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THE STATE OF THE NIGERIAN ECONOMY AND THE POLICY OPTIONS*

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Alhaji A. Ahmed
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The President,
Chartered Institute of Bankers
of Nigeria,
Fellows & Members of the
Institute,
Distinguished Guests,
Ladies and Gentlemen.

I feel highly honoured to be invited once again as Guest Speaker on the occasion of our 1992 Annual Dinner. The subject matter I have chosen to speak on this evening, *The State of the Nigerian Economy and the Policy Options,* is relevant as it is the focal point of attention and some measure of concern.

In deciding to talk about the state of the Nigerian Economy, I was guided by the fact that Nigerians are now generally more reflective on what goes on in the economy than in the days of easy money. Such welcome development demands that frequent incisive information should be made available to enable our people understand why certain policy actions are necessary and some developments inevitable: From the start, let me say that the state of the Nigerian economy reflects a mixed bag of both good performance in a number of areas and unsatisfactory performance in some others. I should also add that the adoption of the Structural Adjustment Programme (SAP) since 1986 has not been the cause of the observed problems of the Nigerian economy. Those who have the tendency to associate the state of the economy with the SAP perhaps expected that the Programme was a magic and to solve all the nation's economic problems and ensure recovery and prosperity almost overnight. Such people are therefore disillusioned that, rather than usher in economic prosperity, SAP appears to have brought hardship to the citizens. Such thinking gives one the impression that Nigerians may have so soon forgotten that our economy was virtually on the verge of collapse during the immediate pre-SAP years. At the risk of boring you, I wish to recapitulate briefly the economic antecedents which made the on-going economic reforms inevitable.

BACKGROUND TO THE ON-GOING ECONOMIC REFORMS

Mr. President, Distinguished Ladies and Gentlemen, you may recall that the story of Nigeria's severe economic down-turn dated back to 1978 when the international oil market experienced its first major crisis. However, the genesis of our problems should be traced back to the immediate post-independence years when the nation, in the haste to ensure rapid economic development, adopted a development strategy which gave undue prominence to the role of government, at the expense of efficiency in resource allocation and utilization. Thus, the problem merely reached crisis proportions in 1978 and the early 1980s, when the sudden collapse of the international oil market led to a sharp reduction in resources. Unfortunately, rather than trim the grandiose projects in the Third national Development Plan to reflect the short-fall in resources, the ostentatious consumption pattern continued unabated. Moreover, domestic production, especially in the manufacturing sub-sector, was oriented to import substitution based on imported raw materials.

The Military Administration in the late 1970's reacted to the economic crisis by introducing wide ranging austerity measures, including tight controls on imports and domestic prices and sharp reduction in public expenditures to restrain aggregate demand. With the temporary favourable developments in the oil market in the middle of 1979, thee measures were, however, relaxed by the succeeding Civilian Administration, culminating in fresh rounds of unprecedented and unbridled spending. When the oil prices again tumbled in 1981 as a result of a fresh global oil glut, the austerity measures were frantically re-introduced. From the advantage of hind-sight, we know that the austerity measures, even when they were further intensified by the Military Administration which took over from the civilian administration in 1983, could not salvage the economy because such demand management measures did not address the fundamental problems of the economy. It was this awareness which later advised the adoption of the SAP which sought to stem the imbalances in the economy and create the right incentives for efficient and sustainable economic growth. As you are aware, the Programme has two broad, but inter-related and mutually reinforcing components. The first emphasizes short to medium-term macro-economic stabilization aimed at minimizing the inflationary tendencies and achieving a viable balance of payments position. The second focuses on the elimination of economic distortions in the country's production and consumption pattern in order to encourage self-sustaining economic growth. I do not need to give details of the policy measures and instruments adopted since they are very well known to you. The most relevant issue at this point is what we have gained and learned from implementing the Programme.

THE STATE OF THE NIGERIAN ECONOMY

Mr. President, Distinguished Ladies and Gentlemen, there is ample evidence that the Nigerian economy initially responded positively to the economic reforms. However, for a number of reasons some of which I shall highlight later, there have been some slippages recently. In contrast to the negative growth rates recorded in the three years immediately preceding the adoption of the structural reform measures, the Gross Domestic Product (GDP) at 1984 factor cost, picked up in 1988, registering a growth rate of 7.0 per cent. The momentum was maintained up to 1991, with an annual average growth rate of 5.6 per cent during the period. This improvement was reflected in the major productive sectors of agriculture, mining and manufacturing. For instance, agricultural output rose steadily by 8.3 per cent in 1987 to 13.6 per cent in 1991, compared with the negligible growth rate averaging about 1.0 per cent between 1980 and 1985. The major agricultural export crops which had declined precipitously until the inception of the SAP in 1986, also bounced back with the liberalization of the export trade and abolition of the Commodity Boards in 1986. Industrial output also grew rapidly since 1986, while the rates of capacity utilization of domestic manufacturing firms edged up steadily from 37.1 per cent 1985 to about 40 per cent presently. Following the abrogation of import licensing, reduction of tariffs on imported machinery, increased emphasis on local sourcing of raw materials and easier access to foreign exchange resources.

In the area of monetary and banking developments, the pace of expansion and structural changes since the inception of the SAP has also been remarkable. The sharp growth in monetary aggregates which was a common feature in the pre-SAP era moderated considerably at the commencement of the Programme. The deregulation of interest rates also engendered positive developments initially by way of keen competition in the banking industry, resulting in improved services and the adoption of new products and strategies to attract deposits and encourage savings mobiilization. However, since 1988 the rapid expansion in money stock had resumed due largely to the method of financing the fiscal deficits. Also the emerging bank lending rates after deregulation have been unduly high and in most cases bear no reasonable relationship to the cost of funds and are detrimental to productive investment.

In the area of fiscal policy, the main objective of the reforms was to realign government expenditure with revenue which was to be boosted through embarking on some tax reforms. However, budget deficits have grown even larger mainly because of the intractable problem of huge debt service. On the other hand, Government has made some progress in the area of divestiture from investments in direct production through the privatization/commercialization of some public enterprises.

In the external sector, the country's balance of payments position; especially the current account, has improved significantly since the inception of the SAP. The supply of foreign exchange has also recorded marginal improvement, although the source remains predominantly oil export earnings. Supply from autonomous sources, mainly from non-oil exports has, however, risen from a modest figure in the immediate pre-SAP period to over US $2 million annually since the SAP. Demand for foreign exchange, on the other hand, has continued to be unduly high, putting severe pressure on the naira exchange rate which has consequently depreciated persistently over the years.

The pressure on the domestic price level has fluctuated widely since 1986. From a low of 5.4 per cent in 1986, the inflation rate rose to a high of 50.5 per cent in 1989. It then declined sharply to 7.4 per cent in 1990 before edging up again to 13.0 per cent in 1991. The main driving force was the excess liquidity in the economy which continuously fuelled aggregate demand. The sharp depreciation of the naira exchange rate and high bank lending rates exacerbated inflationary pressures. With regard to unemployment, official figures indicate relative improvement compared with the pre-SAP period. However, the number of unemployed school leavers has remained unduly high.

Thus, on balance, it should be stated that, for an economy which was virtually at the brink of total collapse in 1985, the performance highlighted above represents a significant improvement. However, the situation has changed radically recently owing to domestic and international economic developments. Following the deregulation of interest rates in January and the unification in March of the official and parallel market exchange rates which induced further depreciation in the naira exchange rate, the domestic prices of goods and services were substantially increased which in many cases could not be justified by the change in the exchange rate policy. The high debt over-hand has also been a source of continuous pressure. On the international economic scene, the major problems were the worsening economic situation in the industrial countries, declining world commodity prices and exchange rate fluctuations all of which adversely affected Nigeria and other developing nations. As a result of these development; real economic aggregates in Nigeria deviated from the projections during the first half of 1992. Domestic output growth declined, largely as a result of lower agricultural and industrial output. The balance of payments position showed a deficit, as against the expected surplus, while the inflation rate more than doubled the 13.0 per cent recorded in 1991.

THE LINGERING PROBLEMS AND CHALLENGES

The above developments may engender a feeling of despondency. It might also be convenient to look for scapegoats. However, such an attitude is not only negative and unhelpful but also tends to detract from the need to identify the challenges and make one best endeavours to turn the challenges into opportunities. There have been problems with the implementation of the exchange rate, monetary, fiscal, trade and pricing policies, as well as in policy co-ordination generally. Partly because of these, the restructuring of production and consumption patterns and the achievement of economic recovery have been rather slow. Inflation, unemployment and inadequate capacity utilization have also been matters of concern. The huge debt over-hang is a serious problem that requires new initiatives and strategies. We also have to contend with an increasingly hostile international economic environment from which it has proved extremely difficult to attract external finance and foreign investment to support our adjustment efforts. Even more worrisome is the continued high import dependency of the Nigerian economy which SAP was intended to substantially reduce. Since the country cannot now revert to the regime of stringent trade and exchange controls, what is needed is robust and sustained non-oil export growth.

FUTURE PROSPECTS AND POLICY OPTIONS

Mr. President, Distinguished Ladies and Gentlemen, the immediate challenge facing us in our economic management is to bring the economy back on track and thereafter ensure sustainable economic growth. This implies a steady rise in per capital income, employment opportunities, and reasonable price stability. The future prospects for realizing these desirable goals, in my candid opinion, are intricably tied to the continuation of the on-going economic reforms. Experience with structural adjustment programmes worldwide indicates that they are difficult and costly to implement, both in terms of the short-term economic and political sacrifices they entail. These realities have often compelled some people to raise the issue of alternative economic reform programmes, ranging from an ultra-marxist position, where government is expected to control virtually everything, to an ultra laissez-faire situation where the government has no role. In particular, the most talked about 'alternatives' in this country to-day appear to favour the restoration of massive government controls which were in vogue in the past and had failed woefully. Therefore, advocacy for their reinstatement, especially in our context, seems to me to be retrogressive and out of touch with both our historical experience and the present realities. Indeed, recent developments world-wide suggest that most countries now favour replacing command economies rendered paralytic by weak administrative capacities with market-oriented systems in which prices and private entrepreneurial initiatives rather than administrative fiat determine the direction and pattern of investment and production.

There is a need, however, to fine-tune policies from time to time, in the light of experience. Our experience in the past seven years, for instance, has clearly shown that a major set-back has been the persistence of macro-economic instability. In the years ahead, serious efforts must be made not only to keep within macro-economic targets, but also to ensure a high degree of consistency among the variables. The institutional adjustments for enthroning a more effective financial sector must be speedily undertaken. Exchange rate policy should more than ever before be used to achieve balance of payments viability. Indeed, the medium to long-term objective of our exchange rate policy should be to make the FEM self-supporting and eventually ensure the achievement of complete convertibility for the naira. It must be stressed that the exchange rate reflects the economic condition of the country in relation to the rest of the world and any attempt to fix it arbitrarily will prove unsuccessful and unwise ultimately. The temptation to do so should therefore be resisted. Similarly, there is the need to boost foreign earnings through export diversification and growth.

Finally, it should be emphasized that the effectiveness of macro-economic policies hinges on the efficient implementation of policies. Sectoral policy objectives, strategies and measures should therefore be as far as practicable consistent with and complementary to the macro-economic policy framework. Economic efficiency through insistence on cost recovery should be emphasized, while inefficiencies engendered through subsidies must by systematically eliminated.

Distinguished Colleagues, Ladies and Gentlemen, these are some of the leading issues on the state of the economy which should engage the attention of all especially at this period of transition in our country. I hope the banking industry will continue to make positive contributions to the development of the Nigerian economy in the years ahead. But, individually, we should continuously ask ourselves whether we are making such contributions. This self-examination, should help this economy in the most critical period of its evolution if it results in everyone doing better than before.

I thank you for your kind attention.

13th November, 1992