THE EFFICACY OF DEBT MANAGEMENT STRATEGIES ON NIGERIA'S EXTERNAL DEBT BURDEN (1976 - 1996)

BY

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DECLARATION

I hereby declare that this thesis has been written by me and that it is a record of my own research work. It has not been accepted in any previous application for a higher degree. All sources of information have been specifically acknowledged by means of references.

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CERTIFICATION

This thesis entitled **"THE EFFICACY OF DEBT MANAGEMENT STRATEGIES ON NIGERIA'S EXTERNAL DEBT BURDEN 1976 - 1996)" by P. L. EPUNDU** meets the regulations governing the award of Degree of Master of Science in the Department of Economics, Faculty of Social Sciences, Ahmadu Bello University, Zaria and is approved for it's contribution to knowledge and intellectual endeavour.

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DEDICATION

TO

THE GLORY AND HONOUR OF THE BLESSED TRINITY,
MY STRENGTH OF YESTERDAY
MY JOY OF TODAY
MY GRACE FOR THE FUTURE

AND

MY LOVING PARENTS
CHIEF & MRS. EPUNDU

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ABSTRACT

Research studies were carried out over a period of 21 years (1976 - 1996) to assess the efficacy of debt management strategies on Nigeria's external debt in relation to the looming profile of the country's debt and debt service burden in the 1980s. As a result of the ever increasing debt burden on the government and the telling effect of the burden on the citizenry, the government decided to decisively embark on some policy measures aimed at managing these problem efficiently.

The sole purpose of embarking on effective management policies was to stimulate economic growth. This study has been able to examine critically the extent to which the evolved policies vis-a-vis external debt management strategies put in place have been successful or otherwise. In order to ease our task, ratios such as debt service payment to exports, debt service payment to GDP at current factor cost among others was employed in measuring their respective influence on the debt burden. This is achieved by making debt service payment to export the dependent variable (because it is commonly used as a proxy for external debt burden) while the other ratios - (debt service payment to GDP at factor cost, exchange rate of the naira, external debt outstanding to export earnings amongst others) serve as the independent variables.

The findings of the study revealed that these strategies are short-term in nature and cannot solve the debt problem in the long run.

The study then recommends the application of international debt relief proposals, reduction and cancellation of debt amongst others, as a long term solution to reduce the debt burden of the nation.

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GLOSSARY OF ABBREVIATIONS USED IN THIS THESIS

ADP	African Development Bank
AFEM	Autonomous Foreign Exchange Market
CBN	Central Bank of Nigeria
DCC	Debt Conversion Committee
DCP	Debt Conversion Programme
DSP	Debt Service Payment
EDO	External Debt Outstanding
EFR	Economic and Financial Reviews
EIB	European Investment Bank
ER	External Revenue
ERN	Exchange Rate of Naira
FEE	Foreign Exchange/Earnings
FMF	Federal Ministry of Finance
FOS	Federal Office of Statistics
GDP	Gross Domestic Product
GTCR	Government Total Collected Revenue
IBRD	International Bank for Reconstruction and Development
ICM	International Capital Market
ICOR	Incremental Capital Output Ratio
IMF	International Monetary Fund
LIBOR	London Inter-Bank Ordinary Rate
MTES(P)	Medium Term Economic Strategy (Programme)
ODA	Official Development Assistance
OECD	Organisation of Economic Co-operation and Development
R2	Coefficient of Determination
RRD	Rehabilitation, Reconstruction and Development
SAP	Structural Adjustment Programme
SILICS	Severely Indebted Low Income Countries
SIMICS	Severely Indebted Middle Income Countries
WB	World Bank

CHAPTER ONE

1.0 INTRODUCTION

The Nigerian External debt dates back to 1958 when a US $28 million loan was contracted. Between 1958 and 1977, the country did not borrow much from external sources because in the 1970s, Nigeria experienced an oil boom which fetched the nation sufficient foreign exchange earnings to meet almost all her financial obligations. Unfortunately, little savings were made from the proceeds because the priority of the government as at that time was geared towards quick and massive development with its attendant financial implications.

With the collapse of the oil boom in the late 1970s and the ensuring glut in 1981, the Nigerian economy was beset with crisis situation as the accruing foreign exchange resources fell short of the expenditures as witnessed in the 1970s. The resultant effects were massive and persistent deficits in the balance of payments, low savings, low external reserves, deficits in government finances resulting in external borrowing. Also the fragile production base caused mainly by over dependence of the economy on the oil sector deepened the economic crisis in the country. Moreso, the terms of trade was not in favour of the economy as the nature and quality of its products in the international markets could not stand the stiff competition. A combined effect of all these was a further recourse to external borrowing by the Federal Government to bridge the domestic financial resource gap.

The first major borrowing in the history of the Nigerian economy was the "jumbo loan" of one billion US dollars. This was contracted in 1978 from the International Capital Market (ICM). The loan had a short term maturity with very high interest rate. According to Central Bank of Nigeria (EFR, 1992), the loan was used to finance a number of projects which were mostly unproductive in nature. The spate of borrowing increased with the entry of state governments and some government parastatals into borrowing from external sources to finance projects whose viability were doubtful (Falegan, 1992). While the share of loans from bilateral and multilateral sources declined substantially, borrowing from private (capital markets) sources at stiffer rates increased considerably in 1978.

The magnitude and severity of Nigeria's debt problem is more forcefully demonstrated by the movement of certain debt ratios. For instance, at 5.6% in 1976, the debt/export ratio rose to a staggering height of 452.4% in 1988, although it declined to 289.6% in 1996. The ratio of debt/GDP rose continuously from only 1.4% in 1976 to 115.5% in 1990. The ratio however declined to 38.5% in 1996. Similarly, the ratio of debt service/export of goods and services rose steadily from only 0.5% in 1976 to 21.3% in 1985 and 30.0% in 1996 respectively (CBN, 1988, 1989, 1994 and 1996). Nigeria's major debt indicators, when compared with the critical levels as defined by the World Bank, showed that the debt burden remained problematic in 1992. While the external debt/GDP ratio exceeded the critical level, the

external debt/exports and debt service/exports ratios were at near critical level. Perhaps, one of the reasons for this development is the non-disbursement of the pledges of new financing made by the Paris and London clubs of creditors. In fact, the creditors granted Nigeria a number of debt rescheduling agreements at market rates that offered no reasonable solution to her external debt burden (Uniamikogbo, 1994:82).

Although there was no problem in servicing the debt in the 1970s, government was nevertheless conscious of the need to limit foreign indebtedness. It's first attempt at controlling and managing external debt was in the promulgation of the external loan Decree of 1970 (Rehabilitation, Reconstruction and Development) which limited the level of commitment to a maximum of ₦1 billion. This was however later raised to ₦5 billion under Decree No. 30 of 1978.

However, due to the looming profile of the country's debt and debt service burden in the 1980s, the government embarked on a comprehensive external debt management policy to contain the situation. Policy measures taken include: embargo on new loans, debt relief through refinancing of trade arrears, debt conversion and restructuring on terms consistent with the realities of the country's finances, and the adoption of the Structural Adjustment Programme (SAP), (Ahmed 1988).

With the introduction of SAP in 1986, the trade and investment policy loans of US $450 million and US $500 million were contracted in 1986 and 1989 respectively. These loans paved the way for the rescheduling in 1988 of the sum of US $4.8 billion owed to private creditors at the rate of 5 percent over a period of 23 years, (Ike 1993). Added to this, the government agreed to the use of debt conversion in 1988 as yet another instrument for debt management. Debt conversion allows for equity investment in the debtor country by the creditors and such investment may be for financing a new company, expanding an existing one or financing portfolio investment. The debt stock and interest payments were reduced to the extent of the conversion.

The purpose of this study therefore, is to examine the extent to which these measures have been successful or otherwise in reducing the debt burden of the nation, and the possible use of some other strategies aimed at achieving the same objective.

STATEMENT OF THE PROBLEM

Nigeria in her quest for economic development in the wake of dwindling foreign exchange resorted to external assistance in the form of loans. These loans unfortunately were mostly used in financing economically unviable projects and programmes. Some of them were indiscriminately contracted with their varying interest charges which combined to make the quantum of debt indeterminate, thus, creating uncertainty on subsequent debt service.

Also, rapid decline in export earnings reduced debt service capacity while lack of symmetry between fiscal and monetary policies aggravated the debt burden (Business Times, 1997:13). Furthermore, the heavy dependence of the economy on oil and imported inputs rendered the economy highly vulnerable to external shocks. The gloomy balance of payment prospect with fragile growth and poorly administered debt in the face of declining foreign exchange reserve openly calls for debt management strategies.

With respect to the debt management measures earlier mentioned, their introduction was informed by the assumption that faced with economic crisis, such management policy measures would stimulate growth. However, a reference to official records shows that there has been little or no change on the state of the nation's debt burden. Reasons for such a statement may not be far fetched as they include: inadequate and weak infrastructural base for external debt management in the Country; and poor evaluation of the projects to be financed with the external loans. Specifically, until recently, there has been lack of adequate managerial capacity and skills. There has also been no comprehensive information or data which would allow for proper monitoring of debt obligations. This problem in particular resulted in the bunching of maturities which destablilised repayment schedules, thus creating rooms for default. All these have led to financial deterioration and political instability which inhibits the transfer of capital and investments from the developed countries to Nigeria. This situation has led to the emergence of various

proposals aimed at finding a satisfactory solution to the debt problem. The progress to date in reducing the debt burden has been very slow. This is because either the measures taken are not well articulated or that certain policy actions taken infringe on these measures to make them less effective. In this regard, the following questions are being raised:-

1. What is the nature of the debt burden and it's impact on the economy?
2. Has the huge amount of resources committed to debt servicing yearly succeeded in reducing the debt burden or has it led to the neglect of other sectors of the economy (that is, at the expense of national development programmes), thereby causing untold hardship to the citizens?
3. How effective are the strategies employed so far in the settlement of the debt?
4. What other options are possible?

The study is therefore, an attempt to address these and other related questions concerning the efforts made so far in reducing the nation's debt through the management strategies that have been put in place.

1.2 OBJECTIVE OF THE STUDY

The objective of this study is to examine the extent to which debt management strategies put in place so far have been successful or otherwise in reducing the debt burden of the nation. To achieve this, the study intends to:

i Review the causes, magnitude and structure of Nigeria's external debt.

ii Review the various management strategies that have been put in place to resolve the debt problem.

iii Evaluate their impact and make recommendations where necessary.

1.3 HYPOTHESIS

The study hypothesis is derived directly from the objective. In this regard, the following hypothesis will be examined:-

- The debt management strategies so far employed have played a disincentive role in reducing the external debt burden of the Country.

Accordingly, we have our Null and Alternative hypothesis as:-

$$H_o : \beta = O$$

$$H_1 : \beta \neq O$$

which will help in the validation process. For instance, if H_o is correct, signifying that the co-efficient estimated are statistically insignificant, then a conclusion is reached that the management strategies have played an incentive role in reducing the external debt burden of the country.

On the other hand, if H_1 happens to be correct, then a conclusion is reached by confirming that the strategies have more or less played a disincentive role in the management of Nigeria's external debt.

1.4 JUSTIFICATION OF THE STUDY

The seed of debt problem was sowed in 1978 when the Country borrowed from the Euro dollar International Capital Market (ICM) on commercial terms. By this singular act, the debt profile showed a significant shift from the traditional concessional (Bilateral and multilateral) sources to market sources. This is characterised by high and variable interest rates, shorter repayment and grace periods. Since then, the public debt has increased tremendously.

It will be an understatement to say that an escalating indebtedness can inhibit sustainable economic development by making the total debt burden to increase beyond the payment capabilities of the economy. A good proportion of the proceeds from export is expended on servicing debt. This limits the ability of the government to undertake more productive programmes because less of these receipts are made available for servicing the productive sectors of the economy. The use of a large proportion of current resources to finance past consumption is particularly strenuous for an economy pursuing development and stability.

It is against this background that this study seeks to examine the capabilities of the debt management strategies employed in easing Nigeria's external debt problem. It will also assess the extent to which the options adopted so far have gone in reducing the nation's debt. The study is further justified on the grounds that existing literature on the nation's debt management is mostly descriptive in nature. In other words, some quantitative indicators are called for. This study, thus, seeks to fill this gap in the existing literature.

1.5 SCOPE AND LIMITATION OF THE STUDY

This research work will cover a period of 21 years (1976 - 1996). The choice of this period is premised on a number of factors. First, by 1976 Nigeria was still enjoying the oil boom. Second, the availability of reliable data between 1976 and 1996 makes for a comprehensive research. Finally, for analytical purposes, the period is wide enough to allow for any meaningful analysis and deduction.

However, one fundamental limitation of this study has to do with differentials of data in records of financial institutions concerned. For instance, the figures provided by the Central Bank of Nigeria (CBN) differs from those of the Federal Ministry of Finance (FMF). This also differs from those provided by International Institutions such as the World Bank and the International Monetary Fund (IMF). Though, this sometimes affects the consistency of the

work by creating confusion as to which one is to be accepted as reliable, this study has chosen to make use of CBN statistical data and where such is not available, the World Bank, FMF or IMF figures will be sourced in order to resolve the problem of inconsistency of data.

1.6 METHODOLOGY

1.6.1 Sources of Data

Given the nature of the study area, the data to be used is secondary in nature. In this case, the information needed can hardly be sourced anywhere outside official quarters. Thus, data used would be sourced from the Central Bank of Nigeria's publications which include: the statistical bulletins, Annual Reports and Statements of Accounts, Economic and Financial Reviews, Bullion and Debt Trends.

Other sources of data to be used include those of the Federal Office of Statistics, Ministry of Finance, International Monetary Fund and the World Bank. Materials to build up the literature would be collected from textbooks, journals and magazines among others.

1.6.2 Variables on which data will be collected

The study intends to make use of some macro-economic indicators alongside other variables as defined in the model. These include: the external debt

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outstanding, debt service payments, exchange rate, government revenue, gross domestic product, total export earnings and foreign reserves.

1.6.3 Analytical Technique

The approach to empirical analysis employed in this study is both descriptive and quantitative in nature. While the descriptive approach helps in appraising the debt burden and the management strategies employed, the quantitative technique specifies as well as analyses the model. The method of analysis therefore, shall be the Ordinary Least Squares (OLS) regression. This is because of its simplicity and logical pattern of analysis

1.6.4 The study Model

The model would be made up of two structural equations comprising the following variables:-

DSP_t = Debt Service Payment in period t.

GDP_t = Gross Domestic Product in period t.

$GTCR_t$ = Government Total Collected Revenue in period t.

ER_t = External Revenue in period t.

FEE_t = Foreign Exchange/Export Earnings in period t.

EDO_t = External Debt Outstanding in period t

ERN_t = Exchange Rate of the Naira in period t.

IP_t = Interest Payment in period t.

The general formulation of this model is of the form:

$$EDB_t = F(DSP_t, GDP_t, GTCR_t, ER_t, ERN_t, IP_t, EDO_t, Z_t)$$

from where the two structural equations are reduced.

While the first equation will allow us an insight to variables defining the total external debt outstanding, the second equation would permit an assessment of the debt burden through the variables that define it's proxy - the debt service ratio.

Again, given the chosen period of this study to be 1976 - 1996, 1986 is chosen as a significant year. This is because it marked the beginning of a more serious effort towards managing the nation's external debt. The use of two period analysis (1976 - 1985 and 1986 - 1996) can equally be captured by the use of dummy variable for the entire period (1976 - 1996). This is opted for, for ease of analysis and convenience (Rao and Miller, 1971:88).

ORGANISATION OF THE STUDY

This study is organised into five chapters. The first chapter is the introductory chapter. It comprises the statement of the research problem, objective of the study, the study hypothesis, justification, scope, limitation as well as the study methodology. The study model is also provided in this chapter.

The second chapter takes on the conceptual and theoretical framework. The major concepts are adequately defined and the study framework is theoretically provided. Added to these, is a review of literature related to the study area. This is with respect to causes and structure of the nation's external debt and indicators of debt crisis.

The third chapter deals with the analysis of debt management strategies. Here attention is drawn on the essence of debt management and the various instruments of debt reduction.

The estimation of the model specified, and discussion on the findings, are reflected in the fourth chapter.

Lastly, summary, conclusions and recommendations come up in the fifth chapter.

CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 CONCEPTUAL FRAMEWORK

2.1.1 External Debt

Total public debt for a Country is made up of both internal and external debts. The internal debt consists of government borrowing from the banking system through monetary policy instruments such as treasury bills, treasury certificates, development stocks, treasury bonds and other borrowing from the non-bank public in form of debt to contractors or other economic agents for services rendered.

External debt on the other hand, is defined as the "gross amount at any given time, of disbursed and outstanding contractual liabilities of residents of a country to non-residents to repay principal, with or without interest, or to pay interest, with or without principal". Certain points need to be noted with respect to this definition. First, the definition highlights the fact that gross debt is directly related to the problem of debt service. Second, that debt originates from contractual liabilities thus excluding for example, equity participation. Third, the term "principal with or without interest" brings interest free loans into the definition while "interest with or without principal" means loans of indefinite maturity, such as perpetual bonds, should be included as part of external debt. Fourth, the "contractual liabilities" criterion has to be made with non residents to qualify a loan as external debt. External debt therefore,

covers all government borrowing, parastatal and private sector borrowing, whether guaranteed by government or not, as well as other financial operations of domestic economic agents, including direct investment and leasing.

2.1.2 Debt Management

Debt management may be defined as those policies which seek to alter the stock, composition or structure or terms of a debt with a view to maintaining at any given time a sustainable level of debt service payment. Therefore, an effective debt management is one that contain the debt service burden within that level. In other words, debt management refers to the technical and institutional arrangements involved in organising domestic and external liabilities. The technical aspect involves the need to determine the level of external debt required to ensure that terms and condition of those borrowing are commensurate with the future debt service capacity of the country.

The institutional aspects include the administrative, organisational, legislative, accounting and monitoring aspects of managing both new borrowing and the total stock of debt.

External debt in particular is not so much the debt service payments but the debt service burden because the burden depends essentially on the Country's capacity to service the debt. The debt service burden is linked to some macro-economic indicators which broadly represent such capacity and is converted to ratios in relation to these indicators. The most widely used debt service ratio is debt service payments as a proportion of export earnings. Therefore, in

order to ensure effective debt management, debt service ratio which reflects the debt service burden, has to be stable and kept at a sustainable or desirable level.

2.2 THEORETICAL FRAMEWORK

The preceding analysis has provided an insight on the concept of debt management, drawing on the fact that the aim is to contain the debt service burden within realistic and manageable limits. It is also observed that an effective debt management makes it possible for proper schedule of maturities to be compiled and adhered to in order to avoid bunching of maturities and defaults (Ojo 1997:8).

To ensure an efficient debt management, the debt service burden must be linked with some standard macro-economic indicators. (The most widely used measure of debt service burden is debt service payment as a proportion of export earnings by a country in a given year). There is a simple short and medium term macro-economic model which enables a derivation of a broad macro-economic condition that should be met in order for the debt service ratio to be stable. Below is an analytical framework that could bring out clearly those determinants of debt service ratio (proxied here for debt burden) which would ensure that the debt burden is kept either stable or at a desirable level.

The following is the framework:-

$d = F/P_x$ ----------1

$F = rD + a$ ----------2

Equation 1 can be restated as:

$d = (F/D)\ (D/PY)\ (Y/X)$-----3

$F/D = r + a$----------4

$Y/X = 1/x$----------5

Where

d = Ratio of debt service to exports

F = Debt service

D = External Debt outstanding in nominal prices

Y = Gross domestic product in real terms

P = Price level

X = Exports in real term

r = Average nominal interest rate

a = Average amortisation

x = Relative share of exports to GDP

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Substituting equations 4 and 5 into 3 will give:

$$d = (r + a)\ (D/PY)\ (^1/x)$$
$$= \frac{r + a}{x}\ (D/PY)$$ ------6

Equation 6 indicates that variation in debt service ratio will depend ultimately on those in debt - GDP ratio (D/PY), assuming that the terms of external debt

and the export to GDP ratio (X/Y) remain unchanged. This implies that the debt service ratio will stabilise at a certain level only if the debt to GDP ratio stabilises over the medium term.

In similar vein, positive variation of x will lower the coefficient, all things being equal, hence inducing a reduction in the debt service ratio. This effect is also tenable only if the debt to GDP ratio stabilizes over sometime.

Working within this framework will allow us a comprehensive approach to the analysis of the efficacy of debt management strategies put in place in the country. The instruments of measurement in this case will be the observed behaviour of the ratios of selected variables.

2.3 REVIEW OF RELATED LITERATURE

External loans to Nigeria are from four major sources. These include contractor finance and supplier credit, the Paris club of creditors representing official government creditors and the London club of creditors representing commercial banks spread all over the world. Others are the multilateral creditors such as the World Bank, the International Monetary Fund (IMF), the European Investment Bank (EIB), the International Development Association (IDA), the International Finance Corporation (IFC) - a member of the World Bank group, the International Fund for Agricultural Development (IFAD) and African Development Bank (ADB) (Uniamikogbo, 1994).

In the 1960s, the Nigerian Government relied heavily on contractor finance as a result of inadequate aid supplies. Contractor finance obligations and supplier credits to the public reached an alarming scale and consequently caused acute concern in the 1960s. The concern about such credits was not so much because of their high interest rates but because of the very short repayment period of 5 to 6 years. As a result, the cost of such credits to the economy tended to be very high. From the early 1970s up to 1978, there was a major shift away from procuring loans through contractor finance to bilateral and multilateral sources.

The official government creditors, (the Paris Club) have a bulk of their loans tied to procurements in their home countries thereby encouraging imports and projects of low priority, thus, leading to the non competitiveness of import prices (Ezenwe, 1970). This has negative impact on the export potential of the recipient country (Nigeria), hence, increasing their costs on the economy.
The World Bank group has been the most prominent among the multilateral suppliers of loans to Nigeria. All the World Bank loans have been made to Federal and State Government and to quasi-official institutions with a guarantee by the Federal Government, (Obadan, 1997).

Nigeria's external debts were contracted for various purposes such as: the financing of trade, balance of payments support loans, project tied loans and loans for socio-economic needs of the people including infrastructure, health and education. While the stated purposes for which most of these loans were contracted would attract no objection, as economic realities at certain point in

time would necessarily permit, the current circumstances have proved that the results have not justified the purpose.

2.4 CAUSES OF THE DEBT CRISIS

Nigeria's external debt crisis can be traced to both endogenous factors such as the nature of the economic policies formulated by the various governments and exogenous factors which are beyond the control of government. However, it is important to note that the endogenous and exogenous factors might not be mutually exclusive because the external factors indeed have an effect on what happens domestically and vice-versa. Thus, Khan and Knight (1993), pointed out that "external factors such as changes in terms of trade may also exert a systematic influence on the real effective exchange rate so that it is not always a reflection of domestic factors alone".

In general, the causes of the debt crisis include neglect of agricultural development, import dependent industrialization, debt inducing social reforms, failure to diversify exports and heavy defence expenditure. Until recently, defence expenditure took a lion's share of the national budget. Though from an economic perspective, increased military spending have some positive aspects as it guarantees some internal confidence against external encroachment.

As a necessity for stability, the impact of that on the entire economy is less significant compared to other expenditures. Infact, in the face of poor and limited technology, the impact on economic growth and development, especially in developing countries has been negative (Deger and Sen 1991, Chan, 1985, Grobar and Porter 1990).

Added to this is the impact of external non-commodity price shocks such as the interest rate shocks of the 1980s. While the sharp and sustained decline in oil prices from 1982 precipitated Nigeria's debt crisis, and the high interest rate policy pursued by the Organisation of Economic Co-operation and Development (OECD) countries exacerbated an already difficult situation. It can also be argued that a major cause of Nigeria's present difficulties is an ineffective, inefficient and corrupt administration. The mismanagement of foreign borrowing virtually pre-programmed a debt crisis into Nigeria's economic future (Uniamikogbo 1994).

Nigeria is characterised by a low productive base with an inadequate supply of goods and services. The effect of this has been huge import bills. For instance, the nation's import bills rose from ₦756.4 million in 1970 to ₦143.2 billion in 1992. As at the end of 1996, the figure stood at ₦563.3 billion (CBN 1997). The inability to settle these bills resulted in the rapid build up of trade debt.

The initial ease with which loans were extended to Nigeria without ensuring their viability of the projects to be financed was instrumental to the rapid increase in external debt (Obadan 1997). Some project-tied loans were not only contracted without consideration for economic viability, but were also short-term and sourced mainly from foreign private markets. Although, the projects which they were to finance had long gestation period, short and medium term loans formed about 85% of the total debt outstanding by 1986 and 83.38% by 1996.

The low level of domestic saving and high propensity for consumption of foreign goods and services made it inevitable for Nigeria to borrow from external sources to finance economic development. While average investment was 18.3% of GDP for the period 1971 - 1987, average consumption stood at 78.1% of GDP for the period 1971-88. Infact, in 1984, investment and consumption stood at 6.2 and 91.0% of GDP respectively (Uniamikogbo, 1991b).

The inappropriate monetary and fiscal policies of the government also had serious adverse effect on the economy creating in effect, domestic inflation, capital flight, distortion in relative prices, encouragement of imports and

discouragement of production for exports and other depressant effects. (Sanusi 1988). These distortionary effects makes the domestic economy vulnerable to external shocks and the dependence on external finance for shock proof.

The foregoing arguments have similarly been corroborated by other scholars. For instance, Ezenwe in his work, "The African Debt Burden and policy option (1994)" believed that it was the combination of both the external and domestic factors that made it difficult for a number of African Countries by 1980 to meet debt service obligations while maintaining existing trends in growth of imported goods and services that resulted to the debt issue. He is of the view that slow growth would pose new problems in expanding exports and delay progress in debt restructuring. He, thus, concluded that external finance is a necessary but not a sufficient condition for economic growth and development and that Africa needs all the external assistance it can get to reverse the deteriorating economic situation.

Ojo (1989) in furtherance of the argument, emphasized the domestic factors in the nation's debt crisis. He argued that even in a situation where an external economic development could be a critical factor in the domestic economy, there should be an adjustment to the external shock. In Nigeria, there has not been evidence of sufficient domestic adjustment that would allow for any meaningful developments in the management of the Nigerian economy since

the early 1970s. The factor of over dependence on oil has been maintained for too long without any adjustment reaction. To worsen the situation, the oil boom sparked off by developments in 1973/74 and 1978/80 was not followed by any relevant adjustment. Instead, economic management favoured rapid expansion whose sustainability was never questioned critically. The economic down turn of the 1980's could not stand the test of time as the instruments of economic management were explicitly weak.

As earlier said, the bulk of the loans were short and medium term in nature which made amortization fall due. But what escalated the problem was the reckless and sometimes planless application of loans. Worse still, not only did many government agencies borrow indiscriminately from abroad, but the use to which such loans were put was not also accounted for. The consequence of those faulty external debt policy was the lack of regular stream of income to service disbursed external loans.

The capital - outflows resulting from negative real interest rate which discourages savings and not supplemented by sufficient capital - inflows also contributed to debt accumulation because external financing must be source to bridge the gap.

Thus, the debt crisis period witnessed little or no economic growth due to the adverse effect of the burden on the economy. The excess of debt service

payments over capital inflow has led to a shortfall in resources for domestic investment. For a dependent economy and for its capital goods, the fall in the importation of capital goods and raw materials have reduced the tempo of implementation and initiation of various development projects. The results of these has been the slow growth in the agricultural, industrial and service sectors. The chain reaction effect has also been inflation and unemployment in the domestic economy.

Generally, the external indebtedness of a Country becomes a problem when the burden of servicing the debt becomes so heavy and unbearable that it imposes intolerable constraints on the economy and on the development efforts of the authorities. When the bulk of foreign exchange earnings is earmarked for servicing of the debt, drawing on new loans maybe needed to service existing debt. In such circumstance, only a small proportion of total foreign exchange earnings is available for financing of economic and social projects (Fasipe 1990). Reaching such a point reflects a critical state.

INDICATORS OF DEBT BURDEN

The broad effect of debt crisis is the emergence of a debt overhang and an unsustainable high debt service burden. To service increasing interest and amortisation liabilities, the country has to commit a large proportion of its export earnings to debt service payment. The result is constrained availability

of foreign exchange for use in the domestic economy, hence the development resource gap.

Nigeria's external debt problem can be better appreciated from the analysis of the major indicators. When the resources committed to debt servicing are related to national resources, the result is disturbing. A table of analysis of debt burden and debt servicing capacity is provided in table 8 (see chapt. 4 Pg.71). A glance through the columns would indicate that the ratios have, at most times been over and above the critical level. These ratios are indicative of the fact that there has not been an efficient debt management. An efficient debt management should possess some basic characteristics which includes the following:-

(i) An efficient debt management would result in a debt service ratio that is stable between 20 to 30 percent (Omoruyi, 1996). However, a country's ability to sustain a ratio depends on a number of factors which include, the Country's export level, reserve level and the flexibility of the country in adjusting its policies and economic structures. Also stable economic and monetary system should prevail.

(ii) The structure of debt should reflect an adequate spread of maturities and diversification of sources of debt. Also the maturities should always match the pay-off period of investment so that there would not be bunching of maturities or rolling over of short-run borrowing.

(iii) External borrowing to finance investment should be limited to the point where the marginal product of capital is equal to the cost of borrowing. This is because, borrowing to finance investment whose rate of return falls short of the cost of borrowing would lead to a decline in the growth rate of GDP. This situation makes the debt burden unsustainable.

(iv) Lastly, the Debt/GDP ratio should be kept at a low level. This is because a high Debt/GDP ratio suggest that the debtor country is at great risk. A large Debt/GDP ratio makes external borrowing inevitable as the resource gap has to be bridged to avoid domestic socio-political cum economic conflicts. In addition, an excessive rise in Debt/GDP ratio may increase the perceived probability of future debt servicing difficulties. Thus, raising expectations about increased taxation, inflation, currency depreciation and capital flight. All these have a dampening effect on the domestic business environment (Omoruyi, 1996:10).

It is evident from the foregoing that the absence of these characteristics in debt management can lead to a debt trap - a point where the debt burden is growth disincentive. For instance, the mechanism through which external debt affects economic growth is investment. Investment behaviour is adversely affected by debt servicing especially for a heavily indebted nation. A study by IMF (1989:65) on investment behaviour found investment to be lower in heavily indebted countries. After analysing the different explanations for the decline

in investment, it concludes that "... poor performance of investment in countries with debt servicing problem is generally consistent with the presence of debt overhang".

The debt burden can depress investment and hence, economic growth through illiquidity and disincentive effects. The illiquidity effect results from the fact that there are only limited resources to be divided among consumption, investment and external transfers to service existing debt. The disincentive effect arises because expectation of future burden tends to discourage current consumption (Onah 1994:147).

Finally, it would be appropriate to conclude from the foregoing that while different explanations have been provided for the causes of the nations current debt situation, it is the opinion of this study that alleged reasons for the crisis are collectively reinforcing. And, until it is viewed from such a point, we may not be able to comprehend the length and breath of the crisis. In the same vein, we may also not be able to suggest an effective strategy and proffer a meaningful solution to Nigeria's debt situation.

The chosen framework of analysis is aimed at providing us the tools with which we can aggregatively approach, as a strategy, the management of Nigeria's external debt. As earlier said, working within this framework would permit the employment of instruments of measurement which would in this

case, be the observed behaviour of the ratios of selected macro economic variables. A profile of the nation's debt management as shall be seen in the next chapter would show that the observed point of this study and the approach chosen have not been given much attention by economic analysts because the approach is quantitative in nature.

CHAPTER THREE

3.0 EXTERNAL DEBT MANAGEMENT STRATEGIES AND THE NIGERIAN EXPERIENCE

3.1 INTRODUCTION

External debt management refers to the planned acquisition, deployment and retirement of external loans either for development purposes or for balance of payments accommodation. It implies more rational utilisation of earned foreign exchange. An important trade off exists here. If a sizeable proportion of foreign exchange earnings is employed to reduce external debt outstanding, other important national requirements in industry, agriculture, health, education, etc, may suffer. Conversely, if these basic domestic needs are satisfied with foreign exchange earnings while defaulting on debt servicing, total value of outstanding external debt increases as well as the proportion of future income stream that has to be paid abroad as interest. In this regard, an appropriate strategy to manage external debts should be directed first to domestic needs after which residual external exchange may be employed to service external loans. This encourages growth of the domestic economy and facilitates debt servicing later. Alternatively, if premium is put on debt servicing, it produces economic stagnation, social unrest and political instability.

External debt management can be effective and efficient or inefficient. An efficient management of external debt makes it possible for proper schedule of maturities to be compiled and adhered to in order to avoid bunching and defaults. An effective management of external debt, on the other hand, seeks to share the burden of debt crisis between the debtor and creditor countries. To achieve this, international co-operation is required among debtor countries so as to protect their economic growth and living standards.

Debt management on an individual country basis weakens the bargaining position of debtor countries. This situation led Nigeria to adopt various debt management strategies and measures which have varied from time to time since the early 1980s when the debt crisis became pronounced. It appears however, that an appropriate debt management strategy has not yet been put in place, otherwise the debt problems would not have assumed burdensome dimensions. Moreover, most of the loans procured from private sources at unfavourable terms were either directed or utilised for projects which were unable to generate funds for servicing the underlying debt. The 1996 federal government budget statement confirmed that the past debt management strategies have been unsatisfactory in nature. The effect being that many of the projects financed by external loans were either uncompleted, partially completed and where they have been completed, they are not functioning. Examples of such projects are the Katsina Steel rolling mill, Ajaokuta steel mill, National identity card projects, etc. These projects have invariably not

contributed to the repayment of principal and interest on loans which in effect, is a loss on the economy (Obadan, 1997).

However, comprehensive guidelines were introduced in February 1988 with the following policy objective: to evolve strategies for increasing foreign exchange earnings thereby reducing the need for external borrowing; to select 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; and to define the roles and responsibilities of the various organs of Federal and State Governments as well as the private sector in the management of external debt (CBN Briefs, 1997).

Over the past three years, the government consciously evolved a new external debt management (Medium Term Economic Strategy-MTES) designed not only to stem the tide of rising debt stock but to actually reduce it (Obadan, 1997). The outcome was the achievement of a significant degree of success in external debt management in 1996. The net effect of the implementation of the strategy during the period was the reduction of Nigeria's external debt stock from US $32.584 million in 1995 to US $28.060 million in 1996, out of which arrears accounted for US $11.124 million (see table 1).

Table 1: Nigeria's External Debt Stock as at Nov. 1996

CATEGORY	ARREARS $ MILLION	BALANCE $ MILLION	TOTAL $MILLION	% OF TOTAL
Multilateral	42.00	4,623.00	4,665.00	16.62
Paris Club	11,072.00	8,019.00	19,091.00	68.04
London Club	0.00	2,043.00	2,043.00	7.28
Promissory Notes	0.00	2,140.00	2,140.00	7.63
Non Paris Bilateral	10.00	111.00	121.00	0.43
TOTAL	11,124.00	16,936.00	28,060.00	100.00

Sources: i Federal Ministry of Finance
ii Central Bank of Nigeria

NOTE:

Multilateral Debt stock

IBRD = $2.837 million

EIB = $0.469 million

ADB = $1.359 million

TOTAL $4.665 million

The government attributed the reduction in the magnitude of the debt to the strategies adopted during the year. Some of these strategies were:-

(a) Appraisal of the performance of projects financed with external loans and credits with a view to determining whether or not the country obtained commensurate value from the borrowing. It also determines

how the proceeds of the loans were spent and why most of the projects financed with them did not generate enough local currency resources for the amortization of the loans/credits. The appraisal exercise was meant to underpin government attitude to future external borrowing by public bodies and also to reinforce government determination to progressively withdraw from activities that are more suited for private sector undertakings.

(b) Reconciliation of the Country's debt stock with those of the creditors in order to have a firm base for a meaningful debt reduction strategy. The purpose (of regarding debt reconciliation with creditors as part of debt management strategy) is to ensure that the country has accurate information as to what she is owing so that whatever solution is designed to achieve debt stock and debt service sustainability will be based on accurate information as to the size of the debt problem

(c) Conversion of Paris club debts within the debt conversion programme (DCP) in 1996 and the success achieved has raised the hope that, that class of debt will be increasingly traded under the programme from thence.

(d) Outright restraint on External borrowing by the government for three consecutive years. Since 1994, the government did not take any new external loan and has not guaranteed any such loans on behalf of any public sector institution.

(e) Intensification of discussions with the IMF and World Bank with a view to reaching an agreement on a medium term economic programme (MTEP), which will facilitate an eventual approach to the Paris club for a concessional debt reduction (Iremiren 1997, Obadan, 1997).

3.2. INSTRUMENTS OF DEBT REDUCTION

As part of the pragmatic approach to reduce the debt burden, the government over the years adopted a number of measures such as:

3.2.1 Embargo on New Loans

This involves temporary stoppage of further external commitments in the form of loans until the debt position improves. This measure is not intended to reduce the burden of servicing existing debt, rather it is aimed at preventing the escalation of the level of total debt stock, and consequently minimize the problem of additional debt burden. In 1978, the maximum level of foreign borrowing by the Federal Government was fixed at ₦5 billion while in 1982, new loans taken by any state government was pegged at ₦200 million. This policy was again applied in 1984 on state governments' borrowing from external sources but the latest directive on this was in September 1996. The circular directed that no Ministry, Extra-Ministerial Department, Agency or Parastatal should henceforth enter into negotiation or accept foreign loans without the express permission of the Head of State (Obadan, 1997).

3.2.2 Limit on Debt Service Payments

This requires the setting aside of a proportion of export earnings to meet debt service obligations to allow for internal development. In 1980, the State Governments were mandated to spend not more than 10 percent of their total revenue on debt service payments while the Federal Government was required to set aside 30 percent of export earnings for debt servicing. This was meant to be a target feasible under the current loan rescheduling and other negotiations with the external creditors and not a unilateral moratorium on debt service payments.

3.2.3 Debt Restructuring

This involves the conversion of an existing debt into another category of debt through refinancing of trade arrears, rescheduling, debt buy-back; issuance of a collateralised bond, and the provision of new money. Thus, the various agreements reached in this strategy have provided short term relief which in the long run might amount to a higher debt burden because of fluctuating interest and exchange rates.

3.2.3.1 Refinancing of Trade Arrears/Rescheduling

Refinancing of trade arrears involve the procurement of a new loan by a debtor to pay off an existing debt, particularly short-term trade debt. The new loan may be contracted from the same creditors or a new set of

creditors as the case may be. The repayment of such debts normally negotiated with the creditors is contained in the loan agreements.

Debt rescheduling conversely involves a rearrangement of the repayment terms of an original loan. That is, changing the maturity structure, spreading interest payment over a longer period until the debt is finally liquidated (Uniamikogbo, 1994).

However, debt refinancing/rescheduling is necessary when a country faces a temporary foreign exchange constraint or economic imbalance. This is because it will give the debtor country some time during which the temporary balance of payment problem will be solved (in debt refinancing) and gives room for proper adjustment to redress the basic balance of payments disequilibrium (in rescheduling).

The objective of debt rescheduling like refinancing is to postpone payments of maturity debt in order to allow the authorities time to take fundamental policy actions to correct the underlying economic imbalance. It is also to expand the country's productive and export capacity which will allow it to return to normal international trade and payment practices.

Nigeria first implemented the refinancing/rescheduling programme in July 1983 when it successfully refinanced over US $2.1 billion worth of arrears of

confirmed letters of credit outstanding as at 1983. The main features of this first refinancing exercise included a repayment period of 3 years, a grace period of 6 months at an interest rate of 11/4 percent above LIBOR per annum. These claims were fully repaid in 1986 (Ojo 1989). Following this successful exercises, agreements were reached in 1984 to refinance trade arrears of uninsured short term trade debts that were outstanding as at December 1983. These were contracted through bills for collection, open account transaction and unconfirmed letters of credit by the issuance of promissory note of six years maturity with a grace period of 21/2 years (CBN Briefs, 1992). The total value of notes issued was $3.8 billion at an interest rate of 1.0 percent above LIBOR while the redemption was to begin in October 1986 on a quarterly basis. However, since Nigeria was unable to redeem the Notes on due dates, trade arrears amounting to $4.8 billion were refinanced and covered with promissory notes between 1984 and 1988. The promissory notes have a repayment period of 22 years including a grace period of two years with an effective rate of return of 5 percent per annum. The terms of the promissory note agreement provided one of the best relief packages Nigeria has ever got (Debt Trends, 1996).

Since 1986, efforts have been made to reschedule debts under the auspices of the London Club and Paris Clubs. In 1987, rescheduling involving medium/Long term debt amounting to $1.6 billion falling due to the London

Club for 1986 and 1987 was undertaken. It involved repayment over the period 1986 - 1996 with a grace period of 4 years. Under same agreement, letter of credit due in 1986 and 1987 valued at $2.4 billion were rescheduled for repayment between 1987 and 1990. The grace period was one year with interest payment at a rate of 1**1/4** percent above LIBOR. Under the regie of the Paris Club of official creditors, agreement was reached to reschedule a total of $6.8 billion which was the principal and interest due between October, 1986 and December 1987. However, terms were to be negotiated bilaterally.

In 1988, another round of rescheduling involving $5.9 billion being claims of the London Club took place. The amount consisted of $2.5 billion letters of credit arrears originally rescheduled for 4 years under the 1987 agreement; $600 million representing interest charges and commission payable on letters of credit; $1.7 billion medium/long term debt originally rescheduled in 1987, as well as new maturities for 1988 amounting to $1.2 billion. While the letters of credit were made repayable over 12 years, the conventional loans were to be repaid in 20 years with three years of grace.

However, in-as-much-as the country tried to meet up with these agreements, it defaulted because of the high debt service obligation. This led to a new round of rescheduling with the London Club, signed in March, 1986 and made operational from June 14. The agreement provided for:-

(i) Repayment between 1989 and 1991 of payable debt of $500 million.

(ii) Repayment between 1992 and 2003 of refinanced letters of credit of $2.4 billion.

(iii) Repayment between 1992 and 2008 of medium/long term debt amounting to $2.8 billion.

(iv) Interest rates of **13/16** and **7/8** percent above LIBOR on refinancing and restructuring amendment agreements respectively, while payable debt is non-interest bearing if there is no default.

(v) A menu of options to provide further relief for instance, the conversion of payable debt into interest bearing naira denominated securities with a coupon rate of 13**1/4** percent and maturity of 18 months, conversion of other bank debts into a Nigerian investment bond with a grace period of 10 years and interest of 6 percent flat; and amendment of guidelines on debt conversion to make bank eligible for conversion under the programme (Ojo, op.cit).

The agreement with the Paris Club for 1989 (signed in early March) provided for:-

(i) Rescheduling of 60 percent of arrears of short term trade debts due on December 31st, 1990.

(ii) Rescheduling of all post September 1986 maturities amounting to $110.03 million for repayment between June 30, 1989 and December 31, 1994.

(iii) Rescheduling of all arrears of medium/long term maturities for repayment between February, 28 1995 and August 31, 1999.

(iv) Completion of all bilateral agreements before September 30 1989 (Ojo Op.cit).

Though Nigeria could be said to have won favourable terms and concessions from the debt refinancing/rescheduling efforts, it has not been successful with the management of the Paris Club debt. This is because, the Paris Club debt provides a very temporary cash flow relief rather than a lasting solution to the debt problem. As such, it had in no way resulted in the reduction of the net present value of the debt. Also it provides a short term relief from the severe debt burden thereby enabling the thin foreign exchange resources to be spread over the essential sectors of the economy. In addition, since the package is always restructured to apply only to current maturities (falling due within a consolidated period of about 15 months) and not to the entire debt stock and the capitalisation of the interest thereon, the debt stock instead of reducing, tends to increase without the country contracting new loans (Debt Trends, Op.cit). Hence, the Paris Club debt could be said to be a "pain in the neck", and in order to accelerate the much needed economic growth, this needs to be adequately and effectively addressed.

Despite the importance of this policy, its effects are temporary. For instance, it does not reduce debts but pushes it at higher cost in the future since there is

that tendency for interest rate to rise. Also the exercise has not earned the `new money' package since creditors are eager to recover the debts rather than lend. The result being a net capital outflow which constrain the implementation of adjustment programmes especially in Nigeria. Finally, it leads to a situation whereby the debtor country struggles to settle the interest payments on loans rather than the principal.

3.3 DEBT CONVERSION PROGRAMME (DCP)

The fourth major instrument of debt management is the debt conversion programme. It was introduced to complement other strategies of debt management. Essentially, debt conversion involves the exchange of a debtor country's external debt for a domestic debt in local currency or equity participation in a local development project. Such investment or participation may be for financing an entirely new company, expanding an existing one or finance portfolio investment. The debt stock and associated interest payments are reduced to the extent of conversion. Thus, it is a mechanism for reducing a country's external debt burden by changing the character of the debt.

The two basic types of debt conversion are:-

(a) The exchange of foreign currency debt for domestic currency.

(b) The exchange of foreign currency debt for local currency which can be used for the purchase of equity shares in domestic companies or used for capital investment locally.

Such exchanges can be done by a foreign investor or a local resident investor. In either case, foreign exchange is used to purchase a country's debt (e.g promissory notes) at a discount from a foreign creditor (e.g a commercial bank) and then negotiated with a domestic agency (the Central Bank) in order to exchange the debt for local currency or debt. Other forms of debt conversion include:-

(a) **Debt - Debt Swap:** This involves a change of one creditor for another without changing the terms of payment. In this case, the holder of the debt for country `A' exchanges it for the debt of country `B' for such reasons as liquidity, risk reduction or tax.

(b) **Debt for Equity:** This involves the sale of external debt at favourable discount for equity participation in domestic enterprise. The proceeds are used to finance a new company or expand an existing one. This scheme seeks to reduce the size of the external debt and link the servicing of the external obligations more closely to the country's capacity to pay. In this case, the outflows of dividends would depend upon the earnings generated by the activity being financed.

(c) **Debt for Cash:** This is similar to debt conversion to equity except that the proceeds from conversion are not capitalised but used for local loan repayments, local tax payment or as working capital. This method is very ideal for those multinationals with local subsidiaries in the debtor country. The companies can buy up such funds from the creditor bankers and as they are redeemed in local currency, such funds are injected into their subsidiaries to serve as useful working capital, local loan repayment or tax payment.

(d) **Debt for Export:** In this case, export goods are exchanged for debt obligations. That is, items for exports are used to pay government external debt, but exporters are paid readily in local currency. For example, a sovereign debtor can export goods worth a particular amount in order to cancel external debt of that magnitude.

(e) **Debt for Debt Swap:** This refers to an external debt that is redenominated in local currency. This means that the external debt could be exchanged for domestic debt by selling it for cash in the secondary market.

The debt conversion committee (DCC) was established in July 1988 to implement Nigeria's debt conversion programme. One of the objectives of the programme is the improvement of Nigeria's external debt position by reducing the stock of outstanding external debt in order to alleviate the debt service burden. Essentially, it is aimed at stemming the tide of resource transfer

through the encouragement of capital inflow, repatriation of flight capital and recapitalization of enterprises in the private sector. Through the appropriation of the substantial discounts offered and the commissions paid, the country benefits and reduces it debt stock.

Transactions under the DCP recovered appreciably with the adoption of a more realistic exchange rate under the autonomous foreign exchange market (AFEM) in 1995 - (see table 2 below).

Table 2: Sectoral Breakdown of Applications Received for Debt Conversion

	1992	1993	1994	1995	1996	TOTAL
SECTORS	1	2	3	4	5	1992-1996
Agriculture	9	1	-	19	4	33
Manufacturing	15	5	-	45	33	98
Mining and Exploration	-	1	-	3	2	6
Building and Construction	3	1	-	13	5	22
Hotel and Tourism	-	-	-	3	2	5
Gifts and Grants	2	3	4	6	3	18
Financial	2	-	-	1	-	3
Services	3	-	-	14	7	24
Debt for Debt	-	1	-	4	-	5
Others	-	-	-	-	-	-
TOTAL	34	12	4	108	56	214
VALUE (US $ MILLION)						
Agriculture	63.0	10.0	0.3	134.4	42.0	249.7
Manufacturing	142.9	22.5	-	403.4	211.6	780.4
Mining and Exploration	-	1,000.0	-	30.0	111.3	1,141.3
Building and Construction	133.4	1.0	-	88.2	54.0	276.6
Hotel and Tourism	-	-	-	93.0	50.0	143.0
Gifts and Grants	82.3	27.1	186.5	9.8	78.3	384.0
Financial	36.5	-	-	5.0	-	41.5
Services	7.2	-	9.0	111.6	79.3	207.1
Debt for Debt	-	50.0	-	46.0	-	96.0
Others	-	-	-	-	-	-
TOTAL	465.3	1,110.6	195.8	921.4	626.5	3,319.6

Source: DCC Secretariat, Central Bank of Nigeria, 1997.

From the above data, applications received totalled 108 and 56 for external debt conversion valued at US $921.4 million and US $626.5 million in 1995 and 1996 respectively. This is compared with only 4 applications for US $195.8 million in 1994.

Table 3 shows auction sessions conducted in 1995 and 1996 in which external debt stock of US $73.6 million and US $157.4 million were redeemed. Additional debt of US $21.3 million and US $15.2 million were canceled through the out-of-auction system. The total debt redeemed under the DCP amounted to US $172.6 million in 1996 compared with US $94.9 million in 1995. External debt cumulatively valued at US $448.5 million was redeemed under the programme between 1992 and 1996.

Table 3

Summary of Debt Conversion up to December, 1996

		At Auctions			*Outside Auctions*			*Total*		
		1995 (1)	1996 (2)	1992-1996 (3)	1995 (4)	1996 (5)	1992-1996 (6)	1995 (7)	1996 (8)	1992-1996 (9)
1	**Amount Redeemed**									
a	US $Million	73.6	157.4	370.8	21.3	15.2	77.6	94.9	172.6	448.4
b	N Million	5918.8	12900	21564.4	1708.5	1225.1	3734.5	7627.3	14125.1	25298.9
2	**Discount Offered**									
a	US $Million	33.5	47.2	147.9	9.9	4	31.9	43.4	51.2	179.8
b	N Million	269.3	3480.3	7494.4	792.8	325.6	1464.9	1062.1	3805.9	8959.3
c	Average Discount %	45.5	29.2	-	46.4	26.6	-	45.7	-	-
3	**Proceeds**									
a	US $Million	40.1	116.9	229.6	11.4	11.2	45.7	51.5	128.1	275.3
b	N Million	3225.7	9419.7	14070	915.8	899.5	2269.6	4141.5	10319.2	16339.6
4	**Commission Paid**									
a	US $Million	1.2	4	6.6	0.3	0.1	0.9	1.5	4.1	7.5
b	N Million	14.3	56	75.8	5.7	0	8.2	20	56	84

Agency fee payments to chase Manhattan Bank of New York not deducted.
Source: DCC Secretariat, Central Bank of Nigeria 1997

The major factor that influenced the improved performance in 1995 and 1996 respectively was the liberalization of the foreign exchange market. This allowed sufficient margin on converted debts as against the policy in 1994. In this period, transaction were tied to the official exchange rate of ₦22.00 to US $1.00. In addition to the reduction in external indebtedness achieved through the programme, other benefits derived included the discount of US $179.8 million appropriated to the economy' US $7.44 million commission earned and the conversion for the purposes of cash/grants to non-profit making organisations valued at ₦84.0 million.

Total disbursements of domestic currency proceeds of debt converted stood at ₦9,618.1 million in 1996, compared to only ₦311.6 million in 1994. The total disbursement however, between 1992 and 1996 amounted to ₦15,820.8 million (see Table 4).

Table 4

Sectoral Distribution of Disbursement of Debt Conversion Proceeds (₦million)

SECTOR	1992	1993	1994	1995	1996	TOTAL 1992-1996
Agriculture	115.2	4.4	1.6	145.1	1110.0	1376.3
Manufacturing	617.5	52.7	0.6	2085.2	4298.3	7054.3
Mining and Exploration	-	-	-	-	2.3	2.3
Building and Construction	321.3	31.3	4.6	58.6	572.3	988.1
Hotel and Tourism	120.0	3.4	-	0.0	-	123.4
Gifts and Grants	89.0	121.3	196.6	784.5	1732.6	2924.0
Financial	-	-	-	-	-	-
Services	5.5	266.6	75.7	490.1	1312.6	2150.5
Debt for Debt	128.4	120.9	32.5	330.1	590.0	1201.9
Others	-	-	-	-	-	-
TOTAL	1396.9	600.6	311.6	3893.6	9618.1	15820.8

Source: DCC Secretariat, Central Bank of Nigeria 1997.

From the above table, it can be noticed that four sectors of the economy were the major beneficiaries of the proceeds (i.e of the applications, approvals-in-principle and disbursements) during the period 1992 to 1996. They were: the Manufacturing sector which received the highest of the proceeds with ₦7,054.3 million. It was followed by Gifts and Grants sector with ₦2,924.0 million, while Services and the Agricultural sectors received ₦2,150.5 million and ₦1,376.3 million respectively.

3.4. The Impact of D.C.P

The extent to which debt conversion can serve as an instrument of debt management in Nigeria can be examined through the benefits that would be derived from the implementation of the programme. In the past, the economy has been persistently bedeviled with problems such as shortage of foreign exchange; low level of foreign investment flows, low level of productivity, spiralling inflation, heavy debt burden, declining standard of living, unstable and declining value of the naira (devaluation), etc. The implementation of debt conversion scheme by a debtor Country could lead to the reduction of its debt and debt service obligations as well as encourage foreign capital flows with its attendant benefits on economic growth and transfer of technology.

Specifically, the conversion of some of Nigeria's debts into equity will make available substantial amounts of investible capital which can be channelled into the preferred sectors of the economy in order to increase the level of output and speed up the recovery process. This will solve the problem of low productivity currently facing Nigeria. Also, the introduction of a debt equity swap arrangement will increase the liquidity of the particular enterprises in which the investments are made. This will help in boosting the overall productivity in the economy.

In addition, a reduction of Nigeria's debt burden through securitization will result in lowering the amount of foreign exchange flowing out of the economy.

These could otherwise be used for debt repayment and servicing will be saved either for building up the country's external reserves or to procure inputs needed for increasing the level of productivity in the various sectors of the economy.

Debt equity conversion also entails an element of discounting of debt on the secondary market. The percentage of discounts appropriated depends on the prevailing secondary market discounts of the debt at the time of conversion. This discount will constitute a built in savings for the country. Moreso, if the gains from the discounting are well utilized, a part of Nigeria's external liability will be translated into a domestic asset. The effect will be the expansion of the economy and generation of new business opportunities.

Again, the flight of capital from the country through official and unofficial channels is due to the recession in the economy and the uncertainty which it has created in business circles. If the level of productivity is increased through debt equity conversion in the country and part of renewed growth is embarked upon, then the tide of capital flight will be stemmed or reversed.

Since the debt-equity conversion will make more investible capital available to the country, the government can take the opportunity to channel investments into domestic raw materials production to meet the needs of industrial enterprises. With the increased investment capital that will flow from a debt

equity conversion deal, the government can encourage the expansion of such business concerns that obtain most of their inputs locally and the creation of new ones. This will help to strengthen the economic foundation of the country and help create a more sectoral balanced system of accumulation. Though, this is subject to profit repatriation on the economy and depends on how it is managed. However, investible capital from debt conversion deals can be channelled into ventures that will encourage the commencement of export oriented industrialization in Nigeria. This will boost the country's foreign exchange earnings.

The gains of debt securitization also could be tied to agricultural projects aimed at making the country self sufficient in basic food items, and improving the production of primary commodities which will help to diversify the export base of the country.

Debt conversion can provide a useful link to privatization programme because it will help make funds available for the rationalization of all public enterprises that are marked for privatization. This will bring about a massive injection of capital into many public enterprises.

Finally, other benefits of debt conversion include the widening of the revenue base of the government through taxes, fees and royalties, also the general increase in the tempo of domestic economic activities is bound to increase

income levels and generate more employment opportunities in the country; the financial confidence of the international community will be strengthened and the country will be in a position to enjoy more favourable terms for the rescheduling of the remaining portion of it's debt that has not been converted. Inspite of these positive impacts that D.C.P could have, there are some probable draw backs of the programme.

First, for the strategy to have a meaningful impact on the economy, a large proportion of the country's external debt will have to be converted, yet the absorptive capacity of the economy is limited. This sets limit to the amount of Nigeria's external debt that can be converted into equity. This suggests that the amount of debt that can be converted or securitized within the limits of what the economy can absorb will be so low as to be really inconsequential to the basic problems facing the country.

However, due to the low absorptive capacity of the economy, only an insignificant proportion of the country's external debt can be securitized. It therefore means that the repayment and servicing burden which the nation is presently carrying is not likely to be lightened in the foreseeable future. The implication of this is that the problems and difficulties which have been posed by the country's heavy debt burden are likely to persist for sometime inspite of the debt conversion scheme.

Debt conversion programme could lead to inflationary pressures in the economy because the supply of local currency in exchange for foreign debt increases the domestic money supply. However, this can be mitigated by exchanging government bonds for external debt.

Again, DCP could lead to increased pressure of foreign exchange market (FEM) due to the increased liquidity in the system. This pressure on the exchange market will result in the depreciation of the external value of the naira. The socio-economic implication of this is that there might be a decline in industrial capacity utilization, which is as a result of the decline in the external value of the naira, thereby making importation expensive. The effect of this is a further reduction of the country's productive capacity, leading to unemployment and reduction of the prospects of faster economic recovery.

A more drastic limitation that is feared is that DCP could lead to a serious alteration of the ownership structure thereby bestowing the commanding position of economic power on foreigners. A development of this nature makes the local economy vulnerable to international shocks. This is because, such enterprises would be operated purely on profit motive with little or no national interest, speculation on changing global business situation would impact on the investments in these enterprises, hence, their effect on the domestic business environment. Part of the problem of Malaysian and Indonesian economies are cases in point.

Finally, DCP could lead to strong competition for investment between the holders of the Nigerian debt and normal foreign investors. They will find it hard to resist the temptation of buying Nigerian debt instruments at a discount and then take advantage of the devaluation of the naira when they come to redeem the naira equivalent of the amount they have converted. The end result is an obstacle to the attraction of fresh foreign investment into the country.

3.5 OTHER APPROACHES OF DEBT REDUCTION

A part from the management strategies mentioned above, other instruments for resolving the international debt crisis which became pronounced since 1982 moved from a set called the traditional types to the current ones emphasizing the choice from a `menu' of options. Although the debt problem is seen as an issue between the creditors and debtors, if not resolved, the international economy could suffer given the interrelationship that exists between the economies.

3.5..1 The Traditional Instrument

These instruments of external debt management have aimed at providing relief to the indebted country especially where the burden of debt is very high. This according to Ojo (op.cit pg.54) was the basis of the rescheduling/refinancing agreements discussed earlier where various techniques could be applied. In Nigeria for instance, the techniques of currency redenomination and interest

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rates options were applied. Currency redenomination allows a debtor country to diversify the currency of its debt to other currencies with lower interest rates which could reduce debt service payments. The interest rate option allows the use of an interest base such as LIBOR to which a spread is added. This may lower refinancing and intermediation costs as well as reduce the risks of future increases in market interest rates.

Other traditional techniques of debt management that have not been employed by Nigeria apart from the debt conversion programme include:

3.5.1.1 Interest Retiming: Which extends the interval between interest payments and permits a debtor country to postpone one or more interest payments.

3.5.1.2 On-lending: - It permits the proceeds of a new loan to be transferred to a new debtor who assumes the repayment by the original borrower.

3.5.1.3 Re-lending: - This involves lending repaid proceeds of an outstanding debt to another borrower in the same country. Both on-lending and re-lending usually involves a shift of exposure from public to private sector which tends to reduce the credit risks.

3.5.1.4 New Trade credit: This technique allow creditor banks to extend new money to private sector agents for trade transactions.

3.5.1.5 Co-financing: In this arrangement, creditor banks link their loans to lending from multilateral development institutions like the world bank which are usually responsible for project appraisal, supervision of implementation and loan administration.

3.5.2 THE MENU APPROACH

This approach provides a lot of incentive to both the creditor banks and debtor countries. This is because it expands the available options under rescheduling and new money agreements as used traditionally. Some of the numerous options include:

3.5.2.1 Debt securitization: This involves the exchange of debt for more tradeable financial instruments, thereby allowing the creditor banks to restructure their portfolios. Securitization could be done by the issue of securities to refinance existing debt, while creditor banks or their agents can also issue securities backed by existing loans. In 1983, Nigeria applied a limited version of this technique when the trade debt was converted into promissory notes.

3.5.2.2 Interest Capitalisation: This aims at reducing interest service directly by adding interest payments due to the outstanding loan. This option is really used especially in low income countries since it is an extreme case where postponement of interest payment makes a lot of difference to a debtor country.

3.5.2.3 Exit Bonds: It is also referred to as the alternative participation instrument. This technique was devised to rationalise contributions by big and small lenders. Under the Paris Club rescheduling, the technique involves exemption of banks with exposure below a specified amount of requests to participate in new money packages. It also permits creditor banks to reduce their base exposure for calculating new money contributions by up to the same specified limit. The exit bond have a fixed low interest rate and a long maturity as applied in 1987 in the case of Argentina.

3.5.2.4 Debt Buy-Back: This is a technique which allows debtor countries to repurchase a portion of their debt at a discount, while the remaining debt will be restructured. The debt buy-back operation could be negotiated between the debtor and the creditors (as in the case of Bolivia) without resort to the secondary market. Moreso, foreign exchange obtained from donor governments would be used to effect the transaction.

3.6 THE COOPERATIVE APPROACH

The debt crisis in the developing nations have led to series of international debate. While the industrial nations belief that the debt crisis was caused mainly by the bad economic policies in the indebted developing countries, the developing countries supported by objective analysts argue that the root causes of the debt crisis can be traced to the economic policies of the major industrial countries.

However, it is now accepted that the persistence of the debt crisis is dangerous to the growth of the world economy. Thus, many proposals of a cooperative nature which recognise the interdependence of world economies have been put forward to form a unique set of approaches to the debt crisis and possibly make a positive impact in the future. Among the numerous proposals are the Baker plan, the Brady plan, an International debt adjustment facility etc.

3.7 INTERNATIONAL PROPOSALS FOR DEBT RELIEF

The international proposals for debt relief was informed by Mexico debt crisis signals in 1982. In that year, Mexico announced to its Commercial Bank creditors its inability to meet scheduled debt service obligations and consequently sought a concerted rescheduling. Argentina, Brazil and Chile followed same part so that by the end of 1984, not less than 20 countries had signalled their inability to meet their debt payment obligations (Fashanu, 1995). The first reaction to that was an initiative in 1982 which would ensure

that debtor countries generate trade surpluses which would permit the restoration of full debt service. However, the initiative did not achieve the desired result as the economic growth of debtor countries remained sluggish.

To restore a global economic order, multilateral organisations, governments and individuals came up with new initiatives to try to resolve the debt crisis. Table 5 shows the grouping of debt distressed Countries:

Table 5: International Debt Relief Proposals

Low-Income Countries	Middle-Income Countries
Venice Terms (1987)	Baker Plan (1985) (Commercial Debts)
Toronto Terms (1990)	Brady Plan (1989) (Commercial debts)
Trinidad Terms (1990)	Houston Terms (1990) (Official debts)
Enhance Toronto Terms (1991)	
Naples Terms (1994)	

Source: Adapted from Omoruyi S. E. (1996)

These initiatives were directed at either the severely indebted low-income countries (SILICS) or the severely indebted middle income countries (SIMICS). However, only the SIMICs will be treated in this study because Nigeria fell under the beneficiaries in this category.

3.7.1 The Baker Plan, (1985):

The major elements of the strategy were the implementation of Adjustment Programmes by debtor countries. The plan called for a comprehensive macro-economic reforms to be supported by the international financial institutions - the World Bank and the IMF. The plan has it that the Paris Club would not enter into any debt relief negotiation unless an appropriate adjustment programme is under implementation (Omoruyi, 1996:15).

3.7.2 The Brady Plan (1989)

This plan was a product of the mixed result obtained from the Baker plan. This is because some debtor countries experienced a negative resource transfer and consequently the environment for a sustained growth could not be achieved (Fashanu, 1995:89). The Brady plan allowed for debtor countries either to buy back outstanding loans at a discount or exchange them for securities. This would result in reducing their principal payments or the total debt service obligations. The IMF and World Bank were to provide funding, while the commercial banks would provide debt reduction and new money to the eligible country. A precondition for any benefiting debtor country would be a growth oriented adjustment programme put in place.

3.7.3 The Houston Terms (1990)

Under these terms, Official Development Assistance (ODA) loans were to be rescheduled with a 20 years maturity, including up to 10 years of grace.

Exports credit and non - ODA official loans were to be rescheduled with a 15 year maturity including up to 8 years grace period. Creditor countries could sell or swap the entire ODA loans and a limited amount of non-concessional credits (usually 10% of the outstanding claims or $10 million, which is higher) through debt conversion programmes.

3.7.4 Application of International Debt-Relief Packages

In 1986, after considering all the available options, Nigeria thus availed herself of the opportunity offered by the Baker and Brady Plans. In line with this initiative, the Country was expected to come to an agreement with the IMF and the World Bank on restructuring the economy. The World Bank was to play a leading role including the provision of new money.

In order to revamp the economy, the Structural Adjustment Programme (SAP) was introduced in 1986. It involved measures that would alter and realign aggregate domestic expenditure and productive pattern so as to minimise dependence on imports, enhance the non-oil export base and bring the economy back on the path of steady growth.

In line with both the Baker and Brady plans, the IMF and the World Bank supported Nigeria's rescheduling proposals. In the case of IMF, endorsement was secured under the so called classical stand-by arrangement, entailing

translation of SAP into a sequence of phased programmes with their evaluation of performance indices (Fashanu 1995:91).

The introduction of SAP could not only change for good the economic situation, and in particular, the debt state of the nation. Despite the costs and protracted nature of the rescheduling agreements and the promise to provide new money, the commercial banks did not provide any new money according to the plans (Fashanu 1995:94). Instead, Nigeria paid the banks a total sum of $1,902.28 million between 1988 and 1990 for debt service. Debt service payments subsequently outstripped new disbursements during the period resulting in negative resource outflows which militated against the achievements of the structural adjustment objectives.

Suffice to say here that the introduction of SAP and the failure of creditors to provide additional inflow of financial resources resulted in fundamental changes in the life of the Nigerian populace. There was drastic decline in real wages while unemployment increased.

Finally, the proposals mentioned above share one central objective; the reduction, if not elimination of the debts of distressed low and middle income countries. However, it has been observed that despite these proposals, the terms of financial arrangement between the developed and developing nations have not succeeded in drastically reducing the debt stock of the developing

nations which is weighing down their development efforts. Rather, it has succeeded in subjecting them to debt servicing obligations at the detriment of domestic growth and development.

CHAPTER FOUR

4.0 DATA ANALYSIS AND INTERPRETATION OF RESULTS OF ESTIMATED EQUATIONS

This chapter is divided into two parts. The first focuses on the debt trend and structure while the second part is the data analysis proper.

4.1 THE DEBT TREND AND STRUCTURE

The singular act of contracting a $1 billion loan (mentioned earlier in the introductory chapter) in 1978 changed the character and structure of Nigeria's external debt. Over the years, Nigeria's external debts have grown in leaps and bounds, and so is the debt service payments. The Nigeria external debt outstanding for instance, rose from only ₦0.37 billion in 1976 to a staggering ₦328.1 billion ($33.7 billion) in 1991. This figure came down to ₦617.3 billion ($28.1 billion) in 1996. While the debt service payments expended in 1976 was ₦0.03 billion, the figure rose to ₦8.9 billion by 1986. The decline in 1987 could not be sustained as the figure resumed an increasing trend in 1988 from ₦11.3 billion to ₦74.4 billion in 1993. From 1994 to 1996, the debt service payment decreased from ₦69.4 billion to ₦64.0 billion, (see table 6 below).

TABLE 6

NIGERIA: DEBT STATISTICS

YEAR	External Debt Outstanding	Debt Service Payments	Value of Total Exports	Government Total Collected Revenue	Interest Payments	GDP at Current Factor Cost	External Reserves	Exchange Rate to US$
	Naira (billion)	Naira (billion)	Naira (billion)	Naira (billion)	Naira (billion)	Naira (billion)	Naira (billion)	Naira (billion)
1976	0.37	0.03	6.62	6.77	0.01	26.66	3.06	0.63
1977	0.50	0.03	7.88	8.04	0.02	31.52	2.52	0.65
1978	1.27	0.16	6.38	7.37	0.10	34.54	1.25	1.61
1979	1.61	0.18	10.40	10.91	0.12	41.95	3.04	0.60
1980	1.90	0.90	14.20	15.23	0.10	49.63	5.45	0.55
1981	2.30	0.90	11.03	12.18	0.31	50.46	2.42	0.61
1982	6.80	1.00	9.20	11.76	0.45	51.57	1.03	0.67
1983	8.60	1.50	7.75	10.51	0.44	56.71	0.78	0.72
1984	12.10	1.80	9.14	11.19	0.78	63.01	1.14	0.76
1985	14.00	2.50	11.72	14.69	0.98	71.37	1.64	0.89
1986	31.00	8.90	9.05	12.30	0.99	72.13	3.59	2.02
1987	100.80	7.50	29.58	25.10	2.37	106.88	4.64	4.02
1988	141.10	11.30	31.19	27.60	5.48	142.68	3.27	4.54
1989	240.10	16.30	57.97	47.80	8.59	222.46	13.46	7.39
1990	297.90	39.50	109.89	85.25	15.37	257.87	34.95	8.04
1991	328.10	46.00	121.53	100.99	15.91	320.25	44.25	9.91
1992	544.30	65.80	205.61	190.45	11.20	544.33	13.99	17.30
1993	633.10	74.40	154.69	192.77	10.90	695.99	67.25	22.33
1994	648.80	69.40	206.29	201.91	20.90	908.49	30.46	21.89
1995	716.80	69.70	193.81	459.99	17.30	1,430.58	31.62	21.89
1996	617.30	64.00	213.16	520.20	19.80	1,601.39	48.90	21.89

SOURCES:

1 Central Bank of Nigeria: Statiscal Bulletin Vol.7 No. 1 June, 1996

2 Central Bank of Nigeria: Major Economic, Financial and Banking Indicators, Research Department, April, 1997

3 Uniamikogbo, S.O: In Africa Debt Burden and Economic Development. N.E.S 1994, Annual conference.

Table 6 shows that Nigeria's external debt which increased unabatedly, experienced a respite in 1992 (see table 7 for the dollar equivalent). This was as a result of the substantial decline that materialised in the debt buy-back arrangement with the London Club of private/commercial bank creditors. Under the buy-back arrangement, debts worth $2.2 billion were extinguished through 60% discount on 62% of debts that were bought back. The remaining 38% was rescheduled over a 30 year period with the backing of the US Treasury Zero coupon collaterised per Bond (Ojo 1997). The Brady Plan on debt service and debt reduction was beneficial to Nigeria. Moreso, the seriousness with which the Central Bank of Nigeria pursued the reconciliation of the debts that were mainly on account of short term payment arrears, and the subsequent refinancing and restructuring agreement which were climaxed by the secondary market effort saw to the remarkable success in the rescheduling of the London Club debts.

The debt stock resumed an upward movement in 1993 to 1995 when the level reached the peak of ₦716.8 billion $32.6b). In 1996, the debt stock dropped sharply to ₦617.3 billion ($28.16) (see table 6). This decline was as a result of a number of factors which include: the exclusion of penalty charges, discount arising from the debt buy-back operation, as well as exclusion of projects (with the outstanding loans) which were either distressed or have failed outrightly (Ojo 1997).

An additional factor was the reporting of promissory notes at their real value instead of nominal value as the practice had been. The revaluation exercise resulted in the declining of outstanding debts on promissory notes from $3.1 billion in 1995 to $2.1 billion in 1996 (see table 7 below). This means that if the revaluation was undertaken for earlier years, the drop in promissory notes would have been less significant.

Moreover, a glance at table 7 shows that the bulk of outstanding debts owed to the Paris Club of official creditors amounted to 68% of the total in 1996 as against 66% in 1995. This increase is accounted for by the drop in promissory notes debts, in addition to the sharp drop in other unclassified debts. However, the magnitude of Paris Club debts in real terms which had maintained a steady rise dropped from ₦476.7 billion ($21.7b) in 1995 to ₦420.0 billion ($19.1 billion) in 1996 (see table 7). This is on account of the reconciliation in respect of distressed and failed projects sponsored with Paris Club loans. This disproportionately large share of Paris Club debts and their harsh rescheduling terms imposed by the club have been a major problem for Nigeria's debt restructuring efforts.

TABLE 7

NIGERIAN EXTERNAL DEBT OUTSTANDING BY HOLDERS

	HOLDERS	US $ MILLION								N MILLION							
		1989	1990	1991	1992	1993	1994	1995	1996	1989	1990	1991	1992	1993	1994	1995	1996
1	Multi lateral	2,807.00	3,845.10	4,016.00	4,518.00	3,694.70	4,402.30	4,411.00	4,665.00	21,473.50	34,578.40	39,058.80	89,274.30	81,456.30	97,056.60	97,042.00	102,630.00
2	Paris Club	15,847.00	17,172.10	17,793.00	16,433.90	18,160.50	18,334.30	21,669.60	19,091.00	121,229.60	154,540.70	173,051.20	324,729.90	400,380.90	404,212.60	476,731.20	420,002.00
3	London Club	5,600.00	5,936.80	5,988.00	2,120.00	2,055.80	2,057.80	2,045.00	2,043.00	42,480.00	52,749.60	58,238.10	41,890.60	45,323.80	45,367.90	44,900.00	44,946.00
4	Promissory Note	4,584.00	4,550.00	4,479.00	3,246.00	3,159.90	3,178.20	3,148.00	2,140.00	35,067.60	40,950.40	43,561.90	64,140.00	69,665.70	70,069.10	69,256.00	47,080.00
5	Others	2,586.00	1,675.00	1,454.00	1,226.20	1,647.30	1,456.30	1,311.20	121.00	19,782.90	15,075.20	14,144.30	24,229.30	36,317.70	32,106.80	28,846.40	2,662.00
	Total Debt OUTSTANDING	31,424.00	33,179.00	33,730.00	27,544.10	28,718.20	29,428.90	32,584.80	28,060.00	240,033.60	297,894.30	328,054.30	544,264.10	633,144.40	648,813.00	716,775.60	617,320.00

SOURCES:

1 *Central Bank of Nigeria, Annual Report and Statement of Accounts, 1992, page 68*
2 *Central Bank of Nigeria, Annual Report and Statement of Accounts, 1997, page 83*

Since 1992, payment to the Multilateral institutions/creditors represented the largest single outflow on debt servicing. This is because of the non reschedulable and non default clauses in the terms of acquiring and servicing such loans.

The servicing of the Paris club debts on the other hand, has remained relatively low. This is owing to the insistence of the club on Nigeria reaching a prior agreement with the Bretton Woods institutions before concrete agreement can be negotiated for debt restructuring (Ojo 1997, Obadan 1997).

4.2 DATA ANALYSIS

A reference to Table 6 shows variables in their magnitude employed in the study. Between the period 1976-1996, the general trend of the data has been in upward direction even though, the devaluation of the Naira did inflate some of them like the external debt outstanding.

Table 8 contains figures of ratios of the variables in Table 6. The computation of the ratios is justified on two grounds:-

(i) There is the need to compare these ratios with their internationally adjudged critical level in order to further understand and appreciate the severity of the debt problem

(ii) As a point of departure from other works in the area, to adopt these ratios as working variables in our statistical analysis. It is believed that doing so would allow us identify and recommend the working tools that can be employed in managing Nigeria's external debt.

Table 8: Selected External Debt Ratios, 1976 - 1996 (in Percentages)

YEAR	EDO/EXP	DSP/GDP	DSP.EXP	IP/EXP.	DSP/GTR	ERN	EDO/ER	EDO/GDP
1976	5.6	0.1	0.5	0.2	0.4	0.6265	12.1	1.39
1977	6.3	0.1	0.4	0.2	0.4	0.6466	19.8	1.59
1978	19.9	0.5	2.5	1.5	2.2	1.6060	101.6	3.68
1979	15.5	0.4	1.7	1.1	1.7	0.5957	53.0	3.84
1980	13.4	1.8	6.3	0.7	5.9	0.5464	34.9	3.83
1981	20.9	1.8	8.2	2.8	7.4	0.6100	95.0	4.56
1982	73.9	1.9	10.9	4.9	8.5	0.6729	660.2	13.19
1983	111.0	2.6	19.4	5.6	14.3	0.7241	1102.6	15.16
1984	132.4	2.9	19.7	8.6	16.1	0.7649	1061.4	19.20
1985	119.5	3.5	21.3	8.4	17.0	0.8938	853.7	19.62
1986	342.5	12.3	98.3	10.9	72.4	2.0206	863.5	43.00
1987	340.8	7.0	25.4	8.0	29.9	4.0179	2172.4	94.31
1988	452.4	7.9	36.2	17.6	40.9	4.5367	4315.0	98.89
1989	414.2	8.7	33.3	14.8	40.4	7.3916	1783.8	107.93
1990	271.1	15.3	35.9	14.0	46.3	8.0378	852.4	115.52
1991	270.0	14.4	37.9	13.1	45.5	9.9095	741.5	102.45
1992	264.7	12.1	32.0	5.4	34.5	17.2984	3890.6	99.99
1993	409.3	10.7	48.1	7.0	38.6	22.3268	941.4	90.96
1994	314.5	7.6	33.6	10.1	34.4	21.8861	2130.0	71.42
1995	369.8	4.9	36.0	8.9	15.2	21.8861	2266.9	50.11
1996	289.6	4.0	30.0	9.3	12.3	21.8861	1262.4	38.55
WBCL	275%	20%	50%	20%				50%

Source: Computed from table 6

In structuring the study model, the ratio of debt service payment to total exports (commonly proxied for external debt burden) is chosen as the dependent variable. The choice of this ratio is informed by the fact that the whole idea of debt management revolves around the need to reduce the burden suffered by a nation and its people. Where the burden is not excruciating, too much concern may not be attached to its management as the external debt would not be a problem. This is not the case in Nigeria. For a developing economy that is in dire need of foreign exchange for its development programmes and projects but continuously strangulated by a pending debt servicing, the choice of these variables may be quite appropriate.

4.3 THE STRUCTURAL EQUATIONS

The structural equations emanating from the model and their expected signs are as follows:-

$$Y_1 = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 \quad \ldots\ldots\ldots\ldots\ldots\ldots \quad 1$$

$$Y_1 = \alpha_0 + \alpha_1 X_7 \quad \ldots\ldots\ldots\ldots \quad 2$$

$$Y_2 = \delta_0 + \delta_1 X_2 + \delta_2 X_5 + \delta_3 X_6 \quad \ldots\ldots\ldots\ldots\ldots \quad 3$$

Where

Y_1	=	Debt Service Payment to Export
X_1	=	Debt Service Payment to Gross Domestic Product at factor cost
X_2	=	External Debt Outstanding to Export
X_3	=	Interest Payment to Export
X_4	=	Debt Service Payment to Government Total Collected Revenue
X_5	=	Exchange Rate of the Naira
X_6	=	External Debt Outstanding to External Reserve
X_7	=	External Debt Outstanding to Gross Domestic Product
Y_2	=	Debt Service Payment

The estimated equations of our model are :

$$Y_1 = \underset{(0.96)}{2.23} - \underset{(-2.20)}{2.47X1} + \underset{(1.11)}{0.02X2} + \underset{(2.12)}{2.08X3} + \underset{(2.92)}{1.18X4} + \underset{(3.15)}{0.76X5}$$

$$+ \underset{(2.89)}{1.39X6} \quad \text{.....} \quad 4$$

$R^2 = 0.883 \qquad R^2 = 0.833 \qquad F = 170.628$

$$Y_1 = \underset{(2.65)}{9.87} + \underset{(3.58)}{0.21X_7} \text{----------} 5$$

$R^2 = 0.40 \qquad R^2 = 0.37 \qquad F = 12.81$

$$Y_2 = \underset{(0.25)}{0.53} + \underset{(2.30)}{3.69X_2} + \underset{(7.11)}{3.32X_5} + \underset{(3.31)}{4.56X^6} \text{----------} 6$$

$R^2 = 0.96 \qquad R^2 = 0.96 \qquad F = 153.88$

From the structural equations specified, equation 1 aims at measuring the determinant of the debt burden by making the ratio of debt service payment to exports, the dependent variable on six other explanatory variables. These include ratios of Debt service payments to Gross Domestic product at current factor cost, External Debt outstanding to Exports, Interest Payments to Exports, Debt service payments to Government total collected revenue, Exchange rate of the naira and External debt outstanding to External reserves.

The argument as to the use of these ratios in measuring their respective influence on the debt burden is informed by the desire to understand the working of any management policy put in place with respect to Nigeria's

external debt. It is not enough to propose a cut in external borrowing as that would sound unrealistic especially when other actions that would guarantee good source of investment finance are not put in place. In as much as the resource gap remains, borrowing becomes inevitable to bridge the gap. The equations are therefore, stated in a form that would permit pursuing other ways of generating financial resources to cover the inherent gap.

A look at the estimated equation 4, for instance, shows that except for the variable X_1, (ratio of Debt Service Payment to Gross Domestic Product), all other variables are positively related to the debt burden. Also, except for X_2 (ratio of external debt outstanding to total exports), all other variables prove to be significant. The respective t-ratios (in paranthesis) further confirm their significance at 5 percent level ($t_{.025}$).

The positive values of X_2, X_3, X_4, X_5, X_6 signify the direct relationship between the debt burden and the respective variables. This means that a reduction of the debt burden can be achieved only through the reduction of values of the respective ratios.

For instance, even though the sign of the variable X_1 does not conform with the a priori expected sign, the significance of the variable is indicative that an expansion/increase in GDP would lower the ratio of X_1 and a lower X_1 should be indicative of a reduction in debt burden. Similarly, lower X_3 and X_4

implies debt burden reduction. Of course, X_3 and X_4 can be lower only through expansion/increase in exports (for X_3) and increase in government total revenue collected (for X_4). The other question maybe how do we expand GDP, Exports and Government Revenue collected? Though such a proposal may not sound anew, it is however worth commenting on. A resourcefully endowed economy like that of Nigeria (both humanly and materially) has a lot of potential opportunities for expanding her GDP. Expansion can come about through effective employment of idle and under utilised capacity and where there is a sincere commitment to that, the ICOR (Incremental Capital Output ratio) should be low given the relatively cheap and advanced technology of production already developed in the industrialised countries.

It also follows that where and when domestic production has grown large, there is more than enough for domestic consumption, hence, exports. Nigeria strategically stands a better chance of capturing the West African Sub-regional Market in particular and of course, the African Market in general. This is an opportunity that Egypt and South Africa have begun to avail themselves.

The R^2 and R^2 adjusted (coefficients of determination) of explanatory variables in the equation against the dependent variable Y_1 are large. R^2-adjusted, provides that 83.3 percent of the variation in the ratio of debt service payments to exports (proxied for debt burden) is explained by the variables X_1, X_2, X_3, X_4 X_5 and X_6. The non significance of the autonomous

component is indicative of the extent to which our chosen variables exhaustively explain the behaviour of Y_1. The F-statistics test the significance of the multiple regression coefficient and the coefficient of determination. With respect to equation 1, the F-statistics value is a further confirmation of the significance of the coefficients and that of their determination.

The second estimated equation 5 is also measuring the debt burden against one variable X_7 (ratio of External Debt Outstanding to Gross Domestic Product at current factor cost). The marginal value of the explanatory variable is only 21 percent though significant as shown by the t-value 3.58. Also the high and significancy of the autonomous or constant term is indicative of other influences on the debt burden. However, because of the inexhaustiveness of the explanatory variables in that equation, the coefficient of determination is relatively small. R^2-adjusted has it that only 37 percent of the variation in Y_1 is explained by X_7. This is further buttressed by the very low value of the F-statistics.

The third estimated equation 6 has a multiple regression of Y_2 (Debt Service payment) on X_2, X_5 and X_6. The chosen variables are statistically significant as their marginal values are all above 300 percent. Their respective t-ratios have further buttressed the significance of the explanatory variables. The coefficient of determination (R^2-adjusted) provides that 96 percent of the

variation in Y_2 is explained by the variables X_2, X_5 and X_6. The significance of the variables is further proved by the F-statistics value.

Drawing from the entire regression result, we can conclude that it is not enough to direct debt management action on strategies like debt conversion, debt rescheduling, refinancing and restructuring of the debt portfolio. This is because these are short term management strategies that cannot solve the debt problem in the long run. Rather, long term management strategies should be sought so that while we might not be totally debt-free, we can at least aspire to be burden-free. (A situation where and when the principal and interest payments do not significantly deny the domestic economy the needed resources for investment and provision of adequate social services for the citizenry).

CHAPTER FIVE

5.0 SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 SUMMARY

The genesis of Nigeria's external debt problems as well as the need for debt management efforts have been discussed in this study. This is because the Nigerian external debt problem has been a lingering issue for quite sometime. The root of Nigeria's debt problem was traced to the substantial increases in the debt from 1978 when Nigeria resorted to contracting huge loans from the International Capital Market (ICM). The large loans were of shorter maturities, shorter grace periods, higher and variable interest rates leading to the bunching of debt and heavy debt service burden.

The debt problem was also traced to the fall in crude oil prices in 1978 with the resultant decline in foreign exchange earnings and balance of payments pressures. Other causes of Nigeria's external debt problem were traced to the continuous worsening of the terms of trade, the declining foreign exchange resources when they were most needed, inappropriate fiscal/monetary and exchange rate policy measures.

The need for tracing the origin and causes of the Nigerian external debt problem was to permit some assessment of the current management efforts of the debt and what other options are available for reducing the debt burden in

the future. Also, policy pronouncements were made regarding the need not only to limit the acquisition of new foreign loans but also on how to settle the already contracted debt.

This fiscal scenario gave rise to the need for an effective debt management efforts. The idea was to provide a good estimate of foreign financial requirements and the sources of the fund. It was also to provide a proper monitoring and documentation (of the debt profile), and financial prudence at the domestic level. Above all, the need arises in order to match the country's foreign borrowing with overall economic performance and the ability to pay back so as to avoid balance of payment crisis.

Based on this assessment, Nigeria attempted to reduce her debt burden through negotiations aimed at debt relief and debt reduction which has resulted in lower debt service payments among several options. The principal instruments of this management strategy have been the embargo on external borrowing, debt refinancing and rescheduling, structural adjustment programme and debt conversion in the form of debt equity swaps, debt for cash, debt for exports, etc. The effect of these measures on the total debt stock has not been significant because they are short term measures and Nigeria has only minimally applied all the tools of debt management.

Contrary to the short term approach used, this study opted to analyse the debt situation and the management strategies from the long term perspective. Hence the application of international debt relief proposals such as the Baker Plan, the Brady Plan and the Houston Plan among others.

5.2 CONCLUSION

The findings of this study show that it is not enough to direct debt management efforts on strategies like debt conversion, debt rescheduling, restructuring and refinancing because they are short term management strategies that cannot effectively address the nation's debt situation in the long run.

Secondly, from the various policies and strategies employed, it was realised that there was no significant change in the external debt situation. This was due to the increasing trend in the total debt outstanding.

Finally, inspite of the cost and protracted nature of the rescheduling agreements, and the promise to provide additional inflow of financial resources (new money) by the creditors, it was realised that the banks did not provide any new money according to the plans. This made the problem of adjustment more burdensome and the resultant effect is a fundamental change in the life of the populace due to drastic decline in real wages and high rate of unemployment. It is therefore essential that the nation takes a fresh stand on

the debt issue so as to enable her grow out of the debt burden and occupy a place of pride in the global economic arena of the next millennium.

5.3 Recommendations

Based on the findings of the study, some suggestions on long-term debt relief measures are hereby advanced.

5.3.1 The reduction or cancellation of interest payments and actual cancellation of a significant proportion of foreign debts. This can be achieved within the framework of international relief proposals and terms that are in existence.

5.3.2 Debt rescheduling should be accompanied with other debt relief measures such as interest rate reduction, debt cancellation and debt buy back.

5.3.3 Debt management needs to be part of a sound macro-economic policy. In other words, it does not start only when there is a crisis. On a continuous basis, Nigeria must scientifically determine the volume (how much to borrow), terms and conditions of borrowing from the private and commercial sources. This is in order to avoid a mismatch between benefits stream and repayment of debt.

5.3.4 There is need to meticulously monitor the amount of debt owed at every point in time. This should be related to the economy's absorptive capacity for

foreign capital and ability to service the debt without experiencing external payments problems.

5.3.5 Government authorities should authenticate debts and debt servicing should be secondary to feasible satisfaction of basic national needs.

5.3.6 There is need to make borrowed external funds productive to ease infrastructural bottle necks, expand productive base as well as invest in human resource development. Moreover, the need to ensure that the growth of exports and income exceeds the growth of debt and interest rate is very vital. It is only when the interest rate exceeds the growth of both the GDP and exports that debt stock and debt ratios grow on an explosive and unsustainable path.

5.3.7 Government should try to encourage outward orientation of its products as it results in a more rapid growth of exports. High level of exports create an equally high level demand for imports of various capital and intermediate goods. This will lead to competition with foreign producers which raise efficiency and there maybe externalities associated with exporting that cause open economies to grow more rapidly over long period of time.

5.3.8 Finally, there is need for policy instruments to be implemented harmoniously and consistently in order to be effective in debt reduction. Thus,

macroeconomic policies such as fiscal, monetary and exchange rate policies should be harmonized and consistent. Moreover, policy continuity helps to strengthen credibility and stability while equitable distribution of income reinforces credibility by minimising social and political tension.

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