FINANCIAL INCLUSION IN NIGERIA SHADOW ECONOMY: STRATEGIC ISSUES AND OPTIONS

[1]ADEYEFA SAMSON, [2]OLUWOYO TEMIDAYO, [3]AUDU PETER

[1]United Bank for Africa Plc
[2,3]Nigeria and Kogi State University, Nigeria
E_mail:[1]olukunle.adeyefa@ubagroup.com, [2]oluwoyotemidayo@gmail.com

Abstract - The shadow economy is the last hope of the common masses by absorbing a significant fraction of the populace that are not adequately captured in the formal sector. Many agencies have shown discontent about this sector and hence have veered from supportive to antagonistic role with divergence reasons. Hence Firms in the shadow sector face a number of challenges that can hamper its operations and growth. It is on these backdrops that it is expedient to access strategic issues and options in financial inclusion of the shadow economy in Nigeria using Lewis development theory as framework. The study employed secondary sources of data which was analysed using descriptive statistics. And conclude the future of financial inclusion drive lies in the coffers of electronic channel or payment system. There is need to explore the potential of Digital Financial Services (DFS) market in Nigeria and Know Your Customer requirements should be tailored to take care of the prevailing realities in some areas.
JEL-CODE: O17, O5, D78, H2

Keyword - Informal, Financial, Inclusion Economy

I. INTRODUCTION

It is not out of place to assert that the shadow economy, the black market, the non-observed economy or the underground economy, informal sector, informal economy, or grey economy is the last hope of the common masses by absorbing a significant fraction of the populace that are not adequately captured in the formal sector. The relative absorption rate is higher compare to the other sector. Developing economy usually operates a dual financial system. This sector's processes and procedures are most often outmoded, archaic and out of tune with modernity.

Although the informal sector makes up a significant portion of the economies in developing countries, it is often stigmatized as troublesome and unmanageable. However the informal sector provides critical economic opportunities for the poor and has been expanding rapidly since the 1960s. As such, integrating the informal economy into the formal sector is an important policy challenge [1]

Many agencies have shown discontent about this sector and hence has veered from supportive to antagonistic role with divergence reasons ranging from the fact that the informal firms do not pay tax, major channel of income leakage, filled with tainted goods, uncoordinated and saturated with reports of child labour, low wages (especially for women), human right abuse and all sorts of social menace and economic sabotage.

In spite of this, The International Labour Organisation (ILO) estimates that its average size as a percentage of gross domestic product in sub-Saharan Africa is 41%. This ranges from under 30% in South Africa to 60% in Nigeria, Tanzania and Zimbabwe. It is also a huge employer. It represents about three-quarters of non-agricultural employment, and about 72% of total employment in sub-Saharan Africa. About 93% of new jobs created in Africa during that 1990s were in the informal economy [2].

In affirmation to this above, [3] posits that economic agents working in the informal sector contri bute extensively to the overall economic activity while IFC (2012) affirms that around 80% of total micro, small and medium sized e nterprises (MSMEs) are informal today. However, firms in the shadow sector face a number of challenge s that can hamper their operations and growth among which include but not limited to public infrastructure (power, land and water); weak in stitutions (property rights, legal protection, and corrup tion) or access to benefits associated with participatio n in the formal sector (access to credit, new technolog ies, and greater visibility of business through publicity [4]. Hence the need for financial inclusion in this noble sector in order to integrate and revamp the sector.

Financial inclusion is about ensuring availability, affordability and accessibility of quality financial products and services to all segment of the society which encompasses the have's and the have not.

It is worrisome to note that gaps in financial inclusion remain severe around the world, and in particular in developing countries where more than 2.7 billion people are still financially excluded and about 400 million SMEs do not have access to formal financial services [4] cited in [5]

Also [6] confirmed, Africa lags behind other developing regions with only 23% of adults holding an account at a formal financial institution, twice lower than the World average estimated at 50% .

The result of EFINA access to financial services in Nigeria 2012 survey shows that 34.9 million adults representing 39.7% of the adult population were

financially excluded. Only 28.6 million adults were banked representing 32.5% of the adult population. In 2010, 39.2 million people represent 46.3% out of 84.7 million adult population were excluded from financial services. In addition, 54.4% of these were women while 80% of the excluded people resided in rural areas.

Formal financial institutions have not been able to adequately capture the financial needs of the teeming masses. The formality and complexity of the system makes it ambiguous and enshrouded bottleneck for the illiterate which is typical among the population of the masses. Financial inclusion has become an explicit policy objective in many African countries. While a number of government agencies are typically involved, each with its own mandate, Central banks are increasingly playing an active role in promoting financial inclusion, particularly in the areas of microfinance, consumer protection, rural finance and SME access [7]

A major concern is that as at 2012, 39.7% of the adult population were financially excluded while in 2016, the number of financially excluded adult grew to 41.6% [8] This is a point to two major facts either the adult population growth outpaced the growth in the banked population or the previously financial included population have since left the circle of financial services.

It is on these backdrops that it is expedient to access strategic issues and options in financial inclusion of the shadow economy in Nigeria while providing response to the following objectives;

1. To assess the state of financial inclusion in the shadow economy of Nigeria
2. To evaluate the dimension of shadow economy access to formal financial services, and
3. To identify the constraints to participation in financial inclusion i.e. access and use to/of financial services.

II. LITERATURE REVIEW

2.1 Nigeria Shadow Economy

Giving a spacious view of the concept was [9] who defined financial inclusion as a process that ensures the ease of access availability and usage of the formal financial system for all member of the economy.

Financial inclusion is the process through which accessibility, availability and affordability of the formal financial system is ensured to all members of an economy. It is a determining factor in alleviating poverty, achieving sustainable economic growth and promoting social cohesion. As typical of economic theory, there is also a demand and supply side to financial inclusion. Supply-side data comes from providers of financial services, while demand-side involves the end-users of products: individuals, households, and firms. Demand-side identifies the categories of people who have bank accounts or eligible to demand for financial products.

The G20 Financial Inclusion Indicators suggest that financial inclusion should be measured in three dimensions: (i) access to financial services, (ii) usage of financial services, and (iii) quality of products and service delivery.

The first two indicators are a pointer to demand side while the last indicator points to the supply side. This affirms that the Success of any financial inclusion drive depends not only on supply side but demand side is also equally important.

The informal sector in Nigeria refers to economic activities in all sectors of the economy that are operated outside the purview of government regulation. This sector may be invisible, irregular, parallel, non-structured, backyard, under ground, subterranean, unobserved or residual [10].

Following from the above, it can be deduced that the shadow economy are typically:

- The un-banked
- The under banked
- The low income/profit earners
- The less educated
- The financially excluded
- The socially disadvantaged

According to [11] the informal sector in Nigeria may be categorised into the following sub-sectors:-

(i) Productive;
(ii) Service; and
(iii) Financial

(i) The Informal Productive sector: This sector is concerned with economic activities involving the production of tangible goods among which include the agricultural production, mining and quarrying, small-scale manufacturing, building and construction. woodwork, furniture making, garment making, welding and iron works among others.

(ii) Informal Service sector: This sector encompasses services which include the repairs and maintenance, labour for menial work, tailoring, vehicle repairs and maintenance, tinkering, carpentry and servicing of various household and commercial tools. Informal health services, especially in the rural areas, include traditional birth attendants, herbalists and other traditional medical practitioners. There are also traditional spiritualists who offer counselling services. These services are rendered for fees paid to those who render them.

(iii) Informal Financial Sector: The activities of this sub-sector are mostly underground, unofficial, irregular, informal, shadowy and parallel. The most predominant type of informal finance in Nigeria is the Esusu. Among the Yorubas, it is called either Esusu or Ajo. Among the lgbos, it is called lsusu or Utu

while the Edos call it Osusu. The Hausas call it Adashi', the Nupe Dashi, the Ibibio Etibe, while the Kalahari calls it Oku [11]

2.2Theoretical framework

The Lewis theory of development will be adopted as the framework for the study. The dual-sector model is a model in developmental economics. It is commonly known as the Lewis model after its inventor W. Arthur Lewis. It explains the growth of a developing economy in terms of a labour transition between two sectors, the capitalist sector and the subsistence sector. The capitalist sector can be likened to the formal sector while the subsistence sector is the informal sector.

Lewis defined the capitalist sector sector as "that part of the economy which uses reproducible capital and pays capitalists thereof". The use of capital is controlled by the capitalists, who hire the services of labour. It includes manufacturing, plantations, mines etc. The capitalist sector may be private or public. While subsistance sector was defined by him as "that part of the economy which is not using reproducible capital". It can also be adjudged as the indigenous traditional sector or the "self employed sector". The per head output is comparatively lower in this sector and this is because it is not fructified with capital.

The "Dual Sector Model" is a theory of development in which surplus labor from traditional agricultural sector is transferred to the modern industrial sector whose growth over time absorbs the surplus labor, promotes industrialization and stimulates sustained development. In the model, the subsistence agricultural sector is typically characterized by low wages, an abundance of labour and low productivity through a labour-intensive production process.

The primary relationship between the two sectors is that when the capitalist sector expands, it extracts or draws labour from the subsistence sector. This causes the output per head of labourers who move from the subsistence sector to the capitalist sector to increase.

The Lewis model underestimates the full impact on the poor economy of a rapidly growing population, i.e. its effects on agriculture surplus, the capitalist profit share, wage rates and overall employment opportunities. Similarly, Lewis assumed that the rate of growth in manufacturing would be identical to that in agriculture, but if industrial development involves more intensive use of capital than labor, then the flow of labor from agriculture to industry will simply create more unemployment [1]

Lewis visualized the rural sector as a source of 'unlimited supply' of labour which could be tapped for the development of the industrial sector. He recommended increasing the urban wages slightly more than the rural wages so that this becomes attractive for the people living in the rural areas to migrate to the urban area and be absorbed into the industrial sector.

However in this context, Lewis failed to put into the consideration the constraint capacity of the formal sector to absorb the surplus labour in the informal sector. The formal sector has limited capacity to absorb the growing population that might erupt from the informal sector if the lewis model be implemented. This is because the shadow economy is currently a substitute to the formal economy and not the formal economy being substitute to the shadow economy.

Hence the shadow economy should collaborate with the formal economy rather compete for survival.

III. METHODOLOGY

The study made use of secondary data gotten from various sources among which include but not limited to National Bureau of Statistics, Central Bank of Nigeria, Statistical Bulletin and other research works. Data collected will be analysed using descriptive statistics.

IV. DISCUSSION AND ANALYSIS OF FINDINGS

The Nigerian economy is basically a cash-based economy with considerable proportion of the narrow money stock in the form of currency outside the banking system. Although the average ratio of the currency outside the banking sector (COBs) to narrow money supply (M) trended downward from 61.1% in the 1960s to 44.3% in the 1970s and later to 40.9% in the 1980s, the value, in nominal terms, was still high considering the growth in the level of narrow money in the economy [13]

Various policies were put in place to ensure a reduction in financial exclusion among which includes:

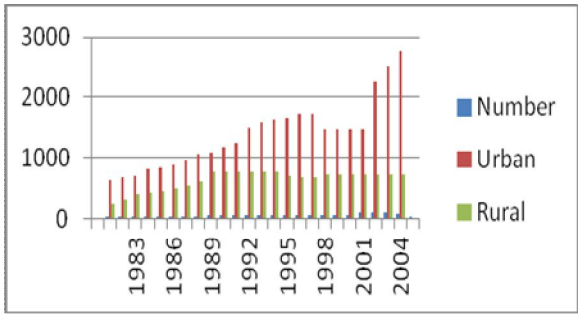


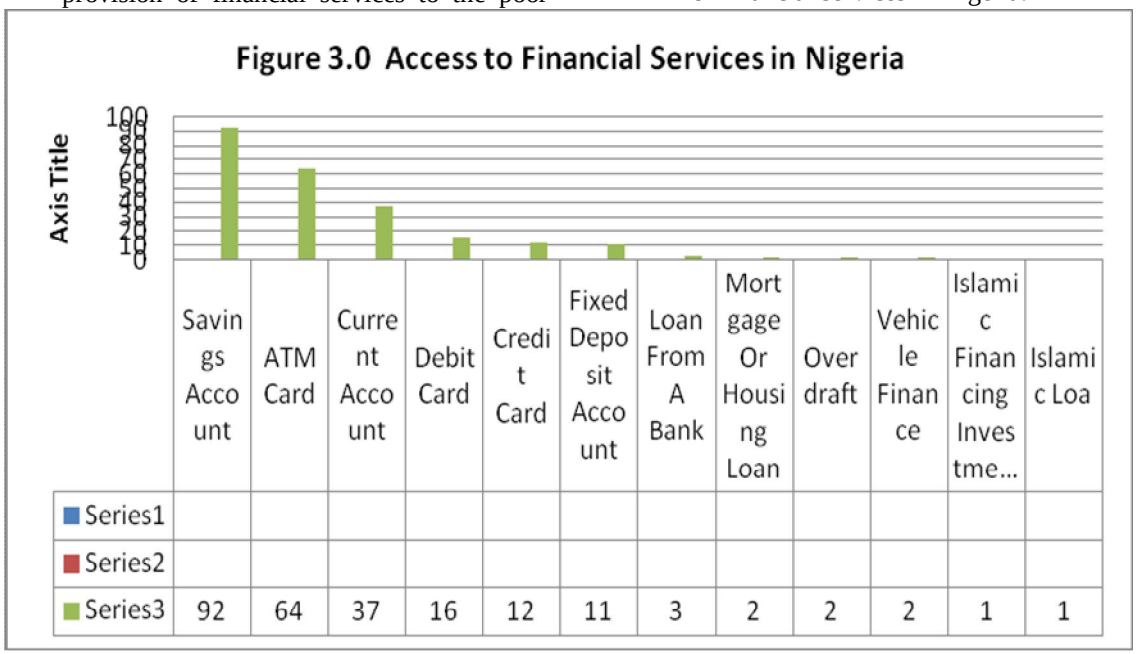
Figure 1.0 Distribution of Commercial Banks in Rural and Urban Areas

(CBN Statistical Bulletin, 2005)

- The adoption of the rural banking programme in the late 1970s. The Scheme was introduced by the Central Bank in 1977 with the goal of achieving one bank branch in each of Nigeria's Local Government Areas. The aim was to ensure mobilisation of savings, promote banking habit and make

credit facility available and affordable in the

- Financial System Strategy 2020 (FSS2020): It identified six stakeholders and six initiatives within the financial sector. The stakeholders include the suppliers of financial service in the financial sectors among which are banking institutions, non-bank financial institutions, insurance companies, capital market players, pension institutions. The six initiatives adopted to strengthen the domestic financial market include the development of varied financial products, enhancement of payment processes; development of credit system; and encouragement of a savings culture
- Microfinance Banking Policy: The microfinance model was adopted to replace the community banks. Which involve the provision of financial services to the poor rural areas. and low-income earners to ensure financial services are taken to the unbanked and those considered poor. These microfinance institutions were duly supervised and legal framework provided by the National Microfinance Policy of 2015. Currently there are about 1024 microfinance banks duly registered with the Central Bank.
- Interest Free Banking: This bank was introduced in June 2011 which is expected to bring into the banking sector a large number of the country's population that had hitherto steered away from the organised conventional financial services, due to their aversion to interest and interest-based products. Jaiz bank is a product of this scheme. Figure 3.0 show the current demand for financial services in Nigeria.



EFInA 2016 (Access to Financial Services in Nigeria)

- Alternative Electronic Channel: This era witness the adoption of new technology and its innovation to advance the growth of branchless banking. A critical example is the use of ATM and Point of Sale (POS). So, as part of efforts to achieve the National Financial inclusion Strategy goal, the CBN in 2011 licensed 21 companies (comprising of 15 non-bank operators and 6 bank operators) to offer mobile payment services. Following this, the CBN introduced agency banking, which allows banks and mobile payment operators (MPOs) to render services through third parties in various locations
- Cashless Policy: This policy has three basic objectives to develop and modernise the payment system; reduce banking cost to drive financial inclusion; and improve effectiveness of monetary policy. In other words, the policy was expected to drive financial inclusion based on the implicit assumption that reduced banking cost and more efficient payment system will encourage more people and business to embrace the formal financial service platforms.

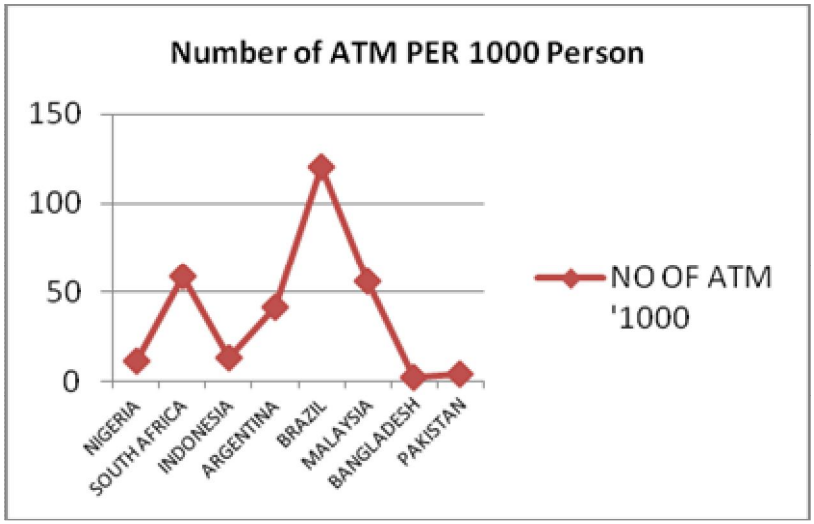


Figure 2.0 Comparative Number of ATM Terminals Per 1000 Person in different Countries

(EFLA, 2016)

4.2Challenges of Financial Inclusion in Nigeria

The successes of financial inclusion in Nigeria have been marred with various constraints identified in many literatures which is inherent in a typical African society as a result of some primitive norms and habit gained from some cultural practices. Among them are identified as follows;

In Nigeria, most citizens have challenge with means of identification which is a basic requirement for opening of account. Most dwellers in the rural areas which host the bulk of the shadow economy do not have valid means of identification.

Also a major drawback to the financial inclusion in the shadow economy is the utility bill usually requested for as means of address verification during account opening process as part of the Know Your Customer initiative introduced by the Central Bank of Nigeria. Among the utilities usually requested for are Electricity Bill, Water Bill, 3 months' Bank Statement, Tenancy Agreement etc. Objectively, Most participants in the shadow economy do not received the public utility usually requested for coupled with the decadence in the public infrastructure, a whole lot of the players in this sector do not enjoy any of the facilities.

Distance to the nearest financial institution is also a major constraint to financial inclusion of the shadow economy. Financial institutions are usually cited in areas that are geographically profitable but not necessarily socially beneficial. Hence in most cases, there is heavy presence of all financial institutions in the administrative headquarters and State capitals that are already financially included as against the rural areas that are financially excluded. Often the main barrier to financial inclusion in rural areas is the great distances that rural residents must travel to reach a bank branch. Poor infrastructure and telecommunications, and heavy branch regulation, also restrict the geographical expansion of bank branches (CGAP, 2009)

Complexity in the structure and operation of financial institutions are also limitation to the policy of financial inclusion. The structure of commercial banks in Nigeria favours the educated and enlightened in which processes becoming too technical to most participants of this sector. In most cases, medium men in form of interpreters are often brought to banks in other to simplify the process and make it understandable.

Sensitivity to charges is also a detriment to account opening. The current monthly charge of N52 in respect of debit card maintenance is seen as heavy burden. It should be noted that the masses are often the main drivers of the informal sector hence the incident of bank charges goes a long way at discouraging the use of financial service. Another similar discouraging charge is the account maintenance fee of N1 per Mille for current accounts. Other charges include stamp duty charge of N50 for every deposit above N1,000 on demand deposits. This and other charges make the players of the shadow economy opt for local means of savings.

The rise in unemployment rates in the country is deemed to be the main driver of the informal sector in Nigeria. There is often no conscious determination of citizen to be players of the shadow economy. Most members often enter as a result of some forms of financial, social, economic or educational disadvantages hence opt for this sector as the last hope of the unemployed, dejected and marginalised.

Rural financial ecosystems are still controlled by informal operators (not regulated by banking regulations - this includes moneylenders, rotating or accumulating savings, credit associations, self-help groups (SHG) and private companies), providing three types of financial products simple credit facilities, basic saving account or a fixed deposit and insurance.

May be its time to take stock of the situation and reboot financial inclusion with a different approach.

For true financial inclusion to happen governments needs to include the semi-formal/informal sector rather than competing with them.

CONCLUSION AND RECOMMENDATION

There is need to explore the potential of Digital Financial Services (DFS) market in Nigeria who has telecommunication base of about 148 million mobile phone subscribers. Digital financial services (DFS) can expand the delivery of basic financial services to the poor through innovative technologies like mobile-phone-enabled solutions, electronic money models and digital payment platforms Mobile services are seen as viable tools to provide basic financial services through mobile technology platform. It is well-developed in other countries with large unbanked populations. Countries such as Cote d'Ivoire, Somalia, Tanzania, Kenya, Uganda and Zimbabwe have more adults using mobile money accounts than traditional financial institutions.

Since a major potential for financial inclusion is new technology and a major reason for financial exclusion of the shadow economy is the low literacy rate, hence electronic channel should be modify into indigenous languages that will warrant no formal education towards its usage.

The Biometric Verification Number (BVN) enrolment report obtained from NIBSS revealed that there are about 86.5 million Nigerians with bank accounts. While that is cheering, statistics from the Nigerian Communication Commission (NCC) leave plenty to actually worry about; as it shows that there are over 148 million mobile phone subscribers. Technically, about 60 to about 90 million Nigerians with mobile phones don't have bank accounts and also do not have access to financial services. Hence, since phone numbers are distinct to individuals and in most cases linked to BVN, it should be adopted as account numbers.

Account opening conditions and documentations need to be reduced to capture prevailing cultural and geographical reality while the KYC requirements should be tailored to take care of the realities in some areas. With the advent of unique Bank Verification Number which incorporate the KYC requirement in its enrolment process. Hence to avoid monotony, the KYC requirement should be streamlined.

Profiteering via excessive charges by financial institutions should be grossly controlled. The strategy of invisible charges should be phased out completely across board. The burden of Stamp duties charge should only be borne by corporate customers who operate in the formal economy as against the shadow economy. This will go along way at encouraging financial inclusion. As against this, interest on savings account should be more attractive for retail deposits as this will boost the savings culture. This can be done by proper segmentation of customers in banks to distinguish the informal sector from formal sector via scheme codes.

Since monthly card maintenance charge is been re introduced then the debit cards should be given at no cost as the cost of production can be recouped from the accumulated charges gotten thereafter. This will go along way to encourage the shadow economy.

In the context of various shortcomings in delivering subsidies, direct transfers using technologies. It is impossible to open branches in every place. Rather to make it easier to open electronic accounts. Technology adaptation by informal sectors would be key feature in this financial inclusion.

REFERENCES

[1] Wikipedia, (2017): 'Informal Sector' Wikipedia, Free Encyclopaedia. https://en.wikipedia.org/wiki/Informal_sector

[2] Terence Mills and Kerry Patterson (2006.): Palgrave Handbook of Econometrics, Vol. 2, Palgrave Macmillan

[3] Schneider F, Andreas Buehn and Claudio E. M. (2010) Shadow Economies all over the World: New Estimates for 162 Countries from 1999 to 2007 World Bank regional report.

[4] IFC (2010). The SME Banking Knowledge Guide. IFC,Washington, DC

[5] Isabella M, (2017)From Financial Inclusion to Financial Health: Addressing the Fundamental Barriers to Financial Inclusion – Part 2. Accessed https://letstalkpayments.com/from-financial-inclusion-to-financial-health-part-2/

[6] Demirguc-Kunt, A and Klapper, L. (2012) "Measuring Financial Inclusion : The Global Findex Database. Policy Research Working Paper; No. 6025. World Bank, Washington, DC. © World Bank. https://openknowledge.worldbank.org/handle/10986/6042

[7] CGAP, (2010), Digital Finance Interoperability & Financial Inclusion, 2016 – http://www.cgap.org/publications/digital-finance-interoperability-financial-inclusion

[8] EFInA (2016), Access to Financial Services in Nigeria 2014, Survey

[9] Sarma, M. and Pais, J. (2008), "Financial Inclusion and Development: A Cross Country Analysis."

[10] Magbagbeola, Nelson O. (1996), "The Role of the Informal Sector in Nigeria's Post-Adjustment Economy", in Nigerian Economic Society Beyond Adjustment: Management of the Nigerian Economy. Ibadan, Nigeria

[11] Ekpo, A.H. and O.J. Umoh (2003) "Economics of the Environment" Nigerian Journal of Social and Development Issues, Vol.1, No. 1, June, pp. 25-36.

[12] Okorie, F.A. and Miller, L.F., 1976. Esusu clubs and their performance in mobilizing rural savings and extending credit, Ohaozara sub-division, East Central State, Nigeria. Tech. Rep.

[13] AETR. 76/1, Department of Agricultural Economics, Univ. Ibadan, Nigera.

[14] Kama and Adigun, (2013) Financial Inclusion In Nigeria:Issues And Challenges Cental Bank of Nigeria Occasional Paper No. 45

★★★