EXTERNAL DEBT MANAGEMENT AND NIGERIA'S ECONOMIC GROWTH (1980-2012)

BY

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ECONOMIC GROWTH

(1980-2012)

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DECLARATION PAGE

I, AKPOCHAFO Emojevwe Kelvin hereby declare that this dissertation is an original research work undertaken by me in the Department of Economics, Delta State University (DELSU),Abraka and that this research work has not been submitted anywhere for the award of any degree.

AKPOCHAFO EMOJEVWE KELVIN

CERTIFICATION PAGE

This is to certify that this dissertation is an original research work carried out by Mr. AKPOCHAFO Emojevwe Kelvin for the Department of Economics, Delta State University (DELSU), Abraka, Nigeria; and that the dissertation has been carefully read, supervised and approved as having satisfied the requirements for the award of Master of Science Degree in Economics.

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DEDICATION PAGE

This Master of Science Dissertation is dedicated to my wonderful family; my Sweetheart, Mrs Enajite Akpochafo and my lovely jewels: Oghenetega, Oghenetekevwe and Oghenetejiri Emojevwe.

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ABSTRACT

The study examines the management of external debt and Nigeria's economic growth. The model built for the study proxied GDP Growth Rate as endogenous variable, measuring economic growth as a function of external debt, external debt service payments and exchange rate as exogenous variables. Annual time-series data were collected from the Central Bank of Nigeria (CBN), Statistical Bulletin and the Debt Management Office(DMO) from 1980-2012.The econometric techniques of Ordinary Least Squares(OLS), Augmented Dickey Fuller(ADF), unit root test, Johansen cointegration test and Error Correction Mechanism(ECM) were employed in the empirical analysis. The cointegration test shows that a long –run equilibrium relationship exists among the variables. It was found in the study also that external debt has no significant impact on the level of economic growth in Nigeria, although it has a negative relationship with economic growth thereby retarding it. Another major finding of the study is that, like external debt, debt service payments deter economic growth. The study therefore recommends that for external debt to contribute positively to economic growth in Nigeria, financial discipline should be taken seriously by the government. Also, the government should always solicit for debt relief and policymakers should be guided in the depreciation of the Naira because of the diverse economic implications of its devaluation.

INTRODUCTION

CHAPTER ONE

1.1 Background to the Study

Obviously, governments borrow to fill the vacuum created by fiscal gaps in the proposed expenditure and expected revenue within a fiscal period. This could be the savings-investment gap or import-export gap. If the government does not want to compromise macroeconomic stability by printing more money and government taxation capacity is limited, then debt option becomes the only available avenue that the government can explore to provide social overhead capital for the citizenry. Governments borrow in principle to finance public goods that increase welfare and promote economic growth. The spending has to be financed either through taxation, through seignorage or with debt. Due to the scarcity of resources, the law of comparative advantage and differences in mineral endowment, nations depend on each other. The necessity for government to borrow in order to finance deficit budgets has led to the development of external debt. External debt sourcing is one of the ways through which countries finance their deficits and execute economic projects that are capable of increasing standard of living and promoting sustainable economic growth and development.

Sustainable economic growth is a major concern of any sovereign nation, especially the developing countries, which are characterized by low capital formation due to low levels of domestic savings and investment (Adepoju, Salau and Obayelu, 2007).It is obvious that these developing countries when they are faced with scarcity of capital resort to borrowing from external sources in order to supplement domestic savings (Aluko and Arowolo2010). Soludo (2003) asserted that countries borrow for two main

reasons; the macroeconomic reason of financing higher level of consumption and investment or to finance balance of payment deficit and avoid budget constraint so as to boost economic growth and reduce poverty. The usual necessity for government to borrow in order to finance budget deficit has led to the creation of external debt(Osinubi and Olaleru, 2006).Hameed, Ashraf and Chawbury,(2008) stated that external borrowing ought to stimulate economic growth, especially when domestic financing is inadequate. External debt also improve total factor productivity through increase in output which in turn promote the growth of Gross Domestic Product (GDP).

Developing countries including Nigeria have always contracted large amount of external debt that has led to the mounting of trade debt arrears at high concessional interest rates. Gohar and Butt(2012) opined that accumulated debt service payments create a lot of problems for developing countries because the debt service payments actually surpasses the acquired loan and this slows down the growth process in such countries

The origin of Nigeria external debt dates back to 1958 when the sum of US$28million was used to finance the Nigeria Railway Construction. Foreign borrowing was minimal between 1958 and 1977, that is, not the level that could be regarded as a burden to the country. Debt contracted during the period were the concessional loans from official sources such as the World Bank and Nigeria's major trading partners(i.e bilateral and multilateral sources) with longer repayment periods from ten to forty years and lower interest rates. The country had a comfortable external reserve as a result of the unprecedented inflow of foreign exchange receipts from crude oil (Uche, 2005).

The Nigerian economy was characterized, during the period of the oil boom of the 1970s, with high degree of openness. The economy was highly dependent on the external sector in its manufacturing development strategy. Consequently, capital-intensive technology, and assembly-type industries dependent on imported inputs were stimulated and Nigeria had a high import-GDP ratio. Indeed, the need to protect a given level of consumer goods availability became so pervasive that it was difficult to cut expenditure in this area. During most of the 1970s, budgetary expenditures were greater than the fast rising income from oil.

The 1978 collapse of oil prices, exerted considerable pressure on government finances and it became necessary to borrow to support balance of payments and to finance developmental projects. The work of Adepoju, Salau & Obayelu(2007) characterized Nigeria as a country with inadequate capital as a result of low productivity, low income and low savings. The situation calls for technical, managerial and financial support from external or foreign bodies to bridge the gap. Capital formation and development in developing countries are hindered as a result of external debt. External debt may not constitute a problem to the economic growth of a developing country. The principal and servicing requirements of debt are what constitute the debt accumulation of developing countries.

Heavy external debt does not necessarily imply a slow economic growth. It is a country's inability to meet its debt obligations compounded by the lack of information on the nature, structure and magnitude of the external debt (Were, 2011). A country may have heavy external debt along with relatively higher level of exports that can help them to sustain their level of external debt. But external debt, if not sustainable, imposes higher

risk to the economic prosperity of a country, as its servicing which is also an indicator of higher current account deficit, may lead to debt overhang in a country. The resultant effect of the debt quagmire in Nigeria could create unfavourable economic problems such as crowding out of investments, poor GDP growth among others (Ngozi- Okonjo Iweala, 2011). However, several studies have laid emphasis on the effects of external debt and its management on economic growth in Nigeria (Adepoju,Salau & Obayeli, 2007;Ayadi and Ayadi, 2008) This study therefore aims at contributing to the existing debate by investigating the influence of external debt on Nigeria's economic growth. The study seeks to determine whether external debt management can be growth promoting in developing countries or not, using Nigeria as a case study.

1.2 Statement of the Problem

Countries, especially the developing ones like Nigeria, seek external debt funds to achieve macroeconomic objectives of sustainable economic growth, reduction of unemployment, to fill the savings-investment gap, to execute specific gigantic projects or to augment a deficit budget among others. Therefore, they continue to borrow externally even when the debt burden or debt service payments begin to have adverse effects on Gross Domestic Product, exports, savings, investment, or on the resources needed for developmental purposes.

Countries experiencing fiscal deficits, especially the developing ones borrow to improve their economic growth. Government borrows in principle to finance public goods that increase welfare and promote economic growth (Ogunmuyiwa, 2011). Due to the fact that the domestic financial resources are not adequate, borrowing is acquired from foreign sources. The amount of fund provided by these foreign sources constitutes

the external debt of a nation. In Nigeria, external debt is sourced from multilateral agencies, Paris club creditors, London club creditors, Promissory Note holders and other creditors. External debt is one of the sources of financing capital formation in any country (Ayadi and Ayadi, 2008).External debt is acquired to contribute meaningfully to the economy but the future debt service payment poses a threat to economic growth.

The problem of external debt of the Less Developed Countries (LDCs) (Nigeria inclusive) is a serious one because they depend heavily on inflows of capital from abroad to finance their developmental needs. (Jhingan2010). Therefore, to accelerate the rate of economic growth and development, they borrow to import capital goods, components, raw materials, technical know-how etc.

Aluko and Arowolo (2010) pointed out that the major cause of the debt crisis situation in Nigeria is the fact that these foreign loans are not being used for developmental purposes. Instead of being ventured into capital projects that will better the economy, they are shrouded in secrecy. According to (Debt Management Office of Nigeria, 2012), the factors that led to Nigeria's external debt burden can be grouped into six areas;

(i) Inefficient trade and exchange rate policies:

(ii) Adverse exchange rate movements.

(iii) Adverse interest rate movements.

(iv) Poor lending and inefficient loan utilization.

(v) Poor debt management practices

(vi) Accumulation of external debt arrears and penalties

External debt stock rose rapidly from US$4.6billion in 1980 to US$18.6billion in 1986, this included the trade arrears accumulated in 1982 and 1983 amounting to US$29.7billion by 1988 and US$32.9billion debt outstanding at the end of 1990,

US$17.1 billion was owed to official creditors who were members of the Paris Club,US$5.9 billion to the London Club of creditors, US$3.7billion to multilateral financial institutions, mainly the World Bank Group, US$4.4billion in the form of promissory notes issued by the Central Bank of Nigeria in respect of rescheduled, uninsured trade arrears, while other creditors accounted for the balance of US$1.7billion. By 1991, the external debt of Nigeria has risen to $33.4 billion while by 1995, it was $32.6 billion.(Ekperiware and Oladeji,2012)

Before the debt cancellation, Nigeria was paying the sum of $4.9 billion for debt servicing every year. This represents a great leakage of financial resources that could have been used to reduce poverty or develop existing infrastructures. During this period, the Nigerian government realized that it had plunged itself into an economic malaise and debt quagmire that normal debt management strategies such as debt rescheduling, debt buyback etc will not suffice to solve the problem. Herein began the campaign for debt relief or cancelation. On election as president of Nigeria in February 1999, and before assumption of office, President Olusengun Obasanjo took a tour round the world pleading for debt relief and wooing investors. This effort yielded results six years after, when in April 2005, the Paris Club of Creditors wrote off about 40 per cent of its debt owed by Nigeria. This represents about $18 billion cancellation of debt and a resounding achievement of the Obasanjo Administration (Adesola, 2009).

Following the successful Paris Club debt deal and exit from the London Club debts, the external debt stock dropped to US$3,544.49 million in 2006 from US$35.94 billion in 2004 and stood at US$3,654.21 as at December 31, 2007(Adesola, 2009)

Going by recent developments and indications, Nigeria's external debt is unfortunately on the increase again. By March 2010, the external debt of Nigeria had hit an all time high amount of $32.5 billion(about N4.875trillion). This amount increased to $36.45 billion (about N5.60 trillion) by March 2011 and to $44.28 billion (about N6.88 trillion) as at March 2012 . Recently, the International Monetary Fund (IMF) raised concern and alarm over Nigeria's rising debt portfolio, warning that the cost of servicing the country's debt could rise to 35 per cent of revenues in the next four years(Adesola,2009).

Moreover, popular theories of economic growth such as the Harrod-Domar and Dual-Gap among others recommend external debt as a prerequisite for growth to take place where savings are low. Therefore, despite all the problems that are associated with external debt , Nigeria still borrows even when such acquisition of external debt do not conspicuously translate into promoting economic growth and development. So, why does Nigeria still borrow? Does external debt retard or augment economic growth? This is the main problem or issue this research is set out to address.

1.3. Research Questions

(i) What are the nature, causes and consequences of Nigeria's external debt?

(ii) What are the effects of external debt accumulation, debt service payments and exchange rate changes on the economic growth of Nigeria?

(iii) Has the management of external debt in Nigeria been able to reduce the debt burden?

(iv) What are the pragmatic approaches/measures used in reducing the debt burden in Nigeria?

1.4. Research Hypotheses

Ho: There is no significant relationship between external debt and Nigeria's economic growth.

Ho: There is no significant relationship between debt service payments and Nigeria's economic growth.

Ho: There is no significant relationship between exchange rate and Nigeria's economic growth.

1.5. Objectives of the Study

The broad objective of this study is to investigate the effect of external debt management on the economic growth of Nigeria. The study therefore has the following specific objectives to:

(a) Observe Nigeria's external debt trend vis-à-vis economic growth

(b) Ascertain the long-run sustainability of external debt-induced growth process

(c) Explore the empirical relationship between external debt management and economic growth in Nigeria.

1.6. Significance of the Study

Most developing countries, including the ones in Sub-Saharan Africa are heavily indebted. Nigeria is not an exception. The debt relief Nigeria got from the Paris Club in 2005 is an attestation to this fact. Therefore, this study is significant in the following ways:

(1) The study will ascertain whether external debt retards or augments economic growth in Nigeria

(2) The study will explore the effects of external debt management strategies on the economic growth of Nigeria.

(3) The study will determine whether changes in exchange rate influence economic growth in Nigeria or not.

1.7. The Scope of the Study

The scope of this study on the management of external debt and the economic growth of Nigeria covers the period from 1980-2012.Therefore, issues pertaining to the domestic debt will not be discussed. The variables to be used include GDP, External Debt Stock and Debt Service Payments. This period is chosen because it is the most recent period as at when the research is being undertaken. Moreover, the country experienced its most devastating debt quagmire during the 1980s following the collapse of world crude oil prices.

1.8. Limitations of the Study

A major limitation of the study is that it takes about three years in Nigeria before reliable and relevant data on the Nigerian economy are published by the Central Bank of Nigeria, Bureau of Statistics, the World Bank etc. Therefore most researches cannot capture recent and current trends in the variables under study.

1.9 Organisation of the Study

This study contains five chapters. The first chapter contains the background of the study, the statement of the problem, the objectives of the study, the research questions etc that guided the study. Chapter two summarises the opinions of different authorities on the subject matter. Chapter three states the methodology, statistical techniques and econometric procedures adopted in the study. Chapter four focuses on the presentation

and interpretation of the regression results. While chapter five, the last of the chapters, presents the summary of the findings, conclusion and appropriate recommendations.

1.10.Operational Meanings

(i) **External Debt:** For the purpose of this study, external debt is referred to as the unpaid portion of borrowed external resources acquired for developmental purposes or balance of payments support which could be paid or unpaid as at when due.

(ii) **Economic Growth:** Economic growth in this context refers to the ability of a country to generate and sustain an increase in its GDP over a fairly long period of time.

(iii) **Debt Service Payment:** This is the amount of money required to make payments on the principal and interest on outstanding loans, the interest on bonds, or the principal maturing bonds.

(iv) **Interest Rate:** An interest rate is the rate at which interest is paid by a borrower(debtor) for the use of money that is borrowed from a lender (creditor).Specifically, it is a percentage of principal paid a certain amount of times per period(usually quoted per annum)

(v) **Debt Rescheduling:** Debt rescheduling refers to the re-negotiation of debt so that payment is made at a later date or repayment period stretched out.

(vi) **Debt Equity Swapping:** This is an external debt management strategy in which external debt is internalized and external debt is converted into equity.

(vii) **Debt Refinancing:** A debt refinancing agreement involves elongating or extending the maturing at which a debt instrument will become liquid

(viii) **Debt Overhang:** The debt overhang theory states that, beyond a certain point, high external debt burden acts as a tax on investments, since whatever is gained in increased output goes to the creditor in the form of debt service payment.

(ix) **Crowding Out Effect:** An economic concept where increased public sector spending replaces, or drives down, private sector spending or investment. In other words, it refers to when government must finance its spending with taxes and/or deficit spending leaving businesses with less money and effectively crowding them out.

CHAPTER TWO

LITERATURE REVIEW AND THEORETICAL FRAMEWORK

2.1. Introduction

In this chapter, the conceptual framework of debt is presented, in which many concepts relating to debt and external debt are presented. Also presented are theories of economic growth according to different Economists. Finally, an empirical review of different literatures relating to the relationship between external debt and economic growth are brought into limelight.

2.2 The Concept of Economic Growth

Economic growth is the increase in market value of goods and services produced by an economy over time. It is conventionally measured as the percent rate of increase in real Gross Domestic Product, or real GDP. Similar to GDP is the growth of the ratio of GDP to population, called GDP per capital, which is also called per capita income. An increase in economic (GDP) growth caused by more efficient use of inputs is called intensive growth. While the GDP growth caused only by increases in inputs such as capital, population or territory is called extensive growth. In Economics, economic growth or economic growth theory typically refers to growth of potential output, that is, production at full employment.

Economic growth is usually measured or calculated in real terms- that is inflation adjusted terms-to eliminate the distorting effect of inflation on the price of goods produced. The measurement of economic growth uses national income accounting. Since

economic growth is measured as the annual percent change of Gross Domestic Product, it has all the advantages and drawbacks of that measure.

2.3 The Concept of External Debt

Debt has been defined by different authors in several ways. According to Oyejide(1985), debt is defined as the resource or money in use in an organization or government which is not contributed by its owners and does not in any other way belong to them. External debt on the other hand is defined as a financial obligation that ties one party (debtor country) to another (lender country). It usually refers to incurred debt that is payable in currencies other than that of the debtor country. The act of borrowing creates debts and this debt may be domestic or external. The focus of this study is on external debt which refers to that part of a nation's debt that is owed to creditors outside the nation Arnone(2005) defines external debt as that portion of a country's debt that is acquired from foreign sources such as foreign corporations, government or financial institutions. According to Ogbeifin (2007), external debt arises as a result of the gap between domestic savings and investment. As the gap widens, debt accumulates and this makes the country to continually borrow increasing amounts in order to stay afloat. He further defined Nigeria's external debt as the debt owed by the public and private sectors of the Nigerian economy to non-residents and citizens that is payable in foreign currency, goods and services. Debt crisis occurs when a country has accumulated a huge amount of debt such that it can no longer effectively manage the debt which leads to several mishaps in the domestic political economy(Adejunwo , James & Soneye, 2010).

2.4 Debt cum Growth Theory

The first strand of thought in the debt cum growth theory is the substituting school of thought. It considers external debt as a substitute for domestic savings and investment

and therefore domestic savings and investment are crowded out as a result (Krugman, 1988; Alesina & Tabellini, 1990; Tornell & Velusco 1992). The thinking is that the returns from investing in a country are seen as being subjected to a high marginal tax by creditors and this may discourage domestic and foreign investors. This is the familiar debt overhang theory. It is also argued that foreign savings may be used for consumption rather than for investment. However, studies by Cohen and Sachs (1986) and Cohen (1992) present endogenous growth models where capital accumulation is the driving force for growth (Nyong, 2005).

Another theory in this regard is the original non-optimizing approach which was advanced in the framework of the 'growth-cum-debt' literature. Here, emphasis has mainly been on foreign borrowing for investment purposes, i.e. for filling the gap between domestic investment and savings (Solomon 1997). The growth-cum –debt models or theory consider debt capacity in terms of the benefits and costs of borrowing in the process of economic growth. The basic argument is that, a country will maintain its capacity to service debt provided that additions to its debt over time contribute significantly to growth.

Another strand of thought in the debt cum growth nexus sees external debt as capital inflow with positive effect on domestic savings and investment and thus on growth which leads to poverty reduction via appropriate targeting of domestic savings and investment (Calvo, 1998)

2.5 Dual Gap Theory

Another theoretical framework on which the relationship between external debt and economic growth is based is the Dual-Gap Theory. According to Boboye and Ojo (2012),they explained that the dual gap analysis shows that economic growth and development is a function of investment and that such investment which requires domestic savings is not sufficient to ensure that economic growth takes place. Therefore, the theory suggests that it is logical for a country to seek the use of complementary external goods and services and funds. This leads to the growth of external debt.(Ajaji & Khan, 2000).Symbolically,

$$I-S = M-X \ (M.>X, I>S)$$

Where I =Investment

S =Savings

M=Imports

X=Exports

(I-S) is the domestic savings gap and (M-X) is the foreign exchange gap

The idea is that the savings gap and the foreign exchange gap are two separate and independent constraints on the target rate of growth (Chenery,1962). Chenery sees foreign aid (that is external debt) as a way of filling these two gaps in order to achieve the target growth rate of an economy.

The savings gap and foreign exchange gap are always equal ex-post but unequal in size in the ex-ante sense. It is assumed that savings and foreign exchange cannot be substituted for each other and potential savings cannot be transformed into exports. Based

on these assumptions and some others, fig 1 illustrates the two ex-ante gaps and their relation to different target growth rates of income (Jhingan, 2010)

If the target growth rate is OG1, then the foreign exchange gap is larger than the savings gap by ab. On the other hand, if the target growth rate is OG2, the savings gap is larger than the foreign exchange gap by cd. At point 'E' the savings gap and foreign exchange gap are equal.

2.6 Harrod-Domar Growth Model

The last theoretical framework underlying this study is the Harrod-Domar growth model. The theory states that economic growth rate depends on the level of savings (higher savings which enable higher investments) and capital-output ratio(efficiency of investment)

Every economy must save a certain proportion of its national income, if only to replace worn-out capital goods (buildings, equipment, materials etc). However, in order to grow, new investments representing net additions to capital stock are necessary. If we assume there is some direct economic relationship between the size of the capital stock, 'K' and total GDP,'Y'. Suppose that this relationship is defined as the capital-output ratio. If we assume further that the national net savings ratio, s, is a fixed proportion of national output and that total new investments is determined by the level of total savings, (Todaro and Smith, 2010)

Todaro and Smith replicated the Harrod-Domar Model as follows:

(i) Net savings(S) is some proportion,'s' of national income(Y) such that we have the simple equation

$$S = sY \qquad (1)$$

(ii) Net investment (l) is defined as the change in the capital stock,'K and can be represented by ΔK such that

$$I = \Delta K \qquad (2)$$

But because the total capital stock ,'K' bears a direct relationship to total national income or output,'Y' as expressed by the capital-output ratio,c. It follows that

$$K/Y = c$$

Or

$$\Delta K/\Delta Y = c$$

$$\text{That is } \Delta K = c\Delta Y \qquad (3)$$

Finally, because net national savings ,S, must equal net investment, I, we write

$$S = I \qquad (4)$$

But from equation (1), we know that $S = sY$ and from equation (2), we can write

$$I = \Delta K = c\Delta Y$$

It therefore follows that we can write the identity of savings equaling investment shown by equation (4) as:

$$S = sY = c\Delta Y = \Delta K = I \qquad (5)$$

Or simply as:

$$sY = c\Delta Y \qquad (6)$$

Dividing both sides of equation (6) first by Y and then by c, we obtain the following expression

$$\Delta Y/Y = s/c \qquad (7a)$$

Note that the left hand side of equation (7) is GDP growth rate. Equation (7) which is a simplified version of the famous equation in the Harrod-Domar theory of economic growth, which states that the rate of growth of GDP ($\Delta Y/Y$) is determined jointly by the net national savings ratio ,s, and the national capital-output ratio,c,

Equation (7) is often expressed in terms of gross savings sg, in which case the growth rate is given by

$$\Delta Y/Y = sg/c - q \qquad (7b)$$

Where q is the rate of capital depreciation

The economic implication of equations 7a and 7b is that to grow, economies must save and invest a certain proportion of their GDP. The more they can save and invest, the faster they can grow. But since the level of savings is low in Less Developed Countries LDCs, external debt constitutes the only complementary option to economic growth.

2.7. Nigeria's External Debt Servicing

The major challenge faced by the Debt Management Office is ensuring that a reasonable level of resources are earmarked for debt servicing to avoid the risk of default and to maintain conducive relations for debt relief negotiations with the creditors. Also, the Debt Management Office faces the challenge of ensuring that budget resources are released in time to effect debt service payments since much of Nigerian's debt stock build – up was accounted for by the capitalization of interest arrears and penalties for default.

Debt service payments to the World Bank are due every 15 days while ADB (African Development Bank) service payments occur frequently. The debts are not subject to debt relief or rescheduling and in case of default, they carry stiff consequences with sanctions coming 30 days after due date. The implications for default include:

(i.) Prohibition of borrower/guarantor from signing new loan or guarantee agreement with the banks.

(ii).Suspension of disbursement in respect of all Bank group loans granted to the borrower/guarantor and lastly.

(iii) Suspension of the granting of any new loan by the Bank group to the borrower/guarantor. The imposition of the above sanctions adversely affected the credit – worthiness of a Country as well as access to further foreign credits or loans. It is therefore to be avoided by all means.

(a) Paris club: Failure of our debt service obligation will undermine Nigerian's effort to obtain substantive debt relief over the medium term coupled with the inability to benefit from normal credit facilities as Export Credit Agencies in Paris club creditor countries in default of debt service payment. Also business and government agencies from such debtor countries seeking to import goods and services are required to pay the full 100% upfront, even against deliveries that will take several months and at times, years.

(b)Bilateral: Defaulters in this category incur penalty charges in the form of late interest, which are usually about 1-3% above the normal interest charged.

(c)London Club: The consequences of defaulting are stiff as the instruments carry legal obligations e.g. If par bonds on promissory notes payment are not received as at when due, creditors could acquire the assets of the Central Bank of Nigeria CBN and Nigerian National Petroleum Corporation (NNPC) anywhere in the world, as Nigeria has expressly waived her sovereign immunity under the terms of the agreement. In line with the desirable consequences of default in debt service payments the best arrangement must be put in place from time to time in response to changes in the economy and the polity.

In order to facilitate the implementation of a new debt service arrangement, the Debt Management Office had agreement with the debtors on the nation's external debt stock

and debt service obligation so that levels of government and their agencies that contracted the loans would know their respective stock of debt and the required amount for servicing.

2.8. Negative Effects of Debt Servicing on the Nigerian Economy

During the oil boom of 1960s, General Yakubu, the then Military Head of State in Nigeria reportedly boasted that how to make money was not a problem to Nigeria and that the problem Nigeria had was how to spend their money. But by 1986, political instability, economic instability, policy fluctuations, bribery, corruption, bank fraud, misappropriation and embezzlement of public funds, non-commitment to sound economic philosophy, politicization of economic projects, weak legal framework, mismanagement and squander-mania led Nigeria to the introduction of the Structural Adjustment Programme (SAP). The programme was in partial fulfillment of the conditionalties imposed on the country by the International Monetary Fund, IMF, as a pre-condition to obtain more international loans. Incidentally, the same conditions that led to obtaining the loan also led to its mismanagement, leaving Nigerians with an acute decline in the standard of living, gross social and economic overhead depreciation, high external dependence, currency depreciation, balance of payment disequilibria, exchange rate depreciation and rising inflationary rate.

Before the year 2000, Olusegun Obasanjo, the then President of Nigeria had started campaigning that no meaningful economic growth could take place in Nigeria with such a heavy external debt burden and its debt servicing conditions. For Nigeria to have the

impact of economic growth, he argued, it must be granted some debt reduction, debt relief, debt buy back or debt cancellation. During that time, Nigeria's external debt stood at $34.0 billion in December, 2004. 85% of the debt was owed to the Paris club, 8% to the multi-lateral financial institutions - the World Bank and African development bank while the remaining 7% was owed to the London club of financial creditors, amongst others. Owing to that campaign, Nigeria gained a debt relief package of about $18 billion by April 2006. That notwithstanding, the $US3.0 billion annual debt servicing which Nigeria was paying prior to that era adversely undermined her capacity for economic growth.

2.9 The Structure of Nigeria's Debt Profile

Nigeria External Debt Creditors

Nigeria has contracted a number of debt obligations from external sources. This could be grouped into two main categories (see table below).

A (i.) **Official Debt:** This consists of Paris club debt, multilateral debts and bilateral debts.

(ii). **Private Debts:** This is made up of uninsured short-term trade areas contracted through the medium of bills for collection, open account, etc. commercial bank debts acquired through loans/letters of credit. Credits are in this case, referred to London club debts.

Much of the Country's external debt is owed to fifteen creditor countries belonging to the Paris Club. Paris Club debt is government-to-government credits or market –based term loans, which are guaranteed by various Export Credit Agencies of the creditor countries. The Paris club is a cartel of creditor countries that provide information forum

where Countries experiencing difficulties in paying their official debts meet with creditors to reschedule the debts. It is an informal group with no permanent members, which works under principle of consensus. Paris club members Countries to which Nigeria is indebted are: Australia, U.S.A, Spain, Israel, France, Switzerland, Germany, Demark, Italy, the Netherlands, Japan, the U.K, Belgium, Russia and Finland. The total amount owed to members of the club as at Dec 31 2004 amounted to US35.9 Billion.

B. The second category is the multilateral debts: These are project loans owed to multilateral financial initiatives (e.g. the World Bank Group, the Africa Development Bank Group, the European Investment Bank Group, IFAD and ECOWAS Fund) by federal and state governments and their agencies. The total amount owed to multilateral institutions by Nigeria as at December 2004 was US $ 2.8 Billion.

C. The third category of debts is bilateral debts otherwise called Non – Paris club bilateral debts: These are debts owed to Countries which are not members of the Paris club and whose debts are not insured by the Export Credit agencies. The amount owed to this category by Nigeria as at December 2004 was US0.05 Billion. Debt service payments in 2001 and 2002 to this source were US33.81 and 34.9 Million respectively.

D. The fourth category of debts are the commercial debts. They are further divided into two groups.

i. London Club: This is a group of commercial banks that join together to negotiate the restricting of their claims against debtor countries. London Club debts are arrears of commercial bank term loans. They also include some arrears of letters of credit, bills for collection, open account, dividends, and airline remittances. The total amount owed by Nigeria as at December 2004 was US1.4 Billion.(Adepoju et al 2007)

Presently, Nigeria does not owe the Paris Club at all.

ii. Central Bank of Nigeria (CBN) promissory notes. These were trade arrears contracted by ordinary Nigerians, between 1981 and 1986 but who deposited the local currency with which to make the remittances. This is why the promissory notes are now regarded as Federal Government of Nigeria debt. The arrears were finally covered with Promissory Notes in January 1988, the stock amount to US 4.8 Billion to be authorized quarterly ending on January 5, 2010. The outstanding balance of promissory notes as at December 31, 2004 was US 0.8 Billion.(Adepoju et al 2007) Today, promissory notes debt is nil

Table 2.1: Composition of Nigeria's External Debt Stock as at 30th June 2010 (*In Millions of USD)*

Category	Principal Balance 1	Principal Arrears 2	Interest Arrears 3	Total 4	Percentage 5
MULTILATERAL					
World Bank Group					
IBRD	58.92	0.00	0.00	58.92	
IDA	3,218.17	0.00	0.00	3,218.17	
IFAD	57.95	0.00	0.00	57.95	

African Development Bank Group	124.82	0.00	0.00	124.82	
ADB	287.20	0.00	0.00	287.20	
ADF					
EDF	109.64	0.00	0.00	109.64	
IDB	3.98	0.00	0.00	3.98	
Sub-total	3,860.68	-	-	3,860.68	90.42%
Non-Paris					
Bilateral	181.38	0.000	0.000	181.38	
Commercial	227.65	0.00	0.00	227.65	
Sub-total	409.03	-	-	409.03	9.58%
Grand-total	4,269.71	0.00	0.00	4,269.71	100.00%

Source: DMO databank Abuja, Nigeria

IFAD: International Fund for Africa Development

ADF: African Development Foundation (US)

EDF: European Development Fund (EU)

IDB: Inter-American Development Bank

ADB: African Development Bank

IDA: International Development Association (The World Bank)

Table 2.2: Nigeria's external debt stock (outstanding) in N' Million 2001-2012

Years	Multilateral	Paris Club	London Club	Promissory Notes	Others	Total
2001	313,504.70	2,475,509.40	228,950.2	144,746.20	13,580.50	3,176,291.0
2002	375,700.10	3,220,823.50	182,964.5	146,341.10	7,055.60	3,932,884.8
2003	413,877.70	3,737,279.90	196,156.9	123,994.60	7,020.20	4,478,329.3
2004	384,248.70	4,196,844.60	196,155.5	106,558.40	6,462.40	4,890,269.6
2005	330,654.40	2,028,580.10	189,768.4	85,526.70	60,542.60	2,695,072.2
2006	332,219.20	0.00	0.00	64,832.60	54,409.90	451,461.70
2007	363,448.79	0.00	0.00	0.00	67,631.05	431,079.85
2008	420,603.58	0.00	0.00	0.00	72,576.64	493,180.22
2009	524,208.11	0.00	0.00	0.00	66,232.97	590,441.08
2010	635,454.90	0.00	0.00	0.00	54,390.40	689,845.30
2011	2,101,250.0	0.00	0.00	0.00	0.00	2,101,250.0
2012	2,028,641.4	0.00	0.00	0.00	0.00	2,028,641.4

Source: Central Bank of Nigeria and Debt Management Office

Figure 2.5: Nigeria's external debt stock 2001-2012

2.10. Analysis of Nigeria's External Debt Policies and performance.

(A). Pre -SAP period 1962 – 1985.

The national economic development planning started with expenditure of £678.8. Fifty percent of which emanated from foreign sources either in form of foreign private investment or direct foreign assistance to Government. The basic objectives of planning in Nigeria is not merely to accelerate the rate of economic growth and the rate at which the standard of living of the population can be raised, it is also to give an increasing measure of control over its future.

Nigeria has four different development plans before 1985. These are;

The first National Development Plan1962 – 1968

The second National Development Plan 1970 – 1974

The third National Development Plan 1975 – 1980

The fourth National Development Plan 1980 – 1985

The performance of the Nigeria economy during the First Two decades after independence was generally impressive than in the Pre – independence period in spite of the atmosphere of tumultuous political resurgence. The average GDP growth rate was 5.1 percent during First National Development Plan, 8.2 percent under the Second and 5.0 percent under the Third. In the same vein the growth rate of capital formation rose from an average of 14.1 percent under the first plan to 26.7 percent in the third plan . Yesufu (1996) judged the actual performances of the economy, the period between 1981 –1985 (The fourth National Development Plan) proved to be relatively the most dismal in the economic history of the country, at least since Planning as a strategy of growth and development was introduced in 1945. The growth rate of GDP per annum was only 1.5 percent (compared to 5.3 percent, 13.2 percent and 4.6 percent under First Three National Development Plans). The devaluation of Naira increased imbalance in the external trade and the external reserves stagnated and declined. While money income was falling, the cost of living was escalating destroying the welfare of the citizens. Over N80m was spent on food importation alone between 1981 and 1984 in spite of the much celebrated Green Revolution Programme. Agricultural production however came to dominance viz – a – viz mining as a contributor to GDP.

The primary per capital consumption that was expected to rise from N 27.5 in 1980, and maintained a steady growth rate of 6% per annum, shot up to N 257.8 in 1983. This made savings and investment difficult. High level of inflation made a mess of cost projection and financial projections were too optimistic and simplistic and therefore the revenue targets were easily frustrated by external shocks in the word oil market. By the end of 1984, the Nation was indebted to the tune of N21, 384, 5 million in external debt alone.

B. Structural Adjustment Programme(SAP) Period 1986 - 1991

The Nigerian SAP was designed to fit the standard IMF – World Bank structural adjustment packages and meant to effectively alter and restructure the consumption and productive patterns of the Nigerian economy, as well, to dominate price distortions and heavy dependence on the exports of crude oil and imports of consumer and producer goods (Anyanwu 1993). The programme was proposed as an economy package designed to rapidly and effectively transform the national economy over a period of less than two years (Yesufu, 1996). According to Adeyemi (1996), the philosophy of SAP was predicated on demand management as a measure of curtailing external imbalance with a restrictive monetary policy. The ultimate objective was to achieve non – inflationary growth and to stimulate domestic production of tradable goods. In addition, SAP was to achieve a sustainable external debt service profile and hence , domestic savings and investment and the inflow of external resources.

The economic performance under the structural adjustment programme appears to have performed better in terms of sectoral and overall GDP growth rates. This is attributable to positive development in the agriculture, oil and financial sectors. The

programme also corrected the over – valuation of the Naira which was a major cause of cheap import, enhanced the Government revenue which consequently reduced the need to borrow. However, the external debt burden increased from US$ 19.5 billion in 1985 to US$ 34.4 billion in 1991 as a result of new borrowings, increase in foreign interest rate, Capitalization of unpaid interest charges as well as the appreciation of exchange rates of various European and Japanese Currencies against US dollar. The debt service ratio which stood at an annual average of 16.3% between 1982–1985 increased to 26.7 percent between 1986 – 1994 creating a great strain on the foreign exchange earnings and reflecting the failure of the debt rescheduling programmes mapped out by the London and Paris Club Creditors (Adeyemi 1996). The pains of SAP however, include endemic inflation, foreign exchange shortage, sharp increases in unemployment, deterioration in health and educational standard, low capacity utilization and ever-rising fiscal deficits (Anyawu, Oyefisi, Oaikhenan & Dimiwo 1997). There was no efficiency in resource mobilization as savings refused to translate into investment (Adeyemi 1996).

C. Post SAP Period: 1997- 1998

The external sector came under severe pressure in 1995 with the balance of payments recording further deficits. On the external sector, the balance of payment deteriorated further than 1994 as well as the current account deficit. The latter was a result of relatively higher import level coupled with sharp increases in net payment of services and income which were huge enough to offset the improvement in export earnings.

There was also further accumulation of debt service arrears, as the nation did not meet the obligations as they fell due. Both the autonomous and parallel market exchange rates closed significantly averaging N82.3: US$ 1 and N83.7: US$1 respectively.

In 1997 there was downward pegging of allocation for debt servicing since other options were being explored to solve the debt problem. This was to allow more foreign exchange to be made available for domestic use. It was generally agreed that the Government should as a matter of policy not take any external loan except such are given on concessionary grounds and these should be used only for export – increasing or import – decreasing activities that can pay their way back.

D. Democratic Period (1999 – 2006)

Nigeria External debt stock in 1999 remained at about the same level as it was in 1988–US$28.77 billion. In spite of the lifting of the embargo on foreign loans, no new loans were contracted. However, some categories of debt were not serviced, particularly those owed to the Paris Club Creditor Countries as well as arrears on post cut off date debt. In spite of the resources constraints, the sum of US$1.5 billion was set apart to service external debt in year 2000 while arrangement continues on debt reduction negotiation with creditors. The Government resumed concessionary borrowing from multilateral and bilateral sources especially from the World Bank. Borrowed funds were strictly to be used for projects with satisfactory social and infrastructural projects and export–increase / import–decreasing features for economic projects (Obadan, 2000).

The debt overhang of US$ 31.0 billion in 2004 constituted a deterrent to private investment and generally to growth and development. The government in its budget proposed to service her external debt in a satisfactory manner without compromising the requirements for domestic growth. This is because some debts must be serviced as at when due, otherwise there may be serious consequences for the country.

Also in the plight of sourcing for substantial debt cancellation, it will help improve the image of the country with its creditors. There is the strong need for Nigeria to seek substantial relief from the heavy debt burden through initiatives that have features of debt reduction. A serious implementation of the NEEDS reform programme may be helpful in this regard (Obadan, 2004).

2.11. External Debt Management Strategies.

In the 1980s, the management of external debt became a major responsibility of the Central Bank of Nigeria (CBN). This necessitated the establishment of a Department in collaboration with Federal Ministry of Finance to the management of external debt. Although, the debt management strategies and measures varied from time to time since the early 1980s when the external debt became pronounced, the following measures were used by the Government as guidelines to external borrowing:

- Economic sector should have positive Internal Rate of Return (IRR) as high as the cost of borrowing

- External loans for private and public sectors projects with the shortest rate of return should be sourced from the International Capital Market while loans for social services or infrastructure could be sourced from concessional financial institutions.

- State Government, Parastatals, Private sectors borrowing receive adequate approval from the Federal Government so as to ensure that the borrowing conforms to the national objectives.

- Projects to be financed with external loan should be supported with feasibility studies which include loan acquisition, deployment and retirement schedule.

- State Governments and other agencies with borrowed funds should service their debts through the foreign exchange market and duly inform the Federal Ministry of Finance for record purposes. Any default will attract deduction (in Nigeria equivalents) at source before the release of statutory allocations.

- Private sector, industries that are export – oriented are expected to service their debt from their export earnings while others should utilize the Foreign Exchange Market facilities for debt servicing.

The government over the years adopted the under listed strategies and measures to deal with the debt problem. They include:

(i) Embargo on new Loans and Directives to State Government to restrict external borrowing to the barest minimum. The embargo was to check the escalation of total debt stock and minimize additional debt burden. However, these have not been particularly effective as indiscriminate quest for external loans have not been abated. Although rescheduling has conferred short term relief on debt service obligations, the debt over-hang has however hardly be abated as the debt stock has continued to increase significantly.

(ii)Limit on debt service payments: This requires setting aside portion of export earnings to allow for internal development.

(iii) Debt Restructuring: This involves the reduction in the burden of an existing debt through refinancing, rescheduling, buy back, issuance of collateralized bonds and the provision of new money.

The Federal Government in year 2001 established a semi – autonomous debt management office under the Presidency called the Debt Management Office (DMO).

The creation of the Debt Management Office (DMO) consolidated the debt management functions in a single agency, ensuring proper coordination of the country's debt, recording and management activities, including debt service forecast, debt service repayments, and advising on debt negotiations as well as new borrowings.

2.12. Nigerian External Debt Rescheduling and Restructuring

Debt Rescheduling involves the postponement, extension and re-ordering of the repayment of the existing debt. An agreement between creditors (government authorities and the commercial banks acting as a group) and the debtor to roll over payment due to the former from the latter over a certain period and under new terms and conditions falls under either debt rescheduling or refinancing. This involves the provision of new money to replace maturing debt. The four elements of loan restructuring are:

(i) Rescheduling of the principal of a part or all of an existing loan by postponing repayment i.e. rearranging maturities and grace periods involves the rescheduling of the interest payments. Official debt restructuring under Paris club involves the rescheduling of both official, medium term and long term debts falling due in a given period including those in arrears. The rescheduling terms under Paris Club are generally non-concessionary. Moreover, Paris Club is extremely reluctant to reschedule payments on short term debt with an initial maturity of one year or less.

(ii) Refinancing of an existing loan by raising fresh or complementary fund to meet existing obligation that is making provision for new credits with proceeds to be used to repay outstanding loans;

(iii) Restoring of trade –related bank credit lines; and

(iv)Persuading the financial community to restore inter-banks lines of credit to a certain minimum level.

2.13. Debt Relief in Nigeria

Ekperiware M.C. & Oladeji S.I (2012) defined debt relief as an agreement by a creditor or a country to accept reduced or postponed interest and redemption payments from the debtor. Nigeria's debt relief deal with the Paris Club is widely recognized in external debt literature and will be discussed here in detail. The Paris Club was formed in 1956 and its role is to provide help to the debt payment challenges faced by debtor nations. It comprises of 14 member nations (United Kingdom, France, Germany, Japan, Italy, United States of America, Belgium, Netherlands, Denmark, Austria, Spain, Switzerland, Russia and Finland).

Nigeria's first loan from the Paris Club of Creditor Nations was a US$13.1 million obtained from the Italian government in 1964 for the building of the Niger Dam. However the oil boom of 1971-1981 introduced the era of massive borrowings in Nigeria. Loans were acquired by various tiers of government as Nigeria embarked on major development and reconstruction projects in the wake of the civil war. The borrowing continued well into the civilian era, as the Federal Government embarked on the guaranteeing of many unviable loans taken by private banks, state governments and government parastatals. In 1982, when oil prices crashed, Nigeria was unable to pay off the loans it borrowed. This resulted in rising interest payments and mounting of trade arrears and their penalties.

After some time, a critical point was reached in 1986 when creditors refused to open new credit lines for imports to Nigeria. The government therefore approached the creditors for debt relief leading to the restructuring arrangements with the Paris Club in 1986, 1989, 1991 and 2000. However this did not stop the "leaps" and "jumps" in the external debt stock which led to Nigeria to stop paying its debts to the Paris Club altogether, after the Paris Club refused to substantially reduce Nigeria's debt. With the return to civilian rule in 1999 under the President Olusegun Obasanjo administration, Nigeria embarked on a relentless campaign for debt relief. The major concern was that Nigeria's spends more on debt service payments than it does on healthcare and education and as such with the high level of debt servicing could not achieve the millennium development goals.

The campaign efforts finally paid off in 2005 when the Paris Club group of creditors agreed to cancel 60% (US$18 billion) of the US$30.85 billion owed to it by Nigeria. This debt relief freed the nation from the yearly US$2.3 billion (N345 billion) debt service burden.

The agreement was however subject to a good track of record in implementing the IMF – supported stand and adherence to the follow-up medium term programme supported by the IMF.

With regard to top commercial debts the Federal Government engaged the services of financial and legal advisers to explore the possibility of restructuring the country's commercial debts based on an assessment of current financial market situation. The advisers proposed the exchange or swap of Nigeria's Par bond and promissory notes with new Global Bonds. However, in deference to advice from IMF on impact of commercial debt restricting on Nigeria negotiation with Paris club the launching of debt restructuring transaction was suspended by Nigeria. Recently, Nigeria resumed discussions with international Capital Market experts and wrote proposal towards restructuring her

external debt to take advantage of unfolding market developments which appear favourable to the states that hold the promissory notes owned by the Federal Government.

Nigeria received a debt-restructuring deal from the Paris Club and a $1 billion credit from the IMF, both contingents on economic reforms. (Adepoju et al 2007) . Nigeria pulled out of its IMF program in April 2002, after failing to meet spending and exchange rate targets, making it ineligible for additional debt forgiveness from the Paris Club. In 2003, the government began deregulating fuel prices, announced the privatization of the country's four oil refineries, and instituted the National Economic Empowerment Development Strategy (NEEDS), a domestically designed and run program modelled on the IMF's Poverty Reduction and Growth Facility for fiscal and monetary management. In November 2005, Abuja won Paris Club approval for a debt-relief deal that eliminated $18 billion of debt in exchange for $12 billion in payments - a total package worth $30 billion of Nigeria's total $37 billion external debt. The deal requires Nigeria to be subject to stringent IMF reviews. Based largely on increased oil exports and high global crude prices, GDP rose strongly in 2007 and 2008, and less strongly in 2009. (DMO, 2010)

2.14. Consequences of Nigeria's Mounting External Debt

Nigeria's high debt burden has grave consequences for the economy and the welfare of the people. The servicing of the external debt has severely encroached on resources available for socio-economic development and poverty alleviation. Although since 1986, Nigeria had taken a decision to limit debt service to no more than 30 percent of oil receipts; this has not brought much relief. In 1999, for example spending on health represented about 0.2% of GDP and 0.7 percent of GNP compared with 3.4 percent (US$1.5billion) annual budget spent on debt servicing during the same period. In 2000,

US$1.9 Billion was used for debt servicing translating to about 4 times Federal Government budgetary allocation to education and about 12 times the allocation to health while in 2001 debt service payment was US$2.13 billion which amounted to 6 times of the Federal Government's budgetary allocation to education and 17 times allocation to health for that year.

Between 1985 and 2001, Nigeria spent 'over US$ 32 billion on servicing external debt. Prior to the recent rescheduling arrangement with the Paris club, creditors annual debt service payment due were in the range of US$ 3.0 billion to US$ 3.5 billion. Debt service due in year 2000 was over US$ 3.1 or (14.5 percent of export earning) excluding arrears of US$ 19.6 billion owed to members of Paris club.

Actual servicing outlays in year 2000 was US$ 1.9 billion translating to about 4 times federal Government's budgeting to education and about 12 times the allocation to health. Yet these two sectors need substantial public expenditure to upgrade the level of facilities and services for any meaningful alleviation of poverty to take place. Also, the external debt overhang is adversely impacting on the Nigeria's economy in the inflow of foreign investments. Due to Nigeria's problem with servicing of her debts, Export credit Guarantee Agencies (ECGAS) suspended insurance cover for exports for goods and services as well as investment capital to the country. Consequently, the much needed inflow of foreign resources for investment stimulation, growth and employment has been hampered. Without credit cover, Nigerian importers are required to provide 100% cash covers for all orders and this therefore place them at a competitive disadvantage compared to their counterpart else where. The situation exacerbates the pains of external

burden as it blocks off the relief that would have been received through speedy economic recovery, growth and development.

In addition, external debt burden has resulted in repudiation risk because we are unable to obtain new loans due to little confidence placed on our ability to repay. The prospects are therefore dim for immediate resumption of net resource transfer from international sources to Nigeria through traditional means. The IMF severe conditionality for Nigeria is a case point. A severe reduction in net capital inflows and the imposition of a net capital outflow over an extended period have consequences on the prospects of economic development in Nigeria. In the face of dwindling oil revenues due to oil glut and fast falling prices but rising imports, balance of payment difficulties are bound to arise. i.e. external liabilities will rapidly increase, therefore raising the real resource cost of the original loans while leading to future foreign exchange crisis.

Lastly, the cost of import substitution will rise. This is because this sector contributes heavily to external debt service and to profits and dividends outflows. For instance, as a result of the Nigerian government servicing her debt before year 2000, there were severe austerity measures on Nigerians in an attempt to survive the external debt crisis.

2.15 Empirical Issues

From literature, the channels through which indebtedness works against economic growth and development are identified as: current stock of external debt as a ratio of GDP, which may stimulate economic growth and development, past debt accumulation, which captures the debt overhang and therefore deters economic growth and development, and debt service ratio to capture the crowding out effects. Attempt will be made in this section to review different studies through which the relationship between

external debt and Nigeria's economic growth will be analysed. Globally, there are divergent viewpoints among economic researchers regarding the impact of foreign loans on a country's economic growth. This study will consider various empirical studies, both ancient and recent and local and foreign.

Sulaiman and Azeez, (2012) carried out a study on the effect of external debt on the economic growth of Nigeria using annual data and econometric techniques of Ordinary least squares (OLS), Augmented Dickey-Fuller unit root test, Johansen Co-integration test and error correction method. The co-integration test shows long-run relationship amongst the variables and findings from the error correction model revealed that external debt has contribute positively to the growth of the Nigerian economy. In addition the study recommends that the Nigeria should ensure political and economic stability so as to ensure effective debt management

A number of researchers have examined the effect of external debt on economic growth since the beginning of the new millenium. Ayadi and Ayadi (2008) examined the impact of the huge external debt, with its servicing requirements on economic growth of the Nigerian and South African economies. The Neoclassical growth model which incorporates external debt, debt indicators, and some macroeconomic variables was employed and analyzed using both Ordinary Least Square (OLS) and Generalized Least Square (GLS) methods. Their finding revealed negative impact of debt and its servicing requirement on the economic growth of Nigeria and South Africa Adesola (2009) empirically investigated the effect of external debt service payment practices on the economic growth of Nigeria. Ordinary Least Square method of multiple regression was used to examine how debt payment to multilateral financial creditors, Paris Club Creditors, London Club Creditors, Promissory Notes holders and other

creditors relates to gross domestic product (GDP) and Gross Fixed Capital Formation (GFCF) using data from 1981 to 2004. The study provides evidence that debt payments to Paris Club Creditors and Promissory Notes holders are positively related to GDP and GFCF while debt payments to London Club Creditors and other creditors show a negative significant relationship to GDP and GFCF. Audu (2004) examined the impact of external debt on economic growth and public investments in Nigeria from 1970-2002. The empirical investigation was done using the Co-integration test and Error Correction Method. The study shows that debt servicing pressure in the country has had a significant adverse effect on the growth process and past debt accumulation negatively affect public investment.

In analyzing the consequences of debt on economic growth, (Pottilo, Poison &Ricci 2001) used a data set for 93 developing countries for the period 1968-1998 and found that the average impact of debt on economic growth becomes negative when debt is about 160-170 percent of export earnings or 35-40 percent of GDP. They further stressed that the marginal impact of debt starts becoming negative at about half of these values; as such high debt reduces economic growth, mainly by lowering the efficiency of investments rather than its volume.

Geiger(1990) used lag distributional models to examine the relationship between GNP growth rate and debt burden for 9 South American Countries over a period of 12 years(1974-1986) and found a statistically significant inverse relationship between debt burden and economic growth.

Furthermore, Chawdhury(2001) investigated the relationship between indebtedness and economic growth using Vector Autoregressive(VAR) Model. The findings show that

debt servicing as a percentage of either export earnings or GDP affects the growth rate of GDP per capita adversely. This effect is equally important and statistically significant for Heavily Indebted Poor Countries (HIPCs). On the contrary, Warner (1992) uses 13 developing countries for a period of 1960-1981 and 1982-1989, he could not find any conclusive evidence whether debt has any negative effect on economic growth or it may have depressed investments in those developing countries.

Empirical studies not related to Nigeria are also reviewed to show evidence from other countries. Choong, Lau, Liew, and Puah (2010) examined the effect of different types of debts on the economic growth in Malaysia during the period 1970 – 2006. Using Co-integration test, the findings suggest that all components of debts have a negative effect on long run economic growth. The Granger causality test reveals the existence of a short-run causality linkage between all debt measures and economic growth in the short-run. Abdelmawla and Mohammed (2005) investigated the impact of external debt on economic growth of Sudan from a period spanning 1978 – 2001. The study showed that export earnings have a significant positive impact while external debt and inflation had negative impact on Sudan's economic growth.

Karogol (2002) investigated both the short-run and long-run relationships between economic growth and external debt service for Turkey during 1956 – 1996. The study employed a standard production function model analyzed using multivariate co-integration techniques. The Vector Autoregression estimates showed that there exists one Co-integration equation. It also revealed that debt service is negatively related to economic growth in the long-run. The causality test showed uni-directional causality between debt service and economic growth.

Clements, Bhattacharya, and Nguyen (2003) examined the channels through which external debt affects growth in low income countries. Their results suggest that the substantial reduction in the stock of external debt projected for highly indebted poor countries (HIPC) would directly increase per capita income growth by about 1 percentage point per annum. Reductions in external debt service could also provide an indirect boost to growth through their effects on public investment.

Malik, Hayat, and Hayat (2010) explored the relationship between external debt and economic growth in Pakistan for the period between 1972 – 2005, using time series econometric technique. Their result shows that external debt is negatively and significantly related to economic growth. The evidence suggests that increase in external debt will lead to decline in economic growth.

Hameed, Ashraf & Chaudhary (2008), explored the dynamic effect of external debt servicing, capital stock and labour force on the economic growth of Pakistan for a period of 1970- 2003. They found an adverse effect of external debt servicing on labour and capital productivity which ultimately hampered economic growth. Butt(2009) investigated the causal relationship between short-term external debt and GDP growth rate for 27 Latin American Caribbean countries over a period of 1970-2003 and found an evidence of Granger causality in 13 countries. Adepoju et. al. (2007) in exploring time to time behaviour of donor agencies as an outcome of various bilateral and multilateral arrangements, they used time series data for Nigeria over a period from 1962-2006.Their findings indicated that accumulation of external debt hampered economic growth in Nigeria.

For the sake of this study, it is pertinent that some few recent and local empirical studies be considered on the relationship between external debt (management) and economic growth. Ogunmuyiwa(2011) used time series data from 1970-2007 examined whether external debt actually promote economic growth in developing countries using Nigeria as a case study. Using various econometric techniques such as Augmented Dickey Fuller(ADF)test, Granger causality test, Johansen cointegration test and Vector Error Correction Method, they revealed that causality does not exist between external debt and economic growth. (Safdari and Mehrizi, 2011) analyzed external debt and economic growth in Iran by observing the balance and long term relation of five variables (GDP, private investment, public investment, external debt and imports). Time series data covering the period 1974-2007 was used and the vector autoregressive model (VAR) technique of estimation was employed. Their findings revealed that external debt has a negative effect on GDP and private investment and pubic investment has a positive relationship with private investment. Ejigayehu (2013) also analyzed the effect of external debt on the economic growth of eight selected heavily indebted African countries (Benin, Ethiopia, Mali, Madagascar, Mozambique, Senegal, Tanzania and Uganda) through the debt overhang and debt crowding out effect with ratio of external debt to gross national income as a proxy for debt overhang and debt service export ratio as a proxy for debt crowding out. Panel data covering the period 1991-2010 was used. The empirical investigation was carried out on a cross-sectional regression model with tests for stationarity using Augmented Dickey Fuller tests, heteroskedasticity and ordinary regression. The concluding result from estimation showed that external debt affects economic growth through debt crowding out rather than debt overhang. In their study on external debt relief and economic growth in Nigeria, (Ekperiware and Oladeji, 2012) examined the structural break relationship between external

debt and economic growth in Nigeria. The study employed quarterly time series data involving external debt, external debt service and real GDP from 1980-2009. An empirical investigation was conducted using the chow test technique of estimation to determine the structural break effect of external debt on economic growth in Nigeria as a result of the 2005 Paris Club debt relief. The result of their findings revealed that the 2005 external debt relief caused a structural break effect in the relationship between external debt and economic growth. Based on these findings they concluded that the external debt relief made available resources for growth-enhancing projects.

Moreover, Ajao and Ogiemudia(2013) reviewed the effect of foreign debt management on sustainable economic development, they found that external debt stock contributes significantly and positively to Nigeria's GDP while debt servicing had a negative but insignificant impact on Nigeria's GDP.

2.16 Appraisal of Literature Review

The motive behind external debt is to boost economic growth and development of any nation. But as a result of future high debt service payments, external debt poses a serious threat to the economy of many nations. Many empirical studies have investigated the effect of external debt on economic growth as seen in the literature review above. Some ended up finding a negative impact between external debt and economic growth such as studies like Ayadi & Ayadi(2008), Adesola(2009), Choong, Lau, Liew & Puah(2010), Abdelmawla and Mohammed(2005) and Ejigayehu(2013) among others. Some other studies cited although few, establish a positive relationship between external debt and economic growth. Examples of such studies are Sulaiman and Azeez(2012) and Ajao and Ogiemudia(2013). On the other hand, some other studies do not find any significant relationship between economic growth and external debt. The findings of these studies

are mixed. Therefore, in these circumstances it is difficult to ascertain whether external debt promotes or retards economic growth and whether external debt management can help prevent debt burden in a country.

CHAPTER THREE

RESEARCH METHOD

3.1 Introduction

In this section, the research design, sources of data, the nature of econometric tests and an analysis of the methodology used are presented.

3.2 Research Design

The Research Design of a study represents the blueprint of the study. The Research Design defines the study type (descriptive, correlational, semi-experimental, experimental, review or meta-analytic)

The Research Design used in this study is the Ex post facto design. An Ex post facto design is a quasi-experimental study examining how an independent variable, prior to the study, affects a dependent variable. (Gorard 2013)

3.3 Sources of Data

This study made use of secondary sources of data. For this purpose, a 32 – year Time Series data were obtained and used for this Study from the Central Bank of Nigeria (CBN) statistical bulletin, Debt Management Office (DMO) Publications and the Word Bank and Financial Year Books.

3.4 Measurable variables

(i) Dependent variables

The dependent variable used in this study is Gross Domestic product (GDP) using Growth Rate of GDP as a proxy. The study measured the relationship between economic growth(that is Growth Rate of GDP) and External debt using vector autoregressive (VAR) model.

(ii) The independent variables are:

(a) External Debt Service Payments: External debt service payments is used to capture the effect of external debt management on Nigeria's economic growth

(b) External Debt Stock: External debt stock is used to capture the effect of external debt on Nigeria's economic growth.

(c) Exchange Rate: Exchange rate is used to capture the effect of net capital inflow on the economic growth of Nigeria.

3.5 Method of Data Analysis

This study investigated the relationship between external debt management and Nigeria's economic growth. It is important to ensure that time series variables included in the model are stationary, that is every variable has a constant mean and constant variance. This makes forecasting or prediction of future values possible. If variables are nonstationary, as expected in most macroeconomic data, we subject our estimated residual to OLS technique. To ascertain the stationarity status of the series variables, the unit root test is conducted. The series variables for this study were stationary after employing the unit root test, therefore Autoregressive Distributed Lag (ADL) model was then used in estimating the parameters of the model. Granger Causality test(Granger 1969) was used to ascertain the direction of causality between Growth Rate of GDP and External Debt Management in Nigeria. Additionally, other econometric tests such as cointegration test and Error Correction Mechanism(ECM) were performed to determine the existence of long-run relationship between the variables.

Since carrying out regression on non-stationary time series data will lead to spurious regression outcomes, the study employed the widely used Augmented Dickey-Fuller(ADF) test to ascertain the stationarity of the data.(Dickey and Fuller,1979). The Econometrics Views(E-views) package was employed to carry out the regression.

3.6 Model Specification

This study adopted the work of Hollis Chenery "Two gap" theory of Economic Growth and Development (Chenery & Strout,1956). Chenery sees foreign debt, that is external debt as a way of filling the savings gap and foreign exchange gap in order to achieve the target growth rate of the economy(Jhingan,2010).

Chenery's model of the two gaps are explained in terms of the national income accounting identities:

$E - Y = I - S = M - X = F$

Where:

E = National expenditure

Y = National output or income

I = Investment

S = Savings

F = Net capital inflow

(I – S) is the savings gap

(M – X) is the foreign exchange gap

The two gap model is an open economy Harrod-Domar model designed to show how a shortage of foreign exchange can reduce economic growth by constraining

both imports and savings. It assumes but does not explain how that shortage arises but does suggest that foreign aid or capital inflows can have a multiplier effect on growth and investment. Beginning with the national income identity:

$$Y=C+I+G+X-M \quad \text{----------(1)}$$

Capital inflows is defined as foreign savings $F=M-X$

At times, it will be convenient to write F as a share of GNP where :

$f = F/Y$ (lower case meaning that the variable is a share of Y)

Since $Y-C = S+T$

Where S and T are total domestic savings and taxes respectively, we can rewrite investment as : $S+(T-G) +F=I$ ----------(2)

Which simply states that the investment (I) that can translate into economic growth must be financed by domestic private savings (S), public savings (T-G) or foreign savings (capital inflows) F.

Therefore, for the sake of this study, the model that is employed is as follow:

$$GRRGDP=B_0 + B_1EXTDS +B_2EXTDBT + B_3EXCH + U$$

Where:

GRRDGP=Growth Rate of GDP

EXTDS=Debt Service Payment

EXTDBT=External Debt

EXCH=Exchange Rate

U = Stochastic Error Term B_1,B_2, B_3,=slope of the regression equation

$B_1< 0, B_2 > 0, B_3<0$

The model of this study bears similarity to that of Chenery in the sense that the growth rate of GDP in the model of this study represents the target growth rate of the economy or economic growth. External Debt represents the savings gap while foreign exchange represents the foreign exchange gap.

On the other hand, in contrast to Chenery's model, External Debt Service has been included in the model for this study to capture the effect of external debt management

From the model above, the a priori expectation is that there is negative relationship between GDP and debt service payment. There is a positive relationship between GDP and external debt and there is a negative relationship between GDP and exchange rate; GDP (Growth Rate of GDP) serving as a proxy for economic growth .

3.7 Stationarity or Unit Root Test

A time series, random or stochastic process is a collection of random variables ordered in time. Broadly speaking, a series is stationary if the mean and variance are constant over time and the value of the covariance between successive time periods depends only on the distance, gap or lag between successive time periods and not the actual time at which the covariance is computed. On the other hand, a series that not stationary is said to be non-stationary. To make a non stationary time series stationary, we take it through a number of differencing operations. The number of time it takes to make it stationary is termed the order of integration. This transformation is necessary to avoid spurious or nonsense regression results. This is why stationarity or unit root test was carried out on each of the variable of the model in this study to ascertain

whether our series is stationary or non-stationary. There are variety of ways of testing for stationary such as the graphical analysis, Autocorrelation function(ACF) and correlogram, unit root test, augmented dickey-fuller(ADF) test and the Phillips-Perron (PP) Unit Root Tests(Guajarati, 2003). There are many more unit root tests. This is because of the size and power of these tests. By size of a test we mean the level of significance (that is the probability of committing a type 1 error)and by power of a test we mean the probability of rejecting the null hypothesis when it is false.

In statistics, a unit root test tests whether a time series variable is non-stationarity using an autoregressive model. A well known test that is valid, in large sample in the Augmented Dickey-Fuller test. The test uses the existence of a unit root as the null hypothesis. For the purpose of clarity and simplicity, this study adopted the popular Augmented Dickey-Fuller test.

3.8 Augmented Dickey-Fuller Test (ADF)

An Augmented Dickey-Fuller Test is a test for a unit root in a time series sample. It is an Augmented version of Dickey-Fuller Test for a larger and more complicated set of time series models. The Augmented Dickey-Fuller Test (ADF) statistic, used in the test is a negative number. The more negative it is, the stronger the rejection of the hypothesis that there is a unit root at some level of confidence.

The testing procedure for the ADF is the same as for the Dickey-Fuller Test except for little variations.By including lags of the order p, the ADF formulation allows for higher-order autoregressive processes. This means that the lag length p has to be determined when applying the test. One possible test down the ages test from high orders

and examine the t-values on coefficients. An alternative approach is to examine information criteria such as the Akaike information criterion, Bayesian information criterion or the Hannan-Quinn information criterion.

Finally, the unit root test is then carried out under the null hypothesis $\gamma = 0$ against the alternative hypothesis of $\gamma < 0$. Once a value for the test statistic.

$$DF_{\gamma} = \frac{\gamma}{SE(\gamma)}$$

is computed it can be compared to the relevant critical value for the Dickey-Fuller test. If the test statistic is less that the (larger negative) critical value, then the null hypothesis of $\gamma = 0$ is rejected and no unit root is present.

3.9 Cointegration Test

Due to the importance of the cointegration test in the methodology of this study, some emphasis will be laid on it. After achieving the stationarity of the variables, we conducted the Johansen (1991) multivariate cointegration test to examine the presence or absence of co-integration relationship; this means that the variables share a common trend and long-run relationship as suggested by a priori knowledge. This test was then employed. We employ the cointegration test to determine whether the variables in our models are cointegrated or not.

The Johansen technique was used in this study because it enables a researcher to estimate dynamic error correction specification, which provides the estimate of both the short and long-run dynamics in the model. Additionally, the technique captures the

underlying times series properties of the data and it provides the estimates of all co-integrating relationships that may exist within a vector of non-stationary variables or a collection of stationary and non-stationary variables (Harris,1995). As a result of the presence or evidence of co-integration, then a Vector Error Correction (VEC) Model specification was made. A (VEC) Model is specified for use with non-stationary series that have been discovered to be co-integrated. The co-integrating model that is specified restricts the long run behaviour of the dependent variables to converge to its co-integrating relationships while creating allowance for short run adjustment dynamics.

3.10 Vector Autoregressive (VAR) Model

Where the variables have no long-run relationship, (i.e. are not co-integrated), though they are integrated of the same order, then the Vector Error Correction (VEC) model earlier mentioned could not be feasible. Consequently, the Granger causality test was conducted using Vector Autoregressive (VAR) model to determine the direction of causality at least in the short run.

The VAR co-integration test as typified by the Johansen method, is a superior test compared to the Eagle-Granger method, which is characterized by problems about the actual co-integrating relationships and inability to detect more than one relationships that may exist in a model (Harris 1995).

In describing Johansen methodology, two issues that have to be attended to are; first determining the appropriate order (k) of the VAR. Brooks (2002) argued that the Johansen test can be affected by the lag length employed in the VECM. It is thus crucial to attempt to select the lag length optimally. By optimally, it is meant that the chosen lag length should produce the number and form of co-integration relations that conform to

all the a priori knowledge associated with economic theory (Seddighi, Lawler and Katos, 2000). On the other hand, (Brooks) argued that economic theory will often have little to say on what an appropriate lag length is for a VAR and how long changes in the variables should take to work through the system. Brooks recommended the use of multivariate versions of the information criterion, which included the sequential modified Likelihood Ratio (LR), Akaike Information Criterion (AIC), Final Prediction Error (FPE), Schwarz Information Criterion (SIC) and the Hannan-Quine information criterion (HQ). However, from experience, these information criteria usually produce conflicting VAR order selections. In the light of these problems, the researcher used both the information criteria approach and the a priori knowledge from economic theory to select the appropriate order of the VAR.

The second issue is related to the choice of deterministic assumptions that the Johansen test requires in testing for cointegration. Various types of VARs can be estimated based on five deterministic trend assumptions. For example, with or without a constant and trend in the cointegrating terms and with or without a constant in the VAR equations. E-views 4 specifically provide the following deterministic trend assumptions. Case 1, assumes no deterministic trend in the data and no intercept or trend in the VAR and in the Co-integration Equation (CE); Case 2, assumes no deterministic trend in the data, but an intercept in the CE and no intercept in VAR; Case 3 assumes a linear deterministic trend in the data and an intercept in CE and VAR test: Case 4 allows for a linear deterministic trend in data, intercept and trend in CE and no trend in VAR; Case 5 allows for a quadratic deterministic trend in data, intercept and trend in CE and linear trend in VAR.As a guide, E-views 4 recommends the use of case 2: if none of the visual

plots of the series and unit root tests show the presence of a trend in the series. Case 3, if the series have stochastic trends, case 4 if some of the series are trend stationary, while Cases 1 and 5 are rarely used in practice (E-views 4 manual). Thus, the graphical analysis of the raw data and unit root tests, together with a priori knowledge from economic theory, should assist in selecting the deterministic trend assumption to be used in Johansen test for co-integration (Rank of 11).Once the appropriate VAR order (k) and the deterministic trend assumptions have been identified, the rank of the 11 matrix can then be tested.

3.11 Statistical (First Order) Tests

Under the statistical tests, we tested for the goodness of fit , that is the individual significance of each regressor using the t-test and finally the significance of the regression model using the f-test.

(i) **Goodness of fit test:** The study made use of coefficient of multiple determination R^2 to find how the variations in the explanatory variables affect the dependent variable.

(ii) **Student's t-test:** This test was used to test the significance of each explanatory variable. We made use of 5% level of significance with (n-k) degrees of freedom, and where necessary, the probability value was used as a rule of thumb.

(iii)**The f-test:** The f-test was used to test the overall significance of the regression model. In other words, it was used to test for the joint impact of the explanatory variables on the dependent variable.

3.12. Econometric (Second Order) Tests

Economic tests were used to test for the empirical verification of the model. These tests include testing for autocorrelation and normality.

(i)Autocorrelation: The Classical Linear Regression model assumes that autocorrelation does not exist among the disturbance terms. In order to find out whether the error terms are correlated in the regression model, we used the Durbin Watson statistics. This is used to test for the presence of series correlation. That is, the serial dependence of successive error terms in the regression.

(ii) Normality test: This test was conducted to find out if the error terms are normally distributed with zero mean and constant variance. This is one of the assumptions of the classical linear regression model.

CHAPTER FOUR

PRESENTATION AND ANALYSIS OF DATA AND DISCUSSION OF FINDINGS

4.1 Introduction

This section provides an in-depth description of the relationship between external depth variables (external Debt stock, external Debt service payments and exchange rates) and the Nigeria's economic growth represented by Growth Rate of GDP. The sample results for 32years is presented, analyzed and interpreted to show the relationship between the dependent variables and the independent variables. An attempt is also made to accept or reject the validity of the hypothesis stated earlier in this study and to make a generalized opinion on the relationship; hence, the section contains the presentation of data, data analysis, interpretation of results and findings.

4.2 Presentation of Data

Table 4.1 Variables

OBS	EXCH	EXTDBT	EXTDS	RGDP	GRRGDP
1980	0.5464	1866.8	621.4169	31546.8	138.68
1981	0.61	2331.2	1146.017	251052'3	391.05
1982	0.6729	8819.4	1400.532	246726.6	182.16
1983	0.7241	10577.7	1924.033	230380.8	280.97
1984	0.7649	14808.7	3294.675	227254.7	569.4
1985	0.8938	17300.6	4428.669	253013.3	909.63
1986	2.0206	41452.4	6808.513	257784.4	580.87
1987	4.0179	100789.1	4635.85	255997	196.69

1988	4.5367	133956.3	11825.82	275409.6	867.99
1989	7.3916	240393.7	16198.8	295090.6	1039.01
1990	8.0378	298614.4	30019.89	472648.7	2666.82
1991	9.9095	328453.8	28711.34	328644.5	2524.14
1992	17.2984	544264.1	47470.49	337288.6	3562.28
1993	22.0511	633144.4	33741.28	342540.5	1689.45
1994	21.8861	648813	40970.88	345228.5	2516.94
1995	21.8861	716865.6	70447.02	352646.2	3820.57
1996	21.8861	617320	177398.9	367218.1	13712.16
1997	21.8861	595931.9	105668.3	377830.8	5366.45
1998	21.8861	633017.O	112379.9	388468.1	5026.83
1999	92.6934	2577374	99197.25	393107.2	3649.89
2000	102.1052	3097384	203195.1	412332	11934.26
2001	111.9433	3176291	128720.7	431783.2	11426.99
2002	120.9702	3932885	118826.9	451785.7	5383
2003	129.3565	4478329	121158.4	495007.2	5696.78
2004	133.5004	4890270	122864.6	527576	5719.19
2005	132.147	2695072	114433.3	561931.4	49375.8
2006	128.65	451461.7	880373.1	595821.6	1680985
2007	125.8331	431079.9	103712.7	634251.1	30333.92
2008	188.5669	493180.2	76584.6	672202.6	7870.86
2009	148.8802	590441.1	103215.9	718977.3	11096.46
2010	150.298	689845.3	101076.6	718977.3	6756.82
2011	153.8616	896832.6	102221.9	834000.8	5568.56

2012	155.09	650000	114467.8	888893	8201.15

Source: Central Bank of Nigeria and Statistical Bulletins. Various issues

Where:

OBS is Observation

EXCH is Exchange rate

EXTDBT is External debt

EXTDS is External debt service payments

RGDP is Real gross domestic product

GRRGDP is Growth rate of real GDP

4.3 Issues, Trend and Nature of Nigeria's External Debt Profile

Nigeria's external indebtedness dates back to pre-independence period. However, the quantum of debt was small until 1978. (Udoka and Ogege, 2012). The debts incurred before 1978 were mainly long-term loans from multilateral and official sources such as the World Bank and the country's major trading partners. The debts were not much of a burden on the economy because the loans were obtained on soft terms. Moreover, the country had abundant revenue receipts from oil, especially during the oil boom of 1973-1976.

The recovery of the oil market from 1979, with oil prices rising to an all-time high of US$39 per barrel in 1980/1981 led to the notion that the economy was buoyant. Consequently, some deflationary measures put in place in 1978 were relaxed. A consumption pattern that favoured imported goods emerged which was aggravated and sustained by the import substitution industrializatioin that depended heavily on imported raw materials and machinery as well as overvalued exchange rate regime.

Many of the projects included in the Fourth National Development Plan(1981-1985) had high import content. The plan was based on an estimated foreign exchange inflow of US$30 billion per annum but, between 1981 and 1982, monthly import bills averaged US$24 billion per annum while monthly export receipts sank drastically to an average of US$1.5 billion(US$18 billion per annum). Besides indiscriminate and excessive importation, there were cases of over-invoicing of imports and under-invoicing of exports. Predictably, the euphoria of the oil boom was short-lived and when oil prices collapsed in 1982, the economy immediately suffered strains. The production and consumption patterns that emerged during the oil boom could not be sustained in the face of declining foreign exchange earnings. Rather than address the problem of declining foreign exchange revenue, both the Federal and State Governments embarked on massive external borrowings from the International Capital Market. Unfortunately, that was also the period of excess loanable funds in the Western World. The international commercial banks with idle 'petrol dollars' in their vaults went out granting loans to unsuspecting developing countries in the guise of assisting their economic development, a phenomenon usually referred to as recycling of petro-dollars. Thus, pressure soon mounted on the various sectors of the Nigerian economy resulting in huge imbalances in government finance, low foreign reserves, deficit in balance of payments and accumulation of trade arrears in respect of insured and uninsured trade deficits. This led Nigeria to the refinancing agreement of 1983 in respect of letters of credit amounting to US$2.1 billion. Trade debts contracted through open account and bills, which were outstanding as at 31st December 1983 were financed through the issuance of promissory notes. As trade arrears

continued to mount, the country could not also service her external debts. (Sulaiman and Azeez 2012)

A critical point was reached in 1986 when creditors refused to open new credit lines for import to Nigeria. Therefore, the government approached the creditors for debt relief leading to the restructuring agreement with the Paris Club in 1986, 1989, 1991 and 2000. The arrangement provided for the capitalization and restructuring of accumulated debt arrears, their penalties late and moratorium interests as well as maturities within the consolidated period. The debt stock therefore increased drastically, even when no new loans were contracted. From this period, the debt stock of Nigeria continually rose unabated. By the end of 2005, the debt stock has risen to about US$30 billion. (Abdullahi et al 2013)

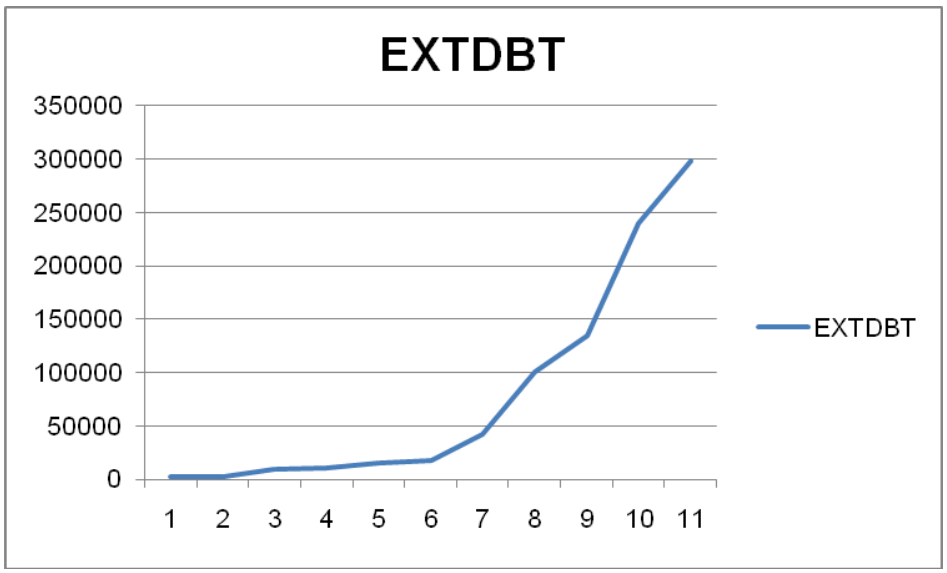

Figure 4.1: Nigeria's External Debt Trend 1980 – 1990

The trend of Nigeria's external debt in the 1980s as seen in the graph above skyrocketed. The trend was astronomical due to drastic decline of crude oil prices and revenue coupled with indiscriminate importation and corruption.

In April 2005, Nigeria got a debt relief package form the Paris Club and in April 2006, Nigeria paid off the debt owed to the Club. Since then, the external debt stock of the country has been kept at relatively low level. Thanks to the proactive measures adopted by the Debt Management Office (DMO) , which was established in October, 2000.

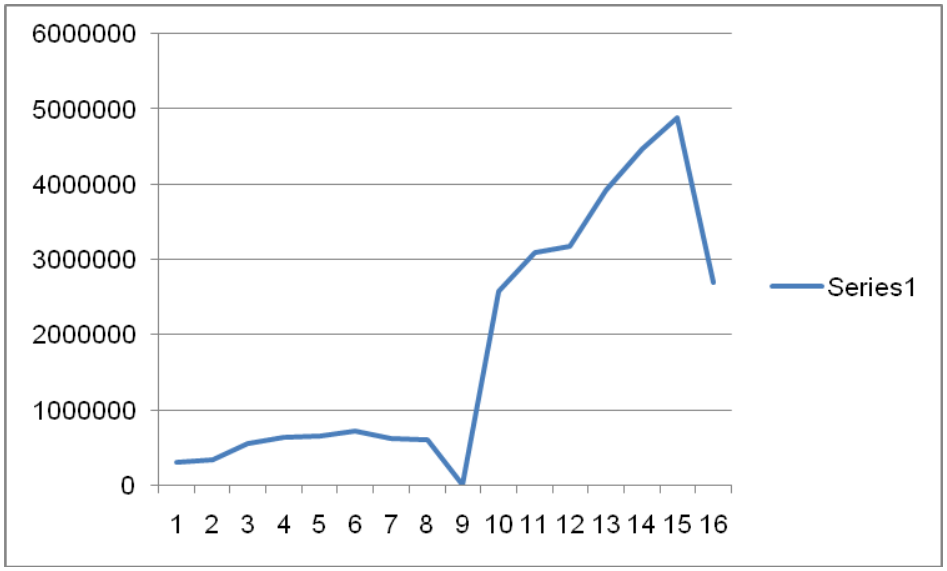

Figure 4.2 : Nigeria's External Debt Trend 1991-2005

According to the Coordinating Minister of the economy and Minister of Finance, Dr Ngozi Okonjo- Iweala, Nigeria's external debt is as low as $6.67 billion(about N1.035 trillion) that is, about 3 percent of Gross Domestic Product as at January 2014

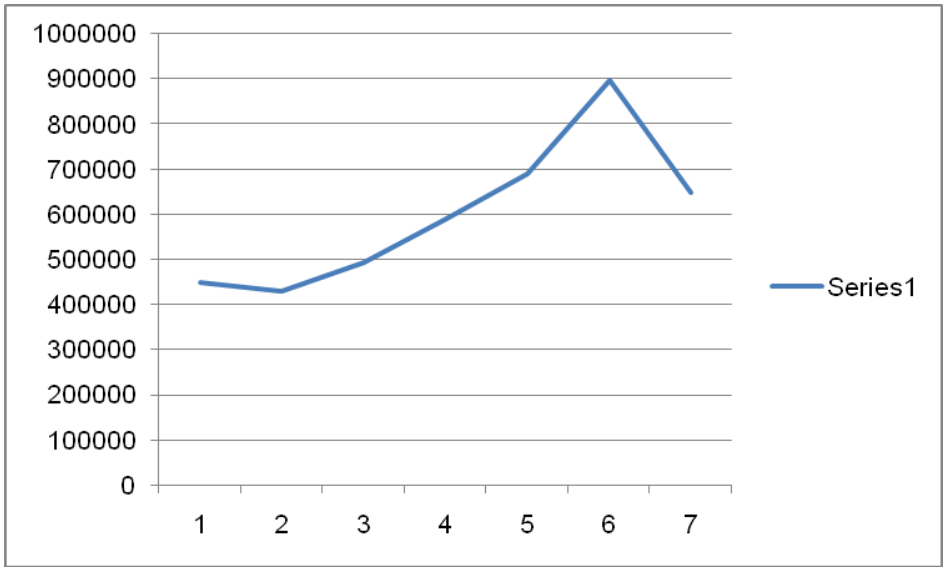

Figure 4.3: Nigeria's External Debt Trend 2006 – 2012

Figures 2.2 and 2.3 above show that Nigeria' external debt trend is rising again. This is not a good omen for the country.

4.4 Analysis of Data

Unit root test

In order to test for the stationary of variables used in the study, unit root testing of all variables was carried out using the Augmented Dickey-Fuller (ADF) method Philip-Perron (PP) test. These tests **(ADF &PP)** are widely considered as the most reliable test of stationarity for economic time series. The unit root test was carried out using Eviews 3.1 econometric software and the following results were obtained.

Table 4.2: Summary of Unit Root Test Using ADF

ADF			
Variables	**Levels**	**1st Diff.**	**5%**
GRRGDP	- 3.8529	- 6.2707	1(0) 1(1)

EXTDBT	- 2.2840	- 3.8370	1(1)
EXTDS	- 3.1278	- 6.4045	1(0) 1(1)
EXCH	- 0.1133	- 4.3076	1(1)

Note: 5% critical value of ADF & PP = 2.96

Source: Author's computation

The above result shows that the dependent variable **(GRRGDP)** is stationary at levels and first difference. One of the explanatory variables **(EXTDS)** is stationary at levels and first difference while the others **(EXTDBT and EXCH)** are non-stationary at levels but stationary at first difference. This conclusion is reached given the 5% critical value of 2.96 for ADF statistics.

Test for Cointegration

Note that all the variables (GRRGDP, EXTDS, EXTDBT and EXCH) are stationary at 1st difference and GRRGDP & EXTDS are also stationary at levels. Since they are all stationary at 1st difference and non-stationary at second difference, Johansen cointegration test was used for the analysis to ascertain the long-run relationship between the dependent variable(GRRGDP) and independent variables (EXTDBT, EXCH and EXTDS).Below is the result of the Johansen Cointegration test.

Table 4.3: Summary of Johansen Cointegration Test

Sample 1980-2012

Included Observations: 30

Test Assumption: Linear Deterministic trend in the data

Series: GRRGDP, EXTDBT, EXTDS, EXCH

Lags interval: 1 to 2

Null Hypothesis	Alternate hypothesis	Eigen Value	Likelihood Ratio	5% Critical Value	1 % Critical Value
R=0	**R=1**	0.913295	104.5627	47.21	54.46
R=1	**R=2**	0.503186	31.20541	29.68	35.65
R=1	**R=3**	0.264890	10.21925	15.41	20.04
R=1	**R=4**	0.032371	0.987197	3.76	6.65

LR test indicate 2 cointegrating equations at 5% significance level

Source: Author's computation

The cointegration result above shows that there are 2 cointegrating equations. The LR of 104.5627 is greater than the 5% and 1% critical value of 47.21 and 54.46 respectively and the LR of 31.20541 is greater than 5% value of 29.68. This implies that we reject the null hypothesis of no cointegration amongst the variables and accept the alternative hypothesis of cointegration and the existence of a long-run relationship between the dependent variable and explanatory variables. One major and recent study that have also found the existence of a long run relationship between external debt and economic growth is that of Sulaiman and Azeez (2012)

Error Correction Mechanism

Having ascertained the levels of stationarity and cointegration of the variables, the error correction mechanism which reconciles the short run and long run disequilibrium becomes a necessity. Table 4.4 shows the summary of VECM result.

Sample (adjusted): 1983-2012.

Included observations: 29 after adjusting end points

Table 4.4 Dependent Variable: GRRGDP

Variables	Coefficients	Standard Error	t-test
C	-86413.52	14424.7	-5.99066
D{EXTDBT(-1)}	-0.682168	0.02796	-24.4015
D{EXTBDT(-2)}	-0.201414	0.04987	-4.03865
D{EXTDBS(-1)}	-0.380671	-0.42677	-0.89198
D{EXTDBS(-2)}	-0.600621	0.38309	-4.17817
D{EXCH(-1)}	16143.02	1138.67	14.1771
D{EXCH(-2)}	5789.034	928.190	6.23690
ECM(-1)	-3.733024	0.22203	-16.8128

$\mathbf{R}^2$ =0.986870, R^2 adjusted=0.980651, F-statistic = 158.6800

Source: Author's computation

4.5 Discussion of the Findings

From the error correction result shown above, the overall fit of each of the variables is good since R^2 =0.986870. This implies 98% of the systematic variation in the rate of economic growth (as proxied by the growth rate of the GDP) is explained by the regressors (EXTDBT,EXTDS and EXCH). The F-statistics of the error correction model is 158.68 and is highly significant; easily passing the significance test at the 5% level. This outcome shows that the hypothesis of a linear relationship between the growth rate of real GDP and the regressors cannot be rejected at the 5% confidence level. The

coefficient of the Error Correction Mechanism (ECM) is -3.733024 and its t-value is -16.8128. This t-statistics is highly significant, effortlessly passing the significant test at the 1% confidence level. The fact that the coefficient of the ECM is largely negative and highly significant means that the error correction mechanism will work properly to move the growth rate of real GDP towards equilibrium whenever the actual level deviates from the long-run equilibrium. The value of the coefficient portrays good dynamics since the required adjustment to a new equilibrium is completed in a given year.

The coefficient of the first lag of EXTDBT is -0.68216 and is negative. This implies that a negative relationship exist between growth rate of real GDP and external debt. Therefore, we accept the null hypothesis of no positive relationship existing between external debt and economic growth. The coefficient of the second lag of EXTDBT is also negative, which buttress the negative relationship. The t-value of the first lag of EXTDBT of 24.4015 is statistically significant at 5% level. This means that external debt is statistically significant in explaining growth rate of the economy. A 1% rise in external debt stock will decrease the growth rate of the economy by 0.68%. Therefore, we accept the null hypothesis that external debt has not made any positive impact on economic growth in Nigeria. On the other hand, external debt deters economic growth in Nigeria. Other studies which have found the existence of a negative relationship between external debt and economic growth are Ayadi & Ayadi (2008), Adesola(2009), Choong, Lau, Liew & Puah(2010) and Butt(2009) among others

The t-value of the first lag of EXTDS (-0.89198) is not statistically significant in explaining growth rate of the economy at 5% level. That of the second lag (-4.17817) is statistically significant in explaining growth rate of the economy.

The coefficients of the first and second lags of EXTDS are negative (-0.380671 and -1.600621 respectively). This conforms to a priori expectation that debt servicing affects economic growth negatively. A 1% rise in the debt servicing will reduce economic growth rate by 1.6%. This has a serious impact on growth rate of economy. The implication of the above is that debt service payment deters economic growth. Therefore, we reject the null hypothesis and accept the alternative hypothesis that debt service payments deter economic growth. This finding is in line with the findings of some previous studies such as that of Ayadi & Ayadi (2008), Chawdhury(2001), Hameed et al (2008) and Ajao & Ogiemudia(2013)

Finally, The t-values of the first lag and second lag of exchange rate are 6.23690 and -16.8128 respectively. This implies that exchange rate is statistically significant in explaining the growth rate of GRRGDP. The signs of the coefficients of exchange rate are positive, implying that depreciation of the Naira results in economy growth. This finding aligns with the studies of Ojo & Awodele (2013) and Sulaiman & Azeez(2012) which also found the existence of a positive relationship between exchange rate and economic growth.

Table 4.5 Pairwise Granger Causality Tests

Sample: 1980-2012

Lags: 2

Null Hypothesis	Observations	F-statistics	Probability
EXTDBT does not Granger cause GRRGDP	31	31.2654	1.2E-07
GRRGDP does not Granger cause EXTDBT	31	0.17359	0.17359

Source: Author's computation

The Granger Causality Test above shows that External Debt (EXTDBT) Granger Cause the Growth Rate of the Economy (GRRGDP). This is deduced from the F-statistics of 31.2654. On the other hand, the F-statistics of 0.17359 shows that GRRGDP does not Granger Cause External Debt (EXTDBT). The probability value of 1.2E-07 depicts super significance.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1. Introduction

This chapter covers the summary of findings, conclusion and recommendations. The research has been on the impact of external debt management on Nigeria's economic growth. The study covered the period between 1980 and 2012. The study is made up of five chapters and the Ordinary Lest Square (OLS) estimation technique was employed to establish a relationship between external debt management and Nigeria's economic growth. The study also employed the Johansen cointegration test, Error Correction Method and Granger Causality test among others.

5.2. Summary of the Findings

This research empirically investigated the impact of external debt management and Nigeria's economic growth between the period of 1980 and 2012. The following are the major findings of the study.

(i) External debt has no significant impact on the level of economic growth in Nigeria. An increase in external debt in Nigeria by 1 percent will decrease the growth rate of the economy or economic growth by only 0.68 percent. The low elasticity of economic growth to external debt revealed that external debt has little influence on economic growth in Nigeria. External debt is therefore not an important determinant of economic growth in Nigeria although it retards economic growth.

(ii) External debt service payments have a negative relationship with economic growth in Nigeria. This conforms to a priori expectation that debt service payments affect economic growth negatively.

A 1 percent rise in debt service payments will reduce economic growth by 1.6 percent. This implies that debt servicing deters economic growth in Nigeria.

(iii) Exchange rate is statistically significant in explaining the growth rate of Real GDP in Nigeria. The signs of the coefficients of exchange rate are positive, implying that depreciation of the Naira results in economic growth. A 1 percent increase in the exchange rate will lead to a decrease in the growth rate of Real GDP by 1.6 percent. Conversely, a 1percent decrease in exchange rate will increase the growth rate of GDP by 1.6 percent.

(iv) The high coefficient of multiple determination in the over-parameterized model, that is 98% led to the overwhelming rejection of the null hypothesis which states that external debt management does not have a significant impact on Nigeria's economic growth. Also, the F-statistics shows that the time to time behaviour of external debt management, debt servicing and exchange rate, all put together, caused a significant change in growth rate of Real GDP or Nigeria's economic growth.

5.3. Conclusion

The major objective of this study is to examine the effect of external debt management on Nigeria's economic growth. The result of the study shows that whereas external debt is not an important determinant of economic growth in Nigeria, it retards

economic growth. Like External debt, external debt service payments also have a detrimental impact on the level of economic growth in Nigeria.

Moreover, the result further revealed that, unlike external debt and debt service payments, increase in the exchange rate, which is depreciation of the Naira promotes economic growth in Nigeria. Finally, the co-integration test shows the existence of long-run equilibrium relationship among the variables of the model

External debt plays a crucial role in any economy. This is why external debt is indispensable to most countries, especially the developing ones. External debt being insignificant to economic growth in Nigeria according to the study could be as a result of mismanagement, corruption and other institutional factors. The optimal utilization of eternal debt resources by the government would avoid debt overhang and crowding out of investments.

5.4. Policy Recommendations

Based on the findings of the study, the following recommendations are made:

(i). External debt sourcing and deficit financing by the Government should be discouraged in Nigeria since external debt is not an important determinant of economic growth. According to the study, external debt retards economic growth through its negative relationship with economic growth

(ii) If external debt must be sourced since this seems indispensable to developing countries like Nigeria, proactive debt management strategies should be put in place so that debt service payments do not accumulate to the extent of retarding economic growth.

(iii) Policymakers should be guided in the depreciation of the Naira because it has diverse economic implications

5.5. Contributions to Knowledge

The study has contributed to knowledge in the following ways:

(i).The study has specifically revealed that Nigeria's problem as regard the issue of external debt is the accumulation of debt service payments which stems from ineffective debt management strategies and not external debt sourcing. The study has revealed that recent and past debt management strategies and measures have been ineffective

(ii) The study revealed that depreciation of the Naira may promote economic growth in Nigeria with its diverse economic implications

(iii) Finally, this study is one of the very few studies which included exchange rate as a variable in external debt and economic growth studies. Of all the very many studies researched, only three were found to include exchange rate in the model of study. They are Mbire B. & Atingi M.(1997), Ojo & Awodele(2012) and Sulaiman & Azeez(2013).

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