THE NIGERIAN DEBT PROBLEM
NATURE AND IMPACT

BY

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MBA/ADMI/0862/1990-91

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CERTIFICATION

This thesis titled THE NIGERIAN DEBT PROBLEM: NATURE AND IMPACT By BELLO, USMAN MUSA meets the regulations governing the award of the degree of Master of Business Administration (MBA) of Ahmadu Bello University, Zaria and is approved for its contribution to knowledge and literary presentation.

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DECLARATION

I hereby declare that this thesis has been written by me and that all information original to this work has been duly acknowledged. The selection of topic structure the work and opinion expressed are the sole responsibility of the author.

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DEDICATION

DEDICATED TO MY WIFE KATTY AND MY CHILDREN HANAN AND AMIR

ABSTRACT

This thesis is focused on the nature, extent and impact of the Nigerian Debt problem. The study therefore aims at determining the genesis of the debt problem, its magnitude, the debt management strategies being employed to cushion its impact on the economy and how effective they have been.

The work is presented in Five Chapter, the first and last chapters being the Introduction and Summary, Conclusions and Recommendations respectively. In the second chapter, the Macro-economic framework of Nigeria was examined. Thereafter debt management was deliberated upon an attempt to provide a background to the study. In the concluding part of chapter two, the Nigerian Debt problem was discussed. The basic methodology used and reviewed in the Third chapter was the historical method with an emphasis on descriptive analysis rather than econometric analysis due to the dearth of statistical data on the topic.

Presentation of data and analysis was carried **out** in the fourth chapter according to certain economic indicators generally used for determination of debt burden such as debt service ratios and debt to exports ratios.

Finally conclusion were drawn from the study and suggestions made on the strategies to be utilized towards ameliorating the pressures of the debt burden and permit the National economy to experience real positive growth.

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GLOSSARY OF TERMS

AMORTIZATION :

The same as principal repayment.

ARREARS

The total scheduled debt service payments that have fallen due but remain unpaid.

BALANCE OF PAYMENT (BOP)

A statement showing the sum of a nation's foreign economic transactions for a given period of time. The main components are: (a) transactions in goods services, and income; (b) transactions in financial claims: (c) transfer payments, which are offsetting entries to one-sided transactions. This flow oriented concept is related to the stock oriented international investment position.

BASE RATE:

A recognized and published interest rate, for example LIBOR, used to determine the rate to be used for variable interest rate loans. The rate for the loan is determined by adding the spread to the base rate.

BILATERAL AGREEMENT:

This is the agreement singed by a debtor country and each of its creditors in the Paris Club. The bilateral agreement incorporates the common rescheduling

terms of the agreed minute and also the rates of interest on the rescheduled debt. These rates of interest are negotiated bilaterally between the debtor and each of the creditors in the Paris Club and they may differ from one creditor and the next.

BORROWER (OR DEBTOR)

The organization which is responsible for servicing the debt.

BUY BACK

The purchases, by a government, of its own debt, usually at a discount. The government reduces its obligations while the creditor receives some payment. Although regarded as not totally legitimate, sometimes the government buys back its own debt on the secondary market.

CANCELLATION:

An agreed reduction in the undisbursed balance of a loan commitment. Compare write-off.

CAPITAL ACCOUNT:

That portion of a nation's balance of payments which includes borrowing and lending (whether public pr private), investment, repayment of loans. See current account.

This can be useful to debtors having assets and income in a currency different to that required for debt servicing; the mechanism provides protection against exchange rate fluctuations.

CURRENT ACCOUNT:

That portion of a nation's balance of payment that includes imports, imports, exports, payments for services, such as insurance and transportation, earnings on foreign investment, military expenditures, private remittances, etc. excluded are capital transactions such as borrowing. Lending, repayment of loans, investment etc.

CURRENT MATURITIES:

Maturities falling due during the consolidation period of a rescheduling.

DEBT EQUITY SWAP:

An agreement to exchange a liability for equity in an enterprise. Typically, there may be clauses in the agreement to prevent the repatriation of capital before some sp.

CURRENT ACCOUNT:

That portion of a nation's balance of payments that includes imports, exports, payments for services, such as insurance and transportation, earnings on foreign investment, military expenditures, private remittances, etc. excluded

PRIVATE CREDITORS:

Bondholders (of bonds that are either publicly issued or privately placed), private banks and other private financial institutions, credits from manufacturers, exporters and other suppliers of goods.

PROMISSORY NOTE:

A written promise to repay a loan (either with or with or without interest). The note specifies the terms of the repayment of principal and interest, and can include the amount of principal installments, the rate of interest, the calculation of interest the due date and the maturity date.

PUBLIC DEBT:

The external obligation of a public debtor, including the national government, a political subdivision (or an agency of either), an autonomous public bodies.

PUBLICLY GUARANTEED DEBT:

The external obligation of a private debtor that is guaranteed for repayment by a public entity.

RESCHEDULE:

A scheme of debt renegotiation in which some percentage of debt service payments falling due during a defined period (the consolidation period), possibly including amounts in arrears at the start of the period, will be subject

are capital transactions such as borrowing, lending repayment of loans, investment etc.

CURRENT MATURITIES:

Maturities falling due during the consolidation period of a rescheduling.

DEBT EQUITY SWAP:

An agreement to exchange a liability for equity in an enterprise. Typically, there may be clauses in the agreement to prevent the repatriation of capital before some specified future date.

DEBT RELIEF:

Any action by a creditor that officially alters the terms established for repayment. Debt reorganization includes forgiveness, rescheduling, rephrasing and refinancing.

DEBT SERVICE:

All payment made against the loan, that is principal repayments plus service payments, ACTUAL is the set of repayments actually made to satisfy a debt, including principal, interest, and late fees. SCHEDULED is the set of repayments that is contractually required to be made through the life of debt, including principal and interest.

DEFAULT:

The failure to meet any obligation or term of a credit agreement or contract. A payment that is overdue or in arrears is technically in default since, by venture of non-payment that borrower has failed to abide by the terms and conditions of the credit. In practical terms, when a loan or credit is considered in default will vary be agency.

DEFERRED PAYMENTS:

Payments that have fallen due but where payment may be delayed pending resolution of some agreement, such as rescheduling agreement.

EXPORT CREDIT:

A loan extended to finance a specific purchase of goods or services from within the creditor country. Frequently, the loans have interest rates subsidized by the government as a means of promoting exports. Export credits extended by the supplier of goods are by the supplier's bank are known as buyers credits. See also export credit agency.

EXPORTS OF GOODS AND SERVICES:

These are the total goods and all services (including workers' remittances) sold to the rest of the world.

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FIXED INTEREST RATE:

A rate of interest that is defined in absolute terms at the time of the loan agreement, for example, 8.5%. Compare variable interest rate.

GNP:

Gross national product.

GRACE PERIOD;

The period between the commitment date of the loan and the date of the first principal repayment. The applies to both new and rescheduled loan.

GRANT:

A legally binding document that obligates a specific value of finds available for disbursement for which no repayment requirement exists. The term also refers to the funds disbursed. See also technical cooperation rants and grant-like flows.

GROSS NATIONAL PRODUCT (GNP):

The measure of the total domestic and foreign output claimed by residents of an economy, less the domestic output by nonresidents. GNP does not include deductions for depreciation.

GUARANTY OF A LOAN:

A legally binding agreement to pay part or all the amount due on a debt instrument extended by a lender in the event of nonpayment by the borrower.

IMF:

International Monetary Fund.

IMPORTS OF GOODS AND SERVICES;

The total value of goods and services purchased from the rest of the world.

INTEREST PAYMENTS:

Payments made in accordance with the contractual terms of a loan that specify the rate or rates of interest that are to be applied, and the way in which the interest is to be computed. The loan may have fixed or variable interest rates.

LOAN:

A legally binding document which obligates specific value of funds available for disbursement. The amount of founds disbursed is to be repaid (with or without interest and late fees) in accordance with the terms of promissory note or repayment schedule.

LONDON INTERBANK OFFERED RATE (LIBOR)

The London Interbank Offered Rate for deposits, such as the six-month dollar LIBOR or six-month Deutschemark LIBOR. This rate is conveniently used to measure the approximate cost to banks of funds which they obtain in the interbank markets, and it is commonly the based on which their lending margins are fixed. Thus, an original loan agreement or a rescheduling agreement may stipulate the interest rate to the borrower at LIBOR dollar six-month plus 1.5 percent, adjusted semi-annually for changes in the LIBOR rare. See also variable interest rate.

LONDON CLUB:

An informal grouping of commercial banks who meet to determine a common approach to rescheduling commercial bank debt to a country. although the term is in common use, no organizational framework or secretariat for commercial bank debt restructuring comparable tot eh Paris Club for official debt exists.

LONG-TERM EXTERNAL DEBT:

Debt that has an original or extended maturity of more than one year.

MATURITY:

The debt service amounts to be paid on a particular date. Final maturity date is the date of the last payment due to the loan. Maturity period is sometimes sued to denote the entire period over which principal repayments are being made for the loan. See also grace period.

MORATORIUM INTEREST:

The rate of interest charged on rescheduled debt. In the Paris Club, it is negotiated bilaterally by the borrowing country with each individual creditor and therefore, differs to the next. In the London Club, were all creditors are deemed to have access to funds at comparable rate , the moratorium interest rate applies equally to all rescheduled obligations under a given agreement.

NEW MONEY:

The term used for additional commitments made by commercial banks to the borrowing country to supplement debt relief. The Paris Club has made it a principle not to provided new money to troubled debtor countries but, has, instead, rescheduled interest as well as principal, unlike the commercial banks which with rare exception, reschedule principal only. In a few cases, Paris Club creditors have provided new financing, but has been done at special pledging sessions outside the framework of the debt renegotiations.

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OFFICIAL CREDITORS

International organization, regional development banks and inter-government agencies, governments and their agencies (including central banks), loans from autonomous bodies and direct loans from official export credit agencies.

PARIS CLUB:

This is forum in which relief been provided since 1956 by the governments belonging to the Development Assistance committee of the organization for Economic Cooperation and Development. participation in the Club is open to any official creditor that which to take part. The chairman of the Club and its small secretariat are provided by the French Treasury, which also arranges the venue for its meetings in Paris.

POLITICAL RISK.

The risk of actions by the government of the borrowing country that prevent, or delay, repayment.

PRINCIPAL REPAYMENTS

The payments which are made against the drawn and outstanding amount of the loan. That is the repayment of drawn amounts as opposed to service payments.

CHAPTER ONE

1.0 INTRODUCTION

1.1 GENERAL INTRODUCTION

Over the last few years many developing countries have faced acute external debt servicing problems. The reasons for this are varied. In some cases debt problems have mainly stemmed from the inefficient use and control of borrowed funds by debtor countries. In some cases returns on investments have not even covered debt servicing costs, while in others an inadequate policy frame work for debt management has lead to an accumulation of external debt that has proved excessive for the countries debt servicing capacity.

Nigeria has fallen into the category of "Debt Servicing" Nations in crises over the last few years; and especially since the onset of the Debt Crises in 1982.

Debt difficulties have been caused by international developments in interest rates, terms of trade and trade policies have often been adverse and unexpected; As a result there has been a much higher than anticipated growth in debt servicing. Furthermore difficulties have arisen out of reversals in the supply of external finance as banks' portfolio constraints have been compounded by the debt-servicing difficulties faced by the borrowers.

Adequate debt management is very essential if a country is to use external resources efficiently in ever increasingly complex financial environment.

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For an effective debt management, institutional framework to control and monitor external indebtedness as well as internal usage has to be well conceived. With rising burden and greater complexity of debt has been arisen; there is placed a greater onus on the authorities. The Nigerian government though the Central Bank of Nigeria and the Federal Ministry of Finance –to manage the external indebtedness through appropriate macro economic policies; including fiscal policies. Typically however, those statistical information and centralized control over external borrowing which should for the bases for policy are lacking. The medium term borrowing plan or the overall balance of payments targets are not adhered to. When an effective debt management undermines a countries ability to continue to raise new external finance by leading to late or part payment; the result can be costly. It may for instance cause a compression of imports and a lower rate of economic growth than had been planned on the assumption that external finance would be available. Furthermore, when problems of maintaining debt-service payments forces a country to seek rescheduling of its debts; Also very costly both in term of additional fees and in the use of scarce domestic management resources that the arrangements pre-empt.

Finally, the effects of a debt rescheduling or even of difficulties in making payments can be pervasive and painful.

Once a country's credit worthiness is in question, it may take some time to re-establish it's name in international markets; in the meantime it will face higher borrowing costs and more limited access to external funds.
At this points, Nigeria is faced with all the aforementioned problems.

1.2 STATEMENT OF THE PROBLEMS

To really appreciate the Nigerian debt problem, one has to look at it form various perspectives such as, the Nigerian Financial system, the Monetary policies adopted; and the method and style of the external reserve management employed by the Central Bank of Nigeria.

The debt problem as is being faced by Nigeria at the moment is critical; as it affects every facet of the Nigerian citizenry. The question as to how and when do the debt burden arise as well as the magnitude shall be paramount.

One of the principal functions of the Central Bank of Nigeria is to formulate and execute monetary policy, to promote monetary stability and a sound financial system in Nigeria. The Central Bank of Nigeria carries out this responsibility on behalf of the Federal Government of Nigeria through a process outlines in the Central Bank of Nigeria Decree 24 of 1991 and the banks and other Financial Institutions Decree 25 of 1991. In general, monetary policy refers to the combination of mesa rues designed to regulate the value, supply ad cost of money in the economy, in consonance with the level of economic

activity. An excess demand for goods and services will cause rising prices and/or a deterioration of the Balance of payments position. On the other hand, an in adequate supply of money could include stagnation in the economy and thereby retard growth and development.

The problem as this paper will view is the fact that the Central Bank or the Central Monetary Authority must attempt to keep the money supply growing at an appropriate rate to ensure sustainable economic growth and maintain internal and external stability. Numerous factors have contributed to the increased size and increasing quantrim of Nigerians public debt; which by the end of 1993 was well over ₦750 billion. The main factors include the rapid growth of public expenditure; particularly for capital projects borrowing from the international community at non earnings interest rates; the continuous decline in oil earning from the late 1970's and the emergence of trade arrears.

The Nigerian debt problem-A problem which needs to be faced very squarely; for the purpose of this wire up can be generalized under the following headings:

- Huge budget Deficits
- Heavy Dependence on oil revenues
- Trade debt
- Balance of payments support loans
- Short term loans for long term projects
- Reckless contraction of loans
- Poor performance on Non-oil export

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It is with the above stated factors in mind that the every increasing Nigeria Debt problem shall be looked at critically.

1.3 OBJECTIVES OF THE STUDY

The Nigerian economy and by extension the Nigerian populace has seen and felt a lot of differences in the last few decades. This has been caused by various reasons ranging from social problems to political and economic upheavals. The Nigerian debt problem is just one of those major factor which forms the core of the problems; as such this paper will attempt to tackle the question of the debt issue.

They key objective of this study is to re look at the ways and means in which Nigeria manages it's external debt. Questions like-are we on the right track?; or where and what have gone wrong? shall be looked at.

1.4 SIGNIFICANCE OF STUDY

Nigeria being a member of the international community has to look inwards and outward in terms of its debt burden. It has bilateral and multilateral relations with other countries and organizations. Which necessities the exchange of goods and services. External reserves are normally kept and should be carefully managed to facilitate such business and diplomatic transactions. More importantly. The management of the reserves affects the

performance of the Nations economy through its influence on the conduct of monetary policy.

This study of the Nigerian debt problem has immense significance considering that directly and indirectly, if affects all facts of the Nigerian economic growth and the various macro economic polices that are invariable imported. To really appreciate the significance of this study; one has to look seriously the various ways and means in which Nigeria manages its public debt. It is also hoped that by this study, certain methods not thought of a ideas towards improving existing ways of implementing policies will surface. This paper along the way will try and analyze the trend of the external and public debt as incurred by Nigeria such elements as the balance of payments s will be developed on. It is significant for example to note that in the early 80's Nigeria external debt stood at about $13 billion; and the debt services ratio then was about 11% while the debt export ratio was on at a round 100%. However by the early 90's the external debt had risen to about $33 billion, the debt service ratio to 30% while the debt export ratio to 400%.

The study will also show us the sources and structure of the debt, causes of Nigeria debt problem and the various strategies for managing the debt. The paper will deliver in detail into Nigeria external debt management taking a look at previous studies, existing set up's and glimpse at similar areas with the same problem or at least had some similar problem. It is hoped that this study

will be quite significant in terms of addressing the problem and coming out with plausible solutions.

1.5 SCOPE AND LIMITATIONS OF STUDY

The main body of this research work will duel on the Nigerian Debt problem, probable causes and effects. However in trying to achieve at reasonable answers , the issue of the Nigerian external debt management will be looked at critically. This will be attempted considering those periods from when Nigeria had debts that were not a cause for serious alarm up to and beyond when the debt problem actually became a crises and the credit worthiness of the country had a question mark. The period of coverage will range from 1980 to 1994.

With such a study as the Nigerian debt problem, especially having gone down quite deep, one of the major limitation will come in the form of the length of time to get back on the right tack even if different and workable strategies are adopted to solve or at least minimize the problem to a great extent. It will take some time and consistent implementation of policy measures before the full impact of debt management can be evaluated. Most of the expected effects, particularly with expenditure policies are of medium to long in nature, and world therefore require much time before a complete evaluation can be undertaken. Also, it is quite difficult to isolate our public debts and external debts; though as a package they form the quantum of the Nigeria debt problem.

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1.6 ASSUMPTIONS

One of the many functions of a central Bank is to serve as banker to the government. In doing this, it keeps the finances and accounts of the Government. It is also involved in raised or borrowed becomes a debt owned by the Government. This debt is referred to as public debt. It is all monies owed by Government to Institutions, Government and other bodies either resident in or outside Nigeria.

The Central Bank of Nigeria (CBN) in conjunction with the Federal Ministry of Finance (FMF), manages the Nations public debt.

In the light of the above, the CBN will be the pivot around which the Nigeria debt problem will be looked at. For the purpose of this study, it will assumed that the Central Bank of Nigeria will be representative of the Nigerian debt problem, and a measure of its performance shall be a guiding factors to possible solutions.

1.7 RESEARCH QUESTIONS

This paper will seek answers for the following questions; How credit worthy is the Country? what is the effectiveness ratio in terms of our debt management? How does the level of Development, the utilization of resources and the direction of the economy relates? Are our balance of payment supports and level of foreign investment in order? In other-words, we could go further and ask; which generation bears the debt burden?

CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 MONETARY POLICY FRAME WORK IN NIGERIA

2.1.1 CBN INSTRUMENTS OF MONETARY POLICIES

One of the principal functions of the Central bank of Nigeria (CBN) is to formulate and execute monetary policy to prompt monetary stability and a sound financial system in Nigeria. In formulating and executing monetary policy, the Government of the CBN is required to make proposals tot eh president of the Federal republic of Nigeria who has the power to accept or amend such proposals. Thereafter, the CBN is obliged to implement the monetary policy approved by the president.

Monetary policy in itself refers to the combination of measures designed to regulate the value, supply and cost of economy; in consonance with the level of economic activity. An excess supply of money which invariable results in an excess demand for goods and services will cause rising prices and/or a deterioration of the balance of payments position. On the other hand, an adequate supply of money could induce stagnation in the economy and thereby retard growth and development. consequently the Central Bank or the Central Monetary Authority must attempt to keep the money supply growing at an appropriate rate to ensure sustainable economic growth and to maintain internal and external stability.

With the above in mind, the discretionary control of the money stock by the Central Monetary influencing interest rates to make money cheaper or more expensive depending on the prevailing economic conditions, and the channeling of money to priority sectors. In short, the aims of monetary policy are basically to control inflation, maintain a healthy balance of payments position for the country and promote an adequate and sustainable level of economic growth and development.

2.1.1 TECHNIQUES OF MONETARY POLICY-DIRECT OR PORTFOLIO CONTROL APPROACH

The main distribution in the direct portfolio control instruments is that is places restrictions on a particular group of institutions (especially deposit banks) by limiting their freedom to acquire assets and liabilities. The monetary and authority uses some criteria to determine monetary and credit targets, and interest rate which are the intermediate targets to attempt to achieve the ultimate objectives of policy. This method is employed mainly in developing economics in which the financial infrastructure necessary for operating indirect monetary control is absent or underdeveloped.

INDIRECT OR MARKET INTERVENTION CONTROL APPROACH

The indirect approach to monetary policy relies on the monetary authority as a dealer in the financial markets to influences the availability and the rate of return on financial assets, thus affecting both the desire of the public to hold

money balances and the willingness of financial agents to accept deposits and lead them to users. Such instruments for indirect control include reserve requirement, discount rate and open market operations.

2.1.2 ADMINISTRATION OF MONETARY POLICY

A memorandum tagged the "monetary and credit policy proposals" usually prepared for a particular fiscal year. Input is gotten from all the policy departments of the CBN and is coordinated by the research department. The memorandum takes into account the views and suggestions of financial system operations, the business community and other interested members of the public. It considers the prevailing economic conditions, prospects and the policy objectives that appear most appropriate to purse in the immediate future.

The sequence of action is such that the memorandum is initially considered by the committee of Governors, the highest management body for the day to day administration of the CBN. After discussions, amendments if any, and approval by the CBN Board of Directors; it is then transmitted by the CBN Governor to the President for consideration and approval. After consultation with other organs of Governments, a decision is taken on which proposals to accept and that goes into the budget for the year. At this juncture, the adopted policy is outline for banks and other financial institutions (BOFI) by the CBN, while fundamental changes must be discussed with the president.

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2.1.3 MONETARY POLICY BEFORE S.A.P

The Structural Adjustment Programme (SAP) introduced in 1986 is a turning point in the economic environment of Nigeria. The monetary policy in the Pre-SAP era which could be termed the period of boom and burst was characterized by the growing importance of the one sector, the expanding role of the public sector in the economy and over dependence on the external sector. In the Pre-SAP setting the main objectives of monetary policy were the maintenance of relative price stability and a healthy balance of payment position. Monetary management depended on the use of direct monetary instruments. The use of market- based instruments was not feasible because of the narrowness and underdeveloped nature of the financial markets, the inadequate supply of the relevant debt instruments and the deliberate restraint on interest rates. Then the most popular instrument of monetary policy was the issuance of credit rationing guidelines. This was done mainly to stimulate the productive sectors and thereby stem inflationary pressures.

From the mid-1970's it became increasingly difficult to achieve the aims of monetary policy. Generally, monetary aggregates, Government fiscal deficit, GDP growth Rate, inflation rate and the balance of payments position moved in undesirable directions. The major sources of problems in monetary management were the nature of the monetary control framework, the interest rate regime and unharmonised fiscal and monetary policies. The rigidly controlled interest rate regime and especially the low level of various rate helped to encourage

monetary expansion while not promoting the rapid growth of the money and capital markets. The low interest rates on Government debt instruments did not sufficiently attract private sector savers, and sine the CNB was required by law to absorb the unsubscribe portion of Government debt instruments, large amounts of high-powered money were usually injected into the economy.

In the oil boom era, the monetization of foreign exchange resulted in large increases in Governments expenditure, which caused monetary instability; thus the beginning of the Nigerian debt problem. In the early 1980's when the oil receipts were not adequate to meet new levels of demand and sine expenditures were not rationalized, Government resorted to heavy borrowing both internally and externally.

2.1.4 MONETARY POLICY UNDER S.A.P

With the crash in the international oil market of 1986 and the resultant deteriorating economic conditions in the country, the structural adjustment programme (SAP) was adopted. It was designed to achieve fiscal balance and balance of payments. Viability by altering and restructuring the production and consumption patterns of the economy; eliminating price distributions, reducing the heavy dependence on crude oil exports and consumer goods imports, enhancing the non-oil export base and achieving sustainable growth. The main strategies of the programme were the deregulation of external trade and payments arrangements; the adoption of a market-determined exchange s rate

for the Naira; substantial reduction in complex price and administrative controls and more reliance on market forces as a major determinant of economic activity.

The stimulation of our put and employment and the promotion of domestic and external stability which from inception has been the key objectives of SAP still remained, with the monetary policy now aimed at including the emergencies of a market-oriented financial system for effective mobilization of financial savings and efficient resources allocation. In order to reduce the observed excess liquidity in the economy in 1980's measures such as reduction in credit growth by banks; special deposit requirement against outstanding external payments arrears, abolition of foreign guarantees/currency deposits as collaterals for Naira loans and the withdrawal of public sector deposits from the banks and their consolidation at the Central Bank of Nigeria, were introduced. In addition insurance of stabilization securities to banks was re-introduced in 1990 as a tool for reducing the excess liquidity in the system. Furthermore as a way of inducing a market-oriented financial system and generally improving it's efficiency, the sectoral credit guidelines were revised to give banks a good measure of flexibility in their credit operations.

Despite the monetary policy reforms introduced at the inception of the SAP, some of the problems of monetary management have persisted. The main constraints were the ineffective control framework and the uncertainty created by fiscal operations. In 1001, the cash reserve requirement was modified such

that its base was expanded to include all deposit liabilities comprising demand, savings and time deposits. The monetary authorities have sought to strength the banking system for effective monetary management.

Two important developments took place in 1991, firstly in the budget the Federal Government made a formal pronouncement of the intended shift towards the techniques of indirect monetary control, secondly the Federal Government promulgated the Central Bank of Nigeria Decree (BOFID), No 25 of 1991, to replace the CBN act of 1958; respectively. Under the Central bank of Nigeria decree, the Bank's s powers in the design and conduct of monetary policy were significantly enhanced, while the BOFID addressed the problems of loopholes in monetary management by bringing the non-bank financial intermediaries under the supervisory control of the Central bank of Nigeria.

2.1.5 THE EMERGING POLICY AND IMPLEMENTATION MODALITIES

With the financial sector reforms undertaken since 1986 and the introduction of indirect monetary control technique in 1991, there is clear evidence that monetary policy in Nigeria is moving gradually in terms of design and implementation toward a more market-based system. The technique is essentially but not limited to the control of money stock through a manipulation of the monetary base. The monetary base is the sum of total bank reserves and currency in the hand of non-bank public.

The introduction of an indirect monetary control frame work has several policy implications for the country and these have elicited some actions on the part of the monetary authorities in the past few year.

Firstly the banking system has to be rid of excess liquidity which has been injected into the economy especially since 1988. to achieve this the CBN has continued to issue stabilization securities to banks since 1990. Secondly, there is need for greater harmonization of fiscal and monetary policies. Under a system that relies on the manipulation of the monetary base, uncontrolled borrowing by Government from the Central Bank of Nigeria will distort the base and money stock. The main implication is to review the whole system of public finance which has assumed greater dimensions under the SAP. Thirdly, where competition among banks essential, as liquid banks is undesirable. Fourthly, leakages in the control system have to be minimized, hence the need to monitor all financial operations. Lastly, for open market operations to be effective, the money market must be further developed, and timely data are required under a regime of indirect monetary control so that the CBN can intervene to stabilize the financial markets as desirable.

In conclusion of the complex issues involved in the introduction of the new techniques of monetary management , the CBN decided to adopt a phases implementation approach. Starting from September 1, 1992, the CBN removed the credit ceiling for any bank that meets following criteria on a continuous

basis; Specified cash Reserve and Liquidity Ratio; Adherence to the prudential goodie lines; the statutory minimum paid up Capital Requirement and Capital adequacy Ratio, as well as s sound management.

In 1993, the CBN outlined some elements of the monetary Policy Framework, with particular emphasis on the conduct of open market operations (OMO) and the use of other supporting instruments, the promotion and development of the money market and the role of macroeconomic indicators such as interest and exchange rates. The CBN is to conduct OMO using all the three existing Government Securities (Treasury Bills and Certificates and Development Stock). With the introduction of OME, the use of stabilization securities will be gradually phased out and applied only as a fall back position and on selective basis to augment other instruments.

In March 1993, first securities Discount House Became the first discount house to being operations in the country; in line with CBN encouragement of in the operation of licensed discount houses; which in turn will directly and promote the growth and efficiency of the money market and enhance the administration of indirect instruments of monetary policy; including:-

i. Primary and Secondary market dealership in treasury instruments
ii. Provision of discounting and rediscounting facilities to other market operations and
iii. Accepting deposits of short term and overnight loans.

Policy measures are to be adopted to improve the money market which will reverse the current inverted yield curve in the market. The CBN and Ministry of Finance are to make conscious efforts to align macroeconomic policy measures with a view to sustaining exchange rate stability. Consequently, the use of OMO supported by other liquidity control measures will be combined with few operations within a liberalized inter-bank market in which CBN will only intervene to buy or sell foreign exchange rate policy.

On 30th June 1993 OMO took off with a 250 Million offer which was 80.81 percent over-subscribed. The bid rates ranged from 23 to 34.0 percent while the Banks discount rate was 25.5 percent.

Roles were traditionally felt mostly in the area of public utilities where competition was s thought to be wasteful, and to prevent the abuse of monopolistic power, their regulations became more or less institutionalized over time. Government controls of economic activities have grown and extended beyond these and now embrace diversed controls on both the domestic and external sectors of the economy.

2.2.0 FISCAL MANAGEMENT AND EXTERNAL DEBT PROBLEMS

2.2.1 Causes of Fiscal Deficits

It is difficult today to find a country, whether developed or developing, without a substantial fiscal deficit, in may of these countries too, the deficit has become immune to the effects of business and economic cycles and does not disappear when economic conditions turn around and improve.

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Fiscal deterioration almost always arise as a result of multiple causes but in each situation one is likely to prevail. Four major causes of deficits in developing countries cane be identified and these deficits have to be financed by borrowing, in most cases external. These causes are:

a. Windfall tax revenues tended to be used for consumption expenditures instead of investment. Several developing countries have economics and tax systems that are highly dependent on the export of one or a few commodities. When the prices of these commodities rise, so do fiscal resources. In many cases, these temporary increases in fiscal resources were not used, as they should have been to reduce deficits or to pay off past debts by running surpluses; instead, because of political pressures, Government used them to increase public spending. When commodity prices fall, these Government found themselves committed to level of public spending that could no longer be sustained with the available and lower ordinary revenues.

b. A second causes of deficits arose out of the tax system, which in many countries has characteristics that make tax revenues in elastic with respect to prices such that they do not automatically a just to price changes. Consequently, exogenous inflationary shocks, regardless of their origin, tend to reduce the ration of taxes to Gross

National Product (GNP) remains unchanged, the inevitable result is a fiscal deficit.

c. The growth of public expenditure, generated either by over ambitions capital projects or by pressures to increase wages, pensions or subsides constitutes a third major cause of fiscal disequilibrium. In some cases, this increase in public spending originated in the activities of public enterprises rather than the central Government. A study by the International monetary Fund about a decade ago revealed that public enterprises in a sample of 25 developing countries accounted for three fourth of the deficits of their central Government in the 1970's Public Enterprises have played a major role in the accumulation of foreign debt in many counties. It is significant to mention that excessive public expenditure on capital projects has consistently proven easier to curtail than spending on wages or pensions presumably because Government do not have legislated or political commitments to capital expenditure.

d. Finally, in many countries fiscal disequilibrium was created by the inability of Government to accept the economic consequences of lower real income associated with worsening terms of trade. For instance, Government of many oil importing countries did not pursue policies aimed at reducing domestic consumption when the share increases in the price of oil in the mid and late 1970's reduced real national income.

2.2.2 Financing Of Fiscal Deficits

Regardless of their origin, fiscal deficits must be financed. These fiscal deficits tend to have a direct connection to the accumulation of foreign debt for two important reason. Firstly, for several years, Foreign borrowing had a lower political and economic cost to Government than domestic financing. Secondly, even without political preferences for foreign borrowing there are relatively narrow limits to the amount of a fiscal that can be met domestically.

2.2.3 Sources of financing

If Government behaved like the national individuals of economic textbooks, each available sources of financing would be used up to the point where the marginal cost of borrowing (a cost that can be economic political) were equal to the marginal benefit from the public spending associated with the borrowing. Economic theory also states that:-

a. The social marginal costs are across all borrowing sources and the social marginal benefits across all expenditure should be equalized; and

b. at the margin the social cost of the last currency raised should be equal to the social marginal benefit of the last currency unit spent. However, the real world is unlikely to follow these theoretical prescriptions. A more realistic interpretation of reality is that once fiscal deficits appear, they are financed from whatever sources are

readily available, as long as these are not to costly, politically or economically. These sources nay be domestic or foreign and may or may not have inflationary consequences.

Often, the first sources used to finance deficits by developing countries is external. This was in the past readily available to countries with a small total foreign debt that were just entering a process of fiscal deterioration and at least at the beginning, this sources had low political and economic costs. Governments started to depend on other sources of financing only after they had exhausted foreign sources of financing that ranged from grants to commercial credits. Foreign reserves seem to have been the next sources of financing utilized. In fact countries have been known to borrow to maintain or even to increases their levels of reserves. The next sources turned to were domestic – non bank credit, domestic arrears, and inflationary finance. These various sources of financing are discussed below.

2.2.4 Foreign Financing Of Fiscal Deficits

Few developing countries follow the decision making process of industrial countries whereby the government first decides on its desired level of public expenditure, then forecasts its ordinary revenue (mostly taxes) and finally faces the question of how to finance the resulting deficits. In developing countries, determining expenditure levels and finding financing sources are likely to be simultaneous exercises in which the availability of financing often determine

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2.2.5 Concessionary Loans:

The next most attractive sources of finance for fiscal deficits is by way of concessionary loans. Such loans are those that carry a lower-than-market rate of interest, or have a substantial grace period and usually have a long maturity: These loans may be made by Government or by international institutions such as the International Bank for Reconstruction and Development (IBRD) and the African Development Bank (ADB). Often, concessional loans are tied to project and as such are likely to entail domestic counterpart expenditure. To the extent that these loans are an integral part of a country's foreign debt, they reduce the burden that would have been associated with the same debt on commercial terms given that the present value of the (discounted) servicing cost is less than the loan (the discount rate being the rate that would have been paid on a normal commercial loan. However, availability of these loans tend to encourage the borrowing country to borrow more, and to engage in capital spending with lower productivity, than it would have otherwise.

Commercial Loans

The next most attractive source of raising funds for financing fiscal disequilibrium are commercial loans. These are usually obtained from commercial banks, foreign suppliers or foreign Government. Their maturities may range from a few months to over a decade and their costs are higher and more variable which introduced an elements of uncertainty tot eh future debt burden.

But as the painful experience of recent years indicates, a country may suddenly find itself cut off from this source just when its need for foreign financing is greatest. Such financing would then become available only when the borrowing Government takes strong economic adjustment measures under an IMF- supported programme. There are a few considerations related to risk assessments by commercial lenders that are worth mentioning. First as overall exposure of commercial banks increases and especially when there is concern over international financial stability, the cost of private loans to any country will rise. Second, given the international financial situation, the marginal cost of borrowing for a particular country, as well as the level of borrowing that it will be able to make, will, ceteros paribus, be related to various indicators of the size of its total foreign debt. As the share of debt service in export earning of the country raise, so will the countries marginal cost of borrowing. Third, the share of short-term debt (of say, less then a year) in total debt is crucially important. The "country risk assessment system" or "country exposure guidelines" may put a cap on medium-term and long-term lending, but they may be more flexible vis-à-vis short-term lending. Unfortunately, some countries have tired to maintain a high level of investment expenditure, which could increases output and exports only over the long run, by short term loans. This strategy has often resulted in serious fiscal and financial crises.

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effect, the foreign bank or supplier is forced to extend a loan to the country equal to the interest or the payment due.

2.2.7 Domestic Financing Of Fiscal Deficits

If countries did not have access to foreign sources, fiscal deficits would exist only if they could be domestically financed. This domestic financing could be of various forms, each with different economic and political costs. A useful distinction is one between borrowing from the non-bank public and from within the banking system.

Borrowing From The Public

Borrowing from the public usually means selling bounds to individuals and/or institutions who have the option of buying or not buying them. In financing deficits this way, the government must make the bonds attractive s enough to induce investors to buy them. In this cases, it is often required that the bond prices must come done and interest rates go up, which in turn may attract foreign capital. Where exchange rates are flexible, this may lead to an appreciation of the exchange rate and have an offsetting effect on the trade account. The larger the deficit and sale of hands, the greater should be the interest rate increases.

In developing countries where the capital markets are small and there is a limit to the amount of deficit that could be financed in this way, the potential for utilization of this option is small. In reality with few exceptions, bond

financing is of little use? And often an insignificant sources of fiscal finance in developing countries.

While the scope for financing a fiscal deficit through the voluntary placement of bonds in the market is limited in developing countries, an alternative exists that is often of greater significance; the sale of bounds to captive buyers. In a large number of development countries many institutions and occasionally even some individuals such as public sector employees are required to invest in public bonds. Social security institutions for instance, pension funds, and public as well as private enterprises are often required by law to buy government bonds.

Borrowing from the public is not limited to the free or compulsory sale of bonds. Another important sources is arrears, vis-à-vis domestic supplier of goods and services, vis-à-vis those who carry out capital projects, vis-à-vis public employees in the form of delayed payment of wages, vis-à-vis tax payers in the form of delays in the payment of tax rebates or? refunds , and so on.

The domestic sources of fiscal disequilibrium financing discussed above are not directly inflationary and to the extern that they reduce foreign borrowing by the government, they reduce the growth of the country's external debt. Thus a country that relies on these domestic sources is les likely to face external

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debt problems. Borrowing from the banking system, however, presents more complex issues.

2.2.8 Borrowing From The Banking System

Although borrowing from the banking system may not necessarily mean borrowing from the central bank considering the government can borrow independently from domestic commercial banks, in practice this distinction is academic since the monetary authorities often accommodate public sector borrowing by increasing the reserves of commercial banks. The distinction becomes important when there is a limit to total credit expansion and commercial banks are required to lend to the public sector. Then the net result is the same whether the government borrows directly from the central bank or indirectly from the commercial banks while the central bank increases their lending capacity. In both cases, there is an increases in the money supply. The question now are that how much can a fiscal deficit be financed by monetary expansion and what are the consequences of such financing.

The existence of high debt, whether domestic or external, created largely to finance past fiscal deficits presents policy makers with serious difficulties for the conduct of fiscal and monetary policies. As concluded by Vito Satanzi (1984) financing this debt adds to the other pressures for public spending and thus increase the likelihood that a country will continue running large fiscal deficits. To the effect that part of the debt is external, or that it generates

inflationary pressure; there will also be effects on the balance of payment. He went on to add that given slow economic growth and high real interest rates, a country that does not take drastic measures to reduce its fiscal deficit in order to stabilize the ratio of its debt to GDP will almost automatically find itself facing an increasing debt problems.

Debt obligations can be eased temporarily by rescheduling. However, the time bought through this rescheduling must be used to make adjustment which are both raising revenues and cutting spending.

2.3.0 INSTITUTIONAL STRUCTURE FOR EXTERNAL DEBT MANAGEMENT

2.3.1 Management of Foreign Debt.

The theory of debt management is very simple. Developing countries resort to foreign finances to foster internal growth and to increase the resources available for investment before seeking and receiving foreign funds. Plans must be made on how to repay them and the limits such debt will impose on future economic policy must be considered. Investment projects financed with foreign debt should yield enough foreign exchange to cover the servicing of the debt. Theoretically therefore, debt management involves knowing the level of the debt, keeping it within desired limits, and obtaining the best available terms for it. In reality, debt management is very different. According to De la Dehesa (1984), public foreign debt in developing countries has been

1. First there are a few countries without exchange controls; any institution or citizen is free to sell foreign debt instruments, and pay interest and principal. In these countries, only a statistical export control exists through the information that banks provide periodically to the central bank or monetary authorities. Germany, Kuwait, the United Kingdom and the United States of America are examples.

2. In a second ground of countries, all foreign borrowing is free, but the central bank or monetary authority must be notified ex-ante, to allow direct statistical control of the value of the foreign debt. An example is the Netherlands.

3. In a third group, the largest, some authorization is required whether for private or for public debt, or both. Some countries also treat non bank and s bank borrowing s differently.

Although both public and private debt need prior approval in most countries they are usually subject to different institutional treatment, public debt being controlled more than private.

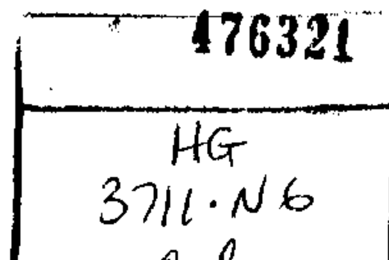
Public debt is usually approved in advance by the ministry of finance, as in Brazil, Mexico and Nigeria. In other countries, the Ministry of Finance has delegated the approval to the Central Bank as in Argentina, Denmark and New Zealand. Finally, there are some countries, where foreign borrowing is

approved by a joint committee of the Ministry of Finance and the Central Bank as in Bolivia, Peru and Spain. This group comprises mainly Spanish speaking countries.

As regards to private debt, no prior approval is required in some countries. Only ex-post registration with the Central Bank of Ministry of finance is needed. Argentina, Denmark and Canada belong to this category. Dehesa found it striking that some of the heavily indebted countries have a liberal stance on private borrowing. However in most countries, private debt was found to be subject to approval by Central Bank. Only in a few countries is a distinction made between commercial and pure financial debt, the former being approved by the ministry of commerce. Brazil, Japan and Spain share this peculiarity; the reason being that the regulation of import financing can be a way of imposing a non tariff protection, consequently as instrument of trade policy.

In some countries, limits are placed on private foreign borrowing above which the approval oft eh ministry of finance of the central bank must be sought. Countries in this category are Bolivia, Columbia and Sweden.

Certain terms are sometimes imposed on private borrowing in some countries to stretch maturities as much as possible. For instance, in Brazil, no-financial borrowing is allowed with maturities shorter than eight years while in Sweden the minimum maturity is two years.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In most countries, commitments and disbursements as well as payment of interest and repayments of principal come under the control of the central bank. While the Ministry of Finance provide the main criteria and regulations for foreign borrowing, the real management and control for the debt is delegated to the central bank.

De La Dehesa also found that central Banks, in most countries, have a statistical unit for foreign debt. This is a vital factor in foreign debt management in that it is almost impossible to manage something whose dimensions are not known with a certain degree of accuracy.

2.3.3 Institutional Priorities

In his study of institutional structures for external debt management, De La Dehesa commented on some institutional priorities which are highlighted below.

a. The first institutional priority for foreign debt management is the statistical unit. This unit would have to depend on the strength and organization of exchange control regulations. The difficulties of some developing countries in ascertaining the extent, level and characteristics of their foreign debt are well known. Where there is an absence of exchange controls, there will be a lack of statistical control. Nigeria for instance ahs introduced a sophisticated registration system to obtain

information on its debt for statistical control. Resident borrowers are required to register their borrowings with the Ministry of Finance and foreign lenders had to register loans with a given non resident bank in London. "The simplest way to have a good statistical record is to oblige to make all their foreign transactions through authorized banks."

b. The second most important institutional priority is to have a control unit for debt service and for foreign debt commitments and disbursements. A vital factor in debt management is to be able to meet annual debt service obligations. Thus the main priority is to establish through balance of payments forecasting, the sustainable level of the foreign debt-servicing burden and then to incur the foreign borrowing appropriate to that level. the control unit must have a global picture of the evolution and movement of external debt and its service to be able to make efficient debt management decisions. If for instance the unit becomes aware of a dangerous short-run accumulation of debt servicing, it must be able to make prompt decisions to effect it-by delaying public sector commitments, slowing down private sector approvals or regulating short-term borrowing in an effort to increases average maturities. Central Banks are most suited to fulfill the tasks of the debt control unit and also the statistical unit as the two are so interrelated that they should not be located in different institutions.

c. A third institutional priority is an advisory unit which can assist in the active management of external debt. This consists of daily analysis of

the foreign markers and study of future options. Such an advisory unit should be able tot advise both the government and the public sector on the best available borrowing opportunities in the markets and to inform the control unit and approval committee, if one exists, so that both the adequate terms of references for authorizing new borrowings.

d. A fourth priority, but one of lesser importance, it a foreign finance committee to provide general criteria for the approval and management of foreign debt in the light of the macroeconomic performance of the economy and the situation of the markets. Members of the committee should include high-ranking economic policy decision makers so that it ahs close connections with the decisions affecting monetary and fiscal policy. It should meet as often as possible to keep up with the dynamic nature of foreign capital markets and macroeconomic performance.

In recent years, there has been increasing government intervention in foreign debt management due to serious problems of solvency and liquidity in many developing and developed countries. In some cases, the institutional structure has become too complicated and cumbersome for flexible debt management. In his study, De La Dehesa concluded that foreign debt control should therefore, be as minimal and as flexible as possible. He opined that a debt management unit consisting of there small components preferably in the Central Bank covering the statistical, the control and the borrowing and advisory aspects of debt management is more then enough for foreign debt management in any

indebted country. he gave two reasons why the unit should be located in the central bank namely that is needs to be under a single direction that the central bank provides currency reserve management team that is in permanent contact with the markets.

2.4.0 Causes And Effects Of Inefficient Debt Management

2.4.1 Causes:

In a paper delivered by S.E. Omoruyi, Director of the Debt management Department of the Central bank of Nigeria at the symposium on the Liberia Monetary system and the challenges for reform on the 1970's held at Monrovai, Liberia (Omoruyi 1993), he deliberated on the causes and effects of inefficient management. The principal causes he outline was that third world countries reacted to the yearning for rapid economic growth and development in an environment characterized by wide savings and investment gaps by massive internal and external borrowing which was too often uncoordinated with various levels of government and parastatals within the country canvassing and acquiring loans independently from the international capital markers without prior approval of the central government. The end result was extensive external borrowing which were not in accordance with the respective governments debt policies and rules which determine sustainable levels of foreign borrowing and its effective utilization. Omoruyo went on to given other causes such as the lack of coordination among all agencies involved in debt management in a debtor country. This resulted in "kinks" in the

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information flows between the agencies leading to conflicting figures on national debt given by them Another causes, of importance, is a weak statistical base and inadequate computerization. An observed major characteristic of debt management systems in the Third World is that while debt statistics at aggregated levels are fairly available, data on loan-by-loan basis are hardly available for any meaningful projections and/or policy analysis. "The dearth of statistics, particularly on a disaggregated basis is perhaps the second most important factor besides the lack of technical expertise of debt managers, that has precluded rapid computerization of debt management in most debtor countries especially in sub-Saharan Africa".

The low level of computerization of debt management functions in the dace of huge magnitudes of public debt and the volume of international loans, trade transactions involved and unskilled debt managers has prevented the evolution of a strong data base, similarly, the monitoring of disbursements for purposes of control is made difficult. Weak monitoring has lad to the emergence of large volumes of loans that were contracted from non-concessional source and in some cases with the bunching of maturities. The cash flow problems inherent in such debt structures have endangered unsustainable debt service burdens in most debt-distressed economics.

2.4.2 Effects

Their broad effect of inefficient debt management according to Omoruyi" is the emergences of debt overhang and unsustainably high debt service burden". To service increasing interest and amortization liabilities, the state has to have the necessary foreign exchange available at its disposal. Thus scarce resources have to be transferred abroad to meet debt service payments and this reduces the availability of foreign exchange for use in the domestic economy. The resultant deficits (budgetary) in the wake of high debt service payments is financed largely through money creation, borrowing through ways and means advances from the Central Bank or through future external borrowings.

In the mid-term however, inflationary monetary and fiscal policies pose difficulties for foreign debt service as capital flight is encourage, adversely affecting domestic savings and ultimately leading to crowding out of private investors. In the same vein, an inflationary policy could reduce the debtor country's credit worthiness and thus inhibit the influx of foreign capital it greatly needs. consequently, in an effort to solve the budgetary problem of foreign debt by inflationary financing, there ensures a negative net transfer of resources and claims on the abroad, these claims have the effect of taxing future investment.

The debt crisis emanating from inefficient debt management will eventually compel debt-distressed country governments to undertake macroeconomic

restructuring aimed at eliciting relief from the creditors in order to achieve meaningful growth for the economy.

2.5.0 The Nigerian Public Debt

2.5.1 Sources Of Public Debt

one of the functions of the Central Bank of Nigeria is to serve as banker to the government. In fulfilling this function, it keeps the finances an accounts of the government. In this regards, it is also involved in raising finance from internal and external sources for the execution of government programmes. The money so raised becomes a debt owed by the government.

Public debt comes in various forms determined by the purposes for which the debt was contracted. The various forms public debt could take are:

a. **Trade Debt:** A trade debt arises with Nigeria trades with other countries and is unable to pay, either partly of wholly, for the goods and services supplied. For instance, Nigeria's inability to settle her import bills in the pest resulted in the accumulation of trade arrears which rose from #2.2 billion in 1982 to 34.4 billion in 1983.

b. **Balance of payments support loans:** The overall economic transactions between a country and the rest of the world, classified into current, capital accounts and official settlement balance, constitute the balance of payments position which may be favourable

when it is surplus or unfavourable when it is a deficit. Persistent unfavourable balance of payments often referred to as balance of payments disequilibrium may inform governments decisions to seek for a balance of payments support loan from one of the multilateral institutions such as the International Monetary Fund (IMF).

c. **Project-tied Loans:** Investments which have good potential and prospects so accelerate economic growth and development may lead government into contracting project-tied loans. As the name implies, such loans are for specific project and are cateris paribus, supported to be self liquidating.

d. **Loans for Socio-Economic Needs:** The provision of socio-economic need of the populace such as infrastructure, health, education and other social amenities may necessitate borrowing by the government to finance them.

Nigeria has contracted several debt obligations from both internal and external sources.

Internal sources of public debt are Central Bank, the commercial banks, the Merchant Banks and the non-bank public. The non-bank body includes Insurance companies, Saving Institutions, State and Local Government, Statutory board and Corporations and Individuals. These Debts are usually contracted through instruments such as Treasury bills, Treasury Certificates, Government Development stock, etc. The CBN has been underwriting the

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instruments on behalf of the Federal Government and taking up unsubscribe portions of the loans. However, with the introduction of the Open Operations, the situation is changing.

The external sources are the Paris Club of creditors representing official government creditors like the USA United Kingdom and France; the London Club of creditors representing commercial banks spread all over the world; the multilateral creditors such as the IMF, World Bank and African Development Bank. Promissory note holder are creditors in respect of refinanced debts. Others are bilateral and private sector creditors.

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2.5.2 Structure of Public Debt.

The components of public debt carry different maturity patterns such as short, medium and long-term. Short-term debts usually have maturity period of not more than one year. Medium-term debts carry maturity period of over one year while long-term debts have maturity period exceeding five years. This structure of the maturity pattern of public debt of a country usually determine the relative ease with which interest and principal payments are made. For domestic debt instruments treasury bills and certificates are issues to raise short-term loans with tenures at 90 days and 1 to 2 years, respectively. The development stocks and treasury bonds are long-term debts with maturities ranging from 5 to 25 years, with regard to external debts, promissory notes, debts owed to bilateral and multilateral agencies, Paris and London Clubs

restructuring agreements are medium to long-term in nature. Trade debts and supplier credits are essentially short-term debts. The structure of the Nigeria debt will be discussed in two part, Domestic and External Debt.

a. Domestic Debt: The origin of domestic debt dates back to 1946 when the first development stock of N600,000 was floated. The first treasury bill and s certificates worth N8 million and N20 million respectively, were issued in 1960 and 1968. Since then, Nigeria's domestic debt has grown very rapidly and reached N161.9 billion by the end of December (see Table 1 and 2). The

TABLE 1
DOMESTIC PUBLIC DEBT OF FEDERAL GOVERNMENT (₦ MILLION).

	1988 (1)	1989 (2)	1990 (3)	1991 (4)	1992 (5)	1989 (6)	1990 (7)	1991 (8)	1992 (9)	1989 (10)	1990 (11)	1991 (12)	1992 (13)
1. Composition of Debt													
i. Treasury Bills	35,476.0	34,126.0	25,476.0	57,763.1	103,317.5	4,350.0	8,650.0	32,287.1	45,554.4	3.8	25.3	126.7	78.9
ii. Treasury Bonds	-	11,350.0	20,000.0	20,000.0	20.000.00	11,350.0	8,650.0	0.0	0.0	-	76.2	0.0	0.0
iii.Treasury certificates	6,794.6	6,944.6	34,214.6	34,214.6	34,214.6	150.0	27,270.0	0.0	0.0	2.2	392.7	0.0	0.0
iv. Development stocks	4,759.0	4,401.0	4,401.0	3,961.0	3,961.0	130.0	228.0	180.0	260.0	2.7	4.9	4.1	6.2
v. Others	1.5	1.5	1.5	N/A	N/A	0.0	0.0	0.0	1.5	0.0	0.0	0.0	100.0
2. Holders													
(i) Banking System	35,578.7	42,160.1	65,837.2	96,939.0	140,950.4	6,581.4	23,677.1	31,101.8	44,011.4	18.5	56.2	47.2	45.4
a. Central Bank	27,682.7	38,391.3	56,564.1	89,412.6	134,406.6	10,708.6	18,172.8	32,848.5	44,994.3	38.7	47.3	58.1	50.3
b. Commercial Banks	7,714.5	3,670.6	8,917.3	6,847.0	5,535.1	4,043.9	5,246.7	2,070.3	1,311.9	52.4	142.9	23.2	19.2
c. Merchant Banks	181.5	98.2	355.8	679.4	1,008.4	83.3	257.6	323.6	329.0	45.9	262.3	90.9	48.4
(ii) Non-Bank Public	11,452.2	14,891.0	18,255.9	19,261.2	20,542.7	3.438.6	3,364.9	1,005.3	1,281.5	30.0	22.6	5.5	6.7
3. Total Debt Outstanding	47,031.1	57,051.1	84,093.1	116,200.2	10.020.0	10.020.0	27,042.0	32,107.1	45,292.9	21.3	47.4	38.2	39.0
Less Loans on-lent to state Govt. & Public Agencies	3,495.4	3,495.4	N/A	N/A	0.0	0.0	2,495.4	0.0	0.0	0.0	100.0		
Federal Govt. Domestic debt	43,535.7	53,555.7	84,093.1	116,300.2	161,403.1	10,030.0	30,532.4	33147.1					

increase in domestic debt reflected the rapid expression in development programmes and changes in the macroeconomic environment. Most domestic debts were raised through the issuance of treasury bills and certificates. As contained in CBN brief series No. 93/04 dated August 1993, the CBN constitute in largest holder of domestic debt instruments due mainly to its underwriting role.

b. **External Debt:** The origin of external debt dates back to 1958 when a sum of US $28 million was contracted for railway construction. During the period 1958-1977, Nigeria did not resort to much borrowing from external sources. Debts contracted during the period were the concessional types of from bilateral and multilateral sources with longer repayment and lower interest rates. They constituted about 78.5 per cent of the total debt stock.

From 1978 onwards, owing to the oil glut which exerted tremendous pressure on government finances, it became expedient to borrow for balance of payments support and project financing. This led to the promulgation of Decree No. 30 of 1978 which empowered the Federal Government to raise external loans up to a maximum of N5 billion. Consequently the major borrowing of US $1 billion, referred to as the jumbo loan was contracted from the International Capital Market (ICM) in 1978, increasing the total external debt stock to US $2.2 billion. Therefore, state Government joined s the fray contacting large external loan obligations. While the share of loans from

bilateral and multilateral loans declined substantially, borrowing from private sources at stiffer rates increased considerably. Consequently by 1982 the total external debt stock stood at US $13.1 billion. It rose further from US $28.3 billion in 1987 to US $33.1 billion in 1990 but declined to Us$27.6 billion at the end of December 1992. The Paris Club constitutes the highest sources with a share of 59.7 per cent in 1992. the balance is owned to the London Club, the multilateral creditors, promissory note holders and others (See tables 3,4 &5).

TABLE 3
EXTERNAL PUBLIC DEBT OUTSTANDING

	($ Million)				(N Million)			
Holders	1989 (1)	1990 (2)	1991 (3)	1992 (4)	1989 (5)	1990 (6)	1991 (7)	1992 (8)
1. Multilateral.............	2,807.00	3,845.1	4,016.0	4,518.0	21,473.5	34,578.4	39,058	89,274.3
2. Paris Club	15,847.0	17,172.1	17,793.0	14,680.0	121,229.6	154,540.7	173,051.2	349,351.5
3. London Club	5,600.0	3,936.8	5,988.0	2,120.0	42,480.0	52,749.6	58,238.1	41,890.6
4. Promissory Notes.....	4,584.0	4,550.0	4,479.0	3,246.0	35,067.6	40,950.4	43,561.9	64,140.0
5. Others	2,586.0	1,675.00	1,454.0	1,210.0	19,782.9	15,075.2	14,144.3	23,909.2

Sources: (1) Central Banks of Nigeria
(2) Federal Ministry of Finance

Converted at end period exchange rates which were N7.650/% 1.0, N9.000/$ 1.0 N 9.7258/$ 1.0 and N19,7597/$1.0 at the end of December 1989, 1990, 1991 and 1992, respectively.

TABLE 4

MATURITY STRUCTURE OF EXTERNAL DEBT OUTSTANDING

(₦ MILLION)

				Percentage of total		
Period	1990 (1)	1991 (2)	1992 (3)	1990 (4)	1991 (5)	1992 (6)
Short-term............	12,191.0	4,613.1	2,931.0	36.7	13.7	10.0
Long-term............	20,988.0	29,116.9	25,843.0	63.3	86.3	90.0
Total	33,179.0	33,730.0	28,774.0	100.00	100.0	100.0

Sources: (1) Federal Ministry of Finance

(2) Central Bank of Nigeria

TABLE 5
SOURCES OF EXTERNAL DEBTS
EXTERNAL DEBT SERVICE PAYMENTS
($ MILLION)

Holders	1991		1997	
	Budget Estimates (1)	Actual (2)	Budget Estimates (3)	Actual (4)
London Club	583.4	516.1	146.9	657.4
Paris Club	1,100.3	1,506.7	1,25.8	536.6
Multilateral	415.3	733.4	386.0	8.101
IBRD	-	689.9	-	-
EIB	-	16.5	-	-
ADB & Others	-	27.0	-	-
Promissory Notes	364.0	376.6	358.5	267.3
Others	508.9	502.2	152.1	141.9
Total	2,971.9	4,168.4	2,279.1	2,393.3

Source: Central Bank of Nigeria

2.5.3 Causes Of Nigeria's Debt Problem

Several factors can be said to have contributed to the growth of Nigeria's public debt which by the end of 1992 stood at N706.2 billion. The major factors as outline in CBN research brief series No. 92/04 include the rapid growth s of public expenditure, particularly for capital projects, borrowing from the international community at non-concessional rate, decline in oil earnings from the late 1970's and the emergence of trade arrears.

As regards the domestic debt problem, this was said to have been caused primarily be the need to finance ever rising government expenditures.

According to the brief, one of the causes of external debt problems was the some project-tied loans were contracted without consideration for economic vitality. In addition, these were short-term loans sources mainly from foreign private markets to execute projects of long gestation period. Consequently, by 1986, short and medium term loans constituted about 85 per cent of the total debt stock. The result of this was the bunching at service which compounded the debt situation. Furthermore upward movements in interest and exchange rates have adversely affected the size of the debt stock.

Dr. Ibrahim Ayagi, a renowned banker, traced the causes of Nigeria's public debt problem in his book, the Trapped Economy (Ayagi 1990).

According to him, then genesis of the Nigeria Public debt problem can be traced to an inherent "dependency culture" in both the Nigerian people and government. He stated inter alia that "with a dependency culture unable to create or sustain its own economic surplus, and with a people always happy to be dependent on government which by itself appears happy to be dependent on foreign government and people Nigeria remained dependent and operated a mixed economic system. '"With sudden and unexpected wealth from the oil boom years, Nigeria embarked on planning for consumption-a practice s obviously unsustainable for a country with an extremely rapidly growing population. To make maters worse, the economy was by then dependent on a single commodity for over 90 per cent of its export revenues.

Then came 1979 with the inauguration of the second civilian republic. National development plans were abandoned and all types of unprogrammed activities were introduced. Various capital projects were initiated with most of them being consumption rather than productive. Federal, State and local government went on a borrowing and foreign sources. At the same time, there was unbridled massive importation of all sorts of foreign goods which inevitably and an adverse impact on domestics production and capacity utilization.

All these importations can capital projects cost money. The came the oil guilt in 1980. Nigeria's current account accumulated huge unpaid foreign liabilities. By 1982, the countries external reserves had been so severely

depleted and had fallen below the minimum requirements for sustaining the country's imports for three months. With the reserves depleted and with imports continuing, Nigeria's current account was continually debited to pay for them. This resulted in heavy deficits in our balance of payments position. Consequently, Nigeria was forced to negotiate a reschedule of its existing medium and long-term loans as well as the removal and conversation of its current account debit balances into medium and long-term loans. During the period (1979-1973), Nigeria's external indebtedness rose from US $3.67 billion to US $ 13.12 billion.

Ayagi finally goes on to infer that the current Nigerian debt problems is the culmination of a grand design by the western industrialized nations to subvert the Nigerian economy and enmesh it in a "debt trap" thereby imposing neocolonialism on a hitherto wealthy nation which had for long been a pain in the neck.

2.5.4 Debt Management And Relief Measures In Nigeria

Debt management has become a major responsibly of the CBN in recent times necessitating the setting up of a department in the bank to undertake the function in collaboration with the Federal Ministry of Finance and other agencies (see Appendix 1).

Nigeria's external debt management strategies have varied from time to time since the early 1980 when the debt crisis became more pronounced. However, it was not until 1988 that a pragmatic, articulate and all embracing plan was set out with the following policy objectives: to outline strategies for increasing foreign exchange earnings thereby reducing the need for external borrowing to set out the criteria for borrowing from external sources and determine the type of projects for which external loans may be obtained; to outline the mechanism for servicing external debts of the public and private sectors; to outline the roles and responsibilities of the various organs of the Federal and State Government as well as the private sector in the management of external debt. Consequently, guidelines were as regards government borrowing (See Appendix II).

As part of the pragmatic approach to seduce the burden of the eternal debt, the following measures have been pursed in recent times.

a. **Embargo on new loans:** This policy was approved in 1984 by the then military administration on state government borrowing from external sources.

b. **Limit on debt service payment:** This requires the setting of a proportion of export earnings to need debt service obligations to allow for internal development. in the case of state government, a limit of 10 percent of their total revenue was established in 1980

while in the case of the federal government, 30 per cent of export earning is set aside for debt servicing.

c. <**Debt restructuring**>: The restructuring of debt involves the conversion of an existing debt into another category of debt through refinancing, rescheduling , buy-back, issuance of a collateralized bound, and the provision of new money.

   i. <Refinancing of trade arrears: >A refinancing arrangement involves the procurement of a debtor to pay off an existing debt, particularly short-term trade debt. The first refinancing arrangement was in July 1993 followed by the second agreement in September 1993. In both agreements, US N2.1 billion worth of trade arrears on confirmed letters of credit were refinanced.

   ii. <Debt rescheduling: >the rescheduling of debt involves changing the maturity structure. Interest payments are usually spread over a longer period unit the debt is finally liquidated. For instance in 1986 debt worth US N1.6 billion due to the London Club and payable in 1987 was rescheduled to extend to 1996 with a four year grace period. Other rescheduling agreement have also been undertaken with both the London and Paris Clubs.

   iii. <Debt buy-back, collateralization and new money options: > The buy back arrangement implies the offer of a substantial

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discount to pay off an existing debt. This type of arrangement was concluded in February, 1992 when Nigeria bought US $3.395 billion commercial debt due to the London Club at 60 percent discount. In other words, Nigeria paid US $1.352 billion on liquidate or buy-back the commercial debt. Furthermore, US N2.054 billion has been collateralized as 30 years per bound with the London Club, with this arrangement, the yield of the bound within a 30 year period would off-set or pay of the collateralized amount, which is referred to as zero coupon option. The new money option refers to the granting of new loans by a creditor or a group of creditors to assist a debt-ridden nation.

d. <Debt conversion: > This was introduced to complement other strategies for debt management. In Nigeria, the debt conversion exercise involves the sale of an external debt instrument for a domestic debt or equity participation in demotic enterprise. Essentially, the programme is amine at stemming the tide of resources transfer through the encouragement of capital inflow, repatriation of enterprises in the private sector. Though the appropriation of the substantial discounts offered and the commissions paid, the country benefits and reduces its debt stock. Form inception in 1988 to 1992, 225 applications values at US $3.7 billion were received out of which 214 applications valued at US $2.2 billion were given approval-in-principle. The total amount of debt actually

redeemed up to 1992 stood at US $760.9 million. Other financial benefits which accrued from the conversions undertaken up to 1992, include total discount of US $360.6 million and transaction commission of US $9.7 million.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 SELECTION OF METHODOLOGY

In the selection of a methodology for this research work, consideration has been given to the problems and the objectives of the study. The aim, to recall, is to determine the nature and the impact of the Nigerian Public dept on the national economy. Thus the study will need to cover the period from where the dept burden became pronounced up to date. Basically, the methodology will be historical analysis, that is a descriptive analysis of the facts available to be supported with statistical where relevant. It is believed that the method selected will, in itself, provide an insight to the problem without the vigors of econometric analysis. The period prior to the dept crisis will mostly be omitted for the reason that it might have little relevance to the main aim of the study.

3.2 COLLECTION OF DATA

The data to be used for the research will mainly consist of primary data obtained from the central bank of Nigeria of Finance. Where necessary, secondary data will be collected from sources and media publication Interviews and questionnaires will not be issued in that they are usually subjective, reflecting the personal views of the persons being interviewed and filling the questionnaires. The aim, therefore, is to utilize factually and statistical data as

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reserves are clearly inadequate to cover the Nation's external debt service obligations.

4.4 EXTERNAL REVERSE TO IMPORTS

The external reserves to imports ration measures the extent to which the country's external reserves will meet the cost of imports over a period. From table 6, it will be observed that the ratio rose gradually 1.1 percent in 1983 to 7.9 percent in 1986. In 1987, it fell to 3.4 percent but again rose to 10.5 percent in 1990. By 1992, it has again declined to 1.4 percent. It is immediately apparent that the level of the country's external reserves relative to imports is indeed very little.

4.5 DEBT TO EXPORTS

The debt to exports ration measures the extent of the exports that would be required to cover the total stock of the country. In 1983, the debt to exports ratio was 148.9 percent and rose over the year to peak at an alarming 418.3 percent in 1988. BY 1992 however, it has declined to 231.9 percent (See Table 6).

The critical level for this ratio as defined by the World Bank is 275 percent. From the table referred to above, it can be observed that from 198 to 1989 where the years in which this ratio recorded its highest levels when the critical level was well exceeded.

to the nature of the Nigerian Public dept and attempt on objectives assessment of its impact on the macroeconomic pulse of the nation.

3.3 METHOD OF ANALYSIS

The analysis of this work will be based on some generally accepted economic indicators of dept burden. Those will include;

a) Data Service ratio

b) External reserves to Imports ratio

c) Dept stock to GDP ratio

d) ratios of external dept stock to exports

The data will be complied and presented in tabular from to be accompanied with an analysis discussion of the table being considered.

3.4 METHODOLOGICAL ASSUMPTION

For the purpose of this study, it will be assumed that the statistical obtained from the central bank of Nigeria and the Ministry of Finance are near accurate and present a true picture of the macroeconomic situation of Nigeria over the period.

CHAPTER FOUR

4.0 PRESENTATION AND ANALYSES OF DATA

4.1 DATA PRESENTATION AND ANALYSIS

The presentation and analysis of data collected for the study will be done on the basis of the performance criteria being considered. This is to say that for each indicator of dept burden being considered, the data pertinent to it will be presented and be accompanied by a descriptive analysis. Also measures already adopted by the Federal Government towards tackling the situation will be critically analyzed. A section will be devoted to each item being considered.

4.2 DEBT SERVICE RATIO

A primary aim of data management is to seek to alter the stock, composition/structure and terms of debt with a view to maintaining at any given time a sustainable level of dept service payments. Thus an efficient dept management is one that contains the debt services within that level.

In the case of external dept, what is partially important is not so much the dept service payments as the service burden because the latter depends essentially on the country's capacity to service external dept. As such, the dept service burden must be linked to some macro-economic indicators which broadly represent such capacity and is converted into relation to those indicators. The most widely used dept service ratio is debt service payments as a proportion of export earnings.

The dept service which was 16.6 percent in 1983 rose to 25.9 percent in 1984, declining to 19.3 percent 1985. It however increased in 1991 **(See Table 6)** In 1992, it declined again to 20.1 percent.

TABLE 6

DEBT SERVICING CAPACITY RATIO

	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
DEBT SERVICING RATIO	16.6	29.9	28.1	29.4	19.3	26.3	21.9	26.4	25.8	20.
DEBT SIRV. 10 I X I.										
RESERVES	190.6	225.3	219.1	89.9	13.9	268.1	104.5	88.3	79.8	295.
EXTERNAL RESERVES										
TO IMPORT (IN MONTHS)	1.1	2.0	3.0	7.9	3.4	2.0	5.9	10.5	6.5	1.
DEBT SERVICE TO GOVT.										
REVENUE	23.9	36.8	37.0	40.5	39.4	36.4	52.7	78.2	109.6	65.
DEBT to G.D.P	20.5	21.1	24.5	62.5	58.9	179.1	278.5	294.2	350.1	121.
DEBT TO EXPORTS	148.9	155.7	151.7	404.2	541.0	418.3	362.9	227.9	241.5	231.

S O U R C E: Compiled from statistics contained in C.B.N. annual reports various years. (i) Excludes cost or closing the London Club deal (0.5 $2.156. Billion).

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The apparently low service ratio in 1992 needs to be interpreted with caution for two reasons. Not only was the cost of closing the London club excluded from the dept service figure, an estimated US $2 billion of external debt obligations stood as arrears by the end of December, 1992. Figure for 1993 were not available.

The critical level for the debt service ratio as defined by the World Bank is 30 percent (See table 7). Considering that the sum of US $2.39 billion was paid out as dept service in 1992, it is immediately apparent that is the cost of closing the London Club deal were to be included in the computations, the ratio for the year would well exceed the 30 percent critical figure.

4.3 DEBT SERVICE TO EXTERNAL RESERVES

As can be observed in Table 6, the ratio of debt service to external reserve which was 190.6 percent in 1983 rose to 225.3 percent in 1984 but defined to 89.9 percent in 1986. It again rose in 1987 and it was not until 1990 hat it again dropped below the 100 percent mark to 88.3 percent. By 1992, it had risen to 29.8 percent, the highest ever figure.

The debt service to external reserve ratio measures extent to which the Nation's external reserves can ever debt service payments in a given year. It is thus immediately apparent that the prognosis cannot be positive as the external

reserves are clearly inadequate to cover the Nation's external debt service obligations.

4.4 EXTERNAL REVERSE TO IMPORTS

The external reserves to imports ration measures the extent to which the country's external reserves will meet the cost of imports over a period. From table 6, it will be observed that the ratio rose gradually 1.1 percent in 1983 to 7.9 percent in 1986. In 1987, it fell to 3.4 percent but again rose to 10.5 percent in 1990. By 1992, it has again declined to 1.4 percent. It is immediately apparent that the level of the country's external reserves relative to imports is indeed very little.

4.5 DEBT TO EXPORTS

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The critical level for this ratio as defined by the World Bank is 275 percent. From the table referred to above, it can be observed that from 198 to 1989 where the years in which this ratio recorded its highest levels when the critical level was well exceeded.

4.6 DEBT STOCK TO GROSS DOMESTIC PRODUCT

From available statistics which are presented in Table 6, it will observed that the ratio of debt outstanding to real Gross Domestic Product (GDP) was only 20.5 percent in 1983. By 1987 it had risen to 62.3 percent and from then on risi8ng continuously to peak at 350.1 percent in 1991. This implies that interest payments apart, Nigeria would need more than three years Gross Domestic Product to pay off her principal obligations.

TABLE 7

RATE	CRITICAL LEVEL %	NIGERIA'S 1992%
Debt Stock/Export	275	231.9
Debt Stock/GDP	50	121.2
Debt Stock/Exports	30	20.1
Interest/Exports	20	5.6

Source: CBN Annual Report and Statement of account, 1992

4.7 EFFORTS MADE TO MANAGE THE EXTERNAL DEBT

Nigeria undertook its first refinancing exercise at the onset of the debt crisis in 1983 when it successfully refinanced over US $2.1 billion worth of arrears of letters of credit outstanding as at 1983. The main features of this first refinancing exercise include a repayment period of 30 months with a grace period of six months. Interest was fixed at libor plus I percent per annum.

Following the success of the first exercise, the government decided in 1984 to refinance the arrears of uninsured short term trade debts that were outstanding

The default necessitated a new round of negotiation culminating in a new agreement signed on 22nd March, 1989. By the new agreement, the annual debt services obligations to the club were reduced from US $1.345 billion. Despite this concession, the country's cash flow situation could still not sustain such a high debt services as a result of which the country approached the club again for the restructuring agreement was reached. The agreement contained a menu of options which include among others.

Buyback

Fully collateralized with US Treasury zero conpons

Fixed interest rate of 5.5 per annum for the first three years thereafter 6.25 percent pr annum on the par bonds (collateralized as to 12 months cover)

Traditional rescheduling with interest rate of LIBOR plus 13/16 percent: and Provision of new money by banks which opted for traditional rescheduling up to 20 percent of the amount so committed to the option.

The deal was successfully closed on January 212, 1992 and the country bought back 62 percent of the debt and issued collateralized par Bonds for the remaining 38 percent. No bank, apparently, elected for the traditional option. The total cost of closing the deal amounted to US #2.156 billion.

From the above, it would be observed that the country has successfully achieve some reasonable debt and debt service reduction. As at January, 1993, the debt covered with promissory notes had been reduced from US $4.8 billion to US

$3.22 billion while the London Club debt was reduced from US #5.8 billion to US $2.1 billion after the restructuring exercise. This was a laudable achievement. Of the US $2.1 billion London Club debt, the sum of US$2.05 was fully collateralized which in effect means that the whole amount of the debt has been prepaid.

However, if would appear that the country has been so successfully with management of it its official debt, notably the Paris Club debt. The first rescheduling agreement Nigeria had with the Paris Club was in 1986 then there has been two other similar agreement with the club which were assigned in March 1989 and January 1991. All the agreement provide for traditional rescheduling terms with market related interest rates.

Although the Paris Club rescheduling had provide very temporary cash flow relief, e.g. has in no way resulted in the reduction of the net present value of the debt. The reason has been that the package was always structured to apply only to current maturities falling due to within a consolidated period of about 15 months and not the entire debt stocks and the capitalization of the interest thereon. Consequently instead of reducing, the debt stock tended to increase without the country contracting new loans. Thus the Paris Club debt has remain a "pain in the neck" and needs to be urgently and adequately addressed in order to accelerate the much needed economic growth. The remaining official debt, meanwhile, which is largely multilateral and non-reschedulabe has largely been paid as and when due.

4.8 DEBT CONVERSION

Another debt management strategy adopted by the country is the debt conversion programme otherwise known as Debt-Equity Swap which was introduced in July 1988. The main objectives were to reduce the external debt stock and lighten the debt service burden, encourage capital inflows including reparation of flight capital; and assist the capitalization of the private sector investment and the generation of employment opportunities. Eligible debt for conversion was initially limited to promissory notes but later expanded to cover back debts. As at the end of 1992, a total sum of US $765.5 billion has been redeemed under the programme.

It is observed that the gain of this programme have been limited when the total amount redeemed so far is compared to the nations total external debt stock. Probably due to political risk and instability, the objective of encouraging capital inflows appear yet to be marginally realized.

CHAPTER FIVE

5.0 SUMMARY CONCLUSION AND RECOMMENDATION

5.1 SUMMARY

Over the last few years, many developing countries have faced acute external debt servicing problems. The reasons for these are varied and so the severity. Nigeria is one such country which found itself in a debt crisis in the 1980s.

Properly used, borrowed external resources can greatly benefit a developing country and contribute to its economic growth. When these external resources are utilized in an ill-advised manner, a country may eventually find itself in difficulties as regards meeting the repayment of the loans.

Adequate debt management is essential of a country is to use external resources efficiently in an increasing complex financial environment. The rising burden and greater complexity of debt that came with the 1970s and 1980s placed a greater anus on the authorities in debtor nations to manage their indebtedness through appropriate macroeconomic policies. In many cases, debt management however, tended to be adhoc.

When ineffective debt management undermines a countries ability to continue to raise new external finance by leading to late or part payments, the results can be costly, and may lead to a low or negative economic growth and compel the country to undertake a restructuring programme. Once a country's credit

worthiness is in question it may take some time to re-establish its name in international markets; in the meantime it will face higher borrowing costs and mere limited access to external funds.

Notwithstanding the exogenous factors affecting a country's payment situation appropriate debt management can help a country maintain a sustainable position in regard to external sources of finance.

In the light of the foregoing, it is relevant to assess the nature of the Nigeria public debt burden in the context of a dynamic international economic environment.

This study was hence undertaken to evaluate the nature and the extent of Nigeria's debt problem and at the same time, it is pertinent to assess the utility and the impact of the corrective measures designed and being implemented.

To set the stage for this dissertation, a review of relevant literature was carried out in the second chapter. This was considered to include a review of Nigeria's macroeconomic policy framework, fiscal deterioration and external debt management. Also considered were institutional frame works for external debt management and the causes and effect of inefficient debt management. Finally, the management of Nigeria's public debt was reviewed.

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An appropriate methodology was then selected. This methodology is considered valid in that such a study is best treated in such a manner given the dearth of statistical data in the country which would be required for economic analysis.

In the fourth chapter, the data gathered from various sources was complied and presented. This presentation was done on the basis of the various economic indicators generally accepted for measurement of debt burden. An analysis of the measures put in place for ameliorating the debt burden was also carried out.

In this final chapter, conclusions drawn from the study will be stated and relevant recommendations put forward to facilitate a reduction of the debt burden.

This study does not attempt to provide an exhaustive treatment of all the issue involved but rather to highlight those aspect that are considered primary.

5.2 CONCLUSIONS

The following conclusions have been drawn from the analysis carried out:

1) A primary cause of the Nigeria Debt problem was the absence or inadequacy of an appropriate institutional frame work for effective external debt management. Prior to 1990, there was no department

set out for management of the Nations Public debt. As such during the Second Republic when the Federal and State Government went on a borrowing space, there was no regulatory body to coordinate and control such external financing as was contracted which resulted in a bunching of maturities and a running down of the country's external reserves. Most of such loans contracted at the time were frittered away on non-productive "white elephant" projects or were merely embezzled. Furthermore, no consideration was given as regards securities the best and most cost effective sources of foreign financing short term funds were invested in long term projects of low or negative returns.

2) The Nigerian Public Debt is problematic and generally crucial. As can be surmised from the economic indicators analyzed, a vast improvement in the debt situation must be achieved fro there to be sustainable growth in the economy as prosperity for the citizenry. The amount of export revenues utilized towards debt servicing is so high the left over is insufficient to meet domestic demand for foreign exchange thus exerting pressure on the local currency.

3) A major problem facing Nigeria is the nature of the relief package given by the Paris Club. Given the short consolidation periods by the time bilateral implementing agreement have been reached. It is time to approach the club for the next round of request for debt relief. Financial planning is difficult with such a short negotiation horizon.

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Nigeria rescheduled her. Paris Club debt three times had even worsened the situation.

6) Along the same vein, the number of negotiations of agreements as highlighted in the study indicates the enormous technical often encountered in external debt management in this country. This is evidenced by the fact that agreements were entered into only to discover later that the finance needed to fulfill the terms of the agreements were not available. This was probably due to an inadequate knowledge of the full implications of the cash flow requirements that would emerge from such agreements.

7) Although the Structural Adjustment Programme appears ti have contributed to positive real growth rates for the economy, the macro-economic imbalance remain problematic. The country's balance of payments position though improved continues to exhibit pressures, the Naira exchange rate continues to depreciate against major international currencies, government deficit rends to increase and price level continues to rise. The development do not present a conducive environment for effective debt management.

5.3 RECOMMENDATIONS

In the light of conclusions drawn from the study, a number of recommendations are proffered below:

i) There should be a comprehensive review of laws governing borrowing both internally and externally. For example, although the statutory limits on borrowing may be deemed to be expedient as at the time they were set, the national debt problem at hand called for a new and well articulated look at them. The effectiveness of the laws must also be ensured.

ii) Debt cannot be well managed without a strong data base. A computer based debt management system such as has been acquired by the Federal Ministry of finance is a welcome development. However, there is a need for properly trained staff of debt management. This must be provided if the debt management system is to be of any use.

iii.) More effort must be exerted towards seeking debt relief the Paris club towards reducing the debt stock. The urgency for this cannot be overemphasized.

iv.) A conducive atmosphere for debt management should be provided bordering mainly on fiscal discipline. Good fiscal and monitory policies are being made yet are hardly over implemented accordingly. It should be remembered that planning without implementation is worse than no planning at all.

v). There should be a move towards the reduction or stoppage of importation of certain luxury items so as to free more export earnings to be used thereafter for debt servicing. The proceeds should be utilized for ventures such as the buyback in the London Club deal of 1992.

vi) Potential foreign exchange earning ventures such as the Liquefied Natural Gas Project should be speedily implemented so as to boost the export earning of the country thereby inducing economic growth, improving the balance of payment position and enhancing the country's foreign reserves.

The implementation of these recommendations would go a long way towards alleviating the National Debt Burden. It is only when the debt has been brought down to a reasonable proportions can be nation experience real positive economic growth and take its rightful place as a continental power within Africa.

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APPENDIX 1

1

DEBT MANAGEMENT DEPARTMENT

HISTORICAL BACKGROUND:

The Debt Management Department was created out of Foreign rations Department in April, 1990, to manage and monitor ernal debts.

THE OBJECTIVES OF THE DEPARTMENT:

The Debt Management Department was established to accomplish following main objectives:

1. To attend all meetings at inter-ministerial, bilateral and multilateral levels where loans or grants are being discussed and prepare report on the outcome of such meetings for the perusal of the Federal Ministry of Finance and Economic Development, the Federal Ministry of Budget and Planning, the World Bank, the International Monetary Fund and the Board of Directors of the Central Bank of Nigeria.

2. To collate and monitor Nigeria's external debt which are in short, medium and long terms.

3. To set up a data base capable of being updated on a continuous basis.

4. To coordinate the activities of it's constituent units and provide a uniform and global picture of various debts for effective monitoring and efficient utilization.

5. To prepare debt stock statistics and debt service projections.

6. To prepare and process payment instructions for relevant external debt service under various agreements.

7. To initiate policies, either alone or in consultations with our consultants on the overall debt management strategy for the country.

8. To monitor key development on debt management, international interest and exchange rates and their implications on Nigeria and advise on appropriate lines of action.

9. To coordinate and monitor development in connection with balance of payments support loans and grants and to help ensure their effective and efficient utilization and also provide regular performance report on same.

. To manage the utilization of the World Bank loan for Small & Medium Scale Enterprises (SME).

. The liaise with the Federal Ministry of Finance and Economic Development and other relevant Ministries or Departments on debt issues and in particular, on negotiation with the various categories of Nigerian creditors.

. To liaise with the International Monetary Fund (IMF) and the World Bank and other relevant institutions on all external debt and debt issues.

ANIZATIONAL STRUCTURE OF DEBT MANAGEMENT DEPARTMENT.

Department is made up of two divisions:
Bilateral Division.
) Multilateral Division.
ivision is sub-divided into functional offices. (see the ed organisational chart)
partment is headed by a Director who is assisted by 2 Directors, 5 Assistant Directors and other members of

FUNCTIONS OF THE DIVISIONS /OFFICES IN THE DEPARTMENT.
divisions and offices are designed to perform various which would ensure the attainment of the above objectives. are:

ATERAL DIVISION.
s division deals with Paris and London Clubs debts. The on is made up of - Refinancing, Administration and External tatistics and Studies Offices.

inancing Office
nitially the office was responsible for processing short erm uninsured claims for the purpose of issuance of romissory notes. This was done with the assistance of Chase anhattan Bank, New York.
rocessing Export Credit Agencies(ECA) claims. These claims nvolve all ECA countries. The claims are sent to the banks) determine their status, i.e. if they were adequately acked by Naira counter value.
econciling Nigeria's external debt obligations with all ECA odies of both members and non-members of the Paris Club.
iaising with Federal Ministry of Finance and Economic evelopment and Embassies in respect of claims, payment nstructions and relevant documents.
reparation of reports on the debt position.
erforming other ad-hoc duties.

Administration Office (formerly Debt Servicing Office)

The office commenced operations in 1986 as a result of cumulation of commercial banks debts which were rescheduled th the London Club group of creditors.

e first Refinancing Agreement was signed on 23rd November, 1987 t was superceded by the one signed on 22nd March, 1989 known Refinancing Amendment Agreement.

e functions of the office include:

- Collating and updating London Club debt stock position.
- Preparing debt stock statistics and debt servicing projections.
- Maintaining close relationship with International Agents such as Standard Chartered Bank, London and Peat Marwick McLintock London.
- Reconciling various accounts affecting external debt servicing.
- Keeping adequate records of transfer of instruments of indebtedness by the creditors.
- Liaising with Federal Ministry of Finance and Economic Development in respect of processing of payment mandates as they affect various foreign creditors especially the London Club.
- Relating with Investment Office of Foreign Operations Department in respect of payments on external debts.
- Performing administrative functions such as maintaining of vote of the department.
- Attending to enquiries from local banks and some creditor banks in respect of duplicated claims.
- Performing other ad-hoc duties.

ith the closing of the London Club deal in 19[illegible], transactions lving the London Club of creditors were transferred to nancing Office. The office was renamed Administration Office.

ternal Debt Statistics and Studies Office

office has the responsibility of Research activities of the tment. The function includes:

Gathering and storing data on the external debts.

Generating various debt reports such as:

a. debt stock profile by creditors.

b. debt stock profile by countries.

c. maturity profile, etc.

Updating the data base frequently.

Preparing debt service projections and providing regular performance reports on same.

Keeping abreast of key developments on the global debt situation.

Monitoring of international interest and exchange rates.

- Initiating debt management policies and strategies from time to time.
- Liaising with the Federal Ministry of Finance and Economic Development, the Financial Consultants and other relevant financial institutions in respect of our external debts.
- Performing ad-hoc duties.

MULTILATERAL DIVISION

This division deals essentially with loans and grants nating from International Financial Institutions such as the ld Bank, International Monetary Fund and African Development k. There are two offices in this division:

1. External Loans and Grants Office.
2. Small and Medium Enterprises (SME) Apex Office.

External Loans and Grants Office

- Ensuring that special account (Counterparts Fund Account) is opened.
- Arranging for withdrawal of the authorised allocation in accordance with the loan agreement.
- Arranging for replenishment of special account where the loan involved is a revolving one.
- Ensuring the maintenance of proper records that will facilitate the preparation of state of draw-down and utilisation of various loans under the scheme.
- Ensuring that proper records are kept and returns adequate to furnish information on funds utilisation are received from Authorised Dealers.
- Arranging and liaising with external auditors in order to audit the scheme.
- Attending to queries and enquiries of the Authorised Dealers.

Small and Medium Scale Enterprises (SME) Apex Office.

SME was established in 1989 as an autonomous unit to manage World Bank assisted Small and Medium Enterprises Development ject Loan Scheme. It became an office in Debt Management artment in 1990. The loan amount of the scheme was orginally 270.00 million but it was reduced to US$142.00 million in 1992 cut down on the commitment fee being paid on the undrawn ance. The scheme was mainly to assist 100 percent indigenous iness enterprises. However, in 1992, it was modified to lude enterprises with foreign but majority indigenous ticipation.

The project concentrations are in areas of Manufacturing and Allied Industries, Mining, Quarrying, Industrial Support vices, Equipment Leasing. Projects like subsistence iculture, Commerce, Real Estate, Finance, Insurance, Hotels Construction are not eligible.

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The Objectives

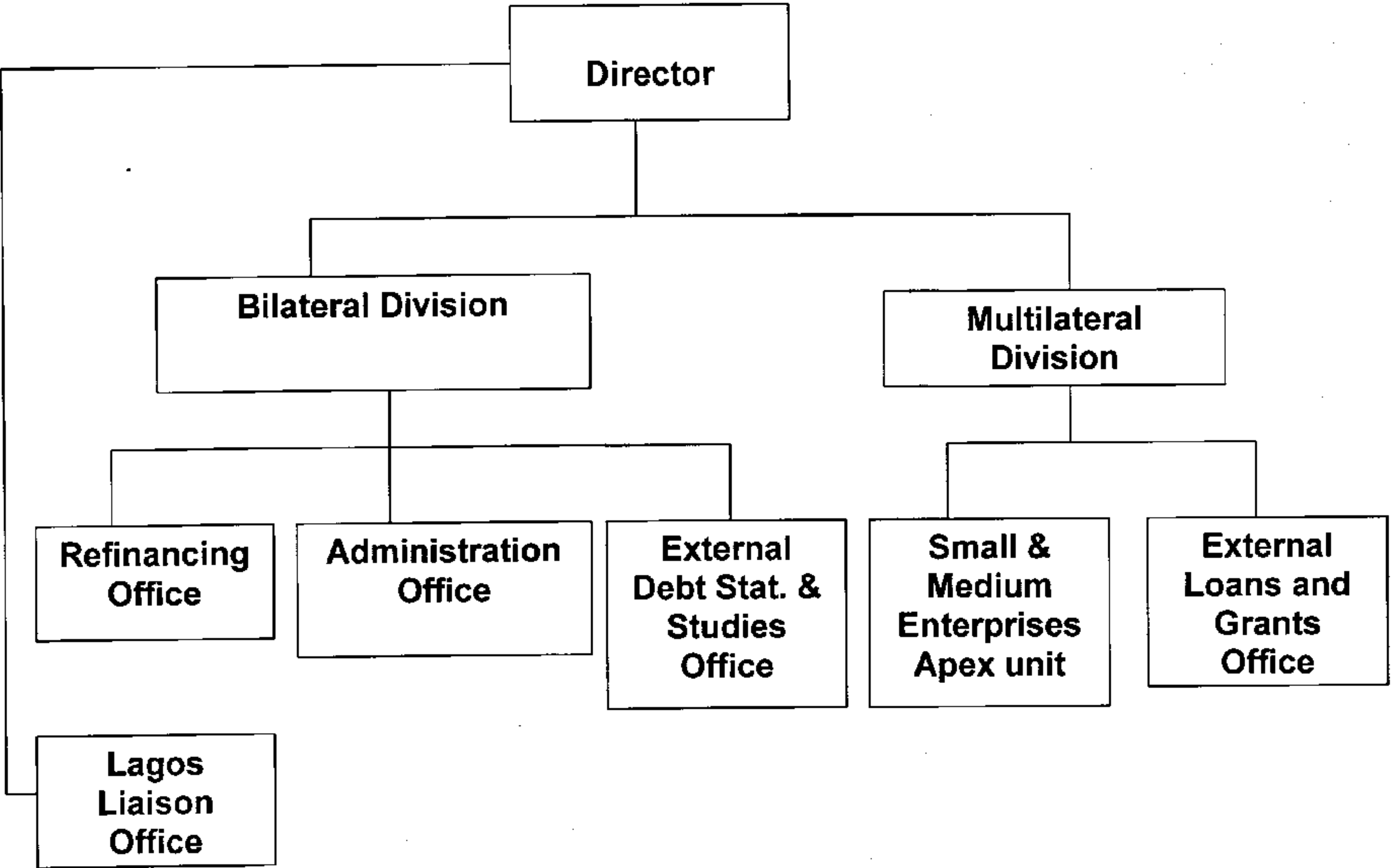
a. To support existing enterprises, restructure and modernise their operations in maintaining their comparative advantage and to regain competitiveness.
b. To help establish a new generation of viable investments in the private productive sector and service activities.
c. To enable small and medium scale entrepreneurs become more competitive by investing in the rehabilitation and expansion of their existing enterprises, and establishing new ones.
d. To revive production and improve viability of selected over-leveraged firms.
e. To support a programme of assistance to micro-enterprises.
f. To provide an alternative and more flexible source of long-term financing to SMEs through equipment leasing.
g. To make the delivery of technical supports services more demand driven and responsive to the needs of SMEs.

The Functions

Based on the afore-mentioned objectives, the functions of the office are as follows:-

- Receiving and processing non-free limit project applications for the approval of the World Bank.
- Initiating and monitoring drawdown from the World Bank Loan Account from time to time.
- Disbursing and monitoring repayment of the loans.
- Reviewing free limit financing from Participating Banks (PB) to ensure that they are in line with eligibility criteria and the World Bank Procurement procedure.
- Reviewing above "free limit" financing proposals from PBs to ensure that prima facie they are in order. These financing proposals should be forwarded to the World Bank within 10 days from date of receipt.
- Liaising with PBs, consultants and the World Bank.
- Monitoring the accounting records of the office and ensuring that the office accounts are reconciled regularly.
- Monitoring the Central Bank of Nigeria Special Account and the PB's sub-accounts regularly. Statement of accounts are sent monthly.
- Ensuring that annual accounts are prepared by the office and audited by external auditors.
- Maintaining adequate records of project operations for control purposes.
- Ensuring that report on the Special Account is forwarded to the World Bank monthly.
- Monitoring utilization of the loan by visiting projects.

ORGANIZATIONAL STRUCTURE OF DEBT MANAGEMENT DEPARTMENT



EXTERNAL BORROWING POLICY

oduction

External borrowing is often resorted to for vari us reasons such as to :

(a) supplement domestic savings in order to en. ble a higher rate of capital formation be achieved ;

(b) build up a country's external reserve position thus strengthening the liquidity sition of the country ;

(c) absorb major external shocks in order to avoid wasteful deflation and stagnation ; d

(d) serve as financial intermediation in countries with weak financial markets.

1.2. Prior to 1975. Nigeria was earning a sizeable amount of foreign exchange and not engage in external borrowing on any significant scale. She made her debut into urodollar market when she obtained the first jumbo loan of one billion dollars from ndication of foreign banks. Since then, external loans have been contracted in a azard manner without adhering to any defin te policy or guidelines. The policy ned below which was approved by the Federal Military Government in December is the result of our experiences in the past and the need to keep our debt burden r control.

ctives

2. The policy objectives are :

(a) to outline strategies for increasing foreign exchange earnings and thereby ducing the need for external borrowing ;

(b) to set out the criteria for borrowing from external sources and determine the pe of projects for which external loans may be obtained ;

(c) to outline the mechanics for servicing external debts of the public and private ctors of the Nigerian economy ;

(d) to outline the roles and responsibilities of the various organs of the Federal and ate Governments as well as the private sector in the management of external debts.

tegies for increasing foreign exchange earnings

3. The following, among others, are identified means which could significantly ease foreign exchange earnings :

(a) expansion of local refinery capacities with a view to shifting emphasis from crude l exports to export of refined oil products ;

(b) successful implementation and funding of the export incentives and strategies dlined under the Structural Adjustment Programme (SAP) ;

(c) measures to attract foreign investments such as simplification of approval ocesses and procedures for business permit, approved status, etc. and review of the

Nigerian Enterprises Promotion Decree to remove obstacles to foreign investment in the country;

(*d*) introduction of buy-back arrangement scheme and counter-trade on non-oil exports.

Management of External Debt

4. The absorptive capacity of the nation's economy is a very important criterion for determining external loan requirements while the nature of a project and its potential to generate foreign exchange for the amortization of a loan as well as the procedure for negotiating, disbursing and repaying loans are important factors in ensuring that the debt burden is kept within limits. Therefore, the following measures will apply :

4.1. *Criteria for obtaining foreign loans* :

(*a*) For projects in the economic sector, there should be a positive internal rate of return which is at least as high as the cost of borrowing while projects in the area of social services or infrastructure will be ranked on the basis of cost/benefit ratios. All projects will be subjected to comparative minimum unit cost tests using national and appropriate international yardsticks.

(*b*) Projects to be financed with external loans should, to the maximum extent possible, be supported with feasibility studies.

(*c*) External loan requirements of private sector projects and public sector projects that are of a commercial and quick-yielding nature may be sourced from the international capital market while concessionary financing may be secured for social service and infrastructural projects.

4.2. *Procedure for obtaining foreign loans* :

(*a*) State Governments and parastatals and the private sector must obtain Federal Government approval before contracting fresh loans. Contracts of projects requiring external financing should therefore not be signed by State governments and parastatals until there is assurance that the required external loan would be guaranteed by the Federal Government. Approval by the Federal Government for private sector borrowing will not constitute a Federal Government of Nigeria guarantee or Currency Undertaking but applies solely to ensure that the external borrowing conforms with national objectives and priorities.

(*b*) State Governments may obtain external loans only after obtaining Federal Government consent that it would guarantee the loan. Potential external creditors are therefore advised not to grant external loans to State Governments and their parastatals without Federal Government backing.

(*c*) All external borrowing proposals of State Governments in a fiscal year should be submitted in good time to the Federal Ministry of Finance and Economic Development for vetting and incorporation in the external borrowing programme of the public sector in the Annual Budget.

(*d*) All foreign loan agreements should first be discussed with the Federal Ministry of Finance and Economic Development and the Central Bank of Nigeria before negotiation with the creditors.

(c) Down payment and counterpart funding required in external loans should be deposited in an account preferably before the loan agreement is signed so as to avoid the perennial problem of payment of commitment charges without any drawing from the loan.

4.3. *Drawing* :

(*a*) Provision should be made in loan agreements for new loans to be guaranteed by the Federal Government, specifying that both the creditor and the borrower should forward advice on draw-downs to the Federal Ministry of Finance and Economic Development.

(*b*) State and Parastatals can draw on existing loans as the need arises but they should immediately send copies of instructions on such draw-downs to the Federal Ministry of Finance and Economic Development for record purposes.

4.4. *Repayments* :

(*a*) For the purpose of ensuring that payments to creditors are promptly made thereby avoiding penalty charges, State Governments and their agencies as well as Federal Parastatals should make available to the CBN directly or by debit of their accounts with the CBN, the naira equivalent of payments due pre-SFEM and transactions covered by the rescheduling agreements. With regard to all other transactions all Public Sector institutions including State Governments and Federal Parastatals should service their debts through the Foreign Exchange Market and promptly inform the Federal Ministry of Finance and Economic Development for record purposes.

(*b*) States or Parastatals which fail to service their loans will have the naira equivalent deducted at source before the balance of the share of the proceeds in the Federation Account in the case of States, and budgetary allocation for parastatals, is released.

(*c*) In the case of loans that are on-lent by the Federal Government to State Governments, the Federal Ministry of Finance and Economic Development will make the due payments and deduct the full amount at source from the statutory allocation.

(*d*) As for private sector loans, industries that are export-oriented should service their debts from their export earnings while others should utilize the Foreign Exchange Market (FEM) facilities for servicing their debts.

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