
| RESEARCH ARTICLE

Does Incentive Improve Export Performance of Firms? An Evidence

Mrs Bernadette C. Onah (PhD)¹, Joseph I. Amuka² ✉ Fredrick O. Asogwa³, Mrs Fidelia N. Onuigbo⁴ and Chukwudi Fidelis Ezeudeka⁵

¹National Directorate of Employment, Okpara Avenue Enugu Nigeria

^{2,3}Department of Economics, University of Nigeria Nsukka

⁴Department of Economics, Enugu State University of Science and Technology, Enugu-Nigeria

⁵Federal Inland Revenue Services, Headquarter, Abuja Nigeria

Corresponding Author: Joseph I. Amuka, **E-mail:** doamuka@gmail.com

| ABSTRACT

Trade is an engine of growth, and favourable international trade is essential to attain internal and external stability. In recent times, many developing countries, including Nigeria, have chosen the path of export incentives as the means of achieving a favourable international trade balance. The paradigm shift is a pointer that globalization has made international trade very competitive and firms in less developed countries are at the receiving end. The present study examined the effect of export incentives on the export performance of Nigerian firms. Data were collected through a survey of 60 firms that benefited from export expansion grants (EEG). The Fixed Effect method was adopted in the study. The result shows that the export performance of the firms improved significantly with the export expansion grant. It then suggests that if the country implements all its incentive programmes, the country's external trade will improve significantly.

| KEYWORDS

Export, Incentives, Firms, Performance

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1. Introduction

International trade is very important to every nation because no country produces all its citizens need. Trade and exchange serve as a means of overcoming the problems of scarcity and surplus in the domestic production of goods and services. Through trade, a country can have access to what it does not produce, and through the same trade, it can dispose of what it produces in excess of needs. Good trade policy determines how well a country's external trade performs. Since the debate between the Mercantilists and Adam Smith, many trade theories have emerged and gone down, showing that every trade policy has its own ups and downs. Smith advocated for free trade because it makes it possible for countries to enjoy different variety of goods, but the problem is the fear of domination. Protected trade encourages the growth of the domestic enterprise, but it breeds incompetence and limits consumer preferences (Jayanthakumaran, 2000). Today, no economy is totally open, and none is entirely protected. Now, countries use incentives to encourage their domestic firms to increase export or use tariffs to regulate imports, all in an effort to maintain internal and external stability.

The export incentive is an export-promotion policy approach aimed at stimulating a country's export through different government assistance to producers of certain export goods. They are monetary and in-kind provisions designed to make domestic producers of exportable goods more competitive in international trade. Anderson et al. (2005) defined export incentive and promotion as government policy directed at increasing the return on export. According to Balassa (1978), the export incentive is any measure taken to reduce the cost of production and increase profit or revenue from export. Countries introduce export incentives for different reasons, but the aim is always to improve a country's external trade in order to achieve a favourable external balance. Export incentives may signify inefficiency in the private production of export goods, and government undertakes to remove the

inefficiency through some assistance. Export incentives differ from country to country and depend on what a country wants to achieve. Notable among the export incentives always used by countries are export expansion grant, duty drawback, tax waiver, manufacture-in-bond scheme, export rebate and export processing free zone.

The use of export incentives as a trade promotion to manage external sector performance dates back to the first half of the twentieth century (Dana et al., 2009). The United States introduced the first export incentives in 1942 to promote export trade after a prolonged period of unfavourable external trade. The success of the incentives in improving America's external trade performance opened the gate for other countries to follow. Balassa (1978) pointed out that government engage in export promotion because a country wants to increase the flow of foreign exchange into the domestic economy. According to this argument, export incentive leads to export growth and inflow of more foreign exchange, which can help a country to stabilize its currency value. In a study, Fanta and Teshale (2014) confirmed the positive effect of export incentives on export growth. Their study in Ethiopia showed convincing evidence that export incentives can lead to an increase in a country's export value and volume.

Nigeria introduced export incentive packages in 1988 in an effort to improve the export performance of the country's non-oil sector. Before the incentive regime, the country was in a long period of current account deficit and external debt burden. The fall in the international oil price in the early 1980s contributed greatly to the country's economic downturn since she relied on the oil sector for her bulk of foreign earnings. Due to the unexpected oil price shock, it became very difficult for the country to finance its import. Following the World Bank prescription, Nigeria implemented a structural adjustment programme in 1986 and introduced many economic reforms to diversify the country's export and reduce the reliance on oil single commodity as the main foreign revenue earner. Consequently, some export promotion policies came into effect so as to assist manufacturers of exportable commodities in competing fairly well in the international market. Among the incentives introduced at the time include export expansion grant, duty drawback, export adjustment scheme fund and manufactures-in-bond scheme.

Before introducing the export incentives in Nigeria in 1988, a glimpse into Nigeria's export pattern showed that the agricultural sector dominated her export trade before 1972. In 1960, for instance, agriculture contributed 90% of the country's total export value (Adedipe, 2004). The rise in the fortune of oil in the international market in the wake of the 1970s affected the agricultural sector badly because of the government's shift of attention towards the new oil commodity. Thereafter, the country's export pattern changed. As a result, the share of agriculture in Nigeria's export fell to 8% in 1980 (World Bank, 2003). Similarly, the share of oil from merchandise export rose from 10.3% in 1962 to 97.06% in 1981.

In the same vein, manufacturing from merchandise export share fell from 5.6% in 1962 to 0.13% in 1981. After the introduction of the export incentives, the oil sector maintained its dominance in Nigeria's export trade while agriculture and manufacturing trailed behind. For example, the share of oil from the merchandise export of Nigeria in 2014 was 90.85%, while the share of agriculture and manufacturing were 6.45% and 2.3% (World Bank, 2017). Going by these statistics, it is doubtful if the export incentives are getting the desired result of diversifying the country's export away from oil. The main objective of this study is to examine the effect of export incentives on the export performance of Nigerian firms.

2. Theory and Related literature

Trade theories are the most dynamic among the theories in social science because of the importance of trade in the life of every nation. From Adam Smith and the mercantilist till today, there has never been common agreement among scholars on the best trade practice to adopt. The classical trade theory never favoured protection because of the belief that market mechanism will always direct production and consumption so that countries can buy and sell as dictated by absolute advantage, comparative advantage or factor proportions (Smith, 1776; Ricardo, 1817; Heckscher-Ohlin, 1933). Adam Smith vehemently made a case for free and unprotected international trade against the Mercantilist doctrine of trade protection. In Smith's absolute advantage, he believed that a country must have a natural or acquired endowment, giving her an advantage in the production of one export commodity.

There was a flaw discovered in the absolute advantage theory because it became obvious that a country can have an absolute advantage over its trading partner in the production of the two goods which they trade on. The big question put forward to Smith was whether trade could still go on under such a situation. In order to overcome the flaws in absolute advantage, Ricardo developed the comparative advantage theory in 1817. The important highlight in the comparative advantage is that even if a country has an absolute advantage over its trading partner in the production of the two export commodities, trade can still go on based on the relative productivity differences. Simplifying this, if in an hour country 'A' can produce 30 tons of rice and 35 tons of beans against the country 'B's 28 tons of rice and 25 tons of beans, it is better for the country 'A' to specialize in the production of beans and allow 'B' to produce rice once the exchange is based on one to one commodity.

According to Ricardo, notwithstanding that 'A' has an absolute advantage in the production of the two commodities over 'B', by using all her two hours to produce beans, 'A's total output of beans will rise to 70 tons. Country 'B' will also be better if she uses her total of two hours to specialize in rice production because her total output of rice will rise to 56 tons. Reordering production

in the two countries, each country will be better off because of the improvement in household welfare once commodity exchange is on one to one basis. Though, the theory has its shortcomings, like the absolute advantage because of the unrealistic assumptions of two countries and two commodity worlds. The theory was able to explain how countries can benefit from free international trade better than the absolute advantage.

Absolute and comparative advantage guided international trade practice in the Seventeenth and eighteenth century until the 1900s when Heckscher and Ohlin came up with the Factor Proportion theory. Factor proportion is a complete departure from the former trade theories of Smith and Ricardo because of its focus on the abundance factor as the determinant of specialization in trade. While Smith and Ricardo recognized labour as the main factor input, Heckscher (1919) and Ohlin (1933) recognized land, labour and capital as very important factors in the production of the traded commodity. In their view, an abundance of the factor used intensively in the production of a commodity makes the cost of that commodity low. This factor abundance will determine the commodity a country will specialize in and export to another. For example, if labour is used intensively to produce rice, and capital is used intensively to produce a car, trade between America and India should depend on the availability of labour and capital in each country. Assuming India has more supply of labour and America has more abundance capital, India should specialize in rice production and allow America to specialize in car production because of the abundance of capital in America, which is used intensively in car production.

Factor proportion paradox failed the reality of life because scholars like Leontief (1953) found that America is highly endowed with capital, and yet her imports are made up of capital-intensive goods while her export is more of labour-intensive goods. This raised a serious blow to the Heckscher-Ohlin theory and led to the emergence of more stable and realistic theories like Product Life cycle (Vernon, 1966) and Global Strategic Rivalry (Krugman, 1980; Lancaster, 1980). Vernon's Product life-cycle identified three stages in the life of a product, viz- (a) the product emerges in the country where the research was done, (b) it matures and can be produced and sold anywhere in the world, and (c) the product is produced in other countries, and the country of origin starts importing the same commodity due to cost advantage of producing it elsewhere. The product life cycle is an important trade theory because it recognizes that innovations have a role in determining the commodity a country can export.

Time and event greatly influence theories, and trade theory is no exception. As regards trade practice today, the world is making a U-turn to the trade policy that existed during the mercantilist era. If the mercantilists are to face Adam Smith today, the war between them will go beyond theorizing to the physical challenge. Smith and his classical brothers saw the devil in mercantilist thinking because of their advocate for protected trade. Today, there is a turnaround, and countries are going back to the same protectionist argument of the mercantilists. Whether one is talking of import substitution, export promotion or trade partnership, they all point to trade protection because they are meant to give domestic firms undue advantage over their foreign competitors. If this is so, it means Yilmaz (2015) is not entirely correct by saying that the old theories are deficient in explaining international trade today. The wave of international trade protection put in place today by countries is an indication that the old theories are still relevant in today's international trade.

Since 1942 when the United States implemented the first export incentive strategy, many countries have used different export promotion strategies to foster foreign trade participation. Pakistan implemented the export bonus scheme in 1959 (Abbasi et al., 2019). The scheme allowed for discriminating foreign exchange systems. Ethiopia introduced various export incentive schemes to foster export growth and overcame economic recession in 2002 (Fanta and Teshale 2014). Other countries that introduced incentives to promote export recently are Brazil, India and China. Reimer et al. (2017) justified export incentives because they can create employment opportunities in the domestic economy because there will always be an increase in the demand for input needed to produce the export commodity. This argument is in line with the assertion made by Ahmad (2015). He maintained that export incentive is offered by the government because it has a growth stimulating effect since the production of export commodities always increases the demand for input in the domestic economy.

There are mixed results from the studies investigating the effect of export incentives on export growth in many countries (Chandra and Long, 2013; Fanta et al., 2014; Holden and Gouws, 1997). A study by Chandra and Long showed that export incentives positively affected firms' export performance in China. A similar result was obtained in Ethiopia, where the result from the study by Fanta et al. showed that export incentives increased the value of Ethiopian export. In South Africa, research by Holden and Gouws revealed that incentives significantly affected export growth in 3 out of 13 sub-sectors where export incentives were implemented. Similarly, a study by Ahmed (2006) showed that 13 incentives implemented in Malaysian significantly impacted on export performance of firms while 7 did not.

The establishment of the export promotion council in Nigeria in 1988 after the structural adjustment programme in 1986 was the second round of export promotion in Nigeria. Among the incentives introduced in 1988 to stimulate export growth is duty drawback, export expansion grant (EEG), export processing free zone (EPZ), export price adjustment, currency retention scheme,

handling charge adjustment, export development fund and manufactures in-bond scheme (MIBS). Furthermore, Nigeria export-import bank was established to help potential exporters access financial resources at a low-interest rate. Moreover, the export development fund was a remarkable incentive because of its provisions. It intended to help intending exporters in market research, advertising and publicity in foreign markets, product designs and consultancy, organization of seminars and participation in the overseas trade fair, as well as backing-up the development of export-oriented industries.

The outlook of Nigeria’s export incentives is highly promising for a country seeking to establish its presence in international trade. Unfortunately, many of the incentives were mere paper incentives as they were not implemented. Only an export expansion grant (EEG) was implemented. Poor implementation of the incentives attracted comments from some trade experts. Oyeola (2012) maintained that poor implementation is a setback to the country’s export growth. In the same vein, Walkenhors (2007) pointed out that the poor performance of Nigeria’s agricultural export beginning from the late 1980s was the result of the removal of some of the incentives farmers enjoyed. However, Ezeudu (2014) asserts that export incentives have positively impacted Nigeria’s export, especially traditional agricultural export. He maintained that the establishment of the export processing zone had stimulated the export growth of Ginger, Cashew, Groundnut and Cassava.

Ojike et al. (2011) examined the effect of the export incentives on the growth of Nigeria’s trade on manufacturers. They used manufactured export data between 1971 and 2004 and applied the chow method to test for structural stability between pre and post incentive periods. Their finding was that Nigeria’s manufactured export performed better before the introduction of the incentives. However, the study has a methodological problem and cannot be relied on to conclude that export incentive has not effectively stimulated export growth in Nigeria. This is because the study did not include any incentive strategy in the model. Since no cross-sectional study of firms that benefitted from export expansion grants was done in Nigeria, we used firm-level data of the manufacturing firms that benefitted from export incentives to examine whether the incentive policy has had a stimulating effect on a firm’s export performance.

3. Methodology

The study adopted the fixed-effect method because of its ability to take care of time-invariant characteristics associated with an individual so that an individual error is allowed to correlate with him alone. Moreover, it ignores the between-subject variation and focuses on the within-subject variation. By so doing, it eliminates the likely contamination that could result from unmeasured characteristics of variables which can give rise to biased estimates. The intention of the authors was to cover up to 100 firms. However, when the questionnaires were administered, many of the firms in the records of Nigeria Export Promotion Council did not benefit from the export expansion grant (EEG). We administered 89 questionnaires and were able to receive 78 back. Out of the 78 firms, 18 firms could not provide clear information as required in the questionnaire. Data from the remaining 60 firms were used for the analysis for three years; they benefitted from the export expansion grant between 2005 and 2007.

3.1 The Model

Functionally:

$$Exv=f(Apv, Eeg, Exp, Emp, Age^2) \dots\dots\dots 1$$

Where

Exv= export value that measures performance, Eeg= export expansion grant, Exp= number of years/experience of the firm, Emp= the number of employees of the firm which measures the size of the firm, Age²= the long run effect of operation.

From (1), the mathematical equation is derived,

$$Exv = \alpha_0 + \alpha_1 Apv + \alpha_2 Eeg + \alpha_3 Exp + \alpha_4 Emp + \alpha_5 Age^2 \dots\dots\dots 2$$

α_0 = the intercept term, $\alpha_1, \alpha_2, \dots, \alpha_5$, = the parameter estimates; other variables remained as defined above.

Econometrically, (2) is transformed:-

$$Exv = \alpha_0 + \alpha_1 Apv + \alpha_2 Eeg + \alpha_3 Exp + \alpha_4 Emp + \alpha_5 Age^2 + \mu \dots\dots\dots 3$$

μ is the stochastic error term, and other variables remain as defined before.

Equation (3) is not appropriate to evaluate the effect of export incentives on the export performance of Nigerian firms because it is not the best linear unbiased estimator. We specify the panel fixed-effect model for this purpose-

$$Y_{it} = \alpha_i + \beta' X_{it} + \varepsilon_{it} \dots\dots\dots(4)$$

Where i= 1.....N (where N= 60); t=1.....n (n=3)

Y_t is the export value of the individual firms, which measures the export performance. This is the dependent variable (Exv), X is the vector of k explanatory variables (Annual product value, Export expansion grant, experience of the firm, number of employees,

long run effect of operation), $\alpha_i = 1 \dots N$ are constant coefficients specific to each firm considered, otherwise known as the fixed effect.

4. Result

Table 1: Summary Statistics

Variable		Mean	Std Dev	Min	Max	Observations
Exp	Overall	18.84444	7.595075	5	88	
	Between		5.639445	6	33.66667	
	Within		5.097924	-8.822222	73.17778	T-bar= 2.95082
Emp	Overall	55.76111	59.8308	4	300	
	Between		61.04381	6	300	
	Within					T-bar= 2.95082
Log_Apv	Overall	17.0539	1.753865	9.472705	23.8187	
	Between		1.622184	13.44775	23.74429	
	Within		0.6632601	12.42771	19.47857	T-bar= 2.95082
Exv	Overall	16.89014	1.760917	12.10071	23.8187	
	Between		1.687161	12.62358	23.74429	
	Within		0.5001948	15.2465	18.82094	T-bar= 2.95082
log_Eeg	Overall	14.70949	1.644474	11.40757	21.51612	
	Between		1.55376	12.16165	21.4417	
	Within		0.5405172	13.06578	16.64022	T-bar= 2.94737
Age ²	Overall	412.4778	585.8876	25	7744	
	Between		346.9129	36.6667	2609.667	
	Within		471.6656	-2161.189	5546.811	T-bar= 2.95082

Source: analysis of data from firms

From summary statistics presented in table 5.1 above, the difference between the overall mean of each variable and the standard deviation is greater than the T-bar. Similarly, the difference between the maximum and minimum value of each variable is greater than their T-bar, suggesting that they are all significant in the panel.

Table 2: Export incentives and export performance (dependent variable-export value)

Variable	(1) Pooled ols	(2) ols1	(3) ols2	(4) Fixed effect	
log_Apv	0.219*** (0.000)	0.373*** (0.000)	0.367*** (0.000)	0.145*** (0.000)	Significant
log_Eeg	0.717*** (0.000)	0.602*** (0.000)	0.606*** (0.000)	0.726*** (0.000)	Significant
Exp	-0.0165 (0.204)	-0.0190 (0.046)	-0.0243 (0.018)	0.0263 (0.345)	
Age ²	0.000166 (0.256)	0.000173 (0.150)	0.000226 (0.073)	-0.000277 (0.356)	
Emp			0.000777		
Const.	2.961*** (0.000)	2.058*** (0.000)	2.139*** (0.000)	3.458*** (0.000)	Significant
observations	168	168	168	168	
R ²		0.94	0.94	0.83	

NB= figures in parentheses are probabilities

***= significant at 1%

Source: analysis of data using Stata

4.1 Discussion of Findings

Table 2 above is the effect of export incentives on export performance of manufacturing firms that benefitted from export expansion grants between 2005 and 2007 in Nigeria. The result of the pooled ordinary least square (ols) result is presented in column 2, and the fixed effect result is presented in column 5. Comparing the result of the ols and fixed effect results, one will observe that the ols are biased either upward or downward. For example, in table 2, ols is biased upward against the annual product value (Apv) and downward against the export expansion grant (Eeg). The value of the R² of the fixed effect is 0.83, showing that the variables in the model explained 83 percent of the changes in export performance of the firms within the period of the study, suggesting high explanatory power of the model.

The estimated result presented in table 2 above showed the effect of the incentives received by manufacturing firms on their export performance. Interpretation and discussion will be on fixed effect in column 5. Starting with the non-incentive factors, annual product value (Apv) and experience in the short-run (Exp) positively affect the export performance of the manufacturing firms. However, in the long run, the effect of experience (Age²) on the export performance of the firms is negative. A unit increase in the firms' annual product (Apv) will lead to a 0.145unit increase in the export of the firms. The variable is statistically significant at 1% level of significance. The effect of experience on performance, in the long run, is, however, surprising. One expected that the more the number of years the firms operate in business, the more they specialize or become familiar with the business environment. It is expected that from the learning by doing theory, firms come to know the best time to produce and supply to the market; learn how to overcome certain risks and the cost minimization strategy in the business. Unfortunately, it did not work in that way here. It may suggest that in the long run in international business, the effect of experience gives way and other factors become more important.

Export expansion grant (Eeg) is an important incentive that many firms have benefited from in Nigeria to help them penetrate the foreign market. It is the only incentive out of the many that firms have less difficulty in accessing in Nigeria. The finding reveals that the export expansion grant positively affects the export of Nigerian manufacturing firms. The effect of the Export expansion grant on export performance is significant at a 1% level of significance. It suggests that the incentive policy in Nigeria is achieving the objective it was set up for. The result is consistent with a previous study in BIC countries by Ledyeva (2018), in Denmark by

Munch and Schaur (2018), and in Pakistan by Abassi et al. (2015). All the studies found that export incentives stimulate export. All the same, the result is inconsistent with an earlier study in Nigeria by Ojike et al. (2011). The difference between the present study and the work of Ojike et al. goes to show that in a study to find out the effect of export incentives on export performance, it is better to use the data of the benefitting firms in the analysis.

5. Conclusion

In the last four decades, developing countries and Nigeria inclusive have used incentives to penetrate the international market and gain a favourable external trade balance position. The practice is not out of place in the first instance because a country's balance of trade position affects its internal stability. Unfavourable trade balance creates foreign exchange scarcity and limits the ability of the firms to import important inputs needed for further production. To this end, the prolonged unfavourable external imbalance is catastrophic because it can lead to domestic economic crises since growth cannot occur without domestic investments. This is why trade incentives are supported.

However, giving incentives is one and having good results from it is another. A good result is possible when export incentives are well implemented. Of more than 10 export incentives outlined to help Nigerian exporters, only an export expansion grant was accessed by many firms. Conditions for the access of others were stiff and have given room for manoeuvring. Evidence in the present study has revealed that export incentive has been of benefit to Nigerian exporters. It is expected that if other incentives are given the expected government attention, Nigeria will diversify her export base away from oil. Developing countries cannot do without trade because trade is the engine of growth. What is expected of developing countries is to put the right trade policy in place, and the trade potentials they have will materialize. **This study focused on export expansion grants as there was no data on other incentives like duty drawback, export development fund, and currency retention scheme because they were not implemented.** It is important that future research should examine the problems associated with the implementation of the remaining export incentives in Nigeria as the delay in their implementation is slowing down the growth of Nigeria's export sector.

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