Economic and Financial Review

Volume 53 | Number 4 Article 9

12-1-2015

Financing government programmes in economic downturn: policy options

F.U. Jacobs

Financing Government Programmes in Economic Downturn: Policy Options

Frank U. Jacobs*

I. Introduction

Distinguished Guests, Ladies and Gentlemen, it is an honour to be a Guest Speaker at the 2016 CBN Executive Seminar with the theme, "Financing Government Programmes in Economic Downturn – The role of Central Bank of Nigeria". The theme of the Seminar is apt and timely, considering what our country is passing through at the moment. I commend the organisers' sense of judgement and remain grateful for the opportunity to speak on "Financing Government Programmes in Economic Downturn: Policy Options". For obvious reasons, I will zero in on policy options for the manufacturing sector of the economy.

The concept of business cycle clearly explains long-term swings in economic behaviour which can be classified as a period of economic boom, recession, depression and recovery. However, while little attention is given to the period of economic boom since it implies economic prosperity; greater attention is paid to the period of economic recession. Interestingly, it is common knowledge that sound economic management in the period of boom can mitigate the challenges of the period of economic downturn. Countries that have effective economic management framework in place tend to be less impacted during economic crisis. The economic impact and policy solutions of the various global economic downturns, including the Great Depression that began in 1929, the Asian economic crises that started in 1997 and the Global Financial Crisis of 2007/2009, are well documented in the literature.

Nigeria has had its fair share of economic crises which include the economic recession of the early 1980s, 1990s, 2007/2009 crisis and the current challenge. I believe that the current economic challenges would be eventually contained. Containing economic crises requires a sound and strategic economic management framework. Each of the three major global economic crises earlier referred to had devastating impact both on world output and on the economic performance of the individual countries

** Dr. Frank Udemba Jacobs is the President of the Manufacturers association of Nigeria (MAN). The usual disclaimer applies.*

affected, but were eventually contained with the implementation of requisite policy actions.

In the case of the Asian economic crisis, key policy actions employed included:

- Strong government commitment to resolving the challenge;
- Strong focus on price stability and economic growth;
- Timely and forceful reactions of both monetary and fiscal policy-makers;
- Good coordination between the two authorities working;
- Reduction of interest rates on main refinancing operations;
- Well designed and implemented stimuli package;
- Tax cut (CIT and PAYE) and increase in unemployment benefits;
- Government support for the banking sector to maintain the flow of credit; and
- Low interest rates on new government bonds.

II. Financing Government Programmes in Economic Downturn: Policy Options

The downturn Nigeria currently is facing calls for strong government resolve and commitment to re-energise the economy for increased revenue, as any programme contemplated by the government can only succeed if there is adequate revenue to execute such programmes. We should take a cue from strategies adopted by other countries to overcome incidences of downturn in their economies. The major problem which Nigeria has experienced and which has impacted negatively on the economy is the over-dependence on crude oil revenue and weak industrial and manufacturing base of the economy. The drive by the current administration to diversify the economy is, therefore, a step in the right direction as this would further insulate the economy from the current ugly experience and also, future external shocks.

To this end, all efforts to increase non-oil revenue should be pursued vigorously through the following strategies: the industrial sector, especially the manufacturing sub-sector, should be strengthened by removing all obstacles restraining the growth and competitiveness of the sector such as the indiscriminate changes in the Monetary Policy Rate (MPR) which has been changed as many os 4 times between 2014 and July 2016, with its distorting effects on the economy; the exclusion of 41 items, mainly of essential raw materials from the official foreign exchange market as well as failure to synchronise monetary and fiscal policy actions. This will enable the sector to be optimally productive and play its expected role of employment generation, capital mobilisation and wealth creation as well as technology acquisition.

The resource-based industrialisation strategy championed by MAN and adopted by the Federal Government should be intensified as it involves the utilisation of the country's abundant natural resources in producing goods that the economy needs. This is a more sustainable and enduring form of industrialisation, compared with the import-dependent industrialisation option which has held sway over a long period. This would also save the country a lot of foreign exchange currently used in importing raw materials and free funds for government's development projects.

Intensification and aggressive undertaking of the development of key selected mineral resources through backward integration, especially those with high inter-industry linkages such as iron ore, zinc-lead, bitumen, limestone and coal. Government should intensify backward integration in the agricultural sector to catalyse more industrial input supply from the sector. These would also free more funds for the government.

Reduction of the MPR and by implication other rates, especially refinancing rates and bank lending rates as the inflationary situation in the economy may not be purely a monetary phenomenon, but could also be a result of output gap created in the real sector; creation of special funding windows for the manufacturing sector, in view of its long-term gestation period, should be given serious consideration. This is in addition to the existing Bank of Industry which, at any rate, is under-funded.

Adoption of concessionary foreign exchange allocation mechanism for the manufacturing sector for raw materials and machinery. This would enable the sector to increase its productivity and become more competitive.

Encourage export of manufactured and other non-oil products as a way of boosting foreign exchange earnings for the country as well as, activate automatic stabilisers, especially for the industrial/manufacturing sector; allowing the payment of import duties and Company Income Tax (CIT) with the existing Negotiable Duty Credit Certificate (NDCC).

Development of support infrastructure so as to facilitate the country's industrialisation efforts. With the current situation, however, it may not be advisable to use borrowed funds only to finance infrastructure development. The private sector should be actively involved in infrastructure development. Government should, therefore, resuscitate the Public Private Partnership (PPP) programme through the establishment of Concession Agreements under Built-

Operate-Transfer (BOT) in road construction and maintenance, rail construction and maintenance, among others.

Proper deregulation of the downstream petroleum sector to encourage private investment in domestic refining and petrochemical industry. Government should consider privatising the four national refineries to make them fully functional and save money for other purposes.

External and Domestic borrowing is an important and veritable option open to Government in this period of economic hardship, considering that Nigeria's current Debt/GDP Ratio of 20.77 per cent stands below the World Bank benchmark of 40 per cent. However, borrowing should be of very low interest rate, contracted on long-term basis, and targeted, preferably at the productive sectors of the economy.

Adjusting taxes (Corporate Income Tax, Value Added Tax, and Personal Income Tax) is another credible option that is open to government. However, considering that the country is at the brink of recession with growth of the productive sector being negative and the prevailing weak consumption as a result of inflation, it is not advisable to increase CIT, VAT and PAYE. Already, the productive sector is hit with dwindling investment, thus, any further tax increase will crowd-out more investment in the sector. I would, therefore, suggest that the current Tax-GDP Ratio of 12.0 per cent, which is below the World Bank Benchmark of 18.0 per cent, may be raised by widening the tax net and ensuring that all taxable individuals and entities are covered. Taxes on luxurious goods and property may also be raised.

III. Conclusion

Distinguished participants, ladies and gentlemen, you may be wondering why I have concentrated mainly on the manufacturing sector of our economy. This is my primary constituency. I recognise that there are other very important options, but I believe that other speakers would speak on those. I am strongly convinced that with the above suggestions, Nigeria should be able to contain the present economic downturn.