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GROWING PUBLIC DEBTS AND ECONOMIC DEVELOPMENT IN NIGERIA.

¹Asinya, Francis Anoka, ¹Nelson Takon, ²Iyamba Godswill Francis.

¹ Department of Economics University of Cross River State

²Department of Business Administration University of Cross River State Calabar (Nigeria)

Correspondences: frankanoka@yahoo.com

Abstract

The paper set to examine the ever-growing public debts profile and economic growth in Nigeria for the period spanning 1986 – 2022. Time series data on domestic and external debts was used to capture the overall debt obligation. An empirical investigation was conducted using time series data on Gross Domestic Product (GDP), domestic and external debts profile from 1986 – 2022. Furthermore, Ordinary Least Squares econometric technique was used. Before estimation, the stationarity of the variables was examined, co-integration technique was applied to test for the order of integration, while Augmented Dickey-fuller (ADF) unit root test was used to determine the stationarity of the data and granger causality test. The result shows that, domestic debt has a negative relationship with GDP while external debt has a positive and significant relationship with GDP. The study recommends, therefore, that external debt should be channeled and utilized for the purpose for which they were acquired.

Keywords: Debt, Debt Servicing, External Debt, Domestic Debt, Economic growth and Development.

1.0 Introduction

Government borrowing is a loan taken by the government that is included in the Budget document as capital receipt. It's essentially the total amount of money borrowed by the federal government to pay for public services and benefits. The government announces an annual borrowing program in the Budget when tax and non-tax revenue is insufficient to fund the government's spending program (Economic times, 2020). Government borrowing becomes necessary, according to Abdulkarim and Saidatulakmal (2021), when government revenue sources are insufficient to finance growing government expenditures. Borrowing at a reasonable rate to fund public and infrastructure development is the key to accelerating economic growth and development. However, excessive borrowing without proper investment planning can result in a high debt burden and interest payments, which can have a number of negative consequences for the economy. Most governments have massive outstanding debts as a result of this process over the years (Joy & Panda, 2020).

Nigeria has struggled with a higher debt service to revenue ratio since the recession in 2016, as revenues have fallen in direct correlation with the drop in oil prices. In 2019, Nigeria's government spent 2.45 trillion Naira on debt service, out of total revenue of N4.1 trillion, for debt service to revenue ratio of 59.6 percent. The rising cost of Nigeria's debt profile breached a new milestone with the country's debt service as a percentage of revenue rising to 83 percent in 2020. This suggests that 83 percent of the revenue generated in 2020 was used to meet debt

service obligations and this is worrisome. In 2020, the government spent N1.76 trillion to service domestic debt, compared to a budget of N1.87 trillion. A total of N553 billion was spent on foreign debts, compared to a target budget of N805.47 billion. Lower interest rates on foreign borrowing, as well as very limited borrowing from the foreign debt market during the year, are likely to have contributed to the decrease. Instead of the budgeted N272.9 billion, the government only contributed N4.58 billion to the sinking fund. The sinking fund is required to set aside funds that will be used to pay down other loans in the future, such as bonds. The government's constant borrowing from the domestic market crowd-out private businesses in need of credit from obtaining financing for expansion and growth (Ogunjimi, 2019).

According to Izuaka (2021), Nigeria's debt situation worsen in 2022, with the government borrowing N5.012 trillion to finance a budget deficit of N6.3 trillion and a budgeted total budget of N16.39 trillion. Complicating the country's debt situation is becoming increasingly unmanageable. While the government claims that its debt-to-GDP ratio is within a safe range of 23 per cent, it has spent the majority of its earnings to service mounting debt for years. In the first five months of 2021, the government spent N1.8 trillion on debt servicing, accounting for nearly 98 percent of total revenue generated during the same period. As of March 31, the country's total debt was N33.11 trillion Izuaka (2021). When a country spends a large portion of its revenue servicing massive debts, it leaves little money to fund critical infrastructure, which has a negative

impact on growth and development. A nation's road to economic growth and development is hampered by an increasing domestic debt profile. The cost of servicing the debt may rise beyond the economy's ability to cope, posing a threat to the country's ability to meet its fiscal and monetary policy goals (Soludo, 2003). Economic development is the process of creating wealth for the benefit of the community. It's more than a job program; it's an investment in growing your economy and improving the prosperity and quality of life for everyone in your community (California Association for Local Economic Development (2021). Furthermore, a growing debt burden may limit the government's ability to invest more productively in infrastructure, education, and public health (Soludo, 2003). Nigeria is currently one of the most heavily indebted countries in Sub-Saharan Africa, with a slowed GDP growth rate, slowed export growth, rapidly dwindling income per capita, and rising poverty levels. The majority of these countries, including Nigeria, have been caught in a cycle of hasty and distress borrowing that they are unable to service. It was investigated that their primary exports world prices are deteriorating, necessitating more borrowing (Ogunjimi, 2019). As a result, the purpose of this research is to look into the impact of growing public debts on Nigeria's economic development in the twenty-first century. Borrowing at a reasonable rate to fund public and infrastructure development is the key to accelerating economic growth and development. However, excessive borrowing without proper investment planning can result in a high debt burden and interest payments, which can have a

number of negative consequences for the economy.

2.0 Theoretical framework and literature review

2.1 The classical theory

According to the classical theory fiscal deficit financed by debt is largely offset by the crowding out effect of deficit financing on private sector investment, and by extension, lowers the level of economic growth. In addition to the crowding out effect on private investment, the society will have to bear the burden of increase in public debt as a result of debt financed expansion in government expenditure. This opposition to deficit financing on the part of the classical economists was based on the assumption of full employment. Obviously, if there is already full employment, any extra expenditure financed by debt or by created money is bound to create inflationary rise in prices. In sum, according to classical economic theory, excessive deficit financing can lead to poor economic performance.

2.2 David Ricardo theory of public debt

This theory of public debt was propounded by David Ricardo in (1819). In his Principles, Ricardo developed the theory of public debts by stating that the ordinary and extraordinary spending of government were mainly payments made to sustain unproductive laborers. Therefore, any saving from the government expenses would be included in the income if not to the capital of the contributors. Ricardo in a letter written to McCulloch in 1816 believed that public expenditure was wasteful venture

undertaken by the state. Ricardo's theory of public debts was then, based on the fact that the primary burden to the community was derived from the wasteful nature of public expenditure itself rather than from the methods adopted to finance such expenditure (Precious, 2015). The theory postulated that financing public expenditure should be focused on drawing the funds from the liquid resources of the community. This is because to focus on the economy, does not make any significant difference whether the funds were raised by loans or taxes. Accordingly, Ricardo argument about payments of interest on public debt deals with a transfer of wealth from one pocket to another within the society. Thus, when countries borrow, it is uncertain whether the loan would be used productively or unproductively. If the loan is used productively, it leads to growth, but it is used unproductively, it deters economic growth in the economy (Okoye, Modebe & Evbuomwan, 2013). In conclusion, this theory is relevant to this study as it would help to determine whether actually, the government expenditures in Nigeria have over time been used productively or unproductively according to the theory.

2.3 Keynesian theory of public debt

The Keynesian theory of public debt was developed partly as a result of the economic crisis created by the great depression of the 1930s in the 19th century. In the theory, constant unbalanced budgets and rapid increase in public debt affect the nations' financial stability. It conceived that huge public debt is a national asset rather than a liability and hence, continuous deficit spending is very essential to the economic

growth of nations because, it leads to full employment (Precious, 2015).

The Keynesian theory postulated that the economy tends to equilibrium at full employment, which was an attack on the classical principles of budgeting and public finance. By assumption, Keynes assume that if there were unemployed resources that the private sector could not employ, these resources can be put to use by adopting an unbalanced budget. Accordingly, Keynes upheld that a rise in public debt via the multiple effects would raise the National Income. It linked public borrowing with deficit financing and urge the government to borrow for all purposes in order to increase effective demand in the economy, which would, in turn, result in increased employment and output. Lerner (1955), opined that duly importance should be given to certain advantage of public borrowing while considering burden thesis of public debt. The economic effect of public debt is assessed in the consideration of the nature of the expenditure for which debt is incurred and in terms of the income generating potentialities. In modern theory, duly importance was given to the net burden of public debt. Furthermore, the theory postulated that additional flow of income generated by increased debt to finance expenditure leads the payment of taxes to serve the debt. During the period of unemployment, public debt increase contributes to current capital for the nation. More so, the theory stated that public borrowing promotes the development of more and more institutionalized sources of savings like stock, capital market, insurance companies, and Banks.

2.4 Theory of economic development growth theory

The idea that economic development should naturally result in the erosion of dualism (in labor and other markets) establishes a link from classical development economics back to growth theory as pioneered by Abramovitz and Solow. This, in brief, seeks to break economic growth into separable components, the most important being (a) growth in the supply of labor and capital, (b) improvements in the efficiency with which they are allocated between sectors in

3.0 Methodology

The data for the variables of interests were collected from the Central Bank of Nigeria Statistical Bulletin (CBN), International Financial Statistics (IFS), Government Finance Statistics (GFS) and the Balance of Payment Statistics (BOPS) of the International Monetary Fund as well as the World Bank Development Indicators and the African Development Bank Indicators, Hence, data were collected for 36 years (1986-2022) to permit a sound and balance analysis.

3.1 Model specification

The model states that Economic development (GDP) is a function of domestic debts (DD) and foreign debts (FD). The functional form can be written as follows:

$$\Delta GDP = f(\Delta LDD, \Delta LFD) \quad \text{----- (1)}$$

Equation (1) above can be specified further as:

$$\Delta GDP = \beta_0 + \beta_1 \Delta LDD + \beta_2 \Delta LFD + \mu_1 \quad (2)$$

Where; Where: $\beta_0 > 0, \beta_1 > 0, \beta_2 > 0,$

f = Functional Relationship

ΔGDP = Log of Gross Domestic Product

ΔLDD = Log of Domestic debts

ΔLFD = Log of Foreign debts

β_0 = Constant term

β_1 and β_4 = Parameters to be estimated

μ_1 = Stochastic error term

The error term (μ_1) is a random variable that has well defined Probabilistic properties. It is assumed to capture other exogenous factors that are capable of influencing GDP.

This study adopted the Ordinary Least Squares (OLS) econometric technique. Before estimation, the stationarity of the variables was examined. Due to mixed order of integration of the variable, a co-integration technique was used to test for the order of integration and the Augmented Dickey-Fuller (ADF) unit root test to determine the stationarity properties of the data to avoid the problem of spurious regression. We assumed a linear relationship between the dependent variable and the independent variables in the specified equation. This was done to avoid the generation of spurious results.

4.0 Discussion of results

This section presents the data used upon which the analysis is based. The data collected are data on Economic growth as measured by the real Gross Domestic Product (GDP), internal debt and external debt. The sample consists of 36 observations collected from Central Bank of Nigeria Statistical Bulletin

Table 4.1 ADF test result

Variable	ADF Test Statistic	Test Value at 5%	Remark
RGDP	-4.097824	-3.568379	Stationary
DD	-4.288191	-3.557759	Stationary
ED	-5.626374	-1.952066	Stationary

Source: Statistical Output from E-views 10.0

Table 4.2 presents only the unit root result of the variables at first difference. As can be seen from the ADF result, the variables are all stationary at first difference, hence the result of the regression output would be deemed to be reliable in statistical perspective.

Table 4.2 ARDF bounds test

T. Test	5% critical value bound		Remark
F. Statistic	Upper bound	Lower bound	
6.797005	3.87	3.1	Null hypothesis Rejected

Source: Statistical Output from E-views 10.0

The bounds testing technique was used to evaluate the long-run relationship between public debts an economic growth in Nigeria. This assertion is deduced on the basis that the Statistic of 6.79 is higher than the upper and lower critical bound

values of 3.87 and 3.1 respectively. An implication that economic growth, domestic debt and external debt are significantly related in the long-run at a significant value of 5%.

Table 4.3 ARDL short-run relationship

Variable	Coefficient	Std. Error	t-statistic	Prob
RGDP(-1)	1.325445	0.176939	7.490954	0.0000
RGDP(-2)	-0.360680	0.346787	-1.040061	0.3107
RGDP(-3)	-0.020960	0.372475	-0.056273	0.9557
RGDP(-4)	0.370654	0.241874	1.532427	0.1411
DD	-1.066497	0.581879	-1.832850	0.0818
DD(-1)	0.768182	0.870053	0.882914	0.3878
DD(-2)	-1.083628	0.910760	-1.189806	0.2481
DD(-3)	1.904836	1.015361	1.876019	0.0753
DD(-4)	-2.421713	0.789419	-3.067714	0.0061
ED	0.400966	0.129287	3.101378	0.0056
C	-5116.386	1374.488	-3.722395	0.0013
Adjusted R-squared	0.998264	Durbin-Watson stat Prob(F-statistic)		1.7536
F-static	1726.157			0.0000

Source: Statistical Output from E-views 10.0

Short-run relationship in Table 3 depicts that domestic debt has insignificant negative relationship with economic growth in Nigeria, while external debt has positive significant relationship with economic growth. Holding domestic debt and external debt constant, economic growth would be valued at -5,116.38. A

percentage rise in domestic debt significantly leads to reduction in economic growth by a factor of 1.06. A unit increase in external debt has the tendency to rising economic growth by a 40.09%. Put differently, the higher the external debt the higher the gross domestic product of Nigeria.

Table 4.4 Granger Causality Test

Null Hypothesis	Obs	F-Statistic	Prob.	Remarks
DD does not Granger cause RGDP		27.8249	0.0000	Causality
RGDO does not Granger cause DD	34	8.80673	0.0057	Causality
ED does not Granger cause RGDP		1.46826	0.2349	No Causality
RGDP does not Granger cause ED	34	2.75836	0.1068	No Causality

Source: Statistical Output from E-views 10.0

The adjusted R-square reveals that 99.82% changes economic growth was attributable to the joint fluctuation in domestic and external debt. This is supported by the p-value (0.0000) of the f-statistic (1726.157) which is significant at a level of 5%. The Durbin Watson value of 1.75 is within the acceptable range of no autocorrelation in the estimated model. With respect to the effect of domestic debt and external debt on economic growth, the granger causality test in Table 4.4 reveals that there is a bidirectional causal relationship between domestic debt and economic growth in Nigeria as causality runs in both directions at a significant level of 5%. This is to say that domestic debt has significant effect on economic growth on one hand, while on the other hand, domestic debt is significantly affected by economic growth. On the contrary, external debt has no significant effect on

economic growth in Nigeria because causality does not flow in either direction that is, from external debt to economic growth or from economic growth to external debt.

5. Conclusion and recommendations

Arguably, Nigeria’s debt crisis can be attributed to both exogenous and endogenous factors: such as the nature of the economy, economic policies, dependency on oil, dwindling foreign exchange receipts, etc. Besides, conscious efforts must be made to secure total exit from all forms of commercial debts that exposes the country to another regime of debt overkill. Nigeria must also diversify the economy and develop more export products outside crude oil. Though external debt would not be considered as an evil fiscal policy arrangement of the government, external

loans contracted should be properly and efficiently channeled to capital expenditure which improves the manufacturing sector capacity, generates employments and reduced poverty which ultimately result in the acceleration of the pace of economic growth. The government of Nigeria can follow the framework of debt swap in order to reduce the large percentage of her revenue used in repaying loans of default on debt service payment. In this scenario, the government can negotiate creditor organizations or institutions to reduce the debt owed and invest the reduced amount into agreed sustainable projects for economic growth and development using the local currency.

Recommendations

- i. Because government borrowings are positively statistically significant to Nigeria's development, the government should direct borrowed monies to sectors/areas of the economy that will spur growth, such as education, health, industry, agriculture and transportation.
- ii. Government borrowing and spending should also be subject to checks and balances.
- iii. The country should focus on domestic debts rather than foreign debt.

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Appendix 1

Year	Real Gross Domestic Product ₦' Billion	Domestic Debt Outstanding ₦' Billion	External Debt Outstanding ₦' Billion
1986	15,237.99	28.44	41.445
1987	15,263.93	36.79	100.79
1988	16,215.37	47.03	133.96
1989	17,294.68	47.05	240.39
1990	19,305.63	84.09	298.61
1991	19,199.06	116.20	328.45
1992	19,620.19	177.69	544.26
1993	19,927.99	273.84	633.14
1994	19,979.12	407.58	648.81
1995	20,353.20	477.73	716.87
1996	21,177.92	419.98	617.32
1997	21,789.10	501.75	595.93
1998	22,332.87	560.83	633.02
1999	22,449.41	794.81	2,577.37
2000	23,688.28	898.25	3,097.38
2001	25,267.54	1,016.97	3,176.29
2002	28,957.71	1,166.00	3,932.88
2003	31,709.45	1,329.68	4,478.33
2004	35,020.55	1,370.33	4,890.27
2005	37,474.95	1,525.91	2,695.07
2006	39,995.50	1,753.26	451.46
2007	42,922.41	2,169.64	438.89
2008	46,102.52	2,320.31	523.25
2009	49,856.10	3,228.03	590.44
2010	54,612.26	4,551.82	689.84
2011	57,511.04	5,622.84	896.85
2012	59,929.89	6,537.54	1,026.90
2013	63,218.72	7,118.98	1,387.33
2014	67,152.79	7,904.03	1,631.50
2015	69,023.93	8,837.00	2,111.51
2016	67,984.20	11,058.20	3,478.91
2017	68,490.98	12,589.49	5,787.51
2018	69,799.94	12,774.40	7,759.20
2019	71,387.83	14,272.64	9,022.42
2020	70,014.37	16,023.89	12,705.62
2021	70,400.71	14,356.97	9,829.08
2022	70,600.97	14,884.50	10,519.04

Source: Central Bank of Nigeria Statistical Bulletin 2023