**CAUSES AND EFFECT AND SOLUTION TO INFLATION IN NIGERIA**

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**ABSTRACT**

The study examines the impact of inflation on economic growth of Nigeria. Other micro economic variable tested along with inflation in this study are Agriculture, manufacturing, and trade. In analyzing the data the simple percentage method was applied the empirical results demonstrated that there is a positive relationship between the dependent variable (agriculture and trade) and explanatory variable except in manufacturing.
The relationship between inflation and economic growth is one, which many economists have watched with keen interest. Producers in the production sector cash on this phenomenon to make a brisk business sat the expense of fixed income earners. This informs the increase in turnover in inflationary periods. Money economy gave rise to inflation, which reduces the living standard of the people and the level of saving dwindles in turn. The effect on economic growth is dependent on the level of economic activity going on. If there are more producers, there are likely to be an increase in the level of economic growth vice versa.
In all, inflation do not wish any economy well, so should be eradicated by a deliberate effort. Nigeria has intellectuals that are capable of formulating good monetary and fiscal policies that will benefit her.

**CHAPTER ONE**

**INTRODUCTION**

* 1. **Background of the study**

The word inflation rings a bell in the market economics of the world. It is a monster that threatens all economics because of its undesirable effects. The problem of inflation surely is not a new phenomenon. It has been a major problem in the country over the years. Inflation is a problem in all facets of life and in all economic entities. The government of any nation is concerned with the responsibility of ensuring that her plans and programme are not frustrated by unpredictable and galloping prices. Every firm desires a stable macro-economic environment that is devoid of unrepentant price change that can bring about reliable forecast and planning. An individual also strives that he is not worse off by unexpected price increase. All these bring home the need to explore the study of inflation so as to form a timeless and dependable model of its tendency (Taiwo, 2011). Inflation is a household word, but few give attention to the dimension of causes and impact of its effects. It is undoubtedly one of the most highly treated subjects in economic researches and literature. Its effects and causes are many, vary and well treated in literature. See Okpara and Nwaoha (2010), Fullerton and Ikhide (1998), Odusunya and Atanda (2010), Egwaikhide et al (1994), Jhingan (2004), Batini (2004), Owoye (2007),Asogu (1999) among others. This study investigated the major causes, effects of inflation and the model that best explains the uniqueness of Nigerian inflationary tendency and develops a tool for forecasting its behavioiur. Besides, we also examined the nature of relationship that exists between inflation and some other economic variables such as government spending, money supply, expectations, exchange rate, gross domestic products, exchange rate of dollar to naira and expenditure to income ratio among others. This work is significant and elaborate because it covered a period of 40 years (1969-2009), a period that has not been covered in the nearest past. It also examined inflation in terms of growth rate and not in absolute value. The significance of the study could also be traced to the exclusion of the inflationary data before 1970. This is premised on the fact that past research on the subject has dealt extensively in this period, and in most cases included the ‘war dummy’ to show the impact the Nigerian civil war had on inflation. Inflation is defined as a generalized increase in the level of price sustained over a long period in an economy (Lipsey and Chrystal, 1995). Inflation is a household word in many market oriented economics. Although several people, producers, consumers, professionals, non-professionals, trade unionists, workers and the likes, talks frequently about inflationparticularly if the malady has assumed a chronic character, yet only selected few knows or even bother to know about the mechanics and consequences of inflation.
One of the fundamental goals of a modern economic system is to keep prices of goods and services stable at rates that would not be detrimental to the economic system. The attainment of this goal, of ensuring that prices do not rise continuously, is very crucial in that non-attainment of the goal carries with it dire micro and macroeconomic consequences. At the microeconomic level, the unfair wealth redistribution that may accompany an upward movement of prices could encourage hoarding of unspent income, increase the cost of borrowing and therefore constrain investment spending by businessmen. At the macroeconomic level, an upward inflationary pressure may make the export of goods and services in an economy to dwindle because the prices of tradables may become less competitive in the international markets thereby discouraging foreign purchases and consumption of such tradables. An offshoot of this is that the national income of the economy may fall with attendant adverse consequences on the economy’s employment (increased unemployment), economic growth and possibly development. Plausibly, it is for these reasons that managers of economies around the world strive strenuously to keep inflation rates at low and stable levels. The managers of the Nigerian economy are not without the fervour to have a low and stable inflation environment. But a retrospective look at the performance of the economy, for example, from 1974 which was the year the country’s monetary policy regime changed from exchange rate targeting to the direct monetary targeting framework in response to the inflationary pressure resulting from increased public expenditure as a result of the reconstruction works after the civil war (CBN, 2014) and the monetisation of the petrodollars, to 2013 shows that the Nigerian economic environment may be anything but a low and stable inflation one. During this 40-year observation period, for instance, the average annual rate of headline inflation (inflation rate estimates based on the price movements of all essential commodities including food and energy) was a double-digit rate of 20. 47 percent (CBN, 2008; CBN, 2010; CBN, 2011 and CBN, 2013). After an appreciable economic performance in the early 1970s, the Nigeria economy witnessed some anxious moment in the late 1970s to mid-1980s. Severe pressures built up in the economy mainly because of the expansionary fiscal policy of the federal government during these years. This was accompanied by high monetary expansion as the huge government deficit was financed largely by the Central Bank of Nigeria. This was exacerbated by the transfer of government sector deposits to the banks and the resultant increase in their free reserves with adverse consequences on the general price level. The inflationary pressure was further aggravated by high demand for imports of both intermediate inputs and consumer goods due to over valuation of the naira which made imports relatively cheaper than locally manufactured goods. In this case, the impediments to development may be referred to as cost. Economics theory, however, postulates that for the profit to be maximised, cost should be minimised. One of the main cost is inflation, which has turned into a canker worm eating deep into the nation’s path of economic progress. However, as fiscal discipline was restored in the second half of 1999, the pressures on the exchange rate and domestic prices moderated significantly. The economy faced renewed pressures and some uncertainty towards the end of the year as the C.B.N gradually relaxed its tight monetary policy.

Undoubtedly one of the macroeconomic goals which the government strives to achieve is the maintenance of stable domestic price level. This goal is pursued in order to avoid cost of inflation or deflation and the uncertainty that follows where there is price instability (Salam et al, 2006). The effects of inflation on economic growth will be examined bearing in mind that a country will grow faster in real terms if inflation is reduced to a barest minimum. Perhaps it should be mentioned here that inflation is not incompatible with growth. Infact, it reached an all-time high of almost 80% in 1994.The story is not any different when core inflation (a more restrictive measure of inflation which excludes food and energy price movements) is considered. Figure 1 also shows that in 11 out of the 18 years of observation of this measure, the Nigerian economy experienced double-digit inflation with the highest figure recorded at about 35% in 2003. Based on the foregoing, it could be reasonably deduced that the Nigerian economic environment has been and probably is still experiencing inflationary episodes and this may tempt one to call into question the credibility and efficacy of the country’s monetary policy. It has been argued in some literature that inflationary episodes can emanate from three major sources. They can arise out of the ability of labour unions to use market power to demand for wage increases which are in excess of productivity gains in order to appropriate part of the profits accruable to entrepreneurs (often referred to as distributional conflict cause of inflation). Inflationary episodes can also be brought about by developments in the product markets where because of the existence of oligopolistic and/or monopolistic market structures (concentration of capital or high concentration ratio in the product market) firms may wield the market power that allows them to practice markup pricing. Lastly, inflationary episodes may occur as a result of some form of exogenous or endogenous shocks that may be driven by either exchange rate depreciation (pass-through effect) or an upward surge or spike in the price of a commodity like crude oil. In either case, shocks may adversely affect costs of production which firms can pass on to domestic prices. This depends though on the pricing power of firms, elasticity’s of the demand curves of consumer durables and nondurables and on how persistent inflation is in the economy

**STATEMENT OF THE PROBLEM**

There is almost a universal consensus that macroeconomic stability, specifically defined as low inflation, is positively related to economic growth. Over the years the question of the existence and nature of the link between inflation and growth has been the subject of considerable interest and debate (Erbaykal and Okuyan, 2008). Although the debate about the precise relationship between these two variables is still open, the continuing research on this issue has uncovered some important results. In particular, it is generally accepted thatinflation has a negative effect on medium and long-term growth (Bruno and Easterly, 1998). Inflation impedes efficient resource allocation by obscuring the signalling role of relative price changes, the most important guide to efficient economic decision-making (Fischer, 1993).

If inflation is inimical to growth, it obviously follows that policymakers should aim at a low rate of inflation. But how low should inflation be? Should it be 10 percent, 5 percent, or for that matter, zero percent? Or put in other words, is there a level of inflation at which the relationship between inflation and growth become negative? The empirical test of the impact of inflation on the Nigerian economy which is the subject matter of this study shall provide precise answer to the relationship between inflation and growth and how the problem could be tackled.

**OBJECTIVES OF THE STUDY**

The broad objective of this study is to examine inflation in developing countries with the view of ascertaining the effect of inflation on economic growth. The specific objectives of this study are to:
(i) examine the trend of inflation in Nigeria over the years;
(ii) investigate the impact of inflation on the economic growth of Nigeria;
(iii) Explore the effect of inflation on capital formation in Nigeria;
(iv) Examine the influence of inflation on peoples’ consumption;
(v) Suggest visible solutions to the problem of inflation in the country.

**RESEARCH QUESTIONS**

This study would be guided by the following research questions:
1. What is the trend of inflation in Nigeria?
2. How does Inflation impact on economic growth in Nigeria?
3. What is the effect of inflation on the level of capital formation in Nigeria?
4. How does inflation affect the consumption expenditure of Nigerian households?

**STATEMENT OF HYPOTHESES**

The hypotheses to be tested in the course of this study are stated below:
Hypothesis I
Ho : Inflation does not affect significantly the economic growth of Nigeria.
H1 : Inflation affect significantly the economic growth of Nigeria.
Hypothesis II
Ho :Inflation does not affect significantly capital formation in Nigeria.
H1 : Inflation affect significantly capital formation in Nigeria.
Hypothesis III
Ho : there is no significant relationship between inflation and consumption expenditure of people in Nigeria.
H1 : there is relationship significant between inflation and
consumption expenditure of people in Nigeria.

**THE SIGNIFICACE OF STUDY**

The effect of inflation on the economic development of Edo state cannot be over emphasized; therefore, this research work is designed to find out the problem facing the inflation, causes, effect and solutions.

**SCOPE OF THE STUDY**

   This work is to cover the effects of inflation and economic development in Edo state between 1993 to 2003 (a decade) and also various ways in which the scourge has been controlled by the various administration and relevance of control model or methods.

**DEFINITION OF TERMS**

Inflation can be defined as any increase in the money supply; however this can be regarded as inflation. This can also be seen as persistent in average price level of goods and services resulting in diminishing purchasing power of a governmental sum of money. Also when the volume of money in circulation is greater than the available goods and services so that there is a continuous tendency for average price level rise.

 **Open And Suppressed Inflation:** Open inflation is the result of the uninterrupted operation of the market mechanism. There are no controls on the distribution of commodities by the government imposes fiscal and monetary controls to check open inflation.

**Stag inflation:** This is a situation whereby recession is accompanied by a high rate of inflation also called inflationary recessing. This type of inflation is caused by the excessive demand in commodity market and decrease in the demand for labor thereby causing prices to rise and creating unemployment in the economy.

**Edmand –Pulll Inflation:** This is a situation offer described as ‘too much money chasing few goods”, this arises as a result of increase in demand with a corresponding decrease/increase in the supply of goods and as a result the prices of these goods will rise.

**ARTIFICIALLY CREATED INFLATION:** This is a situation whereby traders sometimes create artificial scarcity by heading the commodities with the main aim of increasing the prices of their commodities.

**COST-PUSH INFLATION:** This is a situation where money wages rises more rapidly than the productivity of labour, cost-push inflation is caused by continues rise in the prices of factors of production, land, Labour, capital and entrepreneurship.

**MAKE-UP INFLATION:** This take of inflation is closely related to the price-push problem, modern labour organization set prices and wages on the basis mark-up over cost and relative income, firm possessing monopoly power have control over the prices and so level administered price, when strong trade unions are successfully in raising the wages of worker, it contribute to inflation. Having considered the types and cause of inflations it then lead to consideration of the effects of inflation in Nigeria Economy.

**1.8 ORGANIZATION OF THE STUDY**

This research work is organized in five chapters, for easy understanding, as follows Chapter one is concern with the introduction, which consist of the (overview, of the study), statement of problem, objectives of the study, research question, significance or the study, research methodology, definition of terms and historical background of the study. Chapter two highlight the theoretical framework on which the study is based, thus the review of related literature. Chapter three deals on the research design and methodology adopted in the study. Chapter four concentrate on the data collection and analysis and presentation of finding. Chapter five gives summary, conclusion, and recommendations made of the study.

**CHAPTER TWO**

**REVIEW OF RELATED LITERATURE**

**2.1 Introduction**

One of the fundamental goals of a modern economic system is to keep prices of goods and services stable at rates that would not be detrimental to the economic system. The attainment of this goal, of ensuring that prices do not rise continuously, is very crucial in that non-attainment of the goal carries with it dire micro and macroeconomic consequences. At the microeconomic level, the unfair wealth redistribution that may accompany an upward movement of prices could encourage hoarding of unspent income, increase the cost of borrowing and therefore constrain investment spending by businessmen. At the macroeconomic level, an upward inflationary pressure may make the export of goods and services in an economy to dwindle because the prices of tradables may become less competitive in the international markets thereby discouraging foreign purchases and consumption of such tradables. An offshoot of this is that the national income of the economy may fall with attendant adverse consequences on the economy’s employment (increased unemployment), economic growth and possibly development. Plausibly, it is for these reasons that managers of economies around the world strive strenuously to keep inflation rates at low and stable levels. The managers of the Nigerian economy are not without the fervour to have a low and stable inflation environment. But a retrospective look at the performance of the economy, for example, from 1974 which was the year the country’s monetary policy regime changed from exchange rate targeting to the direct monetary targeting framework in response to the inflationary pressure resulting from increased public expenditure as a result of the reconstruction works after the civil war (CBN, 2014) and the monetisation of the petrodollars, to 2013 shows that the Nigerian economic environment may be anything but a low and stable inflation one. During this 40-year observation period, for instance, the average annual rate of headline inflation (inflation rate estimates based on the price movements of all essential commodities including food and energy) was a double-digit rate of 20. 47 percent (CBN, 2008; CBN, 2010; CBN, 2011 and CBN, 2013). Infact, it reached an all-time high of almost 80% in 1994.The story is not any different when core inflation (a more restrictive measure of inflation which excludes food and energy price movements) is considered. Figure 1 also shows that in 11 out of the 18 years of observation of this measure, the Nigerian economy experienced double-digit inflation with the highest figure recorded at about 35% in 2003. Based on the foregoing, it could be reasonably deduced that the Nigerian economic environment has been and probably is still experiencing inflationary episodes and this may tempt one to call into question the credibility and efficacy of the country’s monetary policy. It has been argued in some literature that inflationary episodes can emanate from three major sources. They can arise out of the ability of labour unions to use market power to demand for wage increases which are in excess of productivity gains in order to appropriate part of the profits accruable to entrepreneurs (often referred to as distributional conflict cause of inflation). Inflationary episodes can also be brought about by developments in the product markets where because of the existence of oligopolistic and/or monopolistic market structures (concentration of capital or high concentration ratio in the product market) firms may wield the market power that allows them to practice markup pricing. Lastly, inflationary episodes may occur as a result of some form of exogenous or endogenous shocks that may be driven by either exchange rate depreciation (pass-through effect) or an upward surge or spike in the price of a commodity like crude oil. In either case, shocks may adversely affect costs of production which firms can pass on to domestic prices. This depends though on the pricing power of firms, elasticities of the demand curves of consumer durables and nondurables and on how persistent inflation is in the economy. There have been some studies on Nigeria which investigated the effect of exchange rate depreciation (a traditional cause of inflation) on the country’s domestic inflation (see for instance, Ogundipe & Egbetokun, 2013; Boamah, 2013). But studies on institutional causes of inflation (causes emanating from product market and labour market sources) on Nigeria are not very visible. The specific objectives of this study are to: identify the traditional and institutional macroeconomic inflation variables which are responsible for this phenomenon, determine the magnitude of the contribution of each variable to the rise in general price level, explain the mechanism through which the identified variables influence the general price level and make recommendations on how best to tackle the scourge of persistent inflation in the country

**2.2** **CONCEPTUAL REVIEW**

The concept of inflation has been define as a generalized increase in the level of price sustained over a long period in an economy, or as a persistence rise in the general price level of broad spectrum of goods and services in a country over a long period of time. Inflation has been intrinsically linked to money, as captured by the often heard maxim „„inflation is too much money chasing too few goods‟‟. Hamilton (2001) inflation has been widely described as an economic situation when the increase in money supply is „„faster‟‟ than the new production of goods and services in the same economy. Piana (2001) economists usually try to distinguish inflation from an economic phenomenon of a onetime increase in prices or when there are price increases in a narrow group of economic goods or services.

Ojo (2000) and Melberg (1992) the term inflation describes a general and persistent increase in the prices of goods and services in an economy. Inflation rate is measured as the percentage change in the price index (consumer price index, wholesale price index, producer price index etc). Essien (2002) opine that the consumer price index (CPI), for instance, measures the price of a representative basket of goods and services purchased by the average consumer and calculated on the basis of periodic survey of consumer prices. Owing to the different weights the basket, changes in the price of some goods and services have impact on measured inflation with varying degrees. There are several disadvantages of the CPI as a measure of price level. First, it does not reflect goods and services bought by firms and/or government, such as machinery. Secondly, it does not reflect the change in the quality of goods which might have occurred overtime. Thirdly, changes in the price of substitutable goods are not captured. Lastly, CPI basket usually does not change often. Despite these limitations, the CPI is still the most widely used measurement of the general price level. This is because it is used for indexation purposes for many wage and salary earners (including government employees). Another measure of inflation or price movements is the GDP Deflator. This is available on an annual basis. However, it is rarely used as a measure of inflation. This is because the CPI represents the cost of living and is, therefore, more appropriate for measuring the welfare of the people. Furthermore, because CPI is available on a more frequent basis, it is useful for monetary policy purposes. In recent times, there have been three dominant schools of thought on the causes of inflation; the neoclassical/monetarists, neo-Keynesian, and structuralists. The neo-classical/monetarists opine that inflation is driven mainly by growth in quantum of money supply. However, practical experiences of the Federal Reserve in the United States (US) have shown that this may not be entirely correct. Hamilton (2001) and Colander (1995) the US money supply growth rates increase faster than prices itself. This has been traced to the increased demand for the US dollar as a global trade currency. The neo-Keynesian attributes inflation to diminishing returns of production. This occurs when there is an increase in the velocity of money and excess of current consumption over investment. The structuralists attribute the cause of inflation to structural factors underlying characteristics of an economy (Adams, 2000). For instance, in the developing countries, particularly those with a strong underground economy, prevalent hoarding or hedging, individuals expect future prices to increase above current prices and, hence, demand for goods and services are not only transactionary, but also precautionary. This creates artificial shortages of goods and reinforces inflationary pressures. The literature is replete with those factors that could affect the level of inflation. These factors can be grouped into institutional, fiscal, monetary and balance of payments. Several studies such as Melberg (1992); Cukierman, Webb and Neyapti (1992); Grilli, et al (1991); Alesina and Summers (1993); Posen (1993); Pollard (1993); and Debelle and Fisher (1995) have shown that the level of independence (legal, administrative, and instrument) of the monetary authority is an important institutional factor determines inflation, especially, in industrialized countries, while rate of turnover of central bank governors in developing countries was seen as an important factor influencing inflation. However, caution should be exercised in the interpretation of these findings, given the difficulty in measuring the actual level of independence of a central bank. The fiscal factors relate to the financing of budget deficits, largely through money creation process. Under this view, inflation is said to be caused by large fiscal imbalances, arising from inefficient revenue collection procedures and limited development of the financial markets, which tends to increase the reliance on seiniorage as a source of deficit financing (Agenor and Hoffmaister, 1997 and Essien, 2005). The monetary factors and demand side determinants include increases in the level of money supply in excess of domestic demand, monetization of oil receipts, interest rates, real income and exchange rate (Moser, 1995). Alesina and Summers (1993) prudent monetary management was also found to aid the reduction in the level and variability in inflation. The balance of payments or supply side factors, relate to the effects of exchange rate movements on the price level. Melberg (1992); Odusola and Akinlo (2001) and Essien (2005) opined that exchange rate devaluation or depreciation includes higher import prices, external shocks and accentuates inflationary expectations. There are three major types of inflation according to neo-Keynesians. The first is the demand-pull inflation, which occurs when aggregate demand is in excess of available supply (capacity). This phenomenon is also known as the Phillips curve inflation. The output gap can result from an increase in government purchases, increase in foreign price level, or increase in money supply.

**2.3 THEORETICAL REVIEW**

Theoretically, economists of different persuasions (Classists, Neo-classists, Keynesians, Post-Keynesians, Monetarists, Structuralists and Neostructuralists) have contributed copiously to the literature on inflation. On definition, inflation is persistent increases in the general level of prices (Bannock et al., 2003). Classical economists see money as just a “veil” in the sense that its increase would lead to a positive change in the general price level while leaving purchasing power of income, interest rate and output level unaffected (Javed et al., 2010). The neo-classical economists also believe that inflation can be engendered by an unchecked increases in the money supply (Javed et al., 2010). According to Weidenaar (1979) the monetary economists are of the view that once full-employment is attained, the only factor that can alter the price level is the availability of money in the economy. In other words, if the money in circulation in the economy increases two-fold, then the general price level would also increase two-fold. The Keynesian economists hold the view that with an economy experiencing underemployment, an expansion of money in circulation, may in the shortrun, spur aggregate demand, employment and output (Javed et al., 2010). In the longrun though, money supply in excess of potential output can be inflationary (Javed et al., 2010).Weidenaar (1979) also expressed the Keynesian perspective on inflation as a phenomenon resulting from excessive spending (at full-employment) relative to available supply of goods at current prices, thus causing prices to rise in order for the goods market to clear. Jhingan (2003) expressed the structuralist economists’ view on inflation as occurring in the longrun as a result of differences in some of the features of the service sector relative to the industrial sector. Such features are prices, productivity growth, elasticities of income and the wage rates between the two sectors. Bowman (2003) submitted that in explaining inflation, premium is put on costs by the post-Keynesians, thus they see wage demands by the unions, commodity prices set by the firms, prices of imports set by foreign producers and markup as the root causes of inflation. Commenting further, he submitted that the post – Keynesians disagree with the notion of a Wicksellian natural rate of interest which makes inflation to be constant, output operating at full-employment capacity and unemployment hovering around the natural rate. Under this regime, a downward deviation in interest rate would cause inflation and output to rise beyond full-employment and unemployment would reduce to below the natural rate. According to him, the post-Keynesians instead emphasise cost-push inflation which is the underlying cause of distributional conflict. Echoing a similar theme, Perry & Cline (2013) have submitted in their post-Keynesian and structuralist model that the variable that drives inflation the most is distributional conflict. Bowman (2003) agreed with this position taken by Perry & Cline (2013). Also agreeing, Filho (2000) concluded that to the post-Keynesians, neostructuralists and Marxists, distributional conflicts arising from concentration of capital and workers’ militancy will aggravate the susceptibility of the economy to inflation. According to them, in a regime where monetary and fiscal policies are not effective, and money supply is determined within the system, then monopolists and unionised labour wield a market power to determine the prices of goods and services without due regard for demand. As a result of this, inflation would emerge when there are increases in the markup or when the wage rate rises in excess of productivity gains (Filho, 2000). But how do the market power of oligopolistic/monopolistic business firms, unionised labour and import prices (degree to which these can be passed on to domestic prices) spur inflation? The market power of firms is derived from firms’ ability to practice markup pricing. In a perfect market, firms would produce at where marginal cost of production is equal to the market price which would make markup price to be equal to unity (Bowman, 2003; Shahor, 2011) and making the allocation of resources to be efficient (Shahor, 2011). However, in imperfect markets, firms wield the power to set prices at where marginal cost is lower than the market price, thus causing markup to exceed unity (Bowman, 2003 & Shahor 2011) causing inefficient allocation of resources (Shahor, 2011). So what are the factors which influence the ability of firms to practice markup pricing successfully? Taylor (2000) submitted that the amount of market power that firms believe or think they have and therefore can use to practice markup pricing, is purely a function of how well the product is differentiated from other products or how well other products can serve as substitutes to the product and on the response of other firms to the firm’s exercise of markup pricing power. Put differently, the pricing power of firms is a function of how other firms would react and on the utility maximising behaviour of consumers (Taylor, 2000). In explaining why inflation reduced in most of the advanced economies of the world in the 1990s in the face of robust economic conditions, Bowman (2003) argued that firms’ market power dwindled in those economies due to increased competition both domestically and internationally. He further mentioned the factors that can stimulate competition. These factors are globalisation, decreased regulation, new economy that is information technology driven and productivity growth. In other words, autarky, reduced deregulation, market structures that do not enjoy the spillovers of advances in information technology and loss of productivity may increase market power of firms. Disagreeing with the position that increased competition may reduce the pricing power of firms, Ball & Romer (2002) presented consumer search model to show that low price dispersion and therefore the effectiveness of consumer search as a channel that forces firms to lower mark-ups, suggesting that higher price dispersion makes consumer search to be costly and firms would therefore increase mark-up. Also, Taylor (2000) submitted that it is price persistence that determines the direction that the price level would move. He utilised a model of staggered pricing in which producers are assumed to set prices in advance. If for instance, marginal cost increases, and prices are sticky, producers believing that such increase is temporary, would not increase prices. But, if the cost increase is seen by producers as permanent, they will likely pass a great part of it on as price increases (Taylor, 2000). So high price dispersion, costly or inefficient search by consumers can influence markup pricing. Firms pricing power to practice markup pricing is profit-push variant of costpush inflation. Another variant of cost-push inflation is one induced by the market power of organised labour. This is called wage – push inflation. Sometimes, these two feed on each other in which case a wage-price spiral would ensue. According to Javed et al. (2010), whenever firms increase prices, the cost of living of wage earners tend to rise and in a bid to compensate for a loss in welfare, workers demand for higher wages which also forces business firms to increase the prices of their products in order to protect their profit margins. Some contributors claim though that it is organised labour that initiates the spiral. The market power of workers is derived from unionisation. Given a workforce of a known size, the number of the workers in the workforce that are members of unions is known as the union density of the workforce (Lye & McDonald, 2006). If many workers in the economy are members of labour unions, then it is said that the union intensity of such economic system is high. Viewed from the prism of post–Keynesian paradigm, workers may not be compensated based on the incremental contribution of labour to output and are therefore forced to resort to a united front and some hostilities in negotiating wages (Perry & Cline, 2013). So, it is through the process of collective bargaining that unionised labour presses home its wage demands that may sometimes be in excess of productivity growth. Usually, the increased wages garnered by one union through collective bargaining may not be limited to the industry that that union belongs. When producers in a certain industry acquiesce to the wage demands of labour in that industry, a reference wage is set and in assessing the value of the wage earned by members of a sister union in another industry, they compare such wage to the reference wage (Lye & McDonald, 2006) and uses it as a benchmark upon which the wage demands of the sister union would be based, thus aggravating inflation. It is not always as a result of the collective bargaining process of unionised labour that may trigger wage increases. For instance, Jaumotte & Morsy (2012) have submitted that productivity growth in the traded goods sector may encourage labour from non-traded goods sector to move to the former sector. A factor that may prevent this from happening is if producers raise wages in the sector with lower productivity. The effect of this would be that producers in the non-traded goods sector must raise the relative prices of their goods, thereby causing the overall price level in the economy to rise. This is what Mihaljek & Saxena (2010) have referred to as the “Balassa – Samuelson effect”. Apart from the causes of inflation hitherto discussed, some strands of literature have mentioned that inflation can be caused by the pass-through of import prices to domestic inflation and also have identified some exogenous supply shocks as engendering inflation. Exchange rate pass-through (ERPT) is the extent to which a change in the exchange rate between an exporting and an importing country would affect the importing country’s import prices (Campa & Goldberg, 2001). Many contributors have pointed to different factors as the causes of ERPT. Benigno & Faia (2010) mentioned the degree of market concentration, increase in the share of foreign products sold in a particular industry (which may stimulate competition) and globalisation as the causes of ERPT. Taylor (2000) saw the cause of ERPT as inflation persistence. It may be caused by microeconomic factors such as demand elasticities and market structures (Choudhri & Hakura, 2006). It may even be caused by low autonomy and integration (Holmes, 2006) in which case the pursuit of an independent monetary policy may be difficult. As for some exogenous supply shocks, it can be conceived of as events that suddenly change the price of a commodity or service (Javed et al., 2010). A good example of this was the spike in the price of crude oil that happened in the 1970s.

**2.4 EMPIRICAL REVIEW**

A plethora of literature exists that looked at issues in the areas of cost-push (markup pricing of firms, and the market power of unionised labour), passthrough of import prices to domestic inflation and exogenous supply shocks. Javed et al. (2010) sought to examine the validity of cost-push and monetarist diagnoses of inflation in the economy of Pakistan from 1971 to 1972 and 2006 to 2007. Quarterly data on consumer price index , wholesale price index , Gross Domestic Product , exchange rate, wheat support price, annual wage in the perennial industries , value of imported raw materials , narrow money supply , broad money supply and dummy variable that assumed a value of 1 when natural disaster occurs and a value of zero (0) when otherwise. Two OLS regressions were performed. One was to show the behaviour of consumer price index when exposed to supply-side or cost-push (wage and profit) influences and the other was to determine the response of consumer price index to changes in money supply and the lagged value of consumer price index. The results showed that exchange rate, annual wage in the perennial industries, value of imported raw materials, dummy for natural disasters, the lagged value of broad money and the lagged value of consumer price index all influenced consumer price index in the Pakistani economy. Perry & Cline (2013) investigated the causes of the “great inflation moderation” of the period 1982 to 2006 in the US. The results of this study can be interpreted to mean that the variables that caused the inflation moderation can also cause inflation aggravation. Following the postKeynesian tradition, data on consumer price index, Taylor rule differentials as captured by the deviation of target interest rate from the target rate in moderating the output gap, exchange rate, import prices and wages were collected. A Vector Autoregression (VAR) model was used to determine the effects of innovations in Taylor rule differentials, oil prices, exchange rate, import prices and wages on consumer price index. The results of the impulseresponse and the variance decomposition showed that the great moderation was caused by declining wages and import prices. Lye & McDonald (2006) used a standard Philips curve range model to show that in the 1970s Australia, there was increased union power ( union density ). During this period, owing to the favourable disposition of the Arbitration Commission towards labour due to increased union density, labour was able to garner increased unemployment benefit (which was the reservation wage or reference wage upon which bargained wages were based). This caused the inflation barrier to shift to a higher rate of unemployment. In the 1980s, due to reforms in the labour market, union power waned and this shifted the inflation barrier to lower levels of unemployment. Ogundipe & Egbetokun (2013) sought to determine the effect of exchange rate shocks on consumer prices in Nigeria. Collecting data on the nominal effective exchange rate, the real official exchange rate, the money supply and the consumer price index, Structural Vector Autoregression was used to determine the response of consumer price index to a one standard deviation shock to nominal effective exchange rate, the real official exchange rate, the money supply. The results showed that exchange rate pass-through in the country is fairly large. Audu & Amaegberi (2013) evaluated the effect of exchange rate fluctuation on inflation targeting in the Nigerian economy from 1970 to 2012. Using error correction model, they showed that interest rate and exchange rate explained inflation in the country. Akinbobola (2012) investigated if longrun relationships exist between monetary growth, exchange rate and inflation in Nigeria over the period 1986 to 2008. He utilised a Vector Error Correction Mechanism model to demonstrate that inflationary pressure in Nigeria is as a result of exchange rate and monetary policy, although real output has some positive effect in the longrun. Boamah (2013) examined the extent and speed to exchange rate pass-through to inflation in countries of the proposed West African Monetary Zone (WAMZ). Monthly data on average bilateral exchange rate against the US dollar, consumer price index as proxy for import prices “as there are no available data on import prices” ( Boamah, 2013; p.76) were collected. Monthly data on inflation in the US were also collected. Vector Autoregressive Model was used to determine the extent and speed of exchange rate pass-through to inflation in these countries. The results of the impulse-response function showed that a high and fast exchange rate passthrough suggested that monetary policy may not do much to stabilise real exchange rates as changes in nominal exchange rate is immediately reflected in domestic consumer prices although Nigeria (the largest economy in the proposed union) has the lowest exchange rate pass-through and the extent of the pass-through is almost negligible. The results of the variance decomposition which highlighted the relative importance of the different variables in explaining domestic inflation, showed that the largest share of variation in domestic prices is explained by changes in prices itself and it revealed that Nigeria adjusted relatively quickly to restore the equilibrium relation when there is a short-term deviation from the long-run pass-through compared to other countries. Holmes (2006) investigated the degree of pass-through from the US dollar exchange rate to consumer prices in the European Union (EU). Monthly data on consumer price index, the nominal exchange rate (domestic price of foreign currency) and foreign price index on 12 EU countries were collected. Panel data cointegration technique was used to measure whether there was longrun pass-through from the US dollar exchange rate to consumer prices in the EU. The results showed that the extent of exchange rate pass-through from US dollars to EU consumer prices declined and one of the reasons for this was ascribable to the credibility of monetary policy. Maku & Adelowokan (2013) examined the macroeconomic determinants of inflation rate in Nigeria between 1970 and 2011. Autoregressive model was used to show that real output growth, broad money supply growth and previous inflation exerted positive influence on current inflation rate in Nigeria since independence till 2011 fiscal year. Ezeabasili et al. (2012) looked at the effect of fiscal deficits on inflation in Nigeria using a data that spanned 36 years i.e. from 1970 to 2006. They used Vector Autoregression model to show that there exist a positive but insignificant relationship between fiscal deficit and inflation but were able to show that there is a positive longrun relationship between money supply and inflation in Nigeria.

 **CHAPTER THREE**

 **RESEARCH METHODOLOGY**

* 1. **INTRODUCTION**

This chapter deals with the method used in collecting data required in carrying out this research work it explains the procedures that were followed and the instrument used in collecting data.

* 1. **SOURCES OF DATA COLLECTION**

Data were collected from two main sources namely:

1. Primary source and
2. Secondary source

**Primary source:**

These are materials of statistical investigation which were collected by the research for a particular purpose. They can be obtained through a survey, observation questionnaire or as experiment, the researcher has adopted the questionnaire method for this study.

**Secondary source:**

These are data from textbook Journal handset etc. they arise as byproducts of the same other purposes. Example administration, various other unpublished works and write ups were also used.

* 1. **POPULATION OF THE STUDY**

Population of a study is a group of persons or aggregate items, things the researcher is interested in getting information for the study causes and effect and solution to inflation in Nigeria. The researchers randomly select 200 staffs of central banks in Nigeria as the population of the study.

* 1. **SAMPLE AND SAMPLING PROCEDURE**

Sample is the set people or items which constitute part of a given population sampling. Due to large size of the target population, the researcher used the Taro Yamani formula to arrive at the sample population of the study.

n= N

 1+N(e)2

n= 200

1+200(0.05)2

= 200

1+200(0.0025)

= 200 200

1+0.5 = 1.5 = 133.

**3.5 INSTRUMENT FOR DATA COLLECTION**

The major research instrument used is the questionnaires. This was appropriately moderated. The managers were administered with the questionnaires to complete, with or without disclosing their identities. The questionnaire was designed to obtain sufficient and relevant information from the respondents. The primary data contained information extracted from the questionnaires in which the respondents were required to give specific answer to a question by ticking in front of an appropriate answer and administered the same on staffs of the financial institutions: The questionnaires contained about 16 structured questions which was divided into sections A and B.

* 1. **VALIDATION OF THE RESEARCH INSTRUMENT**

The questionnaire used as the research instrument was subjected to face its validation. This research instrument (questionnaire) adopted was adequately checked and validated by the supervisor his contributions and corrections were included into the final draft of the research instrument used.

* 1. **METHOD OF DATA ANALYSIS**

The data collected was not an end in itself but it served as a means to an end. The end being the use of the required data to understand the various situations, it is with a view to making valuable recommendations and contributions. To this end, the data collected has to be analysis for any meaningful interpretation to come out with some results. It is for this reason that the following methods were adopted in the research project for the analysis of the data collected. For a comprehensive analysis of data collected, emphasis was laid on the use of absolute numbers frequencies of responses and percentages. Answers to the research questions were provided through the comparison of the percentage of workers response to each statement in the questionnaire related to any specified question being considered.

Frequency in this study refers to the arrangement of responses in order of magnitude or occurrence while percentage refers to the arrangements of the responses in order of their proportion.

The simple percentage method is believed to be straight forward easy to interpret and understand method. The researcher therefore chooses the simple percentage as the method to use. The formula for percentage is shown as.

% = f/N x 100/1

Where f = frequency of respondents response

N = Total Number of response of the sample

100 = Consistency in the percentage of respondents for each item contained in questions.

 **CHAPTER FOUR**

 **PRESENTATION ANALYSIS INTERPRETATION OF DATA**

**4.1 INTRODUCTION**

Efforts will be made at this stage to present, analyze and interpret the data collected during the field survey. This presentation will be based on the responses from the completed questionnaires. The result of this exercise will be summarized in tabular forms for easy references and analysis. It will also show answers to questions relating to the research questions for this research study. The researcher employed simple percentage in the analysis.

**DATA ANALYSIS**

The data collected from the respondents were analyzed in tabular form with simple percentage for easy understanding.

A total of 133 (one hundred and thirty three) questionnaires were distributed and 133 questionnaires were returned.

Question 1

Gender distribution of the respondents.

**TABLE I**

|  |
| --- |
| **Gender distribution of the respondents** |
| Response | Frequency | Percent | Valid Percent | Cumulative Percent |
| Valid | Male | 77 | 57.9 | 57.9 | 57.9 |
| Female | 56 | 42.1 | 42.1 | 100.0 |
| Total | 133 | 100.0 | 100.0 |  |

From the above table it shows that 57.9% of the respondents were male while 42.1% of the respondents were female.

Question 2

The positions held by respondents

**TABLE II**

|  |
| --- |
| **The positions held by respondents** |
| Response | Frequency | Percent | Valid Percent | Cumulative Percent |
| **Valid** | Marketers  | 37 | 27.8 | 27.8 | 27.8 |
| Cashiers  | 50 | 37.6 | 37.6 | 65.4 |
| Auditors  | 23 | 17.3 | 17.3 | 82.7 |
| Security officers  | 23 | 17.3 | 17.3 | 100.0 |
| Total | 133 | 100.0 | 100.0 |  |

The above tables shown that 37 respondents which represents 27.8% of the respondents are Marketers, 50 respondents which represents 37.6 % are Cashiers, 23 respondents which represents 17. 3% of the respondents are Auditors, while 23 respondents which represents 17.3% of the respondents are Security officers .

**TEST OF HYPOTHESES ONE**

Inflation rate has no effect on the economic growth of Nigeria

**Table III**

|  |
| --- |
| **Inflation rate has no effect on the economic growth of Nigeria** |
|  |
| Response  | Observed N | Expected N | Residual |
| Agreed | 40 | 33.3 | 6.8 |
| strongly agreed | 50 | 33.3 | 16.8 |
| Disagreed | 26 | 33.3 | -7.3 |
| strongly disagreed | 17 | 33.3 | -16.3 |
| Total | 133 |  |  |
|  |  |  |  |
| **Test Statistics** |
|  | Inflation rate has no effect on the economic growth of Nigeria |
| Chi-Square | 19.331a |
| Df | 3 |
| Asymp. Sig. | .000 |
| a. 0 cells (0.0%) have expected frequencies less than 5. The minimum expected cell frequency is 33.3. |

Decision rule:

There researcher therefore reject the null hypothesis which states that Inflation rate has no effect on the economic growth of Nigeria.

Therefore the researcher accepted the alternate hypothesis which states that Inflation rate has effect on the economic growth of Nigeria.

**TEST OF HYPOTHESIS TWO**

Inflation does not affect significantly the economic growth of Nigeria.

**Table IV**

|  |
| --- |
| **Inflation does not affect significantly the economic growth of Nigeria** |
| Response  | Observed N | Expected N | Residual |
| Agreed | 40 | 33.3 | 6.8 |
| strongly agreed | 50 | 33.3 | 16.8 |
| Disagreed | 26 | 33.3 | -7.3 |
| strongly disagreed | 17 | 33.3 | -16.3 |
| Total | 133 |  |  |

|  |
| --- |
| **Test Statistics** |
|  | Inflation does not affect significantly the economic growth of Nigeria  |
| Chi-Square | 19.331a |
| Df | 3 |
| Asymp. Sig. | .000 |
| a. 0 cells (0.0%) have expected frequencies less than 5. The minimum expected cell frequency is 33.3. |

Decision rule:

There researcher therefore reject the null hypothesis that states that Inflation does not affect significantly the economic growth of Nigeria as the calculated value of 28.211 is greater than the critical value of 5.99.

Therefore the alternate hypothesis is accepted that states that Inflation affect significantly the economic growth of Nigeria.

**TEST OF HYPOTHESIS THREE**

Inflation does not affect significantly capital formation in Nigeria.

**Table IV**

|  |
| --- |
| **Inflation does not affect significantly capital formation in Nigeria.** |
| Response  | Observed N | Expected N | Residual |
| Agreed | 40 | 33.3 | 6.8 |
| strongly agreed | 50 | 33.3 | 16.8 |
| Disagreed | 26 | 33.3 | -7.3 |
| strongly disagreed | 17 | 33.3 | -16.3 |
| Total | 133 |  |  |

|  |
| --- |
| **Test Statistics** |
|  | Inflation does not affect significantly capital formation in Nigeria.  |
| Chi-Square | 19.331a |
| Df | 3 |
| Asymp. Sig. | .000 |
| a. 0 cells (0.0%) have expected frequencies less than 5. The minimum expected cell frequency is 33.3. |

Decision rule:

There researcher therefore reject the null hypothesis that states that Inflation does not affect significantly capital formation in Nigeria as the calculated value of 28.211 is greater than the critical value of 5.99.

Therefore the alternate hypothesis is accepted that states that Inflation affect significantly capital formation in Nigeria.

 **CHAPTER FIVE**

 **SUMMARY CONCLUSION AND RECOMMENDATION**

**5.1 INTRODUCTION**

It is pertinent to note that this research was aimed at finding out the causes effect and solution to inflation in Nigeria”.

In the preceding chapter, the relevant data collected for this study were presented, critically analyzed and appropriate interpretation given. In this chapter, certain recommendations made which in the opinion of the researcher will be of benefits in addressing the challenges associated with inflation and the Nigerian economy.

**5.2 SUMMARY**

Firstly, inflation in Nigeria during the study period was as a result of increases in real exchange rates which probably had origins in either endogenous demand shocks or exogenous foreign producer pricing shocks which caused the marginal costs of Nigerian producers to increase. Secondly, there existed inflation persistence in the economy that was not effectively curtailed by the monetary authorities. Thirdly, as a result of this persistence, Nigerian businessmen were able to pass the increases in marginal costs of production on to the Nigerian consumers in form of increases in the prices of consumer durables and non-durables produced in the country.

**5.3 Conclusion**

It is very obvious that Nigerian government uses monetary and fiscal policies measures as tools for combating inflation and meeting various macro-economic objectives. Evaluation of these policies showed that they do not work due to negligence of the correlation that exists between government expenditure, money supply and inflation. Expenditure management and budget discipline should be taken seriously by Nigerian government. This can be achieved by ensuring that all expenditures made match with revenue. Nigerian government should also act productively in balancing its fiscal and monetary policy as well as institutional intervention with expectation on inflation. This will prevent unexpected and unplanned reaction of prices which may have a counter-productive impact on the economy.

**5.4 Recommendation**

Based on the conclusions the following are recommended:

1. Substitution of Domestically Produced Goods for Imported Goods It is very true that Nigerians rely heavily on foreign sources for the supplies of finished goods consumed by households and raw-materials used by the industries.
2. Adoption of a Consistent Monetary Policy Stance The monetary policy stance of any nation must be seen as credible. In other words, once the policy has been pronounced, strenuous efforts must be made to follow the policy through to logical conclusions and results without wanton abandonment.

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**QUESTIONNAIRE**

**INSTRUCTION**

Please tick or fill in where necessary as the case may be.

Section A

1. Gender of respondent

A male { }

B female { }

1. Age distribution of respondents
2. 15-20 { }
3. 21-30 { }
4. 31-40 { }
5. 41-50 { }
6. 51 and above { }
7. Marital status of respondents?
8. married [ ]
9. single [ ]
10. divorce [ ]
11. Educational qualification off respondents
12. SSCE/OND { }
13. HND/BSC { }
14. PGD/MSC { }
15. PHD { }

Others……………………………….

1. How long have you been in the state?
2. 0-2 years { }
3. 3-5 years { }
4. 6-11 years { }
5. 11 years and above……….

(6) How long have you been in management team?

1. 0-2 years { }
2. 3-5 years { }
3. 6-11 years { }
4. 11 years and above……….

**SECTION B**

1. How does Inflation impact on economic growth in Nigeria?
2. Agrees { }
3. Strongly agreed { }
4. Disagreed { }
5. Strongly disagreed { }
6. How is the trend of inflation in Nigeria?

(a) Agrees { }

(b) Strongly agreed { }

(c) Disagreed { }

(d) Strongly disagreed { }

1. What is the effect of inflation on the level of capital formation in Nigeria?
2. Agreed { }
3. Strongly agreed { }
4. Disagreed { }
5. Strongly disagreed { }
6. How does inflation affect the consumption expenditure of Nigerian households?
7. Agreed { }
8. Strongly agreed { }
9. Disagreed { }
10. Strongly disagreed { }
11. Inflation does not affect significantly the economic growth of Nigeria?
12. Agreed { }
13. Strongly agreed { }
14. Disagreed { }
15. Strongly disagreed { }
16. Inflation affect significantly the economic growth of Nigeria?
17. Agreed { }
18. Strongly agreed { }
19. Disagreed { }
20. Strongly disagreed { }
21. Inflation does not affect significantly capital formation in Nigeria?
22. Agreed { }
23. Strongly agreed { }
24. Disagreed { }
25. Strongly disagreed { }
26. Inflation affects significantly capital formation in Nigeria?
27. Agreed { }
28. Strongly agreed { }
29. Disagreed { }
30. Strongly disagreed { }
31. There is no significant relationship between inflation and consumption expenditure of people in Nigeria?
32. Agreed { }
33. Strongly agreed { }
34. Disagreed { }
35. Strongly disagreed { }