IV Structural Reform and Macroeconomic Policy, 1986–90

It became clear to Nigeria's economic policymakers that short-run stabilization measures and increased regulation were not appropriate responses to deep-seated impediments to growth. After considerable popular debate, the Babangida Government adopted in June 1996 a comprehensive structural adjustment program (SAP) that signaled a radical departure from previous adjustment efforts. It emphasized reliance on market forces and deregulation. The SAP was originally intended to last for two years, but was extended when it was realized that implementing many of the reforms required more time. However, toward the end of 1990, the Government began to retreat from the basic reforms of the initial program, and much of the momentum of the reform effort had been lost by then. Nigeria's adjustment efforts were supported by three stand-by arrangements with the Fund, but the Government decided not to use the Fund's resources (Box 3). The World Bank also supported the adjustment program through a US$450 million trade policy and export diversification loan.

The objectives of the SAP were to (1) restructure and diversify the productive base of the economy so as to reduce dependency on the oil sector and imports; (2) achieve fiscal and balance of payments viability over the medium term; and (3) promote noninflationary economic growth. The growth and inflation objectives for 1987–88 were a real GDP growth of 3–4 percent and a reduction of inflation to 20 percent per year on an average annual basis. It was thought that the anticipated devaluation of the naira would have a considerable impact on consumer prices.

The key policies designed to achieve these objectives were

- the tightening of financial policies through a reduction of the fiscal deficit to below 3 percent of GDP by 1988 and a limiting of the growth of broad money to 12 percent per year, the latter requiring limits on the expansion of net domestic bank credit on the order of 5–6 percent per year and net bank credit to the Government of 3 percent
- the adoption of a market-determined exchange rate
- the liberalization of the external trade and payments system
- the elimination of price controls and commodity boards
- the decontrol of interest rates
- the rationalization and restructuring of public expenditure
- the rationalization of the tariff structure and the overall lowering of tariffs
- the privatization or commercialization of most federal public enterprises (see Table 4).

Although significant progress was made in the liberalization of the economy, specifically through reform of the exchange and the trade system and the freeing of prices, macroeconomic policy implementation remained erratic and failed to bring inflation under control. Public criticism of economic policies increased, based on the notion that the disappointing results of the adjustment effort were a product of misguided policies under the SAP, rather than on the realization that incoherent implementation of SAP policies caused most the economic ills.

Price Liberalization and Subsidy Policy

The decontrol of prices at the start of the SAP was an important step in the liberalization of the economy. In 1986 the *Price Control Decree of 1971* and the *Commodity Board Decree of 1977* were repealed. The *Price Control Decree* had mandated the Productivity, Prices, and Incomes Board (PPIB) to announce annual price and wage guidelines for the private sector. The seven commodity boards[6] were

[6]The Cocoa Board (cocoa, coffee, and tea), the Groundnut Board (groundnuts, soya beans, benniseed, peanuts, and ginger), the Cotton Board, the Palm Produce Board (palm oil, palm kernel, and copra), the Rubber Board, the Grains Board (corn, millet, maize, wheat, rice, and beans), and the Tuber and Root Crops Board (yams and cassava).

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Box 3. Experience with Fund-Supported Programs

Nigeria's adjustment efforts were supported by three stand-by arrangements (SBA) between 1986 and 1992, spanning a noncontinuous period of 42 months. The Fund committed a total of SDR 1.44 billion, but Nigeria decided, based on the results of a national referendum, not to make purchases under these arrangements. The arrangements with the Fund opened the door to official debt rescheduling, which was a high priority for the authorities. The first Fund program (January 1987–January 1988) quickly went off track; the second (February 1989–May 1990) was successfully implemented; and the third (January 1991–April 1992) also went off track soon after its approval.

The three SBAs focused on fiscal adjustment and were designed against the background of volatile world oil prices. The last two SBAs incorporated some form of fiscal stabilization mechanism, which took account of deviations from programmed oil export prices. Over time, the stabilization mechanism did not prove very useful as it became a major source of funding of extrabudgetary projects. The first SBA incorporated a major exchange market reform and other liberalization measures, including a substantial increase in retail prices of petroleum products. It went off track early because of the diversion of oil revenue, which caused a budgetary shortfall and led to the accumulation of external payments arrears. The second SBA focused on fiscal adjustment, consolidation of earlier foreign exchange system reforms, adjustment of domestic petroleum product prices, and measures to strengthen the banking system. This program benefited from the recovery in oil prices, which, in combination with wide-ranging reforms at the outset of the SAP, led to a broad-based recovery of the economy. Fiscal adjustment was assisted by the establishment of a stabilization account to sterilize some of the windfall oil receipts, while monetary growth was controlled, in part, by the decision to transfer federal government accounts from commercial banks to the Central Bank in the summer of 1989. The vast improvement in the oil sector helped the country to achieve its macroeconomic objectives. The third SBA came in the aftermath of the 1990 oil price boom and in the midst of heightened efforts to regain the momentum of the transition to civilian rule. The emphasis of the program was on fiscal adjustment, but it went off track in the first quarter of 1991, mainly because of uncontrolled growth in federal government expenditures.

In terms of design, the reform efforts undertaken under the different programs incorporated some structural fiscal reforms, particularly in the areas of budgetary practices, public expenditure programming and management, oversight of state and local government budgets, and prioritization of investment projects under the rolling plan. However, these formal changes in official procedures had little effect on actual budgetary practices. Overall, fiscal adjustment was limited to short-lived stabilization measures without addressing the structural fiscal problems that were the root cause of Nigeria's internal and external imbalances. The lack of a durable fiscal adjustment, the inability to develop efficient allocative and distributional budgetary functions, and the backsliding in the implementation of key policies undermined domestic and international confidence in Nigeria's adjustment efforts.

responsible for setting producer prices for the country's major agricultural crops. Their elimination, in conjunction with the devaluation of the naira, was instrumental in improving the profitability of non-oil export production, which increased substantially during the subsequent years.

Prices of goods and services provided by public enterprises remained largely under the control of the Government. This was especially true for the Nigerian National Petroleum Corporation (NNPC), the National Fertilizer Company of Nigeria (NAFCON), the Nigerian Electric Power Authority (NEPA), and other public utilities. Electricity tariffs remained unchanged between 1979 and 1989 at an average rate of ₦0.07 per kilowatt hour, equivalent to US$0.01.[7] They were raised to an average of ₦0.32 per kilowatt hour in mid-1989. The new tariff, equivalent to US$0.029 per kilowatt hour at the parallel exchange rate, was still less than half the rate prevailing in the United States in that year and substantially below the rate needed to improve services and eliminate the operating deficit of the parastatal.

The Government's efforts in the early part of the SAP to reduce further the subsidy on fertilizer and free up prices and marketing in the sector were overtaken by strong domestic pressure to stall the reforms, which led to higher subsidies during 1988–90. While the retail sales price of fertilizer was increased once during the SAP period (in 1986), the estimated subsidy element increased from about 30 percent in 1986 to more than 80 percent in 1989, largely as a result of the impact of the devaluation. The rising cost of the subsidy commanded some 70 percent of the agriculture ministry's capital budget in 1989, as compared with about 15 percent in 1983. With state and local governments sharing the cost of the subsidy equally with the Federal Government, the rising costs quickly overwhelmed their resources, with fertilizer-related costs accounting for an estimated 50

[7]At the average official exchange rate for 1989; the tariff was only 0.5 U.S. cents at the parallel exchange rate.

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Table 4. Structural Reforms and Policy Implementation

	1986	1987	1988	1989	1990	1991	1992	1993	1994
Structural/Policy Reforms									
Foreign exchange market[1]	√	√		√	√		√	×	×
Import liberalization[2]	√	√	×	×	×	×			
Export promotion[3]	√	×	√ ×	×					
Debt conversion			√				√		
Prices	√							√	√
Privatization/commercialization			√						
Interest rates[4]	√	√		×		×	√		×
Credit guidelines	√	√					√		
Financial sector					√	√		√	
Budget (tax/expenditure)									
Policy Implementation									
Inflation	—	+	+	+	–	+	+	+	—
Fiscal deficit/GDP	+	+	+	–	–	+	+	+	–
Petroleum subsidy		*	*	*	*	*	*	*	*
Fertilizer subsidy	*	*	*	*	*	*	*	*	*
Extrabudgetary expenditures	—	+	+	+	+	+	+	+	–
Growth in broad money	–	+	+	–	+	–	+	–	–
Real effective exchange rate (+ appreciate)	–	–	+	–	–	–	–	+	+
Official and parallel exchange rate spread	–	–	+	+	–	+	–	+	+
External current account	–	+	–	+	+	–	–	–	–

Key: √ indicates reform, × indicates reversal of reform; change relative to previous year where, – indicates a decline, + indicates an increase; * indicates variable was positive; — indicates figure is zero, or that the item does not exist.

[1]Prorate allocation of foreign exchange by CBN in 1993, fixed exchange rate in 1994.

[2]During 1988–91 higher tariffs or import bans were introduced.

[3]In 1987 export bans on grains were introduced and bans were extended to other commodities in 1988 and 1989. In 1989 the rediscount/refinancing facility for exports was introduced by the CBN.

[4]On November 10, 1989, the CBN introduced a maximum interest rate spread between saving and prime lending rates, the prime and the highest lending rates, and the interbank and prime lending rates. Ceilings were imposed on maximum lending rates at the beginning of 1991 and 1994.

percent of state and local government capital outlays in 1989. As important as the rising fiscal implications of the subsidy were the growing distribution problems, including unequal and delayed distribution, increased smuggling to neighboring countries, and a disproportionate share of the subsidy going to marketers.

The pricing of domestic petroleum products, especially gasoline, contained a large subsidy element. Domestic petroleum product prices are set by the Federal Government, as is the amount of national oil production allocated for domestic consumption. However, in January 1986 product prices were increased between 24 and 725 percent, with gasoline prices rising by nearly 200 percent.[8] The increase in the price of gasoline raised the domestic price well above import parity.[9] Prices for domestic petroleum products were subsequently raised in 1988 and 1990, and the implicit subsidy was temporarily reduced each time until it caught up with the depreciation of the naira. Thus, the ratio of the domestic price of gasoline to the world price fell from 186 percent immediately after the 1986 price increase to a low of 37 percent in 1990 (Figure 2).

Reform of the Exchange Rate

The precipitous decline in the terms of trade (52 percent) in 1986 convinced the authorities that exchange rate reform was unavoidable. The foreign ex-

[8]The price of household kerosene remained unchanged. With this exception, the lowest increase was for liquefied petroleum gas (24 percent).

[9]Measured at the official exchange rate, the domestic price of gasoline was 186 percent of the world wholesale price after the increase. Measured at the parallel exchange rate, the domestic price was still 10 percent below the world price.

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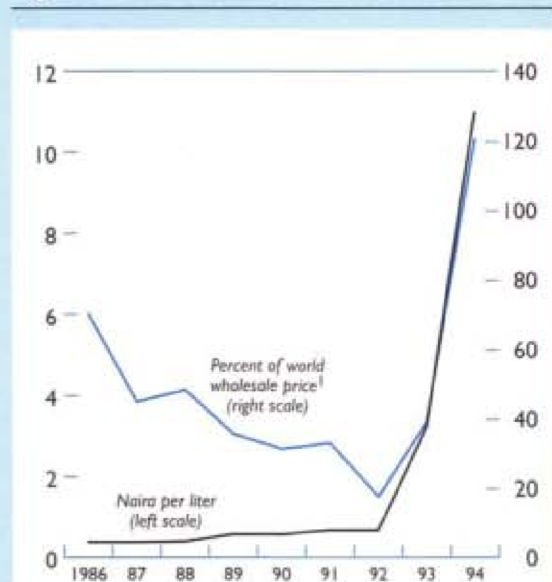
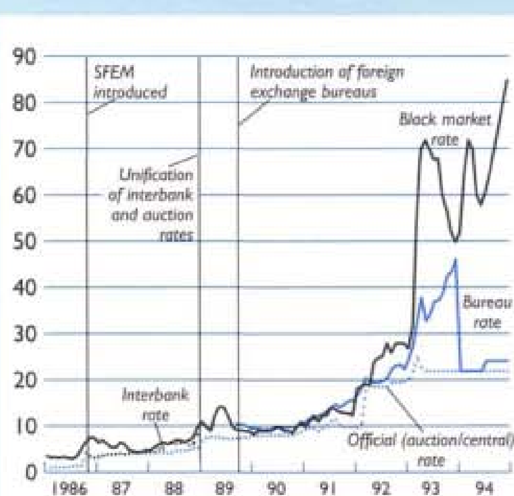
Figure 2. Domestic Gasoline Prices



Sources: Government of Nigeria; and IMF staff estimates.
[1]Measured at the parallel exchange rate.

Figure 3. Exchange Rate Developments
(Naira per U.S. dollar)



Sources: Data provided by the Nigerian authorities; and IMF staff estimates.

change market was liberalized in a number of steps, thereby allowing the economy to restore external competitiveness and to absorb severe terms of trade shocks.

On September 26, 1986, a dual exchange rate system was introduced, consisting of an administratively determined official rate and an auction rate. The official rate was applied to external debt-service payments, official foreign capital inflows, and other federal government transactions. The auction rate, determined in weekly foreign exchange auctions by the Central Bank of Nigeria (CBN), applied to all other transaction.[10] Foreign exchange obtained from the auction was traded in an interbank market, which was also funded from private non-oil export proceeds.[11] The official exchange rate was devalued by 22 percent, to ₦1.538 per U.S. dollar, and the first auction resulted in a 65 percent devaluation of the naira, to ₦ 4.20 per U.S. dollar (Figure 3).

The pricing of foreign exchange in the auctions was based on a marginal bid system. An important provision of the auction was the ceiling on the share of the total foreign exchange that could be purchased by individual dealer banks. The three largest dealer banks were each allowed to purchase no more than 5 percent of the total offering and the other banks no more than 3 percent. This provision intended to prevent the emergence of monopolistic or oligopolistic practices in the foreign exchange market, but also had the effect of depressing the price that emerged from the auction. To reinforce this policy, the Central Bank required all transactions in the interbank market to be carried out at the rate established in the previous auction, adjusted for a maximum buying and selling spread of 1 percent.

Official Supply of Foreign Exchange

	1987	1988	1989	1990
Official supply				
In billions of U.S. dollars	2.0	2.8	2.2	2.5
In percent of official foreign exchange earnings	. . .	54	33	. . .

In January 1987, however, the exchange rate in the interbank market was fully liberalized. Given the continued quantity restrictions on bids in the central bank auction and the segmentation of the two markets during the subsequent six months, a spread emerged between the interbank and auction rates that, however, never exceeded 5 percent.

[10]Only authorized dealer banks were allowed to participate in the auction, which was designated as the Secondary Foreign Exchange Market (SFEM).

[11]The foreign exchange surrender requirement to the Central Bank for non-oil export proceeds was lifted in 1986, but exporters were still required to surrender 75 percent of foreign exchange earnings to commercial banks at the prevailing interbank rate. In 1987, the surrender requirement was eliminated altogether.

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In an effort to reduce speculative bids by authorized dealers, which had caused considerable volatility in the weekly auction rates, the marginal bid system was replaced with a Dutch auction system on April 2, 1987. Henceforth, auctions were held every fortnight. Furthermore, on July 2, 1987, following nine months of frequent devaluations of the official exchange rate, this rate was merged with the auction rate.[12] At the same time, the auction market for foreign exchange became more restrictive as dealer banks could now bid only on behalf of their customers. The interbank rate applied only to foreign exchange obtained outside the Central Bank. Consequently, despite the "unification" of the exchange rates, there were still two rates: the auction rate and the interbank rate, with the latter depreciating more rapidly over time. The differential between the two rates widened from 8 percent at the end of 1987 to 55 percent by the end of 1988.

The large spread between the two exchange rates prompted the authorities to unify the auction and the interbank rates into a "central" rate in January 1989. The new system incorporated an auction mechanism, but the Central Bank retained a large degree of discretion in setting the rate. Official foreign exchange was allocated among the participating banks on a daily basis in proportion to their capital base. During the next two years, the official exchange rate depreciated by 44 percent against the U.S. dollar. Small-scale purchasers of foreign exchange had limited access to the official market, and a broadening of the foreign exchange market was accomplished with the introduction of foreign exchange bureaus in September 1989. The bureaus were allowed to buy and sell currency and traveler's checks at freely negotiated rates. The funding of the foreign exchange bureaus was limited to private remittances, private capital inflows, and other invisible proceeds. While the bureaus operated on a relatively small scale, they provided an important source of additional foreign exchange for importers who could not fulfill their demands through the auction.

Trade and Tariff Reform

A major reform of the trade and tariff system was implemented concurrently with the introduction of the dual exchange rate system in September 1986. The import and export licensing schemes were abolished, the number of import bans was reduced from 74 to 16, and the number of export bans from 11 to zero.[13] The 30 percent import surcharge, which had been imposed in January 1986, was removed[14] and the 100 percent advance payment for import duty was reduced to 25 percent in 1987. Pending a comprehensive tariff reform, the *Customs and Excise Provisions Decree of 1986* was issued to provide immediate relief from the impact of the devaluation of the naira on the cost structure of selected tradable goods. As a result, the level and dispersion of tariffs were significantly reduced and the average nominal tariff rate was lowered from 33 percent to 23 percent. Reduced tariffs were applied to agricultural inputs, basic industrial raw materials, and selected agricultural commodities; but higher rates were introduced on capital goods, essential consumer goods, and agricultural machinery. Most tariffs were set in a range of 10–30 percent, but for agricultural and industrial imports that competed with major domestic producers high rates of 100 percent or more were maintained. The *Customs and Excise Tariff (Consolidation) Decree of 1988* superseded the 1986 decree and set out a tariff regime for the period through 1994. The decree reduced the (unweighted) average tariff rate for chemicals, base metals, machinery and equipment, and vehicles, but raised it for most textile products. More important, it significantly reduced the dispersion of tariffs within each SITC group, although the average unweighted tariff of 28 percent was higher than in 1986. Subsequently, in response to mounting pressures, there were numerous revisions to the 1988 decree, which aimed at increasing protection for domestic manufacturers. Duties were increased on 22 items in 1989 and 1990, mostly on finished goods, and reduced on 16 items, mostly on industrial inputs.

The progress in trade liberalization, made in the early years of the SAP, particularly with respect to the lifting of trade bans, suffered setbacks in the following years. Exports of unprocessed timber were banned in 1987 and exports of cassava, maize, yams, beans, and rice were banned in 1989. By 1990, the export bans applied to 63 percent of the volume of crop production. The immediate impact of these bans on trade was negligible, as these products accounted for a very small proportion of exports prior to the imposition of the bans. But their existence inhibited significantly the diversification of the country's export base. While the total number of import bans did not change, selected commodities were re-

[12]The two rates were unified at ₦3.73 per U.S. dollar (the prevailing auction rate) and the SFEM was renamed the FEM (foreign exchange market).

[13]The remaining import bans covered cigarettes, poultry, vegetables, rough wood, eggs, fruit, most textile fabrics, plastic wares, mineral water, jewelry and precious metals, rice, maize, wheat, selected alcoholic beverages, gaming machines, and vegetable oils.

[14]A 6.02 percent surcharge was reimposed in January 1987.

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moved from the import prohibition list between 1987 and 1990, but others were added.

External Debt Policy

Prolific external borrowing during the first half of the 1980s increased Nigeria's official external debt from US$4.1 billion at the end of 1980 to US$24.6 billion by the end of 1986. The debt-service ratio rose from 6 percent to 72 percent during this period. The increased debt-service burden reflected, in part, the Federal Government's assumption of external debt-service obligations of state governments, but also the sharp contraction in export revenue, especially in 1986. Nigeria's external debt strategy aimed at regularizing relations with its external creditors, and reducing debt-service obligations to around 30 percent of official foreign exchange receipts. This was to be accomplished through a series of rescheduling agreements with Paris and London Club creditors, and, in 1988, through the introduction of a debt conversion scheme. The SAP paved the way for two rescheduling agreements with Paris Club creditors (October 1986 and March 1989) and three agreements with London Club creditors (November 1986, August 1987, and April 1989).

Paris Club Agreements

The 1986 Paris Club agreement covered current maturities on medium- and long-term debt falling due from October 1986 to the end of 1987 (US$2.8 billion), as well as arrears accumulated on short-term trade credits and medium- and long-term maturities (US$1.1 billion). Of the arrears, US$0.5 billion was to be paid between November 1987 and the end of 1989. The remaining rescheduled amounts were to be repaid over a 4½-year period commencing November 1992.

The agreement soon ran into trouble as the authorities were not able to honor their obligations. In an attempt to stabilize the newly established interbank exchange rate, the supply of official reserves to the market exceeded substantially the amounts programmed in the 1987 budget. Thus, the allocation of additional foreign exchange receipts to the FEM was achieved at the cost of accumulating arrears on Paris Club and other external debt. This problem continued well into 1988. As a result, US$230 million in external payment arrears were accumulated in 1987, and a further US$4.5 billion in the subsequent year. Following the approval by the Fund of a second stand-by arrangement with Nigeria, a new rescheduling agreement with Paris Club creditors was reached in March 1989.

In view of the previous rescheduling and the fact that arrears had accumulated on debt-service payments due on previously rescheduled debt, the terms of the new agreement were rather complex.[15] The total amount of debt relief (including arrears) involved for 1989 and the first four months of 1990 was about US$5.3 billion. Partially reflecting delays in bilateral negotiations and reconciliation efforts, Nigeria again began to accumulate arrears to Paris Club creditors in 1989 and continued to do so through 1990 pending the signing of the third stand-by arrangement with the Fund in January 1991, which facilitated the authorities' third rescheduling agreement with Paris Club creditors in that same year.

London Club Agreements

In 1984 Nigeria reached an agreement with the London Club commercial banks to reschedule arrears that had built up on trade credits during the 1982–83 period, and the final payments under this arrangement were made in October 1986. During 1986, faced with a large drop in export earnings, Nigeria accumulated an estimated US$2.8 billion in arrears on letters of credit extended by London Club banks (including late interest). In April 1986, an agreement was reached for a moratorium on payments on principal, pending a comprehensive rescheduling of all debt payments due to the banks. In November 1986, an agreement was concluded on the repayment of arrears on letters of credit over a four-year period starting December 1987. Due to delays in finalizing the agreement, however, the London Club creditors agreed to a modified repayment schedule in November 1987, involving US$520 million in new credits during 1988 and 1989, with repayment of interest and principal to occur over a three-year period commencing in January 1988. In the event, this agreement was never implemented owing to the delay in reaching an agreement with the Fund on a program and the London Club creditors' subsequent refusal to provide new money.

A breakthrough was finally achieved with the signing of a more comprehensive agreement in April 1989 on terms much more favorable to the authorities. The original US$2.6 billion in trade arrears were to be repaid in 144 equal monthly installments

[15]Creditors agreed to reschedule: (1) all principal and interest (excluding late interest) due from January 1, 1989, up to April 30, 1990 on medium- and long-term debt contracted before October 1, 1985 (the cutoff date used for the previous rescheduling); (2) all arrears (including late interest) outstanding as of end-1988 on medium- and long-term debt contracted before the cutoff date; (3) up to a maximum of 60 percent of the amounts that were due before December 31, 1988, and not paid, on previously rescheduled debt; and (4) all arrears outstanding at end-1988 on short-term credits, contracted before that date.

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beginning in January 1992 at an interest rate of LIBOR plus 13/16. In addition, the new agreement covered US$2.9 billion in arrears and current maturities, which were rescheduled over a 20-year period, also commencing in January 1992.

In 1991, Nigeria made substantial progress in reducing its commercial debt; following an agreement in principle with London Club creditors in March, which was finalized in December, a debt and debt-service reduction operation (DROP) was completed in January 1992. The DROP involved the purchase of US$3.4 billion of commercial debt at a 60 percent discount and the exchange of another US$2.0 billion at par for 30-year bonds carrying an interest rate of 5.5 percent per annum for the first three years and 6.25 percent per annum thereafter. Principal for the par bonds was collateralized by Treasury zero coupon bonds and 12 months of interest was collateralized by cash and certain permitted investments. As a result of the DROP, Nigeria's debt outstanding to the London Club banks was reduced from nearly US$6 billion at end-1991 to US$2.2 billion. The Nigerian authorities have since remained current on these obligations.

Fiscal Adjustment and Reform

Fiscal policy was erratic during the SAP period, as it had been during the first half of the 1980s. During the first two years (1987–88), the overall and primary fiscal balances deteriorated substantially, but increased world oil prices contributed to a marked improvement in the fiscal position during the 1989–90 period (see Table 5). Thus, in 1990 the overall deficit fell to below 3 percent of GDP, and the primary balance recorded a surplus of nearly 9 percent.

The deterioration in the fiscal position in 1987 was primarily due to the assumption of large external debt-service obligations of the state governments by the Federal Government (Box 4). Nondebt expenditure rose modestly in that year, and the primary fiscal balance turned to a surplus of 1 percent of GDP, from a deficit of ½ percent in 1986. In 1988, however, the Government adopted a "reflationary package" as part of its budget proposals to alleviate the adverse impact of the large increase in petroleum prices, the elimination of price controls, and the sizable devaluation of the naira. This caused nondebt expenditure to rise by more than 45 percent compared with the 1987 outcome, while government revenue rose by only about half that amount. In only two years, government nondebt expenditure increased by 90 percent, while under the influence of the devaluation and higher oil export volumes government revenue increased by 60 percent.

The improvement in the fiscal position during the 1989–90 period was attributable to a substantial moderation in the rate of growth of nondebt expenditure and a surge in oil revenue, owing to the rise in world oil prices. Nonetheless, the degree of fiscal adjustment was insufficient to redress inflationary and exchange rate pressures. In circumstances where the bulk of government revenue is coming from abroad, the usual indicators of the stance of fiscal policy, such as the overall or primary fiscal balance, may fail to provide a proper measure of the monetary impact of the Government's budget. In those circumstances, the evolution of nominal nondebt expenditure is a more useful indicator of the underlying fiscal stance (see Box 5). Thus, an increase in nominal government expenditure in excess of real output growth would result in inflation or in a crowding out of real private absorption, or a combination of both. This seems to have been the case in Nigeria, where nominal nondebt government expenditure increased by 213 percent during the SAP period, and by 44 percent in 1990 alone, compared with a growth of real GDP of 27 percent over the entire period.

Tax policy during the SAP was aimed primarily at attenuating the impact of higher import prices arising from the depreciation of the naira. Little was done to enhance non-oil tax revenue, which increased only to 5½ percent of GDP in 1990, from 4½ percent in 1986, largely on account of rising customs revenues. Tax reform at the federal level consisted of rate reductions in corporate and personal income taxes. The corporate income tax rate was reduced from 45 percent to 40 percent in 1987, and the top marginal rate in personal income taxes was lowered from 70 percent to 55 percent.[16] In 1988, the number of excisable items was reduced from 412 to 118, including the exemption of all imported intermediate inputs. There were other minor changes in the tax system, such as tax relief for dividend income, income of small-scale manufacturers, and capital investment. During 1986–90, no new taxes were introduced.

Government expenditure policy suffered from weak budgetary procedures and lack of transparency, as reflected in the underbudgeting of various expenditure categories, including domestic interest payments, and the emergence of sizable extrabudgetary spending. The structure of government spending changed significantly during the

[16]Since the personal income tax is levied at the state level, this measure had virtually no impact on federal government revenue. The Federal Government collects income taxes only from residents of the Federal Capital Territory (Abuja), and the armed forces.

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Table 5. Summary of Federal Government Fiscal Operations

	1985	1986	1987	1988	1989	1990
			(In billions of naira)			
Federally collected revenue	15.1	15.9	23.3	29.5	55.4	93.7
Of which: oil revenue	(10.9)	(12.7)	(18.5)	(23.6)	(46.7)	(79.8)
Federally retained revenue	9.0	10.2	12.6	16.1	31.0	56.2
Total expenditure	11.0	14.0	25.4	35.8	46.6	63.8
Of which: non-debt	(8.1)	(10.5)	(11.7)	(20.2)	(22.3)	(32.9)
Overall balance	–2.1	–3.8	–12.8	–19.7	–15.6	–7.7
Primary balance	0.9	–0.4	1.0	–4.2	8.7	23.3
Financing	2.0	3.8	12.8	19.7	15.6	7.7
Foreign (net)	–0.4	–0.3	3.5	5.4	8.2	–0.3
Domestic	2.4	4.1	9.3	14.3	7.4	7.9
Of which: banking system	(1.6)	(–0.8)	(2.4)	(6.1)	(–9.3)	(2.8)
			(In percent of GDP)			
Federally collected revenue	20.9	21.7	21.4	20.3	24.6	35.9
Of which: oil revenue	(15.1)	(17.4)	(17.0)	(16.3)	(20.8)	(30.6)
Federally retained revenue	12.4	13.9	11.6	11.1	13.8	21.5
Total expenditure	15.2	19.1	23.3	24.7	20.7	24.5
Of which: non-debt	(11.2)	(14.4)	(10.7)	(13.9)	(9.9)	(12.6)
Overall balance	–2.8	–5.2	–11.7	–13.6	–7.0	–2.9
Primary balance	1.2	–0.5	0.9	–2.9	3.9	8.9
Financing	2.8	5.2	11.7	13.6	7.0	2.9
Foreign (net)	–0.5	–0.3	3.2	3.7	3.7	–0.1
Domestic	3.3	5.6	8.5	9.8	3.3	3.0
Of which: banking system	(2.2)	(–1.1)	(2.2)	(4.2)	(–4.1)	(1.1)

Sources: Data provided by the Nigerian authorities; and IMF staff estimates.

SAP period. With the assumption by the Federal Government in 1987 of the state government's external debt obligations, foreign interest obligations rose sharply, accounting for more than 30 percent of total expenditure during 1987–90. The lack of budget control was particularly evident in growing extrabudgetary spending, which reached by 1990 an estimated 17 percent of total spending, equivalent to 50 percent of budgeted nondebt expenditure. This development occurred despite the introduction of a warrant system in 1985, in which all expenditure was to be authorized by quarterly warrants issued by the Accountant General. In fact, the budgetary process became less and less transparent during the SAP period. Extrabudgetary outlays were financed from oil revenues kept outside the Federation Account; during 1989–90, this source of funding was augmented by spending from the stabilization account (Box 6). As these expenditures were not covered by the warrant system, their nature is largely unknown, but it is believed that much of it was spent on the construction of the federal capital of Abuja. As extrabudgetary expenditures grew, the official budgets lost much of their meaning (Table 6).

State and Local Government Finances

The state governments derive nearly 90 percent of their revenue from the Federation Account.[17] The remainder comes mostly from income and sales taxes. Local governments and the special funds rely almost entirely on transfers from the Federation Account.[18] The budgets of these tiers of government were broadly in balance during the SAP period. Total revenue from these sources increased from 9.8 percent of GDP in 1986 to 13.7 in 1990, while total expenditure increased from 10.3 percent of GDP to 13.1 percent during the same period.

[17]Data limitations preclude a comprehensive accounting of the fiscal operations of the state and local governments and the special funds. Data are available for allocations from the Federation Account, statutory claims on transfers to the Federation Stabilization Account, highly aggregated state budgetary data, and net bank credit to state and local governments. Little information is available on the financial operations of the special funds or revenue collected directly by local governments.

[18]Local governments collect some fees and municipal taxes, but these revenues are relatively small.

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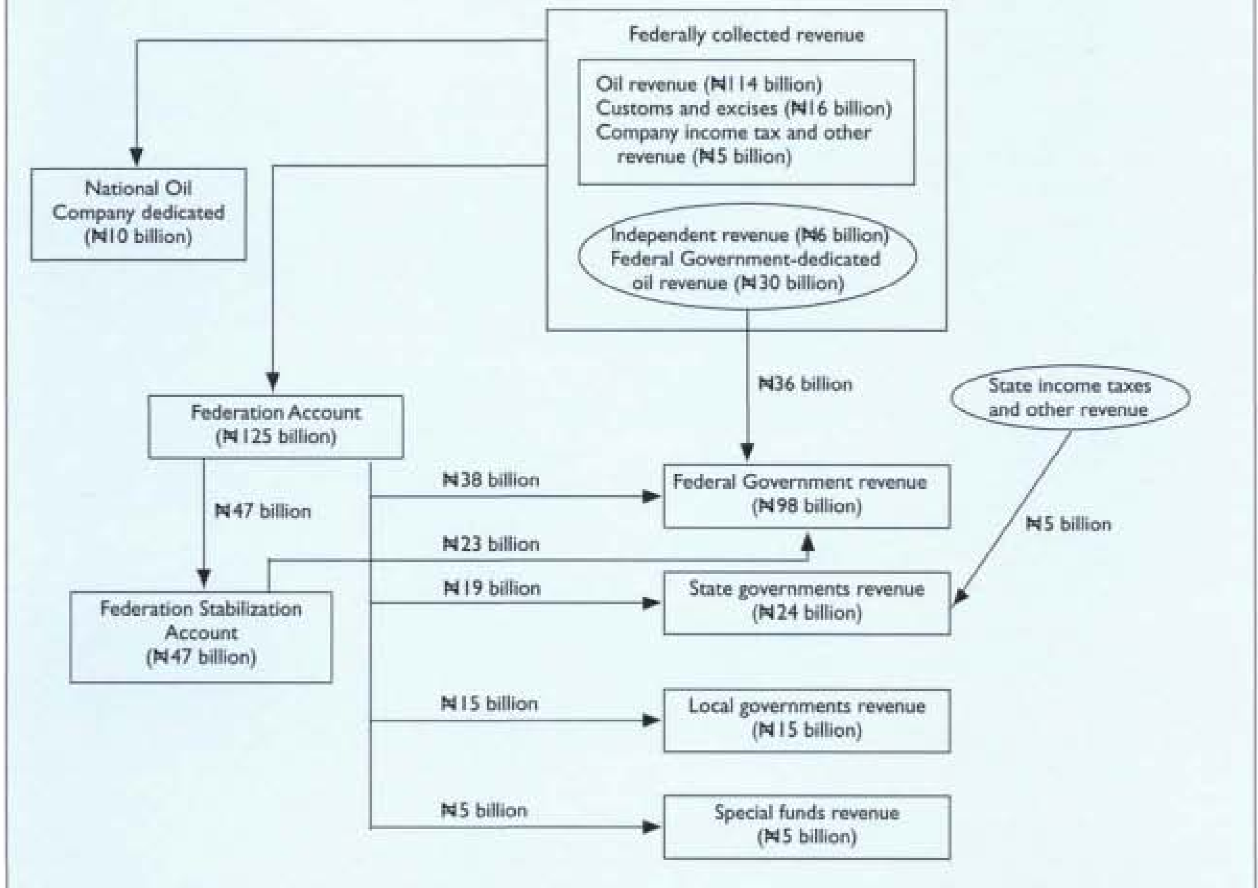
Box 4. Fiscal Federalism

The Government of Nigeria consists of the Federal Government, 30 state governments, and 589 local governments. The bulk of government revenue is collected at the federal level and shared among the three tiers of government, including oil proceeds, customs duties, excise taxes, and corporate income taxes. These revenues accrue to the Federation Account, from where they are distributed as follows: 48.5 percent to the Federal Government, 24 percent to state governments, 20 percent to local governments, and 7.5 percent to five special funds. These are the Ecology Fund, the Federal Capital Territory Fund, the Mineral Derivation Fund, the Mineral Producing Areas Fund, and the Statutory Stabilization Account. The Federation Account allocation to individual state and local governments is based on a distribution formula that takes into account equality (40 percent), population (30 percent), social development (10 percent), land mass (10 percent), and internal revenue mobilization efforts (10 percent). In addition to the Federation Account allocations, the revenue generated from the value-added tax, introduced in 1994, is shared between the Federal Government (20 percent, increased to 40 percent in 1995) and state governments (80 percent). Apart from the allocations from the Federation Account, state governments raise their own revenue from income taxes and fees. In the diagram below the main components of the resource flows are depicted, with illustrative figures for 1992 (in naira). Totals may not add due to rounding.



The consolidated fiscal position of federal, state, and local governments mirrored broadly the pattern of fiscal developments within the Federal Government, namely a sharp deterioration during the first two years of the SAP followed by a remarkable turnaround in 1989–90.

Monetary Policy and Financial Sector Reform

In the absence of a supportive fiscal policy, monetary policy had to play a dominant role in macroeconomic stabilization. However, at the same time its ef-

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Box 5. Measuring the Stance of Fiscal Policy in an Oil Economy

A simple model can be used to analyze the inflationary impact of government expenditure when the bulk of fiscal revenue is generated from external trade:

$$Mv = Py, \quad (1)$$

$$M = NFACB + NFAOB + NDCG + NDCRE, \quad (2)$$

$$NFACB = NFACB_{t-1} + XOIL - FI + FGB + Z, \quad (3)$$

$$NDCG = NDCG_{t-1} - D - FBG - DNBBG, \quad (4)$$

$$D = t{*}XOIL + OGR - G - FI, \quad (5)$$

where: M = the stock of broad money; v = velocity; P = non-oil GDP deflator; y = real non-oil GDP; $NFACB$ = net foreign assets of the Central Bank (adjusted for valuation effects); $NFAOB$ = net foreign assets of the rest of the banking system (net of valuation effects); $NDCG$ = net bank credit to the Federal Government; $NDCRE$ = net bank credit to the rest of the economy (including other items net); $XOIL$ = value of oil exports; FI = foreign interest payments due; FGB = net external financing of the fiscal deficit; Z = the overall balance of payments, excluding $XOIL$, FI, and FGB; D = the overall fiscal balance; $DNBBG$ = domestic nonbank borrowing by the Government; t = government oil revenue as a share of oil export revenue; OGR = government non-oil revenue; and G = government expenditure excluding foreign interest due.

Equation (1) states the quantity theory of money. Since Nigeria is assumed to be a price taker with respect to exports, monetary shocks are assumed to affect only prices in the non-oil sector. Hence, the equation is defined in terms of non-oil GDP and the non-oil GDP deflator. Equation (2) defines the stock of broad money in terms of its counterparts in the balance sheet of the consolidated banking system. Equation (3) defines the relationship between the net foreign assets of the Central Bank and the overall balance of payments, which are here disaggregated into nominal oil exports, foreign interest obligations, and net external borrowing of the Government, and the remaining balance of payments, excluding changes in international reserves. Equation (4) states that the change in net bank credit to the Government is equal to the overall fiscal deficit minus net foreign financing and nonbank borrowing by the Federal Government, and equation (5) defines the government budget deficit.

Equations (1) through (5) can be combined to yield equation (6):

$$P = (v/y){*}[NFACB_{t-1} + NDCG_{t-1} + NFAOB + NDCRE + (1-t){*}XOIL + Z - DNBBG - OGR + G], \quad (6)$$

which defines the aggregate price level as a function of the income velocity of money, real non-oil GDP, and the stock of broad money, which has been decomposed into its constituent parts as defined by equations (2) through (5).

Equation (6) shows that an increase in government expenditure (G), excluding foreign interest payments, that is not offset by an increase in either domestic nonbank borrowing or in non-oil fiscal revenue, will be inflationary, unless there is an equivalent leakage through the balance of payments, or a corresponding contraction of net bank credit to the rest of the economy. The inflationary impact of additional oil revenue is equivalent, therefore, to an increase in domestic bank borrowing. Clearly, the future debt dynamics of the two cases differ, and, hence, so will the subsequent monetary impact.

This result captures the basic characteristic of the Government's fiscal policy during most of the 1986–90 period; during periods of low oil prices the deficit was large and the Government borrowed from the banking system; during periods of high oil prices the deficit was small and the Government monetized most of the higher oil revenues and reduced its borrowing from the banking system. In both cases, however, fiscal operations contributed to the expansion of broad money and the attendant pressures on domestic prices and the exchange rate.

The extent to which government expenditure in 1990 was "excessive" can be determined by comparing actual expenditure with the level of expenditure that

fectiveness was severely constrained by the lack of instruments and the multiple and often conflicting roles it had to fulfill. Monetary policy was charged not only with bringing inflation under control, but also with a variety of sectoral and regional objectives, such as stimulating local production, promoting non-oil exports, and ensuring a proper distribution of credit. The most important handicap, however, was probably the Central Bank's lack of independence from the Federal Government, which gave the latter almost uncontrolled access to Central Bank credit and considerable influence over interest rate policy.

The Central Bank's inability to control the growth of money was to a large extent the result of fiscal policies, which relied heavily on central bank financing of large deficits. Monetary control was also complicated by the monetization of rising government oil revenues during 1989–90 (Table 7). Thus, strong money growth fueled inflationary pressures throughout most of the SAP period and placed increasing pressure on the exchange rate and interest rates. The inability to bring inflation under control contributed to the erosion of popular support for the SAP.

Credit Controls

The Central Bank relied on a system of direct credit controls, with bank-specific ceilings on credit

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Stance of Fiscal Policy (Alternative Scenarios)
(In percent of GDP, unless otherwise indicated)

	1986	1987	1988	1989	1990
Actual outcome					
Aggregate price level (1986=100)[1]	100	129	163	195	214
Government expenditure (in billions of naira)[2]	13.0	15.5	24.4	28.3	41.3
Overall fiscal balance	–5.2	–11.7	–13.6	–7.0	–2.9
Primary fiscal balance	–0.5	0.9	–2.9	3.9	8.9
Targeted 20 percent inflation					
Aggregate price level (1986=100)[1]	100	120	144	173	207
Government expenditure (in billions of naira)[2]	13.0	13.3	19.5	23.1	39.2
Overall fiscal balance	–5.2	–9.7	–10.2	–4.7	–2.1
Primary fiscal balance	–0.5	2.9	0.5	6.2	9.7
Relative price stability[3]					
Aggregate price level (1986=100)[1]	100	102	105	108	113
Government expenditure (in billions of naira)[2]	13.0	9.3	9.3	8.1	11.2
Overall fiscal balance	–5.2	–6.0	–3.2	2.0	8.6
Primary fiscal balance	–0.5	6.6	7.5	12.8	20.5
Memorandum items:					
Consumer price index (average; 1986=100)	100	110	148	223	239
Average official exchange rate (naira/U.S. dollar)	1.75	4.02	4.54	7.36	8.04

[1]Non-oil GDP deflator.
[2]Excluding foreign interest payments.
[3]Inflation rate equal to consumer price inflation in partner countries.

would have been consistent with the Government's inflation objectives. Analytically, this involves solving equation (6) for government expenditure (G) under different assumptions of the price level (P), as shown by equation (7). The strong assumption of this analysis is that all the variables on the right-hand side of (7) are independent of government expenditure.

$$G = P*(y/v) - [NFACB_{t-1} + NDCG_{t-1} + NFAOB + NDCRE + (1-t)*XOIL + Z - DNBBG - OGR]. \quad (7)$$

As shown above, a more ambitious inflation target, e.g., with an inflation rate in line with trading partners, would have required much more restraint in government expenditure and growing primary fiscal surpluses.

expansion to the private sector. It also maintained guidelines on the sectoral and regional allocation of credit, which specified certain minimum shares of total bank lending to agriculture and other priority sectors and required commercial banks to maintain a minimum ratio of rural loans to rural deposits. In addition, it used minimum liquidity and cash reserve requirements, but not as active instruments of monetary policy. To reduce excess liquidity in the banking system, in November 1989 the Central Bank started an auction-based system for the issuance of treasury bills and certificates and introduced in August 1990 the so-called mandatory stabilization securities. The mandatory stabilization securities were issued selectively to banks on the basis of their liquidity positions and soundness.

In the aggregate, the credit ceilings proved largely ineffective in restraining the growth of bank credit to the private sector (Table 8), not only because of the relatively minor penalties for exceeding the stipulated ceilings, but also because of the rapid increase in new banks, which would have required frequent adjustments to individual bank ceilings.

Interest Rate Policy

Interest rate policy lacked consistency during the SAP, as periods of liberalization were intertwined

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Box 6. Oil Revenue in Nigeria

Nigeria's fiscal revenue relies heavily on the oil sector. This reliance has continued unabated since the mid-1970s, despite numerous efforts to diversify the revenue base. As a share of total government revenue, oil revenue increased from 82 percent in 1986–89 to 84 percent in 1990–93, before dropping to 75 percent in 1994, largely on account of the fall in oil export prices and the introduction of the value-added tax. More important for 1994, the substantially overvalued official exchange rate affected oil revenue (in naira terms) significantly.

Oil revenues derive from the operations of the Nigerian National Petroleum Company (NNPC), and its joint venture partners. The NNPC's contribution to the budget consists of net export proceeds and the domestic retail sales of petroleum products. The joint venture partners pay a royalty to the Federal Government of 19.6 percent of total exports and a profit tax of 85 percent. They are permitted to withhold certain amounts from their net export proceeds in the form of "notional" costs and guaranteed profits, both of which are denominated in U.S. dollars per barrel. The partner companies settle their actual tax liability to the Federal Government at the end of each company's fiscal year.

Through the end of 1994, the NNPC was permitted to sell a specified number of barrels each day to cover its dollar-denominated costs ("dollar cash calls") and to help finance its capital budget ("dedicated oil"). A certain number of barrels per day were also sold on behalf of the Federal Government, which accrued directly to an offshore account. The NNPC's net export proceeds (excluding dollar cash calls and all dedicated oil) were deposited in the Central Bank's account at the Federal Reserve Bank of New York and the naira counterpart was deposited into the Federal Government's "Royalty Account" at the Central Bank. In addition, the NNPC generates revenue from the domestic retail sales of petroleum products and is expected to pay the Federal Government both a notional cost for the crude oil it uses for domestic refining (at a transfer price in 1994 of 183 naira per barrel) and operating profits. In the 1991–94 period, the NNPC incurred losses on its domestic operations, as a result of the low retail prices set by the Government, and did not pay the Federal Government for crude oil. In October 1994, the retail price of gasoline was raised substantially (from 3.25 naira to 11 naira per liter), and the NNPC has since been able to pay a higher transfer price (US$17 per barrel) to the Federal Government.

The system for collecting oil revenue was modified substantially in 1995, when the Federal Government closed the off-budget dedicated accounts and began depositing the total amount of NNPC export proceeds directly into a Federal Reserve Bank account. From this account, the Government's contribution to operating costs of the oil industry ("first charges" against the budget) are then deducted. Another change has been that profits from domestic sales have been transferred to a newly created Petroleum Trust Fund, which is managed outside the federal government budget. The Petroleum Trust Fund resources are being used for priority infrastructure and social sector projects.

with the reimposition of some forms of control. The liberalization of bank deposit and lending rates, with effect from August 1, 1987, had little impact on interest rate developments. The commercial banks followed the Central Bank's rediscount rate in adjusting their rates, even if the signals sent appeared to go in the wrong direction. This was particularly evident toward the end of 1987, when the CBN lowered its discount rate and the banks followed suit in the face of accelerating inflation. Responding to pressure from the private sector, the CBN reintroduced controls in November 1989 by imposing a maximum spread between lending and deposit rates and imposing a maximum lending rate. Real deposit and lending rates turned negative in early 1988 (Figure 4) and remained so until the beginning of 1990, when inflation temporarily abated. Negative real interest rates depressed financial savings, which dropped in 1988 and 1989 as a share of non-oil GDP; the currency-deposit ratio rose from an average of 30 percent in 1986–87 to 40 percent in 1988–89.

Financial Intermediation

The financial sector expanded rapidly during the SAP, with the number of commercial banks increasing from 29 in 1986 to 58 in 1990, and the number of merchant banks increasing from 12 to 49, respectively (Figure 5). During the same period, the number of commercial and merchant bank branches increased from 1,394 to 2,182. This rapid expansion occurred for a number of reasons. First, the Central Bank began issuing new banking licenses after a moratorium of several years. Second, the trade liberalization measures implemented under the SAP increased the demand for trade-related financing. Third, the emergence of a spread between the official exchange rate and the interbank rate (and later the foreign exchange bureau rate) made exchange rate arbitrage very profitable. Many of the emerging merchant banks were established almost solely for the purpose of participating in the Central Bank foreign exchange auctions, in which foreign exchange could be purchased at a growing discount relative to

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Table 6: Structure of Federal Government Expenditures

	1986	1987	1988	1989	1990
			(In percent of total expenditure)		
Total expenditure and net lending	100.0	100.0	100.0	100.0	100.0
Of which: non-debt	(75.3)	(46.0)	(56.5)	(47.8)	(51.5)
Recurrent expenditure	54.8	70.8	62.7	68.9	64.8
Personnel costs	11.2	9.3	7.8	7.3	8.0
Overhead costs	18.9	7.4	11.5	9.4	8.3
Foreign interest due	7.1	33.1	29.0	35.2	32.9
Domestic interest due	17.7	15.0	11.7	12.9	13.3
Pre-SFEM payments	—	5.9	2.8	4.1	2.3
Capital expenditure	45.8	26.7	30.5	23.6	20.1
Of which: domestically financed	(17.6)	(15.1)	(23.9)	(12.0)	(11.6)
Net lending to state governments	–0.5	–0.6	–0.2	–1.0	–1.8
Supplementary/extrabudgetary outlays	—	3.2	7.0	8.5	16.9
			(In percent of GDP)		
Total expenditure and net lending	19.1	23.3	24.7	20.7	24.5
Of which: non-debt	(14.4)	(10.7)	(13.9)	(9.9)	(12.6)
Recurrent expenditure	10.5	16.5	15.5	14.3	15.9
Personnel costs	2.1	2.2	1.9	1.5	2.0
Overhead costs	3.6	1.7	2.8	2.0	2.0
Foreign interest due	1.4	7.7	7.1	7.3	8.1
Domestic interest due	3.4	3.5	2.9	2.7	3.2
Pre-SFEM payments	—	1.4	0.7	0.8	0.6
Capital expenditure	8.8	6.2	7.5	4.9	4.9
Of which: domestically financed	(9.1)	(3.5)	(5.9)	(2.5)	(2.8)
Net lending to state governments	–0.1	–0.1	—	–0.2	–0.5
Supplementary/extrabudgetary outlays	—	0.7	1.7	1.8	4.1
Memorandum items:			*(In percent of non-oil GDP)*		
Non-debt expenditure	16.9	14.3	18.0	15.5	19.1
Personnel	2.5	2.9	2.5	2.4	3.0
Overhead	4.2	2.3	3.6	3.1	3.1
Capital expenditure	10.3	8.3	9.7	7.7	7.5
Supplemental/extrabudgetary outlays	—	1.0	2.2	2.8	6.3

Sources: Data provided by the Nigerian authorities; and IMF staff estimates.

the interbank or foreign exchange bureau exchange rates. Fourth, the bank-specific credit ceilings provided an incentive for the establishment of new banks, rather than expanding lending activities at existing banks. Finally, the rapid growth in reserve money, arising from either Central Bank financing of government fiscal deficits or the monetization of rising official oil receipts, resulted in a strong expansion of the deposit base.

Notwithstanding the rapid growth in the number of commercial and merchant banks, only a few commercial banks dominated the industry. In 1985, three of the 28 commercial banks accounted for roughly one half of total deposits. By the end of 1990, this share had fallen to just below 40 percent, but the industry remained concentrated, with the top ten banks holding 63 percent of total deposits. While this concentration gave rise to concerns about the exploitation of monopoly power by the largest banks, especially in the Central Bank foreign exchange auctions, it contributed indirectly to sound banking practices, as the few dominant banks had extensive contacts with foreign institutions and followed international accounting standards. To encourage community-based savings and lending in the rural areas, community banking was introduced in 1990. In a similar vein, the People's Bank of Nigeria, which was established by the Government in 1989, provided services to small-scale private enterprises.

One of the central themes of the SAP was financial liberalization, while improving the confidence in Nigeria's financial system. As part of this effort, the Nigerian Deposit Insurance Corporation (NDIC)

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Table 7. Monetary Targets and Outcomes
(Annual percentage change)

	1986	1987	1988	1989	1990
Net domestic credit					
Target	. . .	4.4	8.1	9.5	13.5
Outcome	11.1	13.9	33.0	–14.4	18.5
Credit to the private sector					
Target	. . .	8.4	13.3	10.7	15.8
Outcome	28.7	18.2	24.4	3.6	20.4
Net credit to the Federal Government					
Target	. . .	1.5	2.5	8.3	10.9
Outcome	–4.1	12.4	28.6	–33.7	15.1
Narrow money					
Target	. . .	11.8	15.0	14.6	13.0
Outcome	–6.0	15.8	55.5	20.0	47.8
Change in reserves (in millions of U.S. dollars)					
Target	. . .	. . .	300	200	300
Outcome	–851	–78	–331	1,272	2,508
Memorandum items:					
Broad money (actual)	2.7	22.7	43.3	7.2	42.3
Velocity (GDP/average broad money)	3.0	4.0	4.0	4.9	4.9

Sources: *Approved Budget of the Government of the Federal Republic of Nigeria*, various issues; Central Bank of Nigeria, *Annual Report and Statement of Accounts*, various issues; and IMF staff estimates.

was established in 1988 to protect depositors against bank failures and to instill greater confidence in the banking system. At the same time, the Central Bank addressed solvency concerns by increasing the minimum paid-up capital requirements for commercial and merchant banks. Subsequently, in 1990, it introduced minimum risk-weighted capital adequacy requirements, which were based on international standards, further raised the minimum paid-up capital requirements for banks, and introduced new accounting standards. International prudential guidelines were adopted by the CBN in 1990 to establish sound practices for asset classification, disclosure, and adequate provisioning for nonperforming assets. For the nonbank financial sector, a new *Securities and Exchange Commission (SEC) Decree* was approved in 1988, which repealed the decree of 1979 and gave the Commission broader powers to regulate and supervise the Nigerian capital market, including the power to revoke the registration of stockbrokers and disapprove the establishment of a new stock exchange in Nigeria. The role of the SEC was further expanded by the *Companies and Allied Matters Decree of 1990*, which gave the power to approve and regulate mergers and acquisitions.

The Nigerian Stock Exchange (NSE) has grown considerably since its establishment in 1960. A rapid expansion occurred during the oil boom in the early 1970s, fostered by the Government's indiginization program, and a further expansion during the SAP period. Responding to investors' increased confidence in the economy, as well as the introduction of the second-tier securities market (SSM) to assist small and medium-sized firms, activity on the exchange increased significantly in 1986, with the NSE all-share index increasing by 23 percent. However, activity in the stock market slowed in 1988 as alternative financial instruments, namely higher yield corporate bonds, increased as companies tried to escape the Central Bank's cap on credit to the private sector. The stock market again expanded rapidly in 1989 as higher interest rates brought firms back to the capital market and the Government's privatization program increased the volume of activity. The all-sector NSE equity price index rose from a base of 100 at the end of 1984 to 164 at the end of 1990.[19]

[19]The exchange included 217 securities at the end of 1990, including 131 equities, 43 government securities, and 43 industrial loans and preferred stocks. The market is heavily concentrated, with 20 stocks representing over 70 percent of the total equity capitalization during the same period.

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Table 8. Credit Guidelines for Commercial Banks

	1986	1987	1988	1989	1990
			(Percent change)		
Loans and advances[1]					
Target	10.0	8.0	12.5	10.0	12.5
Actual	28.1	11.6	14.4	11.1	31.7
			(Percent of total credit)		
Allocation of credit					
Agriculture					
Target	15.0	15.0	15.0	15.0	15.0
Actual	11.8	12.9	15.3	15.3	15.9
Manufacturing					
Target	44.0	35.0	35.0	35.0	35.0
Actual	41.6	29.1	30.1	30.7	30.3
Other					
Target	41.0	50.0	50.0	50.0	50.0
Actual	46.6	58.0	54.6	54.0	53.8
			(Percent of rural deposits)		
Rural loans					
Floor	40.0	40.0	45.0	45.0	50.0
Actual	42.8	40.1	47.9	64.9	56.6
			(Liquid assets as a percent of deposit liabilities)		
Liquidity ratio[2]					
Floor	25.0	25.0	27.5	27.5	30.0
Actual	57.3	49.0	41.6	35.9	43.9
			(Cash reserves as a percent of deposit liabilities)		
Cash reserve ratio					
Actual	4.1	4.9	4.7	8.9	6.4

Source: Central Bank of Nigeria.
[1]Target applied to aggregate credit after 1989. Includes, in addition to loans and advances, investments, call money, certificates of deposit, bankers acceptances, commercial paper, bills discounted, and promissory notes.
[2]Total liquid assets less penalties and cash reserve requirements as a percent of total deposit liabilities.

boosted by the improved outlook for the economy during these years.

Public Enterprise Reform

State intervention in major sectors of the economy spread throughout the 1970s and early 1980s. Virtually all the country's largest enterprises were wholly government owned, including those in the petroleum, communications, transportation, banking, and steel, paper, and other manufacturing activities. Public enterprises posed a significant burden on the Federal Government's budget and contributed little to the budget in the form of dividends or debt repayments. In 1986, 33 percent of the Federal Government's domestically financed capital budget was allocated to investment in public enterprises, and they absorbed an estimated 40 percent of the Federal Government's nonsalary recurrent expenditure in the form of subsidies.

As part of the SAP, the commercialization and privatization program was announced in June 1986, but implementation did not commence until 1989. The Technical Committee on Privatization and Commercialization (TCPC) classified the parastatals it would deal with into four groups: those to be fully or partially privatized (50 enterprises), fully commercialized (9 enterprises), and partially commercialized (26 enterprises). The Government would fully divest itself of ownership of enterprises falling into the first category. Partially privatized enterprises were to be held to hard budget constraints and receive no financial support from the Federal Government. Fully and partially commercialized enterprises would continue to be wholly owned by the

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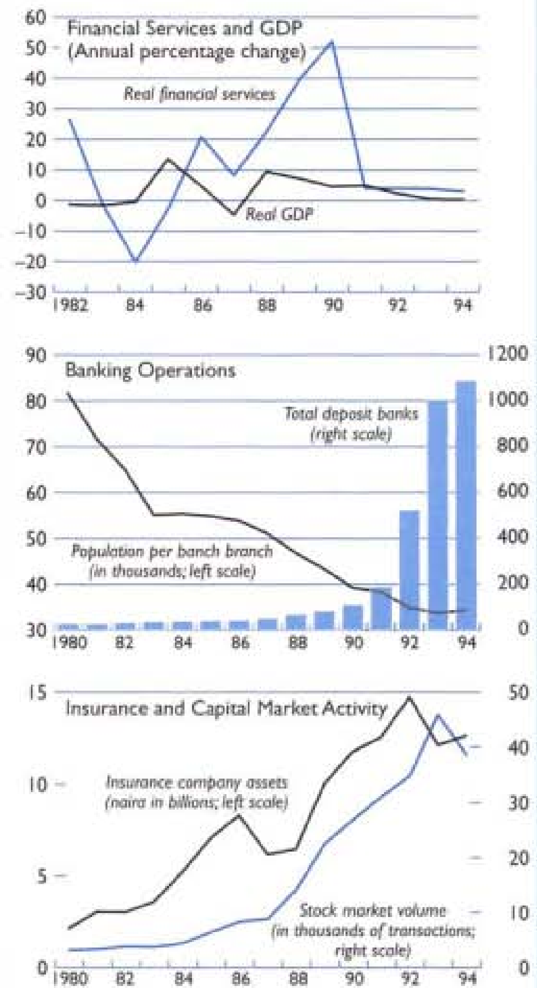
Figure 4. Selected Interest Rates

Sources: IMF, *International Financial Statistics*; and Central Bank of Nigeria.

Figure 5. Financial Intermediation



Sources: IMF, *International Financial Statistics*; and Central Bank of Nigeria.

Federal Government. The former were to receive no budgetary support for either recurrent or capital expenditure, while the latter would receive support for both.

The TCPC privatized 16 federal public enterprises in 1989, comprising two oil companies, 13 insurance companies, and a flour mill, with a total market capitalization of about ₦130 million. Another five enterprises, with a capitalization of ₦116.5 million were privatized in 1990, including three cement companies. Little progress was made with respect to the commercialization of public enterprises. All the major wholly government-owned public enterprises continued to receive subventions from the federal budget, and none of the seven largest paid any dividends through 1990. Furthermore, while the proportion of the Federal Government's capital budget allocated for support of public enterprises fell from 33 percent in 1986 to 7 percent in 1990, actual lending deviated substantially from budgetary provisions. Total lending in 1990 amounted to ₦1.4 billion, compared with a budgeted ₦0.4 billion, and was nearly three times as large as in 1986.

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