Why Nigeria's rising debt and falling revenues are a challenge for growth

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Background

In 2021, the World Bank rated Nigeria fifth on its list of ten nations with the biggest debt exposure. This was coming at a time when Nigeria was using 97% of its revenues to service outstanding debt, a cause for concern for the multilateral organization. Nigeria owes the International Development Association (IDA), one of the World Bank's two lending arms, US$11.7 billion. IDA gives loans to nations at low to zero interest rates based on a country's creditworthiness or per capita income. These loans are the World Bank's contribution to helping low and lower-middle-income countries maintain some level of stability and growth at almost zero interest rates. Nigeria is eligible for these concessional loans from IDA based on its per capita income. If the World Bank is raising some concerns about Nigeria's debt exposure, why then has Nigeria not been cautious about its borrowing? Why has the Nigerian government recently continued to borrow despite spending all its revenue on debt servicing? Why has the finance minister, Dr. Zainab Shamsuna Ahmed, responded that the country does not have a debt problem but a revenue problem? These and other questions will be addressed in detail in this article.

What you should know

i. **Nigeria has a debt and revenue problem.**
ii. **The twin issues of poor macroeconomic fundamentals and the ensuing fiscal deficit are currently befuddling the Nigerian economy.**
iii. **The need to diversify the economy, reduce the cost of governance and improve revenue generation are panaceas towards economic development.**

Nigeria's debt profile

Nigeria's debt stock rose to ₦42.84 trillion in June 2022. From these figures, external debt stock approximates $40.06 billion (₦16.62 trillion). Debt to multilateral agencies like the World Bank, IMF, African Development Bank, Afreximbank, and bilateral lenders like China, Japan, China, France, and India accounted for around 58 percent of the external debt stock, followed by commercial debts (33 percent), while promissory notes and other forms of debts constitute the remaining 9 percent. Domestic debt on the other hand approximates ₦26.23 trillion. Nigeria's overall debt statistics show that approximately 38.78 percent of borrowings are from external sources while the remaining 61.22 percent are from internal sources. In addition, Nigeria's debt figures, as presented by the Debt Management Office (DMO), do not include what was borrowed from the Central Bank of Nigeria (CBN). If the ₦4.61 trillion that was borrowed between January and August 2022 is included in our estimation, then the ₦22.07 trillion Ways and Means borrowing would bring the total debt to ₦64.91 trillion.

Source: The Budget Office, 2022; CBN Statistical Bulletin, 2022

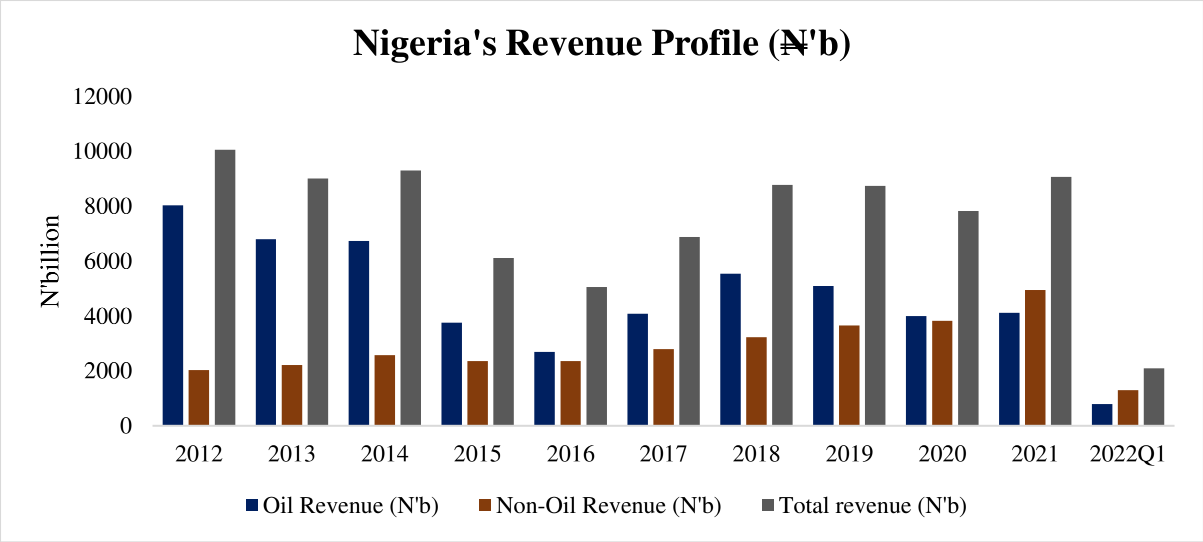
Can Nigeria sustain its debt?

Economists generally assess a country's debt sustainability using two metrics. The first is the proportion of debt as a ratio to a country's gross domestic product (GDP). This is usually known as the debt-to-GDP ratio. Economists argue that when the entire debt-to-GDP ratio hits 60 percent, it begins to harm economic growth. In 2021, Nigeria's debt-to-GDP ratio was around 37 percent. Presently, we can argue that Nigeria's debt is not unreasonable based on this criterion. The second important criterion used to measure the quality of a country's debt is the proportion of debt service to the export of goods, services, and primary income. That is the proportion of export proceeds used to service debt, including principal and interest payments. A healthy ratio is less than 15 percent. As of 2020, Nigeria had a debt service to exports ratio of 13.36 percent. Figures for 2021 are however yet to be established.

Based on these two indices, Nigeria has maintained a healthy debt profile. However, the concerns surrounding Nigeria's debts have always been over Nigeria's ability to service its existing debts in the future. This is because if you take Nigeria's debt services and place them as a proportion of what the country is generating as revenue, then Nigeria's debt service becomes enormous. Nigeria's debt service to revenue ratio is 118% as of the first quarter of 2022. Meaning that for every ₦1 the country earns, it uses ₦1.18k to service existing debts.

Nigeria's revenue profile

Nigeria is commonly referred to as an 'oil economy' due to its vast oil reserves. Even though the country has largely depended on oil as its main source of revenue over the years, the petroleum sector has contributed about 10 percent of the country's gross domestic product (GDP) over the past 5 years and approximately 7.5 percent in 2021 according to figures from the Central Bank of Nigeria's (CBN) statistical bulletin. In comparison to other Gulf states, the petroleum industry generates nearly half of Kuwait's GDP. Qatar and Saudi Arabia's oil and gas sector contributes about 40 percent to their respective GDPs, while the United Arab Emirates (UAE) oil and gas sector contributes around 30 percent to their GDP. In Africa, Nigeria is currently the fourth largest producer of oil. Its 937,766 barrels a day based on direct communication in September 2022 is behind Angola (1.18mb/d), Libya (1.12mb/d), and Algeria (1.04mb/d). The decline in oil production volumes has been a result of continuous vandalization of the pipelines, crude oil theft, and low investment flow in Nigeria's oil and gas sector. The continuous frictions within the oil and gas sector and the continuous application of subsidies on the premium motor spirit (PMS) have been the main reasons for shrinking revenues over the last couple of years. Moreover, the non-oil revenues outstripped oil revenues in 2021, dispelling any further evidence regarding the notion that Nigeria is an oil economy.



Source: CBN Statistical Bulletin, 2022

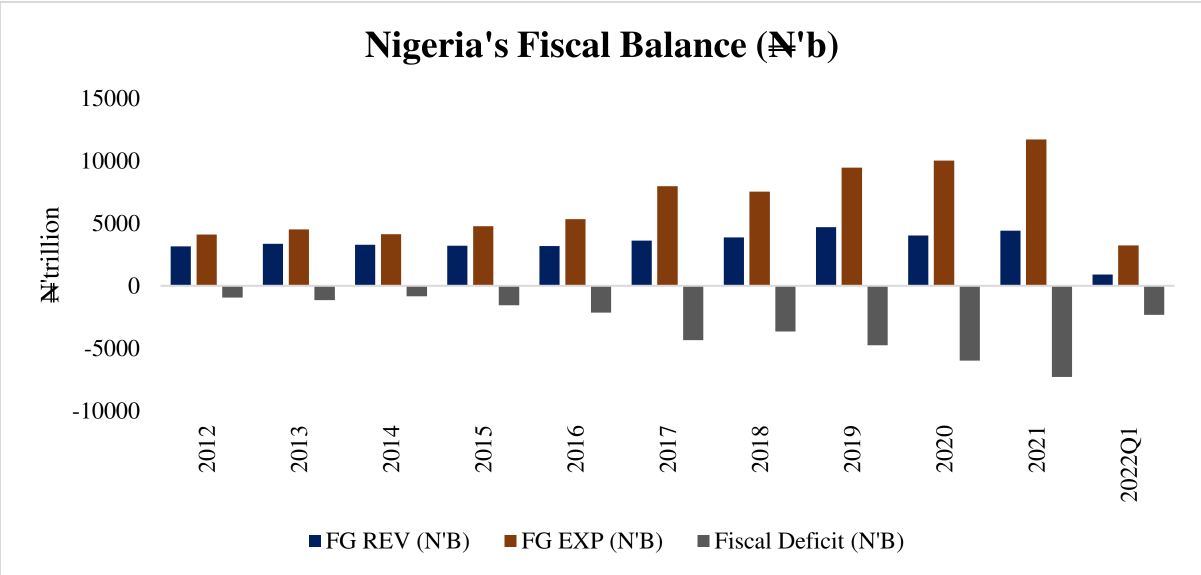
Does Nigeria have a Revenue Problem?

The question that however arises from the current scenario is if Nigeria has a revenue problem. A country has a revenue problem when its actual revenue is less than the projected revenue over a period. In 2021, Nigeria was projected to make a revenue of ₦6,208.19 billion between January and November. However, it underperformed by making ₦4,308.76 billion, a variance of ₦1,899.43 billion (The Budget office, 2022). Between January and April 2022, it was estimated that Nigeria would generate ₦3.33 trillion. Howbeit, revenues generated during the period performed lower than expectations, totalling ₦1.6 trillion as of April end (The Budget Office, 2022). The finance minister noted that the inability to increase crude oil production and NNPC's continuous PMS subsidy deductions have been the main issues in improving revenue.

In addition, debt repayments are made through revenue generation. Nigeria has one of the lowest revenue-to-GDP ratios in Africa, at less than 6 percent. The average for Sub-Saharan African countries is around 20 percent, while oil-exporting countries average 30 percent. Due to our over-reliance on crude oil revenue and borrowing, Nigeria's inability to improve revenue drive may hinder its ability to repay existing loans and future borrowings since debt service payments are already gulping the entire revenue proceeds.

Fiscal Deficits arising from rising expenditures and falling revenues

The revenue and debt problem Nigeria is currently facing may not seem to abate anytime soon. This is because as of 2021, about 72 percent of the nation's budget was focused on non-capital expenditure, while the proposed 2023 budget amounts to 74 percent. Furthermore, the ensuing gap between recurrent expenditure and government revenue (the primary balance) is causing a fiscal problem for the authorities as they have been resorting to borrowing, with borrowings expected to cater for around 55 percent of the proposed 2023 budget.



Source: CBN Statistical Bulletin, 2022

Poor macroeconomic fundamentals may be affecting performance

Asides from Nigeria having a debt and revenue problem, it may be argued that the decline in economic performance over the past 10 years may have contributed heavily to the poor economic fundamentals that are currently befuddling the economy. Nigeria's economic growth plummeted from 5.31 percent in 2011 to -1.62 percent in 2016 due to falling crude oil prices in 2016, then fell to -1.8 percent in 2020 due to the COVID-19 pandemic. During the same period, inflation increased from 10.84 percent in 2011 to 15.68 percent in 2016, and further rose to 16.98 percent in 2021, while the unemployment rate increased from 6 percent in 2011 to 33.3 percent in 2020 (NBS, 2022). Furthermore, between 2011 and 2021, the naira lost 147 percent of its value in the official segment of the market, while it lost about 200 percent of its value in the unofficial (BDC) segment of the market. These challenges have led to a slide in the nation's macroeconomic fundamentals, thereby affecting the nation's ability to witness any meaningful development.

The way forward

In essence, Nigeria has a debt and revenue problem. For people to change their perception of the country, the leaders need to carefully manage the country's debt. The Nigerian government should launch a public education campaign regarding Nigeria's debt to give assurances that they can manage the debt sustainably. More importantly, fiscal policy reforms at all levels of government are needed for the authorities to manage debt effectively. These reforms must be extended toward the debt management office, pension funds, and bond market since the bond market and pension funds have been borrowing avenues for the government. The government may also need to look towards equity financing to foster public-private partnerships and manage the extent of government debt liabilities to the private sector.

Nigeria needs to cut its high cost of governance and control corruption. A sustainable anti-corruption strategy must be put in place to support anti-corruption behaviour. Judicial reforms that promote more anti-corruption agencies must be instituted to influence social norms and attitudes that help anti-corruption thrive in Nigeria with a view of effecting social change. This would create an impetus for citizens to act against corrupt practices. Indeed, resources must be directed toward measures aimed at preventing corruption and increasing citizen engagement in the fight against corruption. To achieve change, dealing with deep-seated corruption will require several methods, repetition, and follow-up actions.

Nigeria must accelerate its revenue drive by investing in the needed infrastructure to improve revenue and sustainable economic growth. Tax revenues need to be expanded since the country is currently undertaxed with tax revenues accounting for around 5.2 percent of GDP. This should be done by expanding the tax bracket and cut tax leakages. Finally, there is a pressing need to diversify the economy and reduce the reliance on oil since the issues around oil theft and vandalism are not expected to end anytime soon. That non-oil revenues constitute the larger chunk of revenues in 2021 does not give any credence that the Nigerian economy has been diversified, it only tells a true picture of the leakages within the oil and gas sector. Recently, an illegal pipeline and a loading port that was part of an organized crude theft operation happening over the last nine years were discovered from the Forcados terminal operated by Shell. Estimates suggest that the pipeline exports 250,000 barrels of oil per day into the sea, while the Group Managing Director of Nigerian National Petroleum Corporation (NNPC), Mr. Mele Kyari, noted that Nigeria is losing potential revenue from some 600,000 barrels of crude oil per day. This implies that Nigeria may be losing potentially up to 40% of its oil export revenue in a day and efforts must be directed at uncovering many other leakages happening in the oil and gas sector.