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A Decisive Moment in Nigeria: Fiscal Strategy, Policy Coordination, and Macroeconomic Stability

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Summary

Despite the enthusiasm associated with political campaigns in Nigeria, the reality is that the next administration will have to contend with a nation facing significant fiscal-macroeconomic challenges. This note focuses on adopting a more integrated and comprehensive framework for the conduct of fiscal policy, with emphasis on improving domestic resource mobilization, enhancing expenditure efficiency and exploring alternative sources of fiscal-deficit financing consistent with macroeconomic stability and growth. The note equally discusses the criticality of coordination between fiscal and monetary policy. The new administration has a major role to play in adopting a more encompassing fiscal framework and ensuring more effective policy coordination, including through limiting or eliminating the quasi-fiscal activities of the monetary authority and other agencies and establishing a fiscal and monetary coordination council. The international financial institutions need to stand ready to assist the new administration in terms of additional financing, strategic technical assistance, and reverting to considering intergenerational equity in their fiscal policy advice to Nigeria.

Context

Nigeria's recovery from adverse economic and health shocks has been relatively weak. The period under consideration (2012–2022) was marked by the Ebola outbreak of 2014, the 2014–15 oil price shock and the subsequent volatility, the 2020 pandemic and the Russian invasion of Ukraine in 2022. These adverse shocks impacted macroeconomic performance considerably. The Nigerian government must be commended for its proactive actions, including a robust infection tracking

system that helped to contain the health and macroeconomic impacts of the Ebola outbreak and the 2020 pandemic. The monetary and fiscal responses to the 2020 pandemic resulted in taking the economy out of recession. However, initial macroeconomic and structural conditions before the occurrence of these shocks combined with incomplete policy adjustment and inadequate economic coordination have somewhat contributed to the current economic challenges.

The limited economic coordination at the Federal Government level is impacting economic performance. The existence of various forms of quasi-fiscal activities makes it difficult to ascertain the level of aggregate demand at the policy design stage. For example, the central bank of Nigeria has been performing developmental functions through its various interventions and at the same time financing fiscal operations. These sectoral interventions could eventually and potentially deliver on alleviating supply-side constraints. In the short term, however, these well-intended interventions contribute to aggregate demand impulse, resulting in inflation and exchange rate pressures. As empirical literature has demonstrated, sterilization of quasi-fiscal interventions and fiscal-deficit financing tends to be associated with higher interest rates, with implications for growth. Additionally, a lack of consolidation of quasi-fiscal activities with the government's fiscal position may reduce the transparency and effectiveness of fiscal policy, engendering fragmentation of the budget and blurring of institutional responsibilities.

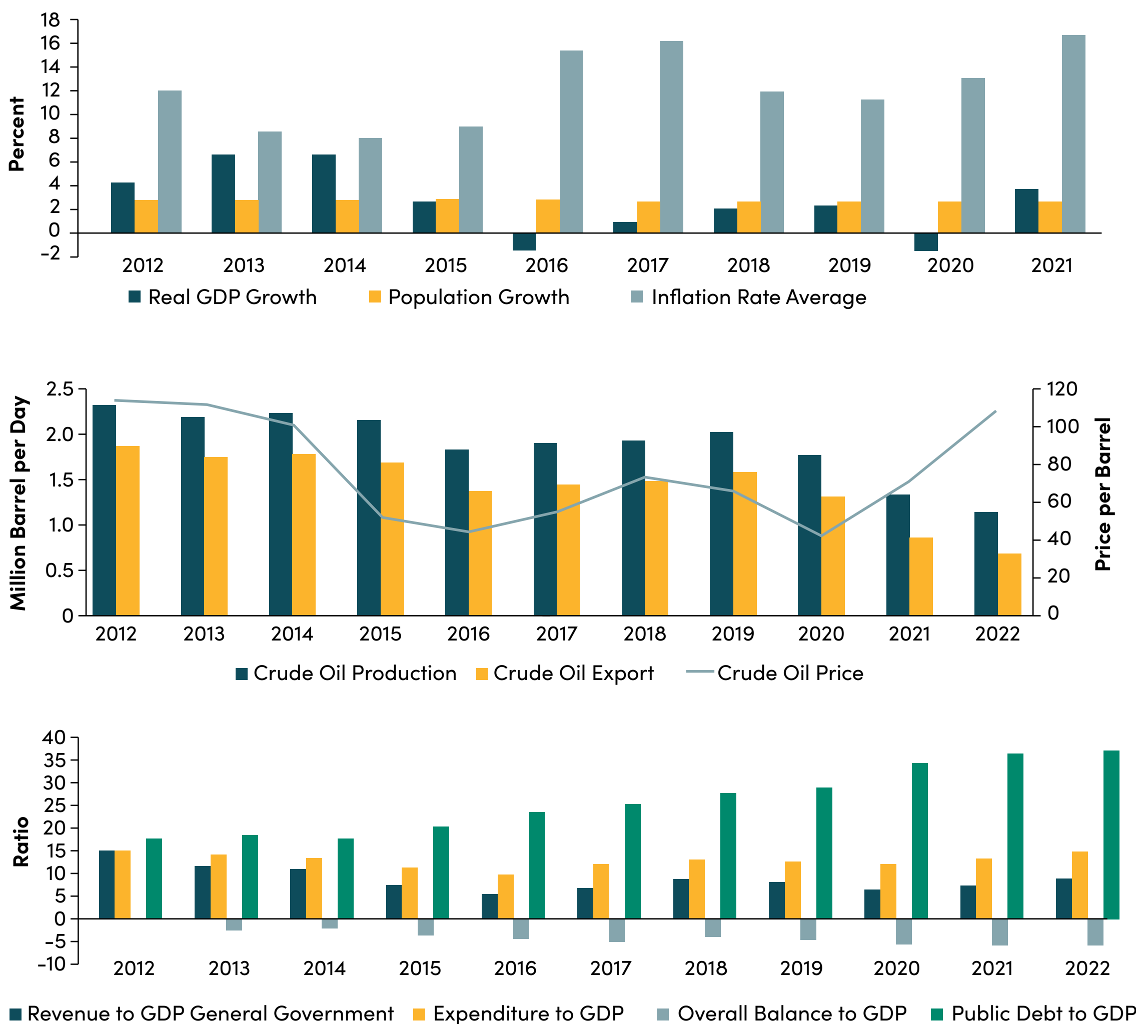
Despite the usual excitement associated with political campaigns in Nigeria, the next administration will have to contend with a nation with deep-rooted macroeconomic problems. The election campaign has commenced for the 2023 elections and some parties have released their economic blueprints. These blueprints need to be intensively interrogated by all Nigerians, laying the foundation for what has to be done differently in the next four years to take the country out of the current economic and social quagmire. There are many issues that Nigeria's policy makers are grappling with, but this thought piece focuses mainly on fiscal-related issues. Fiscal policy is important for macroeconomic stability, economic prosperity and for re-building social contract.

This note covers a wide range of critical issues germane to achieving macroeconomic stability in Nigeria. It lays out current macroeconomic challenges in Nigeria and discusses the main global macroeconomic developments and potential implications for fiscal policy design and implementation. It presents an assessment of the 2023 Federal Government budget and its consistency with the monetary policy stance. The note assesses the fiscal component of political parties' manifestos, highlighting the key issues that have to be addressed. The note offers a roadmap for fiscal policy with a view to achieving macroeconomic stability and emphasizes the criticality of policy coordination and institutional reform. The specific roles of international financial institutions (IFIs) in complementing the domestic reform agenda are discussed.

Macroeconomic developments

The Nigerian economy is besieged with varying macroeconomic issues (Figure 1). Real GDP growth and population growth rate averaged 2.5 percent and 2.6 percent, respectively during 2012–2021. Headline inflation, reflecting demand and supply factors, averaged 12.4 percent during the past 10 years. High inflation tends to adversely affect the poor segment of the population, given their fixed incomes and/or informal sources of income, and the inability to hedge against rising prices. The fiscal framework has been under pressure: revenue-to-GDP ratio averaged 8.6 percent during the period under consideration, expenditure at 12.6 percent, and public debt at 25 percent. Reserve money growth averaged 18.5 percent and during the same period, the stock of central bank financing of the fiscal deficit (ways and means) moved from N134.8 billion (0.2 percent of GDP) in 2012 to about N20 trillion (10.9 percent of GDP) as at end-June 2022.

Figure 1. Nigeria: Selected real and fiscal indicators

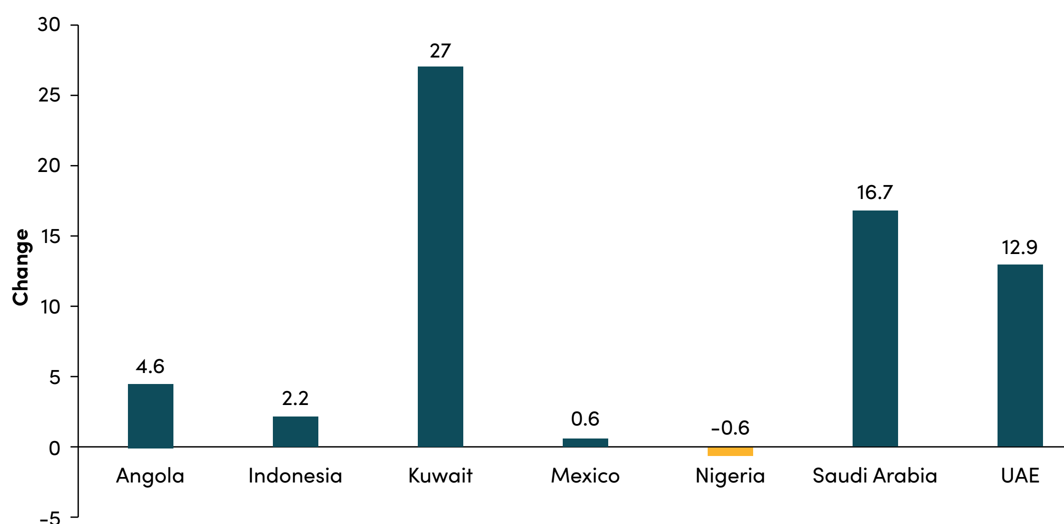


Sources: CBN, IMF, NBS.

Recent data point to deepening macroeconomic challenges. The growth rate of the economy shows some resiliency, with real GDP growth averaging 3.3 percent during the first half of 2022. However, real GDP growth fell to 2.3 percent during the third quarter of 2022. Year-on-year inflation reached 21.1 percent in October, 2022 with food inflation at 23.7 percent. Based on the 2018/19 national monetary line, the poverty rate is about 40 percent. However, a recently released report indicates that 63 percent of the population is multidimensionally poor, taking into consideration health, education, living standards, work and shocks (NBS, 2022). The last official statistics point to an unemployment rate of 33.3 percent. The gaps between the parallel market and official exchange rates have widened significantly, with the former currently at about N750 to $1 and the latter at N445 to $1 (investors and exporters' FX window). The CBN has been hamstrung in intervening in the foreign exchange market, as accretions to the Federation account through oil export proceeds have been limited as subsidy on refined petroleum products surged and oil production is at historical low. External reserves stood at about US$37 billion as at end-November 2022 (5.2 months of imports of goods and services) compared to US$40.5 billion (5.7 months of imports of goods and services) as at end-December 2021.

The paradox of an oil-producing country experiencing less-favorable macroeconomic performance in the context of higher oil prices largely reflects lower oil production and higher fuel subsidies. Oil prices have increased considerably in 2022 largely due to the Russia-Ukraine War. Oil prices are currently hovering around $75 a barrel, after surging as high as $130 in March. In this context, other oil-exporting countries have been experiencing improved macroeconomic performance in 2022 characterized by higher revenues, reduced fiscal deficits (Figure 2), appreciated exchange rates (for countries with flexible foreign exchange regimes) and higher external reserves. In the case of Nigeria, however, the fiscal challenges have further deepened. Despite elevated oil prices, the country's (net) official oil earnings have not increased due to lower crude oil production associated with oil theft and pipeline vandalization (Figure 2) and higher subsidies on imported gasoline. At the federal Government level, debt service as a ratio of revenue reached 83 percent during the first eight months of 2022. General government debt (inclusive of overdrafts from the CBN and liabilities of the Asses Management Corporation) reached 36.6 percent of GDP in 2021. Despite higher oil prices, Nigeria's balance of payment is under pressures due to reduced production of crude oil, limited share of non-oil exports in total exports (about 7.5 percent during the third quarter of 2022), higher import prices for refined fuel products and food, and negative net capital outflows associated with domestic macroeconomic challenges and increasing interest rates in advanced economies. International rating agencies recently downgraded Nigeria's sovereign rating, citing ongoing fiscal and external weakening in the context of higher crude oil prices.

Figure 2. Nigeria and selected oil-exporting countries: Cumulative change in overall balance-to-GDP ratio (2020–2022)



Sources: Fiscal Monitor Database, IMF, Author's Calculation.

Global developments and fiscal operations

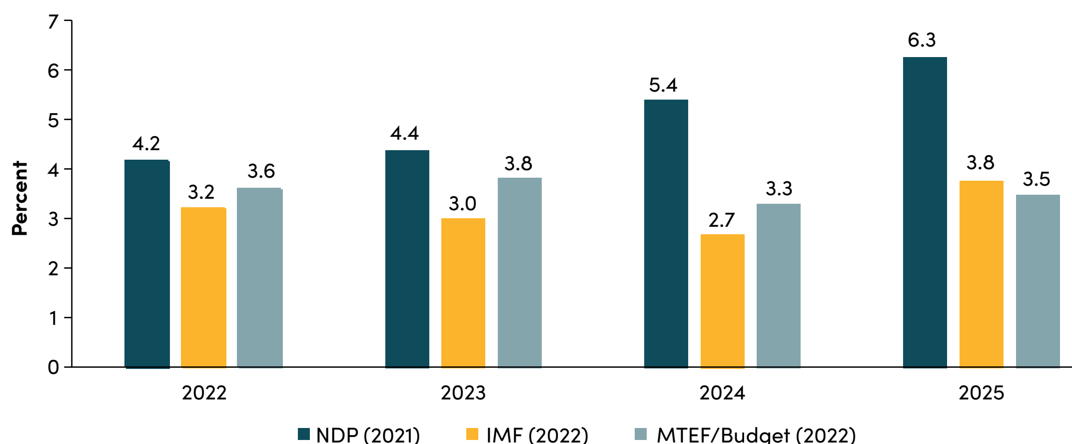
The global environment in the near term portends challenges for fiscal policy design and implementation. Multiple shocks affecting the overall Nigeria's economic outlook and fiscal policy design and implementation include the slowing down of the global economy and tightening global financial conditions. Global growth is projected at 3.2 percent in 2022 and to slow to 2.7 percent in 2023. Despite the fragility of real GDP growth in Nigeria, higher interest rates in advanced economies would continue to result in increased interest rates to sustain some levels of capital flows, ameliorate exchange rate pressures and reduce stubbornly high inflation. From a domestic and external perspective, the cost of servicing public sector debt will be on the increase.

To build resilience and absorb the cost of a higher interest bill, the new administration will need to imbibe fiscal prudence. Further, credible medium-term fiscal frameworks—including effective debt management—can reduce exposure to shifts in risk sentiment and can lower borrowing costs. The fiscal policy has to be at the center of striking appropriate balance among competing priorities of demand management, debt stabilization, protection of vulnerable populations, and investment for the future.

Continuation with the current macroeconomic framework and management in Nigeria would not deliver macroeconomic stability and sufficient economic growth. The current Administration has in place a National Development Plan (2021–2025) with programs and policies. The key challenge

is the lack of adequate alignment between this Plan and annual budget (Figure 3). The projected medium-term growth rate (based on the IMF and the 2023 budget projections) would be only slightly above population growth rate of around 2½ percent. This highlights the criticality of putting in place appropriate policy measures and strong commitment to their implementation to bring about meaningful improvement in macroeconomic stability and prosperity.

Figure 3. Nigeria: Comparison of real GDP growth



Sources: FMFBNP, IMF

An assessment of the 2023 budget

The link between the current and new administration is the 2023 budget. Against this background, the 2023 Federal Budget focuses on maintaining fiscal viability and ensuring smooth transition to the incoming administration. The proposed 2023 federal government budget implies a general government fiscal deficit of about 5.8 percent in 2023 compared to estimated 6.2 percent in 2022.

Fiscal policy has to align with monetary policy stance to achieve macroeconomic stability:

- In line with historical variance between actual and budgeted revenues, it is appropriate to mention that the actual deficit in 2023 at the Federal Government level could turn out to be higher than the target. Optimistic revenue targets tend to result in recourse to central bank financing with attendant macroeconomic consequences. The fiscal deficit is elevated (way above the target of 3 percent in the Fiscal Responsibility Act), impacting debt dynamics. When deficit and debt accumulation result in a decline of net wealth of the public sector and in the context of a country with exhaustible oil and gas resources, there is re-allocation of resources from the future to the current generation.

- A general government fiscal deficit objective of close to 6.0 percent of GDP in an environment of macroeconomic instability appears to be too permissive. The CBN has been increasing its policy rate to tighten monetary policy stance. At the same time, a general government deficit of about 6 percent of GDP would entail additional central bank financing in view of the difficult external environment and the need to limit crowding out the private sector. Attempts to withdraw liquidity injections associated with fiscal-deficit financing through the CBN's mop-up operations would lead to further increase in interest rates, with adverse implications for growth.

- Macroeconomic trade-offs imply that when inflationary pressures are high as is the case in Nigeria, fiscal policy should protect the most vulnerable while pursuing a tightening stance to avoid overburdening monetary policy in the fight against inflation. Tightening fiscal policy requires prioritizing spending among competing needs and mobilizing revenues in a growth-friendly way. A more ambitious fiscal consolidation could send a powerful signal that policymakers are aligned in their fight against inflation, which, in turn, could reduce the size of required policy rate increases to keep inflation expectations anchored and keep debt-servicing costs lower than otherwise.

Political parties' manifestos and fiscal policy direction

Many political parties have launched their manifestos, laying out their economic agendas for the next four years. As the campaigns progress and Nigerians engage with all these political parties, the following fiscal-related issues need special attention:

- *How will the programs and projects of the new administration be financed to deliver on growth and social objectives?* Government is a continuum. The new administration will be inheriting the assets and liabilities of the current administration. This implies that in setting the economic agenda for the next four years, it is important to take into consideration current macroeconomic initial conditions. The initial conditions that would impact the next administration to deliver on its set goals and objectives include the reforms and infrastructural projects already implemented by the current administration; revenue challenges (where revenue to GDP ratio for the general government was about 7.3 percent of GDP in 2021); high interest expenditures and the attendant fiscal implications; existing composition of expenditure—with larger shares allocated to recurrent expenditures); high fiscal deficit and debt (reducing available fiscal space to the new administration to fund on-going infrastructure projects or start new ones); and the constraints imposed by the global environment, particularly the surging interest rates associated with the tightening of monetary policy.

- *What are these political parties' strategies in the near to medium term to bring about improved macroeconomic stability in Nigeria?* Fiscal policy has a role to play in ensuring macroeconomic stability. An environment of macroeconomic instability (characterized by high inflation, high fiscal deficit, wide divergence between official and parallel market exchange rates) would not attract domestic investment and foreign direct investment. It would be useful to set more realistic revenue targets to underline the budget to avoid on-going financing of the fiscal deficit by the CBN.

- *Will these political parties encourage or discourage the use of central bank financing of fiscal deficit?* It has to be recognized that large and sustained financing of fiscal deficit through ways and means is disruptive by engendering macroeconomic instability.

- *How will these parties strike an appropriate balance between the use of fiscal incentives to promote investment and expanding the tax base?* What are the strategies for protecting consumers from higher prices in view of potential bias towards import-substitution strategy? Caution should be exercised in using fiscal incentives to encourage investment so as not to damage the tax base. Industrial policy must focus on improving competitiveness so that companies that receive protections are eventually able to compete in regional and global markets and there must be an exit strategy in place. It is important to note that particularly in the short to medium term, the use of import-substitution strategy could entail transfer of resources from consumers to producers through relatively higher prices.

- *Will these political parties produce a revised 2023 budget or will the issues raised in this section be considered in the 2024 budget?* It is high time to decompose capital expenditure into economic—physical, digital and social (those with high impact on productivity and growth); and administrative (for example, car purchase and others that have limited impact on productivity and growth, but tend to drain foreign exchange).

- *Will these political parties expand or reduce the size of the public sector?* In view of the share of recurrent expenditures in total expenditures (particularly at the federal government level), reducing unemployment rate would entail higher economic growth underpinned by private sector development not necessarily through expanding the size of public sector workers.[1]

1 The share of capital expenditure in total expenditure was about 19 percent during the first eight months of 2022.

Proposed fiscal policy measures for the current administration

As the political process evolves, the current government needs to take additional fiscal measures to set the stage for the new administration. In this regard, this note identifies specific areas that the current administration could help contribute to the success of the new administration, focusing largely on re-building social contract and raising additional fiscal revenue:

The current administration has to lead the required fiscal adjustment process by transparently and significantly reducing the cost of governance. The government has to demonstrate its willingness to make sacrifices. This could take the form of significant reduction in remuneration of political office holders. In addition, consideration could be given to reducing considerably administrative capital expenditures (capital expenditures with low impact on enhancing total factor productivity and alleviating supply bottlenecks). The demonstration effects of these proposed measures could be significant in helping to rebuild social contract and to potentially secure the buy-in of the public for fiscal measures that the new administration will have to consider.

The current administration could assist the next administration by focusing on the following additional specific measures that could help with improved revenue generation: Improved trade balance in 2022 (a surplus of $8.3 billion during January-September 2022 compared to a deficit of $4.4 billion during the same period in 2021) would have been expected to lead to an improvement in the fiscal position. It would be illuminating to assess consistency between the external and fiscal accounts in 2022. Against this background, this note proposes that the current administration could: (i) review the arrangements underpinning the importation of refined fuel products, including estimated daily consumption; (ii) analyze the structure and composition of oil production in Nigeria (joint ventures and production sharing contracts) and implications for public sector oil revenue collection; and (iii) address through effective monitoring and surveillance the thorny issue of oil theft and pipeline vandalization.

It would be useful to undertake an assessment of the taxbase and revenue implications of the use of tax credit scheme. Under this scheme, the total amount spent by a private company in constructing or repairing roads is subsequently used as a tax credit against future company income tax. In line with this scheme, after investing $1.4 billion (about 37 percent of actual capital expenditure at the Federal Government level during January-August, 2022) in road construction, the Nigerian National Petroleum Company Limited (NNPC) is planning to invest additional $2.3 billion to revamp selected roads in Nigeria.

Proposed macro-fiscal focus of the next administration (2023–2027)

The rest of this note takes a comprehensive approach in providing fiscal policy guidance for the next administration, focusing on revenue, expenditure, financing options, and the importance of institutions for fiscal-macro management. It is important that fiscal adjustment takes place without endangering the delivery of critical public services. In addition, fiscal strategy should not focus solely on options for scaling up currently available financing. Such a business-as-now strategy has the potential to bring about unsustainable expenditure levels, with adverse consequences for macroeconomic stability and intergenerational equity. For example, borrowing or other financing options to pay for fuel subsidies, elevated costs of governance, and administrative capital expenditure would result in further deterioration of net worth of the public sector, with adverse repercussions for fiscal sustainability and intergenerational equity (Adedeji, 2021 and 2022).

Revenue

One measure of the trust between the people and government is the amount of tax that the former is willing to pay. In the context of an unwritten social compact, citizens part with a percentage of their earnings with the expectation that the government will provide public services. When this unwritten social contract is challenged, there is less willingness on the part of the citizens to part with their income in form of taxes, culminating in low domestic resource mobilization. This framework is applicable to Nigeria, as general government revenue as a ratio of GDP was 7.3 percent of GDP in 2021. On average, a developing country collects about 15 percent of GDP in taxes relative to an average of 40 percent in a developed economy. The capacity to collect taxes is key to being in a position to finance social services such as education and health, critical infrastructure such as electricity and transportation. Adequate revenue collection has been established as a major determinant of economic growth (Akgun, Cournède, & Fournier, 2017). Moreover, in the case of developing countries, an effective tax system is also a decisive contributor to successful state-building (Fjeldstad & Moore, 2007). Against this background, the next administration has a lot of work to do in re-building social compact with Nigerians.

Georgia's experience is relevant for Nigeria in enhancing revenue collection. By 2003, governance-related issues, including tax evasion and illegal tax credits had left public finances in shambles (Akitoby and others, 2018). Georgia's sweeping tax reform took place with the coming to power of a new government, which had a mandate to reform the economy. The country's new leaders adopted a policy of zero tolerance for corruption, and the culture began to change, along with the laws. A revised tax code, passed in 2004, simplified the tax system and eliminated a series of minor local taxes with little revenue. By 2008, Georgia's tax-revenue-to GDP ratio had doubled to 25 percent.

There are a number of policy lessons for the incoming new administration: (i) It is important to have a clear mandate to reform the tax system. New administrations with such mandates tend to succeed in raising meaningful additional revenues; (ii) political commitment at the highest level and broad buy-in of stakeholders are crucial to improving revenue collection. Effective communication with stakeholders that emphasizes the intended benefits of reforms can help overcome resistance and help to increase the likelihood of reforms being implemented and sustained; and (iii) countries that implement revenue administration measures in conjunction with tax policy reforms tend to experience much larger revenue gains.

The Current Administration and some of the Parties' manifestos seem to focus exclusively on tax-administration measures as the sole instrument for raising additional revenues.[2] While the focus on tax administration measures is important in view of limited tax base and low and fragile economic growth, there is a limit to which tax administration measures alone could be deplored to achieve increased revenue generation. Once the economic fallout from the strong global headwinds dissipates, the new government will need to address the structural problems associated with government revenues. Against this background, consideration will have to be given to redesigning tax incentives toward growth-enhancing activities and the effectiveness of existing fiscal incentives assessed. Efforts to design more progressive tax systems and boost tax collection— particularly, property and/or land taxes—will surely help. Consideration will have to be given to increasing the VAT rate in conjunction with streamlining existing VAT exemptions. There is scope to generate additional revenue by increasing existing excise rates on alcoholic and tobacco products combined with broadening the base.

Expenditure

In an environment of dwindling fiscal space and mounting spending needs, the following expenditure issues need to be at the heart of fiscal policy design and implementation under the new administration: (i) enhancing the quality of public investment by further improving the procurement process to reduce cost and limiting the capital expenditures of Ministries, Departments and Agencies (MDAs) that are not directly responsible for infrastructure provision and public services; (ii) removing fuel subsidy should entail building consensus and trust through public communication campaign and credibly demonstrating plans to protect the poor; (iii) implementing cost-reflective electricity tariffs; (iv) enhancing coverage and efficiency of social assistance programs and derive policy lessons from other countries (for example, the effective use of technology in India to expand the coverage and efficiency of social assistance program); and (v) undertaking civil service reform, with focus on improving provision of public services and merger of MDAs to reduce costs, and enhancing incentives to retire.

2 The Strategic Revenue Growth Initiative (SRGI) of the current administration focuses on increasing general government revenue to 15 percent of GDP by 2025 via blocking leakages, removing tax duplication, and digitalizing tax identification, and rationalizing tax incentives and shifting the focus from improving revenue collection to ensuring tax compliance.

Consideration could be given to establishing a public investment management unit to further improve value for money. Capital expenditure should focus on high-impact and high value-added projects. To move towards achieving these overarching objectives, it would be useful to consider putting in place a public investment management system. Such a system would help to: (i) improve the efficiency and productivity of capital investment; (ii) streamline the preparation, appraisal, approval of all capital projects; (iii) decide on the share of public investment budget subject to project appraisal; and (iv) explore the link between capital expenditure, non-oil exports and growth.

Financing

Public funds are not adequate to finance infrastructure provision in Nigeria and alternative financing options will have to be explored, requiring macroeconomic stability. The current administration in its national integrated infrastructure master plan indicates that about $150 billion is needed annually to finance infrastructure investment over the medium-term period of 2021–2025 (Federal Ministry of Finance, Budget and National Planning, October 2020). It is essential to look for additional capital from development partners, the private sector and institutional investors. Macroeconomic stability is key in exploring financing options and appropriating risks. Emphasis equally has to be placed on further improving the business and regulatory environment as well as a review of the government's stance on the principle of cost recovery and profitability. Enhancing the education and training of the teams involved in infrastructure financing would also be important.

This note advocates for the use of a balance sheet approach to the conduct of fiscal policy in Nigeria (Adedeji, 2022). The adoption of a balance sheet approach entails substituting debt as the main indicator of the financial position of government with 'net worth', with attendant positive implications. Once a government has a better understanding of the size and nature of public assets, it can start the process of managing them more effectively, potentially generating substantial additional revenue or financing. The use of a balance sheet approach could allow for maximizing the return on public assets, resulting in increased domestic resource mobilization.

The new administration could explore the use of advance market commitment to potentially reduce risks and attract additional financing. Advance Market Commitments (AMCs) are market instruments that provide the incentives and guarantees needed to ensure adequate returns on private sector investment. This framework underpinned Operation Warp Speed—the US government's intervention to incentivize the production of COVID-19 vaccine by pre-purchasing hundreds of millions of doses. The same approach could be leveraged by the new administration to attract additional financing in Nigeria, particularly in the health sector. It is critical that AMCs are tailored to different goals along the project development stream and should focus squarely at areas where there is legitimate uncertainty related to the overall costs assessment of whether the initial investment is justified. AMCs are evolving and their effective application in Nigeria as well

as in other developing economies will require considerable support from concessional donors. The fiscal authorities need to ascertain the fiscal implications of such guarantees. For transparency and accountability purposes, such guarantees should be reported regularly.

Enhanced collaboration among different agencies and integrating different initiatives will be key to attracting additional domestic and foreign investments. Many agencies and organizations are involved in attracting investment to fund infrastructure in Nigeria. These include: the Infrastructure Concession Regulatory Commission (established to superintend and regulate PPPs), Nigeria Sovereign Investment Authority (tasked with enhancing the development of Nigeria's infrastructure among other responsibilities), Nigeria Investment Promotion Council (responsible for encouraging, promoting and coordinating all investments in Nigeria), and other development financial institutions (Bank of Agriculture, Bank of Industry, Development Bank of Nigeria PLC, Federal Mortgage Bank of Nigeria, Nigeria Export Import Bank, and The Infrastructure Bank). The Tax Credit Scheme was established in 2019 to encourage private participation in building critical infrastructure. The new administration could look into a more robust framework for coordination to avoid duplication of efforts and possible scope for streamlining and merger.

Policy Institutions and Coordination of Fiscal and Monetary Policies

The quality and strength of policy institutions matter in navigating a country through economic challenges.[3] These important foundations have to be adequate and robust for the proposed fiscal measures to work and produce desired results. Nigeria has in place a number of fiscal rules as stipulated in the Fiscal Responsibility Act (2007). It limits the size of fiscal deficit and presents conditions under which this target could be breached.[4] The CBN Act (2007) limits the size of monetary financing of fiscal deficit.[5] The main reason behind these rules is to anchor the conduct of fiscal and monetary policy and ensure macroeconomic stability. In instances where these rules are not respected on a consistent basis, it would be extremely difficult to achieve and maintain macroeconomic stability, as policy credibility wanes. Respecting or implementing existing legislations pertaining to monetary and fiscal policies will signal policy commitment and bring about credibility.

3 Policy institutions refer to the organizational and procedural arrangements (including enabling legislations) through which decisions on policy matters are taken, or that provide input into such decision making.

4 Nigeria's Fiscal Responsibility Act (2007) limits aggregate expenditure ceiling for each financial year to not more than the estimated aggregate revenue plus a deficit, not exceeding three per cent of the estimated Gross Domestic Product or any sustainable percentage as may be determined by the national Assembly for each financial year. Aggregate expenditure for the financial year may exceed the ceiling imposed by the Act if in the opinion of the President there is a clear and present threat to national security or sovereignty of the Federal Republic of Nigeria.

5 The CBN Act of 2007 allows the monetary authority to grant temporary advances to the federal government due to a temporary shortfall in budget revenue. The total amount of such advances outstanding is capped at 5 percent of the previous year's actual revenue of the federal Government. All advances are repayable by the end of the Federal Government financial year in which they are granted.

Fiscal deficit and central bank financing (ways and means)

With the government relying extensively on the central bank to finance its expenditure, the CBN's political and operational autonomy is inevitably undermined with adverse implications for macroeconomic stability. The stock of central bank financing of fiscal deficit (ways and means) increased from N134.8 billion (0.2 percent of GDP) in 2012 to about N20 trillion (10.9 percent of GDP) as at end-June 2022. The next administration needs to move from relying on ways and means to finance the fiscal deficit. The starting point is expenditure adjustment, focusing on reducing the cost of governance, reducing administrative capital expenditures, and preserving productive expenditures.

Quasi-fiscal activities

The existence of various forms of quasi-fiscal activities makes it difficult to ascertain the level of aggregate demand at the policy design stage. Notable interventions include: the Anchor Borrowers Program, the Micro, Small and Medium Fund, the Real Sector Support Facility, 100 for 100 Policy on Production and Productivity, Tertiary Institutions Entrepreneurship Scheme, Targeted Credit Facility, The Healthcare Sector Intervention Facility, Nigeria Electricity Market Stabilization Facility, Nigeria Bulk Electricity Trading-Payment Assurance Facility, Infrastructure Facility for National Gas Expansion Program. These sectoral interventions could eventually and potentially deliver on alleviating supply-side constraints. In the short term, however, these well-intended interventions contribute to aggregate demand impulse, resulting in imbalances between aggregate demand and supply.

In addition, these quasi-fiscal activities tend to impact the overall public sector balance without affecting the federal government budget deficit, necessitating the call for a more comprehensive and integrated fiscal framework. The size of all these interventions enunciated above reached about N9 trillion (5 percent of GDP), before falling to about N5 trillion (2.7 percent of GDP). It has to be mentioned that Section 31 of the CBN Act (2007) grants it the power to perform developmental function. The Act, however, seems to put a cap on such intervention, as it indicates that "the total value of the holding of shares or, as the case may be, debentures to which this section applies shall not at any time exceed 10 times paid up capital and the general resources fund of the Bank." As at end-December 2021, the paid up capital and general reserves of the CBN stood at N280.08 billion ($632.5 million). This appears to put the maximum amount of CBN's intervention at N2.8 trillion ($6.3 billion).

There are a number of important policy questions that are emerging in view of the evolution of the operating balance of the CBN. The operating balance of CBN was a cumulative surplus of N245.22 billion ($1.3 billion) during 2012–16. This reversed during 2017–2021, with a cumulative deficit of N2 trillion ($5.8 billion). Could these interventions (not done at market-determined interest

rates) and financing of fiscal deficits through ways and means impact the operating balance of the CBN? Could the weakening of the operating balance of the CBN impact its decision to undertake mop-up operations, given interest costs implications? Could possible hesitancy in conducting mop-up operations have adverse implications for macroeconomic stability?

Fiscal-monetary policy coordination

The limited economic coordination at the Federal Government level is impacting economic performance. The important policy issue is no agencies at the Federal Government level have the responsibility for coordinating fiscal and quasi-fiscal activities. Sterilization of various quasi-fiscal interventions and fiscal-deficit financing tends to be associated with higher interest rates, with implications for growth. Additionally, a lack of consolidation of quasi-fiscal activities with the government's fiscal position may reduce the transparency and effectiveness of fiscal policy, engendering fragmentation of the budget and blurring of institutional responsibilities. More recently, the issue of coordination emerged following the announcement by the CBN to redesign and issue new series of N200, N500, and N1,000 denominations.

Striking the right balance between macroeconomic stability and economic development is tricky. Multiple objectives require more coordination, with potential implications for CBN's independence. There is also a risk of political pressure to focus relatively more on economic development policies at the expense of stability. There is broad agreement that there are limits to the scope of monetary policy actions and their effectiveness. Against this background, sustainable growth and price stability will require a coherent, integrated policy strategy that also includes contributions from fiscal and structural policies. One option that could be looked into is to have in place a fiscal and monetary policy coordination council, with the Minister of Finance and Governor of the Central Bank, and independent experts as members. There are countries that already have such a structure in place (the Coordinating Council in Egypt; and the Monetary and Fiscal Policies Coordination Board in Pakistan). In view of the daunting economic challenges that the Nigerian economy is facing, cutting across monetary, fiscal and structural issues, the new administration could consider such a coordination mechanism.

The role of international financial institutions

Economic instability with attendant social consequences in Nigeria has external spillovers for other African countries. The level of interdependence among sub-Saharan countries is significant. Nigerian spillovers to other African countries are mainly through banking, fuel pricing policy, and trade (in the case of its neighboring countries). For example, empirical analysis has demonstrated that removing gasoline subsidies in Nigeria would reduce smuggling and enhance the tax base in Benin and Togo. With its population and the size of the economy, getting things right in Nigeria

is a regional good. The IFIs have to take these external spillovers into consideration in designing financial and technical assistance support for Nigeria.

The section under options for additional financing brings to the fore the role that innovative financing could play in bridging infrastructure gaps in Nigeria and other developing countries. There is urgent need for enhanced efforts by IFIs, including IDA (the World Bank's concessional arm that includes a private sector window), to use their expansive lending toolkits to further catalyze more private infrastructure finance in Nigeria. This is particularly relevant in the use of AMCs and other instruments to attract additional financing to Nigeria and other African countries (Moore, 2022 and Lee and others, 2022).

The IMF could consider reverting to an assessment of intergenerational equity in its fiscal policy assessment and policy recommendation, using non-oil primary as the fiscal anchor (based on various versions of permanent income hypothesis). The International Monetary Fund through its surveillance framework and policy support instrument played a critical role in adopting oil-price based fiscal rule and establishing various forms of stabilization funds in Nigeria. However, since 2018 discussion on intergenerational equity has not really featured in its fiscal policy discussion with the Nigerian authorities (as presented in Article IV reports).

With a new administration and in view of current economic challenges and the need to address them to bring about macroeconomic stability, strategic and hands-on technical support from IFIs will be required. The proposed fiscal agenda is comprehensive, covering revenue, expenditure and financing. The IFIs have been providing TA in these areas. The new Administration will need a reform team to effectively design and implement measures put forward in this note, with TA support from IFIs. Timely delivery of these TAs is important, as the first year of a new administration is important in undertaking considerable economic reforms. TAs that focus on building capacity to sustain reform efforts would equally be important.

Conclusions

This note has covered a wide range of important issues critical to achieving macroeconomic stability in Nigeria. Macroeconomic stability is in jeopardy given current policy trajectory. The government's unfettered access to central bank financing and the extensive use of quasi-fiscal activities have delayed much-needed fiscal consolidation, allowing a build-up of fiscal vulnerabilities with current and future adverse macroeconomic consequences. Going forward, a growth-friendly fiscal consolidation is required. In addition, emphasis has to be placed on effective monetary/fiscal policy coordination, including through the establishment of a fiscal and monetary coordination council. Finally, it is important to note that the quality and strength of policy institutions matter in navigating a country through economic challenges.

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