External Sector Aggregate and Inclusive Growth in Nigeria

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Abstract
External sector aggregate, particularly imports, exports, exchange rate, and foreign direct investment are key to achieving inclusive growth, defined as growth that improves people's lives in many ways like income, education, and health. In Nigeria, these factors are expected to strongly influence inclusive development, but their real impact has been limited. This study looked at how these external sector aggregates affect inclusive growth in Nigeria from 1981 to 2023. The data for this study came from reports by Nigeria's central bank and included information on the human development index, exchange rate, foreign direct investment, imports, and exports. The study used an Autoregressive Distributed Lag - ARDL Bounds testing technique. The results showed that there is a long-term connection between these factors. In the long run, exchange rate and foreign direct investment have a negative but not significant effect on the human development index. On the other hand, imports and exports have a positive but not significant effect. In the short run, exchange rate and foreign direct investment have a negative effect on the human development index. Exchange rate was not statistically significant, but foreign direct investment was at the usual level of significance. Imports had a positive effect, and this was statistically significant, while exports did not. The study suggested that the government should focus more on improving the quality and type of foreign direct investment rather than just increasing the amount. This means directing foreign investment towards areas that create jobs and benefit society, like manufacturing, agriculture, healthcare, and education. It also recommended strengthening local content policies and improving the ability of the country to use foreign investment through better skills and stronger institutions. To make trade more effective, the government should improve trade processes, carefully choose what is imported, encourage a variety of exports, and build better systems and rules to get the most benefits from trade in both the short and long term.

Keywords: External Sector, Inclusive Growth, Foreign Direct Investment, Exports, Imports, Exchange Rate, Nigeria

I. Introduction

The Nigerian economy is greatly affected by how it interacts with the global economy through important external sector aggregate such as imports, exports, exchange rates, and foreign investments. These variables are very important in shaping the country's overall economic health and development. In the past, economic success was mainly measured by Gross Domestic Product (GDP). But now, there's more focus on inclusive growth, which means making sure growth benefits everyone, not just a few. This includes fair income sharing, reducing poverty, and improving people's quality of life (Anand, Mishra, & Peiris, 2013).

To understand how the external sector aggregate affects inclusive growth in Nigeria, we look at how factors like trade, exchange rates, capital inflows, and money sent back from abroad impact jobs, income fairness, and access to opportunities. These factors decide whether the benefits from the external sector spread widely or stay within certain groups (Todaro & Smith, 2020). One important way the external sector aggregate affects inclusive growth is through international trade -[both exports and imports. Expanding exports, especially in areas that use a lot of labour, can create jobs, raise incomes, and cut poverty. But in Nigeria, most exports are crude oil, which requires a lot of capital and doesn't create many jobs. So the benefits of growing exports for inclusive growth are limited. On the import side, getting cheaper goods can help people's well-being, but relying too much on imports can hurt local industries and reduce job chances (World Bank, 2020).

Furthermore, changes in the exchange rate affect how competitive local industries are. If the naira loses value, it can make exports cheaper and imports more expensive. This might help local businesses and create jobs, but it can also raise the cost of imported goods, leading to inflation that hits poor families harder. So, the exchange rate can have both good and bad effects on fair and widespread growth, depending on how stable the economy is (Mankiw, 2021). Also, foreign direct investment (FDI) plays a big role in how the economy grows. When foreign companies invest, they bring in money, new technology, and better management skills. If these investments are in areas that connect well with the local economy, they can improve productivity, create jobs, and help workers learn new skills. In Nigeria, FDI in telecom and services has helped create jobs and encourage new ideas. But FDI in the oil industry often does

not connect well with the local economy, so it doesn't help growth as much (United Nations Conference on Trade and Development, 2021).

The balance of payments (BOP) also influences the economy. When the BOP is stable and good, there is enough foreign currency to import needed equipment and keep the economy steady. But if the BOP is always bad, it can cause the currency to lose value, push up prices, and make it harder for the government to fund important programs. These economic problems can harm inclusive growth by making poverty and inequality worse (International Monetary Fund, 2020).

Remittances sent by Nigerians living abroad give families extra money, which they can use for everyday expenses, schooling, medical care, and small business investments. These money flows are usually more reliable than other types of foreign money and help reduce poverty and improve people's living conditions, especially in rural regions (World Bank, 2022). The prices of goods and the cost of oil also affect the country's growth by influencing how much money comes in from outside. Since Nigeria depends a lot on selling oil, changes in global oil prices greatly affect the government's income and the amount of foreign currency the country earns. When oil prices are high, more money is available for public projects and services like schools and hospitals. But when oil prices drop, there's less money, which can slow down development and make it harder for everyone to benefit (Central Bank of Nigeria, 2021).

Another way the country's foreign sector affects growth is by bringing in new technology and sharing useful knowledge. By being open to trade and welcoming foreign investments, Nigeria can get access to better tools and ideas that improve how efficiently things are done. If these technologies spread across different sectors, they can boost productivity and create new job and business chances. But if people lack proper skills or if the government systems are not strong enough, these benefits might not reach everyone equally, which limits how inclusive the growth is (Grossman & Helpman, 1991).

Importantly, government revenue and how the government spends it are an indirect but important way that affects growth. The external part of the economy, especially oil exports, brings in a lot of money for the Nigerian government. If this money is used well, it can be put into areas like education, healthcare, building roads, and helping people in need, which can help the whole country grow. However, if the government isn't run well, there is corruption, or the

money comes and goes a lot, it can stop these good things from happening (Sala-i-Martin & Subramanian, 2013). Money coming from outside can help financial markets, make it easier for businesses to get loans, and encourage new businesses. But, if there are sudden problems in the global economy, it can make the country's economy more unstable, especially if the country's financial system is not strong. It's important to make sure that this financial development helps more people, especially small businesses and those who have been left out, so that everyone can benefit from being connected to the outside economy (Organisation for Economic Co-operation and Development, 2015).

From the above, it's clear that the overall role of the external part of the economy in helping Nigeria grow in a way that includes everyone happens through several connected ways, like trade, exchange rates, investments, money sent by people living abroad, and how the government handles money. Even though Nigeria has made a lot of money from exports and foreign investments, especially in the oil industry, the good results for people's well-being and how income is spread out have not been very strong (Adeniyi et al., 2012). Also, high levels of imports haven't led to enough local industries or jobs. Unstable exchange rates have made these problems worse by making imports more expensive and creating uncertainty in the economy (Obadan, 2006). According to Adeniyi et al. (2012), Nigeria's external part of the economy has some key problems, like being too dependent on oil, needing a lot of imports, and having unstable exchange rates. These issues stop the external part of the economy from helping grow in a way that includes everyone.

Studies also show different results when looking at how external sector variables affect the economy. Some studies say exports help growth, while others say imports, exchange rates, and foreign investments don't help much or even hurt growth (Akpan & Atan, 2012). These mixed results make it hard to know exactly how the external sector aggregate helps the Nigerian economy grow in a way that includes everyone. For this reason, it's important to carefully look at how these external factors affect inclusive growth in Nigeria spanning 1981 to 2023. The rest of the paper is organized into sections on literature review, materials and methods, results and discussion, and finally, conclusion and recommendations.

2. Literature Review

Conceptual Clarification

External Sector Aggregate

The external sector aggregate refers to all the activities a country has with other countries around the world. These activities include things like exporting goods, importing goods, how much money is exchanged between countries, foreign investments, money sent back home by workers living abroad, and how the country's overall money balance looks. This helps us understand how much a country depends on the world economy and how much it can be affected by changes happening globally (Krugman & Obstfeld, 2009). From a national income accounting perspective, the external sector aggregate is embedded in the identity $Y = C + I + G + (X - M)$, where C stands for consumption, I for investment, G for government spending, and (X - M) is the difference between what the country sells to others (exports) and what it buys from others (imports). This part, called net exports, shows how much the country's trade with the rest of the world helps or hurts its overall economic output. If a country sells more than it buys, it boosts its total income. If it buys more than it sells, it lowers total income. This shows that the external sector plays an important role in how the country's economy grows, how many jobs are created, and how stable the economy is overall (Blanchard, 2017).

Another key part of the external sector aggregate is the balance of payments (BOP), which keeps track of all economic activities between a country's residents and the rest of the world. The BOP includes the current account, which covers trade in goods and services, income, and transfers, and the capital and financial account, which deals with investments and financial transfers. Together, these accounts give a complete view of a country's financial position with the rest of the world and how sustainable it is (International Monetary Fund, 2020). Exchange rates are also an important part of the external sector. The exchange rate shows how much a country's currency is worth compared to others. This affects the prices of goods a country exports and imports. When the currency of a country loses value, the country’s exports become cheaper and imports more expensive, this can improve the trade balance. But how much this affects trade depends on things like how much people want to buy goods and the structure of the economy (Mankiw, 2021).

The flows of capital, such as direct investment form foreign countries (FDI) and portfolio investments are also part of the external sector. These flows help fund domestic investments, bring in new technologies, and boost economic growth. However, they can also lead to instability, especially in developing countries where sudden loss of capital can disrupt financial systems (Todaro & Smith, 2020).

Remittances and foreign aid also play a role in the external sector, especially in countries like Nigeria. Money sent back by people living abroad is a reliable source of foreign currency and helps support families. Foreign aid can fund development projects. These income sources can help countries deal with economic problems and reduce trade deficits (World Bank, 2022). Nigeria's economy relies a lot on selling crude oil, which makes it very sensitive to changes in the price of oil around the world. Because of this, when oil prices go up or down, it greatly affects how much money the government gets, the value of the currency, and the overall health of the economy. Because of this risk, many discussions about economic policy focus on spreading out the types of goods and services Nigeria exports, to make the economy more stable and less dependent on just oil. The external sector, which includes all the ways Nigeria interacts with other countries economically, helps show how global economic factors influence the country's domestic situation. By looking at trade, money coming in and out of the country, currency values, and money sent from abroad, leaders can make better decisions to keep the economy steady, grow it in a way that benefits everyone, and protect it from sudden changes in the global market.

Inclusive Growth

Inclusive growth is a type of economic growth that benefits everyone, especially those who are poorer or have fewer opportunities. It is not just about making the economy grow faster, but also about making sure that the benefits of growth are shared fairly by all people, no matter where they live or how much money they have. Unlike older ways of thinking about growth that only look at how much the economy produces (like GDP), inclusive growth also looks at how evenly the growth is spread. This means that people from different parts of the country, different jobs, and different income levels should all be able to share in the good things that come from economic growth (Anand, Mishra, & Peiris, 2013).

At the heart of inclusive growth is creating jobs that people can use to support themselves and their families. Just having a growing economy doesn't automatically mean people are better off if they don't have stable, well-paying jobs. That's why inclusive growth focuses on areas that can provide jobs to many people, especially in places where many people are not working or are working in poor conditions (World Bank, 2009).

Another important part of inclusive growth is making sure everyone has access to basic things like education, healthcare, banking, and good roads. When people have access to these things, they can improve their skills, take better care of themselves, and be more active in the economy. Without equal access, some people may not get the support they need to move forward, which can keep them in poverty and prevent the growth from being truly inclusive (Rauniyar & Kanbur, 2010).

Inclusive growth also means working to reduce the gap between rich and poor. Having some difference in income is normal, but if the gap gets too big, it can cause problems. For example, it can make people feel angry or disconnected from each other, and it can stop the economy from growing as much as it could. To help with this, governments use different tools like taxes that take more from those who have more, programs that help the poor, and support for specific groups that need it most. These efforts help make sure that the benefits of growth are shared more fairly (Organisation for Economic Co-operation and Development, 2015).

Interestingly, inclusive growth focuses on making sure that everyone benefits from economic progress, especially in different areas and among different groups of people. In many developing countries, most of the growth happens in cities or places with lots of natural resources, which leaves rural and less privileged areas behind. Inclusive growth aims to fix this by helping rural areas develop, supporting small and medium businesses, and giving more attention to regions that are not doing as well (United Nations Development Programme, 2017). Another important part of inclusive growth is sustainability. This means that economic progress should not harm the environment or the future. It also means that the economy and society should be stable enough to support future generations. If growth uses up natural resources too fast or creates long-term problems, it can’t really be called inclusive (United Nations, 2015).

In countries like Nigeria, inclusive growth is especially important because there is still a lot of poverty, people without jobs, and big differences in wealth, even when the economy is

growing. To achieve inclusive growth, there needs to be focused efforts to make the economy more varied, improve how the government works, build stronger systems, and invest in education and health. If these steps aren't taken, growth may only help a few areas, like the oil industry, and not make a real difference for most people (Central Bank of Nigeria, 2022). Overall, inclusive growth gives a better way to look at how well an economy is doing than just looking at how much it produces. By focusing on fairness, equal opportunities, and long-term stability, it helps make sure that economic progress leads to better lives for everyone.

Theoretical Review

The Dependency Theory

Dependency theory argues that there is an unfair relationship between rich, developed countries and poorer, developing countries. This theory states that money, resources, and value usually move from poorer countries to richer ones, which makes the rich countries wealthier while making it harder for poorer nations to grow and develop. This unfair system creates a situation where developing countries depend a lot on foreign markets, outside money, and imported technology to keep their economies going (Frank, 1967; Dos Santos, 1970).

The main idea of this theory is that being poor isn't natural it's a result of past exploitation and being forced into the global capitalist system. Colonial rule and trade patterns after independence made many developing countries focus on exporting basic goods and importing made products. This setup stops them from developing their own industries and makes them depend on foreign countries, which makes it hard for them to grow on their own (Amin, 1976). When looking at the external part of an economy like exports, imports, foreign investments, and currency values this theory shows that these parts often show and support the idea of dependency. For example, an economy that mainly exports one type of raw material is at risk when the price of that material changes in the world market. This dependence means that the external part of the economy might not help the country grow in the long-term, but instead, add to economic problems (Todaro & Smith, 2020).

In Nigeria, the external part of the economy is mostly based on oil exports, which fits with what Dependency Theory predicts. Nigeria's heavy reliance on oil makes it vulnerable to changes in global oil prices and prevents the country from developing a more varied economy.

This situation means that changes in markets controlled by wealthy countries affect Nigeria's money balance, currency value, and overall economic health (Central Bank of Nigeria, 2021).

Furthermore, the theory talks about how multinational companies and foreign investment affect the external part of the economy. While foreign direct investment can bring in money and new technology, it can also lead to profits being sent back overseas and not much local growth. In Nigeria, many oil companies are owned by foreign firms, which means the country might not get as much benefit from this investment. It also means that Nigeria depends a lot on foreign knowledge and money (United Nations Conference on Trade and Development, 2019). When this kind of growth is linked to inclusive growth, it suggests that growth driven from outside the country may not help everyone equally.

In Nigeria, oil exports have helped the economy grow, but the benefits have not been shared fairly. There are still high levels of poverty, joblessness, and inequality, which shows that growth from the external sector has not been inclusive. This fits with the theory's idea that dependency on foreign actors and elites tends to concentrate wealth rather than spread it out (Oxfam, 2017).

The theory also explains how depending on imports and foreign goods can hurt local industries like manufacturing and agriculture. This makes it harder to create jobs and gives fewer people a chance to be part of the economy, which is necessary for inclusive growth. In Nigeria, imported goods have often pushed out local businesses, making it harder for them to create jobs and help the economy grow fairly (Ajakaiye & Page, 2012). To support inclusive growth, the theory suggests that Nigeria should reduce its heavy reliance on the external sector by diversifying its economy, developing local industries, and building up its own productive abilities. Policies that help add value, support local businesses, and manage foreign investment can help change the external sector from a source of dependence into a force for long-term and inclusive development (World Bank, 2020).

Several scholars have questioned the dependency theory, pointing out issues with its basic ideas, how strong its analysis is, and whether it still applies to today's global economy. For example, Chibber (2013) said the theory focuses too much on outside forces and doesn't consider how local institutions and the government's ability to act can influence a country's development. Others, like Gereffi (2021), who study global value chains, argue that developing countries aren't

stuck in a poor position forever, as many have managed to move up in the global production system. Even with these criticisms, the dependency theory still helps explain how Nigeria's connection to international markets affects its ability to achieve broad-based growth. It shows how relying too much on outside influences can hold back development. To make sure growth benefits everyone and builds long-term economic strength, it's important to deal with these structural problems.

Endogenous Growth Theory

Endogenous growth theory is a modern way of understanding how economies grow over time. It says that long-term economic growth comes mostly from things inside an economy, not from outside forces. This is different from older models like the Solow model, which focus on things like savings and population growth Romer, 1986; Lucas, 1988). Endogenous growth theory focuses on factors like education, innovation, the spread of knowledge, and technological improvements as the main reasons for continued growth. The theory suggests that spending on things like education, research, and strong institutions leads to more growth because knowledge can be used by many people without being used up. This means that when one company or person creates new ideas, others can also benefit from them, which helps the whole economy grow. Because of this, economies that invest more in education and innovation usually see better productivity and long-term growth. This approach encourages policies that support building up the skills and creativity within a country rather than just relying on outside help (Aghion & Howitt, 1992).

Regarding the external sector as a whole, endogenous growth theory suggests that parts of the external sector like trade, foreign direct investment (FDI), and technology transfer can help a country grow more, but only if the country has enough capacity to absorb and use these things. In simple terms, the advantages of opening up to the world depend on how well the local economy can learn, adapt, and come up with new ideas. If a country doesn't have strong institutions or enough skilled people, the effects of engaging with the outside world might not be good for growth, or even harmful (Grossman & Helpman, 1991).

In the case of Nigeria, the external sector includes things like exports, imports, exchange rates, and capital flows. If used properly, these can help the country grow. For example, exports

can encourage local businesses to produce more and learn new ways of doing things. Imports of machinery and technology can make businesses more efficient. However, for these benefits to happen, Nigeria needs to take in new knowledge and apply it within the country through education, training, and good policies (Central Bank of Nigeria, 2022).

Foreign direct investment is also important in this growth model. It brings in not just money, but also new technologies, better management practices, and ideas for innovation. In Nigeria, FDI in areas like telecom and services has helped improve productivity. But the benefits differ between sectors. For instance, in industries like oil, the effects are often limited because there's little connection between the foreign investment and the rest of the local economy (United Nations Conference on Trade and Development, 2021).

When thinking about inclusive growth, endogenous growth theory says that for growth to be lasting and fair, the country needs to invest in people's skills and give everyone a chance to take part in the economy. If growth comes from new ideas and knowledge, it can be shared widely if education, healthcare, and financial services are available to all. If not, the benefits might only go to those with skills or money, which makes inequality worse (World Bank, 2018).

In Nigeria, achieving growth that includes everyone through the lens of endogenous theory requires strengthening key domestic drivers such as education, business startups, and strong government systems. Even though Nigeria has had some economic growth, not enough has been invested in people's skills and in basic things like roads and electricity. This has made it hard for many Nigerians to take part in the economy and get the benefits. As a result, there's still a lot of joblessness, poverty, and differences between regions (National Bureau of Statistics, 2022).

How Nigeria uses money it gets from outside, like oil exports, also plays a big role in whether it can grow in a way that helps everyone. If this money is used wisely for education, infrastructure, and industries, it can help the country grow from within. But if it's wasted or only used in a few areas, it might not help people much and could even make inequality worse (Sala-i-Martin & Subramanian, 2013).

To make this work, Nigeria should support different types of exports, invest in new ideas and research, improve government systems, and better education. These steps can help the country use its outside connections more effectively to grow in a fair and lasting way. This

approach makes sure that the economy grows not just from outside help but also from the country's own ability to create and develop. In short, Endogenous Growth Theory shows how internal strengths work together with outside factors to create growth that includes everyone. It also shows that while outside activities matter, their effect depends a lot on what's happening inside the country. Building up those internal strengths is key to turning outside opportunities into real and lasting economic progress.

Empirical Literature

Empirical studies on the overall external sector have given mixed and sometimes opposite results. For example, Lawal and Ezeuchenne (2017) looked at how international trade affected economic growth in Nigeria from 1985 to 2015. They used the Johansen Co-integration and Vector Error Correction Model (VECM) methods to analyze the data. Their findings showed that the variables they studied were linked together in the long run. The VECM results also showed that both exports and the balance of trade were important in explaining Nigeria's economic growth. However, imports and trade openness had the opposite effect.

Akidi, Tubotamuno and Obayori (2018) did a study to see how certain parts of the external sector affected economic growth in Nigeria from 1981 to 2016. They collected time series data on Real Gross Domestic Product as a measure of economic growth, along with data on imports, exports, exchange rate and foreign direct investment from secondary sources. They used descriptive statistics, unit root tests, co-integration tests and error correction methods to analyze the data. Their results showed that imports, exchange rate and foreign direct investment had negative effects on economic growth, while exports had a positive effect. Except for the exchange rate, none of the other variables had a significant impact on economic growth in Nigeria during the study period.

Ewubare and Okpoi (2018) studied how international remittances affected poverty reduction in Nigeria. They used time series data on poverty levels, both incoming and outgoing remittances, ODA and technical cooperation grants. They applied the ARDL method to analyze the data. Their results showed that, in the short term, incoming and outgoing remittances had different effects on poverty reduction. In the short run, incoming remittances had a significant effect, but outgoing remittances did not. ODA and technical cooperation grants also had

conflicting effects on poverty in the short run. In the long run, incoming remittances made poverty worse, while outgoing remittances, ODA and technical cooperation grants all helped reduce poverty, as they had negative coefficients. None of the variables had a significant effect in the long run.

Egungwu (2018) used the Ordinary Least Squares (OLS) regression method to look at how an increase in external debt and the cost of paying that debt affected human capital development in Nigeria from 1986 to 2015. The results showed that both the total amount of external debt and the cost of servicing that debt significantly and negatively influenced the development of human capital. However, when looking at specific sources of debt, debt borrowed from the Paris Club and other multilateral lenders had a small or unimportant negative influence. Loans from abroad – club called London positively and insignificantly influence on the development of human capital, while debt from bilateral creditors significantly and positively influenced the development of human capital. When it came to debt servicing, all groups insignificantly and positively influenced the development of human capital except the London Club, which significantly and positively influenced the development of human capital. The study suggested that while countries can use external funds to cover budget shortfalls, they should make sure the money is used for important projects that can improve the economy and the well-being of their people.

Francis and Augustine (2019) studied how different parts of the external sector affected economic growth in Nigeria between 1980 and 2016, using an error correction model. They looked at external debt, exchange rate, and exports. The results of the error correction model showed that exchange rate had a negative and significant effect on economic growth, while external debt and exports had positive and significant effects on GDP.

Tom-West and Kalu (2022) looked at how certain external sector factors influenced economic development in Nigeria from 1980 to 2021. Their main goals were to check how exchange rate, foreign exchange rate, and trade openness affected economic development using the Autoregressive Distributed Lag (ARDL) model. The study found that there was a long-term relationship among these variables. In the short run, there was a positive connection between foreign exchange reserves and economic development. Exchange rate also had a positive and significant effect on economic development in the short term. Trade openness had a positive

impact too. Based on these findings, the researchers concluded that exchange rate, foreign exchange reserves, and trade openness all helped to promote economic development in Nigeria.

Nkoro and Uko (2022) looked at how the development of the internal financial sector influences the connection between direct investment from foreign countries (FDI) and inclusive growth in Nigeria from 1981 to 2020 using annual data. Their findings showed that FDI had a positive impact on inclusive growth, but only when the internal financial system had reached a certain level of development. They also found that FDI alone had a negative effect on inclusive growth. This suggests that a well-developed domestic financial sector is necessary for FDI to help promote inclusive growth in Nigeria.

Uwakaeme (2022) used Error Correction Model (ECM) and Granger Causality tests to study the link between real GDP and various external sector macroeconomic indicators like foreign exchange rate, total exports, trade openness, total imports, external debt, external debt service charges, and foreign direct investment from 1981 to 2020. The results showed that in the long run, only FDI had a positive effect on real GDP, while others had negative impacts. The Granger Causality tests found that only FDI had a bidirectional relationship with real GDP, meaning that real GDP influenced FDI and vice versa. However, real GDP also came before exports, trade openness, and the exchange rate, suggesting that real GDP drives those variables without them influencing it back. External debt, EXDINT, and imports had independent causal relationships.

Nwafor, Egungwu, and Jessie (2022) looked at how foreign direct investment (FDI) in different sectors like agriculture, manufacturing, oil and gas, and telecommunications in Nigeria affects the Human Development Index (HDI). They used the Autoregressive Distributed Lag (ARDL) method for their analysis. Their findings showed that FDI in agriculture had a negative and significant impact on HDI, while FDI in manufacturing had a positive but not significant effect. FDI in oil and gas had a negative but not significant effect, and FDI in telecommunications had a positive and significant effect on HDI. The study concluded that overall FDI from these sectors influences HDI, especially when investments are made in agriculture, manufacturing, oil and gas, and telecommunications.

Ogbonnaya, Ogbuagu, Michael, Elechi, Eze, and Okereke (2023) used the Autoregressive Distributed Lags model to study how external sector activities affect sustainable economic

development in Nigeria, using time series data from 1970 to 2021. They applied the ARDL model and Bounds Test to check for cointegration and long-run relationships. The study found that external sector aggregates, like exports and imports, had a positive but not significant effect on sustainable economic development, while exchange rate behavior had a negative and significant impact. The findings suggest that exports and imports help maintain balance of payments, but exchange rates have not helped sustain growth in Nigeria.

Nanfa, Ajang, Timnan, Azi, Diemsan, Magit, and Salami (2023) looked at how public debt affects poverty reduction in Nigeria. They examined the impact of external, domestic, and debt servicing. Secondary time series data from 2000 to 2021 was used, and they applied descriptive statistics, correlational matrix, and Error Correction Mechanism (ECM). The results showed that external debt has a positive and significant effect on poverty reduction, while domestic debt and debt servicing have an inverse and significant effect on poverty reduction.

Ewubare and Chioma (2024) studied how external sector factors influence economic growth in Nigeria. They looked at the impact of exchange rate, foreign direct investment inflows, official development assistance, and external debt on GDP per capita from 1987 to 2022. They used the ARDL method for their analysis. The results showed that in the long run, Nigeria's external sector did not have a significant effect on GDP per capita growth. However, in the short run, foreign direct investment inflows and external debt positively influenced GDP per capita growth. Exchange rate and official development assistance were also statistically significant in influencing GDP per capita in Nigeria, but the relationship was negative.

Again, Ewubare and Chioma (2024) looked at how foreign sector factors affect poverty reduction in Nigeria from 1987 to 2022. They used annual time series data on poverty headcount (POV), exchange rate (EXR), foreign direct investment (FDI), official development assistance (ODA), and external debt (XDT). They tested the data using the Augmented Dickey-Fuller (ADF) Unit Root test, auto-regressive distributed lag (ARDL) estimation, and diagnostic tests. The results showed that at the 5 percent level, EXR, FDI, ODA, and XDT had a significant effect on poverty in the short run. In the long run, EXR, FDI, and XDT helped reduce poverty, but ODA did not show a significant impact in the long run.

Agua and Ugwuoke (2024) studied the effect of external debt on poverty reduction in Nigeria using annual time series data from 1981 to 2021 and the Autoregressive Distributed Lag

(ARDL) model. Their findings showed that external debt had a positive effect on the poverty rate in Nigeria.

Okowa and Igbara (2025) used the Autoregressive Distributed Lag (ARDL) method to examine how external sector factors influence Nigeria's economic growth from 1990 to 2022. Their analysis found that imports, exchange rate, and foreign direct investment had a negative effect on real GDP. Exports had a positive effect on economic growth. However, except for exports, none of the other variables had a significant effect on real GDP during the study period.

Despite many studies on external sector factors, some gaps remain. Most studies have focused on how these factors affect GDP growth, not inclusive growth indicators like human development. There is also little attention on how these factors improve welfare, such as through job creation and income distribution. Mixed results in previous research make it hard to determine the real impact of external sector factors on development outcomes. Because of this, this study focuses on inclusive growth instead of just economic growth. This is important because Nigeria's GDP growth has not led to broad-based development. The study looks at how the performance of the external sector affects inclusive development outcomes. It doesn't just ask if external factors affect growth, but whether they actually help improve the living standards of ordinary Nigerians through human development.

3. Materials and Methods

The ex-post facto research design was used in this investigation. Secondary data from 1981 to 2023 were used for analysis. The data came from a report by Nigeria's main bank. To examine how external aggregate affects inclusive growth in Nigeria, the study adapted the model developed by Akidi, Tubotamuno, and Obayori in 2018. Their model looked at how external sector aggregate influenced economic growth in Nigeria from 1981 to 2016. They related exchange rate, foreign direct investment, import, and export to real gross domestic product. In order to have a robust analytical framework, the present study extended the scope and used the human development index (HDI) as the dependent variable. Therefore, the model for this study is presented as follows:

$$HDI = F(EXR, FDI, IMPT, EXPT) \quad (1)$$

From the above functional model or association between the dependent and explanatory variables, the econometric form of the model was specified as follows:

$HDI_t = \alpha_0 + \alpha_1 EXR_t + \alpha_2 FDI_t + \alpha_3 IMPT + \alpha_4 EXPT + e_t$ (2)

The log form of equation (2) produced;

$HDI_t = \alpha_0 + \alpha_1 LnEXR_t + \alpha_2 LnFDI_t + \alpha_3 LnIMPT + \alpha_4 LnEXPT + e_t$ (3)

Where: HDI is human development index, EXR = exchange rate, IMPT = import, EXPT = export, α_0 = intercept parameter, e = is error term which denotes other variables not included in the model, Ln is natural log, t = is the period of time, α_1 - α_4 = slope parameters. It is expected that; $\alpha_1, \alpha_2, \alpha_3,$ and $\alpha_4 > 0$.

Techniques of Data Analysis

This investigation employed the techniques of Augmented Dickey Fuller test (ADF) and the Autoregressive Distributed Lag (ARDL) approach. The ADF test is utilized to check if the data is stationary, meaning it does not change over time in a manner that influences the outcomes. The general formula for the ADF test is:

$\Delta y_t = \alpha_0 + \alpha_1 y_{t-1} + \Sigma\alpha_1 \Delta y_i + \delta_t + U_t$ (3)

Where: y represents a time series, t is a linear time trend, Δ denotes the first difference operator, α_0 is a constant, n is the optimum number of lags in the explanatory variables and U is random error term. To examine both short-term and long-term associations between external sector aggregate and inclusive growth, the Autoregressive Distributed Lag – ARDL technique was used. This approach helps mitigate problems such as autocorrelation and endogeneity, providing unbiased and efficient results. The ARDL model used in this investigation is presented thusly:

$$\Delta HDI_{t,j} = C_0 + C_1 HDI_{t-1,j} + C_2 EXR_{t-1,j} + C_3 FDI_{t-1,j} + C_4 IMPT_{t-1,j} + C_5 EXPT_{t-1,j} + \sum_{i=1}^{n1} a_{1i,j} \Delta HDI_{t-1,j} + \sum_{i=0}^{n2} a_{2i,j} \Delta EXR_{t-1,j} + \sum_{i=0}^{n3} a_{3i,j} \Delta FDI_{t-1,j} + \sum_{i=0}^{n4} a_{4i,j} \Delta IMPT_{t-1,j} + \sum_{i=0}^{n5} a_{5i,j} \Delta EXPT_{t-1,j} + \lambda ECMt - 1 + \mu_t \quad (5)$$

Where; change operator takes the symbol Δ, white noise or error term is μt, optimal lag length is n, short run dynamics of the model are $\alpha_1, \dot{\alpha}_2, \dot{\alpha}_3, \dot{\alpha}_4, \dot{\alpha}_5$ and long run elasticities are c_1, c_2, c_3, c_4, c_5 and error term is μ_t. Error correction term obtained from the co-integration model is ECM_{t-1} .

The error coefficients (λ1) demonstrate how fast the co-integration model amends any unevenness from the preceding period or the speed at which it corrects to get back to the long term stability. The coefficient of ECM is anticipated to be negative and statistically noteworthy. A negative and noteworthy ECMt-1 coefficient suggests that any short-term movement between the outcome and explanatory variables will ultimately return to the elongated term association.

4. Results and Discussion

To prevent incorrect results, this study used the Augmented Dickey Fuller (ADF) test to see if the data is stable. The test works by checking two main possibilities: one idea, called the null hypothesis, says the variable has a unit root and isn't stable, while the other idea, called the alternative hypothesis, says the variable doesn't have a unit root and is stable. The results of the test are shown in Table 1.

Table 1: Unit Root Test Outcome via Augmented Dickey-Fuller

Variables	Level form		First difference		Order of integration
	ADF Statistics	5% Critical Value	ADF Statistics	5% Critical Value	
HDI	-6.381615	-3.520787	-	-	1(0)
EXR	0.263461	-3.520787	-5.306409	-3.523623	1(1)
FDI	-1.539626	-3.520787	-7.719088	-3.523623	1(1)
IMPT	-1.146576	-3.552973	-5.873688	-3.544284	1(1)
EXPT	-6.416931	-3.520787	-	-	1(0)

Recall: HDI, EXR, FDI, IMPT and EXPT as defined previously.

Source: Author's Computation, 2026.

The ADF test results for each series in Table 2 show that at the 5% significance level, HDI and EXPT are stationary at their original levels 1(0) because its ADF statistic is higher than the 5% critical value. On the other hand, EXR, FDI and IMPT become stationary after one difference, which means they are 1(1). Since the variables are integrated of order 1(0) and 1(1), it meets the requirement to use an ARDL model to check for long-run relationships.

Table 2: ARDL Bounds Test for Co-integration

Model		**F-Statistic =** 6.720488
HDI= F(EXR, FDI, IMPT, EXPT)		K = 4
Critical Values	Lower Bound	Upper Bound
5%	3.47	4.57

Recall: HDI, EXR, FDI, IMPT and EXPT as defined previously.

Source: Author's Computation, 2026.

The ARDL bounds test for co-integration shows there is a long-term connection between the variables (HDI, EXR, FDI, IMPT and EXPT). This is because the F-statistic, which is around 6.72, is higher than the upper critical value at the 5% significance level. This result means we can reject the idea that there is no long-term relationship between these variables at the 5% level. As a result, the study was able to determine both the long-run and short-run effects of the variables

Table 3: Estimated ARDL Long Run Coefficients. Dependent Variable: HDI ARDL (1, 0, 2, 2, 0)

Regressors	**Coefficient**	**t-Statistic**	**P-Value**
LOG(EXR)	-0.008495	-0.812367	0.4230
LOG(FDI)	-0.008786	-1.370876	0.1806
LOG(IMPT)	0.009282	0.876110	0.3879
LOG(EXPT)	0.002735	0.586832	0.5617

Recall: EXR, FDI, IMPT and EXPT as defined previously.

Source: Author's Computation, 2026.

The long run coefficients from Table 3 show that in Nigeria, exchange rate and foreign direct investment are linked to lower human development index (inclusive growth). Strictly speaking, the negative long-run relationship between exchange rate, foreign direct investment, and human development suggests that macroeconomic instability and the misallocation of foreign direct investment inflows will undermine welfare outcomes in the long run. Specifically,

persistent currency depreciation will erode purchasing power and increase the cost of essential goods, while foreign direct investment inflows - largely concentrated in enclave sectors with weak domestic linkages will fail to generate inclusive growth. Consequently, these factors jointly will contribute to declining human development outcomes over time. On the other hand, export and import have positive relationship with human development index (inclusive growth) in the long run. This suggests that, over time, increases in trade openness through both imports and exports will contribute meaningfully to improvements in human development outcomes.

In the case of imports, the positive coefficient implies that sustained increases in importation will enhance human development in the long run. This happens because imports help get things like machines, new technology, medical tools, and learning materials that might not be available locally. These imports help make work more efficient, improve healthcare services, and boost education, which are all key parts of the Human Development Index (HDI). Also, imports can help keep local prices stable by filling in gaps in supply, which increases people's real income and overall well-being. In this way, imports help share new technologies and build skills, supporting long-term growth. In a similar way, the positive link between exports and HDI shows that growing exports greatly help human development. When exports increase, it brings in more foreign money, which the government can use to invest in important areas like roads, healthcare, and schools.

Increased export earnings help the economy grow, create jobs, and boost people's incomes. Over time, these benefits lead to better quality of life, longer life expectancy, and more education. Also, when countries trade with others, their businesses face global competition. This encourages them to become more efficient, innovative, and skilled, which helps people develop more. From an ARDL model perspective, these positive relationships show that both imports and exports have a lasting effect on HDI in the long run. This shows that being open to trade is important for growth that benefits everyone, especially when trade focuses on areas that create value and improve well-being. The evidence shows that having a good trade policy, which includes bringing in useful goods like capital and intermediate products, along with a variety of high-value exports, can greatly improve human development. The connection between trade and HDI shows the need for policies that make trade more competitive, improve infrastructure, and

make sure the benefits of trade reach everyone. However, none of the variables showed a statistically significant result at usual levels.

Table 4: Error Correction Representation for the Selected ARDL Model ARDL (1, 0, 2, 2, 0)

Regressors	Coefficients	t-Statistic	P-Value
LOG(EXR)	-0.006913	-0.841942	0.4065
LOG(FDI)	-0.016063	-2.397072	0.0230
LOG(IMPT)	0.026599	2.804255	0.0088
LOG(EXPT)	0.002225	0.584561	0.5632
ECM (-1)	-0.813754	-6.171124	0.0000
R-squared = 0.696649		**D-W stat. =** 1.861441	
Adjusted R-squared = 0.643117		**Akaike info criterion** = -5.087877	
Schwarz criterion = -4.795316		**F-statistic** = 13.01357	
		Prob(F-statistic) = 0.000000	

Recall: EXR, FDI, IMPT and EXPT as defined previously.

Source: Author's Computation, 2026.

Table 3 displays the results of the short-term dynamic coefficients that are linked to the long-term associations found in the ECM equation. In the model, the Error Correction Term has the correct sign, which is negative, and it is statistically significant. This means the model adjusts towards long-term equilibrium over time. In other words, it shows how the model moves from short-term balance to long-term balance. This suggests that any differences from the short-term inclusive growth – human development index eventually return to the long-term equilibrium. The Durbin Watson value of 1.861441, shows that there is no problem of autocorrelation in the model. Additionally, the dynamic connections between the variables, as shown by the ECM, reveal that the model's ability to describe the data measured by R-squared is around 0.696649. This means the model fits the data well. It indicates that during the time period studied, about 70 percent of the changes in the inclusive growth can be explained by the variables included in the

model, while the remaining 30 percent is explained by other factors not included in the model, and these are captured as the error term.

In addition, the coefficients for exchange rate and foreign direct investment are negative in the short run. This suggests that exchange rate fluctuation and foreign direct investment have not helped to increase human development index (inclusive growth) in Nigeria during the time period studied. This result matches the findings of Nwafor, Egungwu and Jessie (2022), who looked at how foreign direct investment inflows into the agricultural, manufacturing, oil & gas and telecommunications sectors in Nigeria and their effect on Human development index using an Autoregressive Distributed Lag (ARDL) technique. They reported that a combination of foreign direct investment inflows affects human development index negatively. The estimated ARDL short-run results indicating a negative relationship between exchange rate (EXR), foreign direct investment (FDI), and human development index (HDI) (inclusive growth) suggest that short-term fluctuations in macroeconomic and external sector variables adversely affect human development outcomes in Nigeria.

This finding has important consequences for how the economy is managed and how policies are made, especially in a country that has fixed structures and relies heavily on imports. When the currency loses value quickly, it leads to worse outcomes for people's well-being in the short term. This happens mainly because the drop in currency value quickly affects the prices of everyday items like food, healthcare, fuel, and school supplies, causing prices to rise sharply. As a result, people's real income goes down, making it harder for them to access important services that improve their quality of life. The key takeaway for policymakers, especially the Central Bank of Nigeria, is that they should focus on keeping the exchange rate stable in the short run. This includes better management of foreign currency reserves, reducing pressure from investors in the foreign exchange market, and possibly tightening money supply if needed.

In addition, temporary financial help like direct subsidies or programmes that support low-income families might be needed to protect them from sudden losses in their living standards caused by changes in exchange rates. When it comes to foreign direct investment (FDI), the early effects on human development are not positive, meaning that just having more investment doesn't automatically improve people's well-being. In Nigeria, most FDI goes into industries that require a lot of money and focus on extracting resources, like the oil and gas

industry. These kinds of investments don't create many jobs quickly and don't strongly connect with the rest of the economy. Also, when companies take profits back to their home countries and invest in isolated areas, it reduces the immediate benefits of FDI. The lesson here is that the government should not just focus on getting more FDI but also on making sure the investments are better quality and go into areas that help people more, like manufacturing, farming, healthcare, and schools. It's also important to support local businesses and improve the country's ability to use these investments by training people and making local institutions stronger. This will help make the short-term effects of FDI on development better.

The combined negative effects of exchange rate changes and foreign direct investment show that there is a weak connection between how the economy interacts with the outside world and improvements in human development. This means Nigeria's economy is very sensitive to changes from abroad, and the benefits from foreign money and economic adjustments don't quickly improve people's well-being. Because of this, policies should focus on keeping the economy stable, changing the structure of the economy, and providing temporary support to people to reduce harm from bad economic conditions. Overall, the study shows that there is a need for both economic and development policies that work together to keep the currency stable, make foreign investment more helpful for development, and improve the ability of institutions to turn foreign economic activity into real benefits for people. Without these actions, economic ups and downs in the short term will keep hurting the well-being of people in Nigeria.

Furthermore, the coefficients of import and export have positive signs in the short run. This is what was expected beforehand. What this means is that, when there is a percentage increase in import and export, it will lead to an increase in human development index by 0.026599 percent and 0.002225 percent respectively. This also shows that import and export have an enhancing effect on human development in Nigeria during the time period studied. This result is consistent with the findings of Ogbonnaya et al (2023) who looked at how employed an Autoregressive Distributed Lags model to investigate the influence of external sector aggregates on sustainable economic development(welfare improvement) in Nigeria using time series data spanning from 1970 to 2021. They provided evidence of positive and insignificant effect of external sector aggregates (export and import) on sustainable economic development (improvement in welfare) in Nigeria. The ARDL short-run results revealing a positive

relationship between imports (IMPT), exports (EXPT), and the human development index (HDI) suggest that increases in trade flows generate immediate improvements in welfare outcomes in Nigeria. This implies that, even within short adjustment periods, trade-related activities contribute to better access to income, healthcare, and education. Such findings carry important policy implications for trade, macroeconomic management, and development strategy. In the case of imports, the positive short-run coefficient indicates that increased importation rapidly enhances human development. This reflects Nigeria's reliance on imports for essential goods, including food items, pharmaceuticals, medical equipment, refined petroleum products, and educational materials. The immediate availability of these goods helps stabilize domestic supply, reduce shortages, and improve living standards.

The policy message is that the government needs to make sure people can get important goods from abroad quickly and efficiently, especially those that help people's well-being. This means keeping enough foreign money available, fixing problems at ports, and choosing to bring in goods that help the economy and people's lives instead of just things people buy for fun. But this has to be done carefully to prevent people from relying too much on imports over time. For exports, there's a clear link in the short term between increasing exports and better development for people. More exports bring in foreign money, help the government earn more, and boost the economy, which leads to more jobs and higher incomes. In Nigeria, export money, especially from oil and other sectors, can quickly help the government spend on health, education, and infrastructure. The message is that leaders should work on making exports grow by supporting non-oil areas like farming and making things, improving trade facilities, and giving support to businesses that export. Making it easier for businesses to operate and reducing trade issues can help these short-term benefits grow even more.

The good things from both imports and exports together show that being open to trade brings quick benefits to people's well-being. This means that activities in the trade sector can quickly help improve human development. Because of this, policymakers should create a trade policy that helps necessary imports while also encouraging strong exports. This involves keeping the exchange rate stable to help trade, making customs processes more efficient, and working better with other regions and countries around the world. Also, since this relationship is short-term, it's important to have other economic policies that keep these benefits going. The

government should use money and spending policies in a way that makes sure the extra money from trade is used to improve areas that help people, like education and health. At the same time, the money supply should be managed carefully to keep prices from rising too much, so that the benefits of more trade are not lost. In short, the fact that imports, exports, and human development are closely linked in the short term shows that trade can quickly improve people's lives in Nigeria. So, policies should focus on making trade easier, choosing the right kinds of imports, helping exports grow in different areas, and improving the systems and rules that support trade so that these benefits can last and get even better over time.

Post Estimation Diagnostic Tests Results

Diagnostic tests were conducted in this study to see if the model's estimates can be relied upon for making policy predictions or recommendations. The study included specific tests such as the Wald test to check restrictions on coefficients, and the Breusch-Godfrey Serial Correlation LM Test, as part of the analysis after estimating the model. The results from these tests are carefully displayed in Tables 5 and 6.

Wald Test

The Wald test is used to check if the coefficients of the cause variables in the ECM model are all important together. The F-statistic in Table 6 was used to determine this.

Table 5 Wald Test Result

Wald Test:

Equation: Untitled

Test Statistic	Value	Df	Probability
F-statistic	638762.6	(5, 30)	0.0000
Chi-square	3193813.	5	0.0000

Source: Author's Computation, 2026.

The results in Table 5 show that the F-statistic is around 638763 and the probability value is 0.0000, which is lower than 0.05 at the usual 5 percent significance level. This means all the predictor variables included in the model together play a significant role in explaining the inclusive growth in Nigeria during the time covered by the study.

Test for Serial Correlation

Table 6: Breusch-Godfrey Test for Serial Correlation

Breusch-Godfrey Serial Correlation LM Test:

F-statistic	0.694262	Prob. F(2,28)	0.5078
Obs*R-squared	1.937134	Prob. Chi-Square(2)	0.3796

Source: Author's Computation, 2026.

The results shown in Table 6 indicate that the error correction model does not have a serial autocorrelation issue. This is because the chi-square value and the associated probability of the chi-square statistic are both above 0.05.

5. Conclusion and Recommendations

This study cautiously examined the influence of external sector aggregate on inclusive growth in Nigeria from 1981 to 2023. The external sector, comprising variables such as exports, imports, foreign direct investment and exchange rate plays a critical role in shaping economic performance and development outcomes. In Nigeria, these variables are theoretically powerful drivers of inclusive development, yet their actual contribution has been limited. In order to understand the actual influence of external sector aggregate on inclusive growth in Nigeria, this study used data from reports by Nigeria's highest bank, and included information on human development index, exchange rate, foreign direct investment, import and export. The study used an Autoregressive Distributed Lag - ARDL to examine how these variables relate in both the short term and the long term. The findings showed that in the long run, exchange rate and foreign direct investment have negative and insignificant relationship with human development index (inclusive growth). However, import and export have positive and insignificant relationship with human development index (inclusive growth). In the short run, exchange rate and foreign direct

investment have negative relationship with human development index (inclusive growth). Meanwhile, exchange rate is not statistically significant but foreign direct investment is statistically significant at conventional level. However, import and export have positive relationship with human development index (inclusive growth). Import is statistically significant while export is not statistically significant. Therefore, this study suggests that the government should stop just focusing on bringing in more foreign investments and instead work on making sure the investments are of high quality and in the right sectors. These should include areas like manufacturing, agriculture, healthcare, and education, which are good for creating jobs and helping society. It is also important to support local businesses by creating rules that encourage using local goods and services, and by improving skills and making institutions stronger. This will help make foreign investments more useful for development in the short term. The central bank and other monetary authorities need to focus on keeping the exchange rate stable. This can be done by managing foreign currency reserves better, reducing unfair pressures in the foreign exchange market, and sometimes tightening money supply if needed. In addition, the government might need to use temporary financial support, like targeted subsidies or social programs, to help people who are most affected by sudden changes in exchange rates. To get the most benefit from trade, the government should work on making trade easier, choose imports that are strategic, encourage more variety in exports, and build strong institutions that can support trade both now and in the future.

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