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Economic Newsletter

A Review of Nigeria's 2017 Budget of Recovery & Growth

Nigeria's President Buhari presented the 2017 Budget to a rare joint session of the National Assembly on December 14th, 2016. The Budget speech was also the first major economic speech of the president since Nigeria went into a recession in the second quarter of 2016. The title of 2017 budget—Budget of Recovery and Growth also seemed to capture the mood of the country as the economy reels in its worst recession in 25 years.

According to the Minister of Budget & Planning—Mr. Udoma Udo Udoma, the strategic thrust of the 2017 budget is ensure that Nigeria gets out "of this recession and back on the path of growth" and to achieve this, "government must find the resources to spend on infrastructure, and to spend to reflate the economy". The central government's game plan is to "stimulate and attract private sector capital and private sector spending" with government spending.

To achieve this, the government intends to spend about 30.7% (₦2.24 trillion) of aggregate expenditure on Capital Expenditure (CAPEX) compared to ₦1.77 trillion in 2016 (22% of aggregate spending). Despite the big rhetoric on CAPEX, the budget still remains heavy on non-debt recurrent expenditure which is 41% of aggregate spending for 2017 (₦2.980 trillion) compared to ₦2.646 trillion in 2016 (36% of aggregate spending). This implies that personnel and overhead costs are on the rise. Debt service will be 23% of aggregate spending in 2017 (₦1.66 trillion) compared to 20% in 2016 (₦1.475 trillion). While fiscal policy makers have often touted Nigeria's benign debt to GDP ratio as a strong positive implying greater borrowing capacity, the largely ignored red flag remains the country's debt to revenue position. Based on these estimates, Nigeria will be spending as much as ₦33 of every ₦100 earned in debt servicing in 2017. This scenario creates a fiscal time bomb that will diffuse in the medium term. At the moment, it also crimps the country's capacity to splurge on infrastructure and also undertake other investments in social overheads.

On the revenue side, oil revenues are projected to rise by 176% to ₦1.985 trillion in 2017 (₦0.718 trillion; 2016) largely on the back of reforms. On the flip side non-oil revenues are projected to shrink by 6% to ₦1.373 trillion in 2017 (₦1.455 trillion; 2016) owing to the failure of reforms, principally in the foreign exchange market, thus affecting corporate performance.

Table 1: Nigeria: Federal Government Budget Summary

	2017		2016		Year-on-year change
	(₦ in trillions)		(₦ in trillions)		
Total Revenues		**4.942**		**3.856**	**28%**
Of which oil revenue:	*1.985*		*0.718*		*176%*
Of which non-oil revenue:	*1.373*		*1.455*		*-6%*
Of which Independent & other revenue:	*1.584*		*1.683*		*-6%*
Total Expenditure		**7.298**		**6.06**	**20%**
Of which non-debt recurrent expenditure:	*2.980*		*2.646*		*13%*
of which Statutory Transfers:	*0.419*		*0.351*		*19%*
Of which Capital Expenditure:	*2.240*		*1.588*		*41%*
Of which debt servicing:	*1.660*		*1.475*		*13%*
Budget Deficit		**-2.356**		**-2.204**	**7%**
Of which financing from Internal Borrowing will be:	*1.250*		*0.984*		*27%*
Of which financing from External Borrowing will be:	*1.067*		*0.900*		*19%*

Sources: Budget Office, Agusto & Co. Research

"The widening budget deficit especially on the domestic debt market where borrowing is projected to rise by 27% in 2017 will lead to a crowding-out effect on the private sector."

The Budget's Sore Spots

At a time of dismal economic performance characterised by economic contraction, and weak fiscal communication, the Budget will assume greater importance as a fiscal policy roadmap. However, this budget fell short of expectations. While Keynesian assumptions may be at the root of the government's fiscal plans to spend its way out of the recession, the budget will do little to stimulate private sector confidence for investments for a number of reasons.

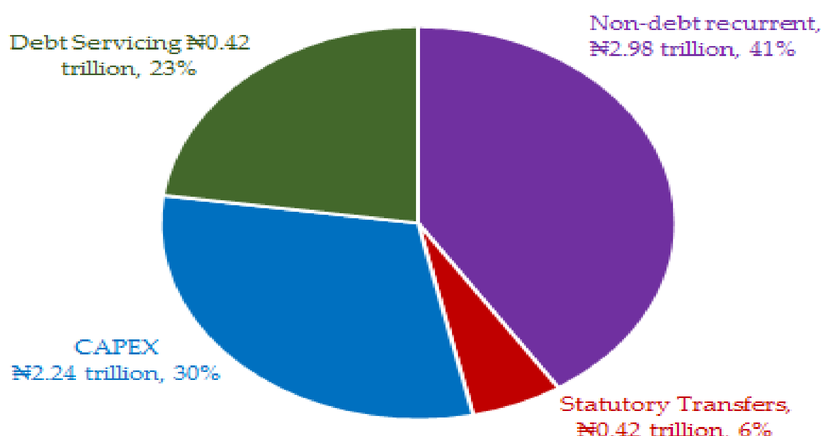
Firstly, the demand management strategies deployed by the Central Bank coupled with other knee-jerked polices—such as the arrest of currency traders selling above ₦400/US$—seem to have attracted little concern in the Budget. This germane issue is at the root of Nigeria's current recession and will remain a deterrent to investors until it is genuinely addressed through the proper policy framework. It has increased Nigeria's macro-risks and even poses greater dangers to the economy than the falling oil prices which initially popped the economic decline.

The inertia towards the FX price controls has led to poor corporate performance which has materially affected the ability of the Federal Inland Revenue Service (FIRS) and the Nigerian Customs Service (NCS) to meet their budgetary revenue targets.

The budget also reflects the statist nature of the Nigerian government. While Keynesian spending models may help prop the economy, the government also needs to embark on macroeconomic reforms that will stimulate investments and create jobs simultaneously.

The widening budget deficit especially on the domestic debt market where borrowing is projected to rise by 27% in 2017 will lead to a crowding-out effect on the private sector. The widening deficit at a time of deteriorating macro-indicators like inflation and unemployment will lead to higher borrowing costs for the government. The rise of the yields on the benchmark debts will also impact private sector borrowing costs and constrict investment capacity.

Figure 1: Breakdown of Government Spending



Source: Budget Office

"In the reforms for the JV cash calls, the government negotiated a significant debt forbearance of 20% on the total debts. This is a resounding victory for the government."

The Budget's Bright Spot

After enduring years of negative rhetoric leading to a hostile investment environment, it's quite ironical to see the oil and gas sector emerge as the bright spot in the 2017 Budget. The oil and gas sector's emergence as the Budget's bright spot has not been as result of increased government spending or increased allocation but largely on the back of progressive macro-reforms. The government is projecting oil revenues will rise by 176% to ₦1.985 trillion in 2017 (₦0.718 trillion; 2016) as a result of macro-reforms principally in the funding of the knotty Joint Venture (JV) cash calls and the sale of oil rounds licenses in 2017.

We like these reforms for a number of reasons and believe it is a game changing policy. In the reforms for the JV cash calls, the government negotiated a significant debt forbearance of 20% on the total debts. This is a resounding victory for the government.

In addition to the forbearance, the government also hinged the repayment of the debt balance on the incremental production by the JV partners. This creates an incentive for IOCs and other JV partners to increase production. This higher production levels can only be achieved through greater investments in production assets. The increased investments will have huge multiplier effects on the larger economy as well.

We genuinely hope that the positive effects of the JV reforms will spur the government to embrace macro-reforms in other sectors. These reforms should not only focus on increasing government spending but also seek to raise revenues while stimulating private capital to achieving wealth creation and generating employment.

When the government curbs its statist tendencies and allows a private sector led growth model, we will inadvertently be achieving the much trumped economic diversification as the government's revenue coffers soar from increased tax collection. Overall government will have to have a clearer understanding of the famous accounting line, profit "after" taxes – which implies that corporate Nigeria needs to generate the profits first in order to pay the taxes after.

Notes

Appropriation Act 2016

Federal Ministry of Budget and Planning: Public Presentation of the 2017 Budget Proposals By Senator Udoma Udo Udoma, Honourable Minister of Budget and National Planning

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