Joseph O Sanusi: A central bank look at fiscal policy management in Nigeria

Keynote address by Dr Joseph O Sanusi, Governor of the Central Bank of Nigeria, at the seminar of the Nigerian Economic Society on “Fiscal Policy Management in Nigeria”, Lagos, 22 May 2003.

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His Excellency, The Executive Governor of Lagos State, Asiwaju Bola Ahmed Tinubu,

The President, Nigerian Economic Society (NES),

Council Members of the NES,

Mr. Chairman,

Distinguished Speaker and Guests,

Ladies and Gentlemen:

I feel highly honoured to be invited as a guest of honour at this year’s seminar of the Nigerian Economic Society on “Fiscal Policy Management in Nigeria” and for an opportunity to present this Keynote Address. The theme of the seminar could not have come at a more opportune time, as the outcome is expected to assist the government in policy fine-tuning and implementation in the context of its economic agenda under the next dispensation. This is in recognition of the fact that fiscal policy is a major dimension of an adjustment programme to ensure a stable macroeconomic environment and improved growth performance. Suffice to say that sound fiscal policy management, predicted on consistency, sustainability, efficiency, accountability and transparency, is essential for accelerating the pace of economic recovery.

Since the 1970s, the government has been overly dependent on the oil sector as the most important source of revenue accounting for four-fifths of the total. Consequently, fiscal operations have been influenced by the uncertainties of the international oil market. To minimize the destabilising influence of the volatility in the price of crude oil on government budgetary operations, efforts have been intensified since the 1980s to broaden government revenue base and enhance the contribution from non-oil sources. Federal government expenditure has closely followed developments in the revenue flow, which has given rise to a boom/bust pattern. The rapid acceleration in government spending between 1973 and 1976 was so strong that the increased revenue earnings from oil over the period was more than absorbed, resulting in substantial deficits. It has been difficult to scale down expenditure whenever there was a significant deterioration in the oil market. The result was that government resorted to borrowing from the banking system, especially from the Central Bank, to finance the deficits, with adverse implications for domestic prices and the exchange rate. Like most of the other oil exporting countries, Nigeria experienced a sharp bust of inflation in mid-1970s as public expenditure rose.

It is noteworthy that fiscal dominance has been one of the sore points of monetary management in Nigeria, as it has tended to undermine the effectiveness of monetary policy. For most of the 1990s, for instance, the major source of general macroeconomic instability was the rising fiscal deficits of the Federal Government, financed mainly by the Central Bank. In recent times, the banking system has been characterized by the problem of excess liquidity arising from the expansionary fiscal operations of the three tiers of government, and the rapid monetisation of crude oil receipts. The large injections of liquidity into the system induced rapid monetary expansion that was substantially out of line with prescribed targets.

A major problem of fiscal adjustment in recent times is the difficulty of lowering the largest components of recurrent expenditure such as wages and salaries, while attempting to raise the level of capital formation. A keen observer will notice that over the past decade, recurrent expenditure has been dominant in total federal government expenditure. It was 67.4 per cent in 2002, compared with 56.9 per cent and 65.9 per cent in 2001 and 2000, respectively. To generate growth, a sizeable proportion of government expenditure should be allocated to capital and socio-economic sectors. Beyond the issue of allocation, the quality of the expenditure remains critical in ensuring efficiency and optimal utilization of resources. In this regard, the Federal Government has instituted the Due Process compliance principle, which is being implemented.

I wish to add that, to be able to measure the effects of policy, the availability of timely and reliable statistics on government revenue and expenditure cannot be over-emphasized. This is also consistent with the principles of transparency and accountability. There is a need for increased information-sharing on a regular basis, as information assymetry undermines policy design and analysis. It is noteworthy that this dispensation has witnessed the return of the Public Accounts Committee of the National Assembly and the oversight function of the Auditor-General of the Federation. These are welcome developments that should be sustained.

Before I conclude, permit me to highlight some of the practical ways of addressing the problem of fiscal dominance in order to enhance the effectiveness of monetary policy. First is ensuring how the overall budget deficit will be reduced and how it will be financed in a non-inflationary way. In this regard, current effort by the Federal Government to access the capital market and restructure the outstanding debt stock is a welcome development. Secondly, the Debt Management Office (DMO) should be encouraged to assume full responsibility for government debt management, thereby relieving the CBN of such role. Thirdly, there is a need to meet the West African Monetary Zone (WAMZ) convergence criterion, limiting central bank financing of government to 10 per cent of estimated current revenue. Fourthly, the enactment of the Fiscal Responsibility Act should be rigorously pursued.

Your Excellency, distinguished ladies and gentlemen, there is no doubt in my mind that the issue of fiscal policy management is very critical to the successful implementation of our economic programmes. In this connection, I hope the seminar will find time to ponder on the following issues:

(i) the need to establish a stabilization fund which will address the problem of revenue/expenditure volatility;

(ii) formulate viable fiscal rules which are consistent with our fiscal federalism, and

(iii) propose the way forward in addressing the problems of inter-generational equity argument arising from debt overhang.

I am convinced that the array of eminent professionals gathered here today will come up with concrete proposals that will enhance our fiscal policy in the medium to long-term.

I thank you for your attention.