Evaluation of the Influence of Defense Expenses on the Economy of Nigeria

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ABSTRACT

Defense spending can have both positive and negative impacts on an economy. On the positive side, it can stimulate economic growth by increasing demand and enhancing security. However, it can also have negative consequences by displacing investment. In countries with a domestic defense industry, military expenditure tends to have a more significant positive effect on economic growth. However, in the case of Nigeria, which lacks a domestic arms industry and relies heavily on importing military equipment, any increase in military spending is more likely to worsen Nigeria's trade deficit rather than boost its GDP. This paper examines the effects of defense expenditure on the economy. While some studies have found a direct positive relationship between military spending and economic growth, these studies were conducted during peaceful times and not in the midst of security challenges. Therefore, in developing economies like Nigeria, which face security challenges, the conditions necessary for defense spending to drive economic growth may be absent. For instance, looking at Nigeria's 1986 budget, only 5.69 percent of government expenditure was allocated to the defense sector. This percentage fluctuated in the subsequent years, with an increase during the early years of democratic governance, followed by a decline. This suggests that when countries grapple with security challenges and are compelled to allocate resources to their military at the expense of other pressing needs, such spending may not yield

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INTRODUCTION

The impact of military expenditure on an economy can be twofold: it can have positive effects by boosting aggregate demand and enhancing security [1], while it can also have negative consequences by crowding out investment. However, there is a limited body of research examining the causal relationship between defense spending and economic growth. According to Keynesian theory, defense expenditure, being a component of government spending, injects funds into the economy and can stimulate it positively through the multiplier effect. An increase in any of the aggregate demand factors can raise the overall capital in society, leading to higher profits and potentially encouraging greater investment. This, in turn, generates short-term multiplier effects and elevates growth rates in the overall economy. Additionally, [2] argued that increased military spending can enhance the skill sets of the workforce through educational provisions within the military industry, contributing to economic growth. Furthermore, defense spending can bring about externalities beneficial to economic growth, such as the development of road infrastructure, which can serve both military and civilian purposes [3]. On the other hand, some contend that there exists a negative correlation between defense spending and economic growth [4]. They argue that since defense spending is financed through taxation, it not only reduces resources available to the private sector but also affects relative prices, such as real wages and real interest rates, which can disrupt economic decision-making. This negative trend may ultimately hamper economic growth. Defense spending can also displace private investment and divert resources from government spending that could otherwise foster human capital development. Furthermore,

it may create bottlenecks in the demand for highly skilled labor and divert resources away from civilian development activities. Given the typically lower productivity of the government sector, this diversion of resources from civilian to military purposes could hinder long-term national productivity, technological advancements, and overall growth [5]. The objective of this study is to assess the impact of defense expenditure on the economic growth of Nigeria.

Empirical Literature

In a study conducted by [6], pool data models, including fixed and random effect models, were employed to explore the connection between defense expenditure and economic growth across 85 countries. This investigation utilized aggregated data for defense spending along with labor, capital, and GDP as variables. The findings displayed a lack of consistent patterns across nations. While a few countries in the sample exhibited predominantly negative coefficients, the researcher contended that, within the growth framework, defense spending generally had a positive coefficient and, therefore, should not be considered detrimental to growth. Another study by [7] uncovered a negative correlation between military expenditure and economic growth. Due to this heterogeneity in results, caution was advised when interpreting the findings. In a different approach, [8] applied the Granger Causality technique to assess the relationship between defense spending and GDP in Turkey from 1955 to 2000. They also utilized impulse response functions to gauge long-term causality. The outcome indicated a negative impact of defense expenditures on Turkey's GDP. Moving on, [9] examined the influence of military expenditure on economic growth and foreign direct investment across five of the seven South Asian Regional Cooperation Council (SARCC) nations using panel data spanning from 1980 to 1999. Interestingly, their results suggested a positive relationship between military expenditure and economic growth, supporting the idea that military spending can have a positive impact on growth. In another investigation, [9] employed a multi-equation, multivariable approach to explore the effects of defense spending on economic growth. They formulated three equations: one for growth, one for saving, and one for defense expenditure. Utilizing cross-sectional data for 64 countries, they employed various statistical methods (OLS, 2SLS, and 3SLS) to derive overall estimates and separate estimates for middle and lower-income countries. The results indicated a negative impact of military spending on growth for middle-income countries but found it insignificant for low-income countries. Moreover, [11] applied a Deger type model to estimate the effects of military spending in Peru. After conducting unit root testing and addressing estimation challenges, they employed OLS, 2SLS, and 3SLS to estimate three-equation models. The resulting estimates revealed a negative relationship between defense spending and economic growth in Peru. Additionally, [12] employed threshold regressions and demonstrated that the impact of military spending on growth is dependent on the spending level. It showed a positive externality effect for low levels of military spending but a negative effect for high levels. [13] used a distributed lag approach to investigate the demand for military spending in Canada, finding that the most significant determinant was European North Atlantic Treaty Organization (NATO) spending, while GDP was deemed insignificant regarding military spending. Furthermore, [14] delved into the long-term impact of military expenditure on growth. They argued that military expenditure triggered by external threats would promote growth, while that driven by rent-seeking and corruption would hinder it. [15] examined the arms race between India and Pakistan and its relation to each country's economic growth, discovering a unidirectional causal relationship between their military expenditures.

[5] focused on Guatemala, employing the Feder-Ram model to assess linear versus non-linear functions. They suggested that the linear model showed an insignificant effect on growth. However, this conclusion changed when using the non-linear model, revealing a positive effect on growth below a certain threshold and a negative effect beyond it. Nevertheless, they found that the defense sector was less productive than the civilian sector. Lastly, [16] found a negative correlation between military burden and economic growth in Egypt, Israel, and Syria. They also noted that civilian expenditure had a positive impact on economic growth in Israel and Syria. In a more recent study, [17] investigated the relationship between military expenditure (milex) and economic growth, breaking military spending down into recurrent and capital components. Their findings consistently showed a positive relationship with saving, investment, and GDP in all cases.

The Structure of Defense Expenditure and Economic Performance in Nigeria

Defense expenditure as a share of the total federal government expenditure, has changed considerably within the period of 1980 to 2010. In 1986 budget, only 5.69 percent of government expenditure was devoted to defense sector. This share dropped during period between 1987 and 1998. At the inception of democratic dispensation, it grew to 6.12 percent in 1999, and this upswing trend continued till 2006, before it fell to 4.40 percent, 1.00 percent and 0.90 percent in 2007, 2008 and 2009 respectively. The relationship between GDP and defense expenditure shows that defense expenditure constituted 1.38 percent of the GDP in 1986; and it witnessed a drop to 0.70 percent in 1987 and 0.50 percent in 1989. However, it increased to 0.60 percent in 1990, 0.72 percent in 1991, fell in 1992 to 0.41 percent and rose again to 0.61 percent in 1993/94 while it dropped to 0.45 percent in 1995. In 1996, it peaked again to 0.50 percent, a level which it maintained prior to the inception of democratic dispensation in 1999, when it reached

its peak of 1.82 percent and maintained the average of 1.11 percent, 1.35 percent and 1.32 percent in 2000, 2001 and 2002 respectively. It fell again to 0.73, 0.76, 0.64, 0.49 0.52, 0.13, and 0.13 percents respectively during the years between 2003-2009. It can thus be summarized that defense expenditure, as a percentage of GDP, fluctuated during the period 1980 to 2010, but did not exceed 1.82 percent throughout the period. While the lowest level of percentage of 0.13 percent was witnessed in 2008 and 2009 respectively. It can be concluded that after its rise in 1999 to 1.82 percent, defense expenditure accounted for only one percent of the GDP in Nigeria.

Impact on Economy

[19] explained that in nations with a well-established defense industry, military spending tends to have a more significant positive impact on economic growth. However, in Nigeria's case, the absence of a domestic arms industry forces it to procure the majority of its military equipment from foreign suppliers. Consequently, any increase in military expenditures is more likely to strain Nigeria's current account deficit rather than bolster its GDP. Additionally, [20] pointed out that studies demonstrating a clear positive relationship between economic growth and military spending were primarily conducted during periods of stability, not in the midst of security challenges. In contrast, in developing economies facing security challenges like Nigeria, the conditions necessary for defense spending to stimulate the economy may be lacking. For example, skilled military personnel might perish before they can transfer their knowledge to the private sector, and the depreciation rate of military hardware and infrastructure improvements may accelerate [21]. Consequently, Nigeria, as a developing nation with limited resources, faces constraints on military spending due to its low income and growth. Therefore, the government can only increase its military expenditures when the economy grows, or it may need to source funds for military spending, which could initially have an adverse impact on the economy, known as the crowding-out effect. Furthermore, in alignment with the Stockholm International Peace Research Institute, Nigeria is a net arms importer. This means that military expenditures are financed using the country's scarce resources and foreign exchange reserves. Hence, military expenditure initially represents an outflow from the country, as it imports nearly all military equipment and invests funds to acquire the technical expertise necessary to operate the new equipment within the nation [22]. However, the economy can ultimately benefit from military expenditure, not necessarily because of its direct impact on economic activity, but rather due to the potential security and safety benefits it provides to the nation. Nevertheless, an increased share of government spending allocated to military expenditures has a positive long-term effect on GDP.

CONCLUSION/RECOMMENDATION

From the literature so far reviewed, findings suggest that there might not be immediate positive economic growth gains from government military expenditure, however, in the long-run; the positive impact of such military expenditure on economic growth will be gained. This implies that when countries are faced with insecurity challenges and are forced to spend on their military in the face of other competing needs, such expenditure may not drive growth in the immediate short term, but may have a long run growth effect in future.

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