International Journal of Economics and Financial Issues

ISSN: 2146-4138

available at http: www.econjournals.com

International Journal of Economics and Financial Issues, 2018, 8(3), 23-28.

Quest for Industrialization in Nigeria: The Role of the Development Bank of Nigeria

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ABSTRACT

The benefits of industrialization in employment generation, poverty reduction, improved living standard, improved economic growth and development, balance of payment stability, self-reliance, stimulation of other sectors of the economy, and development of skilled manpower have been well established in the literature. However, access to finance for industrial development has remained a key challenge in Nigeria. In view of this, this paper describes what the structure and operations of the Development Bank of Nigeria (DBN) should be so that the Bank will not only deliver on the core mandate of empowering micro, small and medium scale enterprises (MSMEs) but also support the nation's quest for industrialization by adequately funding national priority projects in the areas of infrastructure, basic industries, energy, transportation, and the likes. The paper argues that limiting the mandate of the DBN only to facilitating credits for MSMEs in the informal sector will not go far in advancing Nigeria's quest for industrialization.

Keywords: Industrialization, Development Banking, Economic Development, Nigeria
JEL Classifications: O14, E51, O23, N17

1.INTRODUCTION

According to Anyanwu et al. (1997), industrialization can be explained as the process of building up a nation's capacity to convert raw materials and other inputs to finished goods, including the manufacture of goods for other production or for final consumption. It is a situation whereby many industries are established in different parts of the country for the production of many different types of products (Obioma and Ozughalu, 2005; Nyor and Chinge, 2014). In the context of a developing economy like Nigeria, industrialization can be explained as the process of transforming an economy structurally from a primarily agricultural-based or mono-cultural to a predominantly industrial-based or manufacturing economy. The immediate consequence of this transformation is that manual labour is replaced by mechanized labor and craftsmen by assembly lines. The industrial sector in Nigeria includes the manufacturing, construction, electricity, mining, water and gas industries (CBN, 2002).

The benefits of industrialization in employment generation, poverty reduction, improved living standard, improved economic growth and development, balance of payment stability, self-reliance, stimulation of other sectors of the economy, and development of skilled manpower have been well established in the literature (Audi and Mohammed, 2014; Nyor and Chinge, 2014; Mba, 2015). Other studies such as Simandan (2009), Ortiz et al. (2009), and Agba and Odu (2013) support the submission that industrialization leads to large scale production of goods which are available to the consumer at much cheaper rates; saving of time and labor; considerable rise in the standard of living of the people; a variety of substitutes in consumer goods; creation of new job opportunities, leading to the removal of poverty to a great extent; and the development of new modes of transportation. It is therefore obvious that every country that has become a manufacturing hub and taking advantage of scale economies to achieve rapid growth in productivity and living standards, at least in the past few decades, has done so by industrializing.

The desire to realize the above benefits had propelled Nigeria to pursue several industrialization policies since the 1960s (Audi and Mohammed, 2014; Nyor and Chinge, 2014; Tamuno and Edoumiekumo, 2012). Among others, such industrialization policies include the import-substituting industrialization strategy embedded in the first national development plan of 1962–1968, which in the main emphasized domestic production of manufactured goods for domestic markets (Busari, 2005); the indigenization policy of 1972 and 1977 aimed at preparing indigenous entrepreneurs for rapid industrial development; the export promotion industrialization strategy embedded in the structural adjustment programme of 1986, which emphasized domestic production of manufactured goods for export in order to generate more foreign exchange particularly from non oil sources to meet the country's rising import bills, mounting external debt obligations, rising fiscal responsibilities of the government, and to attend to socio economic responsibilities (Obioma and Ozughalu, 2005); the foreign private investment led industrialization strategy adopted since 1999 after years of military dictatorship and targeted at restoring investor's confidence in the Nigerian economy in order to attract massive inflow of foreign capital in the industrial sector; the small and medium enterprises development agency of Nigeria established in to cater for the development of SMEs in Nigeria; and the national economic empowerment and development strategy, which in the main was aimed at growing the private sector as the engine of growth for wealth creation, employment generation and poverty reduction (Okereka, 2015; Ekpo, 2014; Nyor and Chinge, 2014).

Despite the implementation of the above industrialization policies, Nigeria is still far from being industrialized (Nyor and Chinge, 2014). In fact, it seems as if the more the industrial policies Nigeria implements the more the country moves away from being industrialized. These facts indicate that the country has faced several challenges in its journey to industrialization. Ekpo (2014) specifically identified a myriad of factors militating against Nigeria's industrial development. These include poor policy conceptualization and implementation; lack of technological capability, which is a sine qua non for industrial development; high cost of production resulting in non-competitiveness of Nigeria's manufactured goods in both local and international markets; concentration on light consumer goods instead of capital goods which sustain industrialization; inadequate infrastructure such as transportation, water supply, electricity supply and telecommunications, which are crucial enablers of industrialization; and poorly developed human capital. Apart from Ekpo (2014), other studies have also highlighted the challenges impeding Nigeria's journey to industrialization. Some of these challenges include a weak raw material base since more attention is being channeled into mining following the discovery of oil, inadequate technical manpower, poor policy implementation, lack of entrepreneurship skills, political instability arising from several military interference in governance, corruption in private and public sectors, and lack of finance for industrial development activities (Iwuagwu, 2009; Ayodeji and Balcioglu, 2010; Chete, et al., 2014; Isiksal and Odoh, 2016). These points indicate that Nigeria has enormous challenges to overcome in its quest for industrialization. As a step towards solving the problem of lack of finance for industrial development in Nigeria, it is the goal of this study to describe what the structure and operations of the development bank of Nigeria (DBN) should be so that the bank can act as a conduit for powering the nation's industrial development. The overall motivation for this study is therefore situated in the fact that without a proper structure in terms of management and operations, the DBN will not be able to support the nation's quest for industrialization by ensuring that projects of national priority in the areas of infrastructure, basic industries, energy, transportation, and the likes are adequately funded. In other words, we submit in this paper that restricting the operations of the DBN only to increasing access to finance by micro, small and medium scale enterprises (MSMEs) will be not go far in industrializing Nigeria.

2. DEVELOPMENT BANKING: WHAT IS IT AND WHY DOES IT MATTER?

In the foregoing section, lack of finance for industrial development was identified as a key challenge confronting industrialization in Nigeria. In this paper, we argue that the DBN has important role to play towards overcoming this challenge. However, the structure and operations of the Bank (i.e., the DBN) must be properly articulated for it to adequately discharge its responsibilities towards a more industrialized Nigeria. To begin, a development bank (or synonymously, a development finance institution [DFI]) is a type of financial intermediation institution that helps a country reach a higher and sustainable level of development. In this context, the desired level of development includes the whole spectrum of industrialization. This means that a development bank is a national or international financial institution designed to provide medium-and long-term capital for productive investment, usually accompanied by technical assistance, in developing countries. Simply put, a development bank is a bank designed for the function of development financing. Such a bank typically fills the gap left by undeveloped capital markets and the reluctance of commercial banks to offer long-term financing for critical development projects. In sum, development banking can be explained as a form of financial intermediation that provides financing to high priority investment projects in a developing economy (Pragash, 2016; ADFIAP, 2009). Such investment projects are usually geared towards the attainment of the ultimate goal of industrialization.

Historically, development banking dates back to the days industrial expansion in countries now considered to be more industrialized. More than a century ago, the U.S., the Great Britain and a number of other Central European countries built their industrial base. These highly industrialized countries attained industrialization through long-term investment financing of banks that, at the time, performed the entrepreneurial function of funding high risk projects or taking on the risk of entering into new fields of production. Such development financing banks or institutions involved in long-term financing were then called industrial banks. A typical example of this type of financing was the construction of the railroads in the U.S., which goes even back to the 1700s (ADFIAP, 2009). Presently, many national and regional development banks have been established around the world. Examples include the African Development Bank (ADB) established in 1964, the inter-American development bank established in 1959, the Asian development bank that started operations in 1966, the ECOWAS bank for investment and development (EBID) established in 1999; and so on. A common feature of these institutions is that they are all committed to engendering industrialization in their member countries. For instance, the mission of EBID is to create an enabling environment for the emergence of economically strong, industrialized and prosperous West Africa; while the mission of ADB is to spur sustainable economic development and social progress in its regional member countries, thus contributing to poverty reduction. An important point here is that profitability in terms of financial returns is not a paramount goal in development banking, rather, economic, social and ecological objectives are giving priority considerations (Pragash, 2016; ADFIAP, 2009).

Apart from the fundamental desire to industrialize, there are other important reasons for the remarkable growth in the number of development banks across the globe. We summarize them as follows. First, commercial banks (or synonymously, deposit money banks) that dominate most financial systems are usually either contented with short-term banking activities or unwilling to support national priority long-term investments in the real sectors. This clearly represents a market failure that requires government intervention through the establishment of national or regional development bank. Second, developing countries, especially the war-ravaged ones, cannot continue to rely on their existing financial institutions to accelerate long-term investment, which will in turn lead to rapid industrial development. They need "special purpose vehicles" such as development banks to realize their ultimate goal of industrialization. Furthermore, developing countries require the expertise and high degree of efficiency usually associated with specialized banks like development banks to drive investments in key industrial projects so that they can achieve their job creation and poverty reduction objectives (Pragash, 2016; ADFIAP, 2009).

In general, development banks perform five main functions in the industrial and economic advancement of a country. One, as development advocates, they promote the "business of development" such as resource mobilization and allocation, urban renewal, employment generation, and so on. Second, as institution-builders, they develop new methods and systems for raising and increasing investment capital, such as through bonds, private-public partnership financing of large projects under build-operate and transfer arrangement, and so on. Third, as catalysts, they take the lead in developing new financial products in areas where conventional commercial banks will usually avoid, such as guarantee schemes for start-up industrial projects, loan syndication for large industrial projects, and so on. Fourth, as initiators with "supply-leading" roles, they take the lead in supporting strategic industrial sectors like the SME sector, environmental issues, technology transfer, and the likes. Lastly, as bankers of last resort, they provide funding for national priority industrial and economic projects which no other financial institution is willing to finance, thereby promoting industrial and economic advancement (Pragash, 2016; ADFIAP, 2009).

Four main development banking models have been observed in the literature and we describe them briefly following ADFIAP (2009). First, there are policy development banks created to directly support the national government's economic policies, e.g., China development bank. Second, there are special-purpose development banks created to support specific sectors of the economy, e.g., the DBN, created to address the challenges of high interest rates, collateral requirements, and short tenure of loans facing informal sector operators, which function mainly as MSMEs; the Asian Infrastructure Investment Bank and the agricultural development bank in India. Third, there are multi-purpose or universal development banks that undertake both development projects and commercial businesses, e.g., development bank of the Philippines. Lastly, there are commercially-oriented development banks that undertake development through commercial banking services, e.g., the development bank of Singapore (DBS bank).

3. HOW DO DEVELOPMENT BANKS DIFFER FROM COMMERCIAL BANKS?

At this point, we must explain some salient differences between development banks and commercial banks. While the former is created as an instrument of industrial and overall economic development, the latter is created by business opportunities for the main aim of maximizing profits. While development banks are entrepreneurial and pro-active in promoting investment projects and developing institutions, commercial banks are generally reactive to business opportunities since they usually bank transactions after the entrepreneurial decisions have been made. Development banks' activities are predominantly project-based as deliberate efforts are made to finance industrial and economic development projects in the areas of import substitution, export promotion, regional integration, and increased industrial efficiency through technology transfer; while commercial banks have little or no concern for these objectives as their activities are mainly transaction-based. Development bank generally provide counseling and advisory services part of their development lending process, while commercial banks are associated mainly with legal and business advice, appraisal services and credit investigation, usually for a fee. Development banks place less emphasis on collateral, they generally assume project risks; but commercial banks place great emphasis on collateral compared to the project cash flow (Pragash, 2016; ADFIAP, 2009).

Development banks are project-oriented and therefore use project appraisal, which considers the technical, financial, marketing, management, environmental and economic aspects of the project, as a means of selecting viable projects for financing; but commercial banks are borrower-oriented and employ risk management procedures, which consider the 5 C's of credit (character, capacity, capital, collateral and condition), as a means of selecting transactions for funding. While loan repayment in development banking is anchored on the projects cash flow, repayment in commercial banking is based on borrower's capacity (even from other sources outside the transaction). Development banks offer mainly term loans of several-year maturity and often with years of moratorium; but commercial banking is mainly associated with short-term loans or overdrafts of <1 year maturity. This is mainly because development banks obtain funds from concessionary and long-term sources such as pension funds, multilateral financial institutions like the World Bank, ADB, and the likes; while commercial banks usually match their borrowing against their short-term deposits. Development banks promote investment projects in order to match them with concessionary long-term financing, while commercial banks generally mobilize deposits from numerous small depositors, which they in turn lend out to companies. Development banks are specialized institutions in nature, and therefore have limited branching network and range of products, whereas commercial banks are more universal or generalized in character and therefore have extensive branch networks and wide range of products (Pragash, 2016; ADFIAP, 2009).

4. WHY DO DEVELOPMENT BANKS FAIL IN THEIR INDUSTRIALIZATION CUM ECONOMIC DEVELOPMENT OBJECTIVES?

The failure of most development banks to deliver on their industrialization, social and overall economic development goals have been attributed to a number of reasons in the literature. In what follows, we summarize these factors. One main factor impeding the success of most development banks is their inability to mobilize and make vast amounts of money available for large bang development projects that can actually fire the light of industrial and overall economic development. This is particularly the case with most national development banks that are wholly or exclusively funded by national governments. A sustainable development bank should be able to mobilize funds cheaply from a variety of sources such as through bonds, pension funds, from multilateral financial institutions like the ADB and the World Bank or through loan syndication. This will enable it to undertake large industrial and economic developmental projects like rail and other transportation projects, pipeline projects, power generation projects, and the likes, which conventional commercial banks would ordinarily avoid like a plague (Serre, 2005; Lazzarini, 2011; Gutierrez et al., 2012).

Another important factor is lending at very high interest rates, which at best are worrisome and predatory. This clearly negates the broad objective of development banking, which is to act as an instrument for industrial and overall economic development. It must be stressed that whatever interest rate a development bank charges is ultimately transmitted to the broader economy. Hence, charging of high interest rates by national or regional development banks appears quite inconsistent and ironical (Serre, 2005; Lazzarini, 2011; Gutierrez et al., 2012). Clearly, every country will be worried when its national development bank is reporting sterling financial performance in terms of profitability in the face of deteriorating developmental outcomes and declining levels of industrialization.

A further key factor is lending to private enterprises owned by politically exposed persons (PEPs) that have close ties with officials of the same government that is funding the development bank. Sometimes, this particular factor also reappears by way of lending to public enterprises whose top management has close ties with the officials of the same government funding the development banks. Clearly, such lending are usually underlined by corruption and looting of public treasury, since more often than not, the beneficiaries of such loans perceive the funds as their own share of the "national cake." Any development bank that is used as a conduit for distributing political patronage will definitely fail, sooner or later. The reason is quite simple. No bank is too big to fail in the face of corruption and inefficiency (Serre, 2005; Lazzarini, 2011; Gutierrez et al., 2012). Lending to PEPs also suggests that projects that will do the most good to the overall economy and which can also be best monitored and controlled would be neglected in favour of political expediency.

Another important issue is lending mainly for working capital purposes. This clearly puts a national development bank in competition with regular commercial banks whose key objective is to maximize profit and will in the long-run harm the commercial banks and hamper overall economic development. This also means that the development bank may have effectively abandoned its primary goal of driving industrial and overall economic development. For a development bank to succeed along its mandate, it must focus more on such areas as syndicated loans for large developmental projects while not neglecting start-ups and SMEs that generally require unsecured loans (Serre, 2005; Lazzarini, 2011; Gutierrez et al., 2012).

Poor project conception, implementation and supervision is also a key factor in the failure of most national development banks in their quest to drive industrial, social and overall economic development. The argument here is that a development bank is expected to undertake indepth planning in order to identify likely areas to go into. For instance, if it establishes that infrastructure and exports are areas to be promoted, then it should conduct marketing study or research and seek entrepreneurs to implement related investment projects. Where investment projects financed by a development bank consistently fail to go through the cycle of project planning, identification, promotion, and supervision, then it is likely that such a development bank would sooner or later fail to deliver on its mandate of engendering economic development (ADFIAP, 2009).

5. DEVELOPMENT BANK OF NIGERIA: RECOMMENDATIONS AS TO STRUCTURE AND OPERATIONS

In this section, we argue that the DBN, whose wholesale DFI license with national authorization was recently approved by the Central Bank of Nigeria, should operate under certain structures and procedures so that Nigeria will realize her goal of industrialization, social and overall economic development. Even though the Bank was created as a specialized institution to address the challenges of high interest rates, collateral requirements, and short tenure of loans facing informal sector operators, which function mainly as MSMEs, it is our argument in this paper that this structure or mandate will not go far in advancing Nigeria's desire for industrialization (Okonjo-Iweala, 2015). Our submission includes the fact that the US$1.3 billion sourced for the Bank from Nigeria's development partners, including the World Bank, German Development Bank, ADB and French Development Agency is a far cry from the vast amount of funds the Bank is expected to mobilize to fund "big bang" investment projects that can put Nigeria on the path of industrial development (Okonjo-Iweala, 2015; Federal Ministry of Finance, Abuja, 2017). In what follows, we describe our proposed structure and operational guidelines for the Bank. It must be stressed that the DBN may not be able to support the nation's quest for industrialization by ensuring that projects of national priority in the areas of infrastructure, basic industries, energy, transportation, and the likes are adequately funded if the ensuing recommendations are ignored.

The DBN should be able to gather large amounts of funding from a variety of cheap sources. For instance, bonds issued by the DBN should be accorded the same status or treated like other federal government bonds, that is, as risk free assets. This will enable such bonds to attract the desired patronage. The DBN should be able to access the vast amount of pension funds in the country in order to finance national priority projects. Furthermore, the DBN should be able to take the lead in syndicating large investment loans which deposit money banks would not be willing to undertake in their normal course of business. In addition, the DBN should be able to mobilize vast amount of long-term funds from multilateral financial institutions across the globe at concessionary rates. These operational recommendations will ensure that the DBN is able to handle large industrial and economic developmental projects like rail and other transportation projects, pipeline projects, power generation projects, water projects, etc. Such "big bang" projects will in turn enhance the productive capacity of the country towards the attainment of its industrialization and overall economic development goals.

Presently, knowledge about promising sectors or areas for investment in Nigeria appears disjointed and blurred. The structure of the DBN should include a research department that will undertake an indepth study of the Nigerian economy on an ongoing basis with a view to determining the viable sectors for investment. Such sectors must be able to support Nigeria's drive for industrialization and overall economic development. It will then be the duty of the DBN to promote or market these sectors to the global investment community. Our recommendation here is that the DBN should provide a marketplace where investors can buy developmental securities online. This will make it possible for investors anywhere in the world, institutional or otherwise, to purchase the Bank's securities online, which is consistent with the submissions of Michael et al. (2014). This also means that the DBN should be able to bring local and foreign investors together as partners, finance distribution channels, act as a bridge between Nigeria and capital markets abroad, engage in bilateral or multilateral diplomacy in order to access other financial markets abroad, and co-invest in large projects, especially projects like rail transport that is clearly an engine for industrial development. This will enable Nigeria to strategically enter the global production and trade chains.

The structure and operations of the DBN should be such that will sufficiently insulate it from political interference. Indeed, political independence is quite necessary so that the DBN will have the free hand to deliver on its mandate of development financing, especially for the MSMEs in the informal sector. One way of achieving this is to ensure that there is a clear process for appointing and removing the officials of the Bank which cannot be manipulated or controlled by any individual politician. Our recent experience with the Central Bank of Nigeria's leadership points in the direction of this recommendation. If the DBN is allowed to operate under the condition that any arm of government can hire and fire its management at will, then it will be difficult for it to objectively decide on which projects to finance without political interference. Such independence as we have advocated here will in the long-run enhance investors' confidence not only in the DBN as an institution but also in our overall financial system. This is because investors are generally known to be worried or edgy when politicians begin to interfere with investment decisions. Our recommendation here must be seriously viewed because most Nigerian political parties have key politicians at the helms of affairs. Hence, there is high chance of capricious and whimsical state interference in the affairs of the Bank. Similarly, the Bank should not be allowed to interfere in the local politics around the country[1].

The operations of the DBN should be fortified with strong corporate governance standards, adequate risk management policies and procedures and high level of disclosure-based oversight. It could be argued that such procedures may erode the profitability of the Bank. However, studies such as Fang (2005) and the references therein show that high reputation investment banks can pass on the costs of protecting their reputation from excessive risk-taking and control over risks. Besides, our recommendation here will ensure that the Bank operates with high standards of transparency and does not worsen Nigeria's financial fragility nor create systemic instability or distress problems in the financial system.

The DBN should neither get into competition with the deposit money banks in the country nor lend at cut-throat interest rates. It should never seek to declare jumbo profits like the deposit money banks. The Bank should stick to its core mandate of development financing and enhancing the fortunes of micro, small, and medium enterprises (MSMEs), and therefore seek to raise funds from a wide variety of sources as earlier canvassed. The argument that our recommendations above will encroach into the domains of other existing DFIs like the Bank of Industry and the bank of agriculture cannot stand. The critical question should be: Why has Nigeria remained largely far away from being industrialized despite the existence of these other development banks all these years? Whatever answers that are provided for this question will generally show that there is a huge role as canvassed in this paper for the DBN if Nigeria must progress in its journey to industrialization. Thus, DBN's lending activities should always be guided by its ultimate goals of not only enhancing the fortunes of the MSMEs but also driving industrialization and overall economic development underpinned by employment generation, wealth creation, poverty reduction and diversification of industry.

1 Our recommendations here make no claim to the effect that Nigerian government officials interfere with investment decisions of financial institutions in the country. Indeed, our recommendations are strictly based on the understanding that key political interest may want to interfere with the operations of the Bank if adequate safeguards are not put in place.

6. CONCLUSION

In a bid to address the challenge of access to finance for industrial development in Nigeria, this paper describes what the structure and operations of the DBN should be so that the Bank will not only deliver on the core mandate of empowering MSMEs but also support the nation's quest for industrialization by adequately funding national priority projects in the areas of infrastructure, basic industries, energy, transportation, and the likes. To do this, the paper discussed the concept of development banking and why it is an important factor for industrialization. The paper also discussed how development banks differ from commercial banks, and why most national development banks more often than not fail to achieve the ultimate objectives of industrialization and overall economic development. Following these discussions, the paper argued that limiting the mandate of the DBN only to facilitating credits for MSMEs in the informal sector will not go far in advancing Nigeria's desire for industrialization.

In line with this argument, the paper made some important recommendations on what the structure and operations of the Bank should be. Among others, these recommendations include: Gathering large amounts of funding from a variety of cheap sources so that the bank will not only support MSMEs but also handle large industrial and economic developmental projects like rail and other transportation projects, pipeline projects, power generation projects, water projects, etc.; undertaking indepth study of the Nigerian economy on an ongoing basis with a view to determining the viable sectors for investment and marketing them to the global investment community; insulating the Bank from political interference; and maintaining strong corporate governance standards, adequate risk management policies and procedures and high level of disclosure-based oversight.

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