**TITLE PAGE**


**FACTORS THAT REDUCE SAVINGS IN NIGERIA (1980-2010)**


**A PROJECT SUBMITTED TO THE DEPARTMENT OF ECONOMICS IN PARTIAL FULFILLMENT OF THE REQUIREMENT FOR THE BACHELOR OF SCIENCE (B.SC)**


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# APPROVAL PAGE

This project has been supervised and approved as having certified the requirement for the award of Bachelor of Science (B.Sc) in the Department of Economics, Caritas University, Amorji –Nike Enugu.


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## DEDICATION

This research project is dedicated to the Almighty God who has been my only source of strength and inspiration.

I also dedicate this work to my parents Mr. and Mrs. Ime akpan having sacrificed a lot to give me the best in life and for their encouragement, prayers and love during my years of study. It's also dedicated to my siblings: Abasifreke Anniediong and wisdom.

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With profound gratitude for their consistent advice, support and prayers.

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# ABSTRACT

This study investigates the core leading factors that reduce savings in Nigeria between 1980 -2010 using ordinary Least Square (OLS) econometric framework, which will enable us proffer solutions for the improvement of savings in the economy, which is also an important component for economic development in any country. Base on data collected, it is discovered that savings output in Nigeria during the period was unsatisfactory but was later discovered as a necessary factor for economic development and growth. This research shows the significance of savings which is achieved when saving habits is greatly considered by public private and government. The empirical results show a negative influence of trade openness (TDO) on aggregate savings. The work therefore submits that effort should be geared towards improving export capacity by improving productivity in industrial sector, which provide employment and increase per capital income as a bid to accelerate savings. And since interest rate signals a positive influence on savings in Nigeria, there should also be an intensified impact on real rates, spread and financial liberalization and or financial developing in Nigeria.

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**CHAPTER ONE**

## 1.0 INTRODUCTION

## 1.1 BACKGROUND OF THE STUDY

Financial institution, market, regulator and instrument all comprises a set of complex and closely interconnected financial system, proving financial services in an economy, such services includes mobilization and allocation of resources, distribution of investment funds among firms, financial intermediation and foreign exchange transactions.

The Nigeria financial system can be categorized into two via: the formal or organized and informal or unorganized financial system, the banks and non banks financial institutions make up the organized financial system while the unorganized sector comprises of indigenous bankers local money lenders' (ISUSU), shop-keepers or traders, merchants, landlords, saving associations, friends and relatives etc. the system is poorly developed, limited economics information, defective system of according are not integrated into the formal financial system, but very important to the Nigerian financial system. Capital formations, buying and selling of bonds and securities, creation of new assets and liabilities, executing monetary and credit policies of the central bank etc.

Are the roles and functions of financial system geared towards economic development of an economy? Patriotic researchers and policy makers have observed a declining savings rate in Nigeria over the past decades; this is due to the critical importance of saving for the maintenance of strong and sustainable growth in the world economy particularly in Nigeria.

A sound, healthy and reliable financial system relates to savings mobilization and efficient financial intermediation roles:

First, reduces hoarding and help spread the risk between household and firms.

Second, lowers interest rates thereby bringing about stability in capital market.

Third, they create liquidity in the economy by borrowing short-term and lending long-term.

Fourth, disseminate information between ultimate lenders and ultimate borrowers thereby mobilizing savings from surplus units and channeling them to deficit units through the help of financial techniques, instruments and institutions. Fifth the intermediaries promote development investment.

The Nigerian financial system comprise the regulatory /supervisory authorities, bank and non- bank financial institutions. As at the end of 2007, the system comprised of the Regulatory/ Supervisory authority, the Central Bank of Nigeria (CBN), the Nigerian Deposit Insurance Corporation (NDIC), the Securities and Exchange Commission (ESC), the national Insurance Comedienne (NAICOM), the National Pension Commission (NPC), and the Federal Mortgage Bank of Nigeria (FMBN).the CBN is the principal regulate and supervisor in the money market, consisting of a Deposit Money Banks (DMBs), Discount Houses, the Peoples Bank of Nigeria and Community Banks.

The CBN exclusively regulates the activities of finance Companies and promotes the establishment of specialized or development financial institutions. The SEC is the apex regulatory/ supervisory authority in the capital market. The Nigerian Stock Exchange (NSE) is a self-regulatory or user-regulatory institution. The issuing Houses, Registrar and stock brokers, who also interact with the money market, complex the chain in the capital. The Federal Ministry of Finance, together with the CBN constitutes the monetary authorities and share control over Bureau de change. The NAICOM is the regulatory authority in the insurance industry, while

the FMBN regulates mortgage finance activities in Nigeria. Saving is a sacrifice of current consumption that provides for the accumulations of capital, which in term provides additional output that can potential be used for consumption in the future (Gersovitz1988). In other words, savings is the difference between current earnings and consumption. It has also been defined as "deferred consumption" or part of income, which is not spent.

Savings is described as a financial assets accumulated by the public- both government and private agents in the organized financial system. To expand financial savings involves shifting of funds from the personal and household sector to the business or corporate sector which in turn, leads to greater investment, income growth, employment and capital formation: which cannot be achieved without  increasing the rate of savings, Nigeria's saving still falls below the requirements of its financial system due to low per capital income, under- investment in productive instruments, and investment in unproductive channels, e.g. gold, jewelry, income inequalities  and  demonstration effect  Etc. to remedy this problems depend on the level of development of the financial sector mentioned above as well as the savings habit of the citizenry. The availability of investible funds can be a starting point for all

investments in the economy, which will eventually translate to economic growth and development (Uremadu, 2006). The relationship among saving, investment and growth has historically been very close; hence, the unsatisfactory growth performance of several developing countries. Example: Nigeria has been attributed to poor saving and investment. This poor growth performance has generally led to a dramatic decline in investment. Domestic saving rates have not fared better, thus worsening the already uncertain balance of payments position (Chete, 1999). The role of savings in the economic growth of any country cannot be overemphasized. Conceptually, savings represents that part of income not spent on current consumption. Instructions in financial sector like deposit money banks (DMBs)/commercial banks mobilize savings in a economy, the deposit rate must be relatively high and inflation rate stabilized to ensured a high positive real interest rate, which motivates investors to save from their disposable income. In Nigeria Nnann, Odoko and Englama (2004) are of the view that the level of funds mobilization by financial institutions are quite low due to a number of reasons, ranging from low savings deposits rates of the poor banking habit or culture of the people.

According to them, another impediment to funds mobilization is the attitudes of banks to small savers. Another Limitation to savings mobilization is the fact that the concentration of banks and their offices are biased in favor of urban areas. Among the reasons for this, is the fact that the established banks under- rate the volume of saving to be mobilized and channeled into productive investment in the rural areas. It is often argued that since the rural economy operates at a near subsistence level, there is very little that can be squeezed out of income and consumption. Because of this, it has not been realized that large volume of idle funds, though in small units per individual exist in the rural areas. In Nigeria, there is basically lack of incentives to savings which had adversely affects savings. Some of these factors include; poor banking habits, attitudes of banks to small savers, poor orientation, unemployment, instability in the political system, corrupt taxation system, instability in the banking system, etc. one of the economic growth and development in Nigeria.

## 1.2 STATEMENT OF THE PROBLEM

In Nigeria, there is lasting need of further efforts especially in mobilizing small savings in both urban and rural areas, and the process of financial intermediation itself, knowing fully well the

saving culture in Nigeria is very poor relative to other developing economics (Uremadu, 2006). In this respect, Commercial banks in performing their roles, was found to have potential scope and prospects for mobilizing financial resource and allocating them to investment. But given the problems inherent in the formal sector, the informal savings associations, if properly developed would not only facilitate the financing of economics development but would also contribute to the development of incomes, and that necessitates the need to put in place a coherent economics policy that will be capable of providing the much needed enabling environment and also there is an urgent need to encourage Nigerians to change their current attitude towards savings, thereby placing the right saving culture by institutions and regulatory agents who influence the decisions of households, firms and government.

As pointed out earlier, since national policy is it macroeconomic or microcosmic generates variables which could influence the propensity of economics and financial actors to save. This research work could attempt to examine from policy perspectives, the magnitude and direction of such variables as: interest rate, income,

growth, urbanization, foreign (aid) sector, fiscal policy etc, on savings in Nigeria.

Therefore, this research question will try and answer the following:

1. What are the factors that reduce savings in Nigeria?

**2.** What impact does factors reducing saving have on aggregate savings in Nigeria?

**1.3 OBJECTIVES OF THE STUDY:** In the light of the above problems, the objectives of this research work include:-

* To ascertain those factors that reduces savings in Nigeria.

To determine the impact of the factors that reduces saving on aggregate savings in Nigeria.

**1.4 STATEMENT OF THE HYPOTHESIS**

The hypotheses to be tested in this research work are:

a. Ho; the factors that reduce saving has no significant impact on aggregate savings in Nigeria.

b. H1; the factors that reduces saving has a significant impact on aggregate savings in Nigeria.

1.**5 SIGNIFICANCE OF THE STUDY**

This research work will be of immense help to [policy formulators particularly those involved in the development of the Nigerian economic agenda. It will help them in choosing the appropriate policy in the macroeconomic policy management, particularly those affecting saving in Nigeria. Also, through the findings and suggestions of this research project work, a greater awareness will be generated in the financial arena or sectors so as to appreciate the effects being carried out by the federal; government of Nigeria through the Central Bank of Nigeria and Federal Ministry of Financial in improving the policies affecting positive saving in recent years. Finally, this study will assists in a modest way to increasing student's knowledge on the practical and real- life situation of the theories they learn in the classroom.

**1.6 SCOPE AND LIMITATIONS OF STUDY**

 The scope of this study is to estimate and evaluate the factors that reduce savings in Nigeria (1980-2010).

The Limitations are constrained to lack of fund, human error and limited time frame, which imposed difficulties when serious attempt to effect a general in – depth towards the study of the factors that reduce savings in Nigeria.

## CHAPTER TWO

**LITERATURE REVIEW**

**2.1       THEORETICAL LITERATURE**

**2.1.       1 DEVELOPMENT OF SAVING IN NIGERIA**

Banks incur some costs while mobilizing funds from the surplus units of the economy mainly in interest payments on deposit accounts. In order to recover the cost of deposit mobilization and order operating overheads, higher interest rates are charged by banks.

Administratively, the central bank determines the interest rates subsequent to the deregulation of the banking sector. Both the deposit and lending rates were fixed by the CBN on the basis of policy decisions. At that time, the major goals were socially optimum resource allocation, promotion of orderly growth of the financial market, as well as reduction of both inflation and the internal debt service burden on the government. During the period 197 to 1985, the rates were unable to keep pace wit prevailing inflation rate, resulting in negative real interest rates.

Moreover, the performance of the preferred sectors of the economy was below expectation, thus, leading to the deregulation of the interest rate in August 1987 to a market –based system. This enable banks to determine their deposit and leading rates according to the market conditions through negotiations with their customers.

However, the Minimum Rediscount Rate (MRR) which is the Central Bank's nominal continued to be determined by the CBN. The Lack of responsiveness of the structures of deposit and lending rates to market fundamentals makes the interest rate inefficient. The wide divergence between the deposit and lending rates (interest rate spread) was an obstacle to economic growth and development of the Nigerian economy. Between 1980 and 1984, interest rate differentials averaged 3.9%, even though this was reasonable within the accepted limit, the spread widened between 1985 and 1989, averaging 4.3% per annum. This impacted negatively on the amount of loan- able funds available to the private sector for investment.

The interest differential further widened to an average of 7.95 between 1990 and 1994. Thereafter, the yearly interest rate spread maintained an upward trend, rising from 8.2% in 1995 to 24.6% in 2002, before declining to 15.7% in 2005. The widening gap between

the deposit and lending rates reflects the prevailing inefficiencies in the Nigerian banking system and has deterred potential investors from borrowing, and thus, lowered the level of investment in the economy. This use of interest rate spread has however been criticized given that higher levels of interest rates are usually associated with higher inflation rates, ad therefore a higher cost of holding money. As a result of these disadvantages of interest rate spread, net interest margin has been proposed as a better alternative. Net interest margin is equal to total interest revenues minus total interest expenditure divide by the value of assets. Higher values of net interest rate margin indicate a higher spread on deposit and lending rates and therefore lower efficiency.

The interest rate figures in Nigeria between 1870 and 2007 reveals that the nominal interest rate was institutionally determined by the monetary authorities throughout the 1970s and the first half of the 1980s. however, with the advent of the structural Adjustment Programme (SAP) in the mid- 1980s which brought with it a rash of financial sector reforms, Nigeria abandoned its fixed interest rate regime that saw nominal interest treats rising from 9.3% in 1985 to 26.8% in 1989, and reaching a peak of 19.8% in 1992. The figure

has since hovered between 13.5% and 2.4% and finally stood at 16.5% in 2007.

The real interest rate figure presents an interesting picture. Between 1970 and 2007, the figure was negative 20 times attaining positive figures on 18 occasions. The fixed interest rate regime of the 1970s and early 1980s on doubt contributed to this negative trend by fixing the interest rate at artificially low levels. For instance, in the first two decades (1970 to 1989) when the fixed regime dominated, real interest was negative 14 times and positive only 6 times. However, in the last two decades (1990 to 2007), when market forces took over, the real interest rate was negative on only 6 occasions. The inflation rate also played a very important role in making the real interest rate negative for most of the period. During the period when the real interest rate was negative it usually coincides with those of double-digit inflation rates.

## 2.1.2 THEORETICAL REVIEW

Saving literature can be based on two major hypotheses. Following the pioneering work of Keynes which defines savings as a linear function of income, the first major breakthrough in savings literature is the permanent income hypothesis of Friedman. This hypothesis differentiates permanent and transitory components of income as determinants of savings. Permanent income is defined in terms of the longtime income expectation over a planning period and a steady rate of consumption maintained over lifetime given the present level of wealth. Transitory income is the difference between actual and permanent income and since individuals are assumed not to consume out of this income category, marginal propensity to save on transitory income will be unity. Empirical tests of the permanent income hypothesis are mainly concerned with the effect of initial wealth on savings as well as the marginal; propensities to save out of permanent and transitory components of income. The second major contribution to savings literature comes from Ando and Modigliani's life cycle hypothesis, whose basic assumption is that individuals spread their lifetime consumption evenly over their lives by accumulating savings during earning years and marinating consumption levels during retirements. Tests of the life cycle

hypothesis are therefore mainly concerned with the effect of demographic variables such as age groups, birth rates, and describe savings during working life and disc-saving during retirement are financial variables such as interest rates, inflation rates, available financial instruments, and initial wealth levels which affect the inter- temporal consumption decisions of households. Saving behavior is seen to differ based on economic advancement of a nation: '

First, at macroeconomic level distribution of aggregate saving is attainable because savings and growth are key aspect of developed nations, which in the long run promote investment leading to capital formation and economic development and growth is achieved

Secondly, economic development and growth are delayed due to short-comings experienced in saving over decades, resulting either from lack of government policy or unwise polices.

Third, the demographic structures of developing nations are mostly involved in agriculture and proceeds from this sector are much more uncertain due to large and poor households at the microeconomic level. Also distribution of aggregate saving is likely impossible.

Lastly, saving is even more difficult to measure in developing economies than in advanced economics, whether at the household level or as a macroeconomic aggregate. Given the above, Deaton (1989) modification in the life- cycle theory model in which households cannot borrow but could accumulate assets as a bumper stock to project consumption when incomes are low. Those households that consume as often as they save cannot accumulate assets over a long period of time and have no average, very small asset holdings. However, their income Consumption is markedly smoother than their income. That is, a household that consume much of their income do not accumulate assets.

The modification of the life-cycle theory from the standard model in four important respects as regards household saving behavior in developing countries. First household in developing countries tend to be large than those in developed ones, and there is a greater tendency for several generations to live together. Such a household has no need for retirement saving because resources are shared between workers and dependents, and ownership is passed from parents to children. This kind of household can internalize many of the insurance activities that would otherwise require saving. Transfers within the household can insure individuals against

health risk and old age by proving effective annuities, and the close relationship among the individuals concerned may mean not only that moral hazard issues are less severe than in a more individualistic society, but also that the quality of the protection is very high.

Second, income derived from agriculture is naturally uncertain, an uncertainly that spreads from agriculture to related occupations and affects most of the population in predominantly agricultural economics. Uncertainty at low income poses a real threat to consumption levels, a treat that is likely to put forth a powerful influence on the way in which income is saved and spent. The poorer consumers are the more risk averse, they are generally supposed to be, with declining risk aversion having important implications for the shape of the consumption functions (Leland, 1968; Zeldes, 1989 and Kimball,1990). The standard model in which consumption equal permanent income cannot be derived from utility maximization in such a context. The third divergence from the standard model is the assumption that borrowing is not permitted. This is an extreme simplifying assumption, but more appropriate than it's opposite that households are free to borrow and lend at a fixed real interest rate. Borrowing constraints may be

serious because in financially repressed economies, there may be no credit available to non- favored borrowers. Even where there are financial intermediaries, they may be unwilling to lend for consumption purpose to individuals who have no collateral or to lend across agricultural seasons rather than within them.

The fourth distinction between household saving in developed and developing countries is a consequence of the previous three. In the model developed here, saving provides a buffer between uncertain and unpredictable income and an already low level of consumption. Saving here is inter-temporal smoothing saving, not life-cycle intergenerational saving. The analysis is different, and so are the welfare issues, which are focused on the protection of consumption, particularly among those whose consumption levels may not be far above subsistence.

On the macroeconomic aspects of saving in developing countries one of the most celebrated and most investigated predictions of the life-cycle model is that there should be relations between aggregate saving and the rate of income growth. If saving is accumulated during the working years of finance retirement, then income growth provides more savers than dissevers and positive aggregate saving. This is because workers are saving on a larger scale than the

retirees are disc-saving. However, even at the theoretical level, there are complications. If young consumers anticipate a steady growth in income, and can and will borrow against that increase, their disserving in the early years of the life-cycle may include a negative relationship between saving and growth in income. The standard positive relation works best if each worker experience a stationary income stream over his or her own life cycle, with growth taking place between rather than within generations.

The crucial question is whether household really want to have flat consumption stream. Contains young people may not want to borrow against future income growth, even if that growth is extremely likely. Old people also faced with daunting uncertainties about health and death may not run down their assets in the prescribed manner. This is an assumption that is strongly supported by the balance of empirical evidence from developed countries (Deaton, 1989). The cross-country empirical evidence generally supports a positive effect of per capital income growth on saving rates, variously defined (Gersovitz, 1988). However, the results are rarely well- determined and rely on how simultaneity between saving and growth are treated, and on the sample of countries selected.

## 2.1.3.0 DETERMINANTS OF SAVINGS

## 2.1.3.1 INCOME

Both the Keynesian savings function and the permanent income hypothesis indicate a positive effect of income on saving. According to the permanent income hypothesis, which distinguished between permanent and transitory components of income, households will spend mainly the permanent income and therefore the transitory income will immediately be channeled to savings with marginal propensity of savings from this income approaching unity. Studying a group of developing countries, Gupta observed that savings respond positively to transitory income. Koskela and Viren also concluded that unanticipated real income had a positive effect on savings.

Increased growth rates in income are also expected to have a positive effect on household savings. Collins, for example, found that income growth would increase savings especially if it concentrated in higher saving households. In this study all three definitions of income, namely, permanent income, transitory income, and growth rate of income, were used as explanatory variables.

## 2.1.3.2 WEALTH

Different definitions of wealth are used in the literature depending upon the different assumptions regarding the formation of expectations about inter-temporal consumption. Still, wealth is expected to have a negative effect on savings through the reduction of savings out of permanent income. As in the case of the Schmidt-Hebbel, Webb, and Corsetti study, this study also adopted the view that monetary asset holdings can be used to measures wealth both because monetary assets lesson the dependence on current income, especially when it declines temporarily, and the data from monetary assets are available on a comparable basis for all countries in the sample.

## 2.1.3.3 INFLATION

The impact of inflation on saving in the life-cycle model is through its role in determining the real interest rate. This is based on the assumption of the absented of real balanced effect of inflation and the non existence of money illusion in people's saving behavior. Athukorala and Sen (2004) affirm that inflation may not always be neutral because in the first place, the inflation rate is more difficult to predict in the long run than in the short run. Besides, inflation

brings about uncertainly in future income streams. Thus resulting in higher savings on precautionary grounds. Lastly, they posit that inflation could influence saving through it impact on real wealth.

Skinner (1988) and Zeldes (1989) observe that an increase in uncertainty should rise saving since risk- averse consumers set resources aside as a precaution against possible adverse changes in income. Carroll (1991) shows that uncertainty help to explain why consumption is highly correlated with income in the case of young consumers who expect their incomes to increase in the future but do not know by how much. Uncertainty also explains why the older population saves a positive amount as they face a lot of uncertainty regarding the length of their life and health costs. Carroll and Samwick (1995a) obtained results which suggest that precautionary saving may account for a large chunk of household wealth. Loayza,

Schmidt-Hebbel, and Serven (2000) find a positive and significant relationship between inflation and private saving rate.

## 2.1.3.4. FOREIGN SAVINGS

In the empirical work analyzing aggregate savings, foreign savings indicators are commonly used as explanatory variables. The access to foreign borrowing in international markets is expected to supplement domestic savings and fill the gap between domestic investment and national savings. The capital inflows are therefore expected to reduce household saving. Giovannin observed a significant negative effect, and Gupta a positive effect of foreign savings. However, foreign savings which are expected to influence national aggregate savings should not be a significant decision parameter fro household savings.

## 2.1.3.5 DEMOGRAPHIC VARIABLES

The life cycle hypothesis implies that demographic variables affect savings rates. The dependency ratio which is defined as the share of population under age fifteen or over sixty-five is the most popular demographic variables used in savings literature.  The young and the elderly are expected to consume out of past savings while the persons of working age are expected to accumulate savings. It is also indicated that there is a close causal link between the developments of well- organized capital markets and the number of children in the family.

## 2.1.3.6 GROWTH

The lifecycle model of hypothesis predicts that an increase in the rate of growth of income per capital will lead to an increase in the aggregate saving rate. This is because it increases the lifetime resources and saving of the younger population relative to that of the older one (Modigliani 1970; Maisian, 1992; Bosworth, 1993, and Carroll and Weil, 1994). However, controversy is still raging as to its structural interpretation, since some see it was evidence that saving drives growth through the saving investment link and others as evidence that is growth that drives savings. A panel- instrumental variable method was explored by Loayza, Schmidt-Hebbel and Serven (2000) to estimate the impact of income growth on saving. Their results show that a 10% point rise in growth rate increases the saving rate by a similar amount. Using household data, Deaton and Paxson (2000) found that the correlation between saving and growth is largely due to the effect of income growth on saving. If individuals determine their consumption plans on the basis of their respective income profiles. Thus, when wealth is introduced into the life-cycle model as an additional explanatory variable the model yields ambiguous results about the relationship between saving and growth. Attanansio, Picci and Scoru (2000), using different samples

and econometric methods. Found that in each case, growth grander cause saving. Besides, they observed that increase in saving rates do not always come before increase in growth. Lastly, they find that when additional controls were put in place, current income growth had a negative impact on lagged saving rates.

## 2.1.3.7 FINANCIAL DEVELOPMENT

Until recently, financial development was assumed to enhance the saving rate. It consists of elimination of credit ceilings, interest rate liberalization, easing of entry for foreign financial institutions. Enhanced prudential guidelines and supervision, and the development of capital market. Loayzal and Shankar (20000) find tat financial development has led the private sector to increase the durable goods component to their assets. The effect of financial development on saving rates can be separated into a direct short run impact, which is generally positive (Loayza et al, 2000). However, whether increases financial development itself significantly increases overall propensity to save depends on the extent of substitution between saving and other items in the household assets portfolio. Consequently, the expected signs of this relationship in the private saving function are ambiguous (Athukorala and Sen, 2004).

## 2.1.3.8 RATES OF RETURN (INTEREST RATE

The effect of interest rates on savings was inconclusive in the previous empirical studies. According to inter- temporal consumption decision, an increase in the rates of return increases savings but real income effect of higher rates of return can affect savings adversely. In his survey article. Balassa argued that the effect of real interest rates on saving is positive fro developing countries.

The effect of interest rates are may also be explained by the inflation effect: assuming that nominal rates of interest are constant, a rise in the inflation rate lowers the real cost of borrowing and hence has a positive effect on consumer expenditure and a negative effect on savings. Examining the household savings behavior, outliers indicated that real interest rates exert a negative influence on the savings ratio and the fall in real interest rates contributes to the rise in savings ratio.

## 2.1.3.9 URBANIZATION

Urbanization is a requisite for any financial development of a country. It create the opportunities for the enter populace to develop the habit of saving some degree of their need for future purposes and mainly for those that are suited or can fine

themselves in large cities such as Lagos, Port-Harcourt, Abuja,kano, Onitsha etc, and is due to the closeness of these financial institutions to individual(s) thereby minimizing the consumption stream of people in order to inculcate the sense of dome tic saving habit.

## 2.1.4. CONCULSION

From all ramification, one could say that, low income, low interest rate, inflation, wealth, raising population, low growth rate, underdeveloped financial system and low foreign capital inflow exerts the most adverse influence on saving in Nigeria. Therefore, policy strategies to mobilize savings which improves people's ability to save (through raising real per capita income and reducing real incomes or reducing rapid population growth that increases the dependency ratio among households) as well as increase saving opportunity (through increasing the number of saving institutions and spectrum of financial instruments available to the saving public) whelp, at the same time, incorporating those that improve incentives (through keeping real interest rates on saving positive) should be pursued and at the same time encouraged.

## 2.2 EMPIRICAL REVIEW AND EVIDENCE

Keynes (1936), defined savings as the excess of income over expenditure on consumption. Meaning that saving is the part of the disposable income which is not consumed in a particular period (Umoh, 2003 and Uremadu, 2005). Given that income is equal to the value of current output: and current investment (i.e. Gross capital formation) is equal to the value of that which is equal to the excess of income over consumption.

Keynes maintains that on the aggregate, the excess of income over consumption (otherwise called savings) cannot differ from the addition to capital equipment (i.e. Gross Fixed capital formation or gross domestic investment), so to speak (see CBN statistical Bulletin, Vol.1, December, 2000, PP, xvii-xviii). Saving is therefore a mere residual; and the decision to consume or invest determines the volume of national income accumulated in a period. In Keynesian view, therefore, secularly rising income would result in higher savings rate. As a matter of fact, savings is regarded as being complementary to the consumption function. In its simplest form, the savings function is derived from the linear consumption function when the autonomous consumption expenditure is separated off (Umoh, 2003). Keynes (1936), however, brought in the

opportunity cost variable, the rate of interest, which the classical economists now regard as the major determinant to savings (see Olusoji, 2003; Chete, 1999; Mckinnon and Shaw, 1973). The classical economists regard the rate of interest as the factor that brings the demand for investments and the willingness to save into equilibrium with one another (Umoh, 2003). The classical' view accepts the fact that savings and investment are necessarily equal (although this view is still a debatable point). They, however help that every act of increased savings by an individual necessarily bring into existence a corresponding act of increased investments.

There is the Permanent Income Hypothesis (PIH). This is one of the two dominant paradigms which provide the point of departure for most modern research on consumption and savings. The PH focuses on a representative lived consumer. While on the paradigm is the Life-cycle Hypothesis (LCH), which is derived from the aggregation of finitely lived overlapping generations. This theory views individual as choosing a life time stream of consumption and savings in a way what present value of their consumption equals the present's value of their lifetime earnings and inheritance (Deaton, 1990).

There abound numerous theoretical evidence concerning the functional relationships between savings and a wide range of causal variable. Fr instance Juster and Taylor) 1975) report that savings is an increasing function of income.  Moreover, Modigliani (1970), Madison (1992),Bosworth (1993), Carroll and Weil (1993), Schmidt –Hebbel, Serven and Solimano (1994),Modigliani (1995),Jappeli and Pugano (1994), Edwards (1995), Collins (1995) and Uremadu (2000) maintain that there exists a positive relationship between savings and income growth rates. Aghevti (1990) in Ozigbo (1999) reported that there is consensus that the level of savings is largely determined by the level of income.

In addition, studies dealing with savings and interest rates are categorized into two. Those who argue that high interest rates include Mckinnon (1993), shaw (1993), Molho (1986),Balassa (1989). Soyibo and Adekanye (1991), Gupta (1970) and Chandavarkar (1971. Conversely Williamson (1968, Boskin (1978), Juster and Taylor (1975. Howard (1978) and Uremadu (2006) found negative correlation between real interest rates and national savings. Inflation has been found to exert dual influences on savings. First, it encourages the holding of real assets rather than assets fixed in normal values, and thus reduce savings (Howard,

1978) Secondly, inflation creates a feeling of uncertainty and pessimism about the future and thereby encourages savings Deaton, 1977 and Gyifason, (1981). Chete (1999) reports a negative and significant effect on private savings on the broad money ($M_{2)}$ to GDP, thereby refuting the potential for payoffs from efforts at financial deepening. This particular finding accentuates the need to rethink current preoccupation with financial deepening as the route to growth and savings mobilization but contradicts Schhmidt – Hebbel and Serven (1996) who reported a negative sign on the $M_2$ coefficient.

**LIMITATION ON THE PREVIOUS STUDY**

This research work is set up to cover the lapses of the previous studies. The previous work on savings in limited to following area: the impact of savings on economic growth. This stud hopes to look not only on the impact of savings on economic growth but further into the factors that determine the growth rate of savings. Moreover, previous studies covered the period between 1980 and 2000 but this study hopes to study the trend between 1980 and 2010. Hence, this study will capture the most recent trend. This study will have as its focus: savings in Nigeria, as against cross- country studies of previous work.

# CHAPTER THREE

## 3.0 RESEARCH METHODOLOGY

## 3.1 MODEL SPECIFICATION

Model specification is expressing the mathematical and the independent variable, which will be included in the model. As evidence by literature, there are some other macroeconomic

variables which serve as influence to financial saving other than macroeconomic rate, such as; financial Development (FD), Real Per Capital GDP (Y)' Export Capacity (EXP) of Trade Openness (TDO), Net Capital Inflow (NCI) and others. The model in recognition of the fact that it will be intellectually, statistically, and economically unreasonable to assume that financial savings (S) is explained single handled by interest is a multiple regressions model and is stated thus:

AS = f (RGDP, TDO, INT, NCI),

It can also be stated thus:

$AS = B_o + B_1 RGDP + B_2 TDO + B_3 INT + B_4 NCI + e_i$

Where; AS = aggregate saving

RGDP =per capital real GDP.

TDO =Trade Openness.

INT = Interest rate.

NCI = Net capital inflow which is the balance between the inflow and outflow of foreign investment.

$B_o$ = Intercept of the function (constant term)

$B_1$ – B1 Regression coefficients

t =1980 -2009

$E_i$ =Error terms

## 3.2 ESTIMATION PROCEDURE

 The Ordinary least Square (OLS) single equation method is the estimation procedure adopted in the study. This is preferred because it is easy to understand, simple in its computational procedure and parameter estimation. It also possesses the properties of best, linear, unbiased estimator (BLUE), which are consistent and sufficient. The Microsoft Excel and PC Give computer software packages are used for this analysis.

3.3 method of evaluation

## 3.3.1 ECONOMIC APRIORI CRITICAL

This shows whether each independent variable in the equation is comparable with the postulation of economic theory (i.e., if the signs follows with the postulates of economic theory).

Using the OLS technique to estimate our model, we expect the coefficients to appear as follows.

**Table 3.1**

| Coefficient | Expected sign | Level of significant | Confidence Level |
|---|---|---|---|
| $B_1$ | Positive (+) | 5% (0.05) | 95% |
| $B_2$ | Negative (-) | 5% (0.05) | 95% |
| $B_3$ | Positive (+) | 5% (0.05) | 95% |
| $B_4$ | Positive (+) | 5% (0.05) | 95% |

## 3.3.2 STATISTICAL CRITERIA

This aim at the evaluating of the statistical reliability of the estimated parameters. In this case; coefficient of multiple determination ($R_2$), T- Statistics, F- Statistics, and Durbin –Watson Statistic are used.

## 3.3.2.1 COEFFICIENT OF MULTIPLE DETERMINATIONS ($R_2$)

The $R_2$ is used to test the Goodness of Fit of the model in the economy. That is, to show the percentage of total variation in dependents variable explained by the regression plane. The values between 0 and 1.

The $R_2$ is expressed mathematically as:-

$$R_2 = \frac{B_1 \sum_1 Y + B_2 \sum_2 Y + B_3 \sum_3 Y \ldots\ldots\ldots\ldots bn \sum X n Y}{\sum Y^2}$$

The higher the value of $R^2$, the higher percentage of variation of the dependent variable that is explained, by the regression plane. That is the better the Goodness of Fit of the regression plane to the sample observation, while the closer to zero, the sores the Goodness of Fit.

The value of $R^2$ lies between 0 and 1, the closer the value to 1, the better he fit and the closer to zero, the worse the fit.

## 3.3.2.2    T- STATISTICS

The t-test is used to test the statistical significant or reliability of the estimates of the regression coefficients.

If the probability at which $T_{cal}$ is significant in our regressions result for any independent variables is less or equal to our chosen

level of significant (0.05), we reject the null hypothesis (H0), which says that the independent variable is not significant. The invariably means accepting the alternative hypothesis (H1), which states that the independent variable in question is statistically significant in our model.

## 3.3.2.3. F –STATISTICS

The F- statistic is used to test for the overall significance of the regression result that is, the test aims at findings out whether the explanatory variable $(X_1 ..............X_n)$

Do actually have any significant influence on the dependent variable. If the probability at which the $F_{cal}$ is significant in the regression result is les than our chosen level of significance (0.05), we reject the null hypothesis $(H_0)$, which states that the regression is significant. But if the probability at which the $F_{cal}$ is significant in the regression result is greater than our chosen level of significance (0.05), it then implies that the overall regression is insignificant.

### 3.3.3 ECONOMETRIC CRITERIA (SECOND ORDER TEST)

### 3.3.3.1    AUTOCORRELATION TEST

This is used to test for the presence of serial auto- correlation. That is, the serial dependence of successive error terms in the regression.

Auto – correlation usually indicates that an important part of the variation of the dependent variable has not been explained. The problems of Auto- correlation are usually dictated by Durbin-Watson (DW statistic.

**It is given mathematically as:-**

DW = $\frac{\sum (e_t (e_{t} - 1)^2}{(e_t)^2}$

Where: DW = Durbin Watson

$\sum$ = Summation of

$e_t$ = Present Period errors

$e_{t-1}$ = Pervious Period Errors

**The Decision Rule is thus; Table 3.1**

| NULL HYPOTHESIS | DECISION | IF |
|---|---|---|
| No positive autocorrelation | Reject | $0<d<d_1$ |
| NO positive autocorrelation | No decision | $d_1<d<du$ |
| NO negative autocorrelation | Reject | $4-d_1<d<4$ |
| NO negative autocorrelation | NO decision | $4d_1<d<4-d_1$ |
| NO positive or negative autocorrelation | Do not reject | $Du<d<4-d_u$ |

Where:

$d_1$ Lower limit

$d_u$ =upper limit

### 3.3.3.2    TEST FOR MULTICOLLINEARITY

This will be used to check for multicollinearity among the explanatory variables, the basis for the test being the correlation matrix result, using the correlation coefficient between pars of repressors.

### 3.3.3.3.    HETTEROSCEDASTICIT TEST

This test would be conducted to ascertain whether the error $U_i$ in the regression model has a common or constant variance. The white heteroscedasticity test (with no Cross terms) will be adopted.

### 3.4    DATA REQUIRE AND SOURCE/ SOFTWARE PACKAGE

The data employed in this study secondary date obtained from central bank of Nigeria, (CBN), the National Bureau of Statistics (NBS), and Journals of economic studies.

# CHAPTER FOUR

## 4.0 PRESENTATION OF MODEL RESULTS

The results of our models are presented in Table 4, 1

**Table 4.1 Result Summary**

| Variable | Coefficient | Std Error | t-Value | t- Prob | Part $R^2$ |
|----------|-------------|-----------|---------|---------|------------|
| Constant | -1.2179 | 8.5038 | -1.432 | 0.1640 | 0.0731 |
| RGDP | 6.5665 | 1.4693 | 4.469 | 0.0001 | 0.4344 |
| TDO | 1.8661 | 1.7483 | 1.067 | 0.2956 | 0.0420 |
| INT | -57436 | 42416 | -1.354 | 0.1874 | 0.0659 |
| NCT | 9.4328 | 17.744 | 0.532 | 0.5995 | 0.0108 |

$R^2 = 0.68145$,　　$F_{(4, 25)} = 13.905 (0.0000)$, a = 1.06824,

DW =1.18　　　　　RSS = 2.966976134

### 4.2.1   REAL GROSS DOMESTIC PRODUCT (RGDP)

The coefficient of RDGP shows a positive value of 6.5665 implying that a unit change in real gross domestic product will bring about a positive 656.7% increase in aggregate saving.

### 4.2.2 TRADE OPENNESS (TDO)

The coefficient of TDO reflects a positive value of 1.8661 expressing positive relationship between export capacity and aggregate saving therefore exacting an increasing pressure on economic growth. The positive sign shows that a unit change in trade openness will increase Aggregate savings by 186.61%

### 4.2.3 INTEREST RATE (INT)

Interest rate shows a negative value of -57436, implies that a unit increase in interest rate causes aggregate saving to decrease by -57436%. In other words, interest rate is an effective policy instrument for maintaining investment driven as a way of promoting the aggregate economic growth.

## 4.2.4 NET CAPITAL INFLOW (NCI)

Net capital inflow have a positive coefficient of 9.4328, this imply a positive relationship between net capital inflow will contributes about 943.28% to aggregate saving in Nigeria.

## 4.2 ECONOMIC INTERPRETATION OF RESULTS

| Variable | Expected signs | Obtained signs | Conclusion |
|----------|----------------|----------------|------------|
| RGDP | Positive | Positive | Conforms |
| TDO | Positive | Positive | Conforms |
| INT | Negative | Negative | Conforms |
| NCI | Positive | Positive | Conforms |

## 4.3 EVALUATION BASED ON ECONOMIC CRITERIA

As stated early in chapter three, our parameter estimates are expected to conform to a priori expectation consequently the table below summarizes the outcome of our model parameters on a priori ground.

## 4.4 STATISTICAL CRITERIA FOR EVALUATION OF RESULT

These tests are determined by statistical theory and aims at evaluating the statistical reliability of the estimates and parameters of the model (Koutsoyiannis, 1977), from the sample observation. The first order tests is carried out based on the following: $R^2$ T – test and F –test.

### 4.4.1 COEFFICIENT OF DETERMINATION ($R^2$)

In our model. $R^2$ = 0.68145 which implies that approximately 68% of the variation in the dependent variable (SA) is caused by the explanatory variables included in this model.

### 4.4.2 THE T-TEST

This test was conducted to ascertain the significant status of each of the parameters or variables. In doing this, we employed the two-tail tests which compared the t- calculated from each of the explanatory variables with the t- tabulated.

At 5% level of significance

N-k degree of freedom

$\alpha$ = 5%

A/2 = 0.005/2 =0.025

n −k = 30 -5 =25

## Hypothesis

**H$_o$:** Bs = 0 (Individual parameter estimates are not significant)

**H$_1$:** Bs ≠ 0 (Individual parameter estimates are significant)

## Decision rule

If t-cal is greater than t-tab at 5% level of significance we reject the Ho and accept if other wise.

## T-test summary test

| Variable | t- value | t-tab | CONCLUSION |
|----------|----------|-------|------------|
| Constant | -1.432 | ±2.056 | Not Significant |
| RGDP | 4.469 | ±2.056 | Significant |
| TDO | 1.067 | ±2.056 | Not Significant |
| INT | -1.354 | ±2.056 | Not Significant |
| NCI | 0.532 | ±2.056 | Not Significant |

The above results in the table show that only real GDP is statistically significant since their-t-test cal is greater than the t-tab.

## 4.4.3 THE F- TEST

The F- test, which follows an F-distribution, measures the overall significance of the model.

**Hypothesis Test**

$H_0$: $B_1 = B_2 = B_3 = 0$ (The model is statistically insignificant)

$H_1$: $B_1 \neq B_2 \neq B_3 \neq 0$ (The model is statistically insignificant)

At $\alpha = 5\%$ level of significant, with n-k degrees of freedom.

**Decision Rule**

Reject Ho if f-cal > f-tab and accept Ho if f- cal < f-tab.

From the f-table we have 2.7426 which is less than f-cal of 13.905 we reject Ho and conclude that the model is statistically significant.

## 4.5 ECONOMETRIC CRITERIA (SECOND-ORDER TEST)

## 4.5.1 NORMALITY TEST

This test was carried out to check whether the error term follows the normal distribution. The normality test adopted is the **Jargue-Bera (JB) Test of normality**. The JB test of normality is an asymptotic, or large-sample, test and it is based on the OLS residuals. These test computers the skewness and Jusrtosis

measures of the OLS resident and use the Chi -square distribution (Gujarati, 2004: 148).

**Hypothesis: Test**

H0: $q_1 \neq 0$ (The error term follows a normal distribution)

H1: $q_1 \neq 0$ (The error term not follow a normal distribution)

At $\alpha$ = 5% with 2 degree of freedom.

Test Statistics: Type equation here.

$$JB = n \left[ \frac{s^2}{6} + \frac{(k-3)^2}{24} \right] = 7.523$$

Where n= sample size,

S = Skewness coefficient, and

K =Kurtosis coefficient

**Decision Rule:** Reject H0 if X2 cal > x2 tab (2df), and accept H0 if otherwise

From the result obtained from Jarque-Bera (JB) Test of normality,

JB =7.523 which is shown in appendix, and from chi-square table

x2 cal = 5.239

Therefore, since x2 cal = 7.523 ≤ tab = 5.99 at 5% level of significance, we accept H0 and conclude that the error term does not follow a normal distribution.

## 4.5.2 TEST FOR AUTOCORRELATION

The convectional Durbin Watson d statistics is employed. We compare the established lower limit dl and upper limit du of Durbin Watson based on 5% level of significant and k degree of freedom. Where k = number of explanatory variables excluding the constant.

**Decision Rule**

If d < du, we reject the null hypothesis ($H_0$) at α significant level, that is, there is significant positive autocorrelation.

If (4-d) <du, we reject the null hypothesis ($H_0$) at α significant level, that is, there is significant negative autocorrelation.

If d < du or (4-d) <du, we accept the null hypothesis ($H_0$) at 2α significant level. There is significant autocorrelation, positive or negative.

From our regression result and the Durbin Watson d statistical table.

d    =    1.18

dl    =    1.143

Du    =    1.739

From the result, the estimated d = 1.18 and the tabulated DW with 4 degree of freedom for 3 observations are dl = 1.160 an du = 1.735. Since d < du that is 1.18 < 1.735, we conclude that there is a significant positive autocorrelation.

## 4.5.3 TEST FOR HETEROSCEDASTICITY

This test is basically focused on the variance of the error term. The test helps to ascertain whether the variance of the error term is constant.

$H_0$: $B_1$ = $B_2$ = $B_3$ = 0 (Homoscedasticity)

$H_1$: $B_1$ ≠ $B_2$ ≠ $B_3$ ≠ 0 (Homoscedasticity)

Decision Rule: Reject $H_0$ if $x^2$ cal > $x^2$ tab (0.05) and accept if otherwise. From our result, the calculated chi-square ($x^2$) at 8 degrees of freedom is 24.248, while the tabulated $x^2$ 0.05 (8 degrees of freedom) is 15.5, since our estimated 24.248 ≥ 15.5 we reject the null hypothesis of homoscedasticity and accept the alternative hypothesis of heteroscedasticity, meaning that the error terms have a constant variance.

## 4.5.4 TEST FOR MULTICOLLINEARITY

That test is carried out using correlation matrix.

According to Gujarati, 2004. Multicollinearity is a problem, if any correlation exceeds 0.8.

| | AS | RGDP | TDO | INT | NCI | Conclusion |
|---|---|---|---|---|---|---|
| AS | 1.000 | | | | | Absence of Multicollinearity |
| RGDP | 0.7984 | 1.000 | | | | Absence of Multicollinearity |
| TDO | 0.2921 | 0.2398 | 1.000 | | | Absence of Multicollinearity |
| INT | 0.04200 | 0.1861 | 0.4699 | 1.000 | | Absence of Multicollinearity |
| NCI | 0.6602 | 0.7034 | 0.4659 | 0.1094 | 1.000 | Absence of Multicollinearity |

From the table above, there is no correlation that exceeds 0.8; we conclude that there is no presence of Multicollinearity between all the variables.

# CHAPTER FIVE

# SUMMARY, CONCLUSION AND RECOMMENDATIONS

## 5.1    SUMMARY OF FINDINGS

Based on findings in this study with the coefficient of various variables that was conducted employing econometric approach. It can be seen that trade openness is one of the major factors that reduce aggregate savings in the Nigeria. Which may some government policy that conflicts' with policy that aims at improving the export capacity?

Also, a greater proportion of aggregate savings in Nigeria is made by the low income earners who do not engage in long term savings that will generate the needed productive investment while the high-income group (potential investors) that should engage in long term saving engages in conspicuous consumption and stashes their money in foreign accounts.

Furthermore, we found out that the coefficient of **interest rate,** which is -57436, is high in Nigeria. This implies that the higher the interest on savings deposit the more willing will savers be to replace present consumption with future consumption. Hence the classical economists view the interest rate as a real reward or abstinence or thrift. This goes to substantiate the fact that Nigeria savings is predominantly mobilized from "**target saves**" who are mainly civil servants, small businessmen, artisan, traders and those who may be saving for    their children in school or for retirement purposes. Their motive for saving is to provide for future consumption.

## 5.2 CONCLUSION

 After econometrically analyzing the factors that affect savings behavior in Nigeria over the period of 1980 -2010. The empirical findings have some serious policy implications relevant to the growth and development of the nation. For the Nigeria economy to break away from its current level of underdevelopment, policy makers must recognize the importance of these variables- per capital real gross domestic product, trade openness, interest rate, Net capital inflow in the Nigeria economy.

Thus, the effective manipulation of these variables through consistent and effective target policies for facilitating adequate mobilization of savings is necessary for productivity investment.

## 5.3    POLICY RECOMMENDATIONS

Following our empirical findings, the following recommendations are made for effective policy formulations.

* Luxurious consumption should be discouraged through the imposition of taxes on certain luxury goods.

* The banking industry should improve the banking facilities and also inculcate banking habit among Nigerians by innovating attractive products that will attract their customer's varying needs of liquidity, yield, risk, and maturity.

* Export capacity should be improved by simultaneously increasing productivity in capital goods for export as the most effective way of increasing foreign reserve, which has positive effect on the level of savings in Nigeria.

* Increased savings facilities disposable income should be follow up with policies that increase interest rate to achieve the desired objectives of raising the level of savings.

* It is crucial to note that adequate savings mobilization is a fundamental but not sufficient condition for an increase investment. Therefore, adequate mobilization of savings should be followed up with the provision of adequate information on potential investment opportunities in the country.

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