In the short-run, trade and fiscal reforms may promote rather than reverse capital flight as they pose a threat to heavily protected sectors, privileged tax loopholes and tax evasion. However, a substantial reduction of fiscal imbalance could accelerate the beneficial effects of removing other policy distortions.

3. METHODOLOGY

The focus of this paper is set examine the effect of financial institutions on the level of capital flight from Nigeria between 1970 and 2011. The study is quantitative and empirical in nature; it employs the Ordinary Least Square Regression and Co-integration Analysis through an E-View econometric package to test short and long run relation between the dependent and independent variables. The residual approach of World Bank and Erbe (1985) for estimating capital flight was as the method of estimating capital flight.

3.1 Research Questions

The following research questions as stated in the introduction will be answered in the course of this study:

1. What are the impact of financial institution variables and operations on the level of capital flight in Nigeria?
2. What specific impact has each financial institution variable on the level of capital flight from Nigeria?

3.2 Hypotheses

In order to achieve the objectives and proffer solution to the research questions, the following two null hypotheses are formulated for testing

H_{01}: Financial Institution variables and operation has no significant impact on the level of capital flight from Nigeria.

H_{02}: An individual Financial Institution variable has no specific impact on the level of capital flight from Nigeria.

3.3 Model Specification

Based on the above questions and hypotheses and in line with the World Bank and Erbe (1985) version of the residual approach of capital flight estimate, the following model is built to be able to empirically arrive at valid conclusion. From the original model, capital flight is estimated as:

$$KF(WB) = \delta EDEBT + G + F - N \qquad (1)$$

Where:

KF (WB) = Capital Flight measured by the World Bank approach,

δ EDEBT = Changes in Reserve

G = Foreign Direct Investment

F = Current Account Balance

N = Change in External Debt.

A positive value of KF (WB) represents capital flight while a negative value is capital re-flows or the reverse capital flight. For the purpose of this article, the above model shall be modified as:

$$KFW = f(INF, GCF, DR, PRIVCR, USIRD, \delta NEXTAS, \mu) \qquad (2)$$

Where:

KFW = World Bank and Erbe (1985) capital flight estimate

INF = Inflation rate

GCF = Gross Capital Formation

DR = Deposit rate

PRIVCR = Credit to private sector

USIRD = USA and Nigeria interest rate differential

δNEXTAS = Change in foreign asset of domestic banking system

μ = Stochastic error term

F = Functional relationship between the dependent Variable (KFW) and the independent variables.
The World Bank approach is stated explicitly as below:

$$KFC = \delta_0 + \delta_{01}INF + \delta_{02}GCF + \delta_{03}DR + \delta_{04}PRIVCR + \delta_{05}USIRD + \delta_{06}NESTAS \quad (3)$$

Where δ_0 = intercept of the equation, By log-linearising the model, it becomes

$$LogKFW = \delta_0 + \delta_{01Log} + \delta_{02Log}GCF + \delta_{03Log}DR + \delta_{04Log}PRIVCR + \delta_{05Log}USIRD + \delta_{06Log}NESTAS \quad (4)$$

Where: Log = Natural Logarithm
$\delta_0, \delta_{01}, \delta_{02}, \delta_{03}, \delta_{04}, \delta_{05}, \delta_{06}$ Coefficient of estimates
μ = Error term

3.4   Description of Variables

Below are short descriptions of the various variables adopted in this the study:

Inflation Rate (INF) – Inflation is the persistent increase in prices of goods and services. This is a control variable that is used to measure the cause of capital flight in Nigeria.it is an economic situation whereby money chases fewer goods.

Deposit Rate (DR) - Deposit may be in form of cash, cheque or valuables. Deposit rate refers to the minimum rates that can be paid on savings and   time deposits at commercial banks, mutual savings banks, loan association and credit unions.

Credit To Private Sector (PRIVCR)– This are funds given by government to the organised private sector through the commercial banks or any other financial institution saddled with the responsibility of intermidiating between the suplus and the deficit units in Nigeria economy.

Increase In Foreign Asset Of Domestic Banking System (δNEXTAS) – These are assets of domestic banks in another country, this is in form of investments of a bank in another country other than its own country. This investment can be in real assets or financial securities abroad. This variable measures the modification of World bank (1985) and Erbe (1985) by Morgan (1986).

Capital Flight (KF) - The term capital flight as used in this study connotes illegal movement of capital or funds from one country to another usually from developing countries to developed countries. This connotation implies that there may be "normal" or "legal" and "abnormal" or "illegal" flows. This variable as used in the study is the estimate according to World bank (1985) and Erbe (1985).

Gross Capital Formation (Gross Domestic Investment): This is the total change in the value of fixed assets plus change in stocks.

United State of America Interest Rate Differential (USIRD): This is the difference between the interest rate of home economy (Nigeria) and that of U.S.A. The United State of American Dollar is chosen because it is one of the most acceptable high currencies. It is expected that interest rate differential will encourage movement of capital from one economy to another.

3.5 Nature and Sources of Data

For the purpose of this study, time series data were used. These data were sourced through secondary sources from institutions like the Central Bank of Nigeria (CBN), Federal Office of Statistics (FOS), World Bank Statistical Information, World Debt Tables, IMF International Financial Statistics, the United State Federal Reserve and other sources of already processed data that are relevant to the study.

4. RESULTS AND DISCUSSION

Presented below are the results of the Ordinary Least Square (OLS) method of regression analysis, Co-integration and Error Correction Mechanism test. These methods are employed to test the short and long run analysis of the time series data.

Table 4.1 Presentation and Discussion of Short run Results for the Model

Table 4.1 shows the summary of the short-run analysis, test of significance of the explanatory variables and the test of hypothesis for the model which shows the determinant of capital flight using the World Bank and Erbe (1985) estimation approach.

Table 4.1 Presentation and Discussion of Short run Results for the Model (Dependent Variable = KF)

VARIABLES	COEFFICIENT	T-cal.	T-tab.	H_0	H_1	REMARK
CONSTANT	4.003915	0.562194	2.042	REJECT	ACCEPT	Significant
LINF	0.152967	1.138511	2.042	REJECT	ACCEPT	Not Significant
LGCF	-0.072801	-1.133815	2.042	ACCEPT	REJECT	Not Significant
LDR	-0.352330	-1.974098	2.042	ACCEPT	REJECT	Not Significant
LPRIVCR	0.670381	7.367379	2.042	REJECT	ACCEPT	Significant
LSUIRD	-0.016127	-0.146066	2.042	ACCEPT	REJECT	Not Significant
LδNEXTAS	0.287619	3.537076	2.042	REJECT	ACCEPT	Significant

R^2 = 0.9695 **Adj R^2** = 0.9643 **F-cal = 185.7603, Prob. of F- statistics- 0.00000, D-Watson** = 1.5166

Source: Computation, using E-view statistical package

From the table, the variable is significant in the model if the value of T-calculated is greater than the value of T-tabulated.

Validation and testing of hypotheses: The hypothesis to be tested in this model is stated in the null form as follows;

H_{01}: Financial Institution variables and operation has no significant impact on the level of capital flight from Nigeria.

H_{02}: An individual Financial Institution variable has no specific impact on the level of capital flight from Nigeria.

The results in table 4.1 show that Private Sector Credit (PRIVCR), Increase in Foreign Asset of Domestic Banking System (δNEXTAS) and the constant variable are positively related and statistically significant in the model. This shows that these variables are the main financial institution variables that influence the volume of capital out flow from Nigeria to other countries in the short run. Rather than reducing the incidence of capital flight, these variables promote capital flight in Nigeria. The alternative hypothesis is accepted for these variables while the null is accepted for The Inflation Rate (INF), Gross Capital Formation, (GCF), Deposit Rate (DR) and United State and Nigeria interest rate differential (USIRD). The Inflation Rate (INF) is also positively related showing that increase in inflation rate will result to increase capital flight. The Gross Capital Formation, (GCF), Deposit Rate (DR) and United State and Nigeria interest rate differential (USIRD) are positively related to the level of capital flight. This implies that increase in these variables will lead to reduction in the volume of capital flight. All the variables are appropriately signed with the exception of Private Sector Credit (PRIVCR) which is expected to be negatively with capital flight. When financial institutions give out credit to the private sectors, such credits are expected to be invested in the real sectors of the domestic economy. If on the other hand, the domestic environment is not investment friendly, the private sectors/the domestic investors will move such credits and businesses to investment friendly economies where the level of uncertainties is reduced.

TABLE 4.2 Presentation of Cointegration Test for the formulated Model

WORLD BANK AND ERBE (1985) APPROACH				
Hypothesis	**Eigen Value**	**Trace Statistics**	**5%Critical value**	**1%Critical Value**
None**	0.791745	206.1059	124.24	133.57
At most 1**	0.769127	143.3462	94.15	103.18
At most 2	0.578613	84.71076	68.52	76.07
At most 3	0.385607	50.14265	47.21	54..46
At most 4	0.377778	30.65785	29.68	35.65
At most 5	0.236867	11.67950	15.41	20.04
At most 6	0.021431	0.866553	3.76	6.65

*(**) denotes rejection of the hypothesis at the 5%(1%) level

Trace test indicates 5 cointegrating equation(s) at the 5% level

Trace test indicates 3 cointegrating equation(s) at the 1% level

The Cointegration equations for the two approaches are stated below:

$$KFW = 2.403695_{LINF} - 1.344484_{LGCF} - 1.315171_{LDR} + 0.645387_{LPRIVCR} + 0.385139_{LUSIRD} - 0.69101_{LGOCE}$$

The table above shows that a long run equilibrium relationship exist in the Model as likelihood ratios (Trace Statistics) of 206.1059 is greater than 5 per cent critical values of 124.24 at None hypothesized (None**) respectively. In all, there are five cointegrated equation in the model.

4.1 Error Correction Test for the Model

The table shows the over parameterized and parsimonious ECM for the model.

Tables 4.3 Over-Parameterized & Parsimonious ECM

These tables show the over parameterized and parsimonious ECM for model 1.

Over-Parameterized Model (ECM1)

Dependent Variable: D(LKF,2)

Method: Least Squares

Sample(adjusted): 1973 2011

Included observations: 39 after adjusting endpoints

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(LKF(-1),2)	0.101832	0.268578	0.379150	0.7078
D(LINF,2)	-0.089693	0.097212	-0.922655	0.3650
D(LINF(-1),2)	0.133597	0.100520	1.329056	0.1958
D(LGCF,2)	-0.052749	0.033203	-1.588685	0.1247
D(LGCF(-1),2)	-0.084187	0.037171	-2.264873	0.0324
D(LDR,2)	-0.340807	0.447268	-0.761975	0.4532
D(LDR(-1),2)	-0.937113	0.475152	-1.972237	0.0597
D(LPRIVCR,2)	0.629569	0.617427	1.019665	0.3177
D(LPRIVCR(-1),2)	0.340719	0.588477	0.578984	0.5678
D(LUSIRD,2)	0.052363	0.094231	0.555684	0.5834
D(LUSIRD(-1),2)	-0.116661	0.093959	-1.241608	0.2259
D(LNEXTAS,2)	0.297809	0.059346	5.018143	0.0000
D(LNEXTAS(-1),2)	0.142411	0.052221	2.727079	0.0115
ECM(-1)	-1.056276	0.312339	-3.381832	0.0024

R-squared = 0.705495

Mean dependent var = 0.096346

Adjusted R-squared = 0.552353

S.D. dependent var = 0.777161

S.E. of regression = 0.519971

Akaike info criterion = 1.803176

Sum squared resid = 6.759249

Schwarz criterion = 2.400352

Log likelihood = -21.16193

Durbin-Watson stat = 1.571097

Parsimonious Model (ECM2)

Dependent Variable: D(LKF(-1),2)

Method: Least Squares

Sample(adjusted): 1973 2011

Included observations: 39 after adjusting endpoints

Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(LINF(-1),2)	-0.079727	0.063585	-1.253863	0.2190
D(LGCF(-1),2)	0.035940	0.020496	1.753532	0.0891
D(LDR(-1),2)	0.367844	0.262114	1.403373	0.1701
D(LPRIVCR,2)	-0.017082	0.409705	-0.041692	0.9670
D(LUSIRD(-1),2)	0.155417	0.056241	2.763402	0.0094
D(LNEXTAS,2)	-0.104823	0.030524	-3.434119	0.0017
ECM(-1)	0.052575	0.212904	0.246940	0.8065

R-squared = 0.456667

Mean dependent var = -0.003096

Adjusted R-squared = 0.354791

S.D. dependent var = 0.492563

S.E. of regression = 0.395651

Akaike info criterion = 1.144580

Sum squared resid = 5.009269

Schwarz criterion = 1.443168

Log likelihood = -15.31931

Durbin-Watson stat = 2.522469

Source: Computation, using E-view statistical package.

The tables above show the overparameterised ECM (ECM1) and parsimonious ECM (ECM2) for the formulated model. The negative sign in the value of ECM1 shows that the ECM is significant. This implies that the present value of KF adjust rapidly to change in DOP, INF, GCF, δEXDEBT, DR, PRIVCR. The ECM value of --1.056276 in ECM 1 shows a feedback of the value from the previous period disequilibrium of the present level of KF in the determination of causality between the past level of capital flight (LKF) and the present and past level of LINF, LGCF, LDR, LPRIVCR, LUSIRD and LNEXTAS. The coefficient of multiple determinations (R^2) of 0.705495 (about 71%) shows that about 71% in KF can be explained by the independent variables while the remaining 29% is explained by stochastic variables. The Durbin Watson statistics of above 2 (Durbin-Watson

Statistics, 2.522469) shows the absence of autocorrelation in the model.

Presentation of Long Results and test of Significant of Parameters for the Model

The test for the significant of the parameters is done using the standard error test. For a parameter to be significant, the coefficient of the parameter divided by 2 must be greater than the standard error from the Cointegration equation.

Table 4.4 Test of significance of variables

Table **4.4** shows the result of standard error test conducted on the parameter.

WORLD BANK AND ERBE (1985) APPROACH				
Variable	**Coeff.**	**Std. Error**	**Coeff./2**	**Remarks**
LINF	2.403695	0.31365	1.2018475	Significant
LGCF	1.344484	0.17317	0.672242	Significant
LDR	1.315171	0.38642	0.6575855	Significant
PRIVCR	0.645387	0.25767	0.3226935	Significant
USIRD	0.385139	0.25316	0.1925695	Significant
LδNEXTAS	0.691015	0.23456	0.3455075	Significant

The table above shows that all the variables are significance in determining and explaining the behaviour of the dependent variable.

Validation and testing of hypotheses: The under listed hypotheses will be tested under the model:

The formulated hypothesis for long run relationship between the dependents and the dependent variable can be tested base on the above result. The stated hypothesis is:

1. H_{01}: Financial Institution variables and operation has no significant impact on the level of capital flight from Nigeria.

2. H_{02}: An individual Financial Institution variable has no specific impact on the level of capital flight from Nigeria

Since the analyses reveal that all the dependent variables are statistically significance in explaining the level of capital flight in Nigeria, the null hypothesis (H_0) is rejected for each of the explanatory variable while the alternative hypothesis (H_1) is accepted for each of the explanatory variable in the first hypothesis.

For the second hypothesis, the results show that the each of the explanatory variable has specific impact on the dependent variable (capital flight). In the short run analysis, the Gross Capital Formation (LGCF), Deposit rate (LDR) and the United State of America and the Nigeria interest rate differential (LUSIRD) are negative signed while the Inflation rate (LINF), the Credit to private sector (LPRIVCR) and the change in foreign asset of domestic banking system (δNEXTAS) are positively signed. This connotes that the negatively signed parameters have inverse relationship with the volume of capital flight in Nigeria. An increase in any or all of these variables will reduce the level of capital outflow from Nigeria. In the same vein, the positively signed variables

have direct and proportionate relationship with the dependent variables. An increase in any or all of these variables will lead to increase in the level of capital flight. Similar results with minimal deviation were obtained in the long run analysis. Specifically, the United State of America and the Nigeria interest rate differential (LUSIRD) that was negatively related with the dependent variable in the short run reveals a positive relation in the long run. This suggest that the wider the difference between the US dollar and the Nigeria naira, the higher the possibility of moving financial resources from the home economy to the developed economy where the value of money is perceived to be more stable. Again, the change in foreign asset of domestic banking system (δNEXTAS) was positively related with the level of capital flight in the shorty run but negatively related in the long run. The implication of this is that while the change in foreign asset of domestic banking system (δNEXTAS) was detrimental in the short run, it is beneficial in long run.

5. CONCLUSION

Findings from the above discussion reveal that Financial Institutions have a major role to play through their activities either in curbing or stimulating capital in Nigeria. This was demonstrated by the behaviours of the explanatory variables in relation to the dependent variable. The findings reveal that   high inflation rate induces capital flight, increase Gross Capital Formation (LGCF) reduces capital flight, appreciable deposit rate on bank deposit encourages domestic savers and as such reduces capital flight, Credit to Private sector has not brought about the desire expectation of improving and sustaining the domestic economy, the United State of America and the Nigeria interest rate differential (LUSIRD) propel capital outflow from the economy due to the deteriorating value of naira while and Deposits rate with capital flight ion this study. A high inflation rate cause's increase in capital flight while the change in foreign asset of domestic banking system (δNEXTAS) in the long run shows that the rate of illegal transferring of funds and assets by residents in the domestic economy through the financial institutions to foreign accounts abroad has marginally reduced.

6. RECOMMENDATIONS

Based on findings from the study, the following points were recommended:

1. Government should provide an enabling environment that will enhance the ability of the financial institutions to perform their functions effectively and the private individuals to invest in the domestic economy profitably.
2. Appropriate policies should be put in place by the government to address the major economic variables identified in this study to induce capital flight in Nigeria.
3. Since increase gross capital formation encourages domestic investment, government should increase the proportion of nation budget allocated to capital projects.
4. Financial institutions managers and operators should adhere to the sound ethical practices and desist from shape practices that encourage illegal transferring of money.
5. The ongoing financial institutions reforms and consolidation policies of the government should not be abandoned but pursue to logical conclusion. This will enable the Nigeria financial institutions to compete favorably at the international level as well as support the domestic economy in order to enhance rapid development.
6. Every sector of the Nigerian economy should be developed and exploited by the government and corporate institutions in order to widen and diversify the economic base of the economy. This will reduce the currency differential with the advanced economies, strengthens the naira and reduce the level of capital outflow.

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