ECONOMIC EMERGENCY IN NIGERIA

Edited by U.C. NZEWI

EXTERNAL DEBT CRISIS AND STRUCTURAL ADJUSTMENT PROGRAMMES: THE NIGERIAN CASE, 1980 — 1986.

by

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Abstract

Nigeria's balance of payment's position has been adverse since 1981 exerting severe pressure on her foreign exchange position. Nigeria has used a combination of exchange controls and fiscal and monetary policy measures to restrict the high import propensity of Nigerians which has resulted in the persistent external disequilibrium. These measures though severe have not been adequate to correct the external imbalance. In the interim Nigeria's trade debts have mounted and her credit worthiness plummeted. Goods can no longer flow as before. Since the nation's industrialisation efforts are geared towards refining foreign raw materials with very low domestic value added, her industries are closing down and employment position getting worse. It is the contention of this paper that an I.M.F. package would help restructure the economy through its hackneyed conditionalities and provide relief for the revitalization of the nation's industries, increase employment and reduce socio-economic problems. Though Nigeria had rejected the loan, it is still of academic interest. The creation of a 2nd tier foreign exchange market and Nigeria's request for I.M.F. approval of her structural adjustment programmes could substitute for the I.M.F. loan and achieve almost the same results.

Introduction

Nigeria has suffered from balance of payments disequilibria since 1981. In consequence, the nation's foreign exchange reserves are seriously drawn to accommodate the high import propensity of Nigerians and the resulting burgeoning deficits in the balance of payments. Nigeria's foreign exchange reserves fell from a high figure of N7 billion in 1981 to below N1 billion in 1982, a figure hardly adequate to finance two months import bill, a position dangerously below the minimum range of four months import bill prescribed by the I.M.F.

In order to reduce the high propensity to import, Nigeria introduced more comprehensive exchange control measures under the Economic Stabilization (Temporary Provisions) Act of 1982. A comprehensive exchange control measure was adopted with the objective of reducing the country's foreign exchange expenditure to a level that would be compatible with her reduced foreign exchange capacity.

Furtner the famous world oil glut had hit the Organization of Petroleum Exporting Countries (OPEC) of which Nigeria is a member, who accordingly reduced production. Since not much could be done to rapidly expand foreign exchange receipts in the short run, attention was therefore focussed on curtailing the outflow of foreign exchange. To this end, a combination of fiscal and monetary policy measures were initiated by the Federal Government.

In 1983, some of the measures applicable in the Economic Stabilization Act of 1982 were retained and strengthened. This was so because the economic prospects for the country in 1983 were expected to be worse than what obtained in 1982. In 1984 a more stringent exchange control measure was promulgated by the Buhari Military Government with a view to revamp the battered economy which was due to the unsatisfactory administration of exchange control measures by the previous government.

Some of the measures embodied in these various acts of Government included reduction in Basic Travelling Allowance (B.T.A.) from N800 per individual to N100, the prohibition of certain goods from importation, the placing of goods on specific import licence from open general licence, the imposition of compulsory advance deposit for imports and the N100 foreign travel levy.

The compulsory advance deposit for imports was part of exchange control regulations to curtail imports. Some of the items and their percentage deposits are as shown in Table 1 below. The deposits were against imports and were timed to reduce liquidity in the system as well as reducing the high import propensity of Nigerians. The amounts were deposited with the Central Bank of Nigeria by the collecting banks at zero interest rates.

These measures were not adequate to solve Nigeria's balance of payments problems. The deficits in the balance of payments continued until 1984 when a slight surplus was earned as a result of very restrictive foreign exchange budgeting.

The Federal Government was negotiating a loan of N2.2 billion from the International Monetary Fund to help defray the nation's outstanding short-term obligations with trade creditors and restore trading relations which had been harmstrung by the nation's

Table 1
Compulsory Advance Deposits

Items	Percentage Deposits for Imports
Raw Materials	25%
Spare parts	25%
Building Materials	50%
Capital Goods and Books	50%
Motor Vehicles and Trucks	200%
Motor Cars	250%
Other Goods	250%

Source: Central Bank of Nigeria, Monetary Policy Circular 1, 1982.

reduced payment capacity. The I.M.F. had given Nigeria certain conditions to be fulfiled before granting her the loan. These conditions are referred to as I.M.F. conditionalities. It is noteworthy that Nigeria has accepted in principle and implemented to some extent the following fifteen conditionalities:

- Reduction in the aggregate public expenditure, particularly in the size of the Budget deficit.
- 2. Introduction of greater budgetary discipline.
- 3. Review of ongoing projects with a view to determining their priorities.
- 4. Reduction in grants, subventions and loans to parastatals.
- Classification of parastatals into "social" and "economic" activities for purposes of restructuring them to achieve costeffectiveness, accountability and for economic parastatals profitability.
- 6. Stoppage of non-statutory transfers to State Governments.
- 7. Simplification and rationalization of customs tariffs.
- 8. Upward review of interest rates and reduction in the sectoral allocation of credit.
- 9. Phased removal of subsidies on fertilizers.
- 10. Vigorous export drive to broaden the export base.
- 11. Review of industrial incentives and policy and the abolition of

- Approved User Scheme.
- 12. Adjustment of Producer Prices of agricultural commodities.
- 13. Strict external debt control and management.
- Improvement in operational efficiency of revenue collection agencies such as Departments of Customs and Excise and Inland Revenue.
- 15. The withdrawal of subsidies on petroleum products.

The yet unaccepted conditionalities include the following two:

- 1. The devaluation of the naira currency, or exchange rate adjustment by about 25-30% initially followed by further adjustments until the element of over-valuation is eliminated.
- 2. The liberalization of trade.

The above conditions are felt to be too severe and against the interest of the country. It is argued that the liberalization of trade would lead to the dumping of all sorts of foreign goods in Nigeria and the withdrawal of petroleum subsidies would increase transport costs and have cummulative upward impact on all prices. It is also argued that devaluation could worsen our balance of payments position since our major export is oil whose quota is externally allocated through OPEC. Let us look at these areas of disagreement and their likely implications.

Devaluation of the Naira Currency

Devaluation is a monetary technique applied by a country under temporary economic recession for the correction of imbalance in the external accounts of a devaluing country to improve the country's balance of payments position. When a country devalues, she gains in foreign currency in two ways: (i) She could now supply at relatively cheaper rate to the home market those commodities she has to import. Her marginal propensity to import goes down. Then she saves an amount in foreign exchange equal to the increase in turnover in the home market. The imbalance in the external account may be corrected from the savings accruing from this. (ii) By a country devaluing her currency in terms of other national currencies a country which has suffered reverses in her balance of payments cheapens her export goods and becomes more competitive. Foreign exchange is gained at the expense of competing countries. This can help correct the internal imbalance.

On the argument that Nigeria still exports only oil, foreign exchange can still be saved through reduction in imports and the substitution of domestic production which devaluation makes possible. Also in the Nigerian situation export expansion is still valid when viewed in a dynamic sense. In the first instance our oil export quota is not generally fulfilled and in consequence shortfalls are realised in our oil exports as against permissible limits. In the second instance, our agricultural products would become competitive with devaluation and we can now export some of these commodities as before. For instance an Abakaliki rice producer can produce at about N90 per 50 kilogram bag, but foreign produced rice arrives Lagos at landed cost of about \$\%40 per kilogram bag. This means that importers can reap excess profits by importing rice at low foreign prices and selling at high Nigerian market prices. If naira is sufficiently devalued that 50 kilogram bag of rice can land in Lagos at say N100, this would be a boom to Nigerian producers. Alternatively the banning of importation of rice achieves the same result, but Nigeria cannot ban importation of all commodities as the inflationary consequences can be too explosive and capable of bringing down any government.

The Central Bank of Nigeria was entrusted with the responsibility of management of the nation's external reserves. One important aspect of it is the determination of the naira exchange rate. This is based mostly on the currencies of Nigeria's major trading partners, the Central Bank's import weighted basket of currencies. The currencies comprise U.S. dollar, pound sterling, deutschmark, Japanese yen, French franc, Swissfranc, and Dutch Guilder.

Before 1978, the Central Bank of Nigeria held its reserve assets only in the Bank of England and the Federal Reserve Bank of New York in the U.S. As a result, the naira exchange rate was tied to the U.S. dollar and the British pound sterling movement in the international money market. Since 1978, a basket of currencies approach similar to the International Monetary Fund system of valuation of the Special Drawing Rights (S.D.Rs) is used in the determination of the exchange rate of the naira. Like the S.D.Rs., this involves the Central Bank's monitoring of the movement of the exchange values of the currencies of all Nigeria's major trading partners daily. Based on these, the Central Bank of Nigeria estimates the naira exchange rate on a day-to-day basis.

Since the naira is not a convertible or trading currency, its value with respect to other currencies cannot be determined by its supply and demand in the international market, as such, only estimates can be made. The method of estimation by the Central Bank of Nigeria has tended to over-value the naira. The black market rate for the naira viz-a-viz foreign international traded currencies is considera-

bly lower than official rates. This over-valuation has tended to put premium on imports which are relatively cheaper and to discount export-based activities because of Nigeria's uncompetitive position as a result of high production costs. Thus the nation's external imbalance could exacerbate if naira does not depreciate.

Some African countries in recent years devalued in order to expand trade. In 1975, Tanzania devalued her currency by 15% and pegged it to the I.M.F. Special Drawing Rights. Again in January 1979, Tanzania devalued by 10% and delinked her shilling from the S.D.R. and pegged it to the basket of currencies of Tanzania's major trading partners. The main reason for these was that as Tanzania's economic hardship escalated she sought for I.M.F. loan to boost her exports. Devaluation was one of the conditionalities.²

Zaire also devalued her currency by 33% in 1978 and in 1979 by another 25% during its talk with the I.M.F. in Paris. The devaluation was demanded by the I.M.F. as the condition for standby credit of \$153 million. The strategy was to lessen the strain on Zaire's balance of payments which had been in deficit in the preceding years. Zambia devalued her currency (Kwacha) by 20% in 1978. Later, the currency was further devalued by 100% in a period of four years. The devaluation was sequel to the I.M.F. conditions before Zambia could borrow to facilitate increased exports and revamp her sagging economy. Sudan devalued by 20% in 1978. Again in 1984 the commercial value of the Sudanese pound was devalued by 14.3%. Official reason for devaluation was to encourage exports and to boost remittances from her citizens working abroad mainly in oil rich Arab countries. 5

Ghana in 1978 devalued the Cedi by 140%. Supporters of this devaluation held that foreign exchange earnings from Ghana's major exports was not enough to pay for her imports. To them devaluation would reduce importation, stimulate domestic production and increase Government revenue. Ghana again in 1983 explicitly devalued the Cedi by an astronomic 990% (nine hundred and ninety percent) which is recorded as the highest devaluation by any country since World War II.

According to Carver, the devaluation was an indirect devaluation of the Cedi. He stressed that the I.M.F. reluctantly accepted a system of multiple exchange rate proposed by Ghana, whereby a bonus is paid to exporters and surcharge levied on imports. The effect being a devaluation of the Cedi as regards physical commodities while invisible and capital transactions continued at the official rate.⁷

Other developing countries that have devalued recently include

Sierra Leone, Togo, Ivory Coast, Argentina, etc. Nigeria has serious balance of payments problems like any one of these countries. Yet she has refused to devalue to help boost her exports and reduce imports. Most countries listed above who devalued are like Nigeria, mono-product economies, but they embarked on this course to improve their balance of payments position. One may ask if these smaller poorer countries, why not Nigeria? The salutory impact of Nigeria's first and only official devaluation of 10% in 1973 should encourage further such actions to realign her over-valued naira and increase her balance of payments position. 8

Prices may actually fall with devaluation. The market prices of imported goods presently reflect the black market value of the naira. Any commodity that could be bought at say \$1,000 in 11 K. sales 101 \$3,000 and above in Nigerian markets. The 200% over valuation of the naira is already reflected in Nigerian market prices of foreign produced goods. If traders can get foreign exchange at officially devalued rates of 100% to procure foreign produced goods, the price of the above goods would be \$2,000 and not \$3,000. Thus devaluation with less restrictive exchange control measures could reduce prices and not necessarily increase them.

On the contention that debt service burden would increase with devaluation, it is hereby submitted that this would even fall. With the rescheduling of debt repayments, the burden of debt servicing as a percentage of exports would fall. Further the debts are denominated in dollars and not naira, although the naira value of debts would increase with devaluation, but the actual payment in dollars stays the same. Just as the naira values of the debts increase, the naira value of the foreign exchange proceeds from exports increases. Both should nullify each others adverse effect.

Trade Liberalization

Trade Liberalization does not mean that the nation's borders would be open for the dumping of all foreign goods. Our tariff structure is very high and could be reviewed downwards in order to reduce the potential inflationary impact of devaluation. Further with devaluation, foreign goods become more expensive and according to a fundamental economic law, the higher the price, the less the demand. Less foreign goods would be demanded and this would be an additional constraint on foreign exchange disbursement.

Nigeria has rightly abolished the Advance Deposit Scheme and decentralized Form M approvals. Nigeria should go ahead to gradually eliminate prohibition of certain goods since their high

prices would constrain their demand. The area of trade liberalization is an area for skilled negotiation in the interest of the nation. Nigeria should still retain the right of foreign exchange budgeting through the use of import licences in order not to exacerbate the balance of payments position. But the rush for imports would attenuate if the naira finds its true international value as the high profit rip-off from importing goods and selling at fantastic markups would disappear.

Withdrawal of Subsidies

This could be inflationary since transport costs would escalate. But this would lead to less unnecessary trips and lowered accident rates. It would lead to modernization of our telephone services and elimination of waste in consumption of fuel. In order to mitigate the inflationary consequences of this conditionality it is necessary for a phased removal over the span of the Extended Funds Facility. Nigeria's petroleum products are cheaper because of the subsidy and this gives vent to untoward practices like bunkering and smuggling of refined crude to neighbouring countries to be sold at high prices. These untoward practices would stop. Government can then earn more revenue for other development projects. Also to mitigate the impact on fixed income receivers like civil servants. Government can raise salaries as was done in Ghana. Nigeria is ripe for a comprehensive salary review since the Udoji Williams exercise of 1974/75, a decade of increasing prices and stagnant incomes. In 1986, 80% petroleum subsidy was withdrawn but public sector salary review has not yet been made.

Rescheduling of Trade Arrears

It was said that the major obstacle in the rescheduling of the trade arrears is the refusal of the Export Credit Agencies to reschedule their insured trade arrears of about N2 billion unless Nigeria reached agreement with I.M.F. This is the normal practice in official multilateral rescheduling process requiring the participation and concordance of the I.M.F. amongst other agencies before agreements are struck. Official debt rescheduling are negotiated through aid consortia or through credit clubs like the Paris club.

So this is not a conspiracy against Nigeria as some Nigerian critics are wont to say. It is a normal practice. For instance the Paris Club came into being in 1956 when a number of European countries met to renegotiate outstanding balances in their bilateral accounts with Argentina. Since then it has become an official forum for renegotiating debt. It brings as many creditors as are

willing to participate together. The meeting is attended by observers from World Bank, International Monetary Fund, OECD and UNCTAD.

The I.M.F. representative at the meeting presents an assessment of the country's economic situation and prospects including the country's relationship with the Fund. The World Bank representative presents a longer term analysis of the debtors economic prospects. This is then followed by the creditor's representatives and an understanding on the general terms of rescheduling of the country's debt is reached.

If Nigeria had taken the I.M.F. loan and negotiated the conditionalities in the best interest of the nation, this would have been the basis for debt rescheduling with her creditor nations. The agreements with the trade creditors would normally include the following:

- (a) It should involve loans granted or guaranteed by official agencies of participating creditor countries. In Nigeria's case, the insured trade arrears of №2 billion with the British Export Credit Guarantee Department (ECGD) qualifies for rescheduling.
- (b) Nigeria would have to have in force a stabilization programme with the I.M.F. And this is mandatory before rescheduling provision becomes effective.
- (c) Nigeria must reschedule between 85% and 90% of the debt falling due i.e. the №2 billion, and allow for a grace period of five years with a repayment to a further period of up to five years. The non-rescheduled portion should be paid during the grace period.
- (d) All short-term debts and debts rescheduled before must be excluded.

Nigeria would have rescheduled her debts conveniently after the I.M.F. loan must have been concluded. The I.M.F. loan would have refinanced the short-term trade arrears amounting to N2.6 billion.

The Case for the I.M.F. Loan

By 1977, Nigeria's total foreign indebtedness was N365.1 million, a very low figure. By 1983 Nigeria's total foreign indebtedness grew to N10.893 billion⁹. The distribution of Nigeria's external debt, state and federal governments as at the end of 1983 is as shown in Table 2 below.

Nigeria's total external debt increased by 16% in 1979, by 1981

Table 2

External Debt of State and Federal Governments as at 30th December, 1983 (N 'M)

Federal Government (Total)	8,043.9
Refinancing Credit	1,459.6
Other Loans	6,584.3
State Government (Total)	2,849.7
Anambra	321.2
Bauchi	71.2
Bendel	120.9
Benue	85.6
Borno	98.0
Cross River	25.6
Gongola	4.9
Imo	422.1
Kano	27.2
Kaduna	
Kwara	149.5
Lagos	154.3
Niger	34.2
Ogun	73.2
Ondo	220.4
Оуо	313.4
Plateau	306.1
Rivers	82.3
Sokoto	239.1
Total	10,893.5

Surce: Central Bank of Nigeria, Annual Report and Statement of Accounts 1983, p. 80.

me loans increased by 24.9%. By 1982, total external indebteaness use by N4.9 billion showing an increase of 211.7%. This upsurge as as a result of sharp decline in revenue which induced governments of the Federation to seek external loans to execute their deady planned development projects. In 1983 the debt rose to

N10.8 billion.

The high external indebtedness of Nigeria since 1979 has increased substantially the nation's debt service burden. The debt ervice ratio increased from an insignificant 0.8% in 1977 to 1.5% in 1981, 8.9% in 1982, 17.5% in 1983, 25% in 1984 and 45% in 1985. The result of Nigeria's lowered credit worthiness is that she now resorts to trading on cash basis internationally or on expensive confirmed letters of credit. As Professor Nwankwo showed, this method of trading has high markups in prices as high as 50% on products supplied on open accounts basis and 20% on letters of credit. Thus Nigeria's reduced credit worthiness tend to fuel imported inflation and the shortage of goods since trading on cash basis would be fruitful if Nigeria has substantial reserves.

A country facing debt servicing difficulties has three broad choices:

- (a) It may cease repayment on its debts thereby accumulating debt service arrears. This may result to a series of more problems since it would undermine confidence in the country, making it difficult for it to borrow. There is also a tendency for future default in which case that country's assets may be attacked or confiscated and sold to discharge the debt. This is the Castro option.
- (b) A second option will be for that country to try to service its debts at all costs, this may lead to restrictions on other foreign exchange expenditures hence resulting in a reduction in imports. This is the present situation in Nigeria where imports consists of mere essentials. Factories are closing down, unemployment figures mounting, prices escalating. Life is difficult; people starving and dying of hunger and frustration. Debt service ratio is very high and this situation cannot persist for long.
- (c) Finally a country with debt servicing problems may seek a rescheduling which is a re-arrangement of the repayment terms or it may seek refinancing. In Nigeria's case the I.M.F. Loan would have refinanced short-term trade debts of N2.6 billion making it possible for rescheduling of medium term debts due for payment which amounts to N2 billion.

It is evident that Nigeria needs the I.M.F. loan in order to help defray outstanding short-term trade arrears and increase her credit worthiness. Nigeria depends on trade creditors for both producer and consumer goods. So far her industrialization efforts have been geared to processing foreign raw materials. To do so she acquired capital intensive means of production from Europe and America.

In consequence of the reduced credit worthiness, Nigeria can no longer bring in the goods as before. Industries close down and unemployment figures go up. Graduates commit suicide ever so often for being unable to find jobs, and some find themselves suboptimally employed as car drivers, all these because Nigeria cannot reschedule trade debts and continue trading as before.

It may be argued that Nigeria should seek to be self-reliant and depend less on the external sector. But this should be a long-run strategy, planned and implemented by Government. In the interim, the Nigrian industries would have to be reactivated to ful capacity operation. The ordinary goods which Nigerians have been buying based on international division of labour and the theory of comparative advantage, since no nation achieve 100% economic autarky should be allowed to flow. The absence of these commodities has made Nigeria a very difficult place to live in, because of unprecedented inflationary costs of acquiring basic commodities.

To take the I.M.F. loan of N2.2 billion means that Nigeria's trade credit would fall by that amount. Her total indebtedness does not necessarily increase. It has consequences for possible future increased indebtedness since she can now carry on trade on credit basis with her enhanced credit worthiness. This is because conclusion of an I.M.F. package is deemed a stamp of approval on a nation's credit worthiness. Trade creditors prefer to deal with nations with I.M.F. stabilization programme. This is why the I.M.F. is a necessary party in all rescheduling agreements as the creditors do not have the machinery to ensure that the debtor nations have the capacity to meet the terms of agreements.

The Second Tier Foreign Exchange Market and After

Since naira cannot float effectively in the foreign exchange market as a result of its non-convertibility and non-trading status, an alternative is to create a 2nd tier exchange window where the true value of the naira can emerge by the demand and supply of foreign currency in the market. For instance, if five billion Nigerian naira constitutes effective demand for foreign currency and the supply is represented compositively by say two billion dollars of foreign exchange then the exchange value for naira and dollars would be 2.5 to 1. Since naira is over-valued the true value of naira would emerge in the 2nd tier market.

Nigeria has decided to introduce this 2nd tier window in Nigeria's foreign exchange market as an alternative to immediate devaluation of the naira. It is hoped most official and all private

transactions would be routed through this market. In effect there would be two markets for foreign exchange in Nigeria, the 1st tier which would represent official or historical prices for naira and the 2nd tier which would reflect market prices for the naira.

If well implemented the over-valuation of the naira and its untoward consequences of balance of payments deficits, black market transactions, smuggling, trafficking in currencies that tended to reduce the supply of foreign exchange through official channels would be mitigated if not completely check-mated. It is hoped that in a matter of time the official rate, the market rate and the black market rate for the naira would converge at a true market rate that does not overvalue the naira, a gradual devaluation of the naira would have been effected. Also foreign exchange rationing through import licences would be a thing of the past.

Conclusion

Since Nigeria has rejected the I.M.F. loan and since the IMF's concordance and approbation are necessary for Nigeria's external debt rescheduling, the introduction and operation of the 2nd tier foreign exchange market would substitute for devaluation. With this all IMF's conditionalities would have been met and Nigeria can thus get I.M.F.'s stamp of approval through its enhanced surveillance scheme for the rescheduling of her medium-term and long-term debts. This is a substitute for I.M.F. loan but not a perfect substitute as Nigeria's short-term obligations would still be outstanding. In the circumstance this is a second best strategy since Nigeria lacked the political will to take the loan.

NOTES

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