



NIGERIA RESEARCH NOTE

Belated acknowledgment of the fiscal mess - a potential game-changer

Based, as it was, on the most aspirational of assumptions, the expansionary 2016 budget¹ submitted to the National Assembly last December epitomises the triumph of hope over expectation.

Yesterday's announcement that Nigeria is seeking a total of USD 3.5 billion in support from two development finance institutions marked a welcome, if belated, acknowledgement by the Buhari administration of the violent headwinds battering the fiscus. But the transaction mooted is by no means a fait accompli.

1) As will be recalled, **none of the key revenue assumptions** underlying the Appropriations Bill (2016) **ever withstood even the most perfunctory examination²:**

- a price of **\$38 per barrel** for Nigeria's crude – a level that market developments had begun to call into question even before the end of the year;
- daily oil production of **2.2 million barrels** – implying a spectacular improvement on 2015 when oil output had averaged a mere 1.749 million bbd³, eclipsed by Angola's 1.767 bbd⁴;
- an exchange rate of **N197 vs. USD** – when the rate on the parallel market was already at N285, and climbing.

2) When a revised draft was submitted on January 20th, it was natural to assumed it would carry a more realistic set of assumptions⁵. Instead, the only revisions involved a reallocation among items on the expenditure side of the ledger – specifically, the appropriations for the offices of the President and Vice President⁶. The implausible fiscal arithmetic thus remained unchanged, viz.:

- Revenues: **N3,856 billion;**
- Expenditure: **N6,078 billion;**
- Budget deficit: **N2,222 billion – i.e. 2.16% of GDP.**

3) The government's resolute ostrich-like stance in the face of a torrent of negative data **prompted one opposition Senator to declare the revised Bill "dead on arrival"**⁷. In the ensuing days, however, a number of opportunities arose to address the fundamental imbalance between planned expenditure and realistic revenue projections.

¹ Total outlays under the Appropriations Bill (2016) were 35% higher than in the 2015 budget.

² Also, the draft budget implausibly assumes that collections under such major revenue items as *Corporate tax, Customs* and *VAT* will match or exceed the levels initially programmed for 2015 – despite the compelling evidence of a sharp slow-down in economic activity.

³ This had marked a 3.2% decline on Nigeria's 2014 performance, and reflected the shortfall in related capital expenditure resulting from the NNPC's chronic inability to meet cash-call obligations under its various joint-venture agreements.

⁴ Source for statistics cited: Table 8 – OPEC Crude oil production (based on direct communication), in *Monthly Oil Market Report*, published Jan. 16, 2016

⁵ Ironically, it was on the same date that the Nigerian Customs Service publicly bemoaned the sharp reduction in imports caused by the central bank's exchange-control measures and the resulting shortfall in customs revenues.

⁶ The authorities appear to have been stung by the Opposition's taunts of profligacy over allocations such as N3.7 billion for the "purchase of BMW saloon cars" for the Presidency's principal officers; N189 million for "tyres" for the presidential fleet; and N1.415 billion for local and international travels (a significant increase for the N944,672,109 spent in 2015).

⁷ i.e. Sen. Eyinnaya Abaribe (PDP-Abia State), as quoted by Hassan Adebayo in *"National Assembly begins deliberation on Nigeria's 2016 budget"*; *Premium Times*, Jan. 20, 2016. "

4) At its January 25-26 session, the monetary policy committee might have taken to heart the admonitions of the IMF's Lagarde⁸ three weeks earlier and made a move towards exchange-rate flexibility. **A rate of N255 would have increased the Naira proceeds from Nigeria's oil sales by N523.6 billion**⁹ - thereby erasing approximately 24% of the projected fiscal gap of N2,222 billion.

However this was not to be - a point that **Buhari** himself rammed home two days later when he **declared that he was not prepared to "kill the naira"**¹⁰.

5) The National Economic Council which convened on January 28th presented a second opportunity for budgetary realignment – *inter alia* by tackling **Nigeria's VAT rate** which, Mme. Lagarde had observed, **"is among the lowest in the world and well below the rates in other ECOWAS members—so some increase should be considered."**¹¹

Instead, the meeting decided that "Government will not impose additional taxes on individual and corporate bodies to avoid additional burden on Nigerians."¹²

6) Clearly, something had to give¹³, so it did not come as a complete surprise when the news broke on January 31st that **Nigeria was seeking a budgetary support package of USD 3.5 billion** from the World Bank and the African Development Bank¹⁴.

The most significant aspect of this demarche, however, is the fact that **IMF endorsement of the government's economic policies is a precondition** for any such financing from the World Bank.

Based on Lagarde's afore-mentioned admonitions, **no such 'certification' is likely** so long as the dysfunctional exchange-rate regime remains in place.

7) The retired general is therefore stuck with **an invidious choice**¹⁵ between:

- sticking to his guns and **having to raise the required financing elsewhere**¹⁶, at a considerably higher cost than the 3% interest rate reportedly under discussion with the World Bank; and,
- **discarding the heterodox exchange-rate regime** that he has so vocally championed.

⁸ See our research note "Lagarde sounds the alarm", Jan. 7, 2016.

⁹ i.e. N2,583 billion instead of the N1,778 billion projected.

¹⁰ Per transcript by presidential spokesman Garba Shehu, as quoted by Paul Wallace and Emele Onu in "Nigeria's Buhari Rejects Devaluation, 'Won't Kill' the Naira," *Bloomberg*, Jan. 28, 2016.

¹¹ "Nigeria—Act with Resolve, Build Resilience, and Exercise Restraint"; speech by Christine Lagarde, IMF Managing Director, International Monetary Fund, to the Nigerian National Assembly; Abuja, Jan. 6, 2016.

¹² Remarks by Minister for Budget and Economic Planning, as quoted by Ayoola Mudasiru in "No Tax Increase to Fund 2016 Budget; NNPC, FIRS, NIMASA, Others Set for Audit – FG", Jan 29, 2016.

¹³ In a paper ("Nigeria's economy: the road to recovery") delivered on January 21st, the Finance minister had implicitly conceded that the official deficit target was likely to be breached when she alluded to the deficit ceiling of 3% of GDP stipulated in the Fiscal Responsibility Act (2007).

¹⁴ Particularly since it had emerged two days earlier that officials from the IMF and World Bank were in Baku, discussing measures to support the similarly beleaguered Azerbaijani government.

¹⁵ In the strongly monocephalic Buhari administration, it is inconceivable that the finance minister would ever have engaged with the World Bank without written approval/instructions from the Villa. As such, the implication is that whoever issued said instructions was unaware of the IMF prerequisite for such budgetary support.

¹⁶ And after destroying the credibility of his Finance minister.

8) We therefore **anticipate a protracted stalemate until the matter is settled - as we believe it must be -** by the combined weight of:

- the ballooning **fiscal deficit**;
- the **widening arbitrage** between the official and parallel-market exchange-rates; and
- the **relentless depletion** of Nigeria's external reserves.

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