Joseph O Sanusi: Management of Nigeria's domestic debt

Keynote address by Dr Joseph O Sanusi, Governor of the Central Bank of Nigeria, at the 7th Monetary Policy Forum organised by the Central Bank of Nigeria at the CBN Conference Hall, Abuja, 22 May 2003.

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Distinguished Senators,

Honourable Members of the House of Representatives,

Distinguished Invited Guests,

Ladies and Gentlemen,

It is my honour and privilege to welcome you to the 7th edition of the CBN Monetary Policy Forum. The theme of today's Forum "Management of Nigeria's Domestic Debt" has been chosen in view of the increasing concern over the rapid growth of Nigeria's public debt and its implications for economic stability.

An escalating debt profile presents serious obstacles to a nation's path to economic growth and development. The cost of servicing public debt (domestic and external) may expand beyond the capacity of the economy to cope, thereby impacting negatively on the ability to achieve the desired fiscal and monetary policy objectives. Furthermore, a rising debt burden may constrain the ability of government to undertake more productive investment programmes in infrastructure, education and public health. To avoid such a situation, it is imperative that the quantum and structure of the nation's debt be carefully managed in a manner that is consistent with the country's growth and development aspirations.

To appreciate the dimension of Nigeria's domestic debt burden, it would be pertinent to undertake a brief review of its development. First, Nigeria's domestic debt stock stood at ₦23.5 million or 1.0 per cent of GDP in 1960 and subsequently, increased rapidly to ₦8,231.5 million or 16.2 per cent of GDP in 1980, reaching N1,160.0 billion or 83.6 per cent of GDP as at end-December, 2002. The sharp increase in domestic debt stock, over the years, was attributable largely to the failure to embark on necessary adjustment, particularly at the time of declining revenue, that resulted in growing fiscal deficits and further domestic debt accumulation. Secondly, the bulk of the debt has been in short-term treasury securities with maturities of less than one year. Thirdly, the banking system, mainly the CBN remains the dominant holder of Federal Government Securities.

Ladies and Gentlemen, it bears repeating that one major problem that has hindered the attainment of macroeconomic stability and sustainable growth has been the excessive reliance by the Federal Government on borrowing from the banking system, particularly the CBN, to finance its large and unsustainable fiscal deficits. As you are all aware, such borrowing from the CBN amounts to the injection of high-powered money into the system, which has serious adverse implications on price and exchange rate stability. Similarly, it crowds out the private sector from the credit market, thereby stalling investment and output growth. Empirical evidence has shown that fiscal adjustment is critical to successful stabilization effort in countries facing domestic debt overhang.

It should be noted, however, that deficit budgeting, per se, is not the critical issue of concern. Rather, it is the size, source of financing and quality of expenditure. Over the years, the FGN has relied largely on the money market and less on the capital market, thus creating a mismatch between short-term funds and investment in capital projects. This points to the need to reactivate the dormant bonds market to attract household and institutional savings. In addition, the borrowed money must be prudently utilized in the execution of productive projects in order to enhance the capacity for repayment of both the principal and interest elements as they fall due. An effective debt management requires that borrowed resources must be productively utilized such that the economic and social rate of return is higher than the future servicing cost of the loan. A debt problem would naturally ensue when the resources that should have been deployed for the execution of productive projects are employed in the financing of current or past consumption. This raises two issues for discussion. First, there is need to evaluate the economic and social rate of return of all government projects. Second, there is need to resolve the question of inter-generational equity which will arise when the present generation incurs debt that is left for the next generation to settle.

Distinguished participants, until the creation of the Debt Management Office (DMO) in August 2000, the management of Nigeria's public debt statutorily rested with the Central Bank of Nigeria. Up until now, the law establishing the CBN entrusts it with the issue and management of Federal Government's debt instruments. The Bank is also empowered to grant temporary advances to the Federal Government (Ways and Means Advances) in respect of temporary deficiency in budget revenue, subject to a limit and full repayment by the end of that year. It is pertinent to note here that the discharge of these domestic debt management responsibilities by the CBN could be, and often had been, in conflict with monetary policy objectives. The establishment of the Debt Management Office should therefore be seen as a positive development that will enhance the efficiency of not only domestic debt management but also the effectiveness of monetary policy.

Indeed, in spite of the Bank's best endeavours in the prudent management of government's domestic debt, not much has been achieved by way of rationalizing public expenditure and trimming the size of domestic public debt stock. Some of the outstanding problems that call for urgent solutions include:

- How to ensure that borrowed resources are productively utilised, such that economic and social rate of return is higher than the future servicing cost.
- The restructuring of the existing public debt in favour of long-term in a way to compel better quality evaluation of the loans.
- How the capital market can play an increasing role in the funding of the federal government fiscal operations.
- The problem of intergenerational equity argument arising from debt over-hang.
- How to reduce CBN funding of Government and bring it in line with the Government's obligation under the West African Monetary Zone Protocol. Acceptable progress has, however, been made in this regard during the last two years.

Against this background, this Forum has been organised to proffer practical solutions on how to tackle the problem of the burgeoning domestic debt of the Federal Government. Participants are therefore challenged to come up with a credible framework that would prepare the road map, which will guide the Nigerian government in resolving this problem.

To this end, Ladies and Gentlemen, we have assembled today scholars, seasoned professionals and other key stakeholders in the economy to lead the discussions. I therefore urge all the participants at this forum to discuss freely and frankly in order to come up with useful ideas that will crystallize into an enduring solution to the country's debt problem.

Once more, I welcome you to this forum and wish you fruitful deliberations.