



EFFECT OF UNEMPLOYMENT AND INFLATION ON ECONOMIC GROWTH IN NIGERIA (1985-2017)

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Abstract

This paper studies the effect of unemployment and inflation on the Nigeria economic growth (GDP) from 1985 – 2017. Secondary Data was used, and the relevance of Ordinary Least Square (OLS) technique was also use in determines the effects of unemployment and inflation on GDP. Granger Causality test, was also used to examine the causation between unemployment and inflation on GDP. The results of OLS from the model indicates that unemployment and inflation has an insignificant relationship with GDP which implies that with increase in GDP, ceteris paribus inflation rate will increase, so also unemployment rate. The results of the Causality test also suggest that LGDP does not granger causes inflation as indicated in the Probability value (0.0755), while LINF also does not granger causes unemployment as indicated also in the Probability value (0.0593). A major policy implication of this result is that, there has been no effectiveness in terms of monetary policies aimed at tackling or controlling the inflation rate in Nigeria. Furthermore, the rate of inflation and unemployment was too high to the point that it created impediment to investment, rather it scares away investors. Therefore, Policy makers and researchers in Nigeria should intensive effort or adopt a proper monetary and fiscal policy that can reduce the prices of goods and services in order to boost the growth of the economy that can lead to investment, subsequently employment will be followed.

Keywords: Unemployment, Inflation, Economic Growth, Nigeria

Introduction

Nigeria as an open economy since its independent has perused some macroeconomics policies and programmed in order to attain stability in its economic growth. This policies include among others, is the attainment of a reasonable level of economic growth. Most of this economic growth are coming from the oil sector which accounts for more than 75 % of the country total GDP and the oil sector is face with a low level of capacity utilization or employment, or it has remained largely underdeveloped despite the increases in growth rate declare every year (Balami 2006).

Unemployment and inflation are some of the major problems currently being faced in the 21st century and the Nigerian government is not an exemption. Unemployment is a situation whereby people, who are physically fit, capable, qualified and ready to work at any time, but without jobs (Fatukasi, 2012). The issue of unemployment in Nigeria is highly different compared to other nations. This is due to high level of corruption, mismanagement of public funds, among others over the years. One major challenge of policy makers are how to maintain low unemployment level as well as relatively stable prices so as to achieve higher economic growth. The National Bureau of Statistics (NBS) put the unemployment rate at 14.2 % in the last quarter of

2016 up from 13.9 % in the preceding quarter and it's the ninth consecutive quarter that the unemployment rate has been increased, however, the current rate of unemployment in Nigeria is put at 18.80 percent in 2017. Unemployment Rate in Nigeria averaged at 10.63 percent from 2006 to 2017, reaching an all-time high of 24.5 percent in 2012 and record low of 5.10 percent in the fourth quarter of 2010, and when compare with emerging economies such as Brazil, the situation in Nigeria is highly alarming. The unemployment rate in Brazil is 12.3 percent in 2017.

Not only the level of unemployment that is disturbing along, the level of inflation is also raising with an increase of two digit figure, if combining together will affect the level of economic growth which resulted from high inflationary pressure, against a high rate of unemployment and underemployment, a large public sector, low wages and poor working conditions has been persistent in the country. The issue of unemployment brought about some social and economic consequences such as; increase in crime rate, loss of respect and identity, reduction in purchasing power, psychological injuries, corruption among others.

According to (Fatukasi, 2012), inflation refers to a sustained rise in general price level. Inflation can affect all aspects of a country through influencing economic growth, employment, investment, distribution of income and wealth, and even social and political conditions. Available data showed the current inflation rate in Nigeria at 14.15 percent in 2017. Inflation Rate in Nigeria averaged 12.49 percent from 1996 to 2018, reaching an all-time high of 76.8 percent in 1994 and a record low of 0.2 percent in 1999 as shown by the National Bureau of Statistics (NBS). Thus, Unemployment, inflation and GDP are termed as nonstop and unfriendly situation that describe the common nature of a country's economy.

According to Balami (2006), policy-makers generally believed that inflation causes a more serious problem than unemployment in a society. The most important task of economists and economic officials in every country primarily lies in controlling inflation in order to achieve economic growth with development of appropriate infrastructures. Experiencing high levels of development in the past decades has kept inflation at a low level, promoted social welfare and provided high levels of living standards for the citizens. It seems that necessary conditions for targeted control of inflation rate in Nigeria can be met by adopting required fiscal tools and complementary monetary policies.

Economic growth is a key policy objective of any government in addressing important issues in economic management, experts and economic planners have to choose between or combine some of these macroeconomic variables, such as inflation and unemployment in achieving Economic growth. There are so many policies which have effect on inflation, unemployment and economic growth with abundant amount of human and natural resource. If properly implement, will led to a reasonable rise in economic growth and reduction in inflation and unemployment in Nigeria.

However, this growth has not translated into lower level of inflation and unemployment rate. Nigeria GDP is averaged at 1.08 percent from 2010 to 2018, reaching an all-time high of 10.59 percent in the third quarter of 2010 and a record low of -13.98 percent in the first quarter of 2016. Available data show by the National Bureau of Statistics (NBS), indicate that the Nigerian economy grew relatively in the greater parts of the 1970s, with respect to the oil boom of the 1970s; the outrageous profits from the oil boom encouraged wasteful expenditures in the public sector, upset in the employment factor and also distorted the revenue bases for policy planning.

However, the researcher hope that the effort of the Nigeria government over the years on the level of inflation and unemployment should not be undermine and government need to enhances its social and economic policies in the society and the country at large in order to reduce this problem and base on this, so many question has arises because of this phenomenal.

Growth in Nigeria was not encouraging and the trends in the economic growth rates, unemployment rates and inflation rates over the period 1985-2017 have been confusing. The data obtained from the Central Bank of Nigeria (CBN) 2013, Statistical bulletin revealed that 1986 economic growth rate stood at 3.1 percent, in 1987 the value became negative -0.69 implying retrogression and was the least ever achieved for the period under review; the highest economic growth rates achieved was 11.36 in 1990 after which the rates has been terribly until 2003 when the growth rates hits 10.2 percent.

Similarly, several studies were conducted and despite the level of economic growth and persistence increase in unemployment and inflation, government have put tremendous effort in solving this problem. The level of unemployment and inflation is still rising, and the rate of economic growth is alarming. However, many studies were conducted and the studies were jointly in academically aspect in order to address this problem, but still the rate of inflation and unemployment is still persistence. There are all sort

of problem, probably in the study or difference methodology that was been adopted and the recommendation from the result did not yield the required expectation of the real impact of this study.

Literature Review

Unemployment can be defined as a situation in which people are willing to work at the prevailing rate of pay, but cannot find a job. Jhingan, M. L. (2001). However, he has categorized unemployment as frictional, seasonal, structural or cyclical in nature. Frictional unemployment refers to a situation when people are temporarily unemployed. This may arise due to changing labour force and jobs in an economy. Seasonal unemployment on the other hand refers to a situation when people lose their jobs due to the nature of jobs. Structural unemployment arises in an economy when all factors of production are committed to production of goods and services (full-employment). While, cyclical unemployment is caused as a result of changes in aggregate demand.

The major causes responsible for the persistence of unemployment in Nigeria include the following; slow growth of the economy, undiversified economic structure, inadequate infrastructure, Shortages of skilled personnel, inadequate capacity of vocational skills etc Balami (2006).

The problem of unemployment has in recent years aggravated the problem of poverty, political instability and insecurity in Nigeria. As such the provision of employment opportunities and eradication of poverty has been at the center stage of economic policy reform in Nigeria. For example the National Economic Empowerment Development Strategies (NEEDS) have job creation, poverty reduction and wealth creation as its major goals (National Planning Commission, 2004).

Concept of Inflation

It is the persistent increase in the general price level within the economy which affects the value of the domestic currency (Fatukasi, 2012). It is not once and for all upward price movement but has to be sustained over time and affect all goods and services within the economy. There are several factors that are responsible for inflation in Nigeria. The inflation which results from excess aggregate demand is called the demand Pull inflation. The cost push inflation results from upward movement in the cost of production while the structural inflation arises from some constraints such as inefficient production, marketing and distribution systems in the productive sectors of the economy (Fatukasi, 2012). Other forms of inflation in developing countries could be imported, open and seasonal inflation. In Nigeria other factors can be attributed to inflation such as, the fiscal and monetary policy direction. Emeka (2013).

In the words of Friedman, inflation is always and everywhere a monetary phenomenon and can be produced only by a more rapid increase in the quantity of money than output.” Dernberg and McDougall (1976) are more explicit when they wrote that the term inflation usually refers to a continuing rise in prices as measured by an index such as the consumer price index (CPI) or by implicit price deflator for gross national product.

Concept of Economic Growth

Based on its multi-dimensional nature, the term economic growth is described as the positive and sustained increase in aggregate goods and services produced in an economy within a given period of time. When measured with the population of a given country, then economic growth can be stated in terms of per capita income according to which the aggregate production of goods and services are produced in a given year is divided by the population of that country. Lewis (1978). According to Balami (2006), economic growth can be defined as a sustained increase in per capita national output or net national product over a long period of time. It implies that the rate of increase in total output must be greater than the rate of population growth. Another quantification of economic growth is that national output should be composed of such goods and services which satisfy the maximum want of the maximum number of people. Economic growth is the quantitative increase in the monetary value of goods and services produced in an economy within a given year. Balami (2006).

Theoretical Framework

Keynesian theory of Aggregate demand

John Maynard Keynes is often referred to as the father of macroeconomics. His pioneering work "The General Theory of Employment, Interest and Money" published in 1936 provided a completely new approach to the modern study of macroeconomics. The notion of "effective demand" and its influence on economic activity was the central theme in Keynes's Theory of Effective Demand. While refuting the Classical theory which believed in strong general tendency of market mechanism to move output and employment towards full employment, Keynes explained that, in some situations, no strong automatic mechanism moves output and employment towards full employment levels. Keynes was the first economist to advocate the role of government especially fiscal policy, as the primary means of stabilizing the economy.

The concept of aggregate demand (AD) refers to the total demand for goods and services in an economy. AD is related to the total expenditure flow in an

economy in a given period. It consists of the following:

- Consumption demand by the households (C)
- Investment demand, i.e., demand for capital goods (I) by the business firms.

- Government expenditure (G)
- Net income from abroad minus Net income from domestic goods (X – M).

Thus symbolically, it can be written as equation (1)

$$AD = C + I + G + (X-M) \dots\dots\dots (1)$$

According to Keynes, full employment is not a normal situation as stated in the Classical theory. He argued that economy's equilibrium level of output and employment may not always correspond to the full employment level of income. It is possible to have macroeconomic equilibrium at less than full employment. If current level of aggregate demand (expenditure) is not adequate to purchase all the goods produced in the economy (i. e. a situation of excess supply) then output will be cut back to match the level of aggregate demand. Aggregate demand or what is called aggregate demand price is the amount of total receipts which all the firms expect to receive from the sale of output produced by a given number of workers employed. Aggregate demand increases with increase in the number of workers employed.

The Theory of Inflation

According to classical, the key factor is the money supply because in accordance with the quantity theory of money only an increase in the money supply is capable of raising the general price level. In modern income theory, however, demand-pull is interpreted to mean an excess of aggregate money demand relative to the economy's full employment output level. The theory assumes that prices for goods and services as well as for economic resources are responsive to supply and demand forces, and will, thus, moves readily upward under the pressure of a high level of aggregate demand.

Economists like Friedman, Hawtrey, Golden Weiser, who regard inflation as a purely monetary phenomenon, strongly support this theory of inflation caused by excess money supply. The excess demand in the economy develops owing to large-scale investment expenditure either in the public or in the private sector, thereby exceeding the total output. As a result of this excess demand, prices will rise and excess demand inflation or demand-pull inflation comes to exist.

Empirical Review

In A Study, Umaru and Zubairu (2012) examined the effect of inflation on economic growth and development of the Nigerian economy. Their work covers the periods (1970 – 2010) and they applied econometric techniques of Augmented Dickey Fuller techniques and Granger causality test. Their

findings revealed that all the variables in the model are stationary and that GDP Granger cause inflation and inflation does not Granger cause GDP. This implies that, it is the output of the economy that influences a rise in the price level and not the price level causing increases in output.

In another work, Elegbede (2012) examined the causes, consequences and implication of graduate unemployment in Nigeria, his findings revealed that economic recession, government policy, employment of expatriates and trade unions wage demand are the major causes of unemployment. In a similar work, Gregory and Mark (2000) studied how wage inflation causes price inflation. They found out that wages either conventionally measured by comparison or adjusted through productivity and converted to unit labour cost are helpful for forecasting inflation. Their results indicated that, inflation helps in predicting wages, thus they concluded that higher prices leads to wage growth in an economy.

In addition, Engelbert and Simon (2012) studied the impact of monetary policy on unemployment hysteresis, their samples includes 40 recessions in 19 OECD countries. Thus, results of the econometric analysis revealed strong effects of monetary policy, and depending on the specification of change in terms of trade, but weak if any affects labour market institutions during recession periods. This implies that the unemployment hysteresis that occurs in a period of recessions depends on monetary policy reactions.

In a study, Balami (2006) investigated the relationship between unemployment and inflation in Nigeria and using time series data found that there is negative relationship between unemployment and inflation with the coefficient of -0.412, this validates the Philips hypothesis. However, the results of the causality test indicate no causality between unemployment and inflation in Nigeria.

Okafor (2011) also pointed out the problem arising from the concept of labour force. In most countries, particularly Nigeria, people below the age of 15 years and those above the age of 55, who are actively engaged in economic activities, is usually excluded

from labour statistical surveys. All these factors have the tendency to result in underestimation of unemployment thereby making international comparison very difficult. Factors such as the preponderance of full housewives (but who are willing to be engaged in paid job) and unpaid family workers also contribute significantly to the underestimation of unemployment.

Olu and Idih (2015) investigated inflation rate and economic growth in Nigeria between 1980 and 2013. The study made use of secondary data sourced from the Central Bank of Nigeria (CBN) Statistical Bulletin and the National Bureau of Statistics (NBS). The Ordinary Least Square (OLS) multiple regression was employed with Gross Domestic Product (GDP) as the dependent variable and Inflation Rate (INFR), Exchange Rate (EXCHR), Input of Labour and Input of Capital serving as the explanatory variables. Their results showed that inflation rate in line with a priori expectations had a positive relationship but non-significant with the economic growth rate. This suggested that as the GDP raises inflation also rises, meaning that there has been no effectiveness in the monetary policies aimed at tackling or controlling inflation rate in Nigeria.

Bhattarai (2016) examined the relationship between inflation and unemployment in 35 OECD countries using a panel VAR model to analyse the quarterly data used from 1990:1 to 2014:4. He submitted that the Phillip's curve is still significant in 28 out of 35 OECD countries and the coefficients of Okun curve for growth on unemployment were significant only in 13 of these countries. He concluded that as the natural rate of unemployment results from the balance between job creation and destruction processes, reductions in unemployment rates require

complementing macro stimulations by microeconomic structural and institutional reforms.

Akeju and Olanipekun (2014) validated the Okun's law in Nigeria using the Error Correction Method and Johansen cointegration technique. The findings showed that there is both a short and long run relationship between unemployment rate and output growth in Nigeria. Hence, there is need to incorporate fiscal measures and increase the attraction of foreign direct investment (FDI) to reduce the high rate of unemployment in the country. Onwanchukwu (2015) examined the impact of unemployment on the economic growth in Nigeria from 1985 to 2010, using ordinary least squares regression technique. His findings revealed that unemployment does not have a significant impact on the economic growth of Nigeria. Inflation, however, was found to significantly impact on the economic growth of Nigeria.

Methodology

The study employed ordinary least square and Granger Causality test for multiple regression method and data analysis. The data used for this study are basically time series data, secondary in nature, ranging from 1985 to 2017, which is thirty three years period of analysis. Therefore, data were sourced from Central Bank of Nigeria, Statistical bulletin and various editions, NBS statistical abstract to be used for the study.

Also, it is quite obvious that the secondary data will permit the estimation of the stochastic equation representing the impact or causes of unemployment and inflation on economic growth (GDP) of Nigeria. Data on these variables can be easily collected and estimated

Model Specification

The functional relationship is given as:

$$GDP = f(\text{Unemp}), (\text{Infl}) + Ut \dots\dots\dots (2)$$

Where:

Infl =inflation rate

Unemp= unemployment rate

GDP =gross domestic output

Ut = error term

To determine the model for a relationship between unemployment rate, inflation and gross domestic

$$LGDP_t = \alpha + \beta_1 L UNEMP_t + \beta_2 L INFL_t + \beta_3 L GDP_{t-1} + Ut \dots\dots\dots (3)$$

To determine the model for a causality effect between unemployment rate, inflation and gross domestic Product (GDP) from the above equation and due to the problem of non-stationary inherent in time series data and in particular, the real GDP, the

$$LGDP_t = a_0 + a_1 LINF_{t-1} + \dots\dots\dots + a_i LINF_{t-i} + B_1 LUNP_{t-1} + \dots\dots\dots + B_i LUNP_{t-i} + Et \dots\dots\dots (4)$$

Product (GDP), we state here the econometric Relationship of the three variables which includes the stochastic error term. And due to the problem of non-stationary inherent in time series data and in particular, the real GDP, the first difference of real GDP is used while the log of inflation and unemployment is also used. The original model is given thus:

first difference of real GDP is used while the log of inflation and unemployment is also used. The original model is given thus:

$$\text{LINF}_{it} = a_0 + a_1 \text{LGDP}_{t-1} + \dots + a_i \text{XLGDP}_{t-i} + B_1 \text{LUNP}_{t-1} + \dots + B_i \text{LUNP}_{t-i} + E_t \dots \dots \dots (5)$$

$$\text{LUNP}_t = a_0 + a_1 \text{LGDP}_{t-1} + \dots + a_i \text{XLGDP}_{t-i} + B_1 \text{LINF}_{t-1} + \dots + B_i \text{LINF}_{t-i} + E_t \dots \dots \dots (6)$$

Where t stands for time (yearly time series data), LINF denotes the Logarithm of inflation rate in Nigeria; LGDP denotes the first difference of the logarithm of real GDP and LUNP stands for the Logarithm of the unemployment rate in Nigeria while The error term or disturbance variable “μ”, as depicted in the equation, captures variable(s) that should have been in the model. The equation suggests that the size of GDP in Nigeria depends on the level of unemployment rate and inflation rate.

A priori expectation

From the model, the priori expectation may be mathematically denoted by:

$B_1 < 0, \beta_2 > 0$, in line with the GDP model, inflation rate, to a large Extent; theoretically determines the level of GDP.

Thus inflation rate (B_2) is expected to have a direct relationship with the level of GDP. Thus we expect the coefficient of inflation rate to be negative i.e. $\beta_2 > 0$.

Theoretically, Gross domestic product (GDP) is expected to have negative relationship with unemployment (i.e. $B_1 < 0$) If the GDP is evenly distributed, the living Standard will improve and unemployment will be reduce drastically. Therefore, unemployment is expected to have a negative significant coefficient. All the coefficients are expected to be statistically significant at 5%.

Results and Discussions

Table 1: Multiple Regression Results

LGDP = α 0.245 - β_1 0.026 LINF - β_2 0.011 LUEMP		
T- stat:	(0.407)	(-0.363) (-0.123)
R ² = 0.95		
F-stat = 214.7		
Durbin Watson statistic = 1.98		

Source: Author’s computation, 2018

The result from the model above indicates that unemployment and inflation has an insignificant relationship with GDP which implies that with increase in GDP, ceteris paribus inflation rate will increase, so also unemployment rate. This implies that when GDP increases by one per cent point, inflation rate of the nation will increase by 0.026 per cent point and 0.011 per cent point for unemployment. (The interpretation is on percentage point because the log of GDP, inflation rate and unemployment rate is used). It is obtains that the inflation and unemployment were found to be insignificant. In other words, they were no statistically different from zero.

This is very clear in the probability value. That is, 0.7191 for inflation rate and 0.9028 for unemployment rate respectively. On the other hand, the lagged dependent variable which is GDP _{t-1} was found to be significant in explaining variation in the independent variable.

According to the result obtained, the GDP _{t-1} co-efficient was 0.993717. This implies that, if there is increase in the lagged of GDP, by 0.99%, it will also lead to increase in inflation rate by 0.7191, so also it will have effect on the level of unemployment rate.

Thus, there is a positive relationship between the gross domestic product and its lag.

The coefficient of determination (adjusted R² = 0.95 = 95%) shows that, after adjusting for any likely error as a result of additional explanatory variable, about 95% of the variation in the GDP is accounted for or explained by the variation in unemployment and inflation rate. Meanwhile, the remaining 5% might be as a result of marginal variables not captured in the model.

The f-statistics or f-ratio which tests for the significance of the entire model or all the parameters of the model simultaneously shows that the model is significant at 5% level of significance and strongly supported the co-efficient of determination of the F-statistics, which are 214.7699. It implies that, all the variables in the model are fit in explaining the dependent variable. Fortunately, the variables are free from serial correlation with the fact that, there is a positive serial correlation, with Durbin Watson which is less than 2.

Finally, the Durbin Watson d-statistic which is 1.989 shows that, there is evidence of negative correlation. If the Durbin Watson is equal to 2, there is neither positive nor negative serial correlation. In this case,

the result of the Durbin Watson statistic is 1.99 (approximately to 2). This implies that the variables are free from serial correlation.

Table 2: Granger Causality Result

Pair wise Granger Causality Tests

Date: 10/06/18 Time: 13:49

Sample: 1985 2017

Lags: 2

Null Hypothesis:	Obs	F-Statistic	Prob.
LINF does not Granger Cause LGDP	31	0.39148	0.6800
LGDP does not Granger Cause LINF		2.85744	0.0755
LUEMP does not Granger Cause LGDP	31	1.37552	0.2705
LGDP does not Granger Cause LUEMP		1.86280	0.1754
LUEMP does not Granger Cause LINF	31	2.30478	0.1198
LINF does not Granger Cause LUEMP		3.15556	0.0593

Source: Author's computation, 2018

From the above table, LGDP does not granger causes inflation as indicated in the Probability value (0.0755). The implication is that, when there is rise in oil prices, Government will have more revenue in its output (GDP) and more money in circulation and can also lead to increase in the inflation rate as a result of excess money coming from oil prices or (GDP) output. This is in conformity with the words of the monetarist position which is in sharp contrast to Structuralist's school, who believed that financial factors are forces broadcasting inflation rather than causing it.

On the other hand, LINF does not granger causes unemployment as indicated in the Probability value (0.0593). This implies that, when there is rise in inflation rate, unemployment rate will also rise as result of high cost of raw-material or commodities good for industries which in turn will results to many companies to operate below their installed capacity and lead to collapse of many industries which will make workers to become jobless. Therefore, Government and its relevant authorities should provide conducive environment for investment by removing the structural rigidities that exist in the economy to create jobs in order to prevent high rate of inflation and subsequently lead to industrial expansion and improvement in growth rates of the economy which would provide employment opportunities for the people

Major Findings

(i) There was a positive and insignificant relationship between economic growth rates, inflation rate and unemployment rate in Nigeria during the years under review as indicated by the overall result, suggesting that increase in GDP,

increases the rate of inflation rate as well as unemployment.

(ii) There was a significant positive intercept, suggesting that there are other exogenous variables apart from unemployment and inflation that defined significant impact on the economic growth rate in Nigeria. This confirmed the Keynesian position that growth of the economy proxy by GDP has autonomous component.

(iii) The results also revealed that unemployment and inflation are positively related with economic growth, which means unemployment and inflation does not hinder economic growth. These type of growth in economic is technically termed as 'Exclusive Growth' that is, growth that does not reflects in the standard of living of average citizen of the country.

Conclusion and Policy Recommendations

The Twin Macroeconomic Variables, Unemployment and Inflation are the major problems confronting Nigerian economy which have the propensity to be among the complex economic and social dimensions. The inability of government to find a lasting solution to these problems has affected the economic life, economic activities and political system of the country as a whole. Therefore, this paper attempted to investigate the effect of unemployment and inflation on GDP in Nigeria through the application of Ordinary Least Square and Granger causality test of causation between unemployment, inflation and GDP.

Therefore, there is a need for strong institutional collaboration for dealing with these triple macroeconomic variables; unemployment, inflation and GDP in Nigeria. Consequently, policy options

suggested by this study includes: (1) the payment of unemployment benefits by the government to control social problems; (2) the curbing of inflationary trends so as to enhance investment in the economy; (3) the vocational education and skill acquisitions to improve productivity and reduce

high dependency rate in the economy; (4) There must be concrete efforts to ensure that our porous borders are well managed to forestall leakages which is very pivotal for the reduction of unemployment and inflation.

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