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The Structural Adjustment Programme: the Journey so Far

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THE STRUCTURAL ADJUSTMENT PROGRAMME: THE JOURNEY SO FAR*

Mr. Chairman,
Eminent Professional Colleagues,
Distinguished Ladies and Gentlemen,

It is a pleasure for me to be invited as the guest of honour on this august occasion of our 10th Anniversary Dinner. After the sumptuous food and drinks that we have been served this evening, I am sure that we are not in the mood for any long speeches. Mr. Chairman, the Institute has given me the liberty to address you *briefly* on any topic of my choice. I have therefore chosen to address you this evening on: "The Structural Adjustment Programme: the Journey so far" since I believe that this forum is an appropriate one to review briefly our experience so far with the Structural Adjustment Programme (SAP) now in place. The Programme has been widely acclaimed as the most radical economic programme ever to be launched by any government in this country. As co-participants in the implementation of the programmme, I welcome the opportunity offered us to come together and reflect on the path which we have trodden since SAP was introduced in July, 1986.

Distinguished Ladies and Gentlemen, it is logical to begin this address by casting a retrospective look at the economic situation in the country before the adoption of the SAP. In this regard, we should remind ourselves that the SAP was designed to attack and remove the fundamental structural distortions prevalent in the Nigerian economy since the 1970's. Although it must be acknowledged that while we made significant progress in some areas in the past, notably in the provision of physical and economic infrastructures, some of the projects executed were later found to be unviable while others were beyond the capacity of government agencies to execute. Instead of making the economy more self-reliant, the policies pursued during the period made the Nigerian economy vulnerable to further external shocks. Specifically, price distortions created by a highly over-valued currency and inappropriate institutional arrangements led to inadequate pricing of agricultural and other local products. Also the policy incentives and control measures only encouraged the setting up of manufacturing ventures based on wholesale imported inputs. The public sector involvement in economic activities became pervasive such that the sector accounted for about half of the GDP and two-thirds of modern sector employment by 1980. The apparent affluence at the time blinded us as a nation to the precarious economic situation. It only needed the glut in the world oil market in the second half of 1981 to expose the shortcomings of the economic policies being pursued and the unpreparedness of the government to tackle realistically a fundamental economic problem. In any case, it was thought at the time that the problems caused by the oil glut would be short-lived. We now know better that the hope was illusory.

The policy measures taken between 1982 and early 1986 were in the form of intensified payments and trade controls, the effects of which are so familiar that they do not need any elaborate enumeration here. Suffice it to say that the control measures were not only largely unsuccessful, but also led to a situation of drastic short-supply of industrial inputs, plant closures, large scale retrenchment of workers, shortage of goods and price inflation. At the same time, external debt increased rapidly through an indiscriminate recourse to external borrowing and accumulated unpaid trade bills. Even then, debt service payments rose many folds from 1984/85 above the level in 1980. Our foreign creditors thus became more impatient with us and in consequence refused to grant us further credit and in exceptional cases where lines of credit were provided, they were given at prohibitive costs to the economy. By the end of 1985, it became obvious that nothing less than a comprehensive structural adjustment would effect the desired turn-around of the economy. It was in this regard that the 1986 Budget set the tone for the two-year Structural Adjustment Programme which was launched in July 1986.

The Structural Adjustment Programme (July 1986 to June 1988)

The SAP was introduced to achieve the following objectives:

(i) To restructure and diversify the productive base of the economy in order to reduce dependence on the oil sector and imports;

(ii) to achieve fiscal and balance of payments viability over the period;

(iii) to lay the basis for sustainable non-inflationary or minimal inflationary growth;

(iv) to lessen the dominance of unproductive investment in the public sector, improve the sector's efficiency and intensify the growth potential of the private sector.

In order to achieve these objectives, a shift in economic policies became necessary. The main elements of the SAP evisaged not only strengthening demand management policies but also adopting measures to stimulate domestic production and broaden the supply base of the economy. Thus, the adoption of a realistic exchange rate policy, rationalisation and restructuring of the tariff to promote industrial deversification and increased trade and payments liberalisation, and abolition of complex administrative controls are therefore the key elements of the SAP.

Summary of the Economic Measures Adopted so far under the SAP

Since the introduction of the SAP, a number of economic measures both monetary and fiscal, have been adopted to deal with the identified internal and external problems facing the Nigerian economy. With respect to the external sector policy measures, the Federal Government introduced the second-tier foreign exchange market (SFEM), now FEM, with the effect from 29th September, 1986. The objective was to allow market forces of demand and supply to determine the naira exchange rate and thereby do away with the discretionary administrative fixing of the rates. To complement the new exchange rate policy, there was an interim review of the Customs and Excise tariff, while the list of banned items was pruned down from 74 to 16.

Appropriate changes were also made in the Monetary Policy Circular No. 20 of January 1986 including the reduction from 10.0 per cent to 7.6 per cent in the ceiling imposed on the rate of credit expansion by the big and medium-sized banks. The maximum ratio of merchant banks' total loans and advances to total assets less contingent liabilities was limited to 50.0 per cent. A more flexible interest rate policy was also adopted. Thus interest rate payable on time deposit was fixed at 9.5 per cent in place of the previous range of 8.5 to 12.0 per cent. This gave depositors freedom to negotiate higher rates with their banks. The ceiling

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on bank lending rates was raised from 13.0 to 15.0 per cent while other rates were to adjust accordingly.

Also, the Export (Incentive and Miscellaneous Provision) Decree No. 18 was promulgated in July 1986 to provide refinancing and rediscounting facilities by the Central Bank of Nigeria aimed at assisting the banks to provide the requisite export financing. This became necessary because following the abolition of the Commodity Boards in 1986, the Commercial and Merchant Banks once again assumed the task of providing the funds to finance export activities of the private sector.

Some of the fiscal measures adopted before July 1986 were reviewed and rationalised in line with the SAP with a view to ameliorating the envisaged inflationary impact of the FEM and also to protect local industries. An interim Customs and Excise tariff was introduced which made temporary adjustment in the tariff structure. The 30.0 per cent Consolidated Import Levy introduced at the beginning of 1986 was abolished. Import duties on basic industrial raw materials, agricultural inputs and some consumer/final goods were reduced. On the other hand, duties on some capital, consumer and luxury items were raised.

In 1987, the fiscal measures were strengthened and reinforced. An adjustment was made in the interim tariff in order to, among others, protect local industries as well as rectify some anomalies already identified in the interim tariffs and enhance the competitiveness and productivity of the affected industries. Consequent on the adjustment, duties on public transport items as well as those on newsprint and kraft paper were adjusted downward. Similarly, advance payment of import duty was reduced to 25.0 per cent of the assessed cost of goods.

The taxation measures in 1987 were geared towards improving the revenue collection machinery, maximising tax revenue, stimulating investment in priority sectors and reducing the tax burden. The new tax reliefs granted, relating to companies and individuals in 1987, include the enjoyment of tax free dividends for a period of three years if:

(a) The company is incorporated in Nigeria;
(b) the equity participation is imported into the country between 1st January, 1987 and 31st December, 1992; and
(c) the recipients' equity participation in the company constitutes at least 10.0 per cent of the company's share capital.

In addition to these, the company paying the dividends will enjoy a tax free period for five years if it is engaged in any of the following activities: agricultural production within Nigeria, processing of Nigerian agricultural products within Nigeria, and the production of petro-chemical or Liquefied Natural Gas (LNG). Concerning Companies Income Tax, the tax rate was reduced from 45.0 per cent to 40.0 per cent. Finally, Capital Allowances rates were reduced by 5.0, 12.5 and 5.0 percentage points, respectively, for furniture and fittings, research and development expenditure, and motor vehicles.

The monetary and banking policies for 1987 as contained in the Monetary Policy Circular No. 21 were designed in the context of the SAP with the objectives of moderating inflationary pressures likely to arise from FEM operations and stimulating domestic financial and efficient resource allocation. The other objectives were to encourage foreign capital inflow and increase export earnings from non-oil sources: stimulate local production of goods and services and ensure an improvement in the balance of payments. In conformity with these objectives, the 1987 monetary policy was largely restrictive, curtailing the growth in money supply to 11.8 per cent and placing a ceiling of 4.4 per cent on the expansion of aggregate bank credit to the economy. It also reduced the categories of sectors of the economy for purposes of bank lending from 4 to 2, namely, "high priority sectors" comprising agriculture and manufacturing enterprises and "others."

In order to accelerate the attainment of the objectives of the SAP, it became necessary to amend Monetary Policy Circular No. 21. Thus with effect from 1st August, 1987, the following changes were introduced:

(i) The 8.0 per cent of ceiling on commercial bank credit expansion for the whole year was revised to 7.4 per cent for the last three quarters of the year. Quarterly targets were also set to facilitate monitoring of the banks' performance.
(ii) In the case of the merchant banks, their ratio of total loans and advances to total assets (less contingent liabilites) during the remaining three quarters of 1987 was reduced from 55.0 to 37.5 per cent. It had earlier on been raised from 50 to 55 per cent in January 1987.
(iii) Henceforth, the ceilings would apply to all loans to agricultural production and marketing, manufacturing, export and export financing.
(iv) New and small banks with total loans and advances of not more than ₦100 million as at end-December 1986, were allowed to increase their lending by up to 15.0 per cent, in 1987.
(v) Banks granting credit in excess of the permissible rate of expansion were required to deposit an amount equivalent to the excess with the Central Bank of Nigeria. Such deposits would be non-interest bearing and not eligible for inclusion in the banks' liquid assets holding for the purpose of calculating the statutory liquidity ratio.

All controls on interest rate were removed in line with the emphasis on deregulation of the economy under the SAP. The minimum rediscount rate of the Central Bank was fixed at 15.0 per cent effective 1st August, 1987. This was meant to serve as a signal to the banks of the desired direction of interest rates changes. As a means of encouraging the private sector non-bank public to invest in government securities, the treasury bill rate was also raised from 10 to 14 per cent while comparable adjustments were made to treasury certificates. The minimum liquidity ratio for commercial banks was raised from 25 to 30 per cent.

In order to encourage manufacturing for exports, a duty drawback-suspension scheme was introduced whereby materials and intermediate imports for use in the manufacture of export products were allowed to be imported free of import duty. With the introduction of FEM, and as an encouragement to promote non-oil exports, exporters were allowed to retain 100 per cent of their export proceeds. Such proceeds which are to be lodged in their domiciliary accounts could be used by them for eligible external transactions.

In the rest of the real sector of the economy, the Directorate of Food, Roads, and Rural Infrastructures was strengthened for the purpose of accelerated programme of rural development. For instance, the Directorate was, among others, required to build additional 30,000 kilometres of feeder roads in 1987, launch a rural electrification scheme as well as implement a national rural water supply scheme during the year.

A Brief Evaluation of the Policy Measures

Most of the measures introduced under the programme are medium-term and as such require more time before a deep and thorough evaluation can be made. Moreover, there are some elements of the SAP which are yet to be fully implemented.

However, the effect of the SAP so far has been generally beneficial though it has created some side problems. The most immediate impact of the SAP has been on the external sector of the economy through the introduction of SFEM to establish a realistic market determined rate for the Naira. The naira exchange rate which was officially fixed at ₦1.5535 = $1.0 on 25th September, 1986 fell to ₦4.6406 = $1.0 at the first bidding session of the SFEM on 26th September, reflecting a depreciation of 66.5 per cent. The value fluctuated widely in subsequent biddings. In 1987, the value of the currency has almost persistently declined from the end-December, 1986 level. As at the end of September 1987, ₦4.2227 exchanged for U.S. $1.0, representing a depreciation of 21.4 per cent from the level at the end of 1986.

One significant highlight in 1987 was the merger of both the first-tier and the second-tier exchange rates at ₦3.7375 to the dollar on 2nd July, thus creating a single free foreign exchange market for the country. Although the FEM exchange rates cannot be regarded as stabilised, there is greater stability in rates now than when SFEM took off. Also the correction of the large over-valuation of the naira exchange rate prevalent before the introduction of the new exchange rate policy was a major policy achievement. The on-going policies have reduced to the minimum the hitherto high taste for consumer imports. The exchange rate policy coupled with the export promotion strategy and the abolition of the Commodity Boards, have boosted producer income and government revenue. The improvement in the domestic revenue of the state governments attendant on the exchange rate policy, has made it possible for them to pay the salaries of civil servants on a more regular basis. In addition, the export promotion strategy has resulted in a more diversified export base. It has been observed that apart from the traditional cash crops, new items such as textiles, beer, handicrafts, etc. have recently entered into the export market although on a modest scale. The retention of export proceeds wholly by the exporters has contributed to the recorded increase in inflow of foreign exchange from autonomous sources. Available data show that during the first eight months of 1987, inflow of foreign exchange from autonomous sources amounted to $654.5 million.

On external transactions generally, the introduction of SFEM has rendered administrative control on trade and foreign exchange unnecessary. This has produced a good relief to all categories of foreign exchange users, particularly the business sectors. The removal of control has eliminated the adverse factors such as delays in processing import licence and foreign exchange applications, corrupt practices associated with controls, and other social factors which used to contribute to increases in the cost of production.

You are no doubt aware of the favourable disposition of the international community towards the SAP. More specifically, the implementation of the SAP has led to an improvement in our external payments arrangements and in our international credit worthiness. Although negotiations to reschedule part of our external debt outstanding have been prolonged, significant progress has been made in this regard.

We have already concluded bilateral agreements with a number of member countries in the Paris Club group of creditors while it is expected that the agreement on rescheduling terms with the London Club creditors may be signed before the end of this year.

As bankers, we already know the immediate impact of the monetary policy being pursued under the SAP. One effect of the policy has been the keen competition among banks for deposits and bankable projects which has been fostered in the past eighteen months. Savings and time deposits with the banking system increased by about ₦1 billion or 9.0 per cent during the first half of 1987 largely as a result of the more attractive interest rates now offered by banks on deposits. The impact of deregulation of interest rate since August 1987 may be too early to assess. However, the policy is meant to ensure that bank credit is put into more efficient use. It is also expected to enhance inflow of foreign capital, discourage capital flight, and lend support to the naira exchange rate.

The increase in interest rate should reduce the incentive for businessmen to carry large inventories and release funds from inflation hedges for productive investment. It should also improve the mix of resources to be utilised in production in favour of labour.

In the area of government finances, significant improvement has also been recorded. While deficit financing remains a problem, the size of government budget deficit has been reduced. The target is to bring government budget deficit down to 3.00 per cent of the Gross Domestic Product (GDP) during the programme period, down from 4.48 per cent in 1986.

The evidence in the industrial sector is that a number of industrial enterprises, particularly those which are heavily dependent on imported inputs, continue to record low rates of capacity utilization. However, in those industries which are less dependent on imported inputs, significant increases in capacity utilisation have been recorded. I believe that the message is clear to our industrialists generally. It is that they should continue to pursue relentlessly local sourcing of their raw materials. In this regard, it is noteworthy that steady growth has been recorded in the volume of locally produced raw materials in plastic products, paints, and meat products among others.

Distinguished ladies and gentlemen, while it is not my intention to paint a rosy picture of our achievements under the SAP, I believe it is worthwhile to highlight, as I have done above, the positive aspects of the programme. We should at the same time remind ourselves that some problems have emerged.

It is in the nature of things that the policies embodied in the SAP have by themselves led to some other problems such as increase inflationary pressure, although the prices of many commodities like milk, sugar, detergent are lower now than before SAP. The economy has also become less liquid, with consequent reduction in aggregate demand which may have become a factor in inventory accumulation. At the same time, some of the perennial problems not related to SAP are still with us. These include high level of unemployment, and disease and pest infestation in the agricultural sector.

While we recognise these problems, we also believe that if the SAP is implemented with full commitment, it is capable of restoring not only full economic recovery but also launching the economy on the path of sustained growth. The general problem is that the Nigerian public expects an immediate solution to deep-seated economic problems. There is probably no magic wand to these economic problems. The problems have been with us for too long that it will be expecting too much of any structural adjustment programme to bring about a turn around in the economy within a short time.

All that is necessary is for us to persevere, remembering that there is no adjustment without pains. Although it is common knowledge that a number of countries, unable to persevere, have abandoned their own structural adjustment programmes mid-way, I believe that it is in our own interest that we should allow the SAP to succeed in this country. Ours should be unique and exemplary for others to follow.

Distinguished ladies and gentlemen, I need not remind you that you have crucial roles to play in ensuring the success of SAP in Nigeria. Your compliance with our Monetary and Credit guidelines as well as other government regulations is the minimum contribution expected from you. I remain convinced that with your usual cooperation the SAP will succeed.

I thank you for your attention.

Alhaji A. Ahmed,
Governor
Central Bank of Nigeria