THE PROPOSED 2016 – 2018 MEDIUM TERM BORROWING PLAN OF THE FEDERAL GOVERNMENT OF NIGERIA: IMPLICATIONS FOR DEBT SUSTAINABILITY

CSJ

CENTRE FOR SOCIAL JUSTICE LIMITED BY GUARANTEE

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ACRONYMS

CBN: Central Bank of Nigeria
DG: Director-General
DMO: Debt Management Office
DSA: Debt Sustainability Analysis
FG: Federal Government
FGN: Federal Government of Nigeria
FMBNP: Federal Ministry of Budget and National Planning
FRA: Fiscal Responsibility Act 2007
GDP: Gross Domestic Product.
MTEF: Medium Term Expenditure Framework
NASS: National Assembly
US$: United States Dollar

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EXECUTIVE SUMMARY

In the 2016-2018 External Borrowing Plan, the President is requesting for legislative approval for borrowing. The total cost of the projects and programmes is $29.960 billion made up of proposed projects and programmes loan of $11.274 billion, special national infrastructure projects $10.686 billion, Eurobonds of $4.5 billion and FGN budget support of $3.5 billion. The presidential request was not accompanied by detailed information explaining the proposal.

This request is coming at a time the Nigerian economy has entered recession and seems to be entering a depression. In succinct terms, this study aought to:

- Discuss the trend of growth of public sector debts in Nigeria since the 2010 fiscal year;
- Discuss the borrowing plan in line with the 2016 Debt Sustainability Analysis prepared by the Debt Management Office of Nigeria;
- Discuss the implication of the borrowing plan in the light of declining oil revenue and economic growth in Nigeria;
- Offer evidence-based policy suggestions that will guide the National Assembly in taking an appropriate stand with respect to their decision on the request by the President.

Public sector debts (domestic and external) have tremendously increased since the year 2010 and debt service costs have also increased. The domestic debt stock increased from N4.552 trillion in 2010 to the end of June 2016 figure of N10.66 trillion. This is a 133 percent increase over the value of debt stock as at 2010. External debt stock increased from $4.532 billion in 2010 to the end of June 2016 figure of $11.262 billion representing 148 percent increase from the 2010 value of the debt stock.

The Fiscal Responsibility Act made clear provisions for debts, debt management and borrowing stipulating that borrowing shall be for only capital projects and human development, concessional in nature, subject to legislative approval and a long period of amortization and in overall, the national debts should be sustainable. The FRA also provides for debt limitation. The study reviewed the debt to GDP ratio analysis and noted that debt to GDP ratio is mostly utilised as a good measure of debt sustainability in countries where taxation is a major source of revenue for the government. In such a case, the ability of the government to pay up its debts depends largely on the incomes of the citizens and corporates, who in turn pay taxes to the government. In the case of Nigeria, the tax to GDP ratio is very low - less than 10 percent. Oil accounts for less than 10 percent of GDP but contributes over 90 percent of foreign currency receipts.

Again, according to the draft MTEF 2017-2019, for the first half of 2016, the country has so far spent N2,419.375billion and has thereby incurred a debt/deficit of N1,467.855billion. Thus, the retained revenue constitutes only 39.33 percent of total expenditure in the first half of the year whilst borrowing funded 61 percent of total half year expenditure. Total capital expenditure in the half year amounted to N159.062billion; the implication of the foregoing is that out of the N1,467.855 billion which Nigeria borrowed, N1,308.793billion was spent on recurrent expenditure[1].

The DSA 2016 was reviewed with its baseline and optimistic scenarios. But the DSA made most of its recommendations based on the optimistic scenario which evidently cannot hold in the face of extant macroeconomic realities. Projected external debt service and oil revenues do not converge in a sustainable manner whilst the proposed figures to be borrowed are far in excess of capital requirements in the MTEF 2017-2019.

The Eurobond component of the request heightens the challenge of sustainability. Extant Nigerian Eurobonds constitute 13.32 of the external debt stock but gulped 38.8 percent of debt repayment in the first quarter of 2016. This clearly shows that the interest rate and charges attached to the Eurobond are very high and beyond the contemplation of the FRA. Going for the Eurobonds at a time of declined commodity prices, depleted foreign reserves and waning investor confidence will ensure that the rates of interest may not be less than 10 percent.

Against the background of the foregoing, the following recommendations are imperative.

(i) Invite the Director-General of the Debt Management Office to proffer policy recommendations on the basis of the baseline scenarios observed in the findings of the Debt Sustainability Analysis exercise of the debt management technical team.

(ii) Ask the President to follow the stipulations of the Fiscal Responsibility Act to wait for the full approval of the submitted Medium Term Expenditures Framework (2017 – 2019), which should serve as the basis for any proposal to borrow.

(iii) Request that the President follows the stipulations of the Fiscal Responsibility Act to revise downwards the proposed amount in the Medium Term Borrowing Plan (2016 – 2018) in order to allow same to correspond to the total capital budget and proposed capital expenditures within these years.

[1] The portion of the debt used for recurrent expenditure amounts to 89.16 percent of the borrowed funds.

(iv) As an alternative, ask the President to withdraw both the proposed MTEF (2017 – 2019) and the proposed Medium Term Borrowing Plan (2016 – 2018) in order to revise both to agree on the capital projects that should demand such a huge loan.

(v) Ask the President for details of the projects and to provide justification for the inclusion of any project as a capital project that should be financed with the proposed loan.

(vi) Ask the President to present the cost benefit analysis of each of the projects to be included in the borrowing plan.

(vii) Ask the President to provide detailed borrowing plan that shows at what point in the three year period a particular amount will be borrowed and from what sources. This will help to show if this request for the approval of medium term borrowing plan is a critically thought out plan.

(viii) Ask the President to provide detailed repayment plan in accordance with the stipulations of the Fiscal Responsibility Act.

(ix) Ask the President to provide evidence of debt sustainability with forecast and justification of the sources of revenue that will be used in servicing the debts at maturity.

(x) NASS should consider rejecting the Eurobond component of the loan.

(xi) Ask the President to put all the foregoing information in the public domain in accordance with the Fiscal Responsibility Act

1. INTRODUCTION

Globally, national and sub-national governments borrow in order to meet their expenditure needs. In this case, public loans may be viewed as either substitute or complement to other sources of revenue like taxes[2]. Therefore, government loans help the government to meet its expenditure requirement without necessarily tampering the taxation rates in order to increase revenues. Nwankwo (2011) holds the opinion that governments look for sources of loans and advances whenever the current receipts of such governments from conventional sources fall short of the governments' spending requirements[3]. It is the loans that are borrowed and accumulated by governments of various countries that become public debts. Public debt can be categorised into external debts and domestic debts. While domestic debts are debts owed to financial institutions or other bodies within the local economy (society) where the government operates, external debts are debts owed to multilateral, bilateral and commercial entities and institutions outside the immediate environment of the debtor-government.

In the 2016-2018 External Borrowing Plan, the President is requesting for legislative approval for borrowing; total cost of the projects and programmes is $29.960billion made up of proposed projects and programs loan of $11.274 billion, special national infrastructure projects $10.696 billion, Eurobonds of $4.5 billion and FGN budget support of $3.5 billion.

1.1 Macroeconomic Environment and the Problem

Nigeria as a country has continued to depend on the export of primary products for foreign exchange earnings. Before the period of commercial oil exploration in Nigeria, the major export commodities of the country remained primary agricultural produce, which were usually exported to the industrial nations as raw materials. The products were being processed and shipped back into Nigeria as finished goods. However, as oil became a major source of revenues since the early 1970s in Nigeria, other sources of revenue generation took a declining path[4].

Revenues from the export of primary products are usually susceptible to volatility. The forces of demand and supply in their international markets make their prices to be very unstable. In the case of Nigeria, oil revenues accounted for 50 – 72 percent of the gross federally-collected revenues between the fourth quarter of 2013 and the fourth quarter of 2015[5]. Such high proportion of oil revenues in the total revenues of the Federal

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[2] Cosio-Pascal, E. (2012) "Public Debt Management". New York: UNESCO-EOLSS Encyclopedia

[3] Nwankwo, A. (2011) "Stages of Nigeria's Public Debt Management". Guest Lecture presented at the University of Nigeria, Nsukka, May 31, 2011.

[4] Oseni, M. (2013) "Internally Generated Revenue (IGR) in Nigeria: A Panacea for State Development". European Journal of Humanities and Social Sciences, 21(1): 1050–66.

[5] Central Bank of Nigeria (2015) *Economic Report for Fourth Quarter 2015*. Abuja: CBN Publications.

Government of Nigeria exposes the government treasury to the oscillations that occur in international oil market prices, which also exposes the government to the risk of inability to implement its budgets. The result of the volatilities is the growing disparity between revenues and optimal expenditures of government.

Fiscal imbalance has always been seen as a norm in many developing countries as long as such state of public finance produces expected macroeconomic goals of the fiscal policy authorities. In recent years, Nigeria's debt profile has continued to rise. The rise in public debt profile has not been seen as much problem over the years due to positive signs of other macroeconomic variables in the country. Nigerian economy grew sporadically even when other economies of the globe were crashing due to the effects of the recent global financial crisis. The country's economy grew to become the largest economy in Africa as at 2014[6]. This period coincides with the period of boom in international market oil prices. At this point, the level of fiscal deficit recorded in Federal Government of Nigeria's annual budget did not raise much dust.

However, the first two quarters of 2016 fiscal year broke Nigeria's economic growth jinx. Within those two quarters, Nigerian economy witnessed two consecutive negative growth rates. The implication is that Nigerian economy entered recession for the first time in over two decades. Interestingly, it is this same 2016 fiscal year that the Federal Government of Nigeria prepared the most optimistic budget in the history of the country.

> *"The 2016 approved budget amounts to a total of ₦6,060,677,358,227. This amount represents about 34.88% increase over the ₦4,493,363,957,158 approved for 2015 budget. The 2016 budget allocates the sum of ₦1,587,598,122,031 for capital expenditures. Capital expenditures therefore represent 26.2% of the entire budget. The amount allocated to capital expenditures in the 2016 budget represents an increase of 185.03% from the ₦556,995,465,449 allocated to capital expenditure in 2015"[7].*

The 2016 budget of the Federal Government of Nigeria projects to borrow the sum of ₦1.84 trillion for deficit financing. Of the said amount projected for deficit financing, about 50 percent is projected to be borrowed from external sources while the remaining 50 percent is projected to be borrowed from domestic sources. On the other hand, the remaining part of the budgeted expenditures is expected to be financed from the federation account. It is important to note that this federation account is mainly funded

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[6] Ogunlesi, T. (2014) "Nigeria overtakes South Africa to become the Largest Economy in Africa". *The Guardian*, Monday 7 April, 2014. Also available at: https://www.theguardian.com/world/2014/apr/07/nigeria-south-africa-largest-economy

[7] Agu, D. O. (2016) "Macroeconomic Framework of the Federal Government of Nigeria (FGN) 2016 Approved Budget". An Advocacy Paper submitted as part of "Engaging the 2016 Approved Federal Budget in Nigeria" to Centre for Social Justice, Abuja. May, 2016.

with proceeds from oil sales. The glut in international market oil prices that started in 2014 became worse in late 2015, which made the Federal Government of Nigeria to peg the oil benchmark at US$38 per barrel in the budget. The expected oil revenue is also predicated upon a daily crude oil production level of 2.2 million barrels, and average Naira exchange rate of ₦197 to US$1[8].

Supposing all the assumptions of the 2016 budget hold, the Federal Government of Nigeria should be able to finance more than two-third of the entire budget without resorting to any loan. However, most of the assumptions did not hold. It is true that there has been a little increase in the international market oil prices since the passage of the 2016 Appropriation Act, yet the level of production has continued to decline due to the activities of the Niger Delta militants. Therefore, the Federal Government of Nigeria has not been able to generate all the needed funds to finance its 2016 budget. Actual revenues (including oil revenues) have continued to be much less than budgeted revenues. The only option remaining for the government to explore is that of borrowing to finance the glaring fiscal deficits.

As a result of the observed variation between budgeted revenues and actual revenues in the 2016 budget of the Federal Government of Nigeria, the President of the Federal Republic of Nigeria sent his request for approval of 2016 – 2018 external borrowing (rolling) plan of the Federal Government of Nigeria to the National Assembly on the 20th of October, 2016. The National Assembly rejected the request on arrival without much consideration of the contents. Furthermore, the National Assembly justified the rejection of the request on the grounds that the President did not attach the breakdown of expenditure line items for which the request for borrowing was initially made to the National Assembly. The request and its attendant rejection aroused great curiosity in the minds of Nigerians. Therefore, there is need to critically analyse the request in the light of Nigeria's current external and domestic debt burden. The outcome is expected to be used in effectively engaging the National Assembly, so as to help the National Assembly make informed decision in their deliberations on the request when the President turns in the request with its accompanying documents.

1.2 Objectives

Drawing from the macroeconomic environment presented above, we can easily infer that the broad objective of this study is to critically analyse the recent request for borrowing by the President of the Federal Republic of Nigeria to the National Assembly. The analysis is expected to look at the request in the light of current external and domestic debt burden on the economy and current capacity of available government

[8] Udoma, U. U. (2016) "Overview of the 2016 Budget and the Strategic Implementation Plan for 2016 Budget of Change". A Presentation by the Honourable Minister of Budget and National Planning, 12th May, 2016.

revenues to continue to service the accumulated debt stock in addition to the burden that will be imposed by the proposed borrowing of 2016 – 2018. In succinct terms, this study tries to:

- Discuss the trend of growth of public sector debts in Nigeria since the 2010 fiscal year;
- Discuss the borrowing plan in line with the 2016 Debt Sustainability Analysis prepared by the Debt Management Office of Nigeria;
- Discuss the implication of the borrowing plan in the light of declining oil revenue and economic growth in Nigeria;
- Offer evidence-based policy suggestion that will guide the National Assembly in taking an appropriate stand with respect to their decision on the request by the President.

1.3 Methodology

This study involves desk review. All the information presented and analysed in this study are gathered from available statistical records. There is no gathering of new information through primary data collection for the sake of this study. Therefore, the study relies solely on available statistical data. Some of such statistical data are gathered from the databases of Debt Management Office (DMO) of Nigeria, Central Bank of Nigeria (CBN), Federal Ministry of Budget and National Planning (FMBNP), etc.

In addition to gathering information from available statistical records of various government agencies, this study equally reviews available documents collated for the sake of this study. Apart from existing literature on what levels of debts are considered sustainable for developing countries like Nigeria, this study equally reviews the recent Debt Sustainability Analyses of the Debt Management Office (DMO) with particular focus on the 2016 Debt Sustainability Analysis. The study equally reviews the fiscal policy implication of the proposed borrowing for overall debt burdens, government revenues, external debt services, foreign exchange earnings and economic growth. Also, the study reviews the request for borrowing and the implication of its approval in the light of provisions of Fiscal Responsibility Act (2007) and other extant laws.

1.4 Limitation

Given that this study is based on desk review, it is mainly limited to the extent to which available statistical records can provide reliable information. It is not every source of information that can be considered reliable. Therefore, this study limits itself to only those sources that it considers reliable. This implies providing for only discussions that can be supported by available information even if a reader may not consider the discussions to be detailed enough.

2. FEDERAL GOVERNMENT OF NIGERIA'S DEBT PROFILE FOR 2010 – 2016 FISCAL YEARS

Nigeria has continued to export primary commodities over the years. This comes with much volatility and unpredictability on the part of foreign exchange earnings and government revenues, with attendant need for borrowing whenever expected level of expenditures is not matched by actual revenues. Even in the years when the prices of those commodities seem to be high, fluctuations in the prices still make them unpredictable as was the case in 2014 (*see DMO, 2014*[9]). It may therefore be observed that the Federal Government of Nigeria continues to borrow even when oil prices soared high as a result of developmental needs of the country. This section considers holistically the debt profiles of the Federal Government of Nigeria over the period of 2010 – 2016.

2.1 Growth Trend in FG's debt profiles (2010 – 2016)

The Federal Government of Nigeria has continued to operate on fiscal deficit throughout the study period. Fiscal deficits necessitate borrowing. From the domestic economy, the Federal Government of Nigeria uses several fiscal instruments to borrow money. Such domestic instruments include FGN Bonds, Nigerian Treasury Bills, and Treasury Bonds. From external sources, the Federal Government of Nigeria borrows from multilateral agencies, bilateral agencies and even foreign commercial financial institutions (using foreign fiscal policy instruments). This section considers the growth trend of Federal Government of Nigeria's public debts over the period of 2010 – 2016.

2.1.1 Domestic Debt Profile of the Federal Government

There was a time when domestic debt was never an issue in Nigerian public financial management. However, as Nwankwo (2011) observed, the second stage in Nigeria's debt management can be seen as when the country exited the Paris Club debt trap through debt relief package in 2005. At this second stage of debt management in the economy, the Debt Management Office, Nigeria started looking inwards on how to raise money from within the domestic economy through several debt instruments. Most of these instruments are usually long dated spanning from 3 years to 20 years[10]. Figure 1 below is a graphical presentation of how the accumulations of domestic debt stocks and services have grown over the years.

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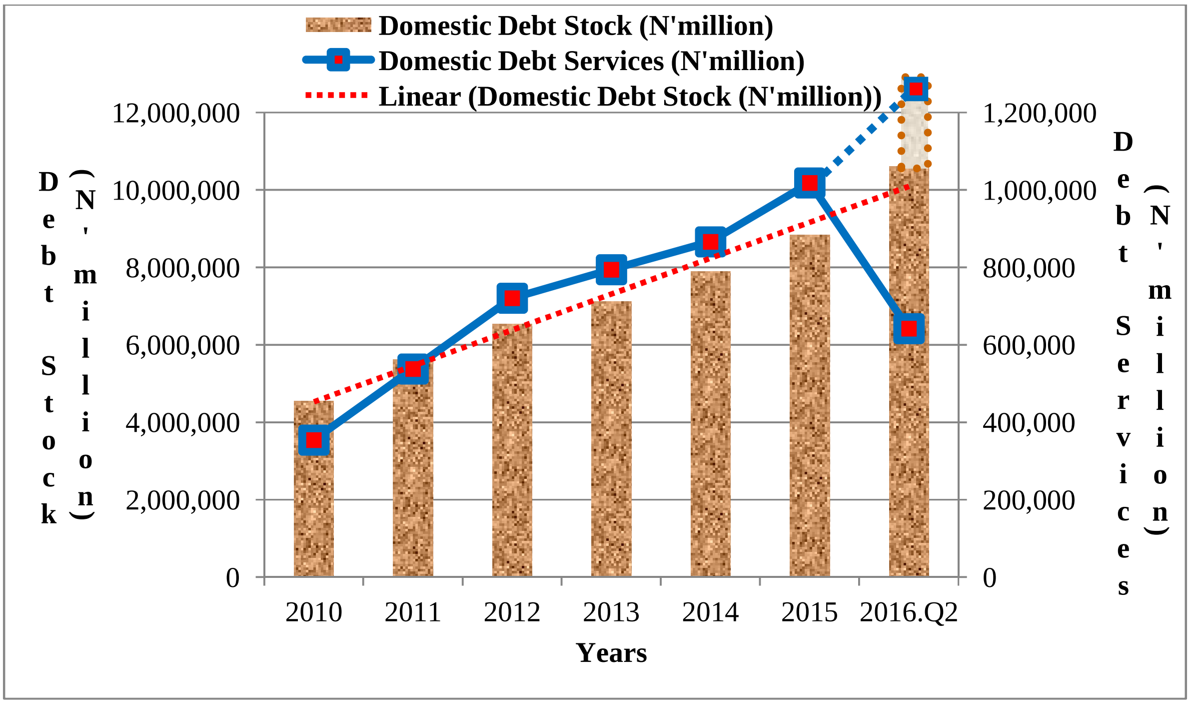
[9] Debt Management Office, Nigeria (2014) *2014 Annual Report and Statement of Accounts (*Director-General's Statement). Abuja: DMO Publications

[10] Nwankwo, A. (2011) "Stages of Nigeria's Public Debt Management". Guest Lecture presented at the University of Nigeria, Nsukka, May 31, 2011.

Figure 1: Growth in FGN Domestic Debt Profile and Domestic Debt Burden on FG Finances



Sources: *DMO's Annual Reports and Statements of Accounts (2010, 2011, 2012, 2013, 2014, 2015); Reports of Domestic Debt Stock and Domestic Debt Service (2016Q1 & Q2)*

From Figure 1 above, as at 2010, the total domestic debt stock of the Federal Government of Nigeria was just about ₦4.552 trillion. With an increase of 23.53 percent of its value in 2010, total domestic debt stock of the Federal Government of Nigeria moved to ₦5.623 trillion in 2011. Another huge increase was recorded in the total domestic debt stock of the Federal Government of Nigeria in 2012. From ₦5.623 trillion in 2011, domestic debt stock of the Federal Government of Nigeria increased by 16.27 percent in 2012 to stand at ₦6.538 trillion. The least level of increase in domestic debt stock of the Federal Government of Nigeria was recorded in 2013 fiscal year when it only increased by 8.89 percent from its value of ₦6.538 trillion in 2012 to ₦7.119 trillion in 2013. With annual increases of 11.03 percent and 11.80 percent in 2014 and 2015 respectively, domestic debt stock of the Federal Government stood at ₦7.904 trillion and ₦8.837 trillion in 2014 and 2015 fiscal years respectively. However, as at the end of the second quarter of 2016 fiscal year (barely one month after the approval of the 2016 FGN budget), domestic debt stock of the Federal Government of Nigeria has reached an unprecedented level of ₦10.606 trillion. This represents semi-annual growth rate of 20.02 percent in domestic debt stock of the Federal Government of Nigeria as at June 2016. Should the trend of accumulation of domestic debt stock in the first half of 2016 be sustained throughout the year, then at the end of 2016 fiscal year, the total domestic debt stock of the Federal Government of Nigeria must have risen to ₦12.730 trillion.

From all the discussions above, total domestic debt stock of the Federal Government of Nigeria has continued to move on an increasing lane. The linear trend line looks like a perfect one. Virtually all the bars representing the annual debt stock in figure 1 seem to be touching the trend line. The implication is that domestic debt stock increased at almost a stable rate throughout the study period. Supposing that domestic debt stock of the Federal Government remains at ₦10.606 trillion by the end of the fourth quarter of 2016, the implication will be that domestic debt stock recorded annual average growth rate of 15.26 percent throughout the period of 2010 – 2016. Also, the value of domestic debt stock of the Federal Government of Nigeria as at 2010 was just about ₦4.552 trillion, whereas as at June 2016, the value has gone up to just about ₦10.606 trillion. The value of domestic debt stock as at June 2016 therefore represents about 133 percent increase from the value of the debt stock as at 2010.

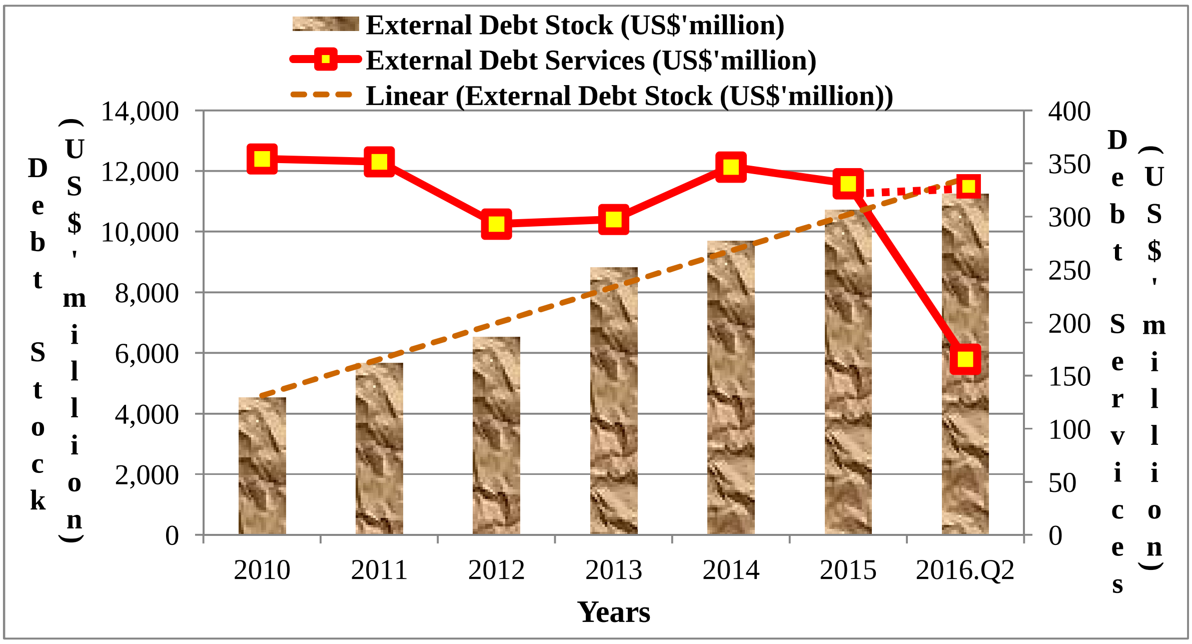
Usually, whenever debt stock increases, the burden of servicing such debts also increases. The case of domestic debts profile of the Federal Government of Nigeria is not an exception in this scenario. In order to service its domestic debts as at 2010, the Federal Government of Nigeria parted with the sum of ₦354.127 billion. The amount used in servicing service domestic debts increased by 51.75 percent from ₦354.127 billion in 2010 to ₦537.391 billion in 2011. It further increased by 34.08 percent from ₦537.391 billion in 2011 to ₦720.550 billion in 2012, and additional 10.21 percent increase from ₦720.550 billion in 2012 to ₦794.105 billion in 2013. As at 2014, the Federal Government of Nigeria parted with the sum of ₦865.809 billion due to domestic debt service, representing 9.03 percent increase from the ₦794.105 billion spent for the same purpose in 2013. The 2015 fiscal year which was an election year in Nigeria had its fair share of domestic debt service. The Federal Government of Nigeria spent the sum of ₦1,018.131 billion on domestic debt service in 2015, representing 26.05 percent increase from the ₦865.809 billion spent for the same purpose in 2014 fiscal year. Interestingly, as at June 2016, the Federal Government of Nigeria had spent the sum of ₦641.684 billion on domestic debt service. This figure is taken from the DMO website but the figure from the MTEF 2017-2019 indicates a total domestic debt service of N567,915 billion. If this trend continues, by the end of 2016 fiscal year, the Federal Government of Nigeria should have spent the sum of ₦1,283.369 billion on domestic debt service.

From the discussion on domestic debt service, it is even clear that the amount spent on domestic debt service as at the first half of 2016 represents 81 percent increase from the amount spent for the same purpose in the whole of 2010 fiscal year. In addition, should the Federal Government sustain throughout the year the trend started in the first half of 2016 for domestic debt service, then the amount that would have been spent on domestic debt service in 2016 fiscal year alone would have represented about 262 percent increase from what was spent on domestic debt service in 2010 fiscal year by the Federal Government of Nigeria. It will also imply that throughout the period of 2010 – 2016, amount spent on domestic debt service increased by an average of 24.79 percent on annual basis.

2.1.2 External Debt Profile of the Federal Government

Nwankwo (2011)[11] identified the period of 2000 – 2006 as the first stage in Nigeria's debt management, when the country's external debt profile was considered unsustainable. However, the debt relief package of 2005 changed the scene. Nevertheless, the gains of the barely one decade ago seems to have been eroded by geometric growth recorded in external debts within the period of 2010 – 2016. Figure 1 below is a graphical presentation of how the Federal Government of Nigeria has accumulated external debts over the period of 2010-2016.

Figure 2: Growth in FGN External Debt Profile and External Debt Burden on FGN Finances



Sources: *DMO's Annual Reports and Statements of Accounts (2010, 2011, 2012, 2013, 2014, 2015); Reports of External Debt Stock and External Debt Service (2016Q1 & Q2)*

[11] ibid.

Figure 2 above shows that as at 2010, external debt stock of the Federal Government of Nigeria amounted to only US$4.532 billion. It increased by 24.97 percent from its value in 2010 to be valued at US$5.667 billion in 2011. Just as 2011, the 2012 fiscal year recorded another increase in external debt stock of the Federal Government of Nigeria. At this point, total external debt stock of the Federal Government of Nigeria had already reached US$6.527 billion. The largest increase in external debt stock of the Federal Government of Nigeria was recorded in 2013 when the total external debt stock stood at US$8.822 billion, implying year-on-year increase of 35.16 percent from its value of US$6.527 billion in 2012. The 2014 and 2015 fiscal years recorded similar trend in the growth rate of external debt stocks. External debt stock stood at US$9.711 billion and US$10.718 billion respectively in 2014 and 2015 fiscal years, implying 10.08 percent and 10.37 percent annual growth rates respectively. As at the first half of 2016 fiscal year, external debt stock of the Federal Government of Nigeria had increased to US$11.262 billion, implying semi-annual increase of 5.07 percent from the 2015 value of the debt stock.

From the discussion above, external debt stocks of the Federal Government of Nigeria continued to increase throughout the study period. As was the case in figure 1 above, the linear trend line in figure 2 above looks like a perfect one. Virtually all the bars representing the annual debt stock in figure 2 seem to terminate at the trend line. The implication is that external debt stock increased at almost a stable rate throughout the study period. Should the external debt stock of the Federal Government of Nigeria remain at US$11.262 billion by the end of the fourth quarter of 2016, growth in external debt stock of the federal government would have amounted to 16.81 percent average annual growth rate through the period of 2010 – 2016. In the same way, the value of external debt stock of the Federal Government of Nigeria as at first half of 2016 which stood at US$11.262 billion represents about 148 percent increase from the 2010 value of the debt stock which was recorded as US$4.534 billion.

Ideally, given that the external debt stock of the Federal Government of Nigeria rose throughout the study period of 2010 – 2016, external debt service requirement of the government should also rise commensurately. However, our observation shows that external debt service of the Federal Government of Nigeria fluctuated downwards throughout the study period. From external debt service obligation of US$354.42 million in 2010, the Federal Government of Nigeria only spent the sum of US$331.06 million in servicing its external debts in 2015. As at June 2016, the Federal Government of Nigeria has also spent the total sum of US$165.66 million in servicing its external debts in 2016. Even if this amount is doubled by the end of the year, the Federal Government of Nigeria would have spent only US$331.32 million in servicing its external debts in 2016. This amount is still much less than the US$354.42 million used in servicing the external debts in 2010, when the total external debt stock was only US$4.534 billion. As at 2015, FGN's external debt stock value represents an increase of about 136 percent from its value as at 2010, whereas the value of external debt service in the same 2015 represents a decline of 6.59 percent from the value of external debt service in 2010.

From the discussion on external debt service, it is clear that the Federal Government of Nigeria is gradually slipping into another era of debt trap. Should the government continue to geometrically increase its external debt stock (as is the case in figure 2 above) without commensurate increase in its commitment to external debt service, soon the government will have to undergo another round of debt relief in less than two decades. This assertion is based on the fact that as at 2005, total external debt of Nigeria stood at about US$30 billion. Given the geometric growth rate of external debt stock, another 148 percent increase in another 5.5 years from June 2016 will mean that as at December 2021, the total external debt stock of the Federal Government of Nigeria would have amounted to US$27.972 billion

2.2 FG's Debt and Fiscal Responsibility Act

There are laws that should guide every responsible and transparent step taken by the Federal Government of Nigeria in the projection and implementation of its fiscal activities. The 2007 Fiscal Responsibility Act is one of such laws. Specifically, section 41 (1) (a) of the FRA, states that:

> *The framework for debt management during the financial year shall be based on the following rules-*
>
> *(a) Government at all tiers shall only borrow for capital expenditure and human development, provided that such borrowing shall be on concessional terms with low interest rate and with a reasonably long amortization period subject to the approval of the appropriate legislative body where necessary;*

Also, Section 44 of the Fiscal Responsibility Act provides that:

> *(2) Without prejudice to subsection (1) of this section, each borrowing shall comply with the following conditions-*
>
> > *(a) the existence of prior authorization in the Appropriation or other Act or Law for the purpose for which the borrowing is to be utilized; and*
> >
> > *(b) the proceeds of such borrowing* ***shall solely be applied*** *towards long-term capital expenditures.*
>
> *(3) Nothing in this section shall be construed to authorize borrowing in excess of the limits set out in section 44 of this Act.*

The implication of the above extract from the 2007 Fiscal Responsibility Act is that the law does not permit any tier of government to borrow funds for recurrent expenditures. Loans are only meant to service long term capital projects and human development in Nigeria. However, the 2016 budget of the Federal Government of Nigeria appropriated the sum of ₦1.59 trillion to capital projects. At the same time, the 2016 budget projected to borrow the sum of ₦1.84 trillion in order to finance its fiscal deficit in the budget. This means that up to ₦250 billion is meant to be borrowed for financing recurrent expenditures in the budget. This is an aberration to the stipulations of the Fiscal Responsibility Act 2007 as quoted above. Moreover, given the high cost of borrowing, it does not make any economic sense to borrow such bogus amount in order to finance recurrent expenditures.

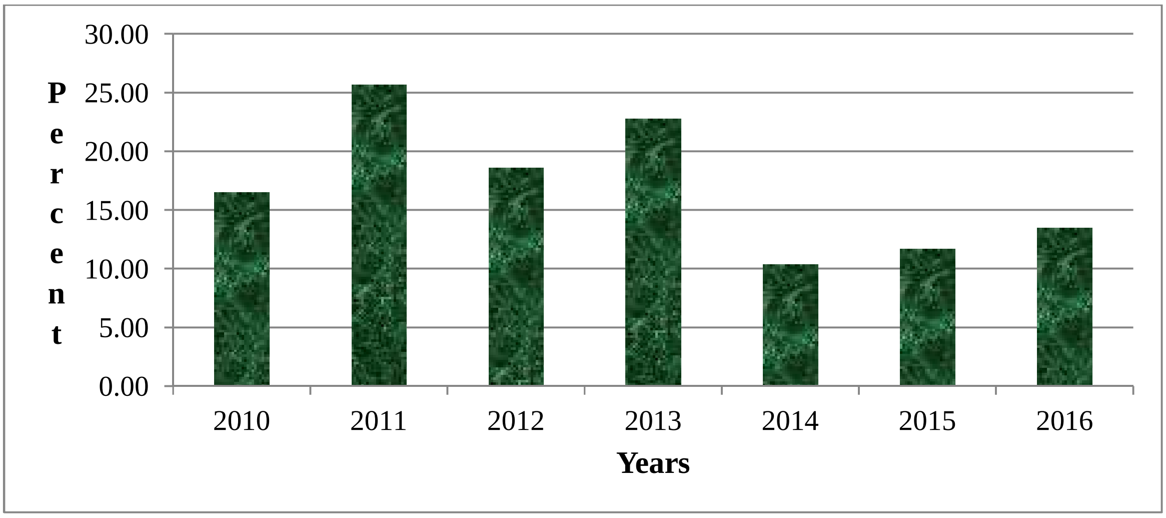
2.3 FG's Debt to GDP Ratio and Implications

Stipulating some important functions of the Fiscal Responsibility Commission and the Debt Management Office, section 44 of the 2007 Fiscal Responsibility Act stipulates that:

> *(4) The Commission shall verify on a quarterly basis, compliance with the limits and conditions for borrowing by each Government in the Federation.*
>
> *(5) Without prejudice to the specific responsibilities of the National Assembly and Central Bank of Nigeria, the Debt Management Office shall maintain comprehensive, reliable and current electronic database of internal and external public debts, guaranteeing public access to the information.*

The above section of the Act implies that the Debt Management Office should prepare Debt Sustainability Analysis of the fiscal position of the Federal Government of Nigeria based on some given guidelines. The Fiscal Responsibility Commission will therefore use the prepared Debt Sustainability Analysis to measure whether the Federal Government should still borrow more or not. One of the major benchmarks for measuring the level of sustainability of a country's debt is using total debt to GDP ratio. Based on available information from the annual reports of Debt Management Office, the Table below presents the annual debt to GDP ratio of Nigeria over the study period.

Figure 3: Trend of Debt to GDP Ratio in Nigeria



Sources: *DMO's Annual Reports and Statements of Accounts (2010, 2011, 2012, 2013, 2014, 2015); DMO's Debt Sustainability Analysis (2016)*

As stated in the DSA 2016, the maximum limit for debt to GDP ratio for Nigeria and countries in its peer group based on the Country Policy and Institutional Assessment is 56 percent. However, Nigeria's DMO has a country specific limit of 19.39 percent in the medium term up to 2017. Therefore, it can be argued that Nigeria remains within an acceptable boundary throughout the study period. The highest observed debt to GDP ratio in Figure 3 above was 25.7 percent recorded in 2011. It is clear that between 2010 and 2013, the ratio of debt to GDP hovered between 16.5 percent and 25.7 percent, but there was a crash in the ratio in 2014. This owes to the fact that Nigerian GDP figure was rebased in 2014, moving the value of total output of Nigeria to about 80 percent of its previous value. The implication is that instead of 10.4 percent recorded in 2014, the ratio of Nigeria's debt to GDP would have still hovered around 18 – 20 percent assuming the economy was not rebased. This is especially true as there was still a huge increase in total domestic and external debt stock of the Federal Government in 2014 from what they were in 2013.

It should be noted that debt to GDP ratio is mostly utilised as a good measure of debt sustainability in countries where income tax makes a major source of revenue for the government. In such a case, the ability of the government to pay up its debts depends largely on the incomes of the citizens, who in turn pay taxes to the government. In the case of Nigeria, income taxes have not been a major source of revenue for the government. Until 2015 fiscal year, oil revenue makes up more than 65 percent of total federally collected revenues. This leaves less than 35 percent for all other sources of non-oil revenues. Even in 2015 fiscal year, oil revenue still accounted for about 55.41

percent of total federally collected revenues in Nigeria, while non-oil sources of revenue accounted for only 44.59 percent of total federally collected revenues in the country. Again, the DSA 2016 acknowledges paradoxically, that there is no direct link between the size of Nigeria's GDP and its revenue base.

It should also be emphasised here that though oil sector accounts for a larger share of total federally collected revenues in Nigeria, yet the sector contributes only about 10 percent of real GDP. For instance, as at 2015, the oil and gas sector contributed only 9.61 percent of real GDP in Nigeria, whereas in the same year, the sector accounted for 55.41 percent of total federally collected revenues. The sensible thing to do is to rather rely on other benchmarks for measuring debt sustainability in Nigeria than debt to GDP ratio.

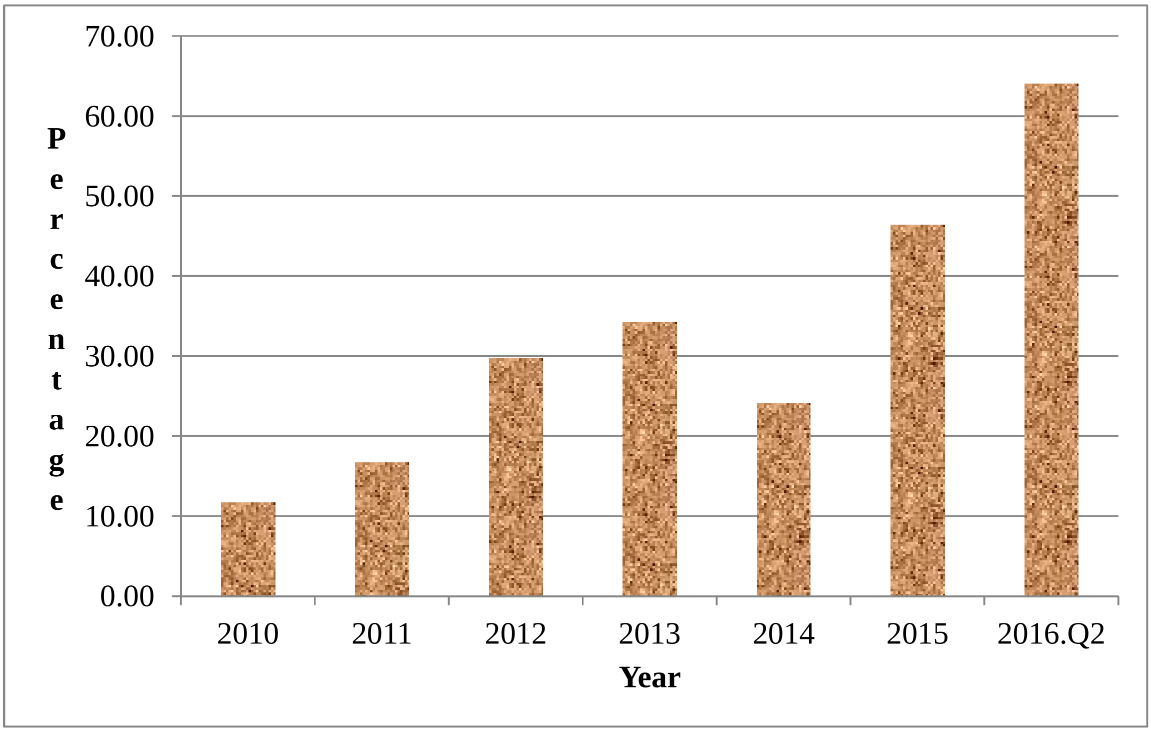
2.4 Debt Servicing and Retained Revenues

It is imperative to examine the debt service as a ratio of retained revenue. From Figure 4 below, we observe that as at 2010 fiscal year, Nigerian government needed only 11.7 percent of its revenue to service its debt. But the ratio grew geometrically to become 34.3 percent as at 2013 – implying almost 200 percent increase in the ratio in a matter of three years. The ratio fell a little in 2014 before moving up to 46.4 percent in 2015 and later settled at 64 percent in the first half of 2016[12]. The implication is that in 2016, if the trend in the first six months continues to the end of the year, Nigeria will dedicate almost two thirds of its retained revenue to service accumulated debts. Without accumulating any further debt, the government will only pay its salaries and cater for the infrastructural needs of the people with only 36 percent of its retained revenues. Such a situation poses a great challenge to the government that will cater for the citizens and its running costs with only 36 percent of its revenues. The usual escape route in such situations is to borrow more and reschedule the debts – merely shifting the evil days.

Again, according to the draft MTEF 2017-2019, for the first half of 2016, the country has so far spent N2,419.375billion and has thereby incurred a debt/deficit of N1,467.855billion. Thus, the retained revenue constitutes only 39.33 percent of total expenditure in the first half of the year whilst borrowing funded 61 percent of total half year expenditure. Total capital expenditure in the half year amounted to N159.062billion; the implication of the foregoing is that out of the N1,467.855 billion which Nigeria borrowed, N1,308.793billion was spent on recurrent expenditure[13]. This is against the dictates of the FRA on borrowing and debt management.

[12] Nigeria spent N609.517billion in debt servicing in the first half of 2016 whilst it earned N951.52billion as overall retained revenue in the same first half of 2016. See the draft MTEF 2017-2019.
[13] The portion of the debt used for recurrent expenditure amounts to 89.16 percent of the borrowed funds.

Figure 4: Trend of Debt Service to Revenue Ratio in Nigeria



Sources: *DMO's Annual Reports and Statements of Accounts (2010, 2011, 2012, 2013, 2014, 2015); 2016 Half Year figure obtained from 2017-2019 MTEF & FSP Executive Proposal.*

3. CURRENTLY PROPOSED EXTERNAL LOAN AND IMPLICATIONS FOR FEDERAL GOVERNMENT OF NIGERIA'S DEBT PROFILES

The President of the Federal Republic of Nigeria has approached the National Assembly to approve the medium term borrowing plan of the Federal Government of Nigeria (2016 – 2018). As important and genuine as the request may be, there are laid down rules for such attempts. Section 44 of the Fiscal Responsibility Act stipulates that:

> *(1) Any Government in the Federation or its agencies and corporations desirous of borrowing shall, specify the purpose for which the borrowing is intended and present a cost-benefit analysis, detailing the economic and social benefits of the purpose to which the intended borrowing is to be applied.*

It is upon the above premise that the National Assembly did not consider the request of Mr President as it did not contain cost-benefit analysis of the intended loans and the detailed economic and social benefits of the line items (projects) for which the money will be borrowed.

It is important to critically analyse the proposed borrowing plan in the light of its sustainability, costs, benefits and capacity to repay. Therefore, this section highlights some of the important issues that need to be considered either in support or opposition to the proposed borrowing plan of the President.

3.1 The 2016 Debt Sustainability Analysis by the Debt Management Office: Implications for the Proposed Loan (2016 – 2018)

The 2016 Debt Sustainability Analysis exercise by the Debt Management Office was organised at a time when the Nigerian economy had just been declared to have entered into recession. Bearing in mind that the fiscal policy instruments of the Federal Government of Nigeria should be considered relevant in reflating the economy so as come out of the recession, it is surprising that this exercise could ignore some of its glaring findings to still make recommendations for further borrowing. It is therefore important to look at some of the findings of that exercise and critically examine if such findings should favour the list of fifteen (15) recommendations that came out from the findings.

3.1.1 Optimistic Findings

i) ***Debt to GDP Ratio:*** With an estimated present value of total debt to GDP ratio of 13.5 percent in 2016, the Debt Management Office believes that the Federal Government of Nigeria still has a wide of up to US$22.08 billion (equivalent of about ₦6.4 trillion) to borrow more. This assertion is based on the country-specific threshold of 19.39 percent of GDP. In addition, using the peer group threshold of 56 percent of GDP, Nigeria still has a lot of space to borrow more than three times its current total debt stocks since that will still leave Nigeria within the threshold. Even when the total public debts of all the tiers of government in Nigeria are considered in terms of their ratio to GDP, their sum still leaves Nigeria with a lot of space to borrow more. The debt sustainability analysis exercise of the DMO reveals that the present value of total public debt of Nigerian governments as a ratio of GDP stands at 15.9 percent in 2016. Just as when the Federal Government debt was considered alone, the total public debts of Nigerian governments still fall below the country specific threshold of 19.39 percent and the peer group threshold of 56 percent.

ii) ***Total Debt to Revenue Ratio:*** With an estimated present value of total public debt of all tiers of government in Nigeria to revenue ratio of 291.9 percent in 2016, the Debt Management Office of Nigeria holds the opinion that Nigerian governments still operate within the country specific acceptable threshold of 350 percent. However, this opinion is strictly for the sum of the total debt stock of all the tiers of government in Nigeria (national and sub-national governments). But the FGN only debt to revenue indicator in 2016 is projected at 395.3 percent and to reach 437.9 percent in 2018 thereby breaching the 350 percent country specific threshold.

3.1.2 Baseline Findings

i) ***Total Debt to Revenue Ratio:*** The debt sustainability analysis exercise by the Debt Management Office arrives at a total debt to revenue ratio of 395.3 percent for the Federal Government of Nigeria alone. This ratio is considered to be clearly above the country-specific threshold of 350 percent for the Federal Government of Nigeria. The proposed borrowing plan of 2016 – 2018 implies that the ratio of Federal Government total debts to revenue will escalate to 437.9 percent by 2018. This ratio will be way above the 350 percent country-specific benchmark. Both the current and proposed total debt stocks suggest that the present value of debt to revenue ratio of the Federal Government of Nigeria is very unsustainable. It becomes very worrisome to observe that the revenue base of the Federal Government cannot sustainably service the public debt.

ii) ***Debt Service to Revenue Ratio:*** The debt sustainability analysis exercise by the Debt Management Office arrives at a debt service to revenue ratio of 50.3 percent in 2016 for the Federal Government of Nigeria alone. This ratio is considered to be clearly above the country-specific threshold of 28 percent for the Federal Government of Nigeria. The projections for subsequent years still fall outside the threshold up till 2031, before it eventually trended downwards to 25.7 percent in 2036. It becomes worrisome that debt service to revenue ratio is up to 50 percent. The implication is that even if the Federal Government borrows any money to support available revenue, the acquired loans may still be used in servicing accumulated debts. Otherwise, this ratio implies that less than 50 percent of Federal Government of Nigeria's revenues will be channelled to administration and infrastructural development of the country.

3.1.3 Lessons from the Findings and Recommendations of 2016 DSA

It is important to emphasise here that the debt sustainability analysis exercise by the Debt Management Office discussed both the optimistic and baseline scenarios in detail, but ignored the baseline scenario only to make recommendations based on the positive scenario. It is imperative to state that the DMO did not consider any need for projecting the usual pessimistic scenario after the baseline scenario. This raises the question thus: why should recommendations be based on debt to GDP ratio when the debts are not serviced with GDP? It is a known fact that Nigeria's GDP growth is unconnected with Federal Government Revenues. Since GDP is not connected with Federal Government Revenues, it becomes necessary to query why the ratio of debt stock to GDP should be an acceptable yardstick for measuring debt sustainability for the Federal Government of Nigeria.

The baseline findings of the debt sustainability analysis exercise seem to be more representative of the reality of the Federal Government of Nigeria's debt management. It is clear that realistic debt sustainability in Nigeria should focus on revenue generating sources of the Federal Government of Nigeria rather than focusing on GDP that yields little (or nothing) to the Federal Government of Nigeria's coffers. Based on repayment capacity of the government from the angle of government revenue, it is clear that the Federal Government of Nigeria has already overshot its capacity. Therefore, recommending that the government should still borrow additional US$22.08 billion on the basis of country-specific threshold of debt to GDP ratio looks as though those making the recommendation do not have full understanding of the macroeconomic environment of Nigerian economy.

Looking at the fifteen (15) recommendations in the report, we can conclude that some of the recommendations are worth reemphasising, while some others should be jettisoned for lack of merit on the basis of the prevailing macroeconomic environment. Below is a summary of our positions on the recommendations:

(i) The first two recommendations are based on the optimistic scenario of debt to GDP ratio, and we have shown why this should not be regarded as a good yardstick for measuring debt sustainability in Nigeria. Therefore, we jettison the recommendations.

(ii) It is true that the third recommendation draws from the second, yet it has some implications that should not be ignored. Critical examination of Figures 1 and 2 above reveals that domestic debts are serviced with 10 – 12 percent of the debt stock without necessarily depleting the principal, whereas, external debts are serviced with 2 – 3 percent of the debt stocks. The implication is that the costs of borrowing (interests) from domestic sources are usually very high for the government. As at 2016, total debt portfolio of the Federal Government of Nigeria skews towards domestic debts. There is therefore need to rebalance the debt portfolio by borrowing more from external sources. However, caution must be applied in doing so, due to the foreign exchange volatility risks that may be associated with foreign debt services.

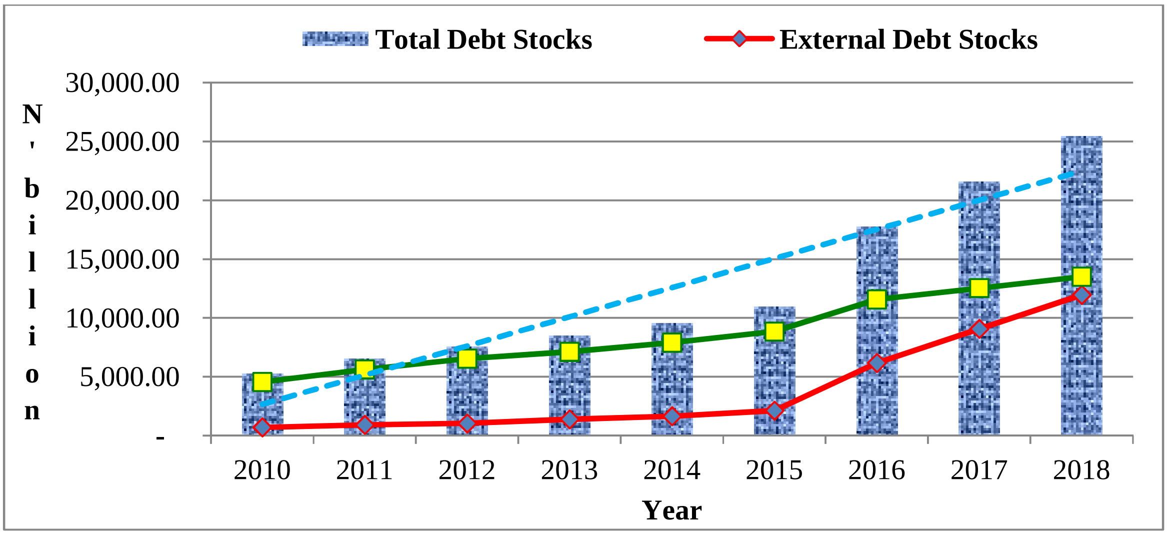
(iii) The fourth recommendation for the DSA report calls on the Federal Government of Nigeria to develop or formulate an ***Economic Blueprint or Roadmap*** for the medium term. Apart from serving as an economic compass for the present administration, the economic blueprint will also serve as a confidence booster in local and international investors' outlook of Nigerian economy. However, it is surprising to observe that even when there is still no economic roadmap, the Debt Management Office throws its full support to the Federal Government's moves towards borrowing US$29.96 billion from external sources.

Apart from the first four recommendations of the DSA report, the rest of the recommendations are regarded as generic recommendations to the government. These other recommendations are not necessarily drawn from the findings of the DSA exercise, but are based on day to day observations from the economic situation in Nigeria. However, it is surprising that there was not a single recommendation that took note of the baseline scenario as contained in the findings of the exercise, even if such a recommendation may be regarded as "on the other hand" recommendation[14].

3.2 Expected Growth Trend in FG's Debt Profiles (2016 – 2018)

With the recent request for external loan of US$29.9 billion, there should be a growth in the current debt profile of the Federal Government of Nigeria. The Figure below shows what the external debt profile of the Federal Government should look like when the loan is obtained. In preparing the expected growth trend, we assume an even distribution of the proposed amount over the three year period of 2016 – 2018 fiscal years.

Figure 5: Expected Growth Trend in FG's Debt Profiles (2016 – 2018)



[14] Recommendations that are given in case the conditions that should have made the major recommendations unattainable or unrealistic.

Sources: *CBN's Statistical Bulletin (2015); DMO's Debt Sustainability Analysis (2016); and the President's Request for Approval of Medium Term Borrowing Plan (2016–2018)*

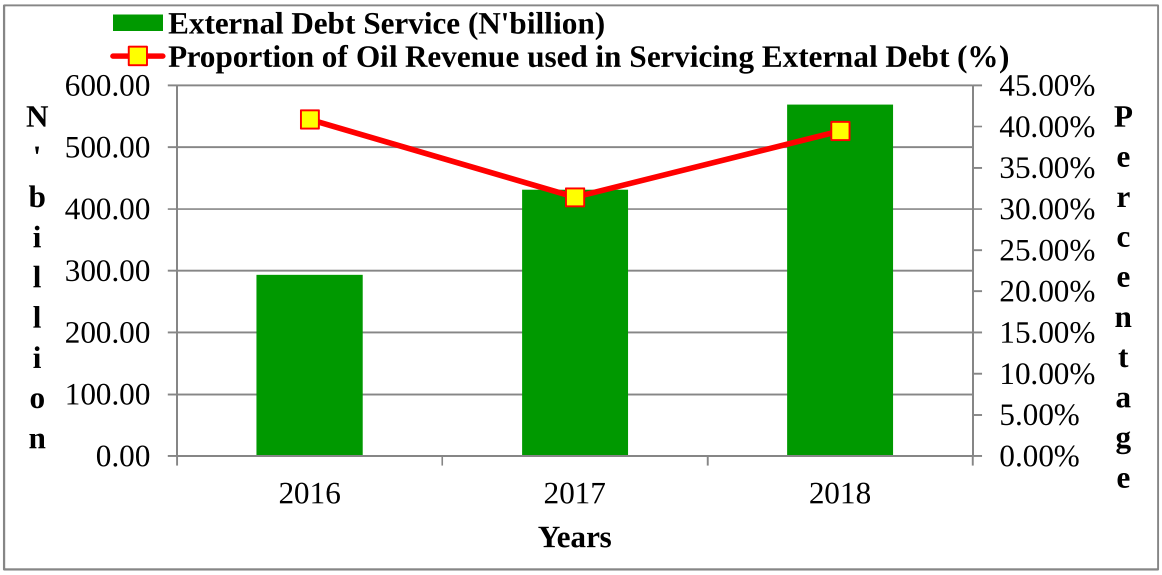
Should the Federal Government of Nigeria secure the requested approval for borrowing US$29.96 billion from external sources, the total debt profile of the Federal Government of Nigeria is expected to rise as shown in Figure 5 above. In preparing the expected growth trend in the Federal Government's debt profiles, we assume that the US$29.96 billion proposed for borrowing by the President of the Federal Republic of Nigeria will be borrowed evenly throughout the medium term period of 2016 – 2018. The implication is that every year the Federal Government of Nigeria will borrow the sum of US$9.987 billion. At the projected exchange rate of ₦290/US$1 throughout the period, the annual expected loan amounts to ₦2.896 trillion that will be added to the existing external debt stock of the Federal Government of Nigeria per year. To this end, the present administration intends to grow the Federal Government's external debt stock from the current value of US$11,261.89 million as at second quarter of 2016 to US$41,221,90 by end of 2018 fiscal year.

It is important to emphasise that the annual average amount projected to be borrowed within the three year period is much more than the entire external debt accumulation of the Federal Government between 2010 and 2015 fiscal years. As at December 2009, the total external debt stock of the Federal Government of Nigeria stood at US$3,947.3 million, whereas it increased to US$10,718,43 million as at December 2015. This means that from January 2010 to December 2015, the Federal Government of Nigeria accumulated total external debt stock of US$6,711.13 million – implying annual average external debt accumulation of US$1,128.52 million over the six year period of 2010 – 2015. The annual average amount proposed to be borrowed within the three year period of 2016 – 2018 sums up to US$9,987 million (much higher than the total sum borrowed within six years – US$6,711.13 million).

3.3 External Debt Service and FGN Oil Revenues

The 2016 oil revenue forecast has been faced with high level of deviation from the reality. This partly owes to the volatility in international market oil prices, and also partly to the volatility in domestic production of crude oil due to militancy in the oil producing areas in the country. To this end, if nothing is done in order to curb the current tide of militancy in that part of the country, the burden of servicing the proposed loan together with existing/accumulated debts may be high. The Figure below uses the oil revenue forecasts in the proposed 2017 – 2019 MTEF of the Federal Government of Nigeria in forecasting what the debt burden of servicing the recently proposed medium term loan of the Federal Government should look like. The Figure also assumes that the annual repayment burden is the average burden of 4.76 percent of the external debt stocks.

Figure 6: Forecast of External Debt Service and FGN Oil Revenues (2016 – 2018)



Source: *Oil Revenue Forecasts from proposed 2017 – 2019 MTEF; External Debt Service Projection is Author's own calculations with assumptions based on previous years' experiences*

Figure 6 above assumes that there is no moratorium period that will be given by the proposed creditors. Therefore, we assume that the need to service the external debts begins to count from the moment the loans are obtained. Given an average of 4.76 percent cost of the loan (based on calculation of external debt service for the period of 2010 – 2015), the equivalent sum of ₦293.32 billion will be required to service external debts in 2016 alone. This required amount implies about 40.88 percent of the total projected oil revenues in 2016 according to the proposed 2017 – 2019 MTEF. However, the required amount for servicing external debts in 2017 is expected to increase due to increase in the overall external debt stock. As a result, by 2017 the sum of ₦431.17 billion will be required to service external debts. The projected debt service implies about 31.42 percent of expected oil revenues in the same year. In like manner, the required amount for servicing external debts in 2018 is also expected to increase due to increase in the overall external debt stock. As at 2018, the sum of ₦569.03 billion will be required to service external debts. The projected debt service implies 39.48 percent of expected oil revenues in the same year. This rate of external debt service (excluding domestic debts) cannot imply sustainability.

3.4 Proposed Medium Term Borrowing Plan (2016 – 2018) and the Proposed MTEF 2017 – 2019: Implications for Fiscal Responsibility Act

The Medium Term Expenditures Framework (MTEF) of the Federal Government of Nigeria for the period 2017 – 2019 provides a roadmap for the capital expenditure forecast of the Federal Government within the three year period. The MTEF shows the Federal Government forecast of expected revenues and what the revenues should be targeted at in the medium term period of 2016 – 2018. It is interesting to observe that the proposed 2017 – 2019 Medium Term Expenditures Framework of the Federal Government of Nigeria estimates that the sum of ₦1.765 trillion will be spent on capital projects in 2017 fiscal year. It also estimates that the sum of ₦1.800 trillion will be spent on capital projects in 2018 fiscal year, the sum of ₦1.850 trillion will be spent on capital projects in 2019 fiscal year. As a sum, the Federal Government of Nigeria proposes to spend the sum of ***₦5.415 trillion*** on capital projects between 2017 and 2019. Adding the 2016 approved capital budget of ₦1.588 trillion to the total amount on proposed 2017 – 2019 MTEF, we have a total of ***₦7.003 trillion*** to be spent on capital projects between 2016 and 2019 fiscal years.

However, recall that the proposed medium term borrowing plan of the Federal Government of Nigeria only covers the period of 2016 – 2018 fiscal years, while the MTEF covers the period of 2017 – 2019 fiscal years. Therefore, we can separate the proposed capital expenditures for 2019 fiscal year as contained in the MTEF and add the 2016 approved capital expenditures in order to arrive at what the borrowing plan should cover. As shown above, the 2016 approved budget of the Federal appropriated the total sum of ₦1.588 trillion for capital projects. On the other hand, the proposed MTEF estimates the sum of ₦1.765 trillion for capital projects in 2017 fiscal year, and the sum of ₦1.800 trillion for capital projects in 2018 fiscal year. Based on the 2016 approved budget and the proposed 2017 – 2019 MTEF, the Federal Government of Nigeria allocates the total sum of ***₦5.153 trillion*** to capital projects between 2016 and 2018 fiscal years.

Using the current exchange rate and the exchange rate forecast in the MTEF, the proposed total external loan sum of US$29.96 billion is equivalent to the sum of ***₦8.688 trillion***. Comparing this amount with the calculated sum of capital expenditures between 2016 and 2018 fiscal years of ***₦5.153 trillion***, we observe a variance of up to ***₦3.536 trillion*** of unaccounted amounts in the proposed loan. Similarly, we may assume that the proposed loan will cover only the period of the proposed MTEF (i.e. 2017 – 2019) as a result of the time lag required for approval of the request by the National Assembly. In this case, we also observe a variance of up to ***₦3.273 trillion*** of unaccounted amounts in the proposed loan. This is based on the difference between the requested loan amount of ***₦8.688 trillion*** and the proposed capital expenditures of ***₦5.415 trillion*** contained in the proposed MTEF of 2017 – 2019 fiscal years. On the other hand, we may assume that the proposed loan will be utilised from 2016 fiscal year and even last up to the end period of the proposed MTEF (i.e. 2019). Even if the loan spreads between 2016 and 2019, we still observe a variance of up to ***₦1.686 trillion*** of unaccounted amounts in the proposed loan. This is based on the difference between the requested loan amount of ***₦8.688 trillion*** and ***₦7.002 trillion*** (the sum of 2016 approved capital budget of ₦1.588 trillion and the proposed capital expenditures of ₦5.153 trillion in the proposed MTEF of 2017 – 2019 fiscal years).

All the above shows that the proposed loan amount in the request for approval as submitted by the President of the Federal Republic of Nigeria to the National Assembly is way above all known capital projects conceivable by this administration. Recall that the position of Fiscal Responsibility Act is clear on a matter like this. Section 44, Subsection 2 of the Fiscal Responsibility Act provides that:

> *(2) Without prejudice to subsection (1) of this section, each borrowing shall comply with the following conditions:*
>
> *(a) the existence of prior authorization in the Appropriation or other Act or Law for the purpose for which the borrowing is to be utilized; and*
>
> *(b) the proceeds of such borrowing* ***shall solely be applied*** *towards long-term capital expenditures.*

If the provisions of this Act is binding on all tiers of government (including the Federal Government of Nigeria), it therefore implies that the Federal Government of Nigeria stands to contravene this section of the Act by requesting for a loan sum of up to ***₦8.688 trillion*** in the medium term of 2016 – 2018 fiscal years. This is because the 2016 approved capital budget of the Federal Government and the capital expenditures estimate of the Federal Government for 2017 and 2018 (as contained in the MTEF) only sum up to ***₦5.153 trillion***. The implication is that the excess of ***₦3.536 trillion*** in the proposed medium term loan contravenes paragraph (b) of Section 44, Subsection 2 of the Fiscal Responsibility Act which stipulates that every borrowing shall solely be applied to long term capital expenditures. This also raises the question of what the Federal Government of Nigeria intends to use the variance of the loan sum to do – for recurrent expenditure or for yet-to-be-identified capital expenditures. Whether the variance will be used for recurrent expenditures or for yet-to-be-identified capital expenditures, the Federal Government will still contravene the Fiscal Responsibility Act because capital projects must have been identified and appropriated before request for loans should be made in order to actualise the appropriation.

It is equally important to analyse the position of the Director-General of the Debt Management Office of Nigeria – Dr Abraham Nwankwo – in the light of the stipulations of Fiscal Responsibility Act. According to the DG of DMO, "If we build infrastructure in the next five to seven years before those loans mature in 15 to 30 years, Nigeria would be in a position to service its debts and turn around the economy[15]." However, this is only possible in a situation where the loan is used in financing real long term capital projects. It should be observed that in the case of the current request for approval of medium term loan by the Federal Government of Nigeria, the Presidency could only show where US$575 million of the proposed loan amount will be spent on. Incidentally, the justified amount only goes for social protection matters and not real capital projects. This leaves us with the question of what could qualify as long term capital projects in line with the stipulation of the Fiscal Responsibility Act. Borrowing to finance social protection issues will become more of a debt trap than the 2004/2005 Paris Club debt of the Federal Government of Nigeria.

Further, the issue of borrowing for budget support needs to be interrogated. What is the support tied to? Is it project aid tied to specific capital projects and deliverables or a general balance of payments support? Will the support be used to fund consumption and recurrent expenditure? The FRA should provide the guide for NASS.

3.5 The Eurobond Challenge

> *"A Eurobond is an international bond that is denominated in a currency not native to the country where it is issued. Also called external bond; "external bonds which, strictly, are neither Eurobonds nor foreign bonds would also include: foreign currency denominated domestic bonds*[16]"

FGN proposes to raise $4.5billion in Eurobonds. These are purely commercial bonds that are not concessional in nature as contemplated in section 41 of the FRA. The section requires that debts be concessional in nature with low interest rate and a long amortization period. The FRA defines concessional debt as a loan that comes with an interest rate that is less than 3 percent per annum. Eurobonds attract other costs which may reduce the final amount the borrower gets. Again, the President's request letter did not tie the Eurobonds to any specific projects and programmes. This makes the utilization flexible and it may be used for matters that are not capital expenditure and human development as stipulated by section 41 of the FRA. It is highly susceptible to mismanagement since it is not project tied.

Expert opinion postulates that the Eurobond component may heighten the sustainability challenge of the overall external debt stock.

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[15] Chiejina, N. (2016) "$29.9b loan not a trap, says DMO chief". The Nation Newspaper, November 08, 2016. Also available at: http://thenationonlineng.net/29-9b-loan-not-trap-says-dmo-chief/

[16] https://en.wikipedia.org/wiki/Eurobond

"According to data obtained from the Debt Management Office website, Nigeria's external debt stock as at 30th June 2016 of about $11.26billion comprises US$7.99 billion from multilateral sources (representing 70.96 per cent), US$1.77billion bilateral (or 15.72 per cent) and US$1.50billion Eurobonds which translates to 13.32 per cent. In spite of the low size of Eurobonds relative to the other two sources, the cost of actual external debt service payments in the first quarter of 2016 was highest for Eurobonds which took up 38.8 per cent with multilateral and bilateral sources accounting for 36.7 per cent and 24.5 percent respectively. To further underscore this point, as at October 31 2016, the closing prices and yields of Nigeria's 10-year Eurobond (2013-2023) were US$97.146 and 6.912 percent respectively. It is instructive to note that the yield of this US$500 million Eurobond at issue was 6.625 percent and given the inverse relationship between bond prices and yields, the increasing yield and lower price is a reflection of the waning investor confidence"[17].

From the above quote, a debt stock of 13.32 per cent gulps 38.8 percent of debt repayment. This clearly shows that the interest rate and charges attached to the Eurobond are very high and beyond the contemplation of the FRA. Going for the Eurobonds at a time of declined commodity prices, depleted foreign reserves and waning investor confidence will ensure that the rates of interest may not be less than 10 percent. The examples of the rates in the Eurobonds issued by Ghana (10.75 percent in 2014 and was reported to have abandoned a 2015 bond after few investors showed interest at 11 percent) and Angola (9.5 percent yield in 2015) bear this out[18]. This raises serious sustainability challenges.

3.6 External Loan and Debt Services: Implications for Exchange Rate Stability

On the surface, external loan will help stabilise exchange rate problem in any borrowing economy in the short run. This may not be true in the deeper sense of exchange rate management. Drawing from Pakistan's empirical evidence, Fida et al (2012) maintained that external debt is one of the significant variables that causes exchange rate to fluctuate over short period as well as longer period of time[19]. This is usually through the transmission channel of debt servicing. External debts can only be serviced with foreign currencies. This poses great threat to the stability of domestic currency especially when the burden of debt servicing is high relative to the revenue generation capacity of the domestic economy. To this end, the proposed medium term borrowing plan of the Federal Government of Nigeria may help monetary policy authorities to stabilise the current exchange rate volatility problem facing the economy, but this solution may not

[17] Uche Uwaleke, Associate Professor of Finance and Head of Department at Nasarawa State University, Keffi in Businesday of November 8 2016 at page 10.
[18] Uche Uwaleke, supra
[19] Fida, B. A.; Khan, M. M. and Sohail, M. K. (2012) Analysis of exchange rate fluctuations and external debt: empirical evidence from Pakistan". African Journal of Business Management 6(4): 1760–68

be a lasting one since the same foreign exchange earnings will also be required to service the debts when they mature.

It may not be uncommon for the Federal Government of Nigeria to propose such a borrowing plan without critically analysing the medium and long term effects of such a borrowing plan on the exchange rate position of the Naira when the debts are matured to be serviced. The short term perceived gains of borrowing from external sources may be eroded by the medium and long term exchange rate risks associated with such loans. Fida et al (2012) equally observed that on one hand, external debt servicing depletes foreign reserves of any developing economy thereby mounting pressure on the exchange rate position of the local currency of such developing country. On the other hand, exchange rate volatility increases the prices of imports in the domestic economy of developing countries thereby causing import-driven inflation in the cost of goods. This has the potency of eroding the purchasing power of the Naira as is currently being observed between 2015 and 2016.

4. CONCLUSIONS AND RECOMMENDATIONS

A lot of issues still need to be clarified in the request for the approval of Medium Term Borrowing Plan (2016 – 2018) submitted by the President of the Federal Republic of Nigeria to the National Assembly. One of such issues has to do with the disagreement between the total value of capital projects in the proposed Medium Term Expenditures Framework (MTEF) of the Federal Government of Nigeria (2017 – 2019) and the amount proposed to be borrowed between 2016 and 2018. Assuming the Federal Government will spend all its annual revenues on recurrent expenditure items throughout the two year period and all capital projects will be financed with proceeds from the proposed loan, it is clear from our discussions that the proposed loan is still higher than the capital projects that the Federal Government of Nigeria has identified so far in 2016 approved budget and 2017 – 2019 MTEF.

Another important issue that needs to be clarified is the justification for using debt to GDP ratio as a basis for declaring the Federal Government’s debt profile as sustainable, even when debt to revenue ratio and debt service to revenue ratio do no suggest such. Available debt data do not suggest that the ability of the Government to service its debts is in any way connected to GDP. This is because of the observed disconnect between the oil sector (main contributor to government revenue) and the real sectors of the economy (main contributors to GDP). Therefore, there could be increase in GDP without proportionate increase in government revenue, whereas instead of the former, it is the latter that is needed for servicing government debts. In summary, since debt to revenue ratio and debt service to revenue ratio do not suggest any sustainability in the Federal Government’s external and domestic debt stocks, it is important to reconsider the recommendations of the Debt Management Office in their 2016 Debt Sustainability Analysis. The recommendations were based on the sustainability suggestions of debt to GDP ratio.

The cost of repaying and servicing the Eurobond component of the debts will be high and needs to be properly reviewed with projections based on empirical data.

It is imperative that the National Assembly considers the President's request on a project by project basis with sustainability as the guiding principle. The expectation is that the request will not be entirely granted but it should not be totally rejected. The following policy recommendations will guide the National Assembly in the reconsideration of the request for the approval of Medium Term Borrowing Plan (2016 – 2018) submitted by the President of the Federal Republic of Nigeria to the National Assembly:

(xii) Invite the Director-General of the Debt Management Office to proffer policy recommendations on the basis of the baseline scenarios observed in the findings of the Debt Sustainability Analysis exercise of the debt management technical team.

(xiii) Ask the President to follow the stipulations of the Fiscal Responsibility Act to wait for the full approval of the submitted Medium Term Expenditures Framework (2017 – 2019), which should serve as the basis for any proposal to borrow.

(xiv) Request that the President follows the stipulations of the Fiscal Responsibility Act to revise downwards the proposed amount in the Medium Term Borrowing Plan (2016 – 2018) in order to allow same to correspond to the total capital budget and proposed capital expenditures within these years.

(xv) As an alternative, ask the President to withdraw both the proposed MTEF (2017 – 2019) and the proposed Medium Term Borrowing Plan (2016 – 2018) in order to revise both to agree on the capital projects that should demand such a huge loan.

(xvi) Ask the President for details of the projects and to provide justification for the inclusion of any project as a capital project that should be financed with the proposed loan.

(xvii) Ask the President to present the cost benefit analysis of each of the projects to be included in the borrowing plan.

(xviii) Ask the President to provide detailed borrowing plan that shows at what point in the three year period a particular amount will be borrowed and from what sources. This will help to show if this request for the approval of medium term borrowing plan is a critically thought out plan.

(xix) Ask the President to provide detailed repayment plan in accordance with the stipulations of the Fiscal Responsibility Act.

(xx) Ask the President to provide evidence of debt sustainability with forecast and justification of the sources of revenue that will be used in servicing the debts at maturity.

(xxi) NASS should consider rejecting the Eurobond component of the loan.

(xxii) Ask the President to put all the foregoing information in the public domain in accordance with the Fiscal Responsibility Act