Folder Title: Economic Adjustment Programs - Nigeria

Folder ID: 1085771

ISAD(G) Reference Code: WB IBRD/IDA DEC-03-82

Series: Records Relating to Adjustment Programs

Sub-Fonds: Records of the Office of the Vice President, Development Economics and Chief Economist and later Senior Vice President, Development Economics and Chief Economist (DECVP)

Fonds: Records of the Office of the Chief Economist

Digitized: 12/19/2018

ECONOMIC ADJUSTMENT

PROGRAMS

NIGERIA

DECLASSIFIED
WBG Archives

Nigeria

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

→ Nigeria RB.

DATE July 1, 1986

TO Distribution

FROM William S. Humphrey, Division Chief, WA1NI

EXTENSION 78058

SUBJECT NIGERIA: Proposed Trade Policy and Export Development Loan

1. I attach a paper produced by the Government of Nigeria setting out its structural adjustment program, as additional documentation for the meeting on July 7th to discuss the Yellow Cover President's Report for the proposed Trade Policy and Export Development Loan (already circulated). Attached to the Government's paper is a brief note giving some background and general comments on it. We propose to send the Government's paper to the Loan Committee with the documentation for the Trade Policy Loan. A draft cover note to the Loan Committee, together with the economic projections to be included in the President's Report will be distributed shortly.

Attachments

cc: Messrs./Mss. Rajagopalan (5), Koch-Weser, Dubey, Choksi, Katz, Golan (3), Krueger, Obidegwu, Vibert, O'Brien, Beguery, Knotter, Alisbah, Squire, Allen, Fuchs, Eccles, Haug, Husain, Hu, Rischard, Baneth, Awunyo, Hittmair, Reinke, Swahn, Jansen, Larkum, Morais, Swayze, Duncan, Tallroth, Mehra, O'Connor, Virata, Walton, Rice, Aiyer, Pinto, Dinh, Bhargava, Ballard, Kumar, Draper, Husain (RMN), Allen, Quirk, van der Mensbrugghe, WAIC

WSHumphrey:pt

NIGERIA - Adjustment Program

Background and General Comments

1. Attached is a copy of the Adjustment Program, July 1986 - June 1988, which the Government of Nigeria distributed in early June to the international financial community (the London Club, the Paris Club, the IMF and ourselves). An earlier version also contained detailed proposals for rescheduling and new money from commercial sources. However, these proposals were omitted from the distributed version these on the advice of IMF and Bank Managements. This was to leave more room for future negotiations with the banks on the rescheduling and new money package after more work had been done by Bank and IMF staff with the Government on the precise financing needs for the period of the program.

2. In early January 1986, the Government announced a budget which contained a number of important reform measures. However, the exchange reform was insufficient, and the subsequent further fall in the price of oil created the need for further expenditure cuts. At the time Messrs. Stern and Thalwitz visited Nigeria in April, no medium-term adjustment program was in place and no internal agreement had been reached on how the elements should be put together. The President agreed with Mr. Stern that such a program should be prepared and endorsed by the Government before the moratorium on principal repayments to commercial banks expired on June 30th. A Committee was appointed to draw up such a program with the advice of Bank and IMF staff. The Bank staff was able to draw on analysis done for our own draft medium-term adjustment paper for Nigeria, and also on the Public Expenditure Report, which had been sent to the Government in late 1985. The IMF staff drew on analysis done as a result of its Article IV Consultation mission in March 1986. The Committee's report was reviewed by a Ministerial Sub-Committee which was able to incorporate further comments made by the Bank and IMF. The final version was further discussed with Bank and IMF in Washington immediately prior to the London Club meeting in New York on June 12th. Both Mr. Erb and Mr. Stern addressed the June 12th meeting of the Steering Committee of the London Club. Mr. Erb said that the Government's programs signalled a major change in Government policy, which in the IMF's view provided a strong basis for international support. The key element was the restructuring of the exchange regime, which would deal with a major rigidity in the economy. Mr. Stern added that the program was one which not only contained measures which would manage and contain domestic demand but also tackled the major distortions in the economy and began to put it on a sustainable growth path. Messrs. Erb and Stern emphasized that the program required both debt rescheduling and new money if it was to be viable. IMF Board approval of the program and Bank Board approval of a quick-disbursing loan could not occur unless it was clear that sufficient financial support from the international community would be available.

3. President Babangida announced the program in a speech to the nation on June 27th. The main change from the earlier version is that direct Government imports would also be included on the second-tier exchange market from its inception. The first-tier will only cover debt

servicing obligations and contributions to international organizations. This, of course, further strengthens the program.

4. The program follows closely the Bank and IMF's stabilization and adjustment recommendations. In particular, the exchange reform will remove the major remaining distortion in the Nigerian economy. There are, however, two important areas which require further discussions with Government. First, the President's speech refers to an updated and streamlined list of imports that are prohibited for reasons of public policy and demand management. The IMF and ourselves will need to agree with the Government on limiting these bans and on a timetable for phasing out those not required for reasons of public safety and security. The second area of concern is public expenditure. Although the public expenditure proposal in the paper are broadly in line with the Bank's recommendations, we need to pin down more precisely the ceilings on expenditures for some major ongoing projects of dubious economic merit. In this connection, we need to look carefully at the implications for public expenditure of the passages in the President's speech which refer to countertrade arrangements. It will be important to ensure that countertrade is not used to get around any budgetary ceilings which are agreed for specific projects.

5. The Government's proposals for parastatal reform are somewhat general. They set sensible guidlines but do not indicate how the reform will be implemented. The selection of the enterprises for commercialization and privatization will not be an easy process, and we have offered to help the Government implement the proposed reforms.

6. The assumptions used in the balance of payments and fiscal projections are quite conservative. The Government projects oil prices to rise from an average of $15 per barrel in 1986 to $20 per barrel by 1990. This is somewhat lower than EPD's current projections. Export volumes are also quite conservative. The assumptions for import growth (3 percent in real terms from 1987 through 1990) are in line with projections for non-oil GDP, agriculture and industrial growth; with improved incentives for agriculture and industry, it should be possible for GDP to grow at about 4 percent per annum and thus keep ahead of population growth.

7. The financing gap which emerges in the balance of payments projections demonstrates the need for both rescheduling by the Paris and London Clubs and new inflows from the international financial community. The mix will depend on the outcome of negotiations with the different creditors. Some illustrative outcomes have been included in the President's Report for the Trade Policy Loan.

15:WH4

STRUCTURAL ADJUSTMENT PROGRAMME
JULY 1986-JUNE 1988

A. Emergence of the Economic Crisis

I. The 1970s Background

1. The oil boom of the 1970s brought with it fundamental changes in the Nigerian economy. The principal aim of the Nigerian decision-makers over this period was to convert the growing oil revenue into investment in social, physical and economic infrastructures. While significant progress was made in a number of sectors - primary school enrolment doubled, power generating capacity tripled and refining capacity quadrupled - some public investments were undertaken which were found to be unviable, questionable in design and in retrospect beyond the execution of capacity of Government agencies.

2. Generally, the policies pursued led to structural changes which left the national economy with substantial price distortions and even more vulnerable to external shocks. First, the economy became heavily dependent on crude oil. By the beginning of the 1980s, the oil sector had come to account for 22 per cent of the GDP, 81 per cent of government revenue and 96 per cent of export earnings. Secondly, the competitiveness of the agricultural sector - the major source of GDP and of export earnings before the oil boom - was eroded by the effect of an appreciating Naira, inadequate pricing policies and rural-urban migration. The sector's share of GDP fell rapidly from around 40 per cent in the early 1970s to 20 per cent in 1980. Thirdly, national expenditure and production became highly linked to imports. By 1980, imports had reached a level equivalent to one-quarter of the GDP; that is double the ratio prevailing in the early 1970s. Nigeria progressively became a major food importer. Expectations of greater wealth further fueled conspicuous consumption of imported goods, and especially of luxury items. The structure of policy incentives and controls also encouraged manufacturing production based on imported inputs. Finally, the public sector began to play an increasingly dominant role in the economy, accounting by, the beginning of the 1980s, for around half of the GDP and two-thirds of the modern-sector employment. The Nigerian Enterprises Promotion Decree of 1972 had set the basis for Government's extensive participation in the ownership and management of banking, insurance, and industry. By 1980, there were around 70 non-commercial and 110 commercial federal parastatals, many of which needed financial support to cover operating losses. There were also large numbers at the State level.

II. Consequences of Oil Slump

3. The economy was thus ill-equipped to handle the collapse of the world oil market which had started about the middle of 1981. The dramatic reduction in domestic crude oil production and the even more dramatic fall in world oil prices led to a sharp deterioration in government

finances and in export revenues. Partly because of expectations that the downturn would be shortlived, the Federal and State Governments were at first reluctant to come to grip with the situation and curb expenditures accordingly. For example, ambitious public investment programmes continued to be implemented. Sizeable external and fiscal imbalances occurred. While external reserves fell abruptly, there continued to be a rapid and large-scale accumulation of trade arrears on top of substantial public borrowing to finance national expenditure programmes.

4. The various austerity measures pursued since 1984 were of course not without a considerable social cost. The drastically reduced supply of raw materials and spare parts to the import-dependent industrial sector had led to extensive plant closure, substantial drop in capacity utilization and large lay-off of the work-force. Severe market shortages have also led to very high prices of many essential commodities. Investment as a proportion of GDP had halved between 1981 and 1985 to 14 per cent. Private investment even shrank at a faster rate than public investment. Across-the-board cut-backs in public expenditure also meant further delays in completing viable projects, thus escalating their costs and depriving the economy of their expected benefits. Even after allowing for a slight upturn in 1985 as a result of some increased oil production and an improved harvest, the GDP in 1985 was some 15 per cent lower than at the beginning of the 1980s, with real per-capita GDP and consumption being well below the levels recorded in the early 1970s.

5. External debt service obligations had meanwhile increased ten-fold to 32 per cent of exports, and still continued to accelerate. The external medium- and long-term public debt outstanding and disbursed at the end of 1985 of US$12.9 billion included a total of US$1.3 billion in promisory notes issued on the uninsured trade arrears and an unpaid balance of US$0.5 billion under the 1983 refinancing of letters of credit. The nation had accumulated substantial general trade arrears, amounting as at the end of 1983 to about ₦ 9.5 billion in claims by foreign exporters. As against such claims, it must, however, be noted that the records of Nigerian importers had only shown a magnitude of ₦ 6.9 billion. Such a fact, combined with revelations like the JMB Affair, would indicate the need for proper official scrutiny and verification before establishing the true magnitudes. What is so far clear is that by 1985, there has been a heavy debt overhang as a proportion of export earnings as compared with other middle-income indebted countries. There had also developed a clearly unfavorable payments profile, given the continued the poor outlook of the world petroleum market.

6. The combination of the downward trend in the world oil market, the policy inadequacies of the past and the bunching of debt servicing obligations have produced a difficult economic situation adversely affecting both the external and the fiscal balances. Despite the policy adjustments made during the last two years, and more thoroughly in the 1986 budget, the recent sharp decline in oil prices has now created the need to further deepen and accelerate the process of structural adjustment. Consequently, the present structural adjustment programme covering the

period July 1986 to June 1988 attempts to set out the Government's strategy for addressing the continuing crisis. The essence of this strategy is the restoration in the medium-term of a healthier path of national economic development as a component of the integrated world economy. The guiding philosophy is the policy thrust of economic reconstruction, social justice and self-reliance, as enunciated in the 1986 Federal Budget. All external support is welcomed and solicited actively, consistent with that philosophy.

B. Policy Actions in the Recent Past

7. The economic and financial situation at the end of 1983, when the Armed Forces assumed power, remained very difficult. Consequently, the Armed Forces had to focus their efforts on improving the general economic situation. Policy initiatives were taken to improve the efficiency of public administration, restructure expenditure policies, foster financial discipline, reduce the overall fiscal deficit of the Federal and State Governments, cut imports sharply and eliminate the accumulation of further external arrears. The present Administration, which took charge of the affairs of State in August 1985, had continued even more vigorously with those reforms.

8. However, it is now recognised that more austerity without structural adjustment constitutes an inadequate response to the fundamental economic and financial problems confronting the country. The present Administration has already made a start by implementing some of the needed structural reforms. It announced in the President's Budget Speech of December 1985, the launching of a broad effort at structural adjustment, on which the further reform programme proposed herein is substantially based. But before turning to the extended programme itself, it might be useful to consider the progress made at economic reforms since 1984. The brief survey is important both in itself and as an indication of the intensified seriousness and commitment with which the present Administration pursues the necessary structural adjustments.

I. Fiscal Measures

9. The tight fiscal policy pursued since 1984 has enabled the overall public sector deficit to be reduced from 11.6 per cent of the GDP in 1983 to 2.7 per cent in 1985. Despite the recent sharp drop in oil prices, the deficit in the first quarter of 1986 has also been maintained at the target level.

10. The reduction in public-sector deficit was achieved by a reduction of expenditures and an increase of revenues. In 1984, the Government's overall expenditure programme was cut by 28 per cent in nominal terms (40 per cent in real terms), while the federally-collected revenues grew by 9 per cent. This trend continued in 1985, as current expenditures

were reduced by 36 per cent simultaneously with the provisional figures of Government revenues showing an increase of 34 per cent as compared with 1984.

11. The recurrent expenditure policy was aimed at streamlining public-sector employment to reduce the burden of the wage bill. Public-sector wages were frozen, and strict limitations were placed on transfers to parastatals as well as to the State Governments. However, the State Governments themselves substantially cut backs their expenditures in real terms. All the States introduced budgets for 1985 in which recurrent expenditures were to be fully covered by revenue from the Federation Account plus State-generated sources; similarly, with the capital budgets at both Federal and State levels. Their level was tailored to realistically available resources. Their composition was also re-oriented.

12. Further measures which were aimed at reducing the Federal Budget deficit were incorporated in the 1986 Budget. Substantial reductions have been made in the salaries and fringe benefits of civil servants. A similar restraint was continued in hiring staff over a wide range of positions. Transfers for commercial parastatals are being cut to 50 per cent of their 1985 levels. The Government has shifted emphasis to maintenance and rehabilitation programmes, especially in education, health, transportation, utilities and other infrastructure.

13. A key reform which was announced in the 1986 Budget was the elimination of the hitherto substantial subsidy on petroleum products consumed domestically. With the recent developments in the international oil market, the domestic prices of these products have recently indeed been above the international prices. Other subsidies, particularly those on agricultural inputs like fertilizer and on-farm services, have also been under downward review. Already, the subsidy on fertilizer has been reduced from 75 per cent to 25 per cent; and is slated to be phased out over the next three years.

II. Monetary Policy

14. The macro-economic strategy pursued by the Government, in addition to austere fiscal measures, relies on a tight monetary policy to stabilize the economy and stem inflation. The improvement in public finances has meanwhile helped in reducing the growth rate of monetary aggregates. Net domestic assets have grown at an average annual rate of only 10 per cent during 1984-85, compared with a 47 per cent increase in 1980 and an average of 13 per cent in 1981-83. The credit to the Government sector also increased at a slower rate of 15 per cent compared with the actual increase of 28.6 per cent in 1983. The pursuit of tight fiscal and monetary policies, together with a bumper harvest of food crops had significant impact on the inflationary pressure. The inflation rate slowed down to about 5.5 per cent in 1985 from an annual rate of 40 per cent recorded for 1984.

15. In order to address distortions in credit allocation caused by the level as well as the structure of interest rates that prevailed in the part, the Central Bank had raised nominal interest rates in the last two years. With the decline in inflation, interest rates are now positive in real terms. This reform in monetary policy is contributing to the structural adjustment process by increasing both the incentive for saving and the efficiency of investment allocation.

16. Since 1969-70 there have been controls on allocation of credit among 18 sectors and sub-sectors. These controls proved to be rigid and unwieldy, leaving the banks with little discretion in their credit operations. The need to encourage initiative and flexibility on the past of the banks and also to facilitate greater effectiveness of the Central Bank's monitoring efforts led to the re-grouping of the various sectors and sub-sectors into eight in 1984-85. In 1986, the number of sectors has been further reduced to four.

III. External Sector

17. The balance of payments performance in 1984 and 1985 also reflected the impact of the stricter demand management policies which were pursued by the Federal Government. The current account deficits of 9.8 per cent of GDP in 1985 and 6.5 per cent in 1983 had been transformed into a modest surplus in 1984 and a clear surplus of 2 per cent of GDP in 1985. The overall balance recorded a surplus of US$1.1 billion in 1984 and US$0.5 billion in 1985. These surpluses allowed for some reduction arrears. The gross international reserves increased from US$1.1 million at the end of 1984 to US$1.6 million at the end of 1985.

18. The Government is fully aware that the results achieved in the last two years cannot be sustained without further compression in imports, continued widespread under-utilisation of industrial capacity and increased unemployment. The import level has been cut from the 1981 peak of US$18 billion to US$8.3 billion in 1985. The need to compress import was reinforced by the increasing demand for debt service payments as amortization on earlier borrowings fell due.

19. Since 1984, the Nigerian Government has allowed the Naira to slide against the major foreign currencies. The nominal Naira/Dollar exchange rate was adjusted downwards by 20 per cent between the end of 1984 and the end of 1985. Similar adjustments were made against the currencies of other major trading partners.

20. The external borrowing strategy of the Government has also been cautious and prudent since 1984. Unlike the period 1980-83, when the external debt increased from around US$4.6 billion in 1980 to around US$11 billion at the end of 1983, the total new external borrowing has been limited since the past two years. The composition and terms of new borrowing have also shifted drastically. The main borrrowings have been from multilateral creditors such as the World Bank whose financing terms are consistent with Nigeria's long-term development needs. Short-term

borrowing at relatively higher interest rates has been generally avoided. Despite the difficult external payments situation, Nigeria has however remained current in its servicing of medium- and long-term debt. It has also fulfilled its obligations in meeting the agreement under the refinanced Letters of Credit programme which was concluded in 1983.

IV. Wages and Employment

21. Wage policy guidelines have also been used to achieve stabilisation policy targets. In order to reduce public-sector expenditure targets and aggregate demand, no general salary increase has been granted to public-sector employees since 1982. Given the high inflation rates which have been experienced in recent years, this has resulted in a very sharp erosion of real wages even after fringe benefits have been taken into account. Furthermore, with effect from 1st January, 1985, the various Government departments have been taking measures to recover the costs of services provided for public-sector employees. The wage policy guidelines for the last three years have put a freeze on private-sector wages and salaries as well as fringe benefits.

22. Substantial reductions in the work force within parastatals and the civil service have also taken place since 1984. The recession in economic activity has forced similar cuts and retrenchment in the private-sector. Available labour statistics indicate that unemployment rose by 18.8 per cent between 1982 and 1984, and is almost certainly higher still today. The Government is deeply concerned with this growing problem of unemployment. For economic, social and political reasons, the problem must now be seriously addressed before the expiration of the national economic emergency period.

V. Agricultural Sector

23. Government has given high priority to the stimulation of agriculture. In particular, the Government has cut back sharply on the inflow of imported agricultural commodities which had hitherto provided a disincentive to domestic agricultural production.

24. A number of important institutional reforms have also been introduced by the present Administration. These have been directed in the main at reduction in Government involvement in direct agricultural production and an increased focus on providing the necessary support services to farmers. The principal measures in this regard deserve mention.

26. First, in a major policy initiative announced in April 1986, the Government removed one constant source of disincentive to farmers when it decided to wind up all the six Commodity Boards by 31st December, 1986. The internal and external marketing of these commodities are now open to private individuals, groups, companies and processors. The decision to wind up the Boards (which had for long enjoyed a monopoly position in the purchase and marketing of their respective cash crops)

was based on the realisation that, on balance, they had for some time now become more of a deterrent to increased agricultural production and that their operations had also become costly and inefficient.

26. Secondly, the River Basin and Rural Development Authorities have been reduced from 18 to 11. In addition, these Authorities are now to discontinue their direct agricultural production activities and focus their attention on the development of water resources. The Agricultural Development Projects (ADP) which have been developed with the support of the World Bank, will intensify their activities in the areas of agricultural extension, inputs supply, on-farm adaptive research and rural infrastructural support. To complement these efforts, a package of incentives has been adopted to encourage companies to invest funds and management skills for the development of commercial farms.

27. Thirdly, the Government decided to wind-up eleven of its companies which were involved in various direct agricultural production activities and to transfer their activities to the private sector. The Government is already in the process of privatising four of such parastatals; namely the Nigerian Dairies Limited, Madara Limited, the Nigerian Food Company and the Bauchi Abbatoir. In addition, the National Livestock Production Company and the Nigerian Ranches Company are being wound-up. Similar enterprises will be privatised or wound-up when the Government completes its on-going review exercise.

28. To improve the efficiency and availability of inputs supply to the farmers throughout the country, the Government is also withdrawing from the importation, transportation and distribution of fertilizers. These would now be imported and distributed by private companies.

29. As a further step to encourage farmers to stay on their farms and to accelerate the movement of agricultural produce from the rural areas to the urban centres, the Government has established the Directorate of Food, Road and Rural Infrastructures. Using funds accruing largely from the withdrawal of domestic petroleum subsidy, the Directorate will work closely with the State Governments in order to reach the various local communities throughout the country. Apart from stimulating agricultural production, the scheme has been designed as a vehicle for moving some resources from the urban to the rural sector.

VI. Industrial Sector

30. The overall strategy of the industrial development has also been shifted from maintaining public-sector-dominated, large capital-intensive industries to that of providing the macroeconomic environment and other incentives for the private sector to assume the lead role in manufacturing. Public sector investment is henceforth to concentrate more on the provision of necessary support industrial services and infrastructures. The importance of small and medium scale industry in providing employment as well as in increasing domestic value-added has

also been recognised. Adequate provision of credit to small enterprises has been made under a line of credit from the World Bank for the purpose.

31. A relevant reform already in place is the simplification and rationalisation of the tariff structure. This was designed to reduce variation in effective protection to local industries. The range of import duties was reduced from its previous extreme variation, and for the most part, they now cluster between 10 and 60 per cent. A wide variety of goods that were previously imported duty-free has, however, been placed under tariffs. The Approved-User-Scheme and the General Concessionary Rates of Duty which granted low and concessional rates on imported raw materials and other imported intermediate products were abolished. The specific import duties were replaced by ad valorem rates. These measures were intended primarily to end the discrimination against domestic resource-based industries and to discourage unfair competing imports. It is however to be noted that Government realises that the various measures undertaken so far have not been sufficient to offset the subsidies implicit in the continued overvaluation of the Naira. It is recognised that imported raw materials and finished goods continue to be attractive.

32. Attempts have been made to re-orientate the import licensing system to increase the utilisation capacities of existing industries. Liberal licences were issued to the manufacturers rather than to general traders and wholesalers of imported goods. However, in order to ensure that the domestic manufacturing industry does not become excessively protected, the coverage of domestic excise duties was enlarged to now include over 300 new products.

C. OBJECTIVES AND STRATEGY OF THE ADJUSTMENT PROGRAMME

33. The present programme aims at altering and re-aligning aggregate domestic expenditure and production patterns so as to minimise dependence on imports, enhance the non-oil export base and bring the economy back on the path of steady and balanced growth. Specifically, the major objectives of the programme are:

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

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

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

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

34. As a first step, a National Economic Emergency Decree which empowers the President to issue orders and make regulations during a 15-month economic emergency period was promulgated in October 1985. Under it, the President is given discretionary powers to put in place measures that will improve the economy. The actions taken thus far under the Decree include reduction in wages and salaries in the public and private sectors, suspension of a number of non-essential public projects, removal of the petroleum subsidy, and the banning of unnecessary food and agricultural products. The 1986 Federal Budget extended, consolidated and articulated these and similar emergency policy measures.

35. It is expected that the economic performance under the present programme would represent a marked departure from the nation's experiences in the recent times. Emphasis is now being placed not only on demand management policies, but also on supply-oriented measures. In particular, the success of the programme would depend to a large extent, on the speed at which the agricultural, manufacturing and construction sectors are rehabilitated.

D. MAIN FEATURES OF THE ADJUSTMENT PROGRAMME

36. The main elements of the present adjustment programme are:

(i) strengthening of the hitherto strong demand management policies;

(ii) adoption of measures to stimulate domestic production and broaden the supply base of the economy;

(iii) adoption of a realistic exchange rate policy;

(iv) further rationalisation and restructuring of the tariffs in order to aid the promotion of industrial diversification;

(v) move towards improved trade and payments liberalisation;

(vi) reduction of complex administrative controls simultaneously with a greater reliance on market forces;

(vii) adoption of appropriate pricing policies, especially for petroleum products and public enterprises; and

(viii) encouragement to rationalisation and privatisation of public sector enterprises.

37. The core policies involve actions to (a) correct for the serious over valuation of the Naira through the setting up of a viable and substantial second-tier foreign exchange market, coupled with adjustments to the official rate and aimed at a convergence of the various exchange rates as soon as possible; (b) overcome the observed public-

sector inefficiencies through improved public expenditure control programmes and the speedy rationalisation of the parastatals sector; and

(c) relieve the debt burden and attract a net inflow of foreign capital, while keeping a lid on foreign loans.

I. Trade and Exchange Policies

38. The Government is aware that a system of bureaucratic controls is not only sumbersome but is also liable to corrupt practices and to unintended distortions in resource allocation. The medium-term policy objective is therefore, to gradually eliminate the existing administrative controls on trade, in line with the progressive take-off of the second-tier foreign exchange market.

39. The central element in the incentive framework is the nexus of policies pertaining to the price and allocation of foreign exchange. These policies have a pervasive effect on all production, and particularly on non-oil exports. The Government is aware of the over valuation of the Naira. It also recognises that the closer the exchange rate is to a realistic level, the less will be the need for the import licensing system, the greater the efficiency in the use of foreign exchange, the higher the level of export earnings in the medium to long term and the smaller the leakage of foreign exchange through smuggling of goods and black marketeering in currencies. As already indicated, the Government, therefore, intends to move the Naira rate towards a realistic level. To assist the process, the second-tier foreign exchange market in which the rate will be market-determined is being established during 1986.

40. Second-tier Foreign Exchange Market (SFEM) mentioned above is expected, over time, to help provide the monetary authorities with the realistic exchange rate of the naira. To achieve this objective the SFEM will be allowed to operate under market conditions and be appropriately funded. In addition to private sources of foreign exchange supply to the market, the World Bank has agreed, in principle, to provide $100 million to the market during the last six months of 1986 and $300 million in 1987. The Government will itself release foreign exchange to support the market. While the total magnitude of official funding will depend on the volume of transactions to be channelled through the market, for a start, the Government will support the market with $1 billion during the second half of 1986 rising to $3 billion in 1987. At its inception, all transactions, except those relating to debt service and direct Government import, will be transferred to the market. In essence, Government will operate on the first tier while all non-governmental transactions will go through the second-tier. This partitioning of transactions is to minimise leakages. For purposes of operating the two-tier system during the adjustment period, 'Government transactions' will be rigorously defined to eliminate inter-tier manipulations and abuse. The objective of policy is to bring about a merger of the two markets and achieve a single realistic and market-determined exchange rate for the Naira by the end of the adjustment period.

41. In the meantime, in order to ease the convergence process, the official exchange rate policy will be geared towards narrowing the gap between the official and the second-tier rates. This will be done by a downward crawling of the official rate. The detailed modalities of the SFEM are now almost completed and will be embodied in a Decree to be promulgated in due course. It is hoped that these exchange rate reforms, plus the other supportive fiscal and monetary policies, will start having a salutary effect before the end of 1986 on the balance of payments, and on diversification of productive and export bases of the national economy. Again, Government expects that once these reforms are in place, they would render the current policy of 30 percent generalised import levy as well as the use of widespread import licensing unnecessary and superfluous.

II. Non-oil exports

42. In order to reduce dependence on the oil sector as the principal earner of foreign exchange, the present Administration is deeply committed to promoting non-oil exports. Although it is realised that the initial base of the non-oil exports has shrunk considerably during the past decade, the government believes that the correction of cost-price distortions through a realistic exchange rate, combined with other positive export incentives and institutional reforms, should make it possible for Nigeria to earn at least $1 billion from non-oil exports by the end of the present decade. But even then, that would still leave the total non-oil exports below the level that was achieved in 1980. A major thrust of the export drive will be aimed at capturing, under a more realistic exchange rate regime, the large ECOWAS market which already benefits from the inflow of a wide range of illegal manufactured goods and commodities from Nigeria.

43. The major policy instruments to achieve the objective of a more aggressive, consistent and comprehensive export expansion programme have been set out in the 1986 Budget. In addition, the conversion of export earnings into Naira at rates prevailing on the second-tier market will boost the Naira incomes of farmers producing for export. The measures are being further strengthened, and streamlined, with analytical support from the Operations Division of the World Bank. A memorandum on "Export Incentives and Promotion Measures" has already been received from the Bank in this connection, and further detailed work is soon to be taken in hand.

44. Meanwhile, various complementary measures to assist exports are being pursued. These include the streamlining and simplifying of the present cumbersome process of obtaining necessary documentation for exports, extending the facility of rediscounting short-term bills to all non-oil exports and ensuring that exporters readily obtain duty drawbacks and exemptions.

III. Fiscal Balance

45. The financial resources for public expenditures for the rest of the 1980s are now likely to be less than was previously envisaged. The grim picture in the world oil market and the substantial debt repayments falling due will mean that public expenditures and especially those involving foreign exchange, will have to be severely curtailed. While some relief would be available through debt rescheduling and inflows of new funds, it is the Government's intention to adjust public expenditures as needed to reflect the revenue constraints, with the aim of containing budgetary deficits within 3 per cent of GDP. An important implication of the continued uncertain financial situation is the need to institutionalise a system of public expenditure planning and budgeting which recognises the uncertainties and can alleviate their negative impact. For this purpose, the Government will use realistic revenue estimates within the framework of this structural adjustment programme and will concentrate on the timely completion of a limited core of viable capital projects that can be adequately funded.

IV. Criteria for Expenditure Allocation

46. Expenditure re-allocation will accompany general expenditure reduction in order to ensure that the net benefits obtained from the limited funds are maximized. The principal considerations in making the necessary decisions are as follows:

(a) Constraints on the growth of the public wage bill will be maintained. Over the last year, there has been significant retrenchment in the public sector as well as cuts in net wages and benefits. In the next few years, the emphasis will be to hold down the level of public-sector employment, mainly through a combination of attrition and extension of the freeze on hiring to all but the most critical skills. Wage increases will be allowed during the programme period but at less than the rate of inflation until the financial situation improves. Substantially, wages for different skills will be allowed to reflect scarcity values.

(b) Constrained supplies and inadequate maintenance of infrastructures have greatly impaired the delivery of public services. Levels of supplies (materials, spare parts, small tools and transport equipment) will be increased in a number of areas to ensure the achievement of reasonable levels of performance. Also, routine and periodic maintenance will have priority over new project investments to avoid the rapid deterioration of existing capital assets (e.g. roads, hospitals and water supply schemes) and in recognition of the higher returns to be gained from the efficient use of these assets. Where extensive rehabilitation is required, it will be judged against new investment on the basis of respective costs and benefits.

(c) Over the years, transfers to parastatals to cover their operating deficits and capital expenditure requirements have been quite high. But now, non-statutory transfers to all economic and quasi-economic parastatals will constitute not more than half of their 1985

levels. Transfers to fully commercially-oriented parastatals will be eliminated by the end of the programme period.

(d) There are a number of partially completed capital intensive projects, some of which are however currently of doubtful economic viability. The Government recognises that across-the-board reduction of allocation to these projects will have to be avoided so that the economy is not burdened by a proliferation of uncompleted and weak projects. Priorities have thus been set for the completion of projects on the basis of their economic viability and proportionate completion costs. Those with high economic viability and high completion ratios will be accorded priority and will be completed expeditiously. Projects with low or doubtful economic viability and low completion ratios will be re-examined to see if they can be re-shaped both in scope and timing to reduce their costs and/or increase their benefits. Those shown to be non-viable or without redeeming features will be dropped.

(e) Exeptionally and on a limited basis, new projects may be undertaken during the programme period where they are clearly essential for the economic recovery process and their funding clearly fully established.

47. As a result of the recent adverse development in the world oil market, it is envisaged that the budgeted federally-retained revenue may decline significantly for part of the programme period. This would clearly call for flexibility in fiscal administration. The Government, therefore, intends to adjust its spending commensurate with the available resources on a quarterly basis. If, however, revenues should exceed those estimated, they will initially be earmarked to further reduce any latent budget deficit, with the next highest priority being also given to further increasing operation and maintenance expenditures in areas which are vital to the reconstruction process. If, on the other hand and based on quarterly revenue receipts, the revenue should significantly fall short of the estimate, non-hardcore releases will be scaled down. All significant upward or downward adjustments in the budgetary administration will be closely watched and controlled by the Monitoring Unit provided under this programme.

V. Public Investment

48. The rationale for the allocation of public investment expenditure among sectors over the programme period rests principally on the relative importance of the different sectors in the Government's development strategy, the increased emphasis to be put on the role of the private sector and, for major projects, rates of return on additional funds needed for project completion. The tentative sectoral allocations made have taken account of project and sector analysis of the World Bank, based on the work of a number of missions related to the review of the public expenditure programme. The allocations will be revised subsequently in the light of various evaluation studies to be undertaken and the priorities to be specified in the Fifth National Development Plan.

49. The capital expenditure in the infrastructural and social sectors will be primarily focused on periodic maintenance and rehabilitation. Some principal exceptions to this will include:

(a) The continued implementation of the Egbin Power generating plant and an upgrading expansion of the transmission and distribution network to ensure a better balance of generation and distribution capacities.

(b) The completion of priority capital projects in road construction of civil engineering works with ascertained designs, specifications, irreducible cost levels and viable funding arrangements.

(c) The continued, but slower-paced, development of Abuja. In recognition of the financial constraints on the pace of development of the new capital, a review of the benefits and costs associated with the alternative transfer scenarios will be undertaken.

50. Capital expenditures in the agriculture and manufacting sectors, particularly the latter, will be most affected by the resource constraints. In agriculture, the ADPs and their support for rural development would justify a greater allocation of the sector's resources. Major supplemental funds have been allocated through the Directorate of Food, Roads and Rural Infrastructures, especially for the provision of feeder roads. Allocations for on-going irrigation will give emphasis to the completion of viable small-scale, low-cost irrigation schemes and earth dams. Increased attention will be given to operational research in order to bridge the gap between extension services and research so as to speed up the adoption of new varieties and technologies and its link to extension.

51. In the industrial sector, gas infrastructural development will be given priority to enable power stations and selected industrial users to substitute gas, that is presently being flared, for the more expensive fuel oil. Construction of the Warri-Lagos gas pipeline will thus be one of the few new projects which will be implemented during the programme period. Priority will also be given to the completion of Phase I of the petrochemical projects; but with proper re-structuring of the carbon black and synthetic detergent plants, both of which are now probably likely to have excess capacity in the short run. A solution would of course be to export the excess products. Implementation of the proposed LNG project will be accelerated during the programme period especially if purchase contracts can be guaranteed and the project is reconfirmed to be economically viable. Other projects in the oil and gas sectors will similarly be reviewed in the light of various continued uncertainties in the world energy industry.

52. A broad study will therefore be carried out to review the strategy for the further development of the gas and oil related industries in the light of the recent deterioration in international oil and petrochemical markets. Such a study will also highlight how to restructure Phase II

of the petrochemical projects in order to increase their potential profitability and explore further opportunities for private-sector participation. The constrained financial situation will require the scaling down and re-structuring of the steel development programme contained in the Fourth National Development Plan. In this context, Federal Government in collaboration with the World Bank will undertake a review study of the steel sub-sector and its major projects very early in the programme period. Meanwhile, public expenditure in the sub-sector will be limited and restricted to essential on-going projects until the review study is completed. As a general rule, these allocations will not exceed their 1986 budget levels. With regard to other industrial projects, the aim will be to complete the Onne fertilizer project as scheduled. Government will also consider all possible options, including private sector participation, to restructure other on-going capital-intensive industrial projects such as Iwopin Pulp and Paper and the Savannah Sugar projects.

VI. Reform of Parastatals

53. The public enterprise (Parastals) sector in Nigeria is quite large, comprising at the federal level alone about 100 enterprises spread over agriculture, mining, manufacturing, transport, commercial and other service activities. Government investment in this sector is over 23 billion (₦8 billion in equity and ₦15 billion in loans), but the returns thereon are less than ₦500 million annually. The Government is thus clearly not receiving a fair return on its investment outlay, while it continues to pay interest charges and principal on the huge loans. Also, as much as 40 per cent of the Federal Government's non-salary recurrent expenditure and 30 per cent of its capital investment budget has gone to support public enterprises. This state of affairs will no longer be allowed to continue. The parastatals and Government-owned companies are therefore now being classified into five broad categories for subsequent action. Based on this classification, they would either be:

(a) fully privatised,

(b) partially privatised,

(c) fully commercialised,

(d) partially commercialised, or remain as

(e) public institutions.

54. Enterprises which function in a fully commercial manner will be fully privatised. The development of the private sector in Nigeria over the last 10-15 years has been such that it can be relied upon to assume responsibility henceforth for such parastatals. Essentially, they are really limited liability companies; and the only thing that distinguishes them from their private sector counterparts is government owner-

ship and control. Such direct controls will now be removed to permit such public enterprises to operate like their private counterparts. Some enterprises will however, only be partially privatised by the sale of part of the Government's equity holding and the requirement that they can operate as private companies where they are not already doing so. Thus, the Government will no longer provide any operating subventions and their future financial needs would have to be met by the private capital market.

55. Another set of enterprises will be either partially or fully commercialised. These will continue to be fully owned by Government, but will have a financial structure which will permit them to raise capital. Those fully commercialised will be expected to operate without government operating subventions and treasury support for future capital development. Those partially commercialised will be those which can generate a fair proportion of the financial resources they need for their operations but will continue to need some government support towards operating costs or future capital investment.

56. The last category consists of purely public institutions. These will continue to be largely funded from treasury resources but will, even then, be expected to impose user charges as may be appropriate.

57. All parastatals irrespective of their organisation have been directed to keep appropriate records, and to effect timely publication of their quarterly, annual and audited reports. Guidelines and performance tests for efficient operation of the parastatals would therefore have to be established and enforced.

58. Although some enterprises have already been offered for sale, an effective mechanism to ensure a non-disruptive release of shares to the market is how being worked out in line with the 1986 Budget. This would be put in place during the third quarter of 1986. For enterprises that will meanwhile be retained in the public sector, measures will also be introduced not only to reduce government intervention in their operations but to avoid the use of monopoly position to impose uneconomic prices on consumers. The operations of all government enterprises will be closely monitored and steps will be taken to ensure their public accountability at all times.

VII. Monetary Policy

59. The programme envisages that monetary and credit policy will be consistent with the targets set for the balance of payments, the increase in reserves, fiscal policies and for control of domestic inflation. Under the 1986 budget which is already in progress, total net domestic credit to the economy will be allowed to increase by 8.7 per cent, while net claims on government will increase by 5.9 per cent. Furthermore, net claims on the private sector are expected to rise by 12.8 per cent. However, in the event that the fiscal policy targets set in the 1986 budget become unachievable, alternative growth

targets in the aforementioned monetary aggregates, have been set under different scenarios. A common feature of the various scenarios is a deliberate pursuit of a tight monetary policy throughout the programme period. Overall, net domestic credit to the economy is envisaged to increase by 5 per cent and 6 per cent in 1986 and 1987 respectively, from their 1985 level.

60. As mentioned in paragraph 16 above and as a strategy for ensuring that the bulk of available domestic bank credit finances the directly productive activities in the economy, the Nigerian economy has since fiscal year 1969-70 been classified into 18 sectors/sub-sectors for the purpose of allocation of bank credit. By 1983 however, the control had become rigid and unwieldy leaving the banks with little discretion in their credit operations. The need to encourage new initiatives and flexibility on the part of the banks and also facilitate greater effectiveness of the Central Bank monitoring efforts led to the regrouping of the sectors/sub-sectors into eight in 1984 and 1985. In 1986 the number of sectors was further reduced to four. This number will be further reduced to two in 1987. The existing system of credit allocation will be kept under close review with a view to eliminating it by the end of the programme period.

61. Currently, the banks are generally very liquid to the extent that some are even reported to be refusing deposits. The Government recognises that such excessive liqudity in the financial system carries with it the danger that a revival in demand could easily be translated into a rapid acceleration of inflation. In order to reduce this liquidity overhang, to allow better control over the monetary situation by the Central Bank and to encourage banks to compete in the mobilisation of savings, the banks will be asked to deposit domestic counterparts of their external payment arrears with the Central Bank in blocked accounts by the end of 1986. To facilitate this process, early attention will be given to the re-financing of the domestic debt owed to non-bank institutions, notably, contractors and supplies. This may be accompanied by the re-introduction of stabilisation securities and a thorough review of the interest rate structure, with a view to further narrowing of the spread between deposit and lending rates during the course of 1986, and followed by the elimination of interest rate differential among sectors by 1988. It is expected that the desired movements in interest rate will form part of the programme review discussions. A review exercise of the restructuring of the financial sector and providing a plan of action for improved financial intermediation, will be set in motion during the second half of 1986. The Government proposed meanwhile to maintain the policy of real positive rates that was established in 1985.

VIII. Agricultural Sector

62. The agricultural sector is an area where improvements can make an immediate impact on the supply situation to dampen inflationary pressure. It is also an area where dependence on the external sector for food and industrial raw materials can be quickly lessened. Previous

fiscal, trade and exchange rate policies which exacerbated price distortions in the economy had been major contributory factors to the poor performance of the agricultural sector. A comprehensive policy package to revamp the sector, therefore, forms the cornerstone of the programme. The major objectives of agricultural sector policies are:

(i) to increase domestic food production with a view to improving nutritional standards and reducing and eventually eliminating external dependence on food supply;

(ii) to increase domestic supply of agricultural raw materials such as cotton, cocoa, oil palm, sorghum, rubber, millet, sugar cane and maize to the manufacturing sector, thereby increasing local value added and reducing dependence on imported raw materials;

(iii) to increase production of exportable cash crops thereby diversifying the export base of the economy;

(iv) to raise rural employment and income; and

(v) to achieve regional optimal crop production mix, reflecting the comparative advantage of each agro-ecological zone.

63. To achieve these objectives, the distortions that continue to impede agricultural production are being removed. Furthermore, the needed structural reforms that have been announced will be vigorously implemented. The winding up of the Commodity Boards, coupled with the adoption of an appropriate exchange rate policy under which all non-oil, export transactions will take place at the free second-tier foreign exchange market, will provide improved price incentives that will enable farmers to complete effectively both in the product and the factor markets including that of labor. The price incentives will also encourage rehabilitation of the existing productive capacity and induce new planting on the scale required to substantially boost production. The implementation of the Land Use Decree will be re-examined with a view to ensuring that land availability does not become a constraint to growth in the agricultural sector.

64. Meanwhile, measures have been announced to encourage local production of rice and maize. In 1986, the national maize production and distribution programmes will provide farm inputs and services that will enable the targets of 3.3 million tons in 1986 and 3.6 million tons in 1987 to be reached. The country would thus have achieved self sufficiency in maize by the end of the programme period. Rice production is also expected to rise from 0.9 million tons in 1985, to 1.1 million tons in 1986 and 1.5 million tons in 1987, and thus gradually cover the domestic supply gap. Again, the production of oil palm has improved substantially, reaching almost 0.6 million tonnes in 1986, and thus reducing the country's deficit therein to about 0.3 million tonnes.

Special emphasis is now being placed upon the construction of 23 oil palm mills in the oil palm belt, 7 of which have indeed already been commissioned.

IX. Manufacturing Sector

65. The current major problem hampering a rapid growth of output in the manufacturing sector is the inadequate supply of imported inputs and spare parts thus resulting in gross under-utilisation of installed capacity. With the stagnation of available foreign exchange at a very low level and the determination to meet external debt service obligations and pay for current imports as and when they fall due, the amount of licenses granted for the purchases of imported industrial inputs was not only insufficient but also thinly spread among various producers. The result has been that most of them could not operate at adequate levels of capacity utilisation. Against the background that the use of import license as a means of rationing raw materials among establishments was originally conceived as a temporary measure, the Government has come to the conclusion that the long-run stable solution to the raw materials problem involves a positive step towards their local production and utilisation. Poor and unreliable infrastructural facilities such as energy, water supply, roads, and telecommunications have also limited the performance of the sector. Inappropriate tariff structure and an over-valued domestic currency have combined to negate in many cases the protection accorded to some domestic industries and are contributory factors inhibiting a meaningful industrial linkage with the domestic resources base.

66. The industrial strategy under the present structural adjustment programme will therefore aim at:

(a) encouraging the accelerated development and use of local raw materials and intermediate inputs rather than depend on imported ones;

(b) development and utilisation of local technology;

(c) maximising the growth in value added of manufacturing production;

(d) promoting export-oriented industries;

(e) generating employment through the encouragement of private sector small- and medium-scale industries;

(f) removing bottlenecks and constraints that hamper industrial development including infrastructural manpower and administrative deficiencies; and

(g) liberalising controls to facilitate greater indigenous and foreign investment.

67. To achieve these objectives, the Government believes as essential the adoption of a realistic and flexible exchange rate policy that will reflect the scarcity of foreign exchange and ensure its efficient allocation. Also essential is an appropriate structure of trade taxes. During the adjustment period, the Government will put into effect a revised tariff and excise tax structure that will be consistent with the new exchange-rate policy in achieving the desired levels of effective protection as well as provide needed support to non-oil export promotion measures. Such revamped tariff and exchange rate policies will also provide the much-needed incentives for developing locally-produced raw materials. Thus, imports of raw materials and spare parts as well as export of manufactures will be channelled through the second-tier foreign exchange market during the programme period. The Government will review the existing system of price controls with a view to phasing it out.

68. The Government attaches importance to appropriate foreign private investment, especially those which can be associated with the development of indigenous expertise and the absorption/diffusion of new technology. Such investments are particularly welcomed in the fields of local processing of agricultural products and minerals to replace imported inputs. To this end, measures will be introduced to provide incentives to local and foreign investors. In order to encourage foreign as well as local private investment, requirements including the procedures for registering new industrial enterprises, and the granting of locational approval for undertaking export activities will be liberalised in order to remove impediments to the free flow of investment. Specifically, the role and powers of the Industrial Development and Co-ordinating Committee (IDCC) will be increased in order to make it the focal point for all the necessary permits and approvals for foreign investment. This will enable foreign investors to deal exclusively with the IDCC rather than to seek clearance from a wide range of Ministries nd Agencies for the establishment of new industries. New foreign investment will be channelled through the second-tier foreign exchange market to take advantage of the prevailing market-determined exchange rates. Likewise, the remittance of dividends and profits declared as from 1986 will be channelled through the same market.

69. In order to enhance technological development and promote the growth of priority industries, including production of export goods, the following incentives, among others, have been provided: accelerated depreciation, duty drawbacks, preferential import licences, etc., all backed up by appropriate pricing policies with regard to exports. Again, up to 25 per cent of gross foreign exchange earnings are being allowed meanwhile to non-oil exporters.

70. A detailed study of the industrial policy and the incentive system has been undertaken, and a White Paper on it will be issued during the course of 1986. A Policy Analysis Department has also been set up in the Ministry of Industries in collaboration with the World Bank and the Ministry of National Planning to implement and keep under constant

review the industrial policy and incentive system.

E. Financing the Adjustment Programme

I. Macro-economic Parameters

71. The Government is committed to carrying through its reform programme successfully even in the face of an import capacity that is somewhat lower than previously anticipated. The key assumptions underlying the present projections are:

(a) The world oil market is unlikely to recover quickly and will probably remain subject to considerable uncertainty for most of 1986.

(b) The Government will ensure the repayment of genuine and authenticated outstanding external debts in an orderly manner.

(c) There will be restricting of new borrowing over the programme period to absolutely necessary levels.

72. All of these clearly call for restraint in planning import levels. In 1986, oil export revenues are likely to be down significantly. Therefore, imports of goods will also have to be cut substantially, probably down to a level of about US$6.0 billion. 1986 will thus be a year of continued economic hardship and austerity. It will however also be one of launching the structural adjustment programme for national economic revival.

73. For 1987, the target for imports would probably lie between US$7 to US$7.5 billion per year (in 1986 prices), growing thenceforth by about 5 per cent annually through to 1990. In order however to be conservative in the face of external uncertainties, import planning is being done on the basis of US$7.4 billion in 1987, with only 3 per cent annual growth in real term to the year 1990. While this is far below the level achieved in recent years, there was excessive import dependence during and immediately after the oil boom period. It has also been observed that there had been substantial over-invoicing of imports and other sharp practices as a means of capital flight. With a realistic exchange rate, this hidden capital flight is expected to decline substantially. Imports in the future will have higher purchasing power than would have been the case without the present reform programme and with continuing over valuation and over-invoicing.

74. During 1986 and 1987, the cumulative gap for which balance of payments financing will be required is estimated at approximately US$9 billion. Given the present low level of international reserves and the uncertainty of the world oil market, it is the Government's intention to allow for some increase in reserves over this period. For every U.S. dollar that the petroleum price falls below the projections, an additional financing requirement of about US$400 million a year would arise. Should this occur on a temporary basis, reserves would be drawn

down and external borrowing marginally increased. If on the other hand, the decline in oil earnings appears long-term, the Government will take further adjustment measures to minimize the impact. Additional earnings beyond the projected levels would be partly used to accelerate the payment of debts, and thus reduce future debt-servicing obligations.

75. As indicated above, the present crisis situation now being faced will lead to a substantial loss in per-capita income and consumption in 1986. However, with the measures under the adjustment programme and the projected balance of payments, a GDP growth target averaging 4 per cent per annum over the rest of the 1980s is feasible. This will allow increases in per-capita GDP and arrest the decline in per-capita consumption. Increased output over the rest of the 1980s will result mainly from the increasing utilisation of existing productive capacity, more selective and sound public investment in key areas and improvements in the productivity of private and public investment as a result of the policy reforms.

76. Investment throughout the period is expected to average around 15 per cent of GDP. With the improved incentive system and more favorable investment climate, it is also expected that there would be a higher ratio of private to public investment, growing to about 40 per cent by 1990. The national savings rate would average around 18 per cent of GDP; public savings over the period are slightly less than public investment but are expected to exceed them in the early 1990s. The anticipated reform of the financial system will be important in the encouragement of private sector savings. Improved revenue mobilisation, control over public expenditures and reform of the parastatals will allow a considerably improved public-sector savings performance. Success of the adjustment programme will also rest heavily on the ability of the economy to expand the trade surplus and ultimately to generate an external current account surplus without resort to administrative controls on imports. Such surpluses are expected to accrue in the early 1990s when the effects of the adjustment programme in encouraging efficient import replacement and non-oil exports would have become evident and when the international oil market would have picked up once more.

II. Debt Management

77. With particular reference to the balance of payments, the crux of Nigeria's external debt problem lies in the structure of the debt, especially in respect of the huge claims under trade arrears. This, along with the bunching of repayments due on medium- and long-term loans, make the debt service burden unsustainable. Without any relief and given the continued depressed state of the international oil market, the debt service to exports ratio would have been 66 per cent in 1986, and even higher in 1987. The structure of public foreign debt outstanding as at the end of 1985 is as follows:

Type	Direct debt	Guaranteed debt 1/	Other	Total
	(In US$ billion)			
International organisations	1.3	--	--	1.3
Bilateral credits (Paris Club)	3.5	1.2	--	4.7
Uninsured bank debt (London Club)	2.7	1.4	--	4.1
Uninsured supplier approvals	0.9	0.1	--	1.0
Foreign exchange approvals	--	--	0.5	0.5
Total medium- and long-term debt	8.4	2.7	0.5	11.6
Reconciled short-term arrears 2/	1.3	--	--	1.3
Total public external debt	9.7	2.7	0.5	12.9
Foreign public debt as percent of GDP				22

1/ Debt guaranteed by the Federal Republic of Nigeria.
2/ Promissory notes issued at 31st December, 1985.

78. Earlier negotiations at refinancing short-term arrears under letters of credit culminated in two separate but identical refinancing agreements in 1983 under which a total of US$2.1 billion was refinanced. As at end of 1985, only ₦ 292 million of the refinanced amount remained outstanding; the final repayment being expected in July 1986. Uninsured creditors agreed to refinance their claims outstanding as at 31st December, 1983 by converting them into floating-rate promissory notes carrying interest at 1 per cent above LIBOR and with maturities of six years, including a two-and-a-half-year grace period in respect of claims verified and accepted by the Central Bank of Nigeria. Promissory notes amounting to US$1,306 million have been issued in respect of reconciled and accepted uninsured claims.

79. Agreement is yet to be reached on refinancing the insured trade arrears, although the Export Credit Agencies have agreed to receive interest with retrospective effect (from 1st January, 1984) on claims if verified and accepted by the Central Bank of Nigeria. As of 31st December, 1985, insured claims totalling US$433 million had been accepted. There are however claims which are yet to be verified and reconciled, with some significant part not likely to turn out authentic. The Government will speed up the process of reconciliation and verification and ensure its early completion.

80. The Government is now also paying attention to the problem area of accumulated internal debts. Their early rescheduling is likely to have a major impact on the process of reviving the economy.

III. External Resource Requirments

81. Faced with the difficult payments prospect, a moderate but firm level of capital inflow is required from the financial community to ease the debt-service burden and to close the financing gap required to support the conservative projected levels of import designed to ensure success of the adjustment process. This will involve the official rescheduling of Paris and London Club debts and of trade arrears, as well as new loan commitments. The rescheduling must be such that would allow the debt-service ratio to be no more than 30 per cent in 1986 and about 20 per cent in 1987.

F. Monitoring and Implementation Mechanism

82. The Government recognises that in a period of economic crisis, programmes and policies, no matter how soundly formulated, become empty words unless they are vigorously implemented. The Government is therefore determined to pursue at all levels of administration, a strategy of close monitoring of all policies and measures enunciated in this programme. The existing mechanisms and procedures are being re-examined to ensure that all facets of the present programme are implemented energetically. Periodic targets and specific tasks have been assigned to various Ministries and Agencies to ensure that performance keeps pace with the programme expectations.

83. A number of issues have been identified in this programme which would require further review, examination or evaluation. Of particular urgency in this regard are:

(a) Monitoring of the Second-tier foreign exchange market.

(b) Export incentives, procedures and documentation.

(c) Restructuring of on-going major industrial projects in the public sector.

(d) Privatisation of some parastatals.

(e) Industrial incentives system including the array of approvals, permits and sanctions.

84. It would be relevant to mention that a number of inter-ministerial committees or special panels have already been set up with specific terms of reference to carry out the implementation of some of the above measures. Indeed some have already completed their assignment. In a number of cases, the Government has even already acted on the recommendations of these committees. Other reports will be considered in due course. This has been done to ensure that the pace of implementation of the measures specified in this programme is not slowed down by lack of prior decisions.

85. Two monitoring techniques have been adopted to ensure that the programme is faithfully implemented. First, where possible targets have been set for certain key variables such as balance of payments and output growth. Ceilings have been set on Government fiscal deficit, overall credit expansion to the economy with sub-ceilings on credit to government and the private sector. Secondly, periodic reviews will be undertaken on the extent of programme implementation to enable timely corrective measures to be effected and also to set targets for the subsequent sub-periods of the programme.

86. For full and proper implementation of the adjustment programme, the monitoring capability of the appropriate Ministries will be specifically strengthened. In addition, a Monitoring Unit comprised in the main of the Cabinet Office, Finance and National Planning Ministries has been established to jointly monitor the implementation process. No Ministry or Agency will be allowed to depart from the approved programme, unless under exceptional circumstances which must be cleared with the Monitoring Unit and approved by the President.

FEDERAL GOVERNMENT BUDGET

	1985	1986 Budget	1986 Projected	1987 1/	1988 1/
TOTAL RETAINED REVENUE	9.32	10.46	11.04	16.96	20.89
PETROLEUM	5.14	4.80	5.17	8.80	11.44
NON-PETROLEUM	2.21	3.77	2.66	3.60	5.11
Inland Revenue	0.58	-	0.63	0.75	0.89
Customs	0.57	-	1.02	1.44	2.20
Excise	0.26	-	0.33	0.60	1.07
Other	0.80	-	0.68	0.81	0.96
INDEPENDENT	1.97	4.10	3.20	4.56	4.34
Import Levy	0.00	-	0.98	1.43	0.00
Other	1.97	-	2.23	3.13	4.34
CURRENT EXPENDITURES	7.68	5.60	8.04	10.38	15.42
Wages	1.49	-	1.60	1.72	2.14
Operation and Maintenance (Current)	1.77	-	2.14	3.46	5.10
Operation and Maintenance (Constant 86 Price)	(2.31)	-	(2.14)	(2.50)	(2.68)
Operation and Maintenance Deflator	(77)	-	(100)	(138)	(191)
Domestic Interest	2.54	-	2.60	2.69	2.75
Foreign Interest	0.63	-	1.03	1.73	4.55
Grant and Subsidies	1.25	-	0.67	0.78	0.89
CAPITAL EXPENDITURES					
Investment (Current)	3.36	4.29	3.13	6.32	8.26
Direct Investment	2.87	-	2.63	5.74	7.60
Lending to Parastatals	0.49	-	0.50	0.58	0.66
Investment (Constant 1986 Price)	(4.65)	-	(3.13)	(3.90)	(3.40)
Investment Deflator	(72)	-	(100)	(162)	(243)
Net Lending to States	-0.29	-	0.23	0.26	0.30
Deficit (- = Financing Need)	-1.71	-1.09	-0.36	0.00	-3.09
Deficit/GDP (- = Surplus)	2.67	-	0.50	0.00	2.50
FINANCING					
Foreign Borrowing	-0.49	-	-0.66	0.39	0.04
Gross	0.68	-	0.67	0.92	1.58
Amortization	-1.17	-	-1.33	-0.53	-1.54
Domestic	2.21	-	1.02	-0.39	3.05

NOTE: 1/ Subject to revision

PROJECTION OF FEDERAL GOVERNMENT BUDGET

1. REVENUE

1.1. Petroleum Revenue - Based upon revenue sharing formula. An increasing proportion of the revenue derived from oil exports is transfered to the Federation Account at the second tier rate. This item also includes revenues derived from domestic oil consumption.

1.2. Non-Petroleum Revenues

1.2.1. Inland Revenue - These are projected to remain at the same proportion of GDP in 1987 (about 2 per cent).

1.2.2. Customs - Projected at 20 per cent of Naira value of imports.

1.2.3. Excise - 3 per cent of GDP in 1985 and share grow by 2 per cent each year thereafter.

1.2.4. Other - Projected to remain about 2 per cent of GDP throughout the period.

2. CURRENT EXPENDITURES

2.1. Wages - Projected to remain constant in 1986 in nominal terms. They subsequently increase so as to compensate for 50 per cent of inflation.

2.2. Operation and Maintenance - The 1986 level is the budget estimate. It is then projected in 1987 to equal the real level of expenditure of 1985 and to grow by 7 per cent in real terms in 1988 and 1989. The deflator is obtained by assuming a 30 per cent import content in 1985.

2.3. Domestic Interest Calculation - Based upon a stock of 24 billion naira of treasury bills and certificates at the end of 1985, the interest due each year starting in 1986 on them is about 2 billion naira. Interest on domestic deficit throughout the projection period is also paid from 1987 onwards.

2.4. Foreign interest - Calculated as the share of government in total foreign loan interest.

2.5 Grants and Subsidies - These are cut in half from their 1985 level. They remain at their 1986 level in real terms for the rest of the projection period.

3. CAPITAL EXPENDITURE

3.1. Lending to Parastatals - Assumed to remain constant at its real 1986 level for the projection period.

3.2. Direct Investment - Calculated as a residual to be consistent with target deficits. The deflator is calculated assuming 60 per cent foreign component.

NIGERIA: BALANCE OF PAYMENTS
(IN BILLIONS OF U.S. DOLLARS)

ANNEX II

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
MERCHANDISE TRADE, F.O.B.	4.27	1.08	0.75	1.47	2.32	3.08	3.60	4.46	5.29	6.09	6.85
EXPORTS	12.56	7.08	8.15	9.51	11.02	12.44	13.63	15.20	16.80	18.41	20.05
PETROLEUM	12.20	6.68	7.65	8.77	10.19	11.46	12.56	14.02	15.48	16.94	18.40
OTHER	0.36	0.40	0.50	0.74	0.83	0.98	1.07	1.18	1.32	1.47	1.65
IMPORTS	-8.29	-6.00	-7.40	-8.04	-8.70	-9.36	-10.03	-10.74	-11.51	-12.32	-13.20
NONFACTOR SERVICES BALANCE	-1.34	-0.90	-1.15	-1.28	-1.35	-1.44	-1.53	-1.62	-1.71	-1.82	-1.94
EXPORT OF NFS	0.29	0.30	0.33	0.33	0.39	0.44	0.48	0.53	0.59	0.64	0.70
IMPORT OF NFS	-1.63	-1.20	-1.48	-1.61	-1.74	-1.87	-2.01	-2.15	-2.30	-2.46	-2.64
GOODS AND NFS BALANCE	2.93	0.18	-0.40	0.19	0.97	1.64	2.07	2.84	3.58	4.27	4.91
INTEREST ON M&LT DEBT	-1.44	-1.04	-0.85	-0.68	-0.53	-0.40	-0.31	-0.24	-0.20	-0.14	-0.09
PARIS CLUB	-0.38	-0.42	-0.38	-0.31	-0.24	-0.17	-0.12	-0.08	-0.05	-0.03	-0.01
LONDON CLUB	-0.55	-0.41	-0.29	-0.18	-0.10	-0.05	-0.03	-0.02	-0.01	0.00	0.00
MULTILATERAL	-0.08	-0.13	-0.14	-0.15	-0.15	-0.15	-0.14	-0.12	-0.11	-0.10	-0.08
OTHER MLT	-0.43	-0.08	-0.04	-0.04	-0.04	-0.03	-0.02	-0.02	-0.03	-0.01	0.00
INTEREST ON PRIVATE DEBT	-0.05	-0.04	-0.03	-0.03	-0.02	-0.01	-0.01	0.00	0.00	0.00	0.00
INTEREST ON ARREARS		-1.10	-0.34	-0.22	-0.09	-0.02	0.00	0.00	0.00	0.00	0.00
INTEREST ON RESERVES		0.06	0.07	0.07	0.07	0.07	0.06	0.06	0.06	0.06	0.06
INTEREST ON FINANCING GAP		-0.16	-0.50	-0.84	-1.10	-1.20	-1.20	-1.20	-1.20	-1.20	-1.20
OTHER INVESTMENT INCOME	-0.29	-0.21	-0.22	-0.23	-0.24	-0.26	-0.27	-0.28	-0.30	-0.31	-0.33
NET TRANSFERS	-0.26	-0.27	-0.32	-0.34	-0.36	-0.40	-0.41	-0.41	-0.41	-0.41	-0.41
OTHER NET PRIVATE TRANSFERS		0.10	0.20	0.20	0.20	0.20	0.20	0.30	0.30	0.30	0.30
CURRENT ACCOUNT BALANCE	0.69	-2.48	-2.39	-1.88	-1.11	-0.37	0.13	1.07	1.83	2.57	3.25
CAPITAL ACCOUNT BALANCE	-0.72	-1.57	-2.63	-2.68	-2.40	-0.74	-0.21	-0.09	0.06	0.36	0.56
DIRECT FOREIGN INVESTMENT	0.35	0.40	0.50	0.55	0.60	0.65	0.70	0.75	0.80	0.85	0.90
M&LT DISBURSEMENTS	1.71	1.22	0.92	0.60	0.37	0.26	0.10	0.00	0.00	0.00	0.00
M&LT AMORTIZATION	-2.82	-3.18	-2.64	-2.34	-1.88	-1.20	-0.94	-0.76	-0.67	-0.43	-0.28
PARIS CLUB	-0.43	-0.96	-1.12	-1.09	-0.94	-0.68	-0.51	-0.39	-0.33	-0.21	-0.09
LONDON CLUB	-1.26	-1.43	-1.29	-0.99	-0.66	-0.25	-0.17	-0.12	-0.10	0.00	0.00
OTHER M&LT	-1.13	-0.79	-0.23	-0.26	-0.28	-0.27	-0.26	-0.25	-0.24	-0.22	-0.19
AMORTIZATION OF ARREARS	0.00	-0.34	-1.37	-1.37	-1.37	-0.34	0.00	0.00	0.00	0.00	0.00
SHORT TERM CAPITAL	0.08	0.28	0.05	-0.04	-0.06	-0.05	-0.03	-0.06	-0.06	-0.05	-0.05
NET PRIVATE	-0.04	0.05	-0.09	-0.08	-0.06	-0.06	-0.04	-0.02	-0.01	-0.01	-0.01
OVERALL BALANCE	0.17	-4.05	-5.02	-4.56	-3.51	-1.11	-0.08	0.98	1.89	2.93	3.81
NET OFFICIAL RESERVES(-,INC.)	-0.30	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
GROSS OFFICIAL RESERVES (EOP)	1.69	1.79	1.89	1.99	2.09	2.19	2.29	2.39	2.49	2.59	2.69
FINANCING GAP	0.00	4.15	5.12	4.66	3.61	1.21	0.18	-0.88	-1.79	-2.83	-3.71

ASSUMPTIONS USED IN THE BALANCE OF PAYMENTS

1. EXPORTS

1.1. Oil Exports - Oil price and quantity projections are shown in table below . The price projection for the rest of the 1980's rise from $15 in 1986 to $16.5 in 1987, thereafter rising steadily to $20 by 1990. It is predicted that there will be a recovery in the world oil market by the mid 1990s, with prices rising to $31.5 for Nigerian crude by 1995. Oil export volumes are estimated conservatively at an average of 1.22 mbd in 1986 rising to 1.27 mbd in 1987 and 1.57 mbd by 1990. Oil exports are projected to remain constant at 1.6 mbd over the period 1991-85.

1.2. Non-Oil Exports - Based on an estimate of $0.3 billion in 1985, these are assumed to go up about 20 per cent per year in nominal terms over the adjustment period, reflecting the impact of the policy reform measures and the low starting base. From 1990 onwards non-oil exports are assumed to grow at about 10 per cent per annum.

1.3. Non-Factor Services Exports - Based upon past relationships. This item was on average 3 per cent of goods exports. Taking into account the new incentive measures it is projected at 3.5 per cent of goods exports.

2. IMPORTS

2.1. Imports - 1986 imports are calculated at a feasible level of $6 billion. Due to the anticipated financial support in 1987, imports are projected rise to $7.4 billion in current prices and grow by 3 per cent a year in real terms thereafter.

2.2. Non-Factor Services Imports - These are projected at 20 per cent of the level of the imports of goods, based on the historical relationship between imports of goods and non-factor services in Nigeria.

3. INTEREST - Is equal to interest due on debt outstanding provided by the World Bank, to this amount interest on future World Bank disbursements, rescheduled debt and commercial borrowing is also added. LIBOR, the base rate used in these projections, is estimated at an average rate of 7.5 per cent in 1986, 8 per cent over the period 1987-90 and thereafter at 7.5 per cent per annum.

4. NET TRANSFERS - Projected to remain fairly constant at their real 1985 level throughout the projection period.

5. OTHER NET PRIVATE TRANSFERS - In response to new incentives, which will encourage private investment, this item is projected to go up by $50 million for each year of the projection period from the level of $350 million in 1985.

6. DIRECT FOREIGN INVESTMENT - In response to new incentives, which will encourage private investment, this item is projected to go up by $50 million for each year of the projection period from the level of $350 million in 1985.

7. MLT Disbursement - This is the sum of projected disbursements based upon the present commitments.

ASSUMPTION USED IN THE MACRO-ECONOMIC PROJECTIONS

1. GDP Growth is the weighted sum of its components below.

1.1. Oil Sector - Growth is based upon production volumes used in the balance of payments.

1.2. Agriculture and Industry - Growth rates set exogeneously to reflect new incentives. Industry growth is expected to be mostly due to better capacity utilization. Note that service sector growth is below industry and agriculture but chosen to be consistent with target growth.

2. INVESTMENT - Separate projections are made for public and private investment. The former is mostly Federal investment which is obtained from the analysis of government budget. The latter is based upon past relationships between private investment and some major macro-economic variables, adjusted to take into account new incentives.

3. SAVINGS - Gross domestic savings are calculated from the national account identity and is equal to Investment plus balance on traded goods and non factor services.

4. NOTE - Incremental capital output ratios implicit in the calculations are based on constant 1984 prices. The calculations under-estimate investment which has high import content component which is calculated at an overvalued exchange rate.

MACRO ASSUMPTIONS

	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Exogenous World Price Parameters												
Import Price Inflation	--	0.009	0.095	0.070	0.055	0.050	0.045	0.045	0.040	0.040	0.040	0.00
Import Price Index	100.0	100.9	110.5	118.2	124.7	131.0	136.9	142.3	148.0	153.9	160.1	166.5
Libor % (Dollar Denominations)	--	--	7.5	8.0	8.0	8.0	8.0	7.5	7.5	7.5	7.5	7.5
Nigerian Price Parameters												
Real Exchange Rate for Goods and Services	--	1.00	0.86	0.71	0.60	0.38	0.38	0.38	0.38	0.38	0.38	0.38
Average Exchange Rate	1.31	1.12	0.85	0.65	0.50	0.30	0.28	0.27	0.25	0.23	0.22	0.21
Domestic Inflation	37.3	10.0	24.0	16.0	14.0	12.0	10.5	10.5	10.5	10.5	10.5	10.5
Oil Sector Production												
Oil Price ($ per barrel)	29.07	27.50	15.00	16.50	17.50	19.00	20.00	21.50	24.00	26.50	29.00	31.50
Oil Production (mbd)	1.393	1.490	1.450	1.500	1.600	1.700	1.800	1.835	1.839	1.844	1.849	1.854
Oil Consumption (Domestic) (mbd)	0.301	0.250	0.230	0.230	0.230	0.230	0.230	0.235	0.239	0.244	0.249	0.254
Oil Exports (mbd)	1.092	1.240	1.220	1.270	.370	1.470	1.570	1.600	1.600	1.600	1.600	1.600
Oil Cost ($ per barrel)	3.90	3.91	4.28	4.58	4.83	5.07	5.30	5.52	5.52	5.74	5.97	6.20

MEDIUM AND LONG-TERM DEBT OF THE FEDERAL REPUBLIC AND STATES OF NIGERIA AS AT 31ST DECEMBER, 1985 (US$ MILLIONS)

Medium and Long-term Debt	*Direct Debt*	*Guaranteed Debt* (1)	*Other*	*Total Foreign Debt*
International Organisation	1,344	—	—	1,344
Bilateral Credits				
Government Credits	(400)	(—)	—	(400)
Export Credits and Guarantees	(3,073)	(1,237)		(4,310)
Total Bilateral Credits	3,473	1,237	—	4,710
Uninsured Bank Debt Credits	2,680	1,382	—	4,062
Uninsured Supplier Credits	900	60	—	960
Foreign Exchange Approvals (State Non-guaranteed Debt)	—	—	480	480
Uninsured Promissory Notes	1,309	—	—	1,309
TOTAL, FOREIGN PUBLIC SECTOR DEBT	9,706	2,679	480	12,865

(1) Debt guaranteed by the Federal Republic of Nigeria.

(2) Approved claims at 31st December, 1985.

TOTAL EXTERNAL DEBT OF THE FEDERAL REPUBLIC OF NIGERIA AS AT DECEMBER 1985

(US$ million)

	₦
Medium and Long-term Public Debt (from Annex IV)	12,865
Private (non-guaranteed)	420
Short-term trade arrears [1]	4,410
Uninsured	(2,640)
Insured	(1,770)
TOTAL, EXTERNAL DEBT	17,695

[1] These are tentative estimates subject to reconciliation and verification. These estimates include $920 of interest arrears. The MLT total of $12,865 million includes a total of $1,309 in promissory notes issued on the uninsured trade arreas as of December 31, 1985.

PUBLIC EXPENDITURE ALLOCATIONS: CAPITAL EXPENDITURES

Sector	Naira million (current prices)			
	1986	1986	1987 1/	1988 1/
	Budget	Likely Outcome	Projected	
Agriculture and Water Resources	893	602	1,181	1,529
Mining and Quarrying	88	60	167	241
Oil and Gas	400	321	667	966
Transport	418	351	972	1,288
Industries	606	502	903	1,207
Power	121	100	236	402
Housing and Urban	260	181	361	483
Communications	98	80	181	241
Education	449	301	431	563
Health	81	70	181	241
Commerce and Finance	206	100	139	161
Other and Unallocated	581	461	903	936
TOTAL	4,290	3,130	6,320	8,260

1/ Subject to revision.

FORM NO. 75
(6-83)

THE WORLD BANK/IFC

ROUTING SLIP	DATE: 5/13

NAME	ROOM NO.
Mr. Choksi	N-623

	APPROPRIATE DISPOSITION		NOTE AND RETURN
	APPROVAL		NOTE AND SEND ON
	CLEARANCE		PER OUR CONVERSATION
	COMMENT		PER YOUR REQUEST
	FOR ACTION		PREPARE REPLY
	INFORMATION		RECOMMENDATION
	INITIAL		SIGNATURE
	NOTE AND FILE		**URGENT**

REMARKS:

We spoke. This is the version of the paper submitted by the Committee to the Secretary of Government.

FROM:	ROOM NO.:	EXTENSION:
W.S. Humphrey	E-327	78058

THE WORLD BANK INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

→ Nigeria. [redacted]

DATE: May 10, 1986

CONFIDENTIAL

TO: Mr. Bilsel Alisbah

FROM: W. S. Humphrey

EXTENSION: 7-8059

SUBJECT: NIGERIA - Work on Government Medium-Term Program Paper

1. Three weeks ago the Government appointed a Committee to draw up a paper for Nigeria's creditors setting out a medium-term adjustment program, building on the 1986 budget and including additional measures on exchange reform, public expenditure and parastatal reform. Last Friday the Committee submitted its report to the Secretary to the Federal Military Government. When I left Nigeria on Thursday evening the Committee was working far into the night putting the last polish on the attached draft in which all substantive points had been settled. The summary still had to be agreed and some of the figures reconciled. ||

2. The Committee was chaired by Mr. Okin, Director of Revenue and Research in the Ministry of Finance. It contained members at equivalent levels from the Cabinet Office, Central Bank and Ministry of Planning. The Secretariat was provided by the Ministry of Finance. There were a number of all-day sessions, the Chairman's approach being to allow discussion on each item to go on until a consensus emerged. Although this lengthened the process, it meant that the Committee members fully identified themselves with the conclusions.

3. The Bank staff worked as full members of the Committee from the start. It was a true joint effort in which we were treated as colleagues not as outsiders. Ishrat Husain ably led our team with Paul Isenman participating for one week. Tom Allen and Iradj Alikani were involved in all the work while T. Swayze and I participated in about half the sessions while we were there. During the first week and a half the Committee discussed various working papers on different topics submitted by its members, including ourselves, and reached decisions on principle substantive issues. We were then invited to produce a first draft of the final paper, reflecting the Committee's substantive decisions. This draft was then discussed line by line in a series of all-day sessions. Sometimes two or three lines were debated for an hour, but a consensus was always reached.

4. The two areas which caused the most intensive and lengthy discussion were the design of the second tier exchange market and composition of public expenditure. The overall size of the expenditure program caused little debate since this followed from the agreed assumptions on oil earnings, exchange reform and the size of the budget deficit in relation to GDP.

5. The Committee had a mandate to recommend the main features of a second tier market scheme. It would have been better if we could have waited for IMF advice on this, but we had to pitch in and help

|| Mr Stern
I attach the final version which arrived this afternoon
WS

P-1867

especially since the government's preliminary ideas were clearly unsatisfactory. What emerged is summarized in paras. 36-37 of the Report. This design will clearly need further reshaping by our IMF colleagues. We emphasized this and also said that a much faster move to a unified rate would be highly desirable. The Annex to the paper on the scheme is not attached since it is being reviewed by Mr. Quirk of the IMF in Lagos this week. We spent a lot of time convincing our Nigerian colleagues not to overcontrol access to the second tier market.

6. The Bank's public expenditure report was reviewed in detail at a long separate meeting chaired by the Ministry of Planning with representatives of the sectoral ministries and Bank project staff from Agriculture, Transport, Education and PHN. While the representatives of the sectoral ministries tended to resist all cuts, the Ministry of Planning official in charge of each sector broadly supported our views. The main area of disagreement, as we expected, were our recommendations to reduce drastically proposed expenditures in the steel and petrochemical sectors. The outcome of the meeting was referred to the Committee. After some hard discussion the outstanding issues were resolved and we emerged with a composition of public expenditure in line with our report. The Committee has recommended that the programs for steel and petrochemicals be studied and, if necessary, restructured with World Bank help. Until this has been done expenditures on the doubtful elements will be minimized.

7. On parastatal reform, recent government announcements provided the framework and the Committee easily reached agreement. There were relatively few problems on monetary and fiscal management. The Committee adopted our recommendations on rescheduling and new money.

8. The macroeconomic, balance of payments and fiscal projections, were a true joint effort. The Committee agreed the major assumptions and Iradj Alikani and his counterpart from the Central Bank sat in front of the IBM-PC at the Bank's office discussing each subsidiary assumption, plugging it in and coming back to the Committee with runs for further advice. As you can see from the Annexes, we have a plausible, if tight, scenario following rescheduling and the injection of new money. Imports rise gradually from their very austere 1986 levels, real GDP growth keeps ahead of population growth and the fiscal position benefits by the exchange adjustment.

9. The oil price assumptions are, of course, crucial. The Committee chose forecasts midway between the IMF's "$15/barrel in 1986 maintained in real terms" formula and the Bank's somewhat higher EPD projections at the date we left Washington. The Nigerian members made very conservative production and export assumptions, since they wanted to be consistent with their position within OPEC as advocates of production restraint. If OPEC remains in disarray, Nigeria will almost certainly export at higher levels than those shown. Assuming that the price projections are neutral, this gives the overall projections a conservative bias.

10. We understand that the procedure for processing the Committee's report will be as follows. It will be sent, without further interdepartmental review, by the Secretary to Government to the Presidential Advisory Committee (PAC). This is a committee of "wise men" outside government, chaired by Professor Aboyadi of the University of Ibadan. Then it will go on to the Council of Ministers (FEC) with the PAC's comments. The FEC's comments and the PAC's comments will accompany the report when it is considered by the Armed Forces Ruling Council (AFRC). Any amendment mandated by the AFRC will be incorporated before the report is submitted formally to the IMF and ourselves, hopefully by June 1.

11. Assuming this procedure is followed, it is important that any informal feedback from IMF staff and senior Bank staff is made as soon as possible. The visit of IMF staff to Lagos this week with Messrs. Ouattara and Allen following on May 18, should provide an opportunity for this. I promised Ishrat that we would try to get a quick reaction from Messrs. Stern and the Regional Management as soon possible, so any additional suggestions can be made before the paper reaches the AFRC. I am also sending the paper to my colleagues on the Nigeria Working Group.

12. When I left Nigeria, the mission led by Mr. Bhargava to work on the "second tier" Bank loan had just begun work. It will be working closely with Mr. Quirk of the IMF in the course of this week with the aim of coming up with a detailed proposal be the end of May.

13. At present the report is regarded by the Government as highly confidential since it has not yet been reviewed by the FEC and AFRC. In theory, only those authorized by the Secretary to Government are supposed to read it (the Nigerian members were asked not to show it to their own superiors, though I think most of them did). We recommended it be given to the IMF staff immediately on their arrival on Monday. Because of the sensitive nature of the paper, I have numbered the copies being distributed at Bank headquarters.

cc: Messrs. Stern, Thalwitz, O'Brien, Eccles, Isenman, Beguery
Dubey, Vibert, Morais, Rischard, Larkum,
WA1NI staff.

MEDIUM-TERM ADJUSTMENT PROGRAMME: JULY 1986 - JUNE 1989

SUMMARY

1. In the face of the current weakness and uncertainty in the world oil market and the mounting debt service burden, the Government has decided to substantially increase the pace of policy reforms articulated in the 1986 Budget and to seek support from the international financial community for their success. These reforms are designed to correct distortions and other long term structural problems facing the economy. The recent substantial decline in oil prices coupled with the bunching of Nigeria's debt service obligations over the next few years have exacerbated the problems. Given the magnitude of these problems, it has become obvious that policy reforms by themselves would not be adequate. Therefore, assistance from the international financial community is needed to help Nigeria achieve growth.

2. Nigeria's debt crisis relates not so much to the size of the debt, but to the unfavourable repayments profile. If Nigeria can spread the burden over a number of years and obtain reasonable levels of new finance on extended terms, then a viable and more resilient economy can emerge. The Government appreciates the recent moratorium on debt repayments granted by commercial bank creditors which has provided some breathing space to put together this adjustment programme. World Bank and IMF endorsement for the reform programme has been sought.

Policy Reforms

3. The main aims of the programme are:

(i) to achieve renewed growth and financial stability;

(ii) to improve the efficiency in the use of existing and additional resources;

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

(iv) to lessen the dominance of the public sector and enhance the role of the private sector.

The core policies involve actions to: (i) correct the overvaluation of the Naira through the setting up of a viable second-tier foreign

which is what?

exchange market and adjustments to the official rate, with the aim of integrating the two markets within the programme period; and (ii) improve public expenditure programmes and the speedy rationalization of the parastatal sector. Other policy reforms which are vital include the liberalisation of trade and price controls, adoption of appropriate interest rates, installing a system of export incentives that encourages non-oil exports and introducing fiscal measures that encourage efficient import replacement. Strict constraints have been placed on the budget deficit and a tight monetary policy will be pursued during the programme period.

Recent? regulations?

4. Exchange Rate Adjustment: The second-tier foreign exchange market will cover a significant and progessively increasing share of external transactions at market-determined exchange rates. Under this framework market forces would increasingly replace administrative controls on imports. The foreign exchange earnings from non-oil exports would be channelled through this market. To give the market an initial spurt, the Government will channel an increasing proportion of its oil revenues through the market and will request commecial banks and the World Bank to supplement these funds. The programme calls for at least $2.5 billion to move through the market within the first calender year of the scheme -- i.e., 1987.

Scale of operation? Size?

5. Improved Public Sector Performance: The Government will revise its expenditures by reorienting their composition and scope to match available resources. A system of public expenditure planning and budgeting which recognizes the uncertainties of oil revenues will be institutionalised and operated within the framework of the three-year adjustment programme. Priorities have been set for the completion of projects on the basis of economic viability and completion costs. Projects of doubtful viability will be re-examined with a view to restructuring or rephasing them. Those that can not be made viable even in the long run will be abandoned. Only few new projects will be commenced but in any case, within each sector, maintenance and supplies needed for efficient operation of existing assets will be given priority over new investment. Transfer of public funds to commercially-oriented parastatals to cover operating deficits will be eliminated during the programme period, while in respect of capital expenditures, such parastatals will be required to increasingly rely on the capital market. Within the context of development strategies for the sectors in which they operate, detailed programmes for the privatisation/commercialisation, winding up or rationalisation of parastatals are being prepared. Commercial orientation and increased autonomy and accountability form the cornerstone of the rationalisation programmes.

?

Prices? Pressures?

6. It is recognised that it will take a number of years to restructure the economy and increase the share of the non-oil sector. Over these years, oil will remain a significant force in the economy, although solid foundations will have been laid for the transition to a more balanced economic structure. While considerable growth in non-oil exports can be expected, the small base from which they are starting means that they cannot be a major force in the national development effort until well into the 1990's. In the

short-run most growth will come primarily from improved capacity utilisation and the efficient production of import substitutes. However, the impact of macro and sectoral policy changes that will be pursued during the programme will encourage more efficiency in agriculture and industry. This will ensure an increasing share of these sectors in the production and consumption structure of the economy, thereby leading to significant increase in the domestic resource content of production for both the domestic and export markets.

Financial Plan

7. A significant but firm level of support from the international financial community is needed. The programme's financing plan is based on conservative forecasts of the oil market. With the policy measures and financing package in place, the achievement of these forecasts would lead to a GDP growth of an annual rate of about 4 percent up to 1990. In the event oil revenues are higher than projected, the additional foreign exchange earnings would be used to increase imports and external reserves as well as reduce external debt obligations. If, however, oil revenues fall below the projected level, the Government will take appropriate additional adjustment measures.

8. The Government envisages a multi-year rescheduling of 100 percent of the principal of medium- and long-term loans falling due to Paris and London Club creditors in 1986 through 1991 with repayment spread over five years beginning in 1992. Repayment of principal on the outstanding verified and accepted arrears on the similar terms is also assumed in the financing plan. However, even with these rescheduled terms, there will be an external resource gap. Consequently, the financial plan assumes new loan commitments averaging $1.4 billion a year during the programme period.

9. The sharing of the new financing should result in an equitable spread of risks. The World Bank has indicated that it would be willing to increase its lending to about $700 million per annum during the programme period. Half of this amount would be in the form of quick disbursing loans. Commitments of about $200 million a year are expected to from multi-lateral institutions such as the African Development Bank and European Investment Bank. New loans of about $500 million a year from the London and Paris Clubs are expected to provide the remaining financing requirements.

MEDIUM-TERM ADJUSTMENT PROGRAMME

July 1986 - June 1989

I. BACKGROUND: THE EMERGENCE OF THE ECONOMIC CRISIS

1. The oil boom (1973-80) brought with it fundamental changes in the Nigerian economy. The principal aim of the Nigerian decision-makers over this period was to convert the growing oil revenues into investments in social, physical and economic infrastructure. While significant progress was made in a number of sectors - primary school enrollment doubled, power generating capacity tripled and refining capacity quadrupled - some public investment projects were undertaken which have been found to be unviable, questionable in their design and probably beyond the implementation capacity of the Government agencies. Further, the policies pursued led to structural changes which resulted in an economy with substantial price distortions and vulnerability to external shock. First, the economy became heavily dependent on crude oil. By the beginning of the 1980s, the oil sector accounted for 22 percent of GDP, 81 percent of government revenues and 96 percent of export earnings. Second, the competitiveness of the agricultural sector - the major source of GDP and exports before the oil boom - was eroded by the effects of an appreciating Naira, inadequate pricing policies and rural-urban migration. The sector's share of GDP had fallen from around 40 percent of GDP in the early 1970s to 20 percent in 1980. Third, expenditure and production became highly dependent on imports. By 1980, imports had reached a level equivalent to one-quarter of GDP, double the ratio prevailing in the immediate pre-boom years. Nigeria became a major food importer and greater wealth enhanced conspicious consumption of imported luxury goods. The structure of incentives and controls encouraged manufacturing production based on imported inputs. Finally, the public sector came to play a dominant role in the economy, accounting for around half of Nigeria's GDP and two-thirds of modern sector employment at the start of the 1980s. The Enterprises Promotion Decree of 1972 set the basis for the Government's large-scale participation in the banking, insurance and industrial sectors. By 1980, there were around 70 non-commercial and 110 commercial federal parastatals, many of which needed financial support to cover operating losses.

2. The economy was thus ill-equipped to handle the collapse in the world oil market which began around the middle of 1981. The dramatic reduction in crude oil production and the fall in oil prices led to a sharp deterioration in public finances and export revenues. Partly because of expectations that the downturn would be short-lived the Federal and State Governments were at first reluctant to come to grip with the situation and curb expenditures accordingly. For example, ambitious public investment programmes continued to be implemented. Sizeable external and fiscal imbalances occured. External reserves fell abruptly and at the same time there was a large scale accumulation of trade arrears on top of substantial public borrowing to finance the investment programmes. The fiscal

and other austerity measures pursued since 1984 were not without considerable costs. The drastically reduced supplies of raw materials and spare parts to the import-dependent industrial sector led to plant closures, a substantial drop in capacity utilization and extensive layoffs of the work-force. Severe shortages of goods led to very high prices for many essential goods. Investment as a proportion of GDP halved between 1981 and 1985 (to 14 percent) with private investment shrinking at a faster rate than public investment. Cut-backs across-the-board in public expenditure meant further delays in completing viable projects thus escalating their costs and depriving the economy of their benefits. Even after allowing for a slight upturn in 1985 as a result of increased oil production and improved harvests, GDP in 1985 was some 15 percent lower than at the beginning of the 1980s with per capita GDP and consumption being well below the levels recorded in the early 1970s.

3. External debt service obligations increased tenfold (to 40 percent of exports) and continue to accelerate. The public external debt outstanding and disbursed at the end of 1985 of $13 billion included $11.4 billion of medium and long-term public debt and reconciled short-term arrears of $1.6 billion. The severity of Nigeria's debt situation relates not so much to the size of the debt overhang (which in 1985 amounted to around 140 percent of exports compared with the 255 percent average of all middle income heavily indebted countries) but to the unfavourable payments profile and the poor outlook for the oil market.

4. The combination of the downward trend in world oil market, the policy inadequacies of the past, and the bunching of debt servicing obligations have produced a difficult economic situation adversely affecting the external and fiscal balances. Despite the policy adjustments made during the last two years and more thoroughly in the 1986 budget the recent sharp decline in the oil prices has created the need to deepen and accelerate the process of structural adjustment. Consequently, this medium-term adjustment program (July 1986 - June 1989) sets out the Government strategy to cope with the present crisis. The essence of this strategy is to implement a medium-term reform program aimed at restoring sustained growth and making the economy less dependent on oil. A rescheduling of the existing external debt as well as modest additional external capital are also required in order to maintain imports at a level consistent with the restoration of growth.

B. POLICY ACTIONS TAKEN SINCE 1984

5. The economic and financial situation at the end of 1983, when the armed forces assumed power, remained very difficult.Consequently, the armed forces had to focus their efforts on improving the general economic situation. Policy initiatives were taken to improve the efficiency of public administration, restructuring expenditure policies, fostering financial discipline, reducing the overall fiscal deficit of the Federal and State Governments, cutting imports

sharply, and eliminating the accumulation of further external arrears. The present Administration, which took charge of the affairs of state in August 1985, has furthered those reforms. In addition, it has recognized that austerity without structural adjustment constituted an inadequate response to the economic problems faced by Nigeria. It has already made a start of implementing some of these structural reforms. It has announced, in the President's Budget Speech of December 1985, the launching of a much broader effort at structural adjustment, on which the medium-term reform program proposed here is based. Before turning to that program, it is useful to consider the progress made since 1984. This progress to date is important in itself and also is indicative of the seriousness and commitment with which the Government approaches the further reforms proposed here.

(i) Fiscal Measures

6. The tight fiscal policy pursued since 1984 has enabled the overall public sector deficit to be reduced from 11.6 percent of GDP in 1983 to 2.7 percent in 1985. Despite the recent sharp drop in oil prices, the deficit in the first quarter of 1986 has been maintained at the target level.

7. The reduction in the public sector deficit was achieved by a reduction of expenditures and an increase of revenues. In 1984, the Government's overall expenditure program was cut by 28% in nominal terms (40% in real terms). while the federally collected revenues grew by 9 percent. This trend continued in 1985 as current expenditures were reduced by 36 percent and preliminary figures of Government revenues show an increase of .... percent relative to the 1984 outcome.

8. Recurrent expenditure policy was aimed at with streamlining public sector employment to reduce the burden of wage bill. Public sector wages were frozen and strict limitations were placed on transfers to parastatals and to state government. The State Governments also substantially cut back their expenditures in real terms. All the states introduced budgets for 1985 in which recurrent expenditure was covered by revenue from the federation account plus state generated sources.

9. The capital budget was revised. Its composition was reoriented and its scope reduced to match available resources.

10. Further measures which were aimed to reduce the federal budget deficit were incorporated in the 1986 Budget. Substantial reductions were accepted by public servants in their salaries andfringe benefits and the restraint was continued in hiring staff in a wide range of positions. Transfers to commercial parastatals are being cut to 50% of their 1985 levels. The Government has substantially increased the relative emphasis on the maintenance, and rehabilitation especially in education, health and highways sectors despite an overall reduction in the level of expenditure.

11. A key reform announced in the 1986 budget was the elimination of the subsidy on petroleum products. With the recent developments in the oil market, the price of these products are now above the international price. Other subsidies particularly those on agricultural inputs including fertilizer and other agro service inputs are also under constant review. Already, the subsidy on fertilizer has been reduced from 75% to 25% and this subsidy will be phased out over a three-year period.

(ii) Monetary Policy

12. The macroeconomic strategy pursued by the Government, in addition to austere fiscal measures, relies on tight monetary policies to stabilize the economy and stem inflation. The improvement in public finances has also helped in reducing the growth rate of monetary aggregates. Net domestic assets have grown at an average annual rate of only 10 percent in the last two years. The growth of money supply has slowed to an annual rate of about 10 percent during 1984-85, compared with a 47 percent increase in 1980 and an average of 13 percent in 1981-83. The credit to the Government sector also increased at a slower rate of 15% compared to the actual increase of 28.6% in 1983. The pursuit of tight fiscal and monetary policies, together with a bumper harvest of food crops had an immediate effect on inflation. The inflation rate slowed down to about .... percent in 1985 from an annual rate of 40 percent recorded a year earlier.

13. In order to address distortions in credit allocation caused by the level as well as the structure of interest rates that prevailed in the past, the Central Bank has raised nominal interest rates in the last two years. With the decline in inflation, interest rates are now positive in real terms. This reform in monetary policy contributes to the structural adjustment by increasing both incentives for savings and the efficiency of allocation of investment.

14. Since 1969/70 there have been controls on allocation of credit among 18 sectors/sub-sectors. These controls proved to be rigid and unwieldy leaving the banks withlittle discretion in their credit operations. The need to encourage initiative and flexibility on the part of the bank and facilitate greater effectiveness of the Central Bank monitoring efforts led to the regrouping of the sectors/sub-sectors into eight in 1984 and 1985. In 1986, the number of sectors was reduced to four. The credit allocation system will be eliminated by the end of 1987.

(iii) External Sector Policy

15. The balance of payments performance in 1984 and 1985 also reflected the impact of stricter demand management policies pursued by the Government. The current account deficits of 9.8 percent of GDP in 1982 and 6.5 percent in 1983 were transformed into a modest surplus in 1984 and a further 2 percent surplus in 1985. The overall balance recorded a surplus of $1.1 billion in 1984 and $0.5 billion in 1985. These surpluses allowed for some reduction of existing arrears. The gross international reserves increased $1.1 million at the end of 1984 and $1.6 million at the end of 1985.

16. The Government is fully aware that the results achieved in the last two years cannot be sustained without further compression in imports with widespread under-utilisation of industrial capacity and increasing unemployment. The import level has been cut from the 1981 peak of US $18 billion to US $7.4 billion in 1985. The need to compress imports was reinforced by the increasing demands for debt service payments as amortizations on earlier borrowings fall due.

17. Since 1984 the Nigerian Government has allowed the naira to slide against the major foreign currencies. The nominal naira/dollar exchange rate was adjusted downwards by 20% between the end of 1984 and the end of 1985. Similar adjustments were made against the currencies of other major trading partners.

18. The external debt borrowing strategy of the Government has also been cautious and prudent since 1984. Unlike the period 1980-83, when the public external debt outstanding increased from around $4.6 million in 1980 to around $11 billion at the end of 1983, the total new external borrowing has been limited to .... over the last two years. The composition and terms of new borrowing have also shifted drastically. The main borrowings have been from the multilateral creditors such as the World Bank whose financing terms are consistent with Nigeria's long-term development needs. Short-term borrowing at relatively higher interest rate has been generally avoided. Despite the difficult payments situation, Nigeria remained current in its servicing of medium- and long-term debt. It also fulfilled its obligations in meeting the agreement under the refinanced letters of credit concluded in 1983.

~~19.~~ (IV) WAGE AND EMPLOYMENT POLICIES

19. Wage policy guidelines have been used to achieve stabilisation policy targets. In order to reduce public sector expenditure targets and aggregate demand, no general salary increase has been granted public sector employees since 1982. Given the high inflation rates in recent years, this has resulted in a very sharp erosiion of real wages, even if fringe benefits are taken into account. Effective January 1, 1985, the Government has taken measures to recover costs for services provided for public sector employees. The wage policy guidelines for the last three years have put a freeze on private sector wages and salaries as well as fringe benefits. Wage increases will be allowed during the programme year but at less than the rate of inflation until the financial situation improves substantially.

20. Substantial reductions in workforce within parastatals and civil service have taken place since 1984. The recession in economic activity has forced similar cuts and retrenchments in the private sector. Available labour statistics indicate that unemployment rose by 18.8% between 1982 and 1984 and may be even higher today. The Government is deeply concerned with the growing problem of

unemployment and intends to channel more of the available resources to the productive sectors of the economy for creation of more job opportunities.

(iv) Real Sector Policy

(a) Agriculture

21. Government has given high priority to stimulating agriculture. In particular, the Government has cut back sharply the flow of imported agricultural commodities that previously provided a disincentive to domestic agricultural production.

22. A number of important institutional reforms have also been introduced by the present Administration. These have, as a major objective, reducing the role of Government in direct production, increasingly focussing on providing the necessary support services to farmers within an appropriate macroeconomic framework.

23. First, in a major policy initiative announced in April 1986, the Government has removed one constant source of disincentive to farmers by deciding to wind up all the six Commodity Boards by December 31, 1986. The internal and external marketing of these commodities are now open up to private individuals, companies, processors, etc. The decision to wind up the boards which had for long enjoyed monopoly in the purchase and marketing of cash crops was based on the realisation that, on balance, they had become a deterrent to increased agricultural production, and their operations had become costly and inefficient.

24. Second, the River Basin and Rural Development Authorities have also been reduced from 18 to 11 and it has been decided that the RBDAs will discontinue their direct agricultural production activities and focus on the development of water resources. The Agriculture Development Projects (ADPs) which have been developed with the support of the World Bank, will now be the centrepiece for the provision of extension, input supply and infrastructure to the nation's small holders, who are to play the key role in Nigeria's strategy for accelerating agricultural growth. To complement these efforts at the smallholder level a package of incentives has been adopted to encourage companies to invest funds and management skills to develop commercial farms.

25. Third, the Government has also decided to wind up eleven of its companies involved in various agriculture production activities and transfer them to the private sector. The Government is already in the process of privatising four parastatals, namely the Nigerian Dairies Limited, Madara Ltd., the Nigerian Food Company and the Bauchi Abbatoir. In addition, the National Livestock Production and Nigerian Ranches Companies are being wound up. Further enterprises will be privatised or wound-up when the Government has completed the on-going review discussed below.

26. To improve the efficiency and availability of input supply to the farmers throughout Nigeria the Government is also withdrawing from importation, transportation and distribution of fertilizers. Fertilizers will now be imported and distributed by the private sector.

27. As a further step to encourage farmers to stay on their farms and to accelerate the movement of agricultural produce from rural areas to urban centres, the Government has established the Directorate of Food, Roads and Infrastructure which will work in concert with the ADPs in the expansion of rural feeder roads as well as encouraging agricultural production.

(b) Industry

28. The overall strategy of the industrial development has also been shifted from one of a public sector dominance through investment in large capital intensive industries to one of providing the macroeconomic environment and other incentives for the private sector to assume the lead role in manufacturing. The public sector investment is to concentrate more on provision of necessary services and infrastructure. The importance of small and medium scale industrty in providing employment as well as increasing domestic value-added has also been recognised. Provision of credit to small enterprises has been made under a line of credit from the World Bank for this purpose.

29. A relevant reform already in place is the simplification and rationalization of the tariff structure. This was designed to reduce variation in effective protection to local industries. The range of import duties was reduced from its previous extreme variation and for the most part clusters now between 10 and 60 percent. A wide variety of goods that were imported duty free were placed under tariffs. The Approved User Scheme and the General Concessionary Rates of Duty which granted low and concessing rates on imported raw materials and other imported intermediate products were abolished. The specific import duties were replaced by ad-valorem rates. These measures were intended primarily to end the discrimination against domestic resource based industries and discouraged the use of competing imports. The measures were not, however, sufficient to offset the subsidy implicit in the overvalued exchange rate which made the use of imported inputs and raw materials relatively attractive.

30. The import licencing policies were also reoriented to increase the utilisation of capacity of the existing industries. Liberal licences were isssued to the manufacturers rather than general traders and wholesale finished goods importers. To ensure that manufacturing industry does not become excessively protected, the coverage of domestic excise duties was enlarged to include over 300 new products.

A. OBJECTIVES AND TARGETS OF THE PROGRAMME

31. The programme aims at altering and realigning aggregate domestic expenditure and production patterns so as to minimise

dependence on imports, enhance the non-oil export base as well as bring the economy back on the path of steady and balanced growth. Specifically, the major objectives of the programme are:

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

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

(iii) to lay the basis for sustainable non-inflationary growth over the medium and long-term;

(iv) to lessen the dominance of the public sector, improve its efficiency and to tap the growth potential of the private sector.

32. As a first step, a National Economic Emergency Powers Decree was promulgated which empowers the President to issue order and make regulations during a 15-month economic emergency period was promulgated in 1985. Under it, the President is given discretionary powers to put in place measures that will improve the economy. The actions taken thus far under the Decree include reduction in wages and salaries in the public and private sectors and suspension of a number of non-essential projects.

33. The economic performance envisaged under the programme represents a departure from past experience in that emphasis is placed not only on demand management policies but also on supply oriented measures. Consequently, the success of the programme depends, to a large extent, on the speed at which the agricultural and the manufacturing sectors are rehabilitated.

34. Nigeria experienced a persistent decline of approximately 3.6% per annum in real GDP between 1981 and 1984. Apart from the oil sector where output increases were recorded, the other sectors, especially agriculture and manufacturing recorded net declines in absolute terms. Against this background, therefore, the real output targets under the programme are cautiously optmistic. On the whole, the non-oil sector is programmed to attain an average real growth rate of 3.5 a year between 1987 and 1989. The agricultural sector is expected to grow at close to 4 percent a year while the envisaged growth rate of the industrial sector is about 5 per cent per annum. The service sector which has witnessed a fairly rapid growth rate in the past partly as a result of the high scarcity premia attached to the ownership of import licence, commodity distributorship and government contracts, is expected to grow by not more than .... per annum. Finally, a growth rate of around 5 percent in oil production is envisaged over the programme period.

C. MAIN ELEMENTS OF THE 1986-89 MEDIUM-TERM ADJUSTMENT PROGRAMME

35. The main elements of the adjustment programme are:

(i) strengthening of the hitherto strong demand management policies;

(ii) adoption of measures to stimulate domestic production and broaden the supply base;

(iii) adoption of a realistic exchange rate policy;

(iv) further rationalisation/restructuring of the tariffs to aid the promotion of industrial diversification;

(v) move towards trade and payment liberalisation;

(vi) adoption of appropriate pricing policies especially for petroleum products and public enterprises;

(vii) reduction of complex administrative controls with greater reliance on market forces; and

(viii) encourage privatisation and rationalisation of public sector enterprises.

36. The core policies involve actions to: (i) correct for the overvaluation of the naira through the setting up of a viable and substantial second-tier foreign exchange market and adjustments to the official rate, with the aim of a rapid integration of the two markets; and (ii) overcome the considerable public sector inefficiencies through improved public expenditure programs and the speedy rationalisation of the parastatal sector; (iii) to relieve the debt burden and to attract inflow of foreign capital.

37. The following sections describe and amplify the actions that the Government will take during the programme period in addition to the policy actions already taken and proposes to take.

Trade and Exchange Policies

38. The Government is aware that a system of bureaucratic controls is not only cumbersome but is also liable to corrupt practices and to unintended distortions in resource allocation. The medium-term policy objective is therefore to gradually eliminate the existing administrative controls on trade as and when the balance of payments position permits.

39. The central element in the incentive framework is the nexus of policies pertaining to the price and allocation of foreign exchange. These policies have pervasive effects on production and particularly on non-oil exports. The Government is aware of the overvaluation of the naira. It also recognises that the closer the exchange rate is to a realistic level, the less will be the need for the import licensing system, the greater the efficiency in the use of foreign exchange, the higher the level of export earnings in the medium to long term, and the smaller the leakage of foreign exchange through smuggling of goods and black marketeering in currencies.

40. The second-tier foreign exchange market (SFEM) mentioned above is expected, over time, to help provide the monetary authorities with the realistic exchange rate of the naira. To achieve this objective, the SFEM will be allowed to operate under market conditions and be appropriately funded. In addition to private sources of foreign exchange supply to the market, the World Bank has agreed in principle to provide $100 million to the market during the last six months of 1986 and $300 million in 1987. The Government will release $550 million to the market in the second half of 1986 and $1.3 billion in 1987. The magnitude of official funding will depend on the volume of transactions channelled through the market. At its inception, all invisible transactions except those of government will be transferred to the market. Selected visible transactions will also be transferred to the SFEM in 1986. Subsequent transfers to the market will be determined from time to time in light of prevailing circumstances. The objective is to phase out transactions at the official market and achieve a unification of the two markets in 2-3 years. In the meantime, in order to ease the process, the official exchange rate policy will be geared towards narrowing the gap between the rates in the two markets. This will be done by a more rapid crawling down of the official rate. The detailed modalities of the SFEM are being worked out and will be embodied in a Decree to be promulgated so that the market will start operating not later than the end of June 1986. It is hoped that the new exchange rate policy plus other supportive fiscal and monetary policies will have salutary effect on the balance of payments, diversification of the productive and export base of the economy, and enhance the effectiveness of the export promotion policy package. The details of the second-tier foreign exchange market can be seen in Annex I. The new exchange rate policy renders the 30% import levey unnecessary and will therefore be eliminated in respect of import licences not valid for foreign exchange, as soon as the SFEM is put in place (with the exception of luxury consumer goods).

41. To allow free access to the second-tier market the Government will issue import licences which are not valid for foreign exchange automatically for the visible transactions covered by the market. Since the licencing will be automatic, this is a major step toward import liberalization. The Government would also gradually move to partially restore the Open General Licences (OGL) category for priority imports such as agricultural inputs altogether eliminating the licencing for these categories. These moves are intended to reduce the rigidities and the distortions of the cost-price relations that have built up in the economy over the years. The further pace of import liberalisation and transfer to OGL will depend upon the success achieved in the management of the balance of payments.

Non-oil Exports

42. In order to reduce dependence on the oil sector as the sole earner of foreign exchange, the present administration is deeply committed to promote non-oil exports. Although it is realised that the initial base of the non-oil exports has shrunk considerably during the past decade, the government believes that the correction

of cost-price distortions through a realistic exchange rate combined with other positive export incentives and institutional reforms should make it possible for Nigeria to earn at least $1 billion from non-oil exports by the end of the present decade. This would still leave total non-oil exports below the level achieved in 1980. A major thrust of the export drive will be aimed at capturing, among others, the large ECOWAS market which already benefits from a wide range of illegal manufactured goods and commodities from Nigeria.

43. The major policy instrument to achieve this target will be the exchange of export earnings into nairas at the second-tier market rate in addition to retention of 25% of earnings in foreign exchange by the exporters. This step will provide remunerative returns to the Nigerian producers and exporters and strengthen their competitiveness in the international market. There are indications that the manufacturers, traders and bankers have already started reorganizing themselves and are showing interest in export trade.

44. Other complementary measures to assist exports include streamlining and simplifying the now cumbersome process of obtaining necessary documentation for exports, extending the facility of rediscounting short-term bills to all non-oil exports and assuring that exporters readily obtain duty drawback and exemption. The whole package of export incentives will be reviewed from time to time and further improvements made if needed to increase incentives or ease implementation.

FISCAL AND PUBLIC EXPENDITURE REVIEW

45. The financial resources for public expenditures over the rest of the 1980s are likely to be less than previously envisaged. Of particular concern is the extremely tight and uncertain financial situation over the next two or three years. The grim picture in oil markets and the substantial debt repayments falling due will mean that public expenditures especially those involving foreign exchange will have to be severely constrained. While some relief would be available through debt rescheduling and new fund inflows, it is the Government's intention to adjust public expenditures as needed to reflect the revenue constraints, with the aim of containing the budgetary deficits to within 3 percent of GDP. An important implication of the uncertain financial situation is the need to institutionalize a system of public expenditure planning and budgeting which recognizes the uncertaintites and can alleviate their negative impact. For this purpose, the Government will use conservative revenue estimates within the framework of this programme and will concentrate on the timely completion of a limited core of viable on-going capital projects that can be adequately funded.

Criteria for Expenditure Allocations

46. Expenditure reallocations will accompany expenditure reduction to ensure that the net benefits obtained from the limited funds are maximized. The principal considerations in making these decisions are:

(i) Constraints on the growth of the public wage bill will be maintained. Over the last year there has been significant retrenchment in the public sector as well as cuts in net wages and benefits. In the next few years the emphasis will be to hold down the level of public sector employment mainly through a combination of attrition and an extension of the freeze on hiring to all but the most critical skills. Wage increases will be limited to partial compensation for inflation during the programme period while over the longer run, wages for different skills will be allowed to reflect scarcity values.

(ii) Constrained supplies and inadequate infrastructure maintenance have greatly impared the delivery of public services. Levels of supplies (materials, spare parts, small tools and transport) will be increased in a number of sectors to ensure the achievement of reasonable levels of performance. Also, routine and periodic maintenance will have priority over new investment to avoid the rapid deterioration of existing capital assets (eg roads, hospitals, water supply schemes) and in recognition of the higher returns to be gained from the efficient use of this stock. Where extensive rehabilitation is required, it will be judged against new investment on the basis of respective costs and benefits.

(iii) Transfers to parastatals to cover their operating deficits and capital expenditure requirements have been extremely high. Non-statutory transfers to all economic and quasi-economic parastatals will constitute no more than half their 1985 levels. Transfers to fully commercially-oriented parastatals will be eliminated completely by the end of the programme period.

(iv) There is a number of partially completed capital intensive projects, some of which are of doubtful economic viability. The Government recognizes that across the board reduction of allocation to these projects will have to be avoided so that the economy is not burdened by a proliferation of uncompleted and weak projects. Priorities have thus been set for the completion of projects on the basis of their economic viability and costs to complete. Those with high economic viability will be accorded high priority and will be completed expeditiously. Projects with low economic or doubtful viability will be re-examined to see if they can be reshaped both in scope and timing to reduce costs and/or increase benefits; those shown to be non-viable will be dropped. Such evaluation will take account of the expenditures already incurred. The private sector will be invited to take over and complete on-going projects wherever desirable. With few exceptions, no new projects will be commenced over the next three years.

Revenues and Expenditures

47. As a result of the recent adverse development in the world oil market is envisaged that the budgetted federally retained revenue will decline by about .... percent. Using the systems of quarterly allocations based on realised revenues Government intends to adjust its spending commensurate with the available resources. The consequent adjustments are reflected in Annex E. Government will ensure that actual funding follows the priorities as outlined in this annex.

48. Throughout the rest of the 1980s, the favorable revenue effects of a lower average exchange rate will be felt, although these will not alleviate the foreign exchange constraints in the annex. If revenues should exceed those estimated, they will initially be earmarked to further reduce the budget deficit, to a target level of 2 percent with the next highest priority being given to further increasing operation and maintenance expenditures in vital areas and to accelerate completion of priority projects. If, based on quarterly revenue receipts, revenues should significantly fall short of estimates, releases will be scaled down and concentrated on finishing the projects with highest returns. Such supplementary allocations or downward adjustments will be approved by the Monitoring Unit provided under this programme.

Public Investment

49. The rationale for the allocation of public investment expenditures among sectors over the 1986-89 period rests principally on the relative importance of the different sectors in the Government's development strategy, the increased emphasis to be put on the role of the private sector and, for major projects, likely returns on additional funds needed for project completion. The tentative sectoral allocations made in this programme have taken account of project and sector analysis of the World Bank, based on the work of a series of missions related to review of the public expenditure programme. These allocations will be revised subsequently in the light of the findings of various evaluation studies to be undertaken and the priorities to be specified in the Fifth National Development Plan.

50. The capital expenditures in the infrastructure and social sectors will be primarily focussed on periodic maintenance and rehabilitation. The principal exceptions will be: (i) the continued implementation of the Egbin power generating plant and an upgrading/expansion of the transmission and distribution network to ensure a better balance of generation and distribution capacities; (ii) the completion of priority on-going capital contracts for road construction; and (iii) the continued, but slower paced, development of Abuja. In recognition of the financial constraints on the pace of development of Abuja, a review of the benefits and costs associated with the alternative transfer scenarios will be undertaken.

51. Capital expenditures in the agriculture and manufacturing sectors, particularly the latter, will be most affected by the

resource constraints. In agriculture, the ADPs and their support for rural development justify a sizeable proportion of public expenditure. Major supplemental funds have been allocated to provide infrastructure in rural areas, especially feeder roads. Allocations for on-going irrigation projects will give emphasis to the completion of viable small scale, low cost irrigation schemes. Increased attention will be given to operational research in order to bridge the gap between extension services and research so as to speed up the adoption of new varieties and technologies. In oil and gas, gas infrastructure development will be given priority to enable power stations and selected industrial users to substitute gas that is presently being flared for the more expensive fuel oil; the construction of the Warri-Lagos gas pipeline will thus be one of the few new projects which will be considered for implementation within the next three years. Priority will be given to the completion of Phase I petrochemical projects. With proper restructuring of the carbon black and synthetic detergent plants, both of which are likely to have excess capacity in the short-run, a solution would be to export the excess products. A study will be carried out to review the strategy for the further development of the subsector in the light of the deterioration in international oil and petrochemical market conditions. This study will also study how to restructure Phase II to increase its profitability and to explore opportunities for private sector participation. The proposed LNG project will only be embarked upon if purchase contracts can be guaranteed and an experienced joint venture partner found. Other projects in the oil and gas sector will be reviewed as indicated earlier in this document. The constrained financial resource situation will require a scaling down and restructuring of the steel development programme as reflected in the Fourth National Development Plan. In this context, the World Bank, in collaboration with Nigerian counterparts, has been requested to undertake a study of the steel sub-sector and its major projects. Public expenditures in the subsector will be limited and restricted to the on-going projects until the study is completed. The aim will be to complete the Onne Fertilizer project on schedule, while the Government will consider all possible options to restructure other on-going capital intensive industrial projects (including their completion by the private sector).

III. REFORM OF PARASTATALS

52 The public enterprise (parastatal) sector in Nigeria is quite large, comprising at the federal level about 100 enterprises in agriculture, mining, manufacturing, transport and other services which undertake essentially commercial activities. Government investment in this sector is over N23 billion (N 8 billion in equity and N15 billion in loans) and the returns are less than N400-500 million annually. The Government is not receiving a fair share on its equity investment or taxes, interest or repayment of outstanding debt. Also, as much as 40 percent of the Federal Government's non-salary recurrent expenditure and 30 percent of its capital investment budget has gone to support public enterprises. This state of affairs will no longer be allowed to continue. The parastatals and Government-owned companies are being classified into five broad categories for subsequent action. Based on this classification, they

would either be (i) fully privatised; (ii) partially privatised; (iii) fully commercialised; (iv) partially commercialised and (v) public institutions.

53. Enterprises which function in a fully commercial manner will be fully privatised. The development of the private sector in Nigeria over the last 10-15 years has been such that it can be relied on to assume responsibilities for them, since they are mostly limited liability companies, and the only thing that distinguishes them from their private sector counterparts is government ownership and control. This will now be removed to permit these enterprises to operate free from government interference. Some enterprises will be partially privatised by the sale of part of the Government's equity holding and the requirement that they operate as private companies where they are not already doing so. The Government would no longer provide any operating subventions and their future financial needs would be met by the private capital market.

54. Another set of enterprises would be either partially or fully commercialised. These would continue to be fully owned by Government but would have a financial structure which would permit them to raise capital. Those fully commercialised would be expected to operate without government operating subventions and treasury support for future capital develoment. Those partially commercialised would be those which can generate a fair proportion of the financial resources they need for their operations but will continue to need some government support towards operating costs or future capital investment. These would include the Steel Companies,the Television Authority, the River Basin Authorities and the Research Institute. The final category is public institutions which will continue to be largely funded by treasury resources but will be expected to improve user charges as appropriate. These include educational and health institutions. As a general principle, the Government has mandated the parastatals to charge economic prices for their goods and services. They have also been directed to keep appropriate records, and make timely publication of their quarterly, annual, and audited reports. Guidelines and performance tests for efficient operation of the parastatals will be established.

55. Although some enterprises have already been offered for sale, the mechanism to ensure a non-disruptive release of shares to the market is being worked out. These will be put in place before July 1986 but the initial set of shares is to be released in the third quarter of 1986. For enterprises that will be retained in the public sector, measures will be introduced to reduce government intervention in operations and to avoid use of a monopoly position to impose uneconomic prices on consumers. The operations of all government enterprises will be closely monitored and adjustments will be made to ensure efficiency and accountability.

IV. MONETARY POLICY

56. The programme envisages that monetary and credit policy will be consistent with the targets set for the balance of payments and the increase in reserves, the fiscal policies and for domestic inflation. Under the 1986 Budget which is already in progress, total

net domestic credit to the economy will be allowed to increase by 8.7 percent, while claims on government will increase by 12.8 percent. However, in the event that the fiscal policy targets set in the 1986 Budget became unavailable, alternative growth targets in the aforementioned monetary targets have been set under different scenarios. A common strategy amongst the various scenarios is a deliberate policy of tight monetary policy throughout the programme period. Overall, net domestic credit to the economy is envisaged to increase by 5% and 6% in 1986 and 1987 respectively, from their 1985 level.

57. As a strategy for ensuring that the bulk of available domestic bank credit finance the directly productive activites in the economy, there have been controls since 1969/70 on allocation of credit among 18 sectors/sub-sectors. These controls proved to be rigid and unwieldy, leaving the banks with little discretion in their credit operations. The need to encourage initiative and flexibility on the part of the bank and facilitate greater effectivensss of the Central Bank monitoring efforts led to the regrouping of the sectors/sub-sectors into eight in 1984 and 1985. In 1986, the number of sectors was reduced to four. The credit allocation system will be eliminated by the end of the programme period, having been reduced from four to two in 1987.

58. The banks are on the average very liquid due to the extent some are even reported to be refusing deposits. The government recognises that the excessive liquidity of the banks carries with it the danger that a revival in demand could easily be translated into a rapid acceleration in inflation. In order to reduce this liquidity overhang, allow better control over the monetarty situation by the Central Bank and encourage banks to compete in the mobilisation of savings, the banks will be asked to deposit donmestic counterparts of external payments arrears with the Central Bank in blocked accounts by the end of 1986. This will be accompanied by the reintroduction of stabilisation securities and a thorough review of the interest rate structure with a view to further narrowing of the spread between deposit and lending rates during the course of 1986, and followed by the elimination of interest rate differential among sectors by 1988. Desired movements in interest rate will form part of programme review discussions. During 1986, a review exercise of the financial system will be set in motion, aimed at articulating a strategy for the restructuring of the financial sector and providing a plan of action for improved financial intermediation. The Government proposes to maintain the policy of real positive interest rates that was established in 1985.

V. SECTORAL POLICIES

(a) Agriculture

59. The agricultural sector is an area where improvements can make immediate impact on the supply situation to dampen inflationary pressures. It is also an area where dependence on the external sector for food and industrial raw materials can be quickly lessened. Previous fiscal, trade and exchange rate policies which

exacerbated price distortions in the economy had been major contributory factors to the poor performance of the agricultural sector. A comprehensive policy package to revamp the sector therefore forms the cornerstone of the programme. The major objectives of agricultural sector policies are:

(i) to increase domestic food production with a view to improving nutritional standards and reducing and eventually eliminating external dependence on food supply;

(ii) to increase domestic supply of agricultural raw materials -- (cotton, cocoa, oil palm, sorghum, rubber, millet, sugarcane) -- to the manufacturing sector, thereby increasing local value added and reducing dependence on imported raw materials;

(iii) to increase production of exportable cash crops, thereby diversifying the export base;

(iv) to raise rural employment and incomes; and

(v) to achieve regional optimal crop production mix reflecting the comparative advantage of each agro-ecological zone.

60. To achieve these objectives, the distortions that have impeded agricultural production have been removed and needed structural reforms that have been announced will be vigorously implemented. The winding up of the Commodity Boards coupled with the adoption of an appropriate exchange rate policy under which all non-oil export transactions will take place at the second-tier foreign exchange market will provide improved price incentives that will enable farmers to compete effectively both in product and the factor markets including that of labour. The price incentives will also encourage rehabilitation of the existing productive capacity and induce new planting to substantially boost production. The implementation of the Land Use Decree will be re-examined to ensure that land availability does not become a constraint to growth in the agricultural sector.

61. Meanwhile, measures have been announced to encourage local production of rice, maize and oil palm. In 1986, the national maize production and distribution programmes will provide farm inputs and services that will enable the target of 3.3 million tons in 1986 and 3.6 million tonnes in 1987 to be achieved. At this level the country will have achieved self-sufficiency in maize. Rice production is expected to rise from 0.9 million tons in 1985 to 1.1 million tons in 1986 and 1.5 million tons in 1987.

62. The production of oil palm has improved substantially, reaching almost 0.6 million tonnes, reducing the country's deficit to about 0.3 million tonnes. Special emphasis is now being placed upon the construction of 23 oil-palm mills in the oil palm belt, 7 of which have already been commissioned. Extension services and their

links to adaptive research will be intensified by the Agricultural Development Projects (ADPs) and State Ministries of Agriculture.

(b) Manufacturing

63. The major current problem hampering rapid growth in output of manufacturing sector is inadequate supply of imported inputs and spare parts resulting in gross under-utilisation of installed capacity. With reduced availabilty of foreign exchange at a very low level and the determination to meet external debt service obligations as well as pay for current imports as, and when they fall due, the amount of licences granted for the purchase of imported industrial inputs was not only insufficient but also thinly spread among various producers with the result that most of them could not operate at adequate level of capacity utilisation. Against the background that the use of import licence as a means of rationing raw materials among establishments was originally conceived as a temporary measure, the government has come to the conclusion that the long-run stable solution of the raw materials problem involves a positive step towards their local production and utilisation. Poor and unreliable infrastructural facilities such as energy, water supply, roads and telecommunications have also limited the performance of the sector. Inappropriate tariff structure and an over-valued currency had combined to negate in many cases the protection accorded to some domestic industries and are contributory factors inhibiting a meaningful industrial linkage with the domestic resource base.

64. The industrial strategy will in the circumstances aim at:

(i) encouraging the accelerated development and utilisation of local raw materials and intermediate inputs rather than dependence upon imported ones;

(ii) development and utilisation of local technology;

(iii) maximising the growth in value added of manufacturing production;

(iv) promoting export-oriented industries;

(v) generating employment through the encouragement of private sector small and medium-scale industries;

(vi) removing bottlenecks and constraints that hamper industrial development including infrastructure manpower and administrative deficiencies;

(vii) liberalising controls to facilitate and encourage greater indigenous and foreign investment.

65. To achieve these objectives, the government believes that the adoption of a realistic and flexible exchange rate policy that will reflect the scarcity of foreign exchange and ensure its efficient allocation coupled with appropriate tariff structure is crucially important. With technical assistance from the World Bank, the governnment will put into effect a tariff and excise tax structure

that will be consistent with the exchange rate policy in achieving the desired levels of effective protection and needed support to non-oil exports. Tariff and exchange rate polciies will provide the much needed incentives for developing and utilising locally produced raw materials. Thus, imports of raw materials and spare parts as well as export of manufactures will be channelled through free second-tier foreign exchange market during the programme period. The Government also will review the existing system of price controls to give more incentives to manufacturers.

66. To encourage foreign private investment, requirements including the procedures for registering new industrial enterprises, the granting of locational approval and for undertaking export activities will be liberalised in order to remove impediments to the free flow of investment. Specifically, the role, powers and effectiveness of the Industrial Development and Coordinating Committee (IDCC) will be increased in order to make it the focal point for all the necessary permits and approvals for foreign investment. This will enable foreign investors to deal exclusively with the IDCD, rather than having to seek clearances from a wide range of ministries for the establishment of new industries. New foreign investment will be channelled through the second-tier foreign exchange market to take advantage of the prevailing market-determined exchange rates. Likewise the remittance of dividends and profits will be channelled through the same market.

67. In order to enhance technological development and promote the growth of priority industries including production for exports the following incentives have been provided -- accelerated depreciation, duty draw-back, preferential import licences, etc -- all backed by appropriate pricing policies. With regard to exports, up to 25 percent of gross foreign exchange earnings will be allowed to exporters. The policy on the reinvestment of dividends has been amended to allow for such reinvestment without the requirement that an investor should import an additional 50% of the amount originally meant for reinvestment. A detailed study of the industrial policy and the incentive system has been undertaken and a white paper on it would be released during the course of 1986. A Policy Analysis Department has been set up in the Ministry of Industry which, in collaboration with the World Bank and the Ministry of Planning is to implement and keep under constant review the industrial policy and incentive system.

III. FINANCING THE PROGRAM

A. Macroeconomic and Financing Parameters

68. The Government is committed to carrying through its reform program successfully even in the face of an import capacity much lower than desirable. The import and finance plan underlying the projections in Table X is based on three key points: (a) oil markets are unlikely to recover quickly and will remain subject to considerable uncertainty; and (b) the Government will ensure the repayment of genuine and authenticated outstanding external debt in

an orderly manner and (c) limit new borrowing over the next several years to minimum feasible levels. All of this call for restraint in planning import levels. In 1986, oil export revenues will be down substantially, even with the Financing Plan proposed below, imports will also have to be cut substantially, down to a level of about $5.7 billion. 1986 will thus be a year of economic hardship and austerity, but it will be one of launching of structural change as well.

69. For 1987 the target for imports would desirably be between $7.5 to $8 billion per year (in 1986 prices). However, to be conservative, import planning is being done on the basis of $7.5 billion in 1987, with 3 percent annual growth. While this is far below the level of the years up to 1985, there was excessive import dependence during and immediately after the oil boom period. There has also been substantial overinvoicing of imports as a means of capital flight. With a realistic exchange rate, this hidden capital flight is expected to decline very substantially with the result that imports in the future will have higher purchasing power than would have been the case without the reform programme and with continuing overvaluation and overinvoicing.

70. The financing plan has been designed to allow for variation in oil earnings in either direction. The plan has no net new commercial borrowing after 1988. In addition, it assumes increases in reserves totalling about $1 billion between 1986 and 1990. In the event that earnings fall temporarily below expectation, reserves could be drawn down and external borrowing increased. To give an idea of orders of magnitude an oil price of $1 per barrel below that projected would result in additional financing requirement of about $400 million per year during the period of the decline. If the decline in oil earnings appears long-term, the Government will take further adjustment measures to minimize the impact. If, on the other hand, oil export earnings are higher than those projected, then imports would increase moderately with resultant increases in investment levels and growth. Additional earnings beyond the target levels would be partly used to accelerate debt repayment and so reduce future debt servicing obligations.

71. As indicated above, the crisis situation now being faced will lead to a substantial loss in per capita income and consumption in 1986. However, with the measures in the programme and the balance of payments projections in Annex C, a GDP growth target averaging around 4 percent over the rest of the 1980s is considered feasible. This will allow some increases in per capita GDP and arrest the decline of per capita consumption. Increased output over the rest of the 1980s will result mainly from the fuller utilisation of existing productive capacity, more selective and sound public investment in key areas and improvements in the productivity of private and public investment as a result of the poplicy reforms. Although over the longer period investment will have to grow more or less in line with GDP. Gross domestic investment throughout the period is expected to average around 15 percent of GDP, with the improved incentive system and investment climate leading to higher private/public investment ratio (to around 40 percent in the early 1990s). Gross domestic savings

would average around 17 percent of GDP; public savings over the period are slightly less than public investment but are expected to exceed them in the early 1990s. The reforms of the financial system will be important in the encouragement of private sector savings while improved revenue mobilization, control over public expenditures and reform of parastatals will allow a considerably improved public sector savings performance. The success of the adjustment program will also rest heavily on the ability of the economy to expand the trade surplus and ultimately to generate an external current account surplus without resort to administrative controls on imports. Such surpluses are expected to accrue in the early 1990s when the effects of the policy reforms in encouraging efficient import replacement and non-oil exports will become evident and when the international oil market is expected to peak.

B. Debt Management

72. As indicated earlier, the crux of Nigeria's external debt problem lies in the structure of the debt, particularly with the huge claims under trade arrears. This, along with the bunching of repayments due on medium and long-term loans, make the debt service burden unsustainable, without any relief and given the expected depressed state of the international oil market the debt service to exports ratio would have to be 66 percent in 1986 and even higher in 1987. The structure of public debt outstanding as at the end of 1985 is as follows (Annex A presents forecasts of Nigeria's existing external debt obligations without any rescheduling).

Public Foreign Debt Outstanding and disbursed in 1985 ($billion)
(To be revised)

	Direct Debt	Guaranteed Debt (1)	Total
International organizations	1.3	-	1.3
Bilateral credits (Paris Club)	3.5	1.2	4.7
Uninsured Bank debt (London Club)	2.7	1.4	4.1
Uninsured suppliers credit	0.9	0.1	1.0
Foreign exchange approvals	-	-	0.3
Total medium and long term debt	8.4	2.7	11.3
Reconciled short-term arrears (2)	1.6	-	1.6
Total public external debt	10.0	2.7	13.0
Foreign public debt as % GDP			22%

(1) Debt guaranteed by the Federal Republic of Nigeria
(2) Approved claims at 31 December 1985

Does not include unreconciled ST arrears which may add $5-6 bn. when reconciliation is complete.

3. Earlier negotiations at refinancing short-term arrears under letters of credit culminated in two separate but idential refinancing agreements in 1983 under which a total of $2.1 billion was refinanced. As at end of 1985, only N292 million of the refinanced amount remained outstanding; the final repayment is expected to be made in July 1986. The uninsured creditors agreed to refinance their claims outstanding as at December 31, 1983 by,converting them into floating rate promisory notes carrying interest at 1% above LIBOR with maturities of six years, including a 2-and half year grace period in respect of claims verified and accepted by the Central Bank of Nigeria. Promisory notes amounting to $1,306 million have been issued in respect of reconciled and accepted uninsured claims. Agreement is yet to be reached on refinancing the insured trade arrears, although the Export Credit Agencies have agreed to receive interest with retrospective effect (from January 1, 1984) on claims if verified and accepted by the Central Bank of Nigeria. As of December 31, 1985, insured claims totalling $433 million have been accepted. There are still claims of short-term arrears totalling $.... billion but a large portion of these are not expected to be authentic. The Government will, however, speed up the process of reconciliation and verification and ensure its completion by the end of June 1986

C. External Resource Requirements

74. Faced with the difficult external payments prospects a moderate but firm level of capital inflows is required from the financial community to ease the debt service burden and to close the financing gap required to support the minimum levels of imports needed to ensure the seccess of the adjustment effort. Ihis involves the official rescheduling of Paris and London Club debts and of trade arrears, and new loan commitments, generating net disbursements of the following orders of magnitude (see Annex C). The rescheduling would allow the debt service ratio to be reduced to 37 percent in 1986 and 25 percent in 1987.

($billion)	1986	1987	1988	1989	1990	1991
Official rescheduling	1.5	2.4	2.1	1.6	0.9	0.7
New lending (disbursemets)						
- IRBD	0.1	0.4	0.5	0.6	0.7	0.8
- London Club/ interest offset	0.3	0.3	0.2	-	-	-
- Other commercial	0.4	0.6	0.3	-	-	-
Other	-	-	0.1	0.1	0.2	0.2
Total	2.3	3.7	3.2	2.3	1.8	1.7

75. Government will seek a multi-year arrangement in which 100 percent of the principals of medium and long term loans falling due to Paris and London Club creditors over the 1986 to 1991 period are rescheduled. The consolidated maturities of these years would be lumped together and treated as a single block. Repayment of the rescheduled amounts would begin in 1992 and be completed by 1997 involving five even installments. The Government also seeks repayment

of principal on the outstanding verified arreas commencing in 1992 on the same terms.

76. The sharing of new commitments should result in an equitable spread of risks. The World Bank has indicated that it would be willing to increase its lending to around $800 million per annum of which up to half would be in quick disbursing form. Commitments of about $200 million a year are assumed to come from the African Development Bank. New loans from primarily London and Paris Club financiers (averaging terms of three years grace then four years to repay) are assumed to provide the remaining financing requirements for the shortfall during 1986 to 1988, half of which would be new funds to offset London Club interest.

Monitoring and Implementation

77. The Government recognises that in a period of economic crisis, programmes and polciies, no matter how soundly formulated, become empty words unless they are vigorously implemented. Government is therefore determined to pursue at all levels of administration, a strategy of close monitoring of all policies and measures enunciated in this programme. The existing mechanisms and procedures are being re-examined to ensure that all facets of the programme are imnplemented energetically. Periodic targets and specific tasks have been assigned to various ministries and agencies to ensure that performance keeps pace with the programme's expectations.

78. A number of issues have been identified in this programme that require further review, examination or evaluation. Of particular urgency in this regard are:

(a) monitoring of the second-tier foreign exchange market;

(b) export incentives, procedures and documentation;

(c) restructuring of on-going major industrial projects in the public sector;

(d) privatisation of parastatals;

(e) industrial incentives system including system of approvals, permits and sanctions.

79. It would be relevant to mention that a number of inter-ministerial committees or special panels have already been set up with specific terms of reference to carry out the implementation of some of the above measures and indeed some have already completed their assignments. In a number of cases, the Government has already acted on the recommendations of these committees while the others would be considered in due course. This has been done to ensure that the pace of implementation of the measures specified in this programme is not slowed down by lack of prior decisions.

80. Two monitoring techniques have been adopted to ensure that this programme is faithfully implemented. First, where possible, targets have been set for certain key variables such as balance of payments and output growth. Ceilings have been set on Government's fiscal deficit, overall credit expansion to the economy with sub-ceilings on credit to Government and private sector. Second, periodic reviews will be undertaken on the extent of programme implementation to enable timely corrective measures to be effected and also to set targerts for the subsequent sub-periods of the programme. For this purpose, the monitoring capability of the appropriate ministries will be specifically strengthened and, in addition, a Monitoring Unit comprising of the Cabinet Office, Finance and National Planning Ministries and relevant agencies of government has been established to jointly monitor implementation. No ministry or agency will be allowed to depart from the approved programme unless under exceptional circumstances which must be cleared with the Monitoring Unit for this programme and approved by the President.

09-May-86

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
BALANCE OF PAYMENT:	ACTUAL	ADJUSTMENT PERIOD								
CURRENT ACCOUNT BEFORE FINANCING (BILLION $US):										
EXPORTS OF GOODS&NFS	11.57	7.38	8.47	9.84	11.41	12.88	14.10	15.73	17.38	19.05
OIL EXPORTS	10.89	6.68	7.65	8.77	10.19	11.46	12.56	14.02	15.48	16.94
NON-OIL EXPORTS	0.32	0.40	0.50	0.74	0.83	0.98	1.07	1.18	1.32	1.47
NFS EXPORTS	0.36	0.30	0.33	0.33	0.39	0.44	0.48	0.53	0.59	0.64
IMPORTS OF GOODS&NFS	-8.60	-6.65	-8.66	-9.44	-10.25	-11.06	-11.86	-12.73	-13.67	-14.66
GOODS IMPORTS_1/	-7.40	-5.73	-7.50	-8.15	-8.81	-9.49	-10.16	-10.89	-11.66	-12.49
NFS IMPORTS	-1.20	-0.93	-1.16	-1.29	-1.43	-1.57	-1.70	-1.85	-2.01	-2.17
RESOURCE BALANCE	2.97	0.73	-0.18	0.40	1.16	1.82	2.24	2.99	3.72	4.39
INTEREST _2/	-1.34	-1.16	-0.94	-0.74	-0.54	-0.40	-0.31	-0.24	-0.18	-0.13
-PARIS CLUB	-0.33	-0.42	-0.38	-0.31	-0.24	-0.17	-0.12	-0.08	-0.05	-0.03
-LONDON CLUB	-0.50	-0.41	-0.29	-0.18	-0.10	-0.05	-0.03	-0.02	0.00	0.00
INTEREST ON ARREARS	0.00	0.00	-0.48	-0.48	-0.48	-0.48	-0.45	-0.36	-0.27	-0.18
INTEREST ON RESERVES (HALF OF LIBOR)		0.06	0.06	0.06	0.05	0.05	0.08	0.13	0.08	0.08
NET TRANSFER	-0.26	-0.27	-0.32	-0.34	-0.36	-0.40	-0.41	-0.41	-0.41	-0.41
REMITTANCES		0.20	0.20	0.20	0.20	0.20	0.20	0.30	0.30	0.30
CURRENT ACCOUNT BALANCE	1.37	-0.44	-1.66	-0.90	0.04	0.80	1.35	2.41	3.24	4.05
CAPITAL ACCOUNT BEFORE FINANCING (BILLION $US):										
DIRECT FOREIGN INVESTMENT	0.35	0.40	0.50	0.55	0.60	0.65	0.70	0.75	0.80	0.85
MLT DISBURSEMENT _2/	1.71	1.23	0.90	0.65	0.50	0.44	0.34	0.00	0.00	0.00
MLT AMORTIZATION _2/	-2.81	-3.38	-3.01	-2.72	-2.23	-1.20	-0.95	-0.76	-0.69	-0.43
-PARIS CLUB	-0.43	-0.96	-1.12	-1.09	-0.94	-0.68	-0.51	-0.39	-0.33	-0.21
-LONDON CLUB	-1.26	-1.43	-1.29	-0.99	-0.66	-0.25	-0.17	-0.12	-0.10	0.00
AMORTIZATION ARREARS	0.00	0.00	0.00	0.00	0.00	0.00	0.00	-1.06	-1.06	-1.06
SHORT TERM CAPITAL	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
CAPITAL ACCOUNT BALANCE	-0.75	-1.74	-1.61	-1.53	-1.13	-0.11	0.10	-1.07	-0.95	-0.64
PRE-FINANCING BOP	0.62	-2.18	-3.27	-2.42	-1.10	0.69	1.45	1.34	2.28	3.41
FINANCING PLAN _3/ :										
RESCHEDULING										
PARIS CLUB AMORTIZATION		0.48	1.12	1.09	0.94	0.68	0.51	0.00	0.00	0.00
LONDON CLUB AMORTIZATION		1.07	1.29	0.99	0.66	0.25	0.17	0.00	0.00	0.00
OTHER MLT										
NEW MONEY										
WORLD BANK		0.10	0.30	0.40	0.40	0.40	0.40	0.80	0.88	0.95
LONDON CLUB INTEREST OFFSET		0.30	0.29	0.18	0.00	0.00	0.00	0.00	0.00	0.00
OTHER COMMERCIAL BORROWING		0.40	0.60	0.30	0.00	0.00	0.00	0.00	0.00	0.00
POST FINANCING BOP:										
RESOURCE BALANCE	2.97	0.73	-0.18	0.40	1.16	1.82	2.24	2.99	3.72	4.39
INTEREST	-1.34	-1.26	-1.82	-1.92	-1.96	-1.95	-1.85	-1.65	-1.36	-1.10
OTHER CURRENT	-0.26	-0.07	-0.12	-0.14	-0.16	-0.20	-0.21	-0.11	-0.11	-0.11
CURRENT ACCOUNT	1.37	-0.61	-2.12	-1.66	-0.95	-0.33	0.18	1.24	2.25	3.18
MLT DISBURSEMENT	1.71	1.73	1.82	1.45	1.05	1.04	0.94	1.00	1.08	1.15
MLT AMORTIZATION	-2.81	-1.53	-0.31	-0.45	-0.73	-0.52	-0.60	-4.19	-4.06	-3.68
-AMORTIZATION OF RESCHEDULED DEBT	0.00	0.00	0.00	0.00	0.00	0.00	0.00	2.00	2.00	2.00
OTHER CAPITAL	0.29	0.40	0.50	0.55	0.60	0.65	0.70	0.75	0.80	0.85
CAPITAL ACCOUNT	-0.81	0.61	2.00	1.54	0.92	1.17	1.04	-2.44	-2.18	-1.68
BALANCE OF PAYMENTS (BOP)	0.56	0.00	-0.12	-0.12	-0.04	0.85	1.22	-1.21	0.07	1.50
RESERVES (END OF PERIOD)	1.60	1.60	1.48	1.36	1.32	2.17	3.39	2.18	2.24	3.75
CHANGES IN RESERVES (- = INCREASE)	-0.56	0.00	0.12	0.12	0.04	-0.85	-1.22	1.21	-0.07	-1.50
MEMO ITEMS										
OIL PRICE ($/BL, WITH $1 NIGERIA PREMIUM))	27.50	15.00	16.50	17.50	19.00	20.00	21.50	24.00	26.50	29.00
OIL EXPORTS (MBD)	1.24	1.22	1.27	1.37	1.47	1.57	1.60	1.60	1.60	1.60
$ IMPORT PRICE INDEX	100.00	109.50	117.17	123.61	129.79	135.63	141.06	146.70	152.57	158.67
DEBT SERVICE/EXPORTS GOODS&NFS _4/	35.90	37.78	25.16	24.17	23.57	19.15	17.43	37.15	31.17	25.08

Notes: _1/ Imports in 1987 are set at $7.5 billion in current prices and grow by 3 percent in real terms thereafter.

_2/ Includes projected disbursements on future commitments of $400 million per year from the World Bank for traditional project lending.

_3/ Six year consolidation of Paris and London club principal repayments Due (1986-91). Repayments made over 1992-96 in 5 equal instalments.

_4/ Debt service is raised by the inclusion of London club interest most of which will be offset with new borrowing.

09:05 AM

FEDERAL GOVERNMENT BUDGET:

	1985	1986 BUDGET	1986 PROJECTED	1987	1988	1989
TOTAL RETAINED REVENUE:	8.77	10.46	8.31	11.57	16.79	22.96
PETROLEUM	4.59	4.80	2.59	4.03	8.07	12.60
-1st Tier	4.59		2.41	3.11	3.30	12.60
-2nd Tier	0.00		0.18	0.92	4.77	0.00
NON-PETROLEUM	2.21	3.77	2.61	3.47	4.39	6.09
-Inland Revenue	0.58		0.63	0.75	0.89	1.04
-Custom	0.57		0.99	1.39	1.80	2.61
-Excise	0.26		0.30	0.53	0.74	1.32
-Other	0.80		0.68	0.81	0.96	1.11
INDEPENDENT	1.97	4.10	3.11	4.08	4.33	4.28
-Import Levy	0.00		0.88	1.13	1.01	0.00
-Other	1.97		2.23	2.94	3.32	4.28
CURRENT EXPENDITURES:	8.06	5.60	7.18	9.23	11.30	16.24
WAGES	1.08		1.08	1.17	1.45	1.62
OPERATION & MAINTENANCE (CURRENT)	2.56		2.65	4.04	5.18	7.44
OPERATION & MAINTENANCE (CONSTANT 86 PRICE)	3.32		2.65	3.30	3.53	3.78
OPERATION & MAINTENANCE DEFLATOR	77		100	122	147	197
DOMESTIC INTEREST	2.54		2.00	2.17	2.48	2.99
FOREIGN INTEREST	0.63		0.78	1.07	1.30	3.20
GRANT&SUBSIDIES	1.25		0.67	0.78	0.89	0.99
CAPITAL EXPENDITURES:						
INVESTMENT (CURRENT)	3.36	5.95	3.12	4.55	8.21	10.31
-Direct Investment	2.87		2.62	3.97	7.55	9.57
-Lending To Parastatals	0.49		0.50	0.58	0.66	0.74
INVESTMENT (CONSTANT 1986 PRICE)	4.55		3.12	3.49	4.94	4.03
INVESTMENT DEFLATOR	74		100	130	166	256
DEFICIT (- = FINANCING NEED)	-2.65	-1.09	-1.98	-2.21	-2.73	-3.59
DEFICIT/GDP (- = SURPLUS)	4.13		2.75	2.50	2.50	2.50
FINANCING:						
FOREIGN BORROWING	-0.49		0.06	0.72	0.53	0.37
-GROSS	0.68		0.73	0.88	0.80	1.39
-AMORTIZATION	-1.17		-0.68	-0.16	-0.26	-1.02
DOMESTIC	-3.14		-1.93	-1.49	-2.19	-3.22

Notes: _1/ Not including development stock for on lending to states. 09:39 AM

NIGERIA: KEY ECONOMIC VARIABLES (CONSTANT VALUES IN 1984 PRICES)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
GDP Growth Rate ([redacted])	2.9	-1.6	3.1	4.6	4.1	4.2	3.7	3.5	3.4	3.5
-Oil Sector Growth	7.0	-2.7	3.4	6.7	6.2	5.9	2.8	0.3	0.3	0.3
-Non-Oil GDP Growth	1.9	-1.3	3.0	4.1	3.5	3.8	4.0	4.3	4.2	4.2
Agriculture	3.5	2.5	3.0	3.6	3.8	3.8	3.8	3.8	3.8	3.8
Industry	-5.0	-10.0	5.0	5.0	5.0	6.0	8.0	8.0	8.0	8.0
Debt Service/Exports	31.7	38.0	25.2	24.5	23.9	19.4	17.7	37.5	31.5	25.3
-Interest/Exports	10.2	17.2	21.5	19.9	17.4	15.3	13.3	10.6	7.9	5.8
Investment/GDP (Current)	13.7	10.2	11.7	17.6	19.5	19.6	19.5	20.0	19.8	19.7
-Public Investment/GDP	10.7	7.9	8.8	13.7	14.6	14.2	13.7	13.8	13.4	12.9
-Private Investment/GDP	2.9	2.3	2.9	4.0	4.9	5.5	5.8	6.1	6.5	6.8
Investment/GDP (Constant)	13.3	8.5	8.3	10.5	10.5	10.8	11.0	11.6	11.8	12.0
-Public Investment/GDP	10.4	6.6	6.2	8.1	7.9	7.8	7.7	8.0	8.0	7.9
-Private Investment/GDP	2.8	1.9	2.1	2.4	2.7	3.0	3.3	3.6	3.8	4.1
Savings/GDP (Current)	19.9	11.3	11.3	18.3	22.5	24.0	24.6	26.4	27.1	27.7
Public Savings/GDP	2.8	3.2	4.7	6.8	8.9	11.8	14.5	16.4	16.8	17.2
-Private Savings/GDP	17.1	8.1	6.6	11.5	13.6	12.2	10.1	10.0	10.3	10.5
Savings/GDP (Constant)	19.0	9.3	8.0	10.8	11.5	12.1	12.6	13.6	14.2	14.6
-Public Savings/GDP	2.7	2.6	3.3	4.0	4.5	6.0	7.4	8.4	8.8	9.1
-Private Savings/GDP	16.3	6.7	4.7	6.8	6.9	6.2	5.1	5.2	5.4	5.6
Private/Public Investment	27.2	29.0	33.3	29.1	33.8	38.5	42.3	44.4	48.3	52.3

Preliminary. ICOR's to be added.
and some revisions to be made including possibly increasing private investment and saving a little more in the outer years.

09-May-86

NIGERIA

MEDIUM TERM GROWTH STRATEGY PAPER

Table of Contents

Page No.

March 24, 1986

SUMMARY

(i) Nigeria's political and administrative structure proved ill-equipped to absorb the sudden oil riches that flowed in starting in 1973; it was even less able to deal with the sharp continued downturn in oil earnings the country has faced over the past four years. There were some notable successes, particularly in building up physical and social infrastructure. But there was widespread waste and corruption and the laying waste of much of the agricultural base of the economy. The economy became almost completely dependent on the oil sector and extremely vulnerable to external shocks. With the decline in oil earnings came two years of dithering (1981-83), two years of what the current President correctly referred to as "austerity without structural adjustment" and two changes of government. The new military Government's budget of December, 1986, announced a number of significant measures initiating an adjustment process. However, the Government judges it politically too risky to reach an agreement with the Fund, and its reform program still has no more than a down payment on exchange rate reform. Lack of a Fund agreement stands in the way of debt rescheduling with the London and Paris Clubs. In the absence of a broad compact with the international financial community involving a formal rescheduling and some substantial new lending, it is unclear how long the Government would be able to pursue further reforms necessary for the adjustment effort. And without a strong reform and financing package, it would be difficult for Nigeria to service its debt in an orderly manner without a precipitous decline in per capita consumption. The seriousness of the problems, the recent policy progress and Nigeria's large share of sub-saharan Africa's total population and economy all suggest the high priority of a leadership effort by the Bank to put together such a reform and financing package.

(ii) The Medium Term Adjustment Program proposed provides the basis for improved creditworthiness, renewed growth and in the longer run a restructured economy based on the non-oil sectors. The adoption of a program along the lines proposed - involving both policy and financial packages - would require a strong political commitment by the Government and greater diligence in curbing corruption and motivating the bureaucracy to meet the challenges ahead.

(iii) Adjustment Policy Package. A broad program has been evolved focussing on improving the efficiency of resource use and encouraging desirable private investment. The package builds on the recent policy initiatives of the Government with the priorities being to: (i) correct the still misaligned relative prices through exchange rate adjustment, liberalized import controls (including appropriate trade tax adjustments) and dismantled price controls; (ii) overcome the considerable public sector inefficiencies through improved public expenditure programs and the speedy rationalization of the parastatal sector; and (iii) reduce the severe imperfections in the financial system, principally through appropriate interest rates. Tight discipline on monetary expansion would have to be maintained with the Government continuing to place strict constraints on the budget deficit. While improved revenue measures should be pursued, these should not be seen as a substitute for a slimmer bureaucracy and the privatization of public commercial activities.

(iv) Adjustment Financial Package. Additional external financial support is proposed through both a rescheduling of Nigeria's existing debts with the Paris and London Club financiers and through new money commitments (including Bank quick disbursing loans). The severity of Nigeria's debt situation relates not so much to the size of the debt overhang, but to the unfavorable payments profile and poor immediate outlook for oil. In recognition of this and in order to keep new money requirements within feasible limits, consolidation of a group of maturities under a multi-year rescheduling would be desirable (preferably through a two-step MYRA). However, Nigeria's large trade arrears would have to be subject to extended repayment arrangements. There is also, a substantial need for new funds from the multilateral institutions and the commercial banks. The financial package proposed involves an increase in external debt outstanding of around $7 billion by the end of 1991, with the commercial banks accounting for around half of this increase. The rescheduled debt and new funds will permit import levels at an average of just over $8 billion (1984 prices) per annum over the 1987-91 period, still far below the levels of the early 1980s but $1½ to $2 billion above what could be achieved without the package.

(v) Adjustment Policy Scenario. Even with the adoption of an adjustment policy package and agreement on a financial package of the order of magnitude specified above, it is unlikely that GDP growth would greatly exceed an average of 3½ percent per annum over the 1987-91 period, rising to around 4 percent per annum through to 1995. These rates are consistent with the Government's expressed desire to contain debt service and new external financing to sustainable limits, and to prevent any further decline in per capita consumption over the next few years with modest but steady improvement in the 1990s. While the external debt outstanding in 1995 of around $20 billion under this scenario is slightly in excess of the present level, it would represent a much lower debt service level (20 percent of exports compared with the present level of 40 percent). Over the long term, a curtailment of the high population growth rate will be critical to the efforts to improve living standards.

(vi) Implementing the Adjustment Program. In view of the current reluctance of the Government to formalize an agreement with the Fund, the Bank will initially have to play the lead role. The next step is to build on the policy dialogue the Bank has pursued with the Government and convince it to adopt an adjustment policy package along the lines outlined. This would include continuing efforts to bring about some form of agreement with the Fund and to explore the means through which this could be achieved. It will be necessary to show the Government not only that substantial additional import financing will be available but that the adjustment program will lead to structural changes setting the foundations for sustained future growth based on non-oil sectors. To convince the international financial community to advance Nigeria significant levels of new funds it has to be concretely illustrated that the Government has the political will and discipline to carry out the necessary further reforms, and that the returns from the use of the funds are sufficient to service the extra debt. In this respect, the role of the Bank and the Fund will be crucial.

I. INITIAL CONDITIONS

A. Economic Performance

1. Structural Legacy of the Oil Boom (1973-80). The buoyant oil market over the 1973-80 period dramatically altered Nigeria's resource position. During this time the main objective of the Government was to translate the large oil revenues into investments in social, economic and physical infrastructure. While there were successes - a large functional network of interstate roads was established, power generating capacity tripled, primary enrollment ratio doubled - the political and administrative systems at federal and state levels were not equipped to handled adequately the new-found wealth. Rampant corruption and gross economic mismanagement resulted in considerable leakages of public revenues and wasteful expenditures, while the policies pursued led to structural changes which made the economy vulnerable to external shocks, i.e.:

- The economy became almost completely dependent on the oil sector. By the beginning of the 1980s oil earnings accounted for 96 percent of exports and over 80 percent of Federal Government revenues. These earnings supported a real growth in investment of 9 percent per annum (reaching 24 percent of GDP in 1980) financed almost entirely out of national savings (26 percent of GDP in 1980).

- The structure of production shifted away from the non-oil producing sector towards construction and other services. Inflation, an appreciating naira and poor pricing policies eroded the competitiveness of non-oil traded good production. Its share of non-oil GDP fell from around 55 percent in the early 1970s to under 40 percent in 1980. The impact on the agricultural sector - the major source of GDP and exports before the oil boom - was particularly severe; by 1980 its share of non-oil GDP had fallen to 30 percent from around 50 percent in the early 1970s. Exports of palm products and groundnuts (of which Nigeria was the largest world exporter) had disappeared.

- Domestic expenditure and production became highly dependent on imports. Within a decade Nigeria became a major food importer. Expectations of greater individual wealth enhanced conspicuous consumption of imported luxury goods. The structure of trade taxes and controls encouraged the growth of import-based light consumer good industries which contributed little to value added. By 1980 imports had reached a level of 24 percent of GDP, nearly double the percentage prevailing in the immediate pre-boom years.

- The public sector grew immensely in size and importance. Nigeria entered the 1980s with around half of its GDP and two-thirds of its modern sector employment accounted for by the public sector. Government recurrent expenditures had risen to 11 percent and public investment to 15 percent of GDP, the latter accounting for over half of total investment. A large part of the recurrent expenditures supported an inflated civil service. Many of the public investment projects (e.g. steel mills, certain large scale irrigation projects) were undertaken without sufficient attention to their viability, the appropriateness of their design and the implementation

capacity of the Government agencies. (The private sector was handicapped by red tape and was led to uneconomic investment decisions by misaligned prices.) The indigenization decree of 1972 laid the foundation for the Government's large-scale participation in the banking, insurance and industrial sectors. By the beginning of the 1980s, there were around 70 non-commercial and 110 commercial federal public enterprises, many of which required extensive financial support to cover operating losses.

2. The Economic Crisis (1981-85). Nigeria was thus ill-equipped politically, administratively and structurally to deal with the abrupt end of the oil boom in 1981. Partly because of expectations that the downturn would be short-lived, but mostly because of lack of political discipline, the Federal and State Governments failed to respond quickly to the plunging oil revenues with strong measures aimed at curbing and redirecting expenditures. They continued, for example, to implement the ambitious public investment programs prepared in the wake of the 1979 oil price hike. Consequently sizeable external and fiscal imbalances emerged; external reserves fell abruptly and at the same time there was a large-scale accumulation of private arrears on top of substantial public borrowings to finance the investment programs.

3. The excesses of the civilian Government and its inability to come to grips with economic realities led to a military takeover at the end of 1983. Through the almost exclusive use of demand management policies involving massive expenditure cuts and the stringent application of import controls, the military Government reduced the budget deficit to GDP ratio from 10 percent in 1983 to 5 percent in 1985 and the external account deficit to GDP ratio from 5 percent to zero. However, it failed to adopt substantial measures to reduce the serious misalignment of relative prices, the complex administrative controls and the public sector inefficiencies. The Government was unable to reach agreement with the IMF for an EFF program which would have paved the way for a structural adjustment loan from the Bank and debt rescheduling by creditors. The naira continued to appreciate (although this was marginally reversed in 1985). Sectoral ceilings for credit allocations by banks were enforced and interest rates were, until recently, at levels resulting in negative real yields. While actions were taken to improve the system of trade taxes, continued price and other trade interventions served to reinforce distorted signals. Moreover, fiscal austerity was characterized by expenditure constraints without sufficient regard to necessary expenditure reallocations. Public investment cutbacks proceeded across the board with little cognizance of priorities and stage of completion. Outlays on supplies, spare parts and routine maintenance were eroded dramatically. Significant sums were set aside to support operating deficits of grossly inefficient parastatals and to provide uneconomic subsidies.

4. In essence, the structure of the economy inherited from the oil boom remained intact and as a result, with the sharp deterioration in the terms of trade, economic performance over the 1981-85 period was dismal:

- Production and employment in all sectors, except agriculture, remained depressed, with real GDP in 1985 being some 15 percent lower than at the beginning of the 1980s. Construction and other service sectors were hard hit by the diminished public expenditures and declined at a faster

rate than GDP. The drastically reduced supplies of raw materials and spare parts to the import-hungry industrial sector led to widespread plant closures, a substantial drop in capacity utilization (averaging 25 to 35 percent) and extensive layoffs of the workforce. Severe shortages of goods boosted the inflation rate - peaking at around 40 percent in 1984 but receding thereafter - with scarcity rents of up to 400 percent for many essential goods accruing to traders who, unlike manufacturers, were not subject to price controls. The population growth rate of an estimated 3.3 percent per annum means significant declines in per capita real income and consumption; in 1985 these were well below the levels recorded in the pre-oil boom 1970s.

- The reduction in investment expenditures was severe. Investment as a proportion of GDP fell to under 14 percent of GDP in 1985, half the peak level of 1981. The across-the-board public expenditure cutbacks meant further delays in completing viable projects thus escalating their costs and depriving the economy of their benefits. Private investment shrank at twice the rate of public investment and by 1985 constituted only a quarter of the total.

- National savings halved in real terms due to the decline in both GDP and terms of trade, with the savings ratio in 1985 being around 17 percent of GDP. Meanwhile, external debt service requirements increased tenfold (to 40 percent of exports) and continue to accelerate. The external debt outstanding and disbursed at the end of 1985 of $18.1 billion included $11.5 billion of medium and long-term public debt (excluding officially recognized converted trade arrears of $1.7 billion) of which Paris and London Club creditors each accounted for around one-third. Moreover, Nigeria accumulated substantial trade arrears estimated to range between $3.5 and $6 billion; although the level and timing of arrears recognition is still open to debate, $4.5 billion has been used in this paper. There are also short-term external debts of around $1 billion and private external debts of a further (estimated) $1 billion. The severity of Nigeria's debt situation relates not so much to the size of the debt overhang (which in 1985 amounted to around 140 percent of exports compared with the 255 percent average of all middle income heavily indebted countries) but to the unfavorable payments profile and the poor outlook for the oil market (see Annex D).

B. Adjustment Efforts

5. Policy Initiatives of the New Government. In the face of the continually weak oil market and mounting debt service burden, it was painfully obvious that demand management policies alone would be insufficient to bring about sustainable external and fiscal positions. Moreover, the rescheduling of external public debts could not be avoided for long. The international financial community was thus hopeful that the new military Government which came into power in August 1985 would address the structural weaknesses of the economy and reach an agreement with the IMF so as to pave the way for external financial support and renewed growth. While the Government declared its intentions to complement "austerity with structural adjustment", it submitted the desirability of an IMF agreement involving a major devaluation to a national open debate. The public gave a resounding "no" and the Government formally announced it

would not pursue negotiations with the IMF. Approaches have been made to creditors about debt rescheduling arrangements, but the Paris Club has said that an upper credit tranche program with the IMF would be required before such arrangements would be contemplated. The new Government announced measures (mainly in the 1986 budget statements) which, if fully implemented, makes significant progress in energy pricing and a good start on exchange rate, public expenditure and parastatal reforms. The principal ones are as follows (see Annex B for a list of the measures):

- Exchange rate, trade and incentive policies. An across-the-board temporary import surcharge of 30 percent was introduced to serve as an implicit devaluation on the import side. A second tier foreign exchange market operated by the commercial banks is proposed to be established, funded by residents with foreign currency bank accounts - including retentions of non-oil exporters - wishing to purchase naira. To boost further non-oil exports the customs tariff drawback scheme was reactivated and the foreign exchange retention allowance of non-oil exporters raised from 10 to 25 percent. Also, the export licensing procedure was simplified, the list of prohibited exports abolished (with some exceptions) and the export monopoly power of the six commodity boards discontinued. No significant steps were taken towards dismantling quantitative restrictions although procedures were simplified and a new category of import licences introduced which allows individuals to finance imports with privately held foreign exchange without recourse to the Central Bank. However, outright bans were placed on some products (e.g. rice, vegetable oil). By increasing the prices of petrol 100 percent and diesel 150 percent (kerosene prices were left unchanged) their financial subsidy was removed; the fertilizer subsidy is also to be phased out by 1989.

- Public resource management policies. The budget incorporated further measures for financial stabilization which, if carried out in full, would bring the federal budget deficit down to only 2 percent of GDP in 1986. Substantive reductions were made in the salaries and fringe benefits of civil servants and the freeze continued on hiring staff in a wide range of positions. Transfers to commercial parastatals are to be cut to 50 percent of their 1985 levels. The Government intends to divest itself of public holdings in commercially oriented enterprises and to entrust to the private sector the procurement and distribution of fertilizers and other agricultural inputs.

- Financial system policies. The credit allocation system was simplified by reducing the number of sectors with ceilings on bank lending from 8 to 4 and narrowing the spread of interest rates.

6. Limitation of Initiatives. While the announced measures make major strides in key policy areas, they still fall short of the requirements for a viable structural adjustment effort. Lack of direct action on the exchange rate and import liberalization is a major shortcoming, with the 'dirty' devaluation implied by the announced measures of 30 percent for imports and 20 to 30 percent for non-oil exports being barely adequate as a first step. (The IMF estimates the equilibrium rate of the naira to fall within the range $0.25 to $0.68 per naira, more likely closer to the former, compared with its present rate of $1 per naira.) Although the Government reconfirmed the policy of crawling adjustments to

the exchange rate, no adjustments have been made since the end of 1985. The export incentives introduced are far from sufficient to offset the discriminatory effects of the import protection system and exchange rate policy on non-oil exports. Reliance on funding the second tier exchange market from the foreign currency domiciliary accounts system will in all likelihood result in an insignificant market. Nigerians with funds outside the country appear to be extremely reluctant to repatriate them since few have confidence that they will not be questioned as to their source and penalized by this or a future administration; the exclusion of marketing boards' export earnings from the retention scheme also reduces considerably the size of the funding base for the market. The mechanisms for operating the market are not yet in place, and if the time taken to introduce regulations for the operations of the foreign currency domiciliary accounts system is a guide, then it could be many months before the market is operating. The measures relating to petroleum and fertilizer prices are laudable, but the continued controls on ex-factory prices overwhelmingly favors traders over producers. The heavy taxes and retentions of the six commodity marketing boards (cocoa, rubber, cotton, groundnut, soya bean and palm oil) have not been adequately addressed. Despite the decrease in budgeted capital expenditures for 1986 and the declared aim of allocating them on the basis of efficiency considerations, the cuts appear to be across-the-board with little cognizance of the economic viability of projects and their costs to complete (e.g. continued large expenditures on Ajuokota steel, petrochemical plants). There is no plan of action for the privatization of the commercial public enterprises and the liquidation of clearly unprofitable ones, nor for overcoming the operating inefficiencies of non-commercial parastatals, despite the fact that a number of officially backed investigations have been undertaken with this purpose in mind over the years (e.g. the Onosode Commission in 1981 and the Study Group on Parastatals in 1984). Finally, the regulatory framework for the financial sector remains complex, including the maintenance of strict ceilings on the structure and levels of lending and deposit rates, hampering the efficient mobilization and allocation of financial savings. Interest rates have not been adjusted since 1984 and real interest rates risk becoming negative again should inflation pick up.

C. Development Prospects

7. Nigeria has exhibited over the last two years the political will for austerity and now appears to have found the political will to make a beginning on structural reforms. The Government has announced its intention to pursue further reforms. However, it is unclear how far it would go (particularly on exchange rate adjustments and import liberalization) and how long it would stick to a major and unpopular reform program in the absence of a broad compact with the financial community involving a formal rescheduling of debts, new funds and the discipline imposed by IMF-type monitoring. Without financial support, it is difficult to envisage a scenario in which Nigeria would be able to service debt in an orderly manner and at the same time avoid a precipitous decline in per capita output and consumption.

8. Austerity Policy Scenario. The uncertainties of the oil market, of the "cold" rescheduling option that would be adopted (and the reactions of the international financial community to it) and of the effects of lower

import levels, make it extremely difficult to predict what the macroeconomic picture might look like if Nigeria did not reach an acceptable arrangement with the IMF and thus did not come to any formal agreement with its creditors. However, an Austerity Policy Scenario for the 1987-91 1/ period has been constructed on the basis of EPF's oil projections 2/ in which the rescheduling of debt service obligations is accomplished de facto by the Government's unilateral imposition of its already announced target on such payments of 30 percent of export proceeds; this would allow payment of all interest and some principal, with external debt outstanding at the end of 1991 being reduced to around $12 billion (under 80 percent of exports). No new commercial funds would be made available, while the Bank and ADB would continue to maintain positive net transfer of resources but on scaled back programs (see paras 36 to 40). The Government's diligence in pursuing the reforms already initiated is uncertain, although the momentum for reforms would slow down as the effects of reduced foreign exchange resources become more pronounced. Continued reliance would be placed on demand management policies and administrative controls to achieve external and fiscal balance with the real exchange rate continuing an appreciating trend.

9. Even if there were no adverse reaction from creditors, GDP growth rates under this scenario would at most average under 2 percent per annum over the 1987-91 period and its political feasibility would be questionable. Increased compression of imports of goods to an average of around $6½ billion (in 1984 prices) would be necessary. The scarcities of raw materials resulting from these cuts would force further reductions in capacity utilization in industry. The worsening shortages of commodities (including foodstuffs) would contribute to a high (around 20 percent per annum) inflation rate and although import replacement production would be encouraged (particularly in agriculture which would grow by just over 2 percent per annum), it would be generally high cost. The recourse to restrictive policies and administrative controls to achieve the needed savings and current account surpluses to meet debt service obligations would perpetuate production inefficiencies. The continued pursual of uneconomic public sector projects (e.g. steel) and escalating costs associated with implementation delays (due to shortage of funds) would reinforce this tendency resulting in high ICORS of around 7 to 8 over an extended period. Private investment would further stagnate - particularly foreign investment because of the deteriorating financial climate - with overall investment averaging under 12 percent of GDP over the 1987-91 period. This scenario implies increasingly severe unemployment problems

---

1/ 1986 is seen as a transition year. This is because (i) of hesitations on the part of the Government in committing itself to a development course and (ii) Nigeria has suffered a large income loss and will have to absorb much of the impact during this year.

2/ EPD projects (i) a world price of $20 a barrel in 1986 and $22 in 1987 and (ii) Nigerian production of 1.5 mbd in 1986 and 1987. Nigerian oil commands a $1 premium. (see Annex D for projections of later years).

and further sharp reductions in living standards, with per capita consumption falling by nearly 2 percent per annum. National savings performance would deteriorate only slightly over the period to 14 percent in 1991 (noting that this represents a significant decline from its 1985 level of 17 percent). Conditions could improve during the 1990s if oil markets strengthen as anticipated and the reduced debt service requirements allow higher import levels. However, the economy would be plagued with inefficiencies and deteriorated plant and infrastructures. It would also continue to be heavily dependent on the health of the oil sector and, given Nigeria's very high population growth, the pursuit of such a limited strategy would not provide solid foundations for growth in the post-oil era.

10. The unilateral adoption by the Government of an interest only rescheduling option (which would presumably include principal repayment to preferred creditors and to creditors continuing disbursements on existing loans) would allow Nigeria to have relatively higher import levels than would the declared 30 percent debt service target; on average 15 percent higher annual import levels would result over the 1986-91 period, which would translate into an increase in the GDP growth rate to 2 to 2½ percent per annum. Other options are also possible and the Government would presumably take into account terms being achieved in rescheduling arrangements by other countries in making its decision. However, unilateral "cold" rescheduling over an extended period could lead to an adverse reaction by creditors which, in turn, would frustrate the Government's ability to maintain any growth momentum; this reaction is likely to be more pronounced with the interest only rescheduling option. In particular, it would have damaging effects on the availability of trade credits to Nigeria. Export credit agencies would not be likely to extend cover which would make it almost impossible to finance new capital projects.

11. The macroeconomic situation would be extremely bleak under the Austerity Policy Scenario if oil prices weakened further than anticipated, bringing even more into question the political feasibility of the scenario. For example, if world prices for the next two years fell to $10 a barrel, then Nigeria would have to pump at its present full capacity production of some 1.8 mbd 3/ and cut its import levels by a further 20 percent in 1987 if it were to continue to meet interest obligations on external debt. Import of goods have already fallen by half since the early 1980s (to $8 billion in 1985) and although econometric studies of Nigeria's import demand have been carried out, it remains difficult to know to what extent imports can be further compressed without reducing consumption to politically unacceptable levels and restricting current and investment

---

3/ Nigeria could increase production beyond 1.8 mbd but marginal costs are expected to average $8 to $9 per barrel, compared with marginal costs of $4 to $5 per barrel below this level.

inputs to levels where growth is not possible. However, the imports implied by these very low oil prices would almost certainly be below the critical levels.

12. Adjustment Policy Scenario. Continued structural reforms (with significant action on the exchange rate and import liberalization) backed by a compact with the international financial community and IMF-type monitoring 4/, would make life a lot easier for the Nigerians, although the going would be still tough and fraught with uncertainties. The Medium Term Adjustment Program presented in Section II provides the basis for improved creditworthiness, renewed growth (averaging around 3½ percent per annum over the 1987-91 period rising to around 4 percent in the early 1990s) and in the longer term, a restructured economy based on the non-oil sectors. An Adjustment Policy Scenario has been constructed to reflect the program. The adoption of a program along the lines proposed would require a strong political commitment by the Government and greater diligence in curbing corruption and motivating the bureaucracy to meet the challenges ahead.

II. MEDIUM-TERM ADJUSTMENT PROGRAM

A. Objectives

13. Given the prospects of depressed oil markets over the next few years, renewed growth and improved creditworthiness will only be possible if the efficiency of resource use can be substantially increased and additional resources mobilized externally and internally. This will require building on the initiatives already taken and embracing an adjustment policy package within the context of a Medium-Term Adjustment Program (1987-91) which recognizes the need to increase and improve the productivity of investment as well as to (i) increase the resilience of the economy to the uncertainties of the oil market; (ii) shift the structure of production toward efficient non-oil traded good sectors; (iii) reduce the import dependence of the economy; and (iv) lessen the dominance of the public sector and enhance the role of the private sector. Financial stabilization and increased savings will be important corollary objectives. The adoption of such a package would be combined with some form of acceptable IMF endorsement and participation. This would open the way for additional financial support through favorable terms for the rescheduling of external debts with the Paris and London Clubs, and new loan commitments.

14. It will take longer than the five years of the adjustment program period to rebuild a viable economy based on the non-oil sectors. Over these years oil will still dominate, although solid foundations will have been set for the transition. While considerable growth in non-oil exports can be expected, the small base from which they start means they cannot be

---

4/ It may be possible, although unlikely, to organize financial support without the IMF but even so, it would be difficult and messy at best.

a major propulsive force in the development effort until well into the 1990's; nor can they generate foreign exchange earnings of the relative magnitudes envisaged for, say, the Latin American heavily indebted countries. In the short run most growth will come from the production of import substitutes. The key to this growth will be essentially the same set of policies needed to promote exports, particularly the removal of price distortions. These policies will encourage more efficiency in agriculture and industry and will be much more effective than current policies, for example, in achieving Nigeria's objective of encouraging the utilization of local raw materials. Gas-based activities will be of growing importance both for the local and export markets. In the longer term a curtailment of the high population growth rate - now estimated at 3.3 percent per annum - will be critical to the efforts to improve living standards. The Government is aware of the implications of the high population growth for development and is preparing a population policy with specific demographic objectives. Some unmet demand exists for family planning and this can be increased through well designed information programs. Over the longer run, large-scale acceptance of family planning will require actions on the determinants of family size, such as low levels of education.

B. Adjustment Policy Package

15. The further policy measures proposed are based on extensive work carried out in preparation for the stalled 1984 SAL and subsequent economic and sector work (including the December 1985 CEM). A broad program has been evolved, with the priorities being: (i) correcting the still misaligned relative prices through exchange rate adjustment, liberalized import controls (including appropriate trade tax adjustments) and dismantled price controls; (ii) overcoming the considerable public sector inefficiencies through improved public expenditure programs and the speedy rationalization of the parastatal sector; and (iii) reducing the imperfections in the financial system principally through appropriate interest rates. Further financial stabilization measures and fiscal/monetary targets would be agreed between the Government and the IMF. Tight discipline on monetary expansion would have to be maintained with the Government continuing to place strict constraints on the budget deficit. While improved revenue measures should be pursued, these should not be seen as a substitute for a slimmer bureaucracy and a reduced Government presence in productive activity 5/. In what follows, the core policy measures required are outlined. Annex A presents a detailed annual action program for 1987 based on these measures while Annex B summarizes the timing of policy actions over the whole of the adjustment period.

5/ Special attention will need to be given to the problems facing the state governments in raising revenues to meet expenditure needs in crucial areas such as education and health, and in keeping expenditures under control. The Bank has ongoing ESW on matters relating to state finances and expenditures and this will have to intensify so that suitable policy recommendations can be formulated.

16. Exchange Rate, Trade and Incentive Policies. The thrust of the policy reforms in this area should be towards a market-determined exchange rate and the phased dismantling of import controls within three years. Provided the underlying trade taxes are structured correctly, the principal impediments to efficient resource allocation - and to non-oil exports and the utilization of local raw materials - will be removed, and the inducements to engage in parallel black market activities minimized. Action on three fronts is proposed. 6/ An initial significant and discrete devaluation would be desirable. Movement from there should be as rapid as possible, combining further devaluations (coinciding with the liberalization of import controls) with a crawl of the real rate. The continued need for the "across the board" temporary import surcharge of 30 percent would be reviewed as such adjustments are made. In parallel, the scope of the newly established second-tier foreign exchange market to be operated by the commercial banks should be expanded through the Government allocating increasing shares of oil as well as non-oil export proceeds to it. This would supplement the amounts available from the foreign currency domiciliary accounts system. However, the second-tier market should be integrated into the formal market as quickly as feasible with the naira then being allowed to find its own level.

17. Initial priority in the dismantling of import controls should be given to raw materials and spare parts (with some exceptions) through their transfer to open general licence status. However, action should be taken to ensure that the system of trade taxes provides the desired longer term signals to producers allowing them to plan ahead with some certainty. Modifications to the customs tariff schedule should be made at the time of the initial devaluation to lower and narrow the range of rates to 15 to 35 percent (with a clustering of rates in a narrower band of 20 to 30 percent). Excise taxes on production for the local market should be structured to be consistent with the principles for the setting of the custom tariff levels and minimum feasible degrees of import protection. High additional excise duties (50 and 100 percent or more) should be applied to the local production and imports of luxury goods. The basis for such reforms was set in the Bank assisted review of the customs tariff and excise tax schedules in 1984.

18. Immediate action should be taken to relax ex-factory price controls in order to shift incentives away from trading to production, to signal relative scarcities and to increase the effective yields and elasticity of the excise tax system. It would be highly desirable to shift farmer incentives from input subsidies to a crop pricing structure which reflects market forces. A re-examination of the role of the six commodity marketing boards and the approach to the setting of support prices for domestic crops with the aim of minimizing Government intervention is also

---

6/ The recommended exchange rate actions are preliminary. Firm recommendations will be formulated after the IMF completes its Article IV Consultations in March 1986.

called for. The government should continue to adjust petroleum product prices in line with the exchange rate adjustments.

19. A package of export incentives should be introduced which removes fully the impediments to non-oil export production inherent in the system of trade taxes and controls. Budgetary considerations and GATT regulations would need to be taken into account in determining the nature, level and coverage of the incentives but the package could include: (i) the recently re-activated customs drawback scheme but extended and adapted to include exemption (or equivalent) from customs tariffs and excise taxes on all inputs directly and indirectly incorporated in export production; (ii) exemption from excise taxes on output; and (iii) a tax credit on export production (or an equivalent measure) to offset the distortionary effects of the import protection system and exchange rate policy on value added. The ability of exporters to retain 25 percent of foreign exchange earnings and sell them in the second tier foreign exchange market goes part of the way towards (iii); an alternative to a tax credit would be for all foreign exchange transactions associated with non-oil exports to be channelled through this market. Appropriate incentives for export traders and service exports would also be required. Other supportive measures are outlined in the Bank's report on the potential for non-oil exports.

20. Public Resource Management Policies. The principle which should guide the Federal and State Governments in their budgetary and planning decisions throughout the adjustment period are as follows. First, the Government should continue its efforts to stabilize the public wage bill. It should restrain attempts to increase real levels of public service salaries and fringe benefits, and the freeze on hiring should be extended to all but the most critical skills. Over the longer run, the emphasis has to be on eliminating overstaffing through a judicious combination of attrition and redeployment and allowing wages for different skill categories to reflect scarcity values. Second, restored levels of supplies will be essential in the health, education and agricultural sectors while routine and periodic maintenance must have priority over new investment to prevent the rapid deterioration of essential infrastructure. Third, transfer to parastatals to cover operating deficits and capital expenditures have to be further reduced; the transfers to commercially-oriented parastatals should be eliminated completely. Within the context of development strategies for the sectors in which they operate, programs for the privatization, liquidation or rationalization of parastatals should be prepared and implemented. Commercial orientation and increased autonomy and accountability should form part of the rationalization program. Where feasible, the process of privatization of commercially-oriented parastatals could commence with the conversion of outstanding government loans to equity and the infusion of new capital by selling shares to the public through the Nigerian Stock Exchange. Finally, priorities should be set for the completion of the large number of capital projects on the basis of their economic viability and costs to complete, with across-the-board cuts being avoided so that the economy is not burdened by unfinished and weak projects. This will mean some politically tough but economically important decisions (e.g. discontinuing or postponing the completion of Ajaokuta steel works). For projects in the early stage of implementation, possibilities for reshaping the scope and/or timing to reduce costs and increase benefits should be assessed, especially

where large sums remain to be spent (e.g., the new capital, Abuja). The Bank's proposals in this area are developed more fully in the October 1985 report on Nigeria's public expenditures.

21. Financial System Policies. To increase the mobilization of financial savings and encourage the more efficient allocation of financial resources, the Government should reduce its intervention in the operation of financial markets, particularly in credit allocation and in the setting of interest rates. Interest rates should be allowed to reflect a positive real yield on holding financial assets and be flexible enough to take into account the frequent changes in the rate of inflation and balance of payment conditions. Also, the differential interest rates applied to the preferred sectors should be eliminated. The percentage credit allocation ceilings on bank lending should be removed. The review proposed by the Government with the aim of articulating a strategy for the restructuring of the financial sector should result in a plan of action for improved financial intermediation.

22. Sector Policies. Intra-sectoral breakdowns of public expenditures should be determined within the context of medium term development strategies for each sector. Special focus should be placed on the removal of technological and supply constraints discouraging private initiative and inhibiting efficient responses to favorable market conditions. While the basic exchange rate, trade, incentive and financial policy reforms will be crucial in this regard, constraints may exist at the sectoral level (e.g. specific infrastructural deficiencies, lack of particular skills) on which action must be taken to ensure the desirable responses to the improved price signals.

- Agriculture: The extensive information now available on agriculture is being drawn together to frame a coherent sector strategy for the sector's development. The strategy will incorporate measures to support and remove impediments to the development of export crops, particularly rubber, oil palm and cocoa. Allocations of public investment for irrigation should emphasize viable small scale low-cost irrigation schemes. The ADPs would continue to justify a sizeable proportion of public expenditure, although the project components need to be examined in the light of the absence of an economic response to applications of current fertilizer compounds on existing varieties of sorghum and millet. Food storage should receive increased attention. In order to expedite the adoption of new varieties and technologies developed by research centers, the Government should actively pursue applied research to establish their appropriateness at the farm level. A large share of expenditures should be directed to combat serious natural resource degradation (e.g., shelter belts, arid zone afforestation and rural forestry).

- Oil and Gas: NNPC should rely on joint ventures in all facets of oil and gas production. It should be reorganized as a holding company with largely independent subsidiaries and divest itself of its petroleum product distribution companies. Gas infrastructure development should be given priority to enable the 1320 mw Egbin power station and selected industrial users to substitute gas that is presently being flared for the more expensive fuel oil. The highest priority is the construction of the Warri-Lagos pipeline and the corresponding development of the gas field of

Utorogu. This program could be related to the gathering of associated gas which could also be used for LPG, initially for export and for domestic markets once they are developed. The proposed LNG project would have the highest chance of success if it were set up on a joint venture basis, with at least a 40 percent share for foreign companies and with an experienced operating company in charge of management; the project should only be embarked upon if purchase contracts can be guaranteed.

- Manufacturing: There is a need to reduce considerably the role of the public sector in manufacturing. The policy reforms outlined will lead to considerably increased domestic and foreign private investment. Meanwhile, public sector efforts should be redirected towards strengthening industrial infrastructure and support services. Given the inadequate market for its products, its high costs and doubtful viability, construction of the Ajaokuta steel works should preferably be discontinued or deferred indefinitely (and the necessary penalties paid); no new projects in the steel sector (including the flat products plant, special alloys plant and foundry) should be started while expenditures on other existing steel plants should be held to the minimum levels. In petrochemicals, priority should be given to the completion of the plants to produce polypropylene, carbon black and synthetic detergents ("Phase I"), provided that a satisfactory restructuring plan can be established for the latter two plants. The first phase ("Phase IIA") of a proposed large polyolephin complex to produce thermo-plastics should be deferred.

- Population: A draft population policy has been prepared by Nigerian population specialists under the guidance of an inter-ministerial group and with support provided through Bank sector work in cooperation with other donors. This policy should now be reviewed and acted upon by appropriate bodies. It includes: (i) establishing a nationwide program of private and public sector family planning services, supported by extensive information and education activities; and (ii) undertaking other initiatives to indirectly reduce fertility by, among other things, improving the status of women and delaying the age at marriage.

C. Adjustment Financial Package

23. A financial package involving exposures along the lines presented in the following table would appear to be feasible. It involves the official rescheduling of Paris and London Club debts and of trade arrears, and new loan commitments. The package is based on: (i) assessment of likely reactions of Nigeria's creditors to the endorsement by the IMF of an adjustment policy package, past practices of the Paris and London Clubs and parameters set for the Baker initiative; (ii) possible lending programs of the Bank, IMF and other international financial institutions under alternative lending conditions; and (iii) iterations of funding requirements to meet necessary import levels implied by the macroeconomic assessments, with funding availabilities implied by the financial workouts.

NIGERIA: Changes in Exposure (Debt Outstanding and Disbursed $ billion)

Creditor	End 1986	Adjustment Policy Scenario End 1991	End 1995	Average Annual Growth 1987-1991	Austerity Policy Scenario End 1991	Average Annual Growth 1987-1991
1. World Bank	1.5	4.6	7.7	25%	2.2	8%
2. IMF	0.0	1.9	0.1	-	0.0	-
3. Paris Club	5.3	6.4	3.4	4%	3.6	Neg
4. London Club	4.8	5.5	2.7	3%	3.3	Neg
5. Other Commercial	0.0	1.9	1.9	-	0.0	-
3 + 4 + 5	10.1	13.8	8.0	6%	6.9	Neg
6. Trade Arrears 1/	2.8	1.6	0.4	Neg	0.1	Neg
7. Other 2/	4.0	3.0	3.9	Neg	2.8	Neg
TOTAL DOD	18.4	24.8	20.1	6%	12.0	Neg

1/ Includes only the $2.8 billion in arrears not yet recognized as of December 31, 1985.

2/ Includes short term, private, arrears already recognized, and other debt not eligible for renegotiation.

24. Debt Rescheduling. Based on Bank analysis of alternative options, the best feasible workout appears to be a two-step six-year rescheduling arrangement (MYRA). This reschedules 100 percent of the principals of the London and Paris Club over the period 1987 to 1992 7/. The two-step MYRA is based on the supposition that creditors would first agree to a very short consolidation period (two years maximum) involving standard rescheduling terms to begin with. Conditional upon satisfactory policy performance during the first two years (1987-88) of the adjustment program period, the creditors would negotiate a longer MYRA (four, possibly

7/ This also implicitly reschedules the principal not paid during 1986 when the 30 percent debt service limit is assumed to have been in effect. It is unlikely that Nigeria would reach formal agreement with its creditors during the course of 1986 and would thus pay all interest, principal due to multilateral creditors and other principal (with preference to those disbursing new monies) to the extent of the announced debt service target.

five, years) 8/. Whereas a year-to-year rescheduling approach affords the creditors somewhat greater control, a MYRA approach is more amendable to obtaining a tenable external situation since it allows Nigeria to concentrate on medium and long term reform. In the case of the trade arrears, it would be consistent to spread the repayment of the principal over ten years (with an interest rate of 1 percent above LIBOR) rather than the 3.5 years used for the arrears already recognized. This reduces the need for new loans.

25. New Loan Commitments. The adoption of an adjustment policy package by the Government would lead to an acceleration of World Bank regular project loan disbursements increasing over the years to around $500 million in 1991, plus SAL and other quick disbursing loans averaging about $500 million per annum over the 1987-91 period. This would lift the Bank's exposure to around $4½ billion in 1991, which represents about 18 percent of total debt outstanding. Commitments of about $200 million per year are assumed to come from the African Development Bank (ADB). New loans from primarily commercial banks averaging terms of three years grace then four years to repay are assumed to provide the remaining financing requirements. These new loans would imply that the share of total debt in Nigeria of commercial bank creditors would increase from 51 percent in 1985 to 55 percent in 1991, decreasing to 40 percent in 1995. This exposure would be reduced to the extent that IMF or other creditors exposure is increased. In finalizing the financing package, it will be necessary to ensure that the sourcing of new commitments results in an equitable spread of the risks.

26. IMF Accord. The overall financial package assumes that Nigeria is able to attain a successful formal agreement with the IMF on an upper credit tranche facility by 1987. This allows one year for the anti-IMF political fervor to cool off. Four one-year standbys (1987-90) of 60 percent of quota are then assumed, followed by a fifth year where net exposure would be maintained. The 60 percent is applied to the present quota (SDR 849 million) without adjustment for inflation. (Another option might would be a one-year standby followed by the three-year EFF the IMF had earlier been planning on.) Because of the first repayment coming due in 1990, the IMF exposure reaches a peak of 220 percent of quota in 1990 and 1991 and declines rapidly thereafter, with all loans being repaid by 1994. An extension of the IMF exposure for a longer period would decrease the amount of commercial loans needed. The absence of IMF funds would increase the new money requirements from other sources in roughly corresponding amount unless the growth targets are reduced.

8/ While commercial banks have entered MYRAs involving consolidation periods of up to five years, Paris Club reschedulings have mostly been confined to single maturities. However, the granting of extended consolidation periods does not, per se, pose important procedural difficulties to the Paris Club. In 1985, Ecuador was accorded a three-year MYRA.

D. Adjustment Policy Scenario: Macroeconomic Implications

27. Even with the adoption of an adjustment policy package and agreement on a financial package of the orders of magnitude specified above, it is unlikely that GDP growth would greatly exceed an average of 3½ percent per annum over the 1987-91 period, rising to around 4 percent per annum through to 1995. 9/ These rates are consistent with the Government's expressed desire to contain debt service and new external financing to sustainable limits, and to prevent any further decline in per capita consumption over the next few years with modest but steady improvement in the 1990s. While the external debt outstanding in 1995 of around $20 billion under this scenario is in excess of the present level, it would represent a vastly improved ratio to exports (around 75 percent compared to the present level of 150 percent) and be associated with a lower debt service level (20 percent of exports compared with the present level of 40 percent). Over the long term, a curtailment of the high population growth rate will be critical to the efforts to improve living standards.

28. Investment and Savings. These growth magnitudes do not call for massive new investment levels. Although over the longer period investment will have to grow more or less in line with GDP, there is considerable scope for increasing output over the medium term through the fuller utilization of existing productive capacity, more selective and sound public investment in key areas and improvements in the productivity of private and public investment as a result of the policy reforms outlined earlier; the effects will be reflected in a decreased non-oil ICOR (between 3½ and 4). Investment throughout the adjustment program period is expected to average around 18 percent (which in real terms is slightly below present levels) of GDP, with the improved incentive system and investment climate leading to the partial restoration of the pre-crisis private/public investment ratio (to around 55 to 60 percent by 1991). The national savings rate would average around 18 percent of GDP; public savings over the period are slightly less than public investment but exceed them in the early 1990s. The uplift in the savings rate in the early 1990s is not entirely dependent on expected increases in oil earnings. The reforms proposed for the financial system will be important in the encouragement of private sector savings while improved revenue mobilization, control over public expenditures and parastatal reforms will allow a considerably improved public sector savings performance.

29. Exports and Imports. The success of the adjustment program will rest heavily on the ability of the economy to expand the trade surplus and ultimately to generate an external current account surplus without resort to administrative controls on imports. Such surpluses are likely to accrue

---

9/ While, as noted in the recent PBD review of "Baker" papers to date, there is no scientific way to quantify the effect of the policies proposed with the RMSM outcomes, the parameters used represent judgements based on what has been gleaned from analysis at the macro and sectoral levels of Nigeria's own experience, and from comparison with other countries.

in the early 1990s when the effects of the policy reforms in encouraging efficient import replacement and non-oil exports begin to really bite and when the international oil market is expected to pick up. Rapid growth in non-oil exports (around 11 percent per annum) can be anticipated as a result of the improved exchange rate and export incentive policies but because of the small base from which they start (about $400 million in 1985), the high growth rates would not result in vast increases in foreign exchange earnings over the 1987-91 period (although they would become significant during the 1990s if even moderate growth continues). Unfortunately, there is considerable uncertainty as to export revenues from oil, although Nigeria does have some flexibility on the margin in adjusting production levels to compensate for price reductions. 10/ There is also uncertainty as to the level of imports consistent with the growth targets set. Imports of goods have been squeezed considerably since the onset of the economic crisis and in 1986 are expected to reach a trough of just over $7 billion (in 1984 prices). This low figure has been used as the base, with growth thereafter being based on a consistent set of judgements of import elasticities for capital, intermediate and consumer goods and on the effects of the exchange rate and trade policy reforms. The foreign exchange made available through rescheduling and new loans enable imports of goods to be maintained at an average of around $8½ billion per annum (in 1984 prices) over the 1987-91 period (compared with around $6½ billion under the Austerity Policy Scenario and just over $7 billion in the interest only 'cold rescheduling option), while the policy reforms will lead to a marked increase in the efficiency of their use.

30. Structural Changes. The Medium Term Adjustment Program would significantly strengthen the non-oil productive sectors and reduce the economy's dependence on oil. Real growth of non-oil GDP is expected to average over 3½ percent per annum during the 1987-91 period. The most important changes would be in the agricultural and industrial sectors, with the former growing at an annual rate of just over 3½ percent and the latter at over 7 percent. There will be a fair degree of "lumpiness" in the industrial sector which is partially reflected in the growth and non-oil export figures (as a result, for example, of LPG production coming on stream). Nigeria's dependence on food imports should be reduced over the period (reflected in declining per capita real imports) as farmers respond to the improved incentive system and reduced supply constraints. Exports of crops should also pick up (mainly cocoa) while forestry could be expected to grow rapidly and serve as a basis for a fast growing export industry in the 1990s. Manufacturing growth in the near term is dependent to a large extent on the availability of raw material imports. Over the medium term, the improved incentive system would result in a more efficient

---

10/ If oil earnings over the adjustment period 1987-91 are lower by 20 percent than those forecast by EPD, the GDP growth would be held to about 3 percent per annum. The income loss would have to be absorbed mainly in 1987, and thereafter the growth path would be similar to that of the Adjustment Policy Scenario but with up to about a two year lag. A comparison of the performance under the Adjustment Policy Scenario with the Austerity Policy Scenario is presented in Annex C.

and expanded industrial structure with considerably increased exports to surrounding countries. Diversification into LNG and LPG would also serve to strengthen the industrial base and broaden exports particularly during the 1990s. The reduced dependence of the economy on imports is reflected in the real import/GDP ratio being contained to around present levels in the early 1990s without recourse to import controls. The exchange rate and trade policy reforms would encourage efficient import replacement production for which comparative advantage is apparent, particularly of raw materials and intermediate goods. Increased levels of investment and production by the private sector should result from the improved incentives system with the public sector dominance being reduced. The ratio of private to public investment, for example, is expected to double between 1986 and 1991, with significant increases in foreign investment contributing to foreign exchange inflows and a strengthened technological base. In all, a much stronger and more resilient economy emerges at the end of the adjustment period, with firm foundations set for future growth based on the non-oil sectors.

NIGERIA: Macroeconomic Performance

	Adjustment Policy Scenario		Austerity Policy Scenario	
Growth Rates (1984 Naira (%)	1987-91		1987-91	
GDP	3.6		1.8	
Non Oil GDP	3.6		1.4	
Agriculture GDP	3.7		2.3	
Industry GDP	7.3		-4.4	
Non Oil Exports	11.2		5.6	
Imports	3.9		-1.0	
Per Capita Consumption	0.3		-1.9	
Ratios (Current Naira)(%)	1987	1991	1987	1991
Interest/GDP	4½	4½	3	1
Savings/GDP	15	21	13	14
Investment/GDP	15	20	12	12
Public Saving/Public Investment	81	92	82	69
Private/Public Investment	36	58	28	20
DOD/Exports a/	173	158	163	77
Imports/GDP (1984 Naira)	14	13	13	11
Other Indicators (Average Annual)	1987-91		1987-91	
Import Levels ($billion)	8.1		6.6	
ICOR (non-oil)	3.5		11.9 b/	

a/ In the Adjustment Policy Scenario, this reduces to around 74 percent by 1995. See Annex C for full table.

b/ The ICOR is high since it includes two years with zero or negative growth. If it was calculated over a slightly longer period, the average would be around 7 to 8.

E. Risks of the Program

31. Uncertain International Economic Conditions. The international macroeconomic picture is shrouded with uncertainties, not only in oil market prospects but also in the ability and willingness of creditors to continue to extend financial support to heavily indebted countries. If the international oil market should weaken even more than projected and Nigeria is unable to maintain revenues through increases in production volumes, then the pace of implementation of the adjustment program would have to be slowed down, growth targets reduced and the time at which sufficient savings are being generated to commence repayment of external debt pushed back and/or per capita consumption squeezed. The alternative would be to seek additional external financial support but at the cost of an extended debt burden. The commercial banks may also take steps to cut back their exposure in Nigeria if (i) they perceive the creditworthiness of the country to be impaired by more unfavorable oil earnings than now anticipated and/or (ii) other heavily indebted countries are not able to meet their revised payment obligations, adversely affecting the liquidity of the banks and their risk perceptions.

32. Internal Resistance to Reforms. The public debate revealed strong opposition to an accord with the IMF. Questions of national sovereignty and wasteful use of money by the Government and its officials were important considerations in moulding the negative response. While the Government has gained considerable political capital as a result of the debate, it will have to now tread a careful path in consummating any form of accord with the IMF. The Government is reluctant to deviate radically from the perceived public opinion so as not to give competing army officers the excuse to plot and possibly overthrow it. The increasing emphasis on price mechanisms relative to administrative controls will mean less scope for corruption and encourage those affected to frustrate the implementation of the reforms. Trade liberalization is likely to meet considerable opposition from those benefiting from excess protection or from quota rents on scarce goods. Agriculture tariff reforms could be seen by urban groups as contrary to their interests leading them to pressure for their suspension. It will need a committed Government to overcome these and other forms of resistance, which will be particularly strong in the middle stages of the adjustment program when the effects of the reforms begin to take hold.

III. INSTITUTIONAL RESPONSIBILITIES AND MONITORING: IMPLEMENTING THE ADJUSTMENT PROGRAM

A. The Next Steps

33. Putting into place a Medium Term Adjustment Program will be a difficult and complex task. In this the Bank will have to take a leadership role. The crucial next step is to convince the Nigerians to undertake the further policy reforms required. This is a sine qua non of obtaining external finance. Thus the Bank should build on the policy dialogue it has pursued with the Government to seek adoption of an adjustment policy package along the lines outlined. This would include

continuing the Bank's efforts to convince the Government of the necessity to have some form of agreement with the IMF and to explore the means through which this could be achieved. It is not going to be easy to sell the adjustment program to the Nigerians. What is proposed goes beyond what they have been willing to accept to date, particularly on the exchange rate, import liberalization and starving the white elephants in the public expenditure program. On the other hand, there are sufficient reasons for cautious optimism to make the effort worthwhile. As noted previously, the reforms already announced in the last budget indicate a recognition of the need for fairly fundamental changes. And even though the Nigerians are undoubtedly considering trying to force acceptance of de jure or at least de facto rescheduling which would bring debt servicing down below the announced 30 percent of exports, the amount of new funds involved in the proposed adjustment financing package should be large enough to appear quite interesting to them at a time of great and growing import stringency. Neither is it going to be easy to sell the financing package to the international financial community even if Nigeria embraces it. The community will be unwilling to advance Nigeria significant levels of new funds if the Government cannot concretely illustrate the political will and discipline to carry out the necessary further reforms and to ensure that the returns from the use of the funds are sufficient to service the extra debt. In this respect, the role of the Bank and Fund will, again, be crucial.

34. Selling the Program to the Nigerians. To convince the Nigerians of the desirability of adopting a Medium Term Adjustment Program, five inter-related aspects should be stressed. First, there is the internal virtues of the policies themselves in creating the foundations for self-sustaining growth based on the non-oil sector of the economy. Second, the additional funds allow considerably more imports - $1.5 to $2 billion per year - and reduce the strains imposed by continued austerity measures. Third, official rescheduling has commercial advantages over a "cold rescheduling" by the Government e.g. continued trade credits, more favorable loan terms in the future. Fourth, the conditionality of an international compact has advantages, especially to support the hands of the reformist elements in a Government continually subject to pressures from interest groups. Finally, there is the flexibility offered by the international compact in responding to the external shocks and other uncertainties. All the participants - the Government, the Bank, the commercial banks and the IMF - will have to pull their weight if, for example, the oil market deteriorates further. The Bank should indicate the extent of its willingness to expand its lending in response to the Government's policy initiatives, especially through quick-disbursing loans to support specific reform packages, and to provide technical support in devising and implementing policy reforms. To help establish and expand the second tier foreign exchange market and to promote non-oil exports, for example, an industrial imports loan has been proposed.

35. Role of the IMF. The Bank and the IMF, at the working level, are in broad agreement on the contents of an acceptable adjustment policy package, and through its Article IV Consultations, the IMF will have made clear to the Government its position. Regarding the exchange rate, the IMF and the Bank are in agreement both on the first-best approach (a "clean" large devaluation and subsequent float) and on second-best steps (including

enlargment of the second window) to get there. In the likely event that Nigeria remains unwilling to adopt any kind of formal IMF program or surveillance in the near future, the Bank's objective is to assist both parties in order to assure that Nigeria has as soon as possible a policy reform package acceptable to the IMF and that there is the closest feasible formal relationship between the two. The formal relationship is important for: (i) obtaining acceptance of the proposed adjustment financial package; (ii) getting IMF money (after a decent interval to allow sensitivities in Nigeria to fade); and (iii) the benefits, mentioned above, of IMF and broader international conditionality.

B. Bank Lending Program

36. The Bank's lending program has an important role to play in efforts to bring about the Medium Term Adjustment Program. The question is how to calibrate the volume and composition of the lending program to best encourage rapid movement toward the adjustment policy package. In this context, the proposed Bank program has been designed to provide flexibility in responding to policy performance. It consists of (i) a core lending program to respond to current policy initiatives; (ii) a minimum lending program if the Government delays in developing these policy initiatives; and (iii) a full lending program to support an acceptable Medium Term Adjustment Program.

37. Agriculture accounts for about one-third of proposed Bank lending under the core program. In industry, Bank management has authorized discussion with the Government of a quick disbursing sectoral operation that would focus on additional policy reforms designed to give a major boost to the second window for foreign exchange and sharply increased incentives for non-oil exports. The program also includes projects in transportation and energy; these had been on hold until the recent elimination of the petroleum subsidies. Regarding longer-run constraints on development, the program also gives some emphasis to water supply. On education, sector work is being undertaken to help develop a project pipeline.

38. When Nigeria's GNP per capita is calculated on the basis of an adjusted exchange rate to compensate for the over-valued naira, it is cut roughly in half, demonstrating that the estimated official per capita income substantially overestimates real income levels. The current ceiling on the Bank's contribution to total project costs is two-thirds. In light of the low level of adjusted per capita income and Nigeria's severe resource constraints, it is proposed that the ceiling be raised to 80 percent for appropriate lending operations.

39. Some major projects in the lending program have been designed to be of the "accordion" type, which can be expanded if the reform program is moving well. The lower level of lending, which is linked to the current policy framework, would be about $350 million annually (about $4 per capita). This level, while less than would be desired in terms of sectoral policy and institutional objectives, seems appropriate as a signal to Nigeria that the Bank supports the reforms made to date but would like to see much more before substantially increasing the program. Until further policy progress is made, creditworthiness concerns are also seen as a

constraint on further expansion. Nigeria does have on balance a good record in paying back the Bank (even when it was running up its large trade arrears). And its large oil and gas reserves mean that it is much less dependent than most other countries with serious debt problems on good policy per se to meet future debt servicing requirements; in fact its oil earnings are projected to be more than adequate to meet debt servicing (and allow import growth) during the period that new loans from the Bank would be repaid. (cf. the projected debt service ratios for the 1990s in Table 4 of Annex D). Nonetheless, the proposal here reflects the view that now is a time for caution on lending levels. As further policy progress is made, the lending program could be expanded and, if circumstances are right, would include the quick disbursing second window loan mentioned above.

40. If the existing policy framework deteriorates, then the lending program would be cut back to focus almost entirely on longer-term development constraints. The level would be about $200-$250 million, the minimum necessary to keep the net transfer positive. On the other hand, if the Government is prepared to implement the Medium Term Adjustment Program in full, the Bank would respond with annual lending levels of about one billion dollars. (The policy package, with its likely implications for other external support and additional growth would also result in a substantial improvement in creditworthiness, as shown in the debt service, growth and import figures for the Adjustments Policy Scenario in Annex C.) This lending program would include a higher portion of quick-disbursing sector loans (up to about 50 percent), concentrated on accelerating structural change. If agreement is reached with the IMF, the program would include a SAL.

NIGERIA: Breakdown of Bank Contribution to Financing Package in Medium Term Adjustment Program (Millions of dollars)

	FY86	FY87	FY88	FY89	FY90
Traditional projects	211	354-479	355-585	405-730	525-870
Quick disbursing	-	300	400	400	500

C. London and Paris Clubs

41. The requirement and importance for rescheduling and new funds from the London and Paris Clubs has already been discussed. The issue is the Bank's approach to them. Nigeria is already approaching both with rescheduling proposals; the latest proposal to the London Club asks for a four year consolidation period, a five year grace period, and then five years for repayment. Some London and Paris Club members may well break ranks, or there could possible even be some formal interim arrangement reached by one or both groups, although some Paris Club members are

strongly opposed. But the best Nigeria could hope for would fall far short of what could be achieved with an IMF-blessed (preferably IMF-supported) program. Some temporary arrangement now would be helpful to avoid a situation where Nigeria must choose between further draconian cuts in imports and a purely unilateral rescheduling, (with the problems the latter would raise for trade financing and for willingness of lenders to cooperate in providing new money in the future). On the other hand, achieving too much in the way of formal rescheduling now would risk a disincentive effect on future policy reform.

42. In any event, if there are prospects of a good reform program the Bank's role is to try to convince the Paris and London Clubs that Nigeria merits the risk of additional new lending as well as long-term rescheduling. The argument here will have to focus on making a credible case that additional lending will indeed increase substantially the chances that the banks can go back to a normal and profitable lending relations with Nigeria. Both London and Paris Club financiers will probably claim initially that putting new money in is virtually impossible, but it is hoped they already recognize that without the kind of financial package proposed, the chances of substantial principal repayments to non-preferred lenders (or, more precisely, to those that are not maintaining or increasing their exposure) is slim at best. In this connection, the Bank would count on help from the London and Paris Clubs in insisting that other debt, including Eastern Bloc debt, be rescheduled on similar terms. The projections made in this paper conservatively do not take account of relief on other debt, since it is uncertain and the amounts are relatively small.

43. The Medium Term Adjustment Program will be difficult to put together and involves the risk of failure. But it is vital to the economic future (and restored creditworthiness) of the country where one in every four inhabitants of Sub-Saharan Africa reside.

NIGERIA: ANNUAL ACTION PROGRAM FOR 1987

The policy reform proposals would be implemented on the basis of annual action programs. This Annex outlines the program for 1987, although some of the actions could take place during the remainder of 1986. High priority actions are indicated by an *.

I. Exchange Rate, Trade and Incentive Policies

1. Initial discrete devaluation and then crawling adjustment.

2*. a. Finalize principles for operation of and activate second tier foreign exchange.
   b. Channel Bank funds (loan for export promotion and utilization of industrial capacity) through second tier market and match with multiple of Nigerian funds.

Import Controls and Taxes

1*. Modify customs tariff schedule, narrowing rates to 15 to 35 percent range.

2*. a. Liberalize import controls on raw materials and spare parts through their transfer to open general licence status.
   b. Formulate a plan for the phased liberalization of remaining import restrictions.

Internal Trade Controls and Taxes

1*. a. Relax ex-factory price controls on all goods.
   b. Formulate approach for shift to crop pricing structure which reflects market forces. Re-examine role of the six commodity market boards to setting of support prices for domestic crops (APP to be responsible).
   c. Further adjust petroleum product prices in line with exchange rate adjustments.

2*. a. Restructure excise tax on ex-factory production of all goods to fall within range of 5 to 25 percent, with appropriate offsetting provision.
   b. Apply additional excise taxes to both locally produced and imported luxury goods (50 or 100 percent or more).

Export Incentives

1*. a. Review and modify appropriate customs drawback scheme and other fiscal export incentives for non-oil exporters (including export traders and service exporters). This should include consideration of (i) putting all foreign transactions associated with non-oil exports through the second tier foreign exchange market; and (ii) allowing exporters wide latitude in what they import with their foreign exchange retentions.
   b. Simplify administration of incentive package.

Investment Incentives

1. Carry out studies to finalize coverage, design and administration of a package of fiscal investment incentives (undertaken jointly be the teams involved with ITAP and APP).

2. Streamline regulatory measures relating to industrial approvals.

3. Review legislation relating to foreign investment to allow greater ownership flexibility in some areas.

II. Public Resource Management Policies:

Public Expenditures

1*. Maintain restraints on public sector wage increases and extend freeze on recruitment to all but the most critical skills.

2*. In 1987 budget, reflect move to (i) restore levels of supplies relative to manpower; (ii) give priority to routine and periodic maintenance over new investment; and (iii) further reduce in transfers to commercially oriented parastatals (basis to be agreed within context of a rolling budget).

3*. Agree on restructured public investment program within context of sector strategies and (i) specify principles for the setting of priorities for completing ongoing capital projects; (ii)* re-assess ongoing and proposed new projects (with completion costs over ₦30 million) against these principles; and (iii) categorize projects into "core", "reserved core" and "non core" within context of agreed budget constraints and incorporate into rolling budget estimates.

4. Adopt a rolling multi-year budget. Begin with a two-year rolling budget.

Public Enterprises

1. Prepare a Statement of Policy on Public Enterprises.

2. Restructure the Ministry of Finance Incorporated (MOFI) or some other agency of Government to effectively support the Ministries in planning and executing public enterprise reforms.

3*. a. Carry out a rationalization program for parastatals.
b. Classify parastatals according to whether they should be left largely unchanged, restructured, privatized or liquidated (in-depth studies required for some enterprises).
c. Establish priorities and timetable for rationalization.
d. Prepare and commence implementation of restructuring sub-program building into it (i) increased autonomy of public enterprises in making operating decisions (management, procurement, staffing, etc.) and improved accountability (ii) further autonomy of public enterprises in setting tariffs and prices (iii) improved accounting practices, financial controls and management in public enterprises and (iv) rehabilitation requirements.
e. Prepare and commence implementation of privatization and liquidation sub-program.

4. a. Increase tariffs of NEPA (at least 25 percent, with further increases proposed for 1988 and 1989), NRC (50 percent), NET (amount to be determined) and NPA (amount to be determined). Establish parameters for the amalgamation of P&T with NET, ensuring adequate autonomy and management.
b. NEPA to improve bill collections and reduce operating costs. Plan to be prepared for closure of some branch lines etc. of NRC; to include plan for staff reductions of around 30 percent over next three years. NPA to initiate measures to minimize costs of maintaining secondary ports and to reduce staff by 10 percent.

III. Financial System Policies

1. Finalize program for restructuring the financial sector. To include means to: (i) reduce barriers to entry; (ii) encourage branch expansion in rural areas; (iii) further develop capital markets as a source of long-term finance; and (iv) improve existing agricultural credit delivery system.

2*. Adjust interest rates to reflect positive real and scarcity yields.

3*. Remove credit allocation ceilings.

IV. Sector Policies

1 a. Prepare statement of policy on agricultural development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.
b. APP to carry out necessary studies on agricultural product prices, marketing and incentives.

2. Prepare statement of policy on oil and gas development, incorporating principles for public investment and parastatal operations in the sector.

3. a. Prepare statement of policy on manufacturing development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.
b. Designate high level interministerial body for guiding and counseling the trade and incentive policy reforms (for both manufacturing and agriculture)
c. Industry studies for refineries, petrochemicals, steel and pulp and paper to be carried out as part of the work of ITAP, with the principal aim of reassessing approach to public involvement in the industries.

4. a. Establish a focal point in Government to facilitate and coordinate the implementation of the proposed National Population Program.
b. Prepare a five-year action plan to guide the inclusion of family planning in federal, state and local health services, and to assure its availability through other outlets.
c. Ensure program reflected in the expenditure plans of responsible ministries and of the states.

NIGERIA: MATRIX OF POLICY ACTIONS IN MEDIUM TERM ADJUSTMENT PROGRAM

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
EXCHANGE RATE, TRADE AND INCENTIVE POLICIES						
A. Exchange Rate: Move to a realistic level appropriate to the reformed trade policy environment.	1. Reconfirmation of policy of crawling adjustment of the exchange rate to reduce overvaluation of Naira.	1. Substantial initial devaluation and adoption of a more flexible exchange rate policy.				
	2. Proposal to establish a second tier foreign exchange market.					
	3. Implicit Devaluation through introduction of import surcharge (see I C 3 - Action recently taken) and export incentives (see I E - Actions recently taken).	2. Expand scope of second-tier foreign exchange market and move towards unification of the market with the 'formal' market.				
B. Export Controls & Taxes: Remove export controls and marketing restrictions on desirable non-oil exports.	1. Abolition of list of prohibited exports (with some exceptions).					
	2. Simplification of export licencing procedures.					
	3. Abolition of export monopoly power of the six commodity boards.					
C. Import Controls & Taxes: Dismantle import controls and move to a situation in which a relatively moderate and uniform customs tariff is the only form of direct intervention in import trade (with limited exceptions).	1. a. Promulgation of new customs tariff (1984) narrowing range of tariffs (10 to 60% with some exceptions). Adjustments made (post-1984) to correct anamolies.	1. Modify further customs tariff schedule, narrowing rates to 15 to 35% range.				
	b. Abolition of approved user and other schemes (1984) providing zero or concessionary rates to favored importers.	2. a. Liberalize import controls on raw materials and spare parts.				
		b. Formulate a plan for the phased liberalization of remaining import restrictions.				
		c. Implement liberalization plan.				
	2. a. Simplification of "two queue" system of import controls and introduction of measures to remove administrative abuses and block leakages in granting import licences.					
	b. Rationalization of priorities for issuance of import licences, with increased emphasis on (i) imports to support food production and (ii) raw materials and spare parts for manufacturers.					
	c. Creation of new category of import licences not valid for foreign exchange for approved priority imports.					
	3. Introduction of a temporary import surcharge of 30%.	3. Import surcharge to be replaced by appropriate exchange rate action.				
	4. Abolition of compulsory advance deposit requirement for imports.					

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
D. Internal Trade Controls and Taxes: Withdrawal of Government from direct intervention in price setting. Excise taxes used as a major revenue measure, with coverage, structure and level being consistent with the principles for the setting of custom tariff levels.	1. Adjustment of domestic petroleum product prices to remove financial subsidy (except kerosine).	1. a. Relax ex-factory price controls on all goods.				
		b. Formulate and implement approach for shift to crop pricing structure which reflects market forces. Re-examine role of the six commodity market boards and approach to setting of support prices for domestic crops.				
	2. Expansion of excise tax base (1984), with taxes re-structured to be consistent with new customs tariff schedule. Further modifications post 1984.					
	3. Creation of Agricultural Prices and Policy Group (APP) to be responsible for recommendations regarding price support and other trade policies relating to agriculture.	c. Adjust petroleum product prices in line with exchange rate adjustments.				
		2.a. Restructure excise taxes on ex-factory production of all goods to fall within range of, say, 5 to 25%.				
		b. Apply additional excise duties to both locally produced and imported luxury goods (say 50 or 100%).				
		c. Formulate (APP) and implement policies for taxation of forestry and agricultural products.				
E. Export Incentives: Introduce a package of fiscal incentives which removes impediments to exports and restores competitiveness of non-oil export production. Adopt other non-distortionary measures to promote non-oil exports.	1. Reactivation and modification of custums tariff drawback scheme.	1.a. Review and modify appropriately Customs Tariff Drawback Scheme and other fiscal export incentives.				
	2. Assistance on export costing and pricing (nature yet to be specified).	b. Adjust these and other export incentives as needed (including phasing out transitory elements of the package) to reflect progress of exchange rate and other trade policy adjustments.				
	3. Extension of the Foreign Exchange Retention Scheme to allow exporters to retain 25% of foreign exchange earnings.					
	4. Activation of an already created Export Credit Guarantee and Insurance Scheme.					
	5. Encouragement of establishment of Free Export Zones in selected part of the country. Revitalization of the Export Promotion Council. Requirement for authorized foreign exchange dealers to set up export desk for a export promotional activity.					

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	AJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
F. Investment Incentives: Introduce a set of fiscal investment incentives which are meaningful to investors, mininally distortionary and simple in their administration. Also improve other efforts to promote foreign and local investment in desirable production activities.		1.a. Carry-out studies to finalize the coverage, design and administration of a package of fiscal investment incentives.				
		b. Introduce incentive package.				
		2. Undertake other measures to improve investment promotion including:				
		a. Improve investment promotion operations of the existing Industrial Development Coordinating Division of the Industrial Policy Review Body.				
		b. Streamline regulatory measures relating to operations of enterprises and investment.				
		c. Review and ammend where necessary, investment policies and guidelines to promote desirable foreign investment.				

II. PUBLIC RESOURCE MANAGEMENT POLICIES

A. Level and Structure of Public Expenditures: Curtail public expenditures in a way which does least damage to the economy and ensures that maximum benefits flow from them. Composition of federal and state expenditures over the five-year adjustment period should support the macroeconomic policy reforms and reflect basic economic principles, with allocations at the sectoral level being made within the consectoral development strategies (see also sectoral Policies).	1. Reduction of salaries of public servants (1985). Freeze on hiring new public service staff in a wide range of positions (1984). Reduction of fringe benefits to public servants.	1. Stabalize public wage bill. (limits to be determined within the context of the rolling three-year budget see II B.1).				
	2. Reduction of non-statutory transfers to all economic and quasi-economic parastatals to 50% of present (1985) levels. Balance of needs to be obtained from increases in tariffs of parastatals.	2. Restore levels of supplies relative to manpower and give priority to routine and periodic maintenance over new investment (basis to be agreed within the context of the rolling three-year budget).				
	3. Major ongoing investment project (over N30 million to complete) reviewed by Inter-Ministerial Committee (with World Bank Technical Assistance - 1984).	3. Reduce and ultimately eliminate transfers to commercially-oriented parastatals to cover their operating deficits and capital expenditure program (with limited exceptions - see II.C).				
		4. Restructure Federal public investment program: within context of agreed (i) sector strategies; (ii) principles for setting priorities and (iii) budget constraints.				

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
PUBLIC RESOURCE MANAGMENT POLICIES (Continued)						
		b. Review public investment program annually in light of current revenue considerations, ensuring consistency with principles and sector strategies.				
B. Public Expenditure Planning and Budgeting: Improve budgetary process by adopting approaches to planning and budgeting which allow implications of resource prospects over an extended period to be taken into account in making decisions on projects and programs.		1. Adopt a rolling multi-year budget:				
		a. Begin with a two year rolling budget.				
		b. Expand to a three-year rolling budget.				
		2. Adopt a core-type approach to planning of capital, investment relating it to the rolling multi-year budget.				
Public Enterprises Improve overall efficiency of parastatals and reduce their heavy dependence on the Government for financial support. Privatize commercially oriented parastatals	1. Appointment of Study Group on Parastatals (1984). Report submitted.	1. Prepare a Statement of Policy on Public Enterprises.				
	2. Decision to divest of public holdings in commercially oriented enterprises (agricultural production, hotels, food, beverages, breweries, distilleries, distribution electrical electronic appliances and all non-strategic industries). Also, consideration to be given to reducing public holdings without losing control in banks, insurance companies and other financial enterprises.	2. Restructure and strengthen a.o. Ministry of Finance Incorporated (MOFI) to effectively support the Ministries in planning and executing public enterprise reforms.				
	3. Direction to parastatals to improve accounting practices and to issue timely financial reports. Accounts to be audited and published.	3. Within the context of sector strategies (see Sector Policies) carry out a rationalisation program for parastatals.				
		a. Classify parastatals according to whether they should be left largely unchanged, restructured, privatized or liquidated. Indepth studies required for some enterprises.				
		b. Establish priorities and time-table for rationalization.				
		c. Prepare and implement restructuring sub-program.				
		d. Prepare and implement privatization and liquidation sub-program.				

	ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
I	FINANCIAL SYSTEM POLICIES Reduce Government intervention in financial markets and allow more discretion to the financial institutions in their operations.	1. Announcement to review financial system with the aim of its restructuring. To include (i) review of barriers to entry in banking and finance (ii) overhaul of operations of Agriculture Credit Guarantee Scheme and the Nigerian Agricultural and Cooperative Bank (NACB), with emphasis on decentralization and closer cooperation of NACB with the commercial banks. 2. Announcement to narrow gap in the margin and spread of interest rates. 3. Credit allocation system simplified by reducing number of sector with ceilings from 8 to 4.	1. Prepare and implement program for restructuring the financial sector. To include means to (i) reduce barriers to entry (ii) encourage branch expansion in rural areas (iii) further develop capital markets as a source of long-term finance and (iv) improve existing agricultural credit delivery system. 2. a. Adjust interest rates to reflect positive real and scarcity yields. b. Phase out interest differential among sectors. 3. Elimate credit allocation system.				
IV.	SECTORAL POLICIES Prepare medium term development strategies for each sector, taking cognizance of broad policy reforms (as relevant), and address the specific policy and institutional reforms required to achieve development objectives in an efficient way as well as the appropriate schedule of public expenditures to support them. Special focus on the removal of bottlenecks and constraints affecting the efficient development of productive sectors.		1. Prepare strategy for agricultural sector. a. Prepare statement of policy on agriculture and water resource development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector. b. APP to carry out necessary studies on agricultural product prices, marketing and incentives. c. Ongoing revision and implementation of sector strategy. 2. Prepare strategy for oil and gas sector. a. Prepare statement of policy on oil and gas development, incorporating principles for public investment, and parastatal operations in the sector. b. Ongoing revisions and implementation of sector strategy.				

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
SECTOR POLICIES (Continued)	Establishment of Industry and Trade Policy Analysis Unit (ITAP) expected soon under World Bank Industry Technical Assistance Project loan to the Government. Will work in collaboration with APP to carry out trade and incentive policy analysis.	3. Prepare strategy for the manufacturing sector.				
		a. Prepare statement of policy on manufacturing development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.	[redacted]			
		b. Designation of high level interministerial body for guiding and counseling the trade and incentive policy reforms (for both manufacturing and agriculture).	[redacted]			
		c. Key industry studies to be carried out as part of the work of ITAP, with aim of: (i) identifying and formulating measure to overcome regulatory constraints and market imperfections affecting efficient development; (ii) reassessing approach to public involvement in the industries and (iii) providing information base for promotion of private investment. Priority to be given to studies of refineries, petrochemicals, steel, and pulp and paper.	[redacted]			
		d. Ongoing revisions (especially in light of findings of industry studies) and implementation of sector strategy.		[redacted]		
		4. Prepare strategies for education and health sectors.				
		a. Prepare statements of policy incorporating federal/state responsibilities, and principles for cost-recovery, public investment and recurrent expenditures.	[redacted]			
		b. Prepare multi-year public expenditure program (categorize core, reserve core, non-core) consistent with policy statement, budget constraints and principles underlying structure of public expenditure program. Relate program to state responsibilities.	[redacted]			
		c. Ongoing revisions and implementation of strategies.	[redacted]			
		5. Prepare, revise and implement strategies for other sectors.	[redacted]			

Key Indicators	ACTUAL 1980	1981	1982	1983	1984	ESTIMATED 1985	1986	PROJECTED: ADJUSTMENT POLICY SCENARIO 1987	1988	1989	1990	1991	AVERAGE 1987-91	AVERAGE 1992-95	1995	AUSTERITY POLICY SCENARIO 1987	1988	1989	1990	1991	AVERAGE 1987-91
GDP Growth Rate	2.3	-5.0	0.1	-8.2	-4.8	1.1	0.5	2.4	3.3	3.8	4.5	3.9	3.6	4.1	3.7	1.4	0.1	0.9	3.5	3.1	1.8
GNP Growth Rate	2.3	-4.9	0.1	-8.1	-4.8	1.3	0.5	2.4	3.3	3.8	4.5	3.9	3.6	4.2	3.7	1.5	0.1	0.9	3.5	3.2	1.8
GNY/Capita Growth Rate						-2.9	-7.7	-0.2	-0.7	-0.3	0.7	0.8	0.1	1.7	1.9	-1.2	-3.9	-3.3	-0.4	0.1	-1.8
Consumption/Capita Growth Rate	5.8	3.3	1.3	-11.6	-13.4	-6.9	-3.4	1.9	0.3	0.2	-0.6	-0.2	0.3	0.5	1.3	-0.2	-4.2	-3.7	-1.0	-0.7	-1.9
Total DOD ($ U.S.Billion)	4.37	6.14	9.01	12.34	13.70	18.11	18.36	19.63	21.05	23.02	24.09	24.84	22.5	22.9	20.1	18.53	18.05	17.04	14.97	12.02	16.1
DOD/XGS	0.17	0.32	0.71	1.13	1.11	1.38	1.77	1.73	1.80	1.89	1.73	1.58	1.7	1.1	0.7	1.63	1.55	1.40	1.08	0.77	1.3
DOD/GDP	0.05	0.07	0.11	0.17	0.19	0.25	0.28	0.38	0.52	0.64	0.60	0.56	0.5	0.4	0.3	0.25	0.22	0.19	0.15	0.10	0.2
Debt Service ($ U.S.Billion)	0.54	0.93	1.46	1.99	3.06	5.05	3.12	3.44	3.29	3.50	3.04	3.27	3.3	5.2	5.5	3.41	3.50	3.65	4.14	4.68	3.9
Debt Service/XGS (%)	2.1	4.9	11.5	18.2	24.8	38.6	30.0	30.3	28.2	28.7	21.8	20.8	25.9	23.3	20.3	30.0	30.0	30.0	30.0	30.0	30.0
Debt Service/GDP (%)	0.6	1.1	1.8	2.7	4.2	6.9	4.7	6.7	8.1	9.7	7.6	7.4	7.9	9.0	8.2	4.6	4.3	4.1	4.1	4.1	4.2
Interest/XGS (%)	1.7	3.0	6.4	9.6	9.5	11.5	15.2	20.1	18.1	19.1	14.9	13.0	17.0	8.5	5.6	19.9	17.0	16.5	11.2	8.1	14.5
Interest/GDP (%)	0.5	0.7	1.0	1.4	1.6	2.0	2.4	4.4	5.2	6.5	5.2	4.6	5.2	3.2	2.3	3.0	2.4	2.2	1.5	1.1	2.1
(Rates below are current/current)																					
Gross Domestic Investment/GDP (%)	23.6	29.7	24.1	17.4	12.9	13.7	14.0	15.0	16.8	19.1	19.5	20.2	18.1	22.0	22.9	12.3	12.1	11.8	11.7	11.8	11.9
Domestic Savings/GDP (%)	26.5	18.3	14.8	14.1	19.4	19.0	16.1	16.7	18.6	19.8	21.9	22.9	20.0	27.0	28.1	15.0	15.0	15.0	15.2	15.5	15.1
National Savings/GDP (%)	23.6	15.7	12.0	11.3	17.4	16.9	14.4	14.8	16.5	17.7	19.8	20.9	17.9	24.9	26.1	13.3	13.4	13.6	13.8	14.1	13.6
Marginal National Savings Rates (%)		-33.4	-23.9	-5.6	54.1	-2.8	-14.7	2.5	11.6	7.1	12.0	5.4	7.7	5.8	-0.2	-8.0	0.9	1.1	1.7	2.5	-0.4
Public Investment/GDP (%)	14.4	15.6	14.7	10.8	9.9	10.8	10.9	11.0	11.7	12.7	12.6	12.8	12.2	13.3	13.4	9.5	9.6	9.7	9.7	9.8	9.7
Public Savings/GDP (%)						11.2	9.6	9.0	10.2	11.2	11.7	11.8	10.8	14.9	15.8	7.8	6.5	5.3	6.6	6.1	6.5
Private Investment/GDP (%)	9.2	14.1	9.4	6.6	3.0	2.9	3.1	4.0	5.1	6.4	6.9	7.5	6.0	8.7	9.5	2.8	2.4	2.1	2.0	2.0	2.3
Private Savings/GDP (%)						5.7	4.8	5.8	6.3	6.5	8.1	9.1	7.1	10.0	10.2	5.5	6.9	8.2	7.1	8.0	7.2
Private/Public Investment (%)	63.9	90.4	63.9	61.1	30.3	26.8	28.2	36.1	43.8	50.6	54.8	58.4	48.7	65.1	71.1	29.9	25.3	21.7	21.1	20.4	23.7
ICOR													3.5	3.7							12.0 a/
Export Growth Rates (%)	-9.5	-32.3	-27.3	1.0	19.8	12.0	2.2	0.1	2.2	4.4	8.9	4.5	4.0	3.3	0.1	0.1	2.1	4.2	8.8	4.4	3.9
Exports/GDP (%)	28.9	22.8	15.9	14.7	17.0	17.8	15.6	22.0	28.7	33.9	35.0	35.7	31.1	38.6	40.5	15.2	14.3	13.6	13.6	13.6	14.1
Import Growth Rates (%)	21.9	18.2	-22.8	-22.1	-24.1	-12.2	-9.3	10.8	-1.6	2.6	2.2	5.5	3.9	7.8	11.8	-1.0	-6.8	-5.9	4.4	4.4	-1.0
Imports/GDP (%)	24.0	29.2	23.0	18.8	16.6	12.5	13.5	20.3	26.9	33.2	32.7	33.0	29.2	33.6	35.2	12.6	11.4	10.4	10.2	9.9	10.9
Current Account ($ U.S.Million)	-640	-6515	-7387	-4696	-92	2110	-483	-1715	-1719	-2446	-1521	-1264	-1733	602	1500	-605	66	504	1572	2558	819.0
Current Account/GDP (%)	-0.7	-7.9	-9.3	-6.4	-0.1	2.9	-0.7	-3.3	-4.2	-6.8	-3.8	-2.9	-4.2	0.9	2.2	-0.8	0.1	0.6	1.6	2.2	0.7
Terms of Trade Index	101.3	113.3	113.0	100.3	100.0	95.2	68.6	71.3	67.5	63.5	62.6	63.7	65.7	71.8	80.2	71.1	67.4	63.4	62.2	63.6	65.5
Non-Oil Export Growth (%)	15.4	-31.1	-35.4	63.6	-44.2	-24.6	35.9 b/	12.8	10.2	8.9	19.8 c/	4.4	11.2	4.9	5.2	10.0	5.8	-0.2	15.7	-3.0	5.6
Exports/GDP (Constant, %)	23.7	16.9	12.3	13.5	17.0	21.5	21.8	21.3	31.1	21.2	22.2	22.3	21.6	22.2	21.6	21.5	21.9	22.6	23.7	24.0	22.8
Imports/GDP (Constant, %)	25.5	31.8	24.5	20.8	16.6	14.4	13.0	14.0	13.4	13.2	12.9	13.1	13.3	13.9	15.1	12.6	11.7	10.9	11.0	11.1	11.5

NOTE: Inconsistencies may exist between current and constant ratios as a result of terms of trade and exchange rate adjustment. In the Adjustment Policy Scenario, three years of large real devaluations over 1987-89 of 70 percent is assumed and constant in real terms thereafter. In the Austerity Policy Scenario, no large devaluation assumed; the nominal exchange rate is assumed to be adjusted to compensate for half of the difference between international and domestic inflation each year.

a/ The ICOR is high since it includes two years with zero or negative growth. If it was calculated over a slightly longer period, the average would be around 7 to 8. Both ICORs are non-oil ICORs.

b/ Improved cocoa harvest.

c/ LPG comes on stream.

NIGERIA: Assumptions and Results of Financial Assessments

1. Tables 1-7 summarize the results of the various projections made of Nigeria's external balance. Table 1 presents the debt outstanding as of the end of 1985. Table 2 shows the import levels that would result if Nigeria pays all debt service as scheduled (i.e. no reschedulings) and receives new commitments only from IBRD and ADB. Table 3 presents these debt service obligations in more detail. Table 4 shows the effect on import levels of assuming a 30% limit on debt service payments without other new loans (the Austerity Policy Scenario). Table 5 presents the import levels that would result from the Adjustment Policy Scenario. Table 6 compares the two scenarios and displays the sources of the higher import levels in the Adjustment Policy Scenario. Table 7 describes the changes in exposure of the various creditors that would result from the Adjustment Policy Scenario. The detailed assumptions used to make these estimates are described below.

2. Oil Exports. Oil price assumptions are from the EPD base case. While the world oil price projections are much lower than previous forecasts, they are not as low for 1986 as current spot prices both because average selling prices are above spot prices at the moment and because markets may stabilize later in the year. Oil prices could be several dollars lower than in these projections, especially in the next few years. We have done sensitivity analysis assuming world oil prices fall to a level $10 below the EPD's base case. It is assumed that OPEC quantities will be higher in the future than they have been in recent years because the lower prices will stimulate demand and because non-OPEC supplies will be less forthcoming at these lower prices. In that environment, EPD assumes that Nigeria's share of OPEC production will decrease from 8.6% in 1985 to 8.1% (their official share) by 1988 in the base case.

3. Nigeria's production increases from 1.50 m.b./day in 1986 to 1.71 in 1990 to 2.0 in 1995.

4. Nigeria's price (including a $1 premium above the world oil price) is $21 in 1986, $24 in 1990, and $40 in 1995.

5. The estimates of domestic consumption are based on the best data for 1985 (.25 m.b./day) followed by a decrease to .23 m.b./day in 1986 due primarily to the recent increase in petroleum product prices. This grows to .242 in 1990 and .275 in 1995 in the Austerity Policy Scenario, and .247 in 1990 and .274 in 1995 in the Adjustment Policy Scenario. The two scenarios are quite similar because the higher GDP growth rates in the Adjustment Policy Scenario are offset by the effects of the higher prices for domestic products.

6. Non-Oil Exports. These numbers are taken from the macro model. The estimate for 1986 is $358 million in both scenarios compared to $270 million in 1985 -- most of that growth is in cocoa. From 1987 onwards the growth in real terms for manufacturing exports is 0% through 1989 and -2% thereafter in the Austerity Policy Scenario and 2% growing gradually to 12% in 1985 in the Adjustment Policy Scenario. Other agricultural exports grow very little in either case. Cocoa increases from 180,000 tons to 220,000 tons in the Adjustment Policy Scenario while actually decreasing from 1987 onwards in the Austerity Policy Scenario. Gas exports of $100 million have been added in both cases from 1990 onwards. By 1990 the difference between the two cases in non-oil exports is $190 million. By 1995 the difference is $520 million ($300 million in 1985 dollars).

7. Export NFS are assumed to be 3% of total goods exports.

8. Import NFS. This is comprised of two major parts: freight, insurance, and other services which vary with imports and repatriated profits which depend mostly on oil exports. Based on historical figures, the relationship has been 10% of imports + 4% of oil exports. In order to try to capture the recent changes in profit retention rules for the oil industry, the projections assume import NFS will be 10% of imports + 5% of oil exports beginning in 1986.

9. Other Balance of Payments Items. Travel is assumed to be included in the NFS imports. Direct foreign investment grows at zero per cent in real terms in 1986 in both scenarios and by zero per cent in nominal terms throughout the rest of the Austerity Policy Scenario. In the Adjustment Policy Scenario, the growth is zero per cent in real terms through 1987 and 2% in 1988, 3% in 1989, 4% in 1990, and 5% thereafter. The difference between the two scenarios is $146 million in 1990 and $439 million in 1995. Net transfers are constant in real terms in both scenarios.

10. MUV. The manufacturing unit value index (MUV) is used to deflate imports to a constant dollar value. The projections for the different countries are from EPD's latest estimates, but the weights used correspond to the shares of those countries in Nigeria's imports. The index that results grows by 6.7% in 1986, 6.0% in 1987 and 1988, 6.2% in 1989, 6.3% in 1990 and then falling gradually to 4.3% in 1995. The cumulative MUV to produce 1985 dollars values is 1.35 in 1990 and 1.73 in 1995.

11. MLT Debt. All figures on MLT debt are from EPD unless specified otherwise in these notes. Interest due, amortization due, and disbursements scheduled are provided for Paris Club, London Club, Multilateral Creditors, and other MLT for 1986-1995. EPD also provides end 1985 DOD. The only change in these projections is that larger amounts are assumed for World Bank and ADB disbursements which require adjusting the interest and amortization due to the World Bank and ADB. Disbursements from existing commitments are projected by EPD based on disbursement schedules and past performance. While some obviously non-operating loans have been eliminated, the projected disbursements are probably on the high side. To the extent that disbursements from existing commitments are less, however, disbursements from new commitments would most likely be more since creditors are concerned about total net exposure.

12. Arrears. The MLT figures already include $1.7 billion that represents the arrears that had been converted to MLT as of end 1985. From the remaining claims our projections assume the following amounts will be recognized and paid off as indicated.

Amount	Date of Recognition	Retroactive interest to Jan. 1, 1984 paid	Principal Repayments Due	
			Austerity*	Adjustment
$ 1.8	Jan. 1, 1987	1987	1987-1990	1987-1996
$ .5	Jan. 1, 1988	1988	1988-1991	1988-1997
$ .5	Jan. 1, 1989	1989	1989-1992	1989-1998

The interest rate in both cases is 1% above LIBOR. The principal is to be repaid over 3½ years in the Austerity Policy Scenario and 10 years in the Adjustment Policy Scenario.

* Note that the arrears will not actually be paid off in this period in the Austerity Policy Scenario because of the 30% limit on debt service.

13. Short-Term Debt. After lengthy discussions, EPD felt the stock as of end 1985 was $1-2 billion, IMF felt the number was not much over $750 million. These projections assume a level of $1 billion, yielding interest payments of $100 million per year. There are no payments on principal and no increase in exposure (not even with inflation) in either case.

14. Private Debt. All figures on private debt are from EPD. The stock at end 1985 is about $1 billion. The initial stock of debt, the disbursements from existing commitments and the amortization and interest obligations resulting from those are from EPD. It is unlikely that exposure to private borrowers will disappear in any scenario. The Austerity Policy Scenario assumes that new commitments will produce enough new disbursements to keep exposure to private borrowers constant in nominal terms over the period. In the Adjustment Policy Scenario, new disbursements vary with direct foreign investment yielding an increase in exposure from $1.1 billion in 1985 to $1.3 billion in 1990 and $1.9 billion in 1995.

15. De Facto Rescheduling. In the Austerity Policy Scenario, total debt service (public MLT, private, short-term, and arrears) is limited to 30% of total exports of goods and services. Payments are made in the following order.

1. interest and principal to multilateral creditors.
2. all other interest (including interest on rolled-over principal).
3. all other principal including rolled over unpaid principal from previous years.

Total debt service payments equal 30% of exports provided the sum of debt service owed, including rolled-over interest and principal, equals or exceeds that amount. As a result, the rolled-over balance is eliminated in 1993, the first year debt service falls below 30%.

16. World Bank and ADB Loans. For the Austerity Policy Scenario, the Bank continues to maintain a positive net transfer of resources to Nigeria; at a minimum, commitments are expected to be about $230 million in FY86, rising gradually over the ten years to reach $750 million in 1995. Should the medium-term framework improve over our Austerity Policy Scenario without spectacular breakthrough on the policy front, lending could increase more rapidly. Under a best policies scenario, with significant movements on the exchange rate and on import liberalization, project lending would increase over the years to $1.1 billion in 1995 plus a SAL and other quick disbursing loans averaging $500 million from 1987 to 1995. Total new commitments from the SAL and quick disbursing Bank loans would be $4.5 billion over the period. In all scenarios, the African Development Bank is assumed to provide $200 million per year in new commitments beginning in 1987.

17. IMF Loans. In the Adjustment Policy Scenario, IMF loan disbursements are assumed to be 60% of quota in 1987-1990 followed by a fifth year disbursement equal to amortization due in 1991. The 60% is applied to the present quota and that amount ($510 million) is used without adjustments for inflation. Because of the first repayment coming due in 1990 the IMF exposure reaches a peak of 220% of quota (4 x 60 - 20) in 1990 and 1991 declining rapidly thereafter. All IMF loans are repaid by 1994.

18. Official Rescheduling. In 1986, the 30% limit would apply exactly as in the Austerity Policy Scenario. The unpaid principal which is rolled over to 1987 becomes eligible for Paris and London Club rescheduling.

19. For both the Paris Club and London Club, 100% of the principal due 1987-1992 is rescheduled. Paris Club interest is not rescheduled. This would not actually be in the form of a six-year agreement. It would probably be in the form of a two-year agreement or even two one-year agreements followed by a four-year agreement. The difference is important in practical terms because of the closer monitoring and the ability of the creditors to cancel the agreement if progress is not satisfactory. For estimating the effects assuming progress is satisfactory, however, the multiple agreements are equivalent to a single six-year agreement. Repayment of the rescheduled amounts does not begin until 1993. All rescheduled amounts are repaid by 1997 in five even installments.

20. In the Adjustment Policy Scenario, the arrears are repaid over ten years rather than the 3½ years that have been the terms agreed to in the past. There is no rescheduling of private debt or other MLT (mostly COMECON countries) except that the unpaid principal arising from the 30% limit in 1986 is all assumed to be rescheduled in 1987.

21. Other New Financing. In the Adjustment Policy Scenario, additional borrowing is added to all of the other assumptions in order to reach a particular path of imports considered to be consistent with the macro-economic estimates for that scenario. This new money is assumed to come from London Club banks, Paris Club creditors, and others. The terms are three-years grace and then four years to repay. The total disbursements over the period for this new money is $3.9 billion.

22. Reserves. Foreign exchange reserve assets are estimated at about $1.1 billion at the end of 1985, about 1.6 months of imports of goods in that year. In both scenarios, this percentage is increased to two months of imports of goods. In the Adjustment Policy Scenario, this happens in 1987. In the Austerity Policy Scenario, we assume this is done gradually over the period 1987-1989. Thus reserve assets in nominal terms increase from $1.1 billion at the end of 1985 to $1.3 billion in 1980 and $3.2 billion in 1995 in the Austerity Policy Scenario and $1.7 and 2.9 billion in the Adjustment Policy Scenario.

EXTERNAL DEBT
($ Million as of 12/31/85)

	(Debt Outstanding and Disbursed)		(Undisbursed Debt)	
PUBLIC 1_/ MEDIUM AND LONG TERM	13,225		4,499	
PARIS CLUB CREDITORS		4,733		1,929
LONDON CLUB CREDITORS		4,516		1,194
MULTILATERAL INSTITUTIONS		1,339		954
OTHERS 2_/		2,637		422
SHORT TERM	1,000		0	
PRIVATE	1,081		N.A.	
TOTAL	15,306		4,499	
TRADE CREDIT ARREARS (NOT YET RECOGNISED)	2,800		N.A.	
TOTAL DEBT INCLUDING UNRECOGNISED ARREARS	18,106		4,499	

Note: 1_/ Includes public and publicly guaranteed debt.
2_/ Primarily bilateral loans from COMECON countries and trade credit arrears already recognised and issued.

NIGERIA'S EXTERNAL BALANCE
(Existing Debt Service Obligations)

- No rescheduling
- No New Loans (except ADB and regular IBRD)
- (Millions of Current US$)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Oil Export Revenues	12,447	9,735	10,636	10,884	11,342	12,860	14,577	16,489	19,021	22,139	25,185
Other Exports and NFS	651	661	726	776	809	949	1,020	1,098	1,197	1,316	1,436
Total Export Revenue	13,098	10,395	11,362	11,660	12,151	13,809	15,597	17,587	20,217	23,455	26,621
+ Disbursements	2,636	1,924	1,382	1,069	650	528	464	505	557	605	659
- Interest Due	1,502	1,440	1,788	1,260	1,082	646	531	478	449	442	455
- Amortisation Due	3,547	3,891	3,780	3,814	3,438	2,272	1,332	1,002	761	571	468
Other Balance of Payments Items	1,485	119	343	-61	-35	-67	-437	-321	-332	-380	-435
Imports of Goods and Services	9,200	7,108	7,519	7,595	8,246	11,352	13,761	16,292	19,232	22,668	25,923
Imports of Goods	8,000	5,975	6,304	6,360	6,929	9,677	11,781	13,986	16,533	19,500	22,307
Imports of Goods in 1985 dollars	8,000	5,599	5,574	5,305	5,442	7,150	8,228	9,267	10,433	11,764	12,903
Debt Service/Exports	39%	51%	49%	44%	37%	21%	12%	8%	6%	4%	3%
Total Debt Outstanding and Disbursed at Year's end	1 / 18,106	16,139	13,741	10,996	8,209	6,464	5,597	5,100	4,896	4,930	5,122

Note: 1 / Includes $2.8 billion in arrears not yet recognised.

(NIGERIA'S EXISTING EXTERNAL DEBT OBLIGATIONS)

- No Rescheduling
  Arrears = $ 4.5 billion
- (Current US $ million)
  No new loans (except ADB and regular IBRD)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
A. INTEREST											
Public	1,407	1,262	1,074	882	671	543	485	456	440	438	454
Paris Club	331	390	361	301	230	169	120	80	48	25	11
London Club	508	416	318	223	134	68	34	19	8	1	1
Multilateral	108	126	145	164	184	206	231	257	284	312	342
Short Term	100	100	100	100	100	100	100	100	100	100	100
Other	360	230	150	94	23	0	0	0	0	0	0
Private	95	89	74	56	40	26	14	7	4	3	2
Arrears 1 /	0	88	707	357	369	75	26	6	0	0	0
TOTAL 3 /	1,502	1,439	1,855	1,295	1,080	644	524	470	444	441	456
B. AMORTISATION											
Public	3,302	3,603	3,242	3,012	2,551	1,332	970	816	747	559	457
Paris Club	743	1,056	1,181	1,123	961	649	508	397	309	202	88
London Club	1,400	1,510	1,369	1,155	859	407	181	116	103	3	2
Multilateral	59	87	117	154	163	176	193	228	269	311	351
Short Term	0	0	0	0	0	0	0	0	0	0	0
Other	1,100	950	575	580	568	100	88	75	66	43	16
Private	245	288	281	216	158	140	76	43	14	12	11
Arrears 1 /	0	0	257	586	729	800	286	143	0	0	0
TOTAL	3,547	3,891	3,780	3,814	3,438	2,272	1,332	1,002	761	571	468
C. DISBURSEMENTS											
Public	3,577	1,795	1,307	1,036	636	528	464	505	557	605	659
Paris Club	1,174	849	486	301	206	84	2	0	0	0	0
London Club	560	498	356	321	17	2	0	0	0	0	0
Multilateral	276	285	727	343	378	432	459	507	556	601	659
Other	1,567	163	138	71	35	10	3	(2)	1	4	0
Private	359	129	75	33	14	0	0	0	0	0	0
TOTAL	2,636	1,924	1,382	1,069	650	528	464	505	557	605	659
D. NET FLOWS (C-A-B)											
Public	-1132	-3070	-3009	-2858	-2586	-1347	-991	-767	-630	-391	-251
Paris Club	100	-597	-1056	-1123	-985	-734	-626	-477	-357	-227	-99
London Club	-1348	-1428	-1331	-1057	-976	-473	-215	-135	-111	-4	-3
Multilateral	109	72	64	25	31	50	35	22	3	-21	-33
Short Term	-100	-100	-100	-100	-100	-100	-100	-100	-100	-100	-100
Other	107	-1017	-587	-603	-556	-90	-85	-77	-65	-39	-16
Private	19	-248	-280	-239	-184	-166	-90	-50	-18	-15	-13
Arrears 1 /	0	-88	-964	-943	-1097	-875	-311	-149	0	0	0
TOTAL	-1113	-3406	-4253	-4039	-3867	-2388	-1392	-967	-648	-406	-264

Note: 1 / Includes arrears not yet recognised. Some of the arrears are owed by the private sector.
2 / Totals consist of Public, Private and Arrears.

- Billions of Current US$.
- Limit on Debt Service Equals 30% of Exports.
- No New Loans (except ADB and regular World Bank).

NIGERIA'S EXTERNAL BALANCE
(Austerity Policy Scenario)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Exports Goods and Services	13.1	10.4	11.4	11.7	12.2	13.8	15.6	17.6	20.2	23.5	26.6
+ Disbursements	2.6	1.8	1.3	1.0	0.6	0.5	0.5	0.5	0.6	0.6	0.7
- Interest Paid	1.5	1.6	2.3	2.0	2.0	1.5	1.3	0.9	0.7	0.5	0.6
- Amortisation	3.5	1.5	1.1	1.5	1.6	2.6	3.4	4.3	2.9	0.6	0.5
+ Other Balance of Payments Items	1.5	0.1	0.1	.0	.0	0.1	-0.1	-0.1	-0.2	-0.6	-0.7
= Imports Goods and Services	9.2	9.2	9.3	9.2	9.1	10.2	11.2	12.7	17.0	22.3	25.5
of which: Imports Goods	8.0	7.9	8.0	7.8	7.7	8.7	9.5	10.7	14.5	19.2	22.0
Imports Goods 1985 Dollars	8.0	7.4	7.0	6.5	6.1	6.4	6.6	7.1	9.2	11.6	12.7

Memo items

Percent of Interest Paid	100	100	100	100	100	100	100	100	100	100	100
Percent of Principal Paid to Preferred Creditors	100	100	100	100	100	100	100	100	100	100	100
Percent of Principal Paid To Others 1 /	100	41	30	40	47	100	100	100	100	100	100
Cumulative Unpaid Principal	0.0	2.1	4.4	6.5	8.1	7.7	5.5	2.1	0.0	0.0	0.0
Debt Service/Exports	39%	30%	30%	30%	30%	30%	30%	30%	18%	5%	4%
Total Debt Outstanding and Disbursed 2 /	18.1	18.4	18.5	18.0	17.0	15.0	12.0	8.2	5.9	5.9	6.1

Note: 1 / Does not include rolled over principal from earlier years.
2 / Includes trade arrears not yet recognised.

NIGERIA'S EXTERNAL BALANCE
(Adjustment Policy Scenario)

(Billions of Current US$)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Total Export Revenues	13.1	10.4	11.4	11.7	12.2	14.0	15.7	17.8	20.5	23.9	27.2
+ Disbursements	2.6	2.6	1.8	2.4	2.6	3.1	2.0	2.0	2.0	2.8	1.9
- Interest	1.5	1.6	2.3	2.1	2.3	2.1	2.0	2.0	2.0	1.8	1.5
- Amortisation	3.5	1.5	1.2	1.2	1.2	1.0	1.2	1.8	3.7	3.9	4.0
+ Other Balance of Payments Items	1.5	0.1	-0.1	.0	0.1	0.1	0.1	0.1	0.1	0.2	0.1
Imports Goods and Services	9.2	9.2	10.3	11.0	11.9	13.0	14.5	16.1	17.7	20.3	23.6
of which: Imports Goods	8.0	7.9	8.8	9.5	10.3	11.2	12.4	13.8	15.2	17.3	20.2
Imports Goods (1985 Dollars)	8.0	7.4	7.8	7.9	8.1	8.3	8.7	9.2	9.6	10.5	11.7
Debt Service/Exports	39%	30%	30%	28%	29%	22%	21%	21%	28%	24%	20%
Total Debt Outstanding and Disbursed 1 /	18.1	18.4	19.6	21.0	23.0	24.1	24.8	25.1	24.2	22.2	20.1

Note: 1 / Includes trade arrears not yet recognised.

Comparing Scenarios

- Billions of 1985 US$.

	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
IMPORTS OF GOODS										
Full Debt Service	5.7	5.6	5.4	5.5	7.2	8.2	9.2	10.4	11.7	12.9
Austerity Policy Scenario	7.4	7.0	6.5	6.1	6.4	6.6	7.1	9.2	11.6	12.7
Adjustment Policy Scenario	7.4	7.8	7.9	8.1	8.3	8.7	9.2	9.6	10.5	11.7
COMPARING SCENARIOS										
Austerity Policy vs. Full Debt Service										
Total Difference in Import of Goods 1/	1.7	1.4	1.1	.6	-.8	-1.6	-2.1	-1.2	-.1	-.2
Adjustment Policy vs. Full Debt Service										
Official Rescheduling 2/	1.7	1.7	1.4	1.0	.4	-.2	-.4	-1.4	-1.5	-1.4
IMF Loans		.4	.3	.3	.1	-.1	-.4	-.3	-.3	-.1
Higher IBRD Loans		.1	.3	.3	.3	.3	.2	.2	.1	.1
Other New Loans		.1	.3	.7	-.1	-.1	-.1	.2	-.3	-.3
Higher Non-Oil Exports										
Other Differences 3/		-.2	.2	.2	.3	.5	.5	.3	.6	.2
Total Difference in Import of Goods	1.7	2.2	2.5	2.6	1.1	.5	-.1	-.8	-1.2	-1.2

1/ Due entirely to ceiling on debt service at 30% of export revenues.
2/ Includes longer repayment period for trade arrears.
3/ Includes differences in reserves, foreign investment, and private lending.

NIGERIA

SELECTED ANALYTICAL VARIABLES FOR ECONOMISTS AND MANAGERS

ATLAS PER CAPITA GNP (CUR) (1983) =770
POPULATION IN MILLIONS (1983) =93.642
LT DEBT OUTSTANDING AND DISBURSED IN MILLIONS (CUR)(1983) =13,031.16
BALANCE ON CURRENT ACCOUNT IN MILLIONS (1983) =-4,752

	HISTORIC DATA		REFERENCE YEAR	RECENT DATA		EST. DATA		PROJ.DATA	
	1960-1973	1973-1980	1980	1981	1982	1983	1984	1985	1986
GROWTH OF GDP AGGREGATES (CONST)					GROWTH RATES				
1.GDP	5.97	3.44	85,142	-5.07	-0.65	-6.69	-0.38	-3.15	-0.22
2. AGRICULTURE	1.00	-2.14	16,152	-2.97	7.77	-5.26	1.99	2.01	1.99
3. INDUSTRY	17.99	4.85	38,958	-13.52	-11.52	-8.43	..	..	..
4.GDP OUTPUT DEFLATOR	6.18	16.20	100	6.76	9.20	1.86	..	..	..
5.IMPORTS GNFS (NAT. ACCTS.)	7.24	17.57	20,980	24.36	-31.88	-40.81	..	..	..
6.EXPORTS GNFS (NAT. ACCTS.)	12.92	6.39	27,079	-26.64	-22.69	-23.76	..	..	..
7.MERCHANDISE EXPORTS (1)	8.21	-0.82	26,731	-31.30	-8.30	-18.89	25.24	..	..
8.DOMESTIC ABSORPTION	4.33	5.29	79,043	14.52	-4.47	-10.91	-13.75	-7.55	-2.23
9.INVESTMENT	11.68	6.69	21,152	7.60	5.70	-20.29	-56.14	-23.16	-5.67
10.PER CAP TOTAL CONSUMPTION	0.54	2.30	683	13.22	-10.90	-10.34	-3.00	-8.39	-5.05
11.POPULATION (MIL)	2.51	2.49	85	3.39	3.39	3.39	3.39	3.39	3.39
TRADE PRICE INDICATORS (1980=100)					INDICES				
12.TERMS OF TRADE OF AGR/IND	137.70	106.13	100.00	106.28	119.90	129.52	..	..	..
13.TERMS OF TRADE	47.26	103.80	100.00	102.58	92.15	89.07	..	..	..
14.TERMS OF TRADE (UNCTAD)	17.97	64.60	100.00	111.46	104.26	94.44	95.45	..	..
15.NOMINAL EFFECTIVE EXCHANGE RATE(2)	..	95.18	100.00	104.46	108.84	113.39	121.61	123.57	..
16.REAL EFFECTIVE EXCHANGE RATE(2)	..	96.13	100.00	112.70	114.95	132.97	194.95	241.26	..
INVESTMENT AND SAVINGS					RATIOS				
17.INVESTMENT/GDP (CURRENT)	18.8	26.4	24.8	27.5	22.1	19.1	..	..	..
18.INVESTMENT/GDP (CONSTANT)	14.1	26.1	24.8	28.2	30.0	25.6	11.3	8.9	8.5
19.DOMESTIC SAVINGS/GDP (CURRENT)	19.0	30.2	32.0	20.6	17.3	19.0	..	..	..
20.DOMESTIC SAVINGS/GDY (CONSTANT)	14.1	26.3	32.0	16.7	21.1	21.4	..	..	..
21.GROSS NAT. SAVINGS/GDP (CURRENT)	17.3	28.6	30.0	19.0	16.0	17.8	..	..	..
22.RESOURCE BALANCE/GDP (CONSTANT)	10.5	2.5	7.2	-7.7	-3.0	1.6	..	..	..
23.MARG PROPENSITY TO SAVE (CONSTANT)	53.1	40.5	-1,655.7	359.3	-138.6	16.4	..	..	..
24.TERMS OF TRADE ADJ./GDP (CONSTANT)	-9.9	0.6	0.0	0.6	-1.5	-1.7	..	..	..
25.ICOR (CONSTANT)	..	..	..	..	..	..	..	..	..

EPD 07/17/85

NIGERIA

	HISTORIC DATA 1960-1973	HISTORIC DATA 1973-1980	REFERENCE YEAR 1980	RECENT DATA 1981	RECENT DATA 1982	EST. DATA 1983	EST. DATA 1984	PROJ.DATA 1985	PROJ.DATA 1986
TRADE AND BALANCE OF PAYMENTS						RATIOS			
26.SHARE OF MANUF IN EXPORTS (CUR)(1)	2.1	0.8	..	..	..	..	..	..	..
27.IMPORT GDP ELASTICITY	1.2	5.1	274.3	-4.8	49.4	6.1	..	..	..
28.CUR ACCT BALANCE/GDP (CURRENT)(3)	-2.7	1.7	6.0	-7.8	-10.2	-7.1	..	..	..
29.RESERVES IN MONTHS OF IMPORTS OF GOODS AND SERVICES(3)	1.8	5.0	5.8	2.0	1.1	1.0	1.9	2.6	2.2
DEBT INDICATORS (4)									
30.LT DEBT SERVICE TO EXPORTS RATIO	4.9	2.4	2.9	6.7	12.6	21.0	28.5	34.9	47.6
31.LT INT. SERVICE TO EXPORTS RATIO	1.4	1.0	1.9	3.5	6.7	10.0	10.7	9.5	16.4
32.LT DEBT SERVICE TO GNP RATIO	0.9	0.7	1.0	1.7	2.3	3.5	..	..	..
33.DOD. LT PUB DEBT AT VIR/ DOD. TOTAL LT PUB DEBT	1.3	45.2	72.6	66.8	59.4	60.5	..	..	..
34.NET TRANSFERS/TOTAL DISB	-0.8	53.9	54.1	53.6	54.9	56.7	-39.6	30.1	-52.4
35.WORLD BANK DEBT/TOTAL LT DEBT	29.8	19.2	10.3	8.0	7.2	6.6	8.5	8.0	8.9
MONETARY INDICATORS (CURRENT)									
36.CHG IN CLMS GOV/GOV BUDGET BAL	..	..	..	..	..	..	..	..	..
37.CLMS GOV/CLMS PRIV SECT	89.3	45.2	52.5	70.6	97.7	139.8	151.3	..	..
38.MONEY SUPPLY/GDP	12.7	23.4	30.9	32.3	32.6	39.1	39.3	..	..
GOVERNMENT ACCT (CURRENT)									
39.DIRECT TAXES/GDP(5)	8.0	14.2	..	..	..	..	..	..	..
40.TOTAL REVENUE/GDP(5)	13.8	20.2	..	..	16.1	15.4	14.0	15.3	..
41.GOV. BUDGET BALANCE/GDP(5)	0.5	-3.2	..	..	-8.5	-13.6	-7.2	3.9	..
42.PUBLIC/TOTAL CONSUMPTION	9.6	15.9	15.7	13.5	13.0	14.1	..	..	..

EPD 07/17/85

NOTE: ALL REFERENCE YEAR VALUE DATA IN US$ 1980 MILLIONS, EXCEPT PER CAP TOTAL CONSUMPTION WHICH IS IN US$.
LEGEND: .. INDICATES NOT AVAILABLE
M INDICATES DATA IN MILLIONS

FOOTNOTES:
(1) SERIES STARTS IN 1962.
(2) US$/LOCAL CURRENCY. SERIES STARTS IN 1979. INCREASES INDICATE APPRECIATION; DECREASES INDICATE DEPRECIATION.
(3) SERIES STARTS IN 1967.
(4) SERIES STARTS IN 1970; STOCK AND FLOW FIGURES IN 1983 REFLECT TWO COMMERCIAL BANK LOANS TO REFINANACE $3.9 BILLION OF SHORT-TERM DEBT INTO PUBLIC LONG-TERM DEBT. 1986 DATA ASSUME ADDITIONAL LONG-TERM REFINANCING OF $2.5 BILLION DOLLARS OF SHORT TERM TRADE ARREARS.
(5) SERIES STARTS IN 1972 AND ENDS IN 1978.

MANAGEMENT SUPPLEM

SAVEM TABLES

SELECTED DEBT INDICATORS

1975-1985

NIGERIA

	1975	1980	1981	1982	1983	1984 /a	1985 /b
I. VALUES (in current US$, billions)							
1. Long Term (LT)	1.19	5.37	7.49	9.86	13.03	12.71	15.90 /c
2. Short Term (ST)	..	1.19	1.75	2.78	6.69	7.00	3.10
3. Total Debt (DOD)	1.19	6.56	9.24	12.64	19.72	19.71	19.00
4. Interest	0.05	0.67	0.87	1.17	1.62	1.98	2.05
5. Amortization	0.23	0.28	0.64	0.84	1.23	2.19	3.35
6. XGS, (nominal)	9.13	27.75	19.65	13.81	10.99	12.32	13.19
II. RATIOS (percent)							
7. DOD/XGS	13.1	23.6	47.0	91.5	179.4	160.0	144.0
8. TDS/XGS	3.0	3.4	7.7	14.5	26.0	33.9	40.9
9. INT/XGS	0.5	2.4	4.4	8.5	14.8	16.1	15.5
III. GROWTH RATES (nominal)							
10. DOD (% change)	-8.5	33.5	40.8	36.8	56.1	-0.1	-3.6
IV. VULNERABILITY COEFFICIENTS							
11. VIR/DOD (%)	6.2	77.7	74.0	69.2	74.4	72.4	67.2
12. Concessional/DOD (%)	40.6	7.9	5.0	3.3	2.3	2.0	2.4
13. Preferred Creditors/DOD (%)	30.6	8.7	6.8	6.0	4.6	5.6	6.8
14. Average Cost of Funds (%)	3.8	11.7	11.0	10.7	10.0	10.1	10.6
15. ST/DOD (%)	..	18.1	18.9	22.0	33.9	35.5	16.3 /c
16. Average Maturity (yrs)	17.1	8.8	8.2	7.7	4.5	6.0	5.3
Memorandum Item:							
Use of IMF Credit (in US$, millions)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Service Charges:							
(Repurchases)							
(Charges)							

a. Preliminary.

b. Estimated figures for 1985 assume a $3.9 billion refinancing of short-term debt outstanding at end-1984.

c. Reflects the rescheduling of $3.9 billion into long-term debt.

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

DATE March 24, 1986

TO Mr. Vinod Dubey, Director, CPD

FROM Ismail Serageldin, Acting Vice President, WAN IS

EXTENSION 72305

SUBJECT NIGERIA - Medium Term Growth Strategy Paper

Please find enclose ~~5~~ 16 copies of the draft Medium Term Growth Strategy Paper for Nigeria. This has now been cleared by Mr. Thalwitz.

cc: Messrs. Thalwitz o/r, Alisbah, Humphrey, O'Brien, Eccles, Isenman, Beguery.

TAllen:pm

NIGERIA

MEDIUM TERM GROWTH STRATEGY PAPER

Table of Contents

March 24, 1986

SUMMARY

(i) Nigeria's political and administrative structure proved ill-equipped to absorb the sudden oil riches that flowed in starting in 1973; it was even less able to deal with the sharp continued downturn in oil earnings the country has faced over the past four years. There were some notable successes, particularly in building up physical and social infrastructure. But there was widespread waste and corruption and the laying waste of much of the agricultural base of the economy. The economy became almost completely dependent on the oil sector and extremely vulnerable to external shocks. With the decline in oil earnings came two years of dithering (1981-83), two years of what the current President correctly referred to as "austerity without structural adjustment" and two changes of government. The new military Government's budget of December, 1986, announced a number of significant measures initiating an adjustment process. However, the Government judges it politically too risky to reach an agreement with the Fund, and its reform program still has no more than a down payment on exchange rate reform. Lack of a Fund agreement stands in the way of debt rescheduling with the London and Paris Clubs. In the absence of a broad compact with the international financial community involving a formal rescheduling and some substantial new lending, it is unclear how long the Government would be able to pursue further reforms necessary for the adjustment effort. And without a strong reform and financing package, it would be difficult for Nigeria to service its debt in an orderly manner without a precipitous decline in per capita consumption. The seriousness of the problems, the recent policy progress and Nigeria's large share of sub-saharan Africa's total population and economy all suggest the high priority of a leadership effort by the Bank to put together such a reform and financing package.

(ii) The Medium Term Adjustment Program proposed provides the basis for improved creditworthiness, renewed growth and in the longer run a restructured economy based on the non-oil sectors. The adoption of a program along the lines proposed - involving both policy and financial packages - would require a strong political commitment by the Government and greater diligence in curbing corruption and motivating the bureaucracy to meet the challenges ahead.

(iii) Adjustment Policy Package. A broad program has been evolved focussing on improving the efficiency of resource use and encouraging desirable private investment. The package builds on the recent policy initiatives of the Government with the priorities being to: (i) correct the still misaligned relative prices through exchange rate adjustment, liberalized import controls (including appropriate trade tax adjustments) and dismantled price controls; (ii) overcome the considerable public sector inefficiencies through improved public expenditure programs and the speedy rationalization of the parastatal sector; and (iii) reduce the severe imperfections in the financial system, principally through appropriate interest rates. Tight discipline on monetary expansion would have to be maintained with the Government continuing to place strict constraints on the budget deficit. While improved revenue measures should be pursued, these should not be seen as a substitute for a slimmer bureaucracy and the privatization of public commercial activities.

(iv) Adjustment Financial Package. Additional external financial support is proposed through both a rescheduling of Nigeria's existing debts with the Paris and London Club financiers and through new money commitments (including Bank quick disbursing loans). The severity of Nigeria's debt situation relates not so much to the size of the debt overhang, but to the unfavorable payments profile and poor immediate outlook for oil. In recognition of this and in order to keep new money requirements within feasible limits, consolidation of a group of maturities under a multi-year rescheduling would be desirable (preferably through a two-step MYRA). However, Nigeria's large trade arrears would have to be subject to extended repayment arrangements. There is also, a substantial need for new funds from the multilateral institutions and the commercial banks. The financial package proposed involves an increase in external debt outstanding of around $7 billion by the end of 1991, with the commercial banks accounting for around half of this increase. The rescheduled debt and new funds will permit import levels at an average of just over $8 billion (1984 prices) per annum over the 1987-91 period, still far below the levels of the early 1980s but $1½ to $2 billion above what could be achieved without the package.

(v) Adjustment Policy Scenario. Even with the adoption of an adjustment policy package and agreement on a financial package of the order of magnitude specified above, it is unlikely that GDP growth would greatly exceed an average of 3½ percent per annum over the 1987-91 period, rising to around 4 percent per annum through to 1995. These rates are consistent with the Government's expressed desire to contain debt service and new external financing to sustainable limits, and to prevent any further decline in per capita consumption over the next few years with modest but steady improvement in the 1990s. While the external debt outstanding in 1995 of around $20 billion under this scenario is slightly in excess of the present level, it would represent a much lower debt service level (20 percent of exports compared with the present level of 40 percent). Over the long term, a curtailment of the high population growth rate will be critical to the efforts to improve living standards.

(vi) Implementing the Adjustment Program. In view of the current reluctance of the Government to formalize an agreement with the Fund, the Bank will initially have to play the lead role. The next step is to build on the policy dialogue the Bank has pursued with the Government and convince it to adopt an adjustment policy package along the lines outlined. This would include continuing efforts to bring about some form of agreement with the Fund and to explore the means through which this could be achieved. It will be necessary to show the Government not only that substantial additional import financing will be available but that the adjustment program will lead to structural changes setting the foundations for sustained future growth based on non-oil sectors. To convince the international financial community to advance Nigeria significant levels of new funds it has to be concretely illustrated that the Government has the political will and discipline to carry out the necessary further reforms, and that the returns from the use of the funds are sufficient to service the extra debt. In this respect, the role of the Bank and the Fund will be crucial.

I. INITIAL CONDITIONS

A. Economic Performance

1. Structural Legacy of the Oil Boom (1973-80). The buoyant oil market over the 1973-80 period dramatically altered Nigeria's resource position. During this time the main objective of the Government was to translate the large oil revenues into investments in social, economic and physical infrastructure. While there were successes - a large functional network of interstate roads was established, power generating capacity tripled, primary enrollment ratio doubled - the political and administrative systems at federal and state levels were not equipped to handled adequately the new-found wealth. Rampant corruption and gross economic mismanagement resulted in considerable leakages of public revenues and wasteful expenditures, while the policies pursued led to structural changes which made the economy vulnerable to external shocks, i.e.:

- The economy became almost completely dependent on the oil sector. By the beginning of the 1980s oil earnings accounted for 96 percent of exports and over 80 percent of Federal Government revenues. These earnings supported a real growth in investment of 9 percent per annum (reaching 24 percent of GDP in 1980) financed almost entirely out of national savings (26 percent of GDP in 1980).

- The structure of production shifted away from the non-oil producing sector towards construction and other services. Inflation, an appreciating naira and poor pricing policies eroded the competitiveness of non-oil traded good production. Its share of non-oil GDP fell from around 55 percent in the early 1970s to under 40 percent in 1980. The impact on the agricultural sector - the major source of GDP and exports before the oil boom - was particularly severe; by 1980 its share of non-oil GDP had fallen to 30 percent from around 50 percent in the early 1970s. Exports of palm products and groundnuts (of which Nigeria was the largest world exporter) had disappeared.

- Domestic expenditure and production became highly dependent on imports. Within a decade Nigeria became a major food importer. Expectations of greater individual wealth enhanced conspicuous consumption of imported luxury goods. The structure of trade taxes and controls encouraged the growth of import-based light consumer good industries which contributed little to value added. By 1980 imports had reached a level of 24 percent of GDP, nearly double the percentage prevailing in the immediate pre-boom years.

- The public sector grew immensely in size and importance. Nigeria entered the 1980s with around half of its GDP and two-thirds of its modern sector employment accounted for by the public sector. Government recurrent expenditures had risen to 11 percent and public investment to 15 percent of GDP, the latter accounting for over half of total investment. A large part of the recurrent expenditures supported an inflated civil service. Many of the public investment projects (e.g. steel mills, certain large scale irrigation projects) were undertaken without sufficient attention to their viability, the appropriateness of their design and the implementation

capacity of the Government agencies. (The private sector was handicapped by red tape and was led to uneconomic investment decisions by misaligned prices.) The indigenization decree of 1972 laid the foundation for the Government's large-scale participation in the banking, insurance and industrial sectors. By the beginning of the 1980s, there were around 70 non-commercial and 110 commercial federal public enterprises, many of which required extensive financial support to cover operating losses.

2. The Economic Crisis (1981-85). Nigeria was thus ill-equipped politically, administratively and structurally to deal with the abrupt end of the oil boom in 1981. Partly because of expectations that the downturn would be short-lived, but mostly because of lack of political discipline, the Federal and State Governments failed to respond quickly to the plunging oil revenues with strong measures aimed at curbing and redirecting expenditures. They continued, for example, to implement the ambitious public investment programs prepared in the wake of the 1979 oil price hike. Consequently sizeable external and fiscal imbalances emerged; external reserves fell abruptly and at the same time there was a large-scale accumulation of private arrears on top of substantial public borrowings to finance the investment programs.

3. The excesses of the civilian Government and its inability to come to grips with economic realities led to a military takeover at the end of 1983. Through the almost exclusive use of demand management policies involving massive expenditure cuts and the stringent application of import controls, the military Government reduced the budget deficit to GDP ratio from 10 percent in 1983 to 5 percent in 1985 and the external account deficit to GDP ratio from 5 percent to zero. However, it failed to adopt substantial measures to reduce the serious misalignment of relative prices, the complex administrative controls and the public sector inefficiencies. The Government was unable to reach agreement with the IMF for an EFF program which would have paved the way for a structural adjustment loan from the Bank and debt rescheduling by creditors. The naira continued to appreciate (although this was marginally reversed in 1985). Sectoral ceilings for credit allocations by banks were enforced and interest rates were, until recently, at levels resulting in negative real yields. While actions were taken to improve the system of trade taxes, continued price and other trade interventions served to reinforce distorted signals. Moreover, fiscal austerity was characterized by expenditure constraints without sufficient regard to necessary expenditure reallocations. Public investment cutbacks proceeded across the board with little cognizance of priorities and stage of completion. Outlays on supplies, spare parts and routine maintenance were eroded dramatically. Significant sums were set aside to support operating deficits of grossly inefficient parastatals and to provide uneconomic subsidies.

4. In essence, the structure of the economy inherited from the oil boom remained intact and as a result, with the sharp deterioration in the terms of trade, economic performance over the 1981-85 period was dismal:

- Production and employment in all sectors, except agriculture, remained depressed, with real GDP in 1985 being some 15 percent lower than at the beginning of the 1980s. Construction and other service sectors were hard hit by the diminished public expenditures and declined at a faster

rate than GDP. The drastically reduced supplies of raw materials and spare parts to the import-hungry industrial sector led to widespread plant closures, a substantial drop in capacity utilization (averaging 25 to 35 percent) and extensive layoffs of the workforce. Severe shortages of goods boosted the inflation rate - peaking at around 40 percent in 1984 but receding thereafter - with scarcity rents of up to 400 percent for many essential goods accruing to traders who, unlike manufacturers, were not subject to price controls. The population growth rate of an estimated 3.3 percent per annum means significant declines in per capita real income and consumption; in 1985 these were well below the levels recorded in the pre-oil boom 1970s.

- The reduction in investment expenditures was severe. Investment as a proportion of GDP fell to under 14 percent of GDP in 1985, half the peak level of 1981. The across-the-board public expenditure cutbacks meant further delays in completing viable projects thus escalating their costs and depriving the economy of their benefits. Private investment shrank at twice the rate of public investment and by 1985 constituted only a quarter of the total.

- National savings halved in real terms due to the decline in both GDP and terms of trade, with the savings ratio in 1985 being around 17 percent of GDP. Meanwhile, external debt service requirements increased tenfold (to 40 percent of exports) and continue to accelerate. The external debt outstanding and disbursed at the end of 1985 of $18.1 billion included $11.5 billion of medium and long-term public debt (excluding officially recognized converted trade arrears of $1.7 billion) of which Paris and London Club creditors each accounted for around one-third. Moreover, Nigeria accumulated substantial trade arrears estimated to range between $3.5 and $6 billion; although the level and timing of arrears recognition is still open to debate, $4.5 billion has been used in this paper. There are also short-term external debts of around $1 billion and private external debts of a further (estimated) $1 billion. The severity of Nigeria's debt situation relates not so much to the size of the debt overhang (which in 1985 amounted to around 140 percent of exports compared with the 255 percent average of all middle income heavily indebted countries) but to the unfavorable payments profile and the poor outlook for the oil market (see Annex D).

B. Adjustment Efforts

5. Policy Initiatives of the New Government. In the face of the continually weak oil market and mounting debt service burden, it was painfully obvious that demand management policies alone would be insufficient to bring about sustainable external and fiscal positions. Moreover, the rescheduling of external public debts could not be avoided for long. The international financial community was thus hopeful that the new military Government which came into power in August 1985 would address the structural weaknesses of the economy and reach an agreement with the IMF so as to pave the way for external financial support and renewed growth. While the Government declared its intentions to complement "austerity with structural adjustment", it submitted the desirability of an IMF agreement involving a major devaluation to a national open debate. The public gave a resounding "no" and the Government formally announced it

would not pursue negotiations with the IMF. Approaches have been made to creditors about debt rescheduling arrangements, but the Paris Club has said that an upper credit tranche program with the IMF would be required before such arrangements would be contemplated. The new Government announced measures (mainly in the 1986 budget statements) which, if fully implemented, makes significant progress in energy pricing and a good start on exchange rate, public expenditure and parastatal reforms. The principal ones are as follows (see Annex B for a list of the measures):

- Exchange rate, trade and incentive policies. An across-the-board temporary import surcharge of 30 percent was introduced to serve as an implicit devaluation on the import side. A second tier foreign exchange market operated by the commercial banks is proposed to be established, funded by residents with foreign currency bank accounts - including retentions of non-oil exporters - wishing to purchase naira. To boost further non-oil exports the customs tariff drawback scheme was reactivated and the foreign exchange retention allowance of non-oil exporters raised from 10 to 25 percent. Also, the export licensing procedure was simplified, the list of prohibited exports abolished (with some exceptions) and the export monopoly power of the six commodity boards discontinued. No significant steps were taken towards dismantling quantitative restrictions although procedures were simplified and a new category of import licences introduced which allows individuals to finance imports with privately held foreign exchange without recourse to the Central Bank. However, outright bans were placed on some products (e.g. rice, vegetable oil). By increasing the prices of petrol 100 percent and diesel 150 percent (kerosene prices were left unchanged) their financial subsidy was removed; the fertilizer subsidy is also to be phased out by 1989.

- Public resource management policies. The budget incorporated further measures for financial stabilization which, if carried out in full, would bring the federal budget deficit down to only 2 percent of GDP in 1986. Substantive reductions were made in the salaries and fringe benefits of civil servants and the freeze continued on hiring staff in a wide range of positions. Transfers to commercial parastatals are to be cut to 50 percent of their 1985 levels. The Government intends to divest itself of public holdings in commercially oriented enterprises and to entrust to the private sector the procurement and distribution of fertilizers and other agricultural inputs.

- Financial system policies. The credit allocation system was simplified by reducing the number of sectors with ceilings on bank lending from 8 to 4 and narrowing the spread of interest rates.

6. Limitation of Initiatives. While the announced measures make major strides in key policy areas, they still fall short of the requirements for a viable structural adjustment effort. Lack of direct action on the exchange rate and import liberalization is a major shortcoming, with the 'dirty' devaluation implied by the announced measures of 30 percent for imports and 20 to 30 percent for non-oil exports being barely adequate as a first step. (The IMF estimates the equilibrium rate of the naira to fall within the range $0.25 to $0.68 per naira, more likely closer to the former, compared with its present rate of $1 per naira.) Although the Government reconfirmed the policy of crawling adjustments to

the exchange rate, no adjustments have been made since the end of 1985. The export incentives introduced are far from sufficient to offset the discriminatory effects of the import protection system and exchange rate policy on non-oil exports. Reliance on funding the second tier exchange market from the foreign currency domiciliary accounts system will in all likelihood result in an insignificant market. Nigerians with funds outside the country appear to be extremely reluctant to repatriate them since few have confidence that they will not be questioned as to their source and penalized by this or a future administration; the exclusion of marketing boards' export earnings from the retention scheme also reduces considerably the size of the funding base for the market. The mechanisms for operating the market are not yet in place, and if the time taken to introduce regulations for the operations of the foreign currency domiciliary accounts system is a guide, then it could be many months before the market is operating. The measures relating to petroleum and fertilizer prices are laudable, but the continued controls on ex-factory prices overwhelmingly favors traders over producers. The heavy taxes and retentions of the six commodity marketing boards (cocoa, rubber, cotton, groundnut, soya bean and palm oil) have not been adequately addressed. Despite the decrease in budgeted capital expenditures for 1986 and the declared aim of allocating them on the basis of efficiency considerations, the cuts appear to be across-the-board with little cognizance of the economic viability of projects and their costs to complete (e.g. continued large expenditures on Ajuokota steel, petrochemical plants). There is no plan of action for the privatization of the commercial public enterprises and the liquidation of clearly unprofitable ones, nor for overcoming the operating inefficiencies of non-commercial parastatals, despite the fact that a number of officially backed investigations have been undertaken with this purpose in mind over the years (e.g. the Onosode Commission in 1981 and the Study Group on Parastatals in 1984). Finally, the regulatory framework for the financial sector remains complex, including the maintenance of strict ceilings on the structure and levels of lending and deposit rates, hampering the efficient mobilization and allocation of financial savings. Interest rates have not been adjusted since 1984 and real interest rates risk becoming negative again should inflation pick up.

C. Development Prospects

7. Nigeria has exhibited over the last two years the political will for austerity and now appears to have found the political will to make a beginning on structural reforms. The Government has announced its intention to pursue further reforms. However, it is unclear how far it would go (particularly on exchange rate adjustments and import liberalization) and how long it would stick to a major and unpopular reform program in the absence of a broad compact with the financial community involving a formal rescheduling of debts, new funds and the discipline imposed by IMF-type monitoring. Without financial support, it is difficult to envisage a scenario in which Nigeria would be able to service debt in an orderly manner and at the same time avoid a precipitous decline in per capita output and consumption.

8. Austerity Policy Scenario. The uncertainties of the oil market, of the "cold" rescheduling option that would be adopted (and the reactions of the international financial community to it) and of the effects of lower

import levels, make it extremely difficult to predict what the macroeconomic picture might look like if Nigeria did not reach an acceptable arrangement with the IMF and thus did not come to any formal agreement with its creditors. However, an Austerity Policy Scenario for the 1987-91 1/ period has been constructed on the basis of EPF's oil projections 2/ in which the rescheduling of debt service obligations is accomplished de facto by the Government's unilateral imposition of its already announced target on such payments of 30 percent of export proceeds; this would allow payment of all interest and some principal, with external debt outstanding at the end of 1991 being reduced to around $12 billion (under 80 percent of exports). No new commercial funds would be made available, while the Bank and ADB would continue to maintain positive net transfer of resources but on scaled back programs (see paras 36 to 40). The Government's diligence in pursuing the reforms already initiated is uncertain, although the momentum for reforms would slow down as the effects of reduced foreign exchange resources become more pronounced. Continued reliance would be placed on demand management policies and administrative controls to achieve external and fiscal balance with the real exchange rate continuing an appreciating trend.

9. Even if there were no adverse reaction from creditors, GDP growth rates under this scenario would at most average under 2 percent per annum over the 1987-91 period and its political feasibility would be questionable. Increased compression of imports of goods to an average of around $6½ billion (in 1984 prices) would be necessary. The scarcities of raw materials resulting from these cuts would force further reductions in capacity utilization in industry. The worsening shortages of commodities (including foodstuffs) would contribute to a high (around 20 percent per annum) inflation rate and although import replacement production would be encouraged (particularly in agriculture which would grow by just over 2 percent per annum), it would be generally high cost. The recourse to restrictive policies and administrative controls to achieve the needed savings and current account surpluses to meet debt service obligations would perpetuate production inefficiencies. The continued pursual of uneconomic public sector projects (e.g. steel) and escalating costs associated with implementation delays (due to shortage of funds) would reinforce this tendency resulting in high ICORS of around 7 to 8 over an extended period. Private investment would further stagnate - particularly foreign investment because of the deteriorating financial climate - with overall investment averaging under 12 percent of GDP over the 1987-91 period. This scenario implies increasingly severe unemployment problems

---

1/ 1986 is seen as a transition year. This is because (i) of hesitations on the part of the Government in committing itself to a development course and (ii) Nigeria has suffered a large income loss and will have to absorb much of the impact during this year.

2/ EPD projects (i) a world price of $20 a barrel in 1986 and $22 in 1987 and (ii) Nigerian production of 1.5 mbd in 1986 and 1987. Nigerian oil commands a $1 premium. (see Annex D for projections of later years).

and further sharp reductions in living standards, with per capita consumption falling by nearly 2 percent per annum. National savings performance would deteriorate only slightly over the period to 14 percent in 1991 (noting that this represents a significant decline from its 1985 level of 17 percent). Conditions could improve during the 1990s if oil markets strengthen as anticipated and the reduced debt service requirements allow higher import levels. However, the economy would be plagued with inefficiencies and deteriorated plant and infrastructures. It would also continue to be heavily dependent on the health of the oil sector and, given Nigeria's very high population growth, the pursuit of such a limited strategy would not provide solid foundations for growth in the post-oil era.

10. The unilateral adoption by the Government of an interest only rescheduling option (which would presumably include principal repayment to preferred creditors and to creditors continuing disbursements on existing loans) would allow Nigeria to have relatively higher import levels than would the declared 30 percent debt service target; on average 15 percent higher annual import levels would result over the 1986-91 period, which would translate into an increase in the GDP growth rate to 2 to 2½ percent per annum. Other options are also possible and the Government would presumably take into account terms being achieved in rescheduling arrangements by other countries in making its decision. However, unilateral "cold" rescheduling over an extended period could lead to an adverse reaction by creditors which, in turn, would frustrate the Government's ability to maintain any growth momentum; this reaction is likely to be more pronounced with the interest only rescheduling option. In particular, it would have damaging effects on the availability of trade credits to Nigeria. Export credit agencies would not be likely to extend cover which would make it almost impossible to finance new capital projects.

11. The macroeconomic situation would be extremely bleak under the Austerity Policy Scenario if oil prices weakened further than anticipated, bringing even more into question the political feasibility of the scenario. For example, if world prices for the next two years fell to $10 a barrel, then Nigeria would have to pump at its present full capacity production of some 1.8 mbd 3/ and cut its import levels by a further 20 percent in 1987 if it were to continue to meet interest obligations on external debt. Import of goods have already fallen by half since the early 1980s (to $8 billion in 1985) and although econometric studies of Nigeria's import demand have been carried out, it remains difficult to know to what extent imports can be further compressed without reducing consumption to politically unacceptable levels and restricting current and investment

---

3/ Nigeria could increase production beyond 1.8 mbd but marginal costs are expected to average $8 to $9 per barrel, compared with marginal costs of $4 to $5 per barrel below this level.

inputs to levels where growth is not possible. However, the imports implied by these very low oil prices would almost certainly be below the critical levels.

12. Adjustment Policy Scenario. Continued structural reforms (with significant action on the exchange rate and import liberalization) backed by a compact with the international financial community and IMF-type monitoring 4/, would make life a lot easier for the Nigerians, although the going would be still tough and fraught with uncertainties. The Medium Term Adjustment Program presented in Section II provides the basis for improved creditworthiness, renewed growth (averaging around 3½ percent per annum over the 1987-91 period rising to around 4 percent in the early 1990s) and in the longer term, a restructured economy based on the non-oil sectors. An Adjustment Policy Scenario has been constructed to reflect the program. The adoption of a program along the lines proposed would require a strong political commitment by the Government and greater diligence in curbing corruption and motivating the bureaucracy to meet the challenges ahead.

II. MEDIUM-TERM ADJUSTMENT PROGRAM

A. Objectives

13. Given the prospects of depressed oil markets over the next few years, renewed growth and improved creditworthiness will only be possible if the efficiency of resource use can be substantially increased and additional resources mobilized externally and internally. This will require building on the initiatives already taken and embracing an adjustment policy package within the context of a Medium-Term Adjustment Program (1987-91) which recognizes the need to increase and improve the productivity of investment as well as to (i) increase the resilience of the economy to the uncertainties of the oil market; (ii) shift the structure of production toward efficient non-oil traded good sectors; (iii) reduce the import dependence of the economy; and (iv) lessen the dominance of the public sector and enhance the role of the private sector. Financial stabilization and increased savings will be important corollary objectives. The adoption of such a package would be combined with some form of acceptable IMF endorsement and participation. This would open the way for additional financial support through favorable terms for the rescheduling of external debts with the Paris and London Clubs, and new loan commitments.

14. It will take longer than the five years of the adjustment program period to rebuild a viable economy based on the non-oil sectors. Over these years oil will still dominate, although solid foundations will have been set for the transition. While considerable growth in non-oil exports can be expected, the small base from which they start means they cannot be

---

4/ It may be possible, although unlikely, to organize financial support without the IMF but even so, it would be difficult and messy at best.

a major propulsive force in the development effort until well into the 1990's; nor can they generate foreign exchange earnings of the relative magnitudes envisaged for, say, the Latin American heavily indebted countries. In the short run most growth will come from the production of import substitutes. The key to this growth will be essentially the same set of policies needed to promote exports, particularly the removal of price distortions. These policies will encourage more efficiency in agriculture and industry and will be much more effective than current policies, for example, in achieving Nigeria's objective of encouraging the utilization of local raw materials. Gas-based activities will be of growing importance both for the local and export markets. In the longer term a curtailment of the high population growth rate - now estimated at 3.3 percent per annum - will be critical to the efforts to improve living standards. The Government is aware of the implications of the high population growth for development and is preparing a population policy with specific demographic objectives. Some unmet demand exists for family planning and this can be increased through well designed information programs. Over the longer run, large-scale acceptance of family planning will require actions on the determinants of family size, such as low levels of education.

B. Adjustment Policy Package

15. The further policy measures proposed are based on extensive work carried out in preparation for the stalled 1984 SAL and subsequent economic and sector work (including the December 1985 CEM). A broad program has been evolved, with the priorities being: (i) correcting the still misaligned relative prices through exchange rate adjustment, liberalized import controls (including appropriate trade tax adjustments) and dismantled price controls; (ii) overcoming the considerable public sector inefficiencies through improved public expenditure programs and the speedy rationalization of the parastatal sector; and (iii) reducing the imperfections in the financial system principally through appropriate interest rates. Further financial stabilization measures and fiscal/monetary targets would be agreed between the Government and the IMF. Tight discipline on monetary expansion would have to be maintained with the Government continuing to place strict constraints on the budget deficit. While improved revenue measures should be pursued, these should not be seen as a substitute for a slimmer bureaucracy and a reduced Government presence in productive activity 5/. In what follows, the core policy measures required are outlined. Annex A presents a detailed annual action program for 1987 based on these measures while Annex B summarizes the timing of policy actions over the whole of the adjustment period.

5/ Special attention will need to be given to the problems facing the state governments in raising revenues to meet expenditure needs in crucial areas such as education and health, and in keeping expenditures under control. The Bank has ongoing ESW on matters relating to state finances and expenditures and this will have to intensify so that suitable policy recommendations can be formulated.

16. Exchange Rate, Trade and Incentive Policies. The thrust of the policy reforms in this area should be towards a market-determined exchange rate and the phased dismantling of import controls within three years. Provided the underlying trade taxes are structured correctly, the principal impediments to efficient resource allocation - and to non-oil exports and the utilization of local raw materials - will be removed, and the inducements to engage in parallel black market activities minimized. Action on three fronts is proposed. 6/ An initial significant and discrete devaluation would be desirable. Movement from there should be as rapid as possible, combining further devaluations (coinciding with the liberalization of import controls) with a crawl of the real rate. The continued need for the "across the board" temporary import surcharge of 30 percent would be reviewed as such adjustments are made. In parallel, the scope of the newly established second-tier foreign exchange market to be operated by the commercial banks should be expanded through the Government allocating increasing shares of oil as well as non-oil export proceeds to it. This would supplement the amounts available from the foreign currency domiciliary accounts system. However, the second-tier market should be integrated into the formal market as quickly as feasible with the naira then being allowed to find its own level.

17. Initial priority in the dismantling of import controls should be given to raw materials and spare parts (with some exceptions) through their transfer to open general licence status. However, action should be taken to ensure that the system of trade taxes provides the desired longer term signals to producers allowing them to plan ahead with some certainty. Modifications to the customs tariff schedule should be made at the time of the initial devaluation to lower and narrow the range of rates to 15 to 35 percent (with a clustering of rates in a narrower band of 20 to 30 percent). Excise taxes on production for the local market should be structured to be consistent with the principles for the setting of the custom tariff levels and minimum feasible degrees of import protection. High additional excise duties (50 and 100 percent or more) should be applied to the local production and imports of luxury goods. The basis for such reforms was set in the Bank assisted review of the customs tariff and excise tax schedules in 1984.

18. Immediate action should be taken to relax ex-factory price controls in order to shift incentives away from trading to production, to signal relative scarcities and to increase the effective yields and elasticity of the excise tax system. It would be highly desirable to shift farmer incentives from input subsidies to a crop pricing structure which reflects market forces. A re-examination of the role of the six commodity marketing boards and the approach to the setting of support prices for domestic crops with the aim of minimizing Government intervention is also

---

6/ The recommended exchange rate actions are preliminary. Firm recommendations will be formulated after the IMF completes its Article IV Consultations in March 1986.

called for. The government should continue to adjust petroleum product prices in line with the exchange rate adjustments.

19. A package of export incentives should be introduced which removes fully the impediments to non-oil export production inherent in the system of trade taxes and controls. Budgetary considerations and GATT regulations would need to be taken into account in determining the nature, level and coverage of the incentives but the package could include: (i) the recently re-activated customs drawback scheme but extended and adapted to include exemption (or equivalent) from customs tariffs and excise taxes on all inputs directly and indirectly incorporated in export production; (ii) exemption from excise taxes on output; and (iii) a tax credit on export production (or an equivalent measure) to offset the distortionary effects of the import protection system and exchange rate policy on value added. The ability of exporters to retain 25 percent of foreign exchange earnings and sell them in the second tier foreign exchange market goes part of the way towards (iii); an alternative to a tax credit would be for all foreign exchange transactions associated with non-oil exports to be channelled through this market. Appropriate incentives for export traders and service exports would also be required. Other supportive measures are outlined in the Bank's report on the potential for non-oil exports.

20. Public Resource Management Policies. The principle which should guide the Federal and State Governments in their budgetary and planning decisions throughout the adjustment period are as follows. First, the Government should continue its efforts to stabilize the public wage bill. It should restrain attempts to increase real levels of public service salaries and fringe benefits, and the freeze on hiring should be extended to all but the most critical skills. Over the longer run, the emphasis has to be on eliminating overstaffing through a judicious combination of attrition and redeployment and allowing wages for different skill categories to reflect scarcity values. Second, restored levels of supplies will be essential in the health, education and agricultural sectors while routine and periodic maintenance must have priority over new investment to prevent the rapid deterioration of essential infrastructure. Third, transfer to parastatals to cover operating deficits and capital expenditures have to be further reduced; the transfers to commercially-oriented parastatals should be eliminated completely. Within the context of development strategies for the sectors in which they operate, programs for the privatization, liquidation or rationalization of parastatals should be prepared and implemented. Commercial orientation and increased autonomy and accountability should form part of the rationalization program. Where feasible, the process of privatization of commercially-oriented parastatals could commence with the conversion of outstanding government loans to equity and the infusion of new capital by selling shares to the public through the Nigerian Stock Exchange. Finally, priorities should be set for the completion of the large number of capital projects on the basis of their economic viability and costs to complete, with across-the-board cuts being avoided so that the economy is not burdened by unfinished and weak projects. This will mean some politically tough but economically important decisions (e.g. discontinuing or postponing the completion of Ajaokuta steel works). For projects in the early stage of implementation, possibilities for reshaping the scope and/or timing to reduce costs and increase benefits should be assessed, especially

where large sums remain to be spent (e.g., the new capital, Abuja). The Bank's proposals in this area are developed more fully in the October 1985 report on Nigeria's public expenditures.

21. Financial System Policies. To increase the mobilization of financial savings and encourage the more efficient allocation of financial resources, the Government should reduce its intervention in the operation of financial markets, particularly in credit allocation and in the setting of interest rates. Interest rates should be allowed to reflect a positive real yield on holding financial assets and be flexible enough to take into account the frequent changes in the rate of inflation and balance of payment conditions. Also, the differential interest rates applied to the preferred sectors should be eliminated. The percentage credit allocation ceilings on bank lending should be removed. The review proposed by the Government with the aim of articulating a strategy for the restructuring of the financial sector should result in a plan of action for improved financial intermediation.

22. Sector Policies. Intra-sectoral breakdowns of public expenditures should be determined within the context of medium term development strategies for each sector. Special focus should be placed on the removal of technological and supply constraints discouraging private initiative and inhibiting efficient responses to favorable market conditions. While the basic exchange rate, trade, incentive and financial policy reforms will be crucial in this regard, constraints may exist at the sectoral level (e.g. specific infrastructural deficiencies, lack of particular skills) on which action must be taken to ensure the desirable responses to the improved price signals.

- Agriculture: The extensive information now available on agriculture is being drawn together to frame a coherent sector strategy for the sector's development. The strategy will incorporate measures to support and remove impediments to the development of export crops, particularly rubber, oil palm and cocoa. Allocations of public investment for irrigation should emphasize viable small scale low-cost irrigation schemes. The ADPs would continue to justify a sizeable proportion of public expenditure, although the project components need to be examined in the light of the absence of an economic response to applications of current fertilizer compounds on existing varieties of sorghum and millet. Food storage should receive increased attention. In order to expedite the adoption of new varieties and technologies developed by research centers, the Government should actively pursue applied research to establish their appropriateness at the farm level. A large share of expenditures should be directed to combat serious natural resource degradation (e.g., shelter belts, arid zone afforestation and rural forestry).

- Oil and Gas: NNPC should rely on joint ventures in all facets of oil and gas production. It should be reorganized as a holding company with largely independent subsidiaries and divest itself of its petroleum product distribution companies. Gas infrastructure development should be given priority to enable the 1320 mw Egbin power station and selected industrial users to substitute gas that is presently being flared for the more expensive fuel oil. The highest priority is the construction of the Warri-Lagos pipeline and the corresponding development of the gas field of

Utorogu. This program could be related to the gathering of associated gas which could also be used for LPG, initially for export and for domestic markets once they are developed. The proposed LNG project would have the highest chance of success if it were set up on a joint venture basis, with at least a 40 percent share for foreign companies and with an experienced operating company in charge of management; the project should only be embarked upon if purchase contracts can be guaranteed.

- Manufacturing: There is a need to reduce considerably the role of the public sector in manufacturing. The policy reforms outlined will lead to considerably increased domestic and foreign private investment. Meanwhile, public sector efforts should be redirected towards strengthening industrial infrastructure and support services. Given the inadequate market for its products, its high costs and doubtful viability, construction of the Ajaokuta steel works should preferably be discontinued or deferred indefinitely (and the necessary penalties paid); no new projects in the steel sector (including the flat products plant, special alloys plant and foundry) should be started while expenditures on other existing steel plants should be held to the minimum levels. In petrochemicals, priority should be given to the completion of the plants to produce polypropylene, carbon black and synthetic detergents ("Phase I"), provided that a satisfactory restructuring plan can be established for the latter two plants. The first phase ("Phase IIA") of a proposed large polyolephin complex to produce thermo-plastics should be deferred.

- Population: A draft population policy has been prepared by Nigerian population specialists under the guidance of an inter-ministerial group and with support provided through Bank sector work in cooperation with other donors. This policy should now be reviewed and acted upon by appropriate bodies. It includes: (i) establishing a nationwide program of private and public sector family planning services, supported by extensive information and education activities; and (ii) undertaking other initiatives to indirectly reduce fertility by, among other things, improving the status of women and delaying the age at marriage.

C. Adjustment Financial Package

23. A financial package involving exposures along the lines presented in the following table would appear to be feasible. It involves the official rescheduling of Paris and London Club debts and of trade arrears, and new loan commitments. The package is based on: (i) assessment of likely reactions of Nigeria's creditors to the endorsement by the IMF of an adjustment policy package, past practices of the Paris and London Clubs and parameters set for the Baker initiative; (ii) possible lending programs of the Bank, IMF and other international financial institutions under alternative lending conditions; and (iii) iterations of funding requirements to meet necessary import levels implied by the macroeconomic assessments, with funding availabilities implied by the financial workouts.

NIGERIA: Changes in Exposure (Debt Outstanding and Disbursed $ billion)

Creditor	End 1986	Adjustment Policy Scenario End 1991	End 1995	Average Annual Growth 1987-1991	Austerity Policy Scenario End 1991	Average Annual Growth 1987-1991
1. World Bank	1.5	4.6	7.7	25%	2.2	8%
2. IMF	0.0	1.9	0.1	-	0.0	-
3. Paris Club	5.3	6.4	3.4	4%	3.6	Neg
4. London Club	4.8	5.5	2.7	3%	3.3	Neg
5. Other Commercial	0.0	1.9	1.9	-	0.0	-
3 + 4 + 5	10.1	13.8	8.0	6%	6.9	Neg
6. Trade Arrears 1/	2.8	1.6	0.4	Neg	0.1	Neg
7. Other 2/	4.0	3.0	3.9	Neg	2.8	Neg
TOTAL DOD	18.4	24.8	20.1	6%	12.0	Neg

1/ Includes only the $2.8 billion in arrears not yet recognized as of December 31, 1985.

2/ Includes short term, private, arrears already recognized, and other debt not eligible for renegotiation.

24. Debt Rescheduling. Based on Bank analysis of alternative options, the best feasible workout appears to be a two-step six-year rescheduling arrangement (MYRA). This reschedules 100 percent of the principals of the London and Paris Club over the period 1987 to 1992 7/. The two-step MYRA is based on the supposition that creditors would first agree to a very short consolidation period (two years maximum) involving standard rescheduling terms to begin with. Conditional upon satisfactory policy performance during the first two years (1987-88) of the adjustment program period, the creditors would negotiate a longer MYRA (four, possibly

7/ This also implicitly reschedules the principal not paid during 1986 when the 30 percent debt service limit is assumed to have been in effect. It is unlikely that Nigeria would reach formal agreement with its creditors during the course of 1986 and would thus pay all interest, principal due to multilateral creditors and other principal (with preference to those disbursing new monies) to the extent of the announced debt service target.

five, years) 8/. Whereas a year-to-year rescheduling approach affords the creditors somewhat greater control, a MYRA approach is more amendable to obtaining a tenable external situation since it allows Nigeria to concentrate on medium and long term reform. In the case of the trade arrears, it would be consistent to spread the repayment of the principal over ten years (with an interest rate of 1 percent above LIBOR) rather than the 3.5 years used for the arrears already recognized. This reduces the need for new loans.

25. New Loan Commitments. The adoption of an adjustment policy package by the Government would lead to an acceleration of World Bank regular project loan disbursements increasing over the years to around $500 million in 1991, plus SAL and other quick disbursing loans averaging about $500 million per annum over the 1987-91 period. This would lift the Bank's exposure to around $4½ billion in 1991, which represents about 18 percent of total debt outstanding. Commitments of about $200 million per year are assumed to come from the African Development Bank (ADB). New loans from primarily commercial banks averaging terms of three years grace then four years to repay are assumed to provide the remaining financing requirements. These new loans would imply that the share of total debt in Nigeria of commercial bank creditors would increase from 51 percent in 1985 to 55 percent in 1991, decreasing to 40 percent in 1995. This exposure would be reduced to the extent that IMF or other creditors exposure is increased. In finalizing the financing package, it will be necessary to ensure that the sourcing of new commitments results in an equitable spread of the risks.

26. IMF Accord. The overall financial package assumes that Nigeria is able to attain a successful formal agreement with the IMF on an upper credit tranche facility by 1987. This allows one year for the anti-IMF political fervor to cool off. Four one-year standbys (1987-90) of 60 percent of quota are then assumed, followed by a fifth year where net exposure would be maintained. The 60 percent is applied to the present quota (SDR 849 million) without adjustment for inflation. (Another option might would be a one-year standby followed by the three-year EFF the IMF had earlier been planning on.) Because of the first repayment coming due in 1990, the IMF exposure reaches a peak of 220 percent of quota in 1990 and 1991 and declines rapidly thereafter, with all loans being repaid by 1994. An extension of the IMF exposure for a longer period would decrease the amount of commercial loans needed. The absence of IMF funds would increase the new money requirements from other sources in roughly corresponding amount unless the growth targets are reduced.

8/ While commercial banks have entered MYRAs involving consolidation periods of up to five years, Paris Club reschedulings have mostly been confined to single maturities. However, the granting of extended consolidation periods does not, per se, pose important procedural difficulties to the Paris Club. In 1985, Ecuador was accorded a three-year MYRA.

D. Adjustment Policy Scenario: Macroeconomic Implications

27. Even with the adoption of an adjustment policy package and agreement on a financial package of the orders of magnitude specified above, it is unlikely that GDP growth would greatly exceed an average of 3½ percent per annum over the 1987-91 period, rising to around 4 percent per annum through to 1995. 9/ These rates are consistent with the Government's expressed desire to contain debt service and new external financing to sustainable limits, and to prevent any further decline in per capita consumption over the next few years with modest but steady improvement in the 1990s. While the external debt outstanding in 1995 of around $20 billion under this scenario is in excess of the present level, it would represent a vastly improved ratio to exports (around 75 percent compared to the present level of 150 percent) and be associated with a lower debt service level (20 percent of exports compared with the present level of 40 percent). Over the long term, a curtailment of the high population growth rate will be critical to the efforts to improve living standards.

28. Investment and Savings. These growth magnitudes do not call for massive new investment levels. Although over the longer period investment will have to grow more or less in line with GDP, there is considerable scope for increasing output over the medium term through the fuller utilization of existing productive capacity, more selective and sound public investment in key areas and improvements in the productivity of private and public investment as a result of the policy reforms outlined earlier; the effects will be reflected in a decreased non-oil ICOR (between 3½ and 4). Investment throughout the adjustment program period is expected to average around 18 percent (which in real terms is slightly below present levels) of GDP, with the improved incentive system and investment climate leading to the partial restoration of the pre-crisis private/public investment ratio (to around 55 to 60 percent by 1991). The national savings rate would average around 18 percent of GDP; public savings over the period are slightly less than public investment but exceed them in the early 1990s. The uplift in the savings rate in the early 1990s is not entirely dependent on expected increases in oil earnings. The reforms proposed for the financial system will be important in the encouragement of private sector savings while improved revenue mobilization, control over public expenditures and parastatal reforms will allow a considerably improved public sector savings performance.

29. Exports and Imports. The success of the adjustment program will rest heavily on the ability of the economy to expand the trade surplus and ultimately to generate an external current account surplus without resort to administrative controls on imports. Such surpluses are likely to accrue

---

9/ While, as noted in the recent PBD review of "Baker" papers to date, there is no scientific way to quantify the effect of the policies proposed with the RMSM outcomes, the parameters used represent judgements based on what has been gleaned from analysis at the macro and sectoral levels of Nigeria's own experience, and from comparison with other countries.

in the early 1990s when the effects of the policy reforms in encouraging efficient import replacement and non-oil exports begin to really bite and when the international oil market is expected to pick up. Rapid growth in non-oil exports (around 11 percent per annum) can be anticipated as a result of the improved exchange rate and export incentive policies but because of the small base from which they start (about $400 million in 1985), the high growth rates would not result in vast increases in foreign exchange earnings over the 1987-91 period (although they would become significant during the 1990s if even moderate growth continues). Unfortunately, there is considerable uncertainty as to export revenues from oil, although Nigeria does have some flexibility on the margin in adjusting production levels to compensate for price reductions. 10/ There is also uncertainty as to the level of imports consistent with the growth targets set. Imports of goods have been squeezed considerably since the onset of the economic crisis and in 1986 are expected to reach a trough of just over $7 billion (in 1984 prices). This low figure has been used as the base, with growth thereafter being based on a consistent set of judgements of import elasticities for capital, intermediate and consumer goods and on the effects of the exchange rate and trade policy reforms. The foreign exchange made available through rescheduling and new loans enable imports of goods to be maintained at an average of around $8½ billion per annum (in 1984 prices) over the 1987-91 period (compared with around $6½ billion under the Austerity Policy Scenario and just over $7 billion in the interest only 'cold rescheduling option), while the policy reforms will lead to a marked increase in the efficiency of their use.

30. Structural Changes. The Medium Term Adjustment Program would significantly strengthen the non-oil productive sectors and reduce the economy's dependence on oil. Real growth of non-oil GDP is expected to average over 3½ percent per annum during the 1987-91 period. The most important changes would be in the agricultural and industrial sectors, with the former growing at an annual rate of just over 3½ percent and the latter at over 7 percent. There will be a fair degree of "lumpiness" in the industrial sector which is partially reflected in the growth and non-oil export figures (as a result, for example, of LPG production coming on stream). Nigeria's dependence on food imports should be reduced over the period (reflected in declining per capita real imports) as farmers respond to the improved incentive system and reduced supply constraints. Exports of crops should also pick up (mainly cocoa) while forestry could be expected to grow rapidly and serve as a basis for a fast growing export industry in the 1990s. Manufacturing growth in the near term is dependent to a large extent on the availability of raw material imports. Over the medium term, the improved incentive system would result in a more efficient

---

10/ If oil earnings over the adjustment period 1987-91 are lower by 20 percent than those forecast by EPD, the GDP growth would be held to about 3 percent per annum. The income loss would have to be absorbed mainly in 1987, and thereafter the growth path would be similar to that of the Adjustment Policy Scenario but with up to about a two year lag. A comparison of the performance under the Adjustment Policy Scenario with the Austerity Policy Scenario is presented in Annex C.

and expanded industrial structure with considerably increased exports to surrounding countries. Diversification into LNG and LPG would also serve to strengthen the industrial base and broaden exports particularly during the 1990s. The reduced dependence of the economy on imports is reflected in the real import/GDP ratio being contained to around present levels in the early 1990s without recourse to import controls. The exchange rate and trade policy reforms would encourage efficient import replacement production for which comparative advantage is apparent, particularly of raw materials and intermediate goods. Increased levels of investment and production by the private sector should result from the improved incentives system with the public sector dominance being reduced. The ratio of private to public investment, for example, is expected to double between 1986 and 1991, with significant increases in foreign investment contributing to foreign exchange inflows and a strengthened technological base. In all, a much stronger and more resilient economy emerges at the end of the adjustment period, with firm foundations set for future growth based on the non-oil sectors.

NIGERIA: Macroeconomic Performance

	Adjustment Policy Scenario		Austerity Policy Scenario	
Growth Rates (1984 Naira (%)	1987-91		1987-91	
GDP	3.6		1.8	
Non Oil GDP	3.6		1.4	
Agriculture GDP	3.7		2.3	
Industry GDP	7.3		-4.4	
Non Oil Exports	11.2		5.6	
Imports	3.9		-1.0	
Per Capita Consumption	0.3		-1.9	
Ratios (Current Naira)(%)	1987	1991	1987	1991
Interest/GDP	4½	4½	3	1
Savings/GDP	15	21	13	14
Investment/GDP	15	20	12	12
Public Saving/Public Investment	81	92	82	69
Private/Public Investment	36	58	28	20
DOD/Exports a/	173	158	163	77
Imports/GDP (1984 Naira)	14	13	13	11
Other Indicators (Average Annual)	1987-91		1987-91	
Import Levels ($billion)	8.1		6.6	
ICOR (non-oil)	3.5		11.9 b/	

a/ In the Adjustment Policy Scenario, this reduces to around 74 percent by 1995. See Annex C for full table.

b/ The ICOR is high since it includes two years with zero or negative growth. If it was calculated over a slightly longer period, the average would be around 7 to 8.

E. Risks of the Program

31. Uncertain International Economic Conditions. The international macroeconomic picture is shrouded with uncertainties, not only in oil market prospects but also in the ability and willingness of creditors to continue to extend financial support to heavily indebted countries. If the international oil market should weaken even more than projected and Nigeria is unable to maintain revenues through increases in production volumes, then the pace of implementation of the adjustment program would have to be slowed down, growth targets reduced and the time at which sufficient savings are being generated to commence repayment of external debt pushed back and/or per capita consumption squeezed. The alternative would be to seek additional external financial support but at the cost of an extended debt burden. The commercial banks may also take steps to cut back their exposure in Nigeria if (i) they perceive the creditworthiness of the country to be impaired by more unfavorable oil earnings than now anticipated and/or (ii) other heavily indebted countries are not able to meet their revised payment obligations, adversely affecting the liquidity of the banks and their risk perceptions.

32. Internal Resistance to Reforms. The public debate revealed strong opposition to an accord with the IMF. Questions of national sovereignty and wasteful use of money by the Government and its officials were important considerations in moulding the negative response. While the Government has gained considerable political capital as a result of the debate, it will have to now tread a careful path in consummating any form of accord with the IMF. The Government is reluctant to deviate radically from the perceived public opinion so as not to give competing army officers the excuse to plot and possibly overthrow it. The increasing emphasis on price mechanisms relative to administrative controls will mean less scope for corruption and encourage those affected to frustrate the implementation of the reforms. Trade liberalization is likely to meet considerable opposition from those benefiting from excess protection or from quota rents on scarce goods. Agriculture tariff reforms could be seen by urban groups as contrary to their interests leading them to pressure for their suspension. It will need a committed Government to overcome these and other forms of resistance, which will be particularly strong in the middle stages of the adjustment program when the effects of the reforms begin to take hold.

III. INSTITUTIONAL RESPONSIBILITIES AND MONITORING: IMPLEMENTING THE ADJUSTMENT PROGRAM

A. The Next Steps

33. Putting into place a Medium Term Adjustment Program will be a difficult and complex task. In this the Bank will have to take a leadership role. The crucial next step is to convince the Nigerians to undertake the further policy reforms required. This is a sine qua non of obtaining external finance. Thus the Bank should build on the policy dialogue it has pursued with the Government to seek adoption of an adjustment policy package along the lines outlined. This would include

continuing the Bank's efforts to convince the Government of the necessity to have some form of agreement with the IMF and to explore the means through which this could be achieved. It is not going to be easy to sell the adjustment program to the Nigerians. What is proposed goes beyond what they have been willing to accept to date, particularly on the exchange rate, import liberalization and starving the white elephants in the public expenditure program. On the other hand, there are sufficient reasons for cautious optimism to make the effort worthwhile. As noted previously, the reforms already announced in the last budget indicate a recognition of the need for fairly fundamental changes. And even though the Nigerians are undoubtedly considering trying to force acceptance of de jure or at least de facto rescheduling which would bring debt servicing down below the announced 30 percent of exports, the amount of new funds involved in the proposed adjustment financing package should be large enough to appear quite interesting to them at a time of great and growing import stringency. Neither is it going to be easy to sell the financing package to the international financial community even if Nigeria embraces it. The community will be unwilling to advance Nigeria significant levels of new funds if the Government cannot concretely illustrate the political will and discipline to carry out the necessary further reforms and to ensure that the returns from the use of the funds are sufficient to service the extra debt. In this respect, the role of the Bank and Fund will, again, be crucial.

34. Selling the Program to the Nigerians. To convince the Nigerians of the desirability of adopting a Medium Term Adjustment Program, five inter-related aspects should be stressed. First, there is the internal virtues of the policies themselves in creating the foundations for self-sustaining growth based on the non-oil sector of the economy. Second, the additional funds allow considerably more imports - $1.5 to $2 billion per year - and reduce the strains imposed by continued austerity measures. Third, official rescheduling has commercial advantages over a "cold rescheduling" by the Government e.g. continued trade credits, more favorable loan terms in the future. Fourth, the conditionality of an international compact has advantages, especially to support the hands of the reformist elements in a Government continually subject to pressures from interest groups. Finally, there is the flexibility offered by the international compact in responding to the external shocks and other uncertainties. All the participants - the Government, the Bank, the commercial banks and the IMF - will have to pull their weight if, for example, the oil market deteriorates further. The Bank should indicate the extent of its willingness to expand its lending in response to the Government's policy initiatives, especially through quick-disbursing loans to support specific reform packages, and to provide technical support in devising and implementing policy reforms. To help establish and expand the second tier foreign exchange market and to promote non-oil exports, for example, an industrial imports loan has been proposed.

35. Role of the IMF. The Bank and the IMF, at the working level, are in broad agreement on the contents of an acceptable adjustment policy package, and through its Article IV Consultations, the IMF will have made clear to the Government its position. Regarding the exchange rate, the IMF and the Bank are in agreement both on the first-best approach (a "clean" large devaluation and subsequent float) and on second-best steps (including

enlargment of the second window) to get there. In the likely event that Nigeria remains unwilling to adopt any kind of formal IMF program or surveillance in the near future, the Bank's objective is to assist both parties in order to assure that Nigeria has as soon as possible a policy reform package acceptable to the IMF and that there is the closest feasible formal relationship between the two. The formal relationship is important for: (i) obtaining acceptance of the proposed adjustment financial package; (ii) getting IMF money (after a decent interval to allow sensitivities in Nigeria to fade); and (iii) the benefits, mentioned above, of IMF and broader international conditionality.

B. Bank Lending Program

36. The Bank's lending program has an important role to play in efforts to bring about the Medium Term Adjustment Program. The question is how to calibrate the volume and composition of the lending program to best encourage rapid movement toward the adjustment policy package. In this context, the proposed Bank program has been designed to provide flexibility in responding to policy performance. It consists of (i) a core lending program to respond to current policy initiatives; (ii) a minimum lending program if the Government delays in developing these policy initiatives; and (iii) a full lending program to support an acceptable Medium Term Adjustment Program.

37. Agriculture accounts for about one-third of proposed Bank lending under the core program. In industry, Bank management has authorized discussion with the Government of a quick disbursing sectoral operation that would focus on additional policy reforms designed to give a major boost to the second window for foreign exchange and sharply increased incentives for non-oil exports. The program also includes projects in transportation and energy; these had been on hold until the recent elimination of the petroleum subsidies. Regarding longer-run constraints on development, the program also gives some emphasis to water supply. On education, sector work is being undertaken to help develop a project pipeline.

38. When Nigeria's GNP per capita is calculated on the basis of an adjusted exchange rate to compensate for the over-valued naira, it is cut roughly in half, demonstrating that the estimated official per capita income substantially overestimates real income levels. The current ceiling on the Bank's contribution to total project costs is two-thirds. In light of the low level of adjusted per capita income and Nigeria's severe resource constraints, it is proposed that the ceiling be raised to 80 percent for appropriate lending operations.

39. Some major projects in the lending program have been designed to be of the "accordion" type, which can be expanded if the reform program is moving well. The lower level of lending, which is linked to the current policy framework, would be about $350 million annually (about $4 per capita). This level, while less than would be desired in terms of sectoral policy and institutional objectives, seems appropriate as a signal to Nigeria that the Bank supports the reforms made to date but would like to see much more before substantially increasing the program. Until further policy progress is made, creditworthiness concerns are also seen as a

constraint on further expansion. Nigeria does have on balance a good record in paying back the Bank (even when it was running up its large trade arrears). And its large oil and gas reserves mean that it is much less dependent than most other countries with serious debt problems on good policy per se to meet future debt servicing requirements; in fact its oil earnings are projected to be more than adequate to meet debt servicing (and allow import growth) during the period that new loans from the Bank would be repaid. (cf. the projected debt service ratios for the 1990s in Table 4 of Annex D). Nonetheless, the proposal here reflects the view that now is a time for caution on lending levels. As further policy progress is made, the lending program could be expanded and, if circumstances are right, would include the quick disbursing second window loan mentioned above.

40. If the existing policy framework deteriorates, then the lending program would be cut back to focus almost entirely on longer-term development constraints. The level would be about $200-$250 million, the minimum necessary to keep the net transfer positive. On the other hand, if the Government is prepared to implement the Medium Term Adjustment Program in full, the Bank would respond with annual lending levels of about one billion dollars. (The policy package, with its likely implications for other external support and additional growth would also result in a substantial improvement in creditworthiness, as shown in the debt service, growth and import figures for the Adjustments Policy Scenario in Annex C.) This lending program would include a higher portion of quick-disbursing sector loans (up to about 50 percent), concentrated on accelerating structural change. If agreement is reached with the IMF, the program would include a SAL.

NIGERIA: Breakdown of Bank Contribution to Financing Package in Medium Term Adjustment Program
(Millions of dollars)

	FY86	FY87	FY88	FY89	FY90
Traditional projects	211	354-479	355-585	405-730	525-870
Quick disbursing	-	300	400	400	500

C. London and Paris Clubs

41. The requirement and importance for rescheduling and new funds from the London and Paris Clubs has already been discussed. The issue is the Bank's approach to them. Nigeria is already approaching both with rescheduling proposals; the latest proposal to the London Club asks for a four year consolidation period, a five year grace period, and then five years for repayment. Some London and Paris Club members may well break ranks, or there could possible even be some formal interim arrangement reached by one or both groups, although some Paris Club members are

strongly opposed. But the best Nigeria could hope for would fall far short of what could be achieved with an IMF-blessed (preferably IMF-supported) program. Some temporary arrangement now would be helpful to avoid a situation where Nigeria must choose between further draconian cuts in imports and a purely unilateral rescheduling, (with the problems the latter would raise for trade financing and for willingness of lenders to cooperate in providing new money in the future). On the other hand, achieving too much in the way of formal rescheduling now would risk a disincentive effect on future policy reform.

42. In any event, if there are prospects of a good reform program the Bank's role is to try to convince the Paris and London Clubs that Nigeria merits the risk of additional new lending as well as long-term rescheduling. The argument here will have to focus on making a credible case that additional lending will indeed increase substantially the chances that the banks can go back to a normal and profitable lending relations with Nigeria. Both London and Paris Club financiers will probably claim initially that putting new money in is virtually impossible, but it is hoped they already recognize that without the kind of financial package proposed, the chances of substantial principal repayments to non-preferred lenders (or, more precisely, to those that are not maintaining or increasing their exposure) is slim at best. In this connection, the Bank would count on help from the London and Paris Clubs in insisting that other debt, including Eastern Bloc debt, be rescheduled on similar terms. The projections made in this paper conservatively do not take account of relief on other debt, since it is uncertain and the amounts are relatively small.

43. The Medium Term Adjustment Program will be difficult to put together and involves the risk of failure. But it is vital to the economic future (and restored creditworthiness) of the country where one in every four inhabitants of Sub-Saharan Africa reside.

NIGERIA: ANNUAL ACTION PROGRAM FOR 1987

The policy reform proposals would be implemented on the basis of annual action programs. This Annex outlines the program for 1987, although some of the actions could take place during the remainder of 1986. High priority actions are indicated by an *.

I. Exchange Rate, Trade and Incentive Policies

1. Initial discrete devaluation and then crawling adjustment.

2*. a. Finalize principles for operation of and activate second tier foreign exchange.
   b. Channel Bank funds (loan for export promotion and utilization of industrial capacity) through second tier market and match with multiple of Nigerian funds.

Import Controls and Taxes

1*. Modify customs tariff schedule, narrowing rates to 15 to 35 percent range.

2*. a. Liberalize import controls on raw materials and spare parts through their transfer to open general licence status.
   b. Formulate a plan for the phased liberalization of remaining import restrictions.

Internal Trade Controls and Taxes

1*. a. Relax ex-factory price controls on all goods.
   b. Formulate approach for shift to crop pricing structure which reflects market forces. Re-examine role of the six commodity market boards to setting of support prices for domestic crops (APP to be responsible).
   c. Further adjust petroleum product prices in line with exchange rate adjustments.

2*. a. Restructure excise tax on ex-factory production of all goods to fall within range of 5 to 25 percent, with appropriate offsetting provision.
   b. Apply additional excise taxes to both locally produced and imported luxury goods (50 or 100 percent or more).

Export Incentives

1*. a. Review and modify appropriate customs drawback scheme and other fiscal export incentives for non-oil exporters (including export traders and service exporters). This should include consideration of (i) putting all foreign transactions associated with non-oil exports through the second tier foreign exchange market; and (ii) allowing exporters wide latitude in what they import with their foreign exchange retentions.
   b. Simplify administration of incentive package.

Investment Incentives

1. Carry out studies to finalize coverage, design and administration of a package of fiscal investment incentives (undertaken jointly be the teams involved with ITAP and APP).

2. Streamline regulatory measures relating to industrial approvals.

3. Review legislation relating to foreign investment to allow greater ownership flexibility in some areas.

II. Public Resource Management Policies:

Public Expenditures

1*. Maintain restraints on public sector wage increases and extend freeze on recruitment to all but the most critical skills.

2*. In 1987 budget, reflect move to (i) restore levels of supplies relative to manpower; (ii) give priority to routine and periodic maintenance over new investment; and (iii) further reduce in transfers to commercially oriented parastatals (basis to be agreed within context of a rolling budget).

3*. Agree on restructured public investment program within context of sector strategies and (i) specify principles for the setting of priorities for completing ongoing capital projects; (ii) re-assess ongoing and proposed new projects (with completion costs over ₦30 million) against these principles; and (iii) categorize projects into "core", "reserved core" and "non core" within context of agreed budget constraints and incorporate into rolling budget estimates.

4. Adopt a rolling multi-year budget. Begin with a two-year rolling budget.

Public Enterprises

1. Prepare a Statement of Policy on Public Enterprises.

2. Restructure the Ministry of Finance Incorporated (MOFI) or some other agency of Government to effectively support the Ministries in planning and executing public enterprise reforms.

3*. a. Carry out a rationalization program for parastatals.
b. Classify parastatals according to whether they should be left largely unchanged, restructured, privatized or liquidated (in-depth studies required for some enterprises).
c. Establish priorities and timetable for rationalization.
d. Prepare and commence implementation of restructuring sub-program building into it (i) increased autonomy of public enterprises in making operating decisions (management, procurement, staffing, etc.) and improved accountability (ii) further autonomy of public enterprises in setting tariffs and prices (iii) improved accounting practices, financial controls and management in public enterprises and (iv) rehabilitation requirements.
e. Prepare and commence implementation of privatization and liquidation sub-program.

4. a. Increase tariffs of NEPA (at least 25 percent, with further increases proposed for 1988 and 1989), NRC (50 percent), NET (amount to be determined) and NPA (amount to be determined). Establish parameters for the amalgamation of P&T with NET, ensuring adequate autonomy and management.
b. NEPA to improve bill collections and reduce operating costs. Plan to be prepared for closure of some branch lines etc. of NRC; to include plan for staff reductions of around 30 percent over next three years. NPA to initiate measures to minimize costs of maintaining secondary ports and to reduce staff by 10 percent.

III. Financial System Policies

1. Finalize program for restructuring the financial sector. To include means to: (i) reduce barriers to entry; (ii) encourage branch expansion in rural areas; (iii) further develop capital markets as a source of long-term finance; and (iv) improve existing agricultural credit delivery system.

2*. Adjust interest rates to reflect positive real and scarcity yields.

3*. Remove credit allocation ceilings.

IV. Sector Policies

1 a. Prepare statement of policy on agricultural development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.
b. APP to carry out necessary studies on agricultural product prices, marketing and incentives.

2. Prepare statement of policy on oil and gas development, incorporating principles for public investment and parastatal operations in the sector.

3. a. Prepare statement of policy on manufacturing development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.
b. Designate high level interministerial body for guiding and counseling the trade and incentive policy reforms (for both manufacturing and agriculture)
c. Industry studies for refineries, petrochemicals, steel and pulp and paper to be carried out as part of the work of ITAP, with the principal aim of reassessing approach to public involvement in the industries.

4. a. Establish a focal point in Government to facilitate and coordinate the implementation of the proposed National Population Program.
b. Prepare a five-year action plan to guide the inclusion of family planning in federal, state and local health services, and to assure its availability through other outlets.
c. Ensure program reflected in the expenditure plans of responsible ministries and of the states.

NIGERIA: MATRIX OF POLICY ACTIONS IN MEDIUM TERM ADJUSTMENT PROGRAM

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
I. EXCHANGE RATE, TRADE AND INCENTIVE POLICIES						
A. Exchange Rate: Move to a realistic level appropriate to the reformed trade policy environment.	1. Reconfirmation of policy of crawling adjustment of the exchange rate to reduce overvaluation of Naira.	1. Substantial initial devaluation and adoption of a more flexible exchange rate policy.				
	2. Proposal to establish a second tier foreign exchange market.	2. Expand scope of second-tier foreign exchange market and move towards unification of the market with the 'formal' market.				
	3. Implicit Devaluation through introduction of import surcharge (see I C 3 - Action recently taken) and export incentives (see I E - Actions recently taken).					
B. Export Controls & Taxes: Remove export controls and marketing restrictions on desirable non-oil exports.	1. Abolition of list of prohibited exports (with some exceptions).					
	2. Simplification of export licencing procedures.					
	3. Abolition of export monopoly power of the six commodity boards.					
C. Import Controls & Taxes: Dismantle import controls and move to a situation in which a relatively moderate and uniform customs tariff is the only form of direct intervention in import trade (with limited exceptions).	1. a. Promulgation of new customs tariff (1984) narrowing range of tariffs (10 to 60% with some exceptions). Adjustments made (post-1984) to correct anamolies.	1. Modify further customs tariff schedule, narrowing rates to 15 to 35% range.				
		2. a. Liberalize import controls on raw materials and spare parts.				
	b. Abolition of approved user and other schemes (1984) providing zero or concessionary rates to favored importers.	b. Formulate a plan for the phased liberalization of remaining import restrictions.				
		c. Implement liberalization plan.				
	2. a. Simplification of "two queue" system of import controls and introduction of measures to remove administrative abuses and block leakages in granting import licences.					
	b. Rationalization of priorities for issuance of import licences, with increased emphasis on (i) imports to support food production and (ii) raw materials and spare parts for manufacturers.					
	c. Creation of new category of import licences not valid for foreign exchange for approved priority imports.					
	3. Introduction of a temporary import surcharge of 30%.	3. Import surcharge to be replaced by appropriate exchange rate action.				
	4. Abolition of compulsory advance deposit requirement for imports.					

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
D. Internal Trade Controls and Taxes: Withdrawal of Government from direct intervention in price setting. Excise taxes used as a major revenue measure, with coverage, structure and level being consistent with the principles for the setting of custom tariff levels.	1. Adjustment of domestic petroleum product prices to remove financial subsidy (except kerosine).	1. a. Relax ex-factory price controls on all goods.				
		b. Formulate and implement approach for shift to crop pricing structure which reflects market forces. Re-examine role of the six commodity market boards and approach to setting of support prices for domestic crops.				
	2. Expansion of excise tax base (1984), with taxes re-structured to be consistent with new customs tariff schedule. Further modifications post 1984.	c. Adjust petroleum product prices in line with exchange rate adjustments.				
	3. Creation of Agricultural Prices and Policy Group (APP) to be responsible for recommendations regarding price support and other trade policies relating to agriculture.	2.a. Restructure excise taxes on ex-factory production of all goods to fall within range of, say, 5 to 25%.				
		b. Apply additional excise duties to both locally produced and imported luxury goods (say 50 or 100%).				
		c. Formulate (APP) and implement policies for taxation of forestry and agricultural products.				
E. Export Incentives: Introduce a package of fiscal incentives which removes impediments to exports and restores competitiveness of non-oil export production. Adopt other non-distortionary measures to promote non-oil exports.	1. Reactivation and modification of custums tariff drawback scheme.	1.a. Review and modify appropriately Customs Tariff Drawback Scheme and other fiscal export incentives.				
	2. Assistance on export costing and pricing (nature yet to be specified).	b. Adjust these and other export incentives as needed (including phasing out transitory elements of the package) to reflect progress of exchange rate and other trade policy adjustments.				
	3. Extension of the Foreign Exchange Retention Scheme to allow exporters to retain 25% of foreign exchange earnings.					
	4. Activation of an already created Export Credit Guarantee and Insurance Scheme.					
	5. Encouragement of establishment of Free Export Zones in selected part of the country. Revitalization of the Export Promotion Council. Requirement for authorized foreign exchange dealers to set up export desk for a export promotional activity.					

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	AJUSTMENT PROGRAM PERIOD 1987 1988 1989 1990/91
F. Investment Incentives: Introduce a set of fiscal investment incentives which are meaningful to investors, mininally distortionary and simple in their administration. Also improve other efforts to promote foreign and local investment in desirable production activities.		1.a. Carry-out studies to finalize the coverage, design and administration of a package of fiscal investment incentives.	
		b. Introduce incentive package.	
		2. Undertake other measures to improve investment promotion including:	
		a. Improve investment promotion operations of the existing Industrial Development Coordinating Division of the Industrial Policy Review Body.	
		b. Streamline regulatory measures relating to operations of enterprises and investment.	
		c. Review and ammend where necessary, investment policies and guidelines to promote desirable foreign investment.	
II. PUBLIC RESOURCE MANAGEMENT POLICIES			
A. Level and Structure of Public Expenditures: Curtail public expenditures in a way which does least damage to the economy and ensures that maximum benefits flow from them. Composition of federal and state expenditures over the five-year adjustment period should support the macro-economic policy reforms and reflect basic economic principles, with allocations at the sectoral level being made within the consectoral development strategies (see also sectoral Policies).	1. Reduction of salaries of public servants (1985). Freeze on hiring new public service staff in a wide range of positions (1984). Reduction of fringe benefits to public servants.	1. Stabalize public wage bill. (limits to be determined within the context of the rolling three-year budget see II B.1).	
	2. Reduction of non-statutory transfers to all economic and quasi-economic parastatals to 50% of present (1985) levels. Balance of needs to be obtained from increases in tariffs of parastatals.	2. Restore levels of supplies relative to manpower and give priority to routine and periodic maintenance over new investment (basis to be agreed within the context of the rolling three-year budget).	
	3. Major ongoing investment project (over N30 million to complete) reviewed by Inter-Ministerial Committee (with World Bank Technical Assistance - 1984).	3. Reduce and ultimately eliminate transfers to commercially-oriented parastatals to cover their operating deficits and capital expenditure program (with limited exceptions - see II.C).	
		4. Restructure Federal public investment program: within context of agreed (i) sector strategies; (ii) principles for setting priorities and (iii) budget constraints.	

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
PUBLIC RESOURCE MANAGMENT POLICIES (Continued)						
		b. Review public investment program annually in light of current revenue considerations, ensuring consistency with principles and sector strategies.				
B. Public Expenditure Planning and Budgeting: Improve budgetary process by adopting approaches to planning and budgeting which allow implications of resource prospects over an extended period to be taken into account in making decisions on projects and programs.		1. Adopt a rolling multi-year budget:				
		a. Begin with a two year rolling budget.				
		b. Expand to a three-year rolling budget.				
		2. Adopt a core-type approach to planning of capital, investment relating it to the rolling multi-year budget.				
C. Public Enterprises Improve overall efficiency of parastatals and reduce their heavy dependence on the Government for financial support. Privatize commercially oriented parastatals	1. Appointment of Study Group on Parastatals (1984). Report submitted.	1. Prepare a Statement of Policy on Public Enterprises.				
	2. Decision to divest of public holdings in commercially oriented enterprises (agricultural production, hotels, food, beverages, breweries, distilleries, distribution electrical electronic appliances and all non-strategic industries). Also, consideration to be given to reducing public holdings without losing control in banks, insurance companies and other financial enterprises.	2. Restructure and strengthen a.o. Ministry of Finance Incorporated (MOFI) to effectively support the Ministries in planning and executing public enterprise reforms.				
	3. Direction to parastatals to improve accounting practices and to issue timely financial reports. Accounts to be audited and published.	3. Within the context of sector strategies (see Sector Policies) carry out a rationalisation program for parastatals.				
		a. Classify parastatals according to whether they should be left largely unchanged, restructured, privatized or liquidated. Indepth studies required for some enterprises.				
		b. Establish priorities and timetable for rationalization.				
		c. Prepare and implement restructuring sub-program.				
		d. Prepare and implement privatization and liquidation sub-program.				

	ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987 1988 1989 1990/91
I	FINANCIAL SYSTEM POLICIES Reduce Government intervention in financial markets and allow more discretion to the financial institutions in their operations.	1. Announcement to review financial system with the aim of its restructuring. To include (i) review of barriers to entry in banking and finance (ii) overhaul of operations of Agriculture Credit Guarantee Scheme and the Nigerian Agricultural and Cooperative Bank (NACB), with emphasis on decentralization and closer cooperation of NACB with the commercial banks. 2. Announcement to narrow gap in the margin and spread of interest rates. 3. Credit allocation system simplified by reducing number of sector with ceilings from 8 to 4.	1. Prepare and implement program for restructuring the financial sector. To include means to (i) reduce barriers to entry (ii) encourage branch expansion in rural areas (iii) further develop capital markets as a source of long-term finance and (iv) improve existing agricultural credit delivery system. 2. a. Adjust interest rates to reflect positive real and scarcity yields. b. Phase out interest differential among sectors. 3. Elimate credit allocation system.	
V.	SECTORAL POLICIES Prepare medium term development strategies for each sector, taking cognizance of broad policy reforms (as relevant), and address the specific policy and institutional reforms required to achieve development objectives in an efficient way as well as the appropriate schedule of public expenditures to support them. Special focus on the removal of bottlenecks and constraints affecting the efficient development of productive sectors.		1. Prepare strategy for agricultural sector. a. Prepare statement of policy on agriculture and water resource development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector. b. APP to carry out necessary studies on agricultural product prices, marketing and incentives. c. Ongoing revision and implementation of sector strategy. 2. Prepare strategy for oil and gas sector. a. Prepare statement of policy on oil and gas development, incorporating principles for public investment, and parastatal operations in the sector. b. Ongoing revisions and implementation of sector strategy.	

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	ADJUSTMENT PROGRAM PERIOD 1987	1988	1989	1990/91
SECTOR POLICIES (Continued)	Establishment of Industry and Trade Policy Analysis Unit (ITAP) expected soon under World Bank Industry Technical Assistance Project loan to the Government. Will work in collaboration with APP to carry out trade and incentive policy analysis.	3. Prepare strategy for the manufacturing sector.				
		a. Prepare statement of policy on manufacturing development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.	[redacted]			
		b. Designation of high level interministerial body for guiding and counseling the trade and incentive policy reforms (for both manufacturing and agriculture).	[redacted]			
		c. Key industry studies to be carried out as part of the work of ITAP, with aim of: (i) identifying and formulating measure to overcome regulatory constraints and market imperfections affecting efficient development; (ii) reassessing approach to public involvement in the industries and (iii) providing information base for promotion of private investment. Priority to be given to studies of refineries, petrochemicals, steel, and pulp and paper.	[redacted]			
		d. Ongoing revisions (especially in light of findings of industry studies) and implementation of sector strategy.		[redacted]		
		4. Prepare strategies for education and health sectors.				
		a. Prepare statements of policy incorporating federal/state responsibilities, and principles for cost-recovery, public investment and recurrent expenditures.	[redacted]			
		b. Prepare multi-year public expenditure program (categorize core, reserve core, non-core) consistent with policy statement, budget constraints and principles underlying structure of public expenditure program. Relate program to state responsibilities.	[redacted]			
		c. Ongoing revisions and implementation of strategies.		[redacted]		
		5. Prepare, revise and implement strategies for other sectors.		[redacted]		

Key Indicators	ACTUAL 1980	1981	1982	1983	1984	ESTIMATED 1985	1986	PROJECTED: ADJUSTMENT POLICY SCENARIO 1987	1988	1989	1990	1991	AVERAGE 1987-91	AVERAGE 1992-95	1995	AUSTERITY POLICY SCENARIO 1987	1988	1989	1990	1991	AVERAGE 1987-91
GDP Growth Rate	2.3	-5.0	0.1	-8.2	-4.8	1.1	0.5	2.4	3.3	3.8	4.5	3.9	3.6	4.1	3.7	1.4	0.1	0.9	3.5	3.1	1.8
GNP Growth Rate	2.3	-4.9	0.1	-8.1	-4.8	1.3	0.5	2.4	3.3	3.8	4.5	3.9	3.6	4.2	3.7	1.5	0.1	0.9	3.5	3.2	1.8
GNY/Capita Growth Rate						-2.9	-7.7	-0.2	-0.7	-0.3	0.7	0.8	0.1	1.7	1.9	-1.2	-3.9	-3.3	-0.4	0.1	-1.8
Consumption/Capita Growth Rate	5.8	3.3	1.3	-11.6	-13.4	-6.9	-3.4	1.9	0.3	0.2	-0.6	-0.2	0.3	0.5	1.3	-0.2	-4.2	-3.7	-1.0	-0.7	-1.9
Total DOD ($ U.S.Billion)	4.37	6.14	9.01	12.34	13.70	18.11	18.36	19.63	21.05	23.02	24.09	24.84	22.5	22.9	20.1	18.53	18.05	17.04	14.97	12.02	16.1
DOD/XGS	0.17	0.32	0.71	1.13	1.11	1.38	1.77	1.73	1.80	1.89	1.73	1.58	1.7	1.1	0.7	1.63	1.55	1.40	1.08	0.77	1.3
DOD/GDP	0.05	0.07	0.11	0.17	0.19	0.25	0.28	0.38	0.52	0.64	0.60	0.56	0.5	0.4	0.3	0.25	0.22	0.19	0.15	0.10	0.2
Debt Service ($ U.S.Billion)	0.54	0.93	1.46	1.99	3.06	5.05	3.12	3.44	3.29	3.50	3.04	3.27	3.3	5.2	5.5	3.41	3.50	3.65	4.14	4.68	3.9
Debt Service/XGS (%)	2.1	4.9	11.5	18.2	24.8	38.6	30.0	30.3	28.2	28.7	21.8	20.8	25.9	23.3	20.3	30.0	30.0	30.0	30.0	30.0	30.0
Debt Service/GDP (%)	0.6	1.1	1.8	2.7	4.2	6.9	4.7	6.7	8.1	9.7	7.6	7.4	7.9	9.0	8.2	4.6	4.3	4.1	4.1	4.1	4.2
Interest/XGS (%)	1.7	3.0	6.4	9.6	9.5	11.5	15.2	20.1	18.1	19.1	14.9	13.0	17.0	8.5	5.6	19.9	17.0	16.5	11.2	8.1	14.5
Interest/GDP (%)	0.5	0.7	1.0	1.4	1.6	2.0	2.4	4.4	5.2	6.5	5.2	4.6	5.2	3.2	2.3	3.0	2.4	2.2	1.5	1.1	2.1
(Rates below are current/current)																					
Gross Domestic Investment/GDP (%)	23.6	29.7	24.1	17.4	12.9	13.7	14.0	15.0	16.8	19.1	19.5	20.2	18.1	22.0	22.9	12.3	12.1	11.8	11.7	11.8	11.9
Domestic Savings/GDP (%)	26.5	18.3	14.8	14.1	19.4	19.0	16.1	16.7	18.6	19.8	21.9	22.9	20.0	27.0	28.1	15.0	15.0	15.0	15.2	15.5	15.1
National Savings/GDP (%)	23.6	15.7	12.0	11.3	17.4	16.9	14.4	14.8	16.5	17.7	19.8	20.9	17.9	24.9	26.1	13.3	13.4	13.6	13.8	14.1	13.6
Marginal National Savings Rates (%)		-33.4	-23.9	-5.6	54.1	-2.8	-14.7	2.5	11.6	7.1	12.0	5.4	7.7	5.8	-0.2	-8.0	0.9	1.1	1.7	2.5	-0.4
Public Investment/GDP (%)	14.4	15.6	14.7	10.8	9.9	10.8	10.9	11.0	11.7	12.7	12.6	12.8	12.2	13.3	13.4	9.5	9.6	9.7	9.7	9.8	9.7
Public Savings/GDP (%)						11.2	9.6	9.0	10.2	11.2	11.7	11.8	10.8	14.9	15.8	7.8	6.5	5.3	6.6	6.1	6.5
Private Investment/GDP (%)	9.2	14.1	9.4	6.6	3.0	2.9	3.1	4.0	5.1	6.4	6.9	7.5	6.0	8.7	9.5	2.8	2.4	2.1	2.0	2.0	2.3
Private Savings/GDP (%)						5.7	4.8	5.8	6.3	6.5	8.1	9.1	7.1	10.0	10.2	5.5	6.9	8.2	7.1	8.0	7.2
Private/Public Investment (%)	63.9	90.4	63.9	61.1	30.3	26.8	28.2	36.1	43.8	50.6	54.8	58.4	48.7	65.1	71.1	29.9	25.3	21.7	21.1	20.4	23.7
ICOR													3.5	3.7							12.0 a/
Export Growth Rates (%)	-9.5	-32.3	-27.3	1.0	19.8	12.0	2.2	0.1	2.2	4.4	8.9	4.5	4.0	3.3	0.1	0.1	2.1	4.2	8.8	4.4	3.9
Exports/GDP (%)	28.9	22.8	15.9	14.7	17.0	17.8	15.6	22.0	28.7	33.9	35.0	35.7	31.1	38.6	40.5	15.2	14.3	13.6	13.6	13.6	14.1
Import Growth Rates (%)	21.9	18.2	-22.8	-22.1	-24.1	-12.2	-9.3	10.8	-1.6	2.6	2.2	5.5	3.9	7.8	11.8	-1.0	-6.8	-5.9	4.4	4.4	-1.0
Imports/GDP (%)	24.0	29.2	23.0	18.8	16.6	12.5	13.5	20.3	26.9	33.2	32.7	33.0	29.2	33.6	35.2	12.6	11.4	10.4	10.2	9.9	10.9
Current Account ($ U.S.Million)	-640	-6515	-7387	-4696	-92	2110	-483	-1715	-1719	-2446	-1521	-1264	-1733	602	1500	-605	66	504	1572	2558	819.0
Current Account/GDP (%)	-0.7	-7.9	-9.3	-6.4	-0.1	2.9	-0.7	-3.3	-4.2	-6.8	-3.8	-2.9	-4.2	0.9	2.2	-0.8	0.1	0.6	1.6	2.2	0.7
Terms of Trade Index	101.3	113.3	113.0	100.3	100.0	95.2	68.6	71.3	67.5	63.5	62.6	63.7	65.7	71.8	80.2	71.1	67.4	63.4	62.2	63.6	65.5
Non-Oil Export Growth (%)	15.4	-31.1	-35.4	63.6	-44.2	-24.6	35.9 b/	12.8	10.2	8.9	19.8 c/	4.4	11.2	4.9	5.2	10.0	5.8	-0.2	15.7	-3.0	5.6
Exports/GDP (Constant, %)	23.7	16.9	12.3	13.5	17.0	21.5	21.8	21.3	31.1	21.2	22.2	22.3	21.6	22.2	21.6	21.5	21.9	22.6	23.7	24.0	22.8
Imports/GDP (Constant, %)	25.5	31.8	24.5	20.8	16.6	14.4	13.0	14.0	13.4	13.2	12.9	13.1	13.3	13.9	15.1	12.6	11.7	10.9	11.0	11.1	11.5

NOTE: Inconsistencies may exist between current and constant ratios as a result of terms of trade and exchange rate adjustment. In the Adjustment Policy Scenario, three years of large real devaluations over 1987-89 of 70 percent is assumed and constant in real terms thereafter. In the Austerity Policy Scenario, no large devaluation assumed; the nominal exchange rate is assumed to be adjusted to compensate for half of the difference between international and domestic inflation each year.

a/ The ICOR is high since it includes two years with zero or negative growth. If it was calculated over a slightly longer period, the average would be around 7 to 8. Both ICORs are non-oil ICORs.

b/ Improved cocoa harvest.

c/ LPG comes on stream.

NIGERIA: Assumptions and Results of Financial Assessments

1. Tables 1-7 summarize the results of the various projections made of Nigeria's external balance. Table 1 presents the debt outstanding as of the end of 1985. Table 2 shows the import levels that would result if Nigeria pays all debt service as scheduled (i.e. no reschedulings) and receives new commitments only from IBRD and ADB. Table 3 presents these debt service obligations in more detail. Table 4 shows the effect on import levels of assuming a 30% limit on debt service payments without other new loans (the Austerity Policy Scenario). Table 5 presents the import levels that would result from the Adjustment Policy Scenario. Table 6 compares the two scenarios and displays the sources of the higher import levels in the Adjustment Policy Scenario. Table 7 describes the changes in exposure of the various creditors that would result from the Adjustment Policy Scenario. The detailed assumptions used to make these estimates are described below.

2. Oil Exports. Oil price assumptions are from the EPD base case. While the world oil price projections are much lower than previous forecasts, they are not as low for 1986 as current spot prices both because average selling prices are above spot prices at the moment and because markets may stabilize later in the year. Oil prices could be several dollars lower than in these projections, especially in the next few years. We have done sensitivity analysis assuming world oil prices fall to a level $10 below the EPD's base case. It is assumed that OPEC quantities will be higher in the future than they have been in recent years because the lower prices will stimulate demand and because non-OPEC supplies will be less forthcoming at these lower prices. In that environment, EPD assumes that Nigeria's share of OPEC production will decrease from 8.6% in 1985 to 8.1% (their official share) by 1988 in the base case.

3. Nigeria's production increases from 1.50 m.b./day in 1986 to 1.71 in 1990 to 2.0 in 1995.

4. Nigeria's price (including a $1 premium above the world oil price) is $21 in 1986, $24 in 1990, and $40 in 1995.

5. The estimates of domestic consumption are based on the best data for 1985 (.25 m.b./day) followed by a decrease to .23 m.b./day in 1986 due primarily to the recent increase in petroleum product prices. This grows to .242 in 1990 and .275 in 1995 in the Austerity Policy Scenario, and .247 in 1990 and .274 in 1995 in the Adjustment Policy Scenario. The two scenarios are quite similar because the higher GDP growth rates in the Adjustment Policy Scenario are offset by the effects of the higher prices for domestic products.

6. Non-Oil Exports. These numbers are taken from the macro model. The estimate for 1986 is $358 million in both scenarios compared to $270 million in 1985 -- most of that growth is in cocoa. From 1987 onwards the growth in real terms for manufacturing exports is 0% through 1989 and -2% thereafter in the Austerity Policy Scenario and 2% growing gradually to 12% in 1985 in the Adjustment Policy Scenario. Other agricultural exports grow very little in either case. Cocoa increases from 180,000 tons to 220,000 tons in the Adjustment Policy Scenario while actually decreasing from 1987 onwards in the Austerity Policy Scenario. Gas exports of $100 million have been added in both cases from 1990 onwards. By 1990 the difference between the two cases in non-oil exports is $190 million. By 1995 the difference is $520 million ($300 million in 1985 dollars).

7. Export NFS are assumed to be 3% of total goods exports.

8. Import NFS. This is comprised of two major parts: freight, insurance, and other services which vary with imports and repatriated profits which depend mostly on oil exports. Based on historical figures, the relationship has been 10% of imports + 4% of oil exports. In order to try to capture the recent changes in profit retention rules for the oil industry, the projections assume import NFS will be 10% of imports + 5% of oil exports beginning in 1986.

9. Other Balance of Payments Items. Travel is assumed to be included in the NFS imports. Direct foreign investment grows at zero per cent in real terms in 1986 in both scenarios and by zero per cent in nominal terms throughout the rest of the Austerity Policy Scenario. In the Adjustment Policy Scenario, the growth is zero per cent in real terms through 1987 and 2% in 1988, 3% in 1989, 4% in 1990, and 5% thereafter. The difference between the two scenarios is $146 million in 1990 and $439 million in 1995. Net transfers are constant in real terms in both scenarios.

10. MUV. The manufacturing unit value index (MUV) is used to deflate imports to a constant dollar value. The projections for the different countries are from EPD's latest estimates, but the weights used correspond to the shares of those countries in Nigeria's imports. The index that results grows by 6.7% in 1986, 6.0% in 1987 and 1988, 6.2% in 1989, 6.3% in 1990 and then falling gradually to 4.3% in 1995. The cumulative MUV to produce 1985 dollars values is 1.35 in 1990 and 1.73 in 1995.

11. MLT Debt. All figures on MLT debt are from EPD unless specified otherwise in these notes. Interest due, amortization due, and disbursements scheduled are provided for Paris Club, London Club, Multilateral Creditors, and other MLT for 1986-1995. EPD also provides end 1985 DOD. The only change in these projections is that larger amounts are assumed for World Bank and ADB disbursements which require adjusting the interest and amortization due to the World Bank and ADB. Disbursements from existing commitments are projected by EPD based on disbursement schedules and past performance. While some obviously non-operating loans have been eliminated, the projected disbursements are probably on the high side. To the extent that disbursements from existing commitments are less, however, disbursements from new commitments would most likely be more since creditors are concerned about total net exposure.

12. Arrears. The MLT figures already include $1.7 billion that represents the arrears that had been converted to MLT as of end 1985. From the remaining claims our projections assume the following amounts will be recognized and paid off as indicated.

Amount	Date of Recognition	Retroactive interest to Jan. 1, 1984 paid	Principal Repayments Due	
			Austerity*	Adjustment
$ 1.8	Jan. 1, 1987	1987	1987-1990	1987-1996
$ .5	Jan. 1, 1988	1988	1988-1991	1988-1997
$ .5	Jan. 1, 1989	1989	1989-1992	1989-1998

The interest rate in both cases is 1% above LIBOR. The principal is to be repaid over 3½ years in the Austerity Policy Scenario and 10 years in the Adjustment Policy Scenario.

* Note that the arrears will not actually be paid off in this period in the Austerity Policy Scenario because of the 30% limit on debt service.

13. Short-Term Debt. After lengthy discussions, EPD felt the stock as of end 1985 was $1-2 billion, IMF felt the number was not much over $750 million. These projections assume a level of $1 billion, yielding interest payments of $100 million per year. There are no payments on principal and no increase in exposure (not even with inflation) in either case.

14. Private Debt. All figures on private debt are from EPD. The stock at end 1985 is about $1 billion. The initial stock of debt, the disbursements from existing commitments and the amortization and interest obligations resulting from those are from EPD. It is unlikely that exposure to private borrowers will disappear in any scenario. The Austerity Policy Scenario assumes that new commitments will produce enough new disbursements to keep exposure to private borrowers constant in nominal terms over the period. In the Adjustment Policy Scenario, new disbursements vary with direct foreign investment yielding an increase in exposure from $1.1 billion in 1985 to $1.3 billion in 1990 and $1.9 billion in 1995.

15. De Facto Rescheduling. In the Austerity Policy Scenario, total debt service (public MLT, private, short-term, and arrears) is limited to 30% of total exports of goods and services. Payments are made in the following order.

1. interest and principal to multilateral creditors.
2. all other interest (including interest on rolled-over principal).
3. all other principal including rolled over unpaid principal from previous years.

Total debt service payments equal 30% of exports provided the sum of debt service owed, including rolled-over interest and principal, equals or exceeds that amount. As a result, the rolled-over balance is eliminated in 1993, the first year debt service falls below 30%.

16. World Bank and ADB Loans. For the Austerity Policy Scenario, the Bank continues to maintain a positive net transfer of resources to Nigeria; at a minimum, commitments are expected to be about $230 million in FY86, rising gradually over the ten years to reach $750 million in 1995. Should the medium-term framework improve over our Austerity Policy Scenario without spectacular breakthrough on the policy front, lending could increase more rapidly. Under a best policies scenario, with significant movements on the exchange rate and on import liberalization, project lending would increase over the years to $1.1 billion in 1995 plus a SAL and other quick disbursing loans averaging $500 million from 1987 to 1995. Total new commitments from the SAL and quick disbursing Bank loans would be $4.5 billion over the period. In all scenarios, the African Development Bank is assumed to provide $200 million per year in new commitments beginning in 1987.

17. IMF Loans. In the Adjustment Policy Scenario, IMF loan disbursements are assumed to be 60% of quota in 1987-1990 followed by a fifth year disbursement equal to amortization due in 1991. The 60% is applied to the present quota and that amount ($510 million) is used without adjustments for inflation. Because of the first repayment coming due in 1990 the IMF exposure reaches a peak of 220% of quota (4 x 60 - 20) in 1990 and 1991 declining rapidly thereafter. All IMF loans are repaid by 1994.

18. Official Rescheduling. In 1986, the 30% limit would apply exactly as in the Austerity Policy Scenario. The unpaid principal which is rolled over to 1987 becomes eligible for Paris and London Club rescheduling.

19. For both the Paris Club and London Club, 100% of the principal due 1987-1992 is rescheduled. Paris Club interest is not rescheduled. This would not actually be in the form of a six-year agreement. It would probably be in the form of a two-year agreement or even two one-year agreements followed by a four-year agreement. The difference is important in practical terms because of the closer monitoring and the ability of the creditors to cancel the agreement if progress is not satisfactory. For estimating the effects assuming progress is satisfactory, however, the multiple agreements are equivalent to a single six-year agreement. Repayment of the rescheduled amounts does not begin until 1993. All rescheduled amounts are repaid by 1997 in five even installments.

20. In the Adjustment Policy Scenario, the arrears are repaid over ten years rather than the 3½ years that have been the terms agreed to in the past. There is no rescheduling of private debt or other MLT (mostly COMECON countries) except that the unpaid principal arising from the 30% limit in 1986 is all assumed to be rescheduled in 1987.

21. Other New Financing. In the Adjustment Policy Scenario, additional borrowing is added to all of the other assumptions in order to reach a particular path of imports considered to be consistent with the macro-economic estimates for that scenario. This new money is assumed to come from London Club banks, Paris Club creditors, and others. The terms are three-years grace and then four years to repay. The total disbursements over the period for this new money is $3.9 billion.

22. Reserves. Foreign exchange reserve assets are estimated at about $1.1 billion at the end of 1985, about 1.6 months of imports of goods in that year. In both scenarios, this percentage is increased to two months of imports of goods. In the Adjustment Policy Scenario, this happens in 1987. In the Austerity Policy Scenario, we assume this is done gradually over the period 1987-1989. Thus reserve assets in nominal terms increase from $1.1 billion at the end of 1985 to $1.3 billion in 1980 and $3.2 billion in 1995 in the Austerity Policy Scenario and $1.7 and 2.9 billion in the Adjustment Policy Scenario.

EXTERNAL DEBT
($ Million as of 12/31/85)

	(Debt Outstanding and Disbursed)		(Undisbursed Debt)	
PUBLIC 1_/ MEDIUM AND LONG TERM	13,225		4,499	
PARIS CLUB CREDITORS		4,733		1,929
LONDON CLUB CREDITORS		4,516		1,194
MULTILATERAL INSTITUTIONS		1,339		954
OTHERS 2_/		2,637		422
SHORT TERM	1,000		0	
PRIVATE	1,081		N.A.	
TOTAL	15,306		4,499	
TRADE CREDIT ARREARS (NOT YET RECOGNISED)	2,800		N.A.	
TOTAL DEBT INCLUDING UNRECOGNISED ARREARS	18,106		4,499	

Note: 1_/ Includes public and publicly guaranteed debt.
2_/ Primarily bilateral loans from COMECON countries and trade credit arrears already recognised and issued.

NIGERIA'S EXTERNAL BALANCE
(Existing Debt Service Obligations)

- No rescheduling
- No New Loans (except ADB and regular IBRD)
- (Millions of Current US$)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Oil Export Revenues	12,447	9,735	10,636	10,884	11,342	12,860	14,577	16,489	19,021	22,139	25,185
Other Exports and NFS	651	661	726	776	809	949	1,020	1,098	1,197	1,316	1,436
Total Export Revenue	13,098	10,395	11,362	11,660	12,151	13,809	15,597	17,587	20,217	23,455	26,621
+ Disbursements	2,636	1,924	1,382	1,069	650	528	464	505	557	605	659
- Interest Due	1,502	1,440	1,788	1,260	1,082	646	531	478	449	442	455
- Amortisation Due	3,547	3,891	3,780	3,814	3,438	2,272	1,332	1,002	761	571	468
Other Balance of Payments Items	1,485	119	343	-61	-35	-67	-437	-321	-332	-380	-435
Imports of Goods and Services	9,200	7,108	7,519	7,595	8,246	11,352	13,761	16,292	19,232	22,668	25,923
Imports of Goods	8,000	5,975	6,304	6,360	6,929	9,677	11,781	13,986	16,533	19,500	22,307
Imports of Goods in 1985 dollars	8,000	5,599	5,574	5,305	5,442	7,150	8,228	9,267	10,433	11,764	12,903
Debt Service/Exports	39%	51%	49%	44%	37%	21%	12%	8%	6%	4%	3%
Total Debt Outstanding and Disbursed at Year's end	1 / 18,106	16,139	13,741	10,996	8,209	6,464	5,597	5,100	4,896	4,930	5,122

Note: 1 / Includes $2.8 billion in arrears not yet recognised.

(NIGERIA S EXISTING EXTERNAL DEBT OBLIGATIONS)

- No Rescheduling
- Arrears = $ 4.5 billion
- (Current US $ million)
  No new loans (except ADB and regular IBRD)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
A. INTEREST											
Public	1,407	1,262	1,074	882	671	543	485	456	440	438	454
Paris Club	331	390	361	301	230	169	120	80	48	25	11
London Club	508	416	318	223	134	68	34	19	8	1	1
Multilateral	108	126	145	164	184	206	231	257	284	312	342
Short Term	100	100	100	100	100	100	100	100	100	100	100
Other	360	230	150	94	23	0	0	0	0	0	0
Private	95	89	74	56	40	26	14	7	4	3	2
Arrears 1 /	0	88	707	357	369	75	26	6	0	0	0
TOTAL 3 /	1,502	1,439	1,855	1,295	1,080	644	524	470	444	441	456
B. AMORTISATION											
Public	3,302	3,603	3,242	3,012	2,551	1,332	970	816	747	559	457
Paris Club	743	1,056	1,181	1,123	961	649	508	397	309	202	88
London Club	1,400	1,510	1,369	1,155	859	407	181	116	103	3	2
Multilateral	59	87	117	154	163	176	193	228	269	311	351
Short Term	0	0	0	0	0	0	0	0	0	0	0
Other	1,100	950	575	580	568	100	88	75	66	43	16
Private	245	288	281	216	158	140	76	43	14	12	11
Arrears 1 /	0	0	257	586	729	800	286	143	0	0	0
TOTAL	3,547	3,891	3,780	3,814	3,438	2,272	1,332	1,002	761	571	468
C. DISBURSEMENTS											
Public	3,577	1,795	1,307	1,036	636	528	464	505	557	605	659
Paris Club	1,174	849	486	301	206	84	2	0	0	0	0
London Club	560	498	356	321	17	2	0	0	0	0	0
Multilateral	276	285	327	343	378	432	459	507	556	601	659
Other	1,567	163	138	71	35	10	3	(2)	1	4	0
Private	359	129	75	33	14	0	0	0	0	0	0
TOTAL	2,636	1,924	1,382	1,069	650	528	464	505	557	605	659
D. NET FLOWS (C-A-B)											
Public	-1132	-3070	-3009	-2858	-2586	-1347	-991	-767	-630	-391	-251
Paris Club	100	-597	-1056	-1123	-985	-734	-626	-477	-357	-227	-99
London Club	-1348	-1428	-1331	-1057	-976	-473	-215	-135	-111	-4	-3
Multilateral	109	72	64	25	31	50	35	22	3	-21	-33
Short Term	-100	-100	-100	-100	-100	-100	-100	-100	-100	-100	-100
Other	107	-1017	-587	-603	-556	-90	-85	-77	-65	-39	-16
Private	19	-248	-280	-239	-184	-166	-90	-50	-18	-15	-13
Arrears 1 /	0	-88	-964	-943	-1097	-875	-311	-149	0	0	0
TOTAL	-1113	-3406	-4253	-4039	-3867	-2388	-1397	-967	-648	-406	-264

Note: 1 / Includes arrears not yet recognised. Some of the arrears are owed by the private sector.
2 / Totals consist of Public, Private and Arrears.

- Billions of Current US$.
- Limit on Debt Service Equals 30% of Exports.
- No New Loans (except ADB and regular World Bank).

NIGERIA'S EXTERNAL BALANCE
(Austerity Policy Scenario)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Exports Goods and Services	13.1	10.4	11.4	11.7	12.2	13.8	15.6	17.6	20.2	23.5	26.6
+ Disbursements	2.6	1.8	1.3	1.0	0.6	0.5	0.5	0.5	0.6	0.6	0.7
- Interest Paid	1.5	1.6	2.3	2.0	2.0	1.5	1.3	0.9	0.7	0.5	0.6
- Amortisation	3.5	1.5	1.1	1.5	1.6	2.6	3.4	4.3	2.9	0.6	0.5
+ Other Balance of Payments Items	1.5	0.1	0.1	.0	.0	0.1	-0.1	-0.1	-0.2	-0.6	-0.7
= Imports Goods and Services	9.2	9.2	9.3	9.2	9.1	10.2	11.2	12.7	17.0	22.3	25.5
of which: Imports Goods	8.0	7.9	8.0	7.8	7.7	8.7	9.5	10.7	14.5	19.2	22.0
Imports Goods 1985 Dollars	8.0	7.4	7.0	6.5	6.1	6.4	6.6	7.1	9.2	11.6	12.7

Memo items

Percent of Interest Paid	100	100	100	100	100	100	100	100	100	100	100
Percent of Principal Paid to Preferred Creditors	100	100	100	100	100	100	100	100	100	100	100
Percent of Principal Paid To Others 1 /	100	41	30	40	47	100	100	100	100	100	100
Cumulative Unpaid Principal	0.0	2.1	4.4	6.5	8.1	7.7	5.5	2.1	0.0	0.0	0.0
Debt Service/Exports	39%	30%	30%	30%	30%	30%	30%	30%	18%	5%	4%
Total Debt Outstanding and Disbursed 2 /	18.1	18.4	18.5	18.0	17.0	15.0	12.0	8.2	5.9	5.9	6.1

Note: 1 / Does not include rolled over principal from earlier years.
2 / Includes trade arrears not yet recognised.

NIGERIA'S EXTERNAL BALANCE
(Adjustment Policy Scenario)

(Billions of Current US$)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Total Export Revenues	13.1	10.4	11.4	11.7	12.2	14.0	15.7	17.8	20.5	23.9	27.2
+ Disbursements	2.6	2.6	1.8	2.4	2.6	3.1	2.0	2.0	2.0	2.8	1.9
- Interest	1.5	1.6	2.3	2.1	2.3	2.1	2.0	2.0	2.0	1.8	1.5
- Amortisation	3.5	1.5	1.2	1.2	1.2	1.0	1.2	1.8	3.7	3.9	4.0
+ Other Balance of Payments Items	1.5	0.1	-0.1	.0	0.1	0.1	0.1	0.1	0.1	0.2	0.1
Imports Goods and Services	9.2	9.2	10.3	11.0	11.9	13.0	14.5	16.1	17.7	20.3	23.6
of which: Imports Goods	8.0	7.9	8.8	9.5	10.3	11.2	12.4	13.8	15.2	17.3	20.2
Imports Goods (1985 Dollars)	8.0	7.4	7.8	7.9	8.1	8.3	8.7	9.2	9.6	10.5	11.7
Debt Service/Exports	39%	30%	30%	28%	29%	22%	21%	21%	28%	24%	20%
Total Debt Outstanding and Disbursed 1 /	18.1	18.4	19.6	21.0	23.0	24.1	24.8	25.1	24.2	22.2	20.1

Note: 1 / Includes trade arrears not yet recognised.

Comparing Scenarios

- Billions of 1985 US$.

	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
IMPORTS OF GOODS										
Full Debt Service	5.7	5.6	5.4	5.5	7.2	8.2	9.2	10.4	11.7	12.9
Austerity Policy Scenario	7.4	7.0	6.5	6.1	6.4	6.6	7.1	9.2	11.6	12.7
Adjustment Policy Scenario	7.4	7.8	7.9	8.1	8.3	8.7	9.2	9.6	10.5	11.7
COMPARING SCENARIOS										
Austerity Policy vs. Full Debt Service										
Total Difference in Import of Goods 1/	1.7	1.4	1.1	.6	-.8	-1.6	-2.1	-1.2	-.1	-.2
Adjustment Policy vs. Full Debt Service										
Official Rescheduling 2/	1.7	1.7	1.4	1.0	.4	-.2	-.4	-1.4	-1.5	-1.4
IMF Loans		.4	.3	.3	.1	-.1	-.4	-.3	-.3	-.1
Higher IBRD Loans		.1	.3	.3	.3	.3	.2	.2	.1	.1
Other New Loans		.1	.3	.7	-.1	-.1	-.1	.2	-.3	-.3
Higher Non-Oil Exports										
Other Differences 3/		-.2	.2	.2	.3	.5	.5	.3	.6	.2
Total Difference in Import of Goods	1.7	2.2	2.5	2.6	1.1	.5	-.1	-.8	-1.2	-1.2

1/ Due entirely to ceiling on debt service at 30% of export revenues.
2/ Includes longer repayment period for trade arrears.
3/ Includes differences in reserves, foreign investment, and private lending.

→ Nigeria RB

Nigeria

1 Paper too long. Text should be ≅ 15-~~20~~ 25 pgs.

2. No sense of timing. PR on pp 8 — or under then = 5 yrs? two phased?

3. No disc. of Scenarios in text

4. Need ~~Act~~ Specific action program for the next 12-18 months.

5. Too many annexes → as long if not longer than the paper.

6. SSW out

7. Annex should be the action prog. in the text

8. Need to discuss in text: the Training Requirements based on your scenarios

9. ~~Text~~ In PR. Matrix: What is joint credit? vehicle for coord → vehicle for monitoring.

10. In section pg 1 why Watsics, HHS?

14 Table A.3 Why not upto 1890. Why 87-91 av.

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

N-623

DATE February 28, 1986

TO Mr. Choksi, CPDTA

FROM Tom Allen, WA1NI

EXTENSION 78056

SUBJECT Nigeria: Baker Initiatve Paper

Following Mr. Humphrey's memorandum of February 24th, attached are the 12 copies of the main report and required annexes that you requested, which I assume you will distribute to those concerned.

Attachments

TAllen:pt

NIGERIA

BAKER INITIATIVE COUNTRY PAPER

TABLE OF CONTENTS

NIGERIA: BAKER INITIATIVE COUNTRY PAPER

I. Economic Performance

A. Structural Legacy of the Oil Boom (1973-80)

1. The buoyant international oil market over the 1973-80 period dramatically altered Nigeria's resource position. During this time the principal objective of the Government was to translate the large oil revenues into investments in social, economic and physical infrastructure. There were successes: a large functional network of interstate roads was established; power generating capacity was tripled and refining capacity quadrupled; and there was a rapid spread of education at all levels with the primary enrollment ratio almost doubling. However, the political and administrative systems at both the federal and state levels were not equipped to handle adequately the new-found wealth. Rampant corruption and gross economic mismanagement resulted in considerable leakages of public revenues and wasteful expenditures while the policies pursued led to structural changes which made the economy extremely vulnerable to external shocks.

2. First, the economy became almost completely dependent on the fortunes of the oil sector. The upsurge in crude oil prices boosted oil earnings to a level where, by the beginning of the 1980s, they accounted for 96 percent of the country's export earnings and over 80 percent of Federal Government revenues. These earnings made it possible to support a high real growth in investment of 9 percent per annum (reaching 24 percent of GDP in 1980) financed almost entirely out of domestic savings (over 26 percent of GDP in 1980). 1/ Although the ambitious investment programs of the Federal and State Governments prepared in the wake of the second oil price hike of 1979 led to the contracting of significant external debts, optimistic projections for the oil market suggested these were well within sustainable limits.

3. Second, there was a marked shift in the structure of production away from the non-oil producing sectors towards services. Inflation and an appreciating domestic currency eroded the competitiveness of non-oil traded good activities to such an extent that their share of non-oil GDP fell from around 55 percent in the early 1970s to under 40 percent in 1980, while the share of non-traded good activities rose correspondingly. The impact on the agricultural sector - the major source of GDP and exports up to the beginning of the oil boom - was particularly severe; by 1980, its share of non-oil GDP had fallen to 30 percent (from around 50 percent in the early 1970s) and production of export crops had virtually disappeared.

4. Third, domestic expenditure and production became highly dependent on imports. Within a decade Nigeria became a major food importer.

1/ Real GDP grew by 4 percent per annum.

The structure of trade taxes and controls encouraged the growth of import-based light assembly consumer good industries which contributed little to value added. By 1980, imports had reached a level of around 24 percent of GDP, nearly double the percentage prevailing in the immediate pre-boom years.

5. Finally, the public sector grew immensely in size and importance. The increased foreign exchange earnings and budgetary resources supported escalating public recurrent expenditures and a large public investment program. By 1980, Government recurrent expenditures had risen to 11 percent and public investment to 15 percent of GDP, the latter accounting for over half of total investment. A large part of the recurrent expenditures supported an inflated civil service. Unfortunately, many of the public investment projects were undertaken without sufficient attention to their economic viability, the appropriateness of their design and the implementation capacity of the Government agencies. (The private sector, on the other hand, was led to uneconomic investment decisions by misaligned prices.) The indigenization decree of 1972 also laid the foundation for the Government's large-scale participation in the banking, insurance and industrial sectors. By the beginning of the 1980s, there were around 70 non-commercial and 110 commercial federal public enterprises, many of which required extensive financial support to cover operating losses. Nigeria entered the 1980s with some 50 percent of its GDP and 65 percent of its modern sector employment accounted for by the public sector.

Priv. Sector
PSEs.

B. The Economic Crisis (1981-85)

6. Nigeria was thus ill-equipped politically, administratively and structurally to deal with the abrupt end of the oil boom in 1981. A sharply deteriorating world oil market left the country with plunging export earnings and fiscal revenues. Partly because of expectations that the downturn would be short-lived, but mostly because of lack of political discipline, the Federal and State Governments failed to respond quickly with strong measures aimed at a corresponding curtailment and appropriate switch of expenditures. Consequently, sizeable external and fiscal imbalances emerged; external reserves fell abruptly and at the same time there was a large-scale accumulation of private arrears on top of substantial borrowings to finance public investment.

7. The excesses of the civilian Government and its inability to come to grips with economic realities led to the military taking power at the end of 1983. Through the almost exclusive use of demand management policies involving massive expenditure cuts and the stringent application of import controls, the military Government significantly reduced the imbalances. Between 1983 and 1985 the budget deficit to GDP ratio fell from 10 percent to 5 percent while the external account deficit to GDP ratio went down from 5 percent to zero. However, like the previous governments, the Government was unwilling to adopt any substantial measures to reduce the serious misalignment of relative prices, the complex administrative controls and

the public sector inefficiencies. The naira continued to appreciate. 2/ The Government called to a halt its discussions with the IMF for an EFF program which would have paved the way for a structural adjustment loan from the Bank and debt rescheduling by creditors. While some actions were taken to improve the system of trade taxes, continued interventions in price setting and other trade controls served to reinforce distorted signals. Moreover, fiscal austerity was characterized by general expenditure constraints with insufficient regard to necessary expenditure reallocations. Public investment cutbacks tended to proceed across-the-board with little cognizance of priorities and stage of completion. Within public recurrent expenditures, outlays on supplies, spare parts and routine maintenance were eroded dramatically. Significant sums continued to be set aside to support operating deficits of grossly inefficient parastatals and to provide uneconomic subsidies. Sectoral ceilings for credit allocations by banks continued to be enforced and interest rates were held to levels resulting in negative real yields. In essence, there was no move to alter the structure of the economy inherited from the oil boom and, as a result, economic performance over the 1981-85 period suffered.

Pub. inv. cutbacks

8. First, production and employment in all sectors - except agriculture - remained depressed with real GDP in 1985 some 15 percent lower than that prevailing at the beginning of the 1980s. 3/ Construction and other service sectors were hard hit by the diminished public expenditures and declined at a faster rate than GDP. The drastically reduced supplies of raw materials and spare parts to the import-hungry industrial sector led to widespread plant closures, a substantial drop in capacity utilization (averaging only 25 to 35 percent) and extensive layoffs of the work force. Severe shortages of goods led to an acceleration in the inflation rate - peaking at around 40 percent in 1984 but receding rapidly thereafter - with scarcity rents of 300 to 400 percent for many essential goods accruing to traders who, unlike manufacturers, were not subject to price controls. The high population growth rate of an estimated 3.3 percent per annum meant significant declines in per capita real income and consumption since the onset of the crisis. In 1985 these were well below the levels recorded in the early 1970s, before the commencement of the oil boom.

9. Second, the cutback in investment expenditures was severe, with investment as a proportion of GDP falling to just over 12 percent of GDP in 1985 - well under half the peak level of 1981. The public expenditure cutbacks meant further delays in completing viable projects thus escalating their costs and depriving the economy of their net benefits. Private

---

2/ This appreciation was marginally reversed in 1985 as a result of continued depreciation of the naira against the US dollar and the country's improved domestic price performance.

3/ However, the Government has estimated that there was a slight upturn in real GDP in 1985 of 2.4 percent (this needs to be verified).

investment shrank at twice the rate of public investment and by 1985 constituted only a quarter of the total.

10. Third, domestic savings halved in real terms due to the decline in both GDP and terms of trade, with the savings ratio falling to 17 percent of GDP in 1985. Meanwhile, external debt service requirements increased tenfold (to 43 percent of exports and around 8 percent of GDP) and continues to accelerate. The external debt outstanding at the end of 1985 included $14 billion of medium and long-term public debt. Moreover, Nigeria accumulated substantial trade arrears which have been variously estimated to range between $3.5 and $6 billion. 4/ There are also some short-term external debts of around $1 billion (which are assumed to be continually "rolled over" and thus interest only paid) and an estimated private external debt of a further $1 billion. The severity of Nigeria's debt situation relates not so much to the size of the debt overhang (which in 1985 amounted to 26 percent of GDP compared with the 49 percent average of all middle income heavily indebted countries) but to its unfavorable payments profile and the poor outlook for the international oil market (see paras 16 and 17).

C. Policy Initiatives of the New Government

11. In the face of a continually weak oil market and a mounting debt service burden, it was painfully obvious that demand management policies alone would be insufficient to bring about sustainable external and fiscal positions. Moreover, the rescheduling of debts could not be avoided for long and per capita consumption was hovering near politically dangerous levels. Hopes were thus high that the new military Government which came into power in August 1985 would address the structural weaknesses of the economy and reach an agreement with the IMF so as to pave the way for external financial support and renewed growth. While the Government declared its intentions to complement "austerity with structural adjustment", it rather oddly submitted the desirability of an IMF agreement involving a major devaluation - never a popular idea - to a national open debate. Not surprisingly, there was a resounding public "no" to such an agreement and the Government responded by formally announcing it would not pursue negotiations with the IMF.

12. However, the 1986 budget contained measures which heralded significant progress in the areas of exchange rate, energy pricing, public expenditures and parastatal reforms (see Annex A). Many of the measures are in line with recommendations made by the Bank in 1984 relating to a proposed structural adjustment loan and in subsequent reports. The budget also incorporated further measures for financial stabilization which, if fully implemented, would bring the federal budget deficit down to only

---

4/ The total amounts that will be recognized as valid is difficult to estimate. The Government has implied the total will be $3.5 billion. A figure of $4.5 billion is used in this paper.

2 percent of GDP in 1986, and for expenditure reallocations to bring them more in line with efficiency considerations. The Government is now moving slowly and in a roundabout way towards a more realistic exchange rate but for the time being has rejected the option to make a significant discrete devaluation. Approaches have been made to creditors about possible debt rescheduling arrangements without a formal IMF involvement. However, the Paris Club has made it clear that an upper credit tranche program with the IMF would be required before such arrangements would be contemplated. The Government's declared aim to hold external debt service at 30 percent of exports was initially thought to endanger its relationship with the international financial community, although this would still be sufficient to cover all interest payments due and some amortization even under recent pessimistic oil projections.

D. The Road Ahead

13. Nigeria now stands at the crossroads. It has exhibited over the last few years the political will for austerity and - as illustrated by the new budget initiatives - has now found the political will to make a strong beginning on structural reforms. However, it is unclear how long the Government would stick to a major and largely unpopular reform program in the absence of a broad compact with the international financial community and of IMF surveillance. The recent further weakening of the oil market will make it more difficult for the Government to maintain the pace of reform for much longer than twelve to eighteen months without external financial support. In the meanwhile, it would be forced into a "cold" rescheduling of the external debt.

14. The uncertainties of the oil market make it extremely difficult to predict what the macroeconomic picture might look like if Nigeria followed the road of no accord with the IMF and no formal arrangement with creditors. However, using EPD's oil price projections, an Austerity Policy Scenario has been constructed for this road which assumes a gradual deterioration of policies and the unilaterally set debt service target of 30 percent. 5/ At most, GDP growth rates would average 1 to 1.5 percent per annum over the 1987-91 period. Increased compression of imports would be necessary. The scarcities of raw materials resulting from these cuts would force further reductions in capacity utilization in industry. The worsening shortages of commodities (including foodstuffs) would contribute to a high (around 20 percent per annum) inflation rate and although import replacement production would be encouraged, it would be generally high cost. The recourse to restrictive policies and administrative controls to

---

5/ See Annexes E and F for assumptions and results of financial assessments and macroeconomic assessments. Unilateral 'cold rescheduling' over an extended period would have damaging effects on the availability of trade credits to Nigeria. Export credit agencies would not extend cover which would make it almost impossible to finance new capital projects.

achieve the needed domestic savings and current account surpluses to meet debt service obligations would result in declining labor and capital productivity. Continued heavy public sector investment (and the associated poor design and choice of projects) would reinforce this tendency. This scenario implies increasingly severe unemployment problems together with further sharp reductions in living standards, especially in urban areas, with per capita consumption falling by nearly 2.5 percent per annum over the 1987-91 period. Conditions would improve during the 1990s as oil markets strengthen and the reduced debt service requirements allow higher import levels. However, the economy would be plagued with inefficiencies and deteriorating plant and infrastructures. It would also continue to be heavily dependent on the health of the oil sector and given Nigeria's very high population growth, the pursuit of such a "non-adjustment" strategy would leave the economy a wreck when the post-oil era arrives.

High Pop.

15. The alternative road - continued structural reforms, a compact with the international financial community and IMF surveillance - would make life a lot easier for the Nigerians, although the going would still be tough and fraught with uncertainties. It may be possible, although unilkely, to organize financial support and set up monitoring mechanisms without the IMF, but even so, it would be difficult and messy at best. The Medium Term Adjustment Program presented in Section II plots a course for this road; 6/ obviously there are acceptable variants. The adoption of a program along the lines proposed would require a strong political commitment by the Government and greater diligence in curbing corruption and motivating the bureaucracy to meet the challenges ahead.

E. Postscript: The External Debt Burden

16. In a world of falling oil prices and large but unverified trade arrears, even a month is a long time beyond which to predict with accuracy Nigeria's external debt service capacity. However, the Government can exercise some control on two fronts in the short run. In terms of the debt service denominator - largely oil revenues - it can pump more oil. Current production capacity has declined from about 2.4 million barrels per day (mbd) to about 1.8 mbd 7/ but this is still well above likely sales and can readily be increased if necessary. The debt service numerator - about 25 percent of which is trade arrears - can be altered by changing the level and timing of arrears recognition since the verifiable number is still open to debate. In this respect as well as because of its low debt/GDP ratio, Nigeria differs significantly from other heavily indebted countries, with important consequences for how it might manage its debt service obligations.

6/ An Adjustment Policy Scenario has been constructed to reflect this program (see also Section II and Annexes E and F).

7/ There is little difference between marginal and average cost up to this 1.8 mbd production level.

17. The main points to bear in mind are: (1) Nigeria has very high scheduled debt service obligations in the near future, with ratios close to Mexico and Argentina but whose structure is more heavily weighted towards short-term trade arrears; (2) prospects for oil revenues have fallen; (3) imports have already fallen by half since the early 1980s and it is difficult to know to what extent they can be further compressed without reducing consumption to politically unacceptable levels and restricting investment to levels where growth is not possible; and (4) while the debt/GDP ratio is low, the likely need for new money to supplement rescheduling for reasonable growth is relatively much higher than for the other major debtor countries with the exception of Mexico and possibly Chile. The table below summarizes the debt service obligations of Nigeria as they now stand and what their impact on import levels would be without rescheduling and without new loans. 8/ While there are good reasons to expect that some reductions could be made in imports from the high levels of the early 1980s without affecting economic growth, it is most unlikely that at the projected levels growth would be possible and that politically acceptable levels of per capita consumption could be maintained.

NIGERIA: Current Debt Service Obligations and External Balance

$ Billion	1985	1986	1987	1988	1989	1990	1991
Inflows							
Export Revenues	11.8	10.4	11.3	11.5	11.9	13.3	14.6
Debt Disbursements	2.6	1.9	1.4	1.1	0.7	0.5	0.5
All Other	-0.2	0.1	0.3	-0.1	-0.1	-0.1	-0.4
Outflows							
Debt Interest Due	1.5	1.4	1.9	1.3	1.1	0.7	0.5
Debt Amortization	3.5	3.9	3.8	3.8	3.4	2.3	1.3
All Imports	9.2	7.1	7.4	7.4	7.9	11.8	12.7
Debt Outstanding	18.1	16.1	13.7	11.0	8.2	6.5	5.6
Debt Service Exports	43%	51%	50%	44%	38%	22%	13%

8/ The key assumptions used here are: (a) EDP's assessment that world oil prices do not collapse completely in 1986 but they stay at low levels throughout the 1980s; increases in Nigeria's production partly offset these lower prices, but oil revenues do not increase in real terms until the 1990s; (b) no rescheduling; (c) Nigeria continues to recognize additional short-term trade arrears over the next three years bringing the total to $4.5 billion by the end of 1988; (d) no new commitments except for a continuing World Bank project lending program averaging about $350 million per year in new commitments and an ADB program averaging $200 million per year; and (e) disbursements continue on all existing commitments.

II. Medium-Term Adjustment Program

A. Objectives and Requirements

18. Given the prospects of depressed oil markets over the next few years, renewed growth and improved credit worthiness will only be possible if the efficiency of resource use can be substantially increased and further external financial support mobilized. This will require building on the initiatives already taken in the 1986 budget and embracing an adjustment policy package which recognizes the need to increase and improve the productivity of investment as well as to (i) increase the resilience of the economy to the uncertainties of the oil market; (ii) shift the structure of production towards efficient non-oil traded good sectors; (iii) reduce the import dependence of the economy; and (iv) lessen the dominance of the public sector and enhance the role of the private sector. Financial stabilization and the maintenance of reasonable levels of domestic savings will be important corollary objectives. The adoption of such a package would be combined with some form of acceptable IMF endorsement and participation. This would open the way for additional financial support through favorable terms for the rescheduling of external debts with the Paris and London Clubs, and new loan commitments. Without such financial support, it is difficult to envisage a scenario in which Nigeria would be able to avoid a precipitous decline in per capita output and consumption and to service debt in an orderly manner.

B. Adjustment Policy Package

19. The adjustment policy package proposed is based on extensive work carried out in preparation for the stalled 1984 SAL and subsequent economic and sector work. There is already a substantial degree of agreement with Nigerian senior officials on many of the measures, although further work is required in some areas to define more precisely required actions (e.g., public enterprise policy). The package involves: (i) correcting the still misaligned relative prices through reforms in the exchange rate, trade and incentive policies; (ii) overcoming the considerable public sector inefficiencies through restructured public expenditures and continued rationalization of the parastatal sector; (iii) reducing the severe imperfections in the financial system through less Government intervention in the operations of the financial markets and improved financial intermediation; and (iv) removing the supply constraints which discourage private initiative and inhibit responses to favorable market conditions. Poverty issues are addressed partly through the public expenditure and agriculture strategies and partly through the effects of growth on employment and incomes. Annex A summarizes recent policy actions of the Government and the timing of further actions over the adjustment period, while Annex B summarizes the actions which would take place in the first year of the adjustment program.

20. Further financial stabilization measures and fiscal/monetary targets would be agreed between the Government and the IMF. Tight discipline on monetary expansion would have to be maintained with the

Government continuing to place strict constraints on the budget deficit. While improved revenue measures should be pursued these should not be seen as a substitute for a slimmer bureaucracy and a reduced Government presence in productive activity. Special attention will need to be given to the problems facing the state governments in raising revenues to meet the expenditure needs in crucual areas such as education and health. The revenue sharing formula may have to be reviewed by the governments; if this poses constitutional difficulties, other revenue sources for the states should be explored with more diligence (e.g., appropriate cost recovery mechanisms).

Exchange Rate, Trade and Incentive Policies

21. The thrust of the policy reforms in this area should be towards a market-determined exchange rate and the dismantling of trade controls. Provided the underlying trade taxes and incentives are structured correctly, the principal impediments to efficient resource allocation - and to non-oil exports and the utilization of local raw materials - will be removed and the inducements to engage in parallel black market activities minimized. However, it is unlikely that the Government would agree to an immediate devaluation of the naira of a magnitude sufficient to reflect the true scarcity value of foreign exchange and bring about the immediate and complete liberalization of import controls. The concern is that the lifting of all import restrictions would cause pent up and speculative demands to place considerable pressures on the still limited amount of foreign exchange and while this would force further reductions in the value of the naira, it runs the danger of essential goods losing out in the process.

22. Although the removal of controls on imports would have to be phased, the dismantling of controls on prices and marketing could be achieved within a relatively short period of time. Immediate action can also be taken to ensure that the system of foreign and internal trade taxes provide the desired longer term signals to producers allowing them to plan ahead with some certainty. These basic reforms should be clearly distinguished from transitory trade tax and other measures used to compensate for the unfavorable effects of distortions caused by the continued use of import controls and the correspondingly overvalued naira.

23. Exchange Rate. A process has to be set in motion through which the phased dismantling of trade controls and other reforms affecting foreign exchange demands and supplies would allow the exchange rate to move towards a realistic level with minimum disruptive effects. An initial large and discrete devaluation should take place and a flexible exchange rate policy adopted. [As an interim measure during the period in which trade controls are being dismantled, the Government could adapt the formula it is using to make crawling changes to the exchange rate to allow regular (monthly) adjustments reflecting domestic-international inflation differentials and a margin for further changes in the real rate. The margin could start at three to four percent and be gradually stepped up as the import and other controls are relaxed. Further substantial discrete adjustments would be made to coincide with the phasing of liberalization of

formula?

import controls. In parallel, the scope of the newly established second-tier foreign exchange market to be operated by the commercial banks could be expanded through the Government allocating an increasing share of oil export proceeds to it. This would supplement the limited amounts sourced from the foreign currency domiciliary accounts system. The Bank could also channel funds associated with, for example, industrial sector loans through this market (with the Government committing equivalent funds). However, the second-tier market should be integrated into the formal market as soon as possible, at the latest by the time the trade and incentive reforms are fully in place with the naira then being allowed to find its own level.] 9/

24. Export Controls and Taxes. There are no taxes of significance on non-oil exports and this situation should be maintained. The Government has recently abolished the list of prohibited exports and simplified export licensing requirements for the 36 affected products. The export monopoly power of the six commodity boards was also abolished, with the private sector being allowed to market externally these products.

25. Import Controls and Taxes. The aim should be for customs tariffs to be the only form of direct intervention in import trade. A new customs tariff schedule was promulgated in 1984 resulting in a considerable narrowing of the range of rates (10 to 60 percent with some exceptions) and the abolition of schemes providing zero or concessionary rates to a large group of favored importers. Further modifications to the schedule should be made at the time of the initial devaluation to narrow further the range of rates (15 to 35 percent, with a clustering of rates in a narrower band of 20 to 30 percent). This would be a reasonable range for the final structure of the schedule taking account of the Government's insistence on some continuing protection for import replacement activities, the level and structure of excise taxes (se para. 29) and revenue considerations.

26. The dismantling of quantitative restrictions on imports should be phased over a maximum three-year period. Initial priority should be to liberalize the import controls on raw materials and spare parts (with some exceptions) through their transfer to open general licence status. 10/ During the first year of the adjustment program, studies should be undertaken to develop a plan for liberalizing the remaining import controls. The plan should include measures to counteract dumping and trade restrictions imposed by other countries and to streamline import licensing and foreign exchange allocation procedures. The Government has already taken steps to simplify the "two queue" system of import controls by

---

9/ These recommended exchange rate actions are preliminiary thoughts of the Bank only. Firm recommendations will be formulated after the IMF completes its reviews in March/April 1986.

10/ Some form of reserve powers will have to be devised to allow the Government to intervene if there should be excessive speculative imports detrimental to the overall reforms.

decentralizing approval power to foreign exchange dealers, harmonizing the issuance of import licenses with the foreign exchange budget and abolishing the system of global and monthly allocations of foreign exchange for trade transactions by authorized dealers.

27. The "across the board" temporary import surcharge of 30 percent recently introduced by the Government serves as an implicit real devaluation (on the import side), allows the Government to capture some of the "quota rents" associated with the goods under import restrictions and provides additional resources to the exchequer. A decision should be made at the end of the first year of the adjustment program as to whether or not the surcharge should continue to be applied, with progress on the exchange rate being the determining factor. Preferably its effects should be captured through an equivalent exchange rate adjustment (which may be required under an IMF program since such a surcharge is regarded as an unfavorable multiple exchange rate practice).

28. Internal Trade Taxes and Controls. The Government should take steps to withdraw its direct interventions in price setting. Immediate action should be taken to relax the controls on ex-factory prices in order to shift incentives away from trading to production, to signal relative scarcities and to increase the effective yields and elasticity of the excise tax system. It would be highly desirable to shift farmer incentives from input subsidies to a crop pricing structure which reflects market forces. A re-examination of the role of the six commodity marketing boards and the approach to the setting of support prices for domestic crops with the aim of minimizing Government intervention is called for. The Agricultural Policy Pricing Unit (APP) would be responsible for the formulation of recommendations in these areas for implementation in the second year of the adjustment program. The Government has recently adjusted petroleum product prices (except for kerosene) to remove implicit financial subsidies, and it should continue to adjust these prices in line with the exchange rate adjustments.

Price control *

29. Excise taxes on production for the local market should be structured so as to be consistent with principles for the setting of custom tariff levels (the excise tax system was broadened in 1984 in parallel with the introduction of the revised tariff schedule). They would be set at a not much lower level than custom tariffs (within the range of 5 to 25 percent) to reflect only a modest net degree of import protection. However, high additional excise duties (50 to 100 percent, perhaps higher for some products) should be applied to the local production and imports of luxury goods. The appropriate rates for industrial products and any required offsetting provisions should be determined prior to the commencement of the adjustment program and be put in place at the same time as the desired tariff schedule, although some fine tuning may be required at a later date. The approach to the taxation of agricultural and forestry products should be reviewed by the APP and policies formulated for implementation in the second year of the adjustment program.

30. Export Incentives. A package of fiscal incentives should be introduced which removes as far as possible the impediments to non-oil

export production inherent in the system of trade taxes and controls. The base level of export incentives should be set to reflect the situation at the end of the import liberalization period, although the temporary import surcharges on inputs into export production would be refunded while they are in force. Budgetary considerations and GATT regulations would need to be taken into account in determining the nature, level and coverage of the incentives but the package could include: (i) the recently re-activated customs drawback scheme but extended and adapted to include exemption (or equivalent) from customs tariffs and excise taxes on all inputs directly and indirectly incorporated in export production; (ii) exemption from excise taxes on output; and (iii) a tax credit on export production (or an equivalent measure) to offset the distortionary effects of the import protection system and exchange rate policy on value added (the ability to sell a portion of foreign exchange earned in the second tier foreign exchange market goes part of the way). This will require a redesign of the existing customs drawback scheme so that it is less cumbersome and allows timely refunds to exporters. The studies required to finalize the design and administration of the incentives would be undertaken jointly by the team involved in the Industry Technical Assistance Project (ITAP) and the ATT during the first year of the adjustment program for implementation in the second year. The design of appropriate incentives for export traders and service exports would form part of the review.

31. Recent other measures introduced by the Government to promote non-oil exports include: (i) activation of the already created export guarantee and insurance scheme; (ii) extension of the foreign exchange retention scheme to allow exporters to retain 25 percent of foreign exchange earnings, which can be used to purchase priority inputs (although an import licence not valid for foreign exchange still has to be obtained) or be sold in the second tier foreign exchange market; and (iii) assistance in export costing and pricing (nature yet to be specified). Steps have also been taken to overcome deficiencies in the operations of the Nigerian Export Promotion Council and to require authorized foreign exchange dealers to set up export desks for export promotion activities.

32. Investment Incentives. A review of the fiscal investment incentives being granted by the Government should be undertaken with the aim of making them non-distortionary and more meaningful to investors without creating an undue burden on the Government budget. The review should be carried by the ITAP team, with changes being implemented in the second year of the adjustment program. Other steps to be undertaken to improve investment promotion during the first three years of the adjustment program would include: (i) establishing the Industry Development Coordinating Division as an effective "one stop" agency for industrial approvals and investment promotion; (ii) streamlining the regulatory measures relating to the operations of enterprises and investment, and (iii) amending investment policies and guidelines to generate further desirable foreign investment. The latter should include increased ownership flexibility in some areas. To encourage further private interest in medium and large scale commercial farming it will also be necessary to review the land tenure arrangements. There is a need to strengthen promotion and support services for the private sector including pre-and

post-investment services, statistical and business information services, applied agricultural research programs and extension and technical support services. A conscious effort should be made to ensure continuous and effective dialogue with the private sector and to seek their active participation in formulating and implementing investment policies and promotion programs.

Public Expenditure Policies

33. Critical Principles in Determining the Composition of Public Expenditures. The principles which should guide the Federal and State Governments in their budgetary and planning decisions over the five-year adjustment program are as follows. (See Annex C: Sector Strategies, for more detailed principles.)

- First, the public wage bill should be stabilized. The Government recently reduced the salaries of public servants and should restrain attempts for real levels to be restored at least over the next three years. The Government's present freeze on hiring should be maintained and extended to all but the most critical skills. Over the longer run, the emphasis has to be on eliminating overstaffing through a judicious combination of attrition and redeployment, and on allowing wages for different skill categories to reflect scarcity values.

- Second, constrained supplies and maintenance expenditures have greatly impaired the efficient delivery of public services. Restored levels of supplies will be essential in a number of sectors (particularly health, education and agriculture) if reasonably modest standards of services are to be achieved. Both routine and periodic maintenance must have priority over new investment to prevent the rapid deterioration of infrastructure.

- Third, transfers to parastatals to cover operating deficits and capital expenditures have to be reduced, with efforts made to ensure that the commercially oriented public enterprises are able to support their own capital expenditure programs. The Government has already taken steps in this direction by reducing transfers to all economic and quasi-economic parastatals to 50 percent of 1985 levels, requiring the parastatals to obtain the balance of their needs from tariff increases and increased operating efficiencies.

- Finally, priorities should be set for the completion of the large number of capital projects on the basis of their economic viability and costs to complete, with across the board cuts being avoided so that the economy is not burdened by a proliferation of unfinished and weak projects. Those with higher priority should be rushed to completion (e.g., the Onne fertilizer and Egbin steam generating plants) while the completion of other viable projects should be deferred until more funds are available (e.g., Iwopin pulp and paper mill). Those which are clearly not economically viable - even on a sunk cost basis - should be cancelled. This will mean some politically tough but economically important decisions (e.g., preferably cancelling most of the Ajuokota steelworks and paying the necessary penalties). For projects in the early stage of implementation,

possibilities for reshaping the scope and/or timing to reduce costs and increase benefits should be assessed, especially where large sums remain to be spent (e.g., the new capital, Abuja). Completing viable ongoing projects should have priority over new projects. The latter should not be commenced unless their economic viability is beyond question and funds can be assured both for their timely completion and to meet their ongoing costs. This will mean that most new projects being proposed by the Government should be cancelled or deferred until after 1990 (e.g., Phase II petrochemical plants, flat steel products plant and the Port Harcourt refinery). Agreement would be reached with the Federal Government on how these principles would be reflected in the budgetary and planning process. The mechanisms for this would be agreement on the initial composition and subsequent criteria for updating the proposed rolling multi-year budget and core investment program.

34. Public Expenditure Planning and Budgeting. The most important institutional reform to be pursued should be the adoption of a rolling multi-year budget which allows the implications of resource prospects over an extended period to be taken into account in making decisions on projects and programs. The system should be introduced in a phased manner, beginning with a selective two-year rolling budget to be put in place for the first year of the adjustment program. This should be supplemented with a core type approach to the planning of capital investments. The essential features of the approach would be the division of projects into two categories: (i) those that would proceed immediately; and (ii) those that would go ahead if and when additional resources would be available. The former set of projects (core list) would be fully funded each year in line with the amounts needed for efficient implementation. No funding would be provided for any of the projects on the standby list unless adequate resources are available to guarantee their full funding to completion. The first steps in this direction have already been taken through the findings of the special inter-ministerial committee set up late in 1983 to review all projects involving completion cost of N30 million or more. Subsequent public expenditure and project reviews of the Government and the Bank can also be used to derive the initial rolling budget. Underlying all these actions would be a move away from the present "shopping list" nature of the Five Year Development Plan to one which is more indicative and policy oriented, with sectoral development strategies forming the principal means for establishing public investment and recurrent expenditure priorities within each sector. The ongoing Bank-sponsored technical assistance project would provide some support for these activities.

Public Enterprise Policies

35. Despite the findings of officially backed investigations - including the Onosode Commission in 1981 and the Study Group on Parastatals in 1984 - the Government has not been able to articulate a cohesive program of policy reforms for the parastatal sector. Such a program should be prepared with the utmost urgency and incorporate actions along the lines outlined below. (See Annex C: Sector Strategies, for more details.) The reforms would be implemented over the five-year adjustment period. A

Bank-sponsored public enterprise technical assistance project is proposed to assist in the formulation and implementation of reforms.

36. Rationalization of the Parastatals. Within the context of the development strategies for the sectors in which they operate, parastatals should be examined and classified according to whether they should be left largely unchanged, restructured, privatized or liquidated. The Government has recently announced its intent to divest itself of public holdings in commercially-oriented enterprises (agricultural production, hotels, food, beverages, breweries, distilleries, distribution, electrical, etc.). Certain enterprises slated for privatization may require prior financial restructuring and perhaps some rehabilitation. In depth studies of a number of enterprises will be required before a final decision can be made on them. The sector ministries should be given the responsibility for completing this task, with a restructured and strengthened Ministry of Finance Incorporated (MOFI) or another designed oversight agency playing a supporting role. Plans for restructuring should include rehabilitation requirements as well as financial and organizational changes. As part of the financial restructuring, outstanding loans to the enterprises would have repayment, grace and interest terms specified; in some cases, outstanding loans could be converted to equity. Guidelines should be developed that will permit certain enterprises to privatize selected aspects of their operations (e.g., NNPC's distribution subsidiaries and trading activities of other parastatals). Financial constraints facing the Government will mean that priorities will have to be set for restructuring.

37. Autonomy and Accountability. Public enterprises should be given autonomy in making operating decisions relating to, for example, day-to-day management, procurement and staffing. The Government, through the supervision ministries, should establish clear objectives and performance targets with the management of each enterprise and assist in drawing up action plans to achieve these targets. The designated oversight agency should be made responsible for monitoring the financial performance of the enterprises, making recommendations on their investment programs where access to budgetary resources and external financing is involved and for ensuring that they produce timely and adequate accounts audited according to appropriate Nigerian standards. Close liaison of the oversight agency chosen for this role with the supervisory ministries will be required, especially in the formulation and review of objectives and plans for each enterprise.

38. Commercial Orientation. Greater autonomy should be given to enterprises to determine their tariff and pricing structures. Where Government approval of tariffs is required (especially of monopolies or quasi-monopolies), they should be reviewed frequently to reflect cost and financial return considerations taking cognizance of enterprise efficiencies. Tariff adjustments of key utilities should also be linked to clearly defined targets for the reduction of budgetary transfers to them (e.g., NEPA, NPA and NRC). Where enterprises are fulfilling non-commercial objectives of the Government, they should be compensated through special budgetary provisions based on estimates of the costs involved. However, cost curtailment and improved operating efficiency should be the first

order of business for most parastatals. The adoption of improved accounting practices and financial controls should be encouraged. Technical assistance should receive particular attention. The appointment of high caliber top management will be essential.

39. Approach to State Parastatals. A similar approach could be adopted for state public enterprises. In this case, the scope of intervention and required policy reforms would be less demanding since the states are principally involved in the industrial sector and the bulk of their holdings are relatively small scale. These enterprises are targets for privatization. The most substantive holding of State Governments tend to be jointly owned with the Federal Government and thus would be covered in the reforms at that level.

Financial System Policies

40. To increase the mobilization of financial savings and encourage the more efficient allocation of financial resources, the Government should reduce its intervention in the operation of financial markets, particularly in credit allocation and in the setting of interest rates. It should allow more discretion to the financial institutions in their operations. Encouragement should be given to the establishment of new banks, branch expansion and to the development of the domestic capital market.

41. Restructuring the Financial Sector. The Government has recently announced its intention to restructure the financial sector. A review is planned which should result in the articulation and subsequent implementation of a strategy to: (i) reduce barrier to entry in banking and finance (which could include liberalization of ownership laws); (ii) encourage branch expansion in rural areas; (iii) further develop capital markets as a source of long-term finance; and (iv) improve existing agricultural credit delivery systems. The latter would include an overhaul of the operations of the Agriculture Credit Guarantee Scheme and the Nigeria Agricultural and Cooperative Bank (NACB), with emphasis on decentralization and closer cooperation of NACB with the commercial banks.

42. Credit Allocation. The credit allocation system gives the banks little discretion in credit allocation across sectors and imposes on them extensive reporting requirements. A timetable for the removal of the percentage credit allocation ceiling should be agreed upon 11/ with the initial steps being a further aggregation of the sectors (and subsectors) for which the ceilings are imposed and the replacement of monthly reports by the bank with semi-annual (or at most quarterly) reports.

11/ The Government recently took steps towards simplification by grouping activities into four sectors (previously eight sectors) for which percentage credit allocation ceilings are set. However, within some sectors subsector ceilings have been set.

43. Interest Rates. An immediate move should be made to adjust the level of interest rates to reflect a positive real yield on holding financial assets. It should be flexible to take into account the frequent changes in the rate of inflation and balance of payment conditions. Also, the differential interest rates applied to the preferred sectors should be eliminated.

Sector Policies

44. As indicated earlier, intra-sectoral breakdowns of public expenditure should be determined within the context of medium term development strategies for each sector. Special focus should be placed on the removal of bottlenecks and constraints affecting the efficient development of the productive sectors. While the basic trade and incentive policy reforms will go a long way in this direction, there are a number of distortions which are only recognizable at the sectoral level (e.g. local content programs, lack of particular skills) on which action must be taken to ensure the realization of comparative advantage and efficient resource allocation. Further, there are various market imperfections (e.g., lack of data and knowledge by potential investors, interdependencies of investment decisions) which require Government initiatives to correct. Such actions would be consistent with the aim of the Government's role in the productive sectors changing from a regulatory to a promotional one, as well as from one which emphasizes Government direct investment and intervention to one supportive of private initiatives. ??

45. The broad strategies proposed for each sector should be completed before the commencement of the reform program in the form of a 'Statement of Policy' so as to form the basis for the specification of sectoral level policy reforms and actions over the adjustment period. They would be updated on a regular basis and would be an important input into the formulation of the rolling multi-year budgets. The key elements which should be incorporated in the strategies for the major sectors are presented in Annex C.

C. Financial Package

46. A financial package involving exposures along the lines presented in the following table would appear to be feasible. The package is based on: (i) the advise of FPA as to likely reactions of Nigeria's creditors to the endorsement by the IMF of an adjustment policy package, past practices of the Paris and London Clubs and parameters set for the Baker Initiative; (ii) knowledge of possible lending programs of the Bank, IMF and other international financial instiutions under alternative lending conditions; and (iii) iterations of funding requirements to cover external current account deficits (associated with various growth and oil market scenarios) implied by the macroeconomic assessments, with funding availabilities

implied by the financial assessments. 12/ The increases in exposure for commercial lenders are higher than the Baker guideline percentages, but are warranted in Nigeria's case because the initial debt/GDP ratio is not very high and some sources of debt (e.g., arrears) must be eliminated.

NIGERIA: Annual Net Dibursements of Creditors
(Exposure Increase)

		Adjustment Program Period						
$Billions	1986	1987	1988	1989	1990	1991	1992	1995
World Bank	.2	.3	.5	.7	.8	.8	.8	.7
IMF	0	.5	.5	.5	.3	0	-.5	-.3
Paris Club	.7	.5	.3	.2	.1	0	0	-1.1
London Club	.4	.4	.3	0	0	0	0	-1.0
Trade Arrears*	0	-.2	-.2	-.3	-.3	-.3	-.3	-.3
Other New Loans	0	.2	.4	1.3	.3	.3	.7	-.8
Other	-.9	-.6	-.6	-.5	-.1	0	0	.1
Total	.4	1.1	1.2	1.9	1.1	.9	.8	-2.7

* Includes only those not recognized by the end of 1985. Previously recognized arrears are in the appropriate MLT category.
NOTE: Net disbursements = Disbursement - Amortization

47. Debt Rescheduling. Based on FPA and WAN analysis, the best feasible workout appears to be a two-step six-year rescheduling arrangement (MYRA). This reschedules 100 percent of the principals of the London and Paris Club over the period 1987 to 1992. 13/ The two-step MYRA is based on the supposition that creditors would first agree to a very short consolidation period (two years maximum) involving standard rescheduling terms to begin with. Conditional upon satisfactory policy performance of Nigeria during the first two years (1987-88) of the adjustment program period, the creditors would negotiate a longer MYRA (four, possibly five, years). 14/ Whereas a year-to-year rescheduling approach affords the

---

12/ A number of options for external debt reorganization were explored with the assistance of FPA (see Annex F).

13/ This also implicitly reschedules the principal not paid during 1986 when the 30 percent debt service limit is assumed to have been in effect. It is unlikely that Nigeria would reach formal agreement with its creditors during the course of 1986 and would thus pay all interest, principal due to multilateral creditors and other principal (with preference to those disbursing new monies) to the extent of the announced debt service target.

14/ While commercial banks have entered MYRAs involving consolidation periods of up to five years, Paris Club reschedulings have mostly been

(Footnote Continued)

creditors somewhat greater control, a MYRA approach is more amenable to obtaining a tenable external situation since it allows Nigeria to concentrate on medium and long term reform. In the case of the trade arrears, it is necessary to spread the repayment of the principal over ten years (with an interest rate of 1 percent above LIBOR) rather than the 3.5 years believed to be the Government's present intention, noting that the extent of new money requirements is highly sensitive to the level of arrears officially recognized.

48. New Loan Commitments. The adoption of an adjustment policy package by the Government would lead to an acceleration of World Bank regular project loan disbursements increasing over the years to around $500 billion in 1991, plus SAL and other quick dispersing loans averaging about $500 million per annum over the 1987-91 period (see Annex D). Commitments of about $200 million per year are assumed to come from the African Development Bank (ADB). New loans from commercial banks and other creditors averaging terms of three years grace then four years to repay are assumed to fill the financing gap, noting that Nigeria's commercial lenders are reportedly reluctant to increase their net exposure significantly. In putting together the financing package, account has been taken of the necessity to ensure that the sourcing of new commitments results in an equitable spread of the risks and is roughly in line with the present pattern of exposure. If it is assumed that these new loans will come from some combination of London and Paris Club creditors, that share of total debt in Nigeria would increase from 51 percent in 1985 to 60 percent in 1991, decreasing to 48 percent in 1995.

49. IMF Accord. The overall financial package is premised on Nigeria being able to obtain a successful formal agreement with the IMF on an upper credit tranche facility by 1987. This allows one year for the political fervor to cool off. Four one-year standbys (1987-90) of 60 percent of quota are assumed, followed by a fifth year disbursement equal to the amortization due in 1991. The 60 percent is applied to the present quota ($510 million) without adjustment for inflation. 15/ Because of the first repayment coming due in 1990, the IMF exposure reaches a peak of 220 percent of quota in 1990 and 1991 and declines rapidly thereafter, with all loans being repaid by 1994. An extension of the IMF exposure for a longer period would decrease the amount of commercial loans needed. The absence of IMF funds would increase the new money requirements from other sources in roughly corresponding amount unless the growth targets are reduced.

(Footnote Continued)

confined to single maturities. However, the granting of extended consolidation periods does not, per se, pose important procedural difficulties to the Paris Club. In 1985, Ecuador was accorded a three-year MYRA.

15/ To obtain better terms, a one-year standby followed by a three-year EFF could be pursued by the Government.

D. Macroeconomic Implications

50. Even with the adoption of an adjustment policy package and agreement on a financial package of the order of magnitude specified in Section II.C, it is unlikely that GDP growth would exceed an average of 3½ percent per annum over the 1987-91 period, rising to around 4 percent per annum through to 1995. 16/ These rates are consistent with the Government's expressed desire to contain debt service and new external financing to sustainable limits, and to prevent any further decline in per capita consumption over the next few years with modest but steady improvement in the 1990s. While the external debt outstanding in 1995 of around $20 billion under this scenario is in excess of the present level (but less than the peak of $25 billion in 1992), it would still represent a reasonable proportion of projected GDP (30 percent) and be associated with a lower debt service level (22 percent of exports).Over the long term, a curtailment of the high population growth rate will be critical to the efforts to improve living standards.

51. Investment and Savings. These growth magnitudes do not call for massive new investment levels. Although over the longer period investment will have to grow more or less in line with GDP, there is considerable scope for increasing output over the medium term through the fuller utilization of existing productive capacity, more selective and sound public investment in key areas and improvements in the productivity of private and public investment as a result of the policy reforms outlined earlier. Investment throughout the adjustment program period is expected to average around 11½ percent of GDP. The effects of the policy reforms will be reflected in an improved non-oil ICOR (around 3.6) and the partial restoration of the pre-crisis private/public investment ratio. The necessity to maintain at least constant per capita consumption implies an initial reduction in the savings rate to an average of around 12½ percent, but this would need to be restored to present levels of about 18 percent in the early 1990s to enable the gradual reduction in external debt. The reforms proposed for the financial system will be important in the encouragement of private sector savings while improved revenue mobilization, control over public expenditures and parastatal reforms will allow an improved public sector savings performance (which is now highly sensitive to oil earnings).

52. Exports and Imports. The success of the adjustment program will rest heavily on the ability of the economy to expand the trade surplus and ultimately to generate an external current account surplus without resort

---

16/ If oil exports are lower by 20 percent than those forecast by EPD over the 1987-91 period, the GDP growth would be held to at most 2½ percent per annum. There is no scientific way to link the policies proposed with the RMSM results for the Adjustment Policy Scenario assessments. The relationships have been looked at in a behavioral way and reflected by the parameters used. See Annex F for detailed assumption and results of the macroeconomic assessments.

to administrative controls on imports. Such surpluses are likely to accrue in the early 1990s when the international oil market starts to pick up and the effects of the policy reforms in encouraging efficient import replacement begin to bite. Some growth in non-oil exports can be anticipated as a result of the improved exchange rate, trade and incentive policies but because of the small base from which they start (about $400 million in 1985), even high growth rates would give only marginal increases in foreign exchange earnings. Unfortunately, there is considerable uncertainty as to export revenues from oil, although Nigeria does have some flexibility in adjusting production levels to compensate for price reductions. There is also uncertainty as to the level of imports consistent with the growth targets set. Import levels have been squeezed considerably since the onset of the economic crisis and in 1986 are expected to reach a trough of $7.4 billion. This low figure has been used as the base, with growth thereafter being based on a consistent set of judgements of import elasticities for capital, intermediate and consumer goods and on the effects of the exchange rate and trade policy reforms.

E. Medium Term Effects

53. Sectoral Performance. The medium term adjustment program will significantly strengthen the productive sectors and reduce the economy's dependence on oil. Real growth of non-oil GDP is expected to average 3½ percent per annum to 1991. The most important changes would be in the agricultural and industrial sectors, with the former growing at an average annual rate of around 4 percent and the latter at around 5 percent. Nigeria's dependence on food imports should be reduced over the adjustment program period (reflected in declining per capita real imports) as farmers respond to the improved incentive system and reduced supply constraints. Exports of crops should also pick up (mainly cocoa) while forestry could be expected to grow rapidly and serve as a basis for a fast growing export industry. Industry's growth in the near term is limited to the availability of raw material imports. Over the medium term, the improved incentive system would result in a more efficient and expanded industrial structure. Diversification into gas and LPG would also serve to strengthen the industrial base and broaden exports. Service sectors will continue to grow at an average of 2½ percent per annum, their slower growth reflecting the increased attractiveness of the productive sectors relative to non-traded goods as a result of the exchange rate adjustments.

54. Other Structural Changes. The reduced dependence of the economy on imports is reflected in the real import/GDP ratio being contained to around 14 percent in the early 1990s (compared with 24 percent in the early 1980s) without recourse to import controls. The exchange rate and trade policy reforms would encourage efficient import replacement production for which comparative advantage is apparent, particularly of raw materials and intermediate goods. Increased levels of investment and production by the private sector should result from the improved incentives system with the public sector dominance being reduced. The ratio of private to public investment, for example, is expected to double between 1986 and 1991 (from 27 percent to 55 percent).

F. Risks of the Program

55. Uncertain International Economic Conditions. The macroeconomic picture is shrouded with uncertainties, not only in oil market prospects but also in the ability and willingness of creditors to continue to extend financial support to heavily indebted countries. If the international oil market should weaken even more than projected and Nigeria is unable to maintain revenues through increases in production volumes, then the pace of implementation of the adjustment program may have to be slowed down, growth targets reduced and the time at which sufficient savings are being generated to commence repayment of external debt pushed back and/or per capita consumption squeezed. The alternative would be to seek additional external financial support but at the cost of an extended debt burden. The commercial banks may also take steps to cut back their exposure in Nigeria if (i) they perceive the creditworthiness of the country to be impaired by more unfavorable oil earnings than now anticipated and/or (ii) other heavily indebted countries are not able to meet their revised payment obligations, so reducing the liquidity of the banks and their risk perceptions. However, a principle objective of the adjustment program is to reduce the vulnerability of the economy to such uncertainties. There is also sufficient robustness in the proposals to enable modifications to be made to the program as circumstances change without altering its main thrust.

56. Internal Resistance to Reforms. The public debate revealed strong opposition to an accord with the IMF. Questions of national sovereignty and wasteful use of money by the Government and its officials were important considerations in moulding the negative response. While the Government has gained considerable political capital as a result of the debate, it will have to now tread a careful path in consumating any form of accord with the IMF. The increasing emphasis on price mechanisms relative to administrative controls will mean less scope for corruption and encourage those affected to frustrate the implementation of the reforms. Trade liberalization is likely to meet with considerable opposition from those benefiting from excess protection or from quota rents on scarce goods. Agriculture tariff reforms could be seen by urban groups as contrary to their interests leading them to pressure for their suspension. It will need a committed Government to overcome these and other forms of resistance, which will be particularly strong in the middle stages of the adjustment program when the effects of the reforms begin to take hold.

57. However, there are a number of features of the adjustment program that serve to minimize the resistance to the reforms. First, measures are proposed to offset some of the adverse short term effects. For example, industrial rehabilitation assistance would be provided to firms to help them adjust to the more competitive environment. Second, the reforms would be announced in advance and implemented in stages to prepare for the required transition. Finally, the Government so far has shown a strong commitment to reforms and has already introduced unpopular but necessary policies (e.g., removal of petroleum subsidy) under extremely adverse conditions.

G. Institutional Responsibilities and Monitoring

53. The Next Steps. The Bank would build on the policy dialogue it has pursued with the Nigerian Government and seek reaction to the adoption of a policy adjustment package along the lines outlined. This would include continuing the Bank's efforts to convince the Government of the necessity to have some form of agreement with the IMF and to explore means through which this could be achieved. The Bank would play a facilitating role to enable the Government to sound out with the IMF (and the Paris and London Clubs) alternative approaches which recognize the sensitive issues involved. The Bank would in any event counsel the Government as to what is needed to continue the progress already made, even if neither the Government nor the IMF are yet able to indicate a willingness to get together on terms acceptable to each other. However, from the viewpoint of the Bank and other creditors of Nigeria, the mere endorsement by the IMF of a home grown policy reform program will not be enough; a strong IMF monitoring presence is desired, especially after the first year or two of the program when the Government's diligence in pursing the reforms is likely to wane.

59. Role of the Bank. The Bank's role in financing should be supportive of and complementary to commercial flows. Through the use of conditionality and a willingness to increase its own exposure - and the provision of expert assistance to the Government in the design of reform programs - the Bank should be able to alleviate many of the concerns of creditors and thus catalyze additional commercial flows. As well as increasing its conventional lending, the Bank would reach agreement with the Government on a series of quick disbursing SAL and sectoral loans which would be the principal vehicles for policy conditionality. Loan agreements and tranche disbursements would be linked to policy performance with the first SAL being linked to an IMF agreement. 17/ The Bank will have to pay at least as much attention to sectoral and institutional issues as to the macroeconomic ones. The proposed vehicles for conditionality in each of the policy areas is indicated in Annex A. Within the context of an agreement with the Government on the overall framework for the medium-term adjustment program (which would also be endorsed by the IMF) the Bank would negotiate appropriate conditionality for each sectoral and structural adjustment loan.

60. Each quick disbursing loan would have specified monitoring and reporting requirements to form the basis for assessing performance, and thus tranche releases and agreement on subsequent loans. Before submitting

---

17/ If the creditors and the new Government agree that the Government should seek initially merely IMF endorsement of its medium term adjustment program and at a later date (say after one year) reach accord on an upper credit tranch program, then the Bank would consider earlier agreement on non-SAL quick disbursing sector loans which would incorporate SAL-type conditionality.

a policy loan to the Board, the Bank would review the progress and effects of the medium term adjustment program. In any event, the Bank would undertake an annual assessment, which would incorporate the IMF's views on financial stabilization and balance of payment matters.

61. Relationships with the IMF. Although the Government may not have established formal dialogue with the IMF, the Bank will continue to develop an operationally effective understanding with IMF on the desirable content of the adjustment policy package. The Bank would concern itself principally with structural reform focussing on relative prices, public expenditure and enterprises policies, sectoral policies and institutional development measures designed to increase the efficiency of resource use and to extend supply. The IMF would concern itself mainly with demand management and exchange rate policies to create an overall macroeconomic environment within which the structural reforms can succeed. Obviously, there would need to be close collaboration between the institutions in looking at all areas to ensure consistency in the overall policy package. Annex A indicates the preliminary agreement reached with the IMF (at the working level) on the nature and division of responsibilities for the policy areas. This builds on the good collaboration in the past and on the joint efforts made in preparing the groundwork for a proposed SAL in 1984 to complement to an IMF-EFF agreement.

III. Bank Strategy

A. Lending Program

62. The proposed Bank lending program has been designed to provide flexibility in responding to policy performance. It consists of (i) a core lending program to respond to current policy initiatives; (ii) a minimum lending program if the Government fails to develop these policy initiatives; and (iii) a full lending program to support an acceptable Medium Term Adjustment Program (see Annex D1). Agriculture accounts for about 33 percent of proposed Bank lending under the core program over the next four years, while the water sector accounts for about 18 percent.In response to the recent reforms of petroleum prices, it also includes projects in transportation and energy (these projects had been contingent on the elimination of the petroleum subsidies). The Bank is undertaking sector work in education to help develop a project pipeline. Investments in industry are contingent on further policy reforms which could trigger substantial support for the manufacturing sector.

63. Built into the core lending program is a range of levels for a number of major projects which provides the opportunity to scale back lending if it is considered there is insufficient progress toward further policy reform. At this bottom level, lending would amount to about $350 million annually; this would permit the Bank to continue work on an array of projects that would be essential for maintaining the Bank's ongoing dialogue and contribution to sector reform and institutional development. In addition, this work would help maintain development initiatives undertaken in many of our recent projects.

64. It would be desirable, however, to encourage the Nigerians to build on their recent policy reforms by aiming for the high end of the core lending range, with annual levels of $500 to $600 million. Some of these loans could be quick disbursing if the Government continues to show sufficient committment to further reform. For example, the FY87 Road Rehabilitation project would be designed with an option for rapid disbursement. An industrial imports loan (now on the reserve list) will be developed that could lead the way to expand the second tier foreign exchange market and to promote non-oil exports. The full lending program would automatically incorporate quick disbursing sector loans, some of which are included on the current reserve list. If agreement is reached with the IMF, the Bank could also proceed with a SAL. The full lending program, to support a Medium Term Adjustment Program, would aim for an annual lending level of about one billion dollars.

B. Economic and Sector Work (ESW)

65. The staff years devoted to ESW would show a more-or-less even split between economic and sector work (see Annex D2). The program for 1987 is based on the restricted staff week levels now proposed by Bank management, while that for 1988 and 1989 assumes a restoration to previous levels in the light of the Government's adoption of a Medium Term Adjustment Program (if this does not materialize, the staff week levels will be scaled back accordingly). The thrust of the economic work would be on tasks addressing the structural adjustment process, with the emphasis on external and internal financial restructuring issues and on the approach to the planning and budgeting of public expenditures. The economic work has been designed to provide an efficient tool for creative dialogue on issues related to the formulation and implementation of a Medium Term Adjustment Program along the lines outlined in Section II. The aim will be to capitalize fully on the results of the extensive studies and reviews already carried out in these areas, with the initiation of new investigations being kept to a minimum.

66. The sector work will also be more sharply focussed. In the productive sector, agriculture will be emphasized because of its importance to economy and because an array of unresolved technical and instututional issues makes it more difficult to formulate a sector strategy than in manufacturing industry. Education will also receive special attention because of its importance in the longer term development efforts and the need to capture the benefits from the large past investments in the sector. Analysis in these and other sectors will focus on those areas of work required to firm up policy recommendations and strategy formulation, and to support the Bank's lending program.

Annex A

NIGERIA: Policy Actions Over Adjustment Program

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
EXCHANGE RATE, TRADE AND INCENTIVE POLICIES												
A. Exchange Rate: Move to a realistic level appropriate to the reformed trade policy environment.	1. Reconfirmation of policy of crawling adjustment of the exchange rate to reduce overvaluation of Naira.	1. Substantial initial devaluation and adoption of a more flexible exchange rate policy.	—					●				
	2. Proposal to establish a second tier foreign exchange market.	2. Move towards unification of the second-tier foreign exchange market with the 'formal' market.		[redacted]				●				(Industry sector loans)
	3. Implicit Devaluation through introduction of import surcharge (see I C 3 - Action recently taken) and export incentives (see I E - Actions recently taken).											
B. Export Controls & Taxes: Remove export controls and marketing restrictions on desirable non-oil exports.	1. Abolition of list of prohibited exports (with some exceptions).											
	2. Simplification of export licencing procedures.											
	3. Abolition of export monopoly power of the six commodity boards.											

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
C. Import Controls & Taxes: Dismantle import controls and move to a situation in which a relatively moderate and uniform customs tariff is the only form of direct intervention in import trade (with limited exceptions).	1. a. Promulgation of new customs tariff (1984) narrowing range of tariffs (10 to 60% w some exceptions). Adjustments made (post-1984) to correct anamolies.	1. Modify further customs tariff schedule, narrowing rates to 15 to 35% range.	[redacted]						●	●		
		2. a. Liberalize import controls on raw materials and spare parts.	[redacted]						●	●		
	b. Abolition of approved user and other schemes (1984) providing zero or concessionary rates to favored importers.	b. Formulate a plan for the phased liberalization of remaining import restrictions.	[redacted]						●	●		
	2. a. Simplification of "two queue" system of import controls and introduction of measures to remove administrative abuses and block leakages in granting import licences.	c. Implement liberalization plan.		[redacted]					●			
	b. Rationalization of priorities for issuance of import licences, with increased emphasis on (i) imports to support food production and (ii) raw materials and spare parts for manufacturers.											
	c. Creation of new category of import licences not valid for foreign exchange for approved priority imports.											

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
C. Import Controls & Taxes (Continued)	3. Introduction of a temporary import surcharge of 30%.	3. Import surcharge to be replaced by appropriate exchange rate action.	[redacted]					●				
	4. Abolition of compulsory advance deposit requirement for imports.											
D. Internal Trade Controls and Taxes: Withdrawal of Government from direct intervention in price setting. Excise taxes used as a major revenue measure, with coverage, structure and level being consistent with the principles for the setting of custom tariff levels.	1. Adjustment of domestic petroleum product prices to remove financial subsidy (except kerosine).	1. a. Relax ex-factory price controls on all goods.	—							●		
	2. Expansion of excise tax base (1984), with taxes re-structured to be consistent with new customs tariff schedule. Further modifications post 1984.	b. Formulate and implement approach for shift to crop pricing structure which reflects market forces. Re-examine role of the six commodity market boards and approach to setting of support prices for domestic crops.	[redacted]							●	●	Agricultural sector and project loans.
	3. Creation of Agricultural Prices and Tariff Group (APP) to be responsible for recommendations regarding price support and other trade policies relating to agriculture.	c. Adjust petroleum product prices in line with exchange rate adjustments.	[redacted]							●	●	Transport sector and project loans. Energy sector and project loans

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
D. Internal Trade Controls and Taxes (Continued)		2.a. Restructure excise taxes on ex-factory production of all goods to fall within range of, say, 5 to 25%.	▬						●	●		
		b. Apply additional excise duties to both locally produced and imported luxury goods (say 50 or 100%).	▬						●	●		
		c. Formulate (APP) and implement policies for taxation of forestry and agricultural products.	▬	▬	▬	▬			●	●		

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
E. Export Incentives: Introduce a package of fiscal incentives which removes impediments to exports and restores competitiveness of non-oil export production. Adopt other non-distortionary measures to promote non-oil exports.	1. Reactivation and modification of custums tariff drawback scheme. 2. Assistance on export costing and pricing (nature yet to be specified). 3. Extension of the Foreign Exchange Retention Scheme to allow exporters to retain 25% of foreign exchange earnings. 4. Activation of an already created Export Credit Guarantee and Insurance Scheme. 5. Encouragement of establishment of Free Export Zones in selected part of the country. Revitalization of the Export Promotion Council. Requirement for authorized foreign exchange dealers to set up export desk for a export promotional activity.	1.a. Review and modify appropriately Customs Tariff Drawback Scheme and other fiscal export incentives.		[redacted]					●	●		Industry sector loans
		b. Adjust these and other export incentives as needed (including phasing out transitory elements of the package) to reflect progress of exchange rate and other trade policy adjustments.			[redacted]						●	

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
F. Investment Incentives: Introduce a set of fiscal investment incentives which are meaningful to investors, mininally distortionary and simple in their administration. Also improve other efforts to promote foreign and local investment in desirable production activities.		1.a. Carry-out studies to finalize the coverage, design and administration of a package of fiscal investment incentives.								●		Industry sector loans
		b. Introduce incentive package.									●	Industry sector loans
		2. Undertake other measures to improve investment promotion including:										
		a. Improve investment promotion operations of the existing Industrial Development Coordinating Division of the Industrial Policy Review Body.								●	●	Industry sector loans
		b. Streamline regulatory measures relating to operations of enterprises and investment.								●	●	
		c. Review and ammend where necessary, investment policies and guidelines to promote desirable foreign investment.								●		
		d. Strengthen support services to the private sector (information, applied research, etc.).								●	●	Industry and Agricultural sector and Project loans.

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
PUBLIC EXPENDITURES POLICIES												
A. Level and Structure of Public Expenditures: Curtail public expenditures in a way which does least damage to the economy and ensures that maximum benefits flow from them. Composition of federal and state expenditures over the five-year adjustment period should support the macro-economic policy reforms and reflect basic economic principles, with allocations at the sectoral level being made within the context of clearly articulated sectoral development strategies (see also V - Sectoral Policies).	1. Reduction of salaries of public servants (1985). Freeze on hiring new public service staff in a wide range of positions (1984). Reduction of fringe benefits to public servants.	1. Stabalize public wage bill. (limits to be determined within the context of the rolling three-year budget see II B.1).	[redacted]						●	●	●	
	2. Reduction of non-statutory transfers to all economic and quasi-economic parastatals to 50% of present (1985) levels. Balance of needs to be obtained from increases in tariffs of parastatals.	2. Restore levels of supplies relative to manpower and give priority to routine and periodic maintenance over new investment (basis to be agreed within the context of the rolling three-year budget).	[redacted]							●	●	
	3. Major ongoing investment project (over N30 million to complete) reviewed by Inter-Ministerial Committee (with World Bank Technical Assistance - 1984).	3. Continue to reduce and ultimately eliminate transfers to commercially-oriented parastatals to cover their operating deficits and capital expenditure programs (with limited exceptions - see also III below).	[redacted]							●	●	
		4. Restructure Federal public investment program: within context of agreed (i) sector strategies (see V); (ii) principles for setting priorities and (iii) budget constraints.	[redacted]							●		

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
PUBLIC EXPENDITURES POLICIES (Continued)												
		b. Review public investment program annually in light of current revenue considerations, ensuring consistency with principles and sector strategies.	▬	▬	▬	▬	▬			●	●	Sectoral and project loans.
B. Public Expenditure Planning and Budgeting: Improve budgetary process by adopting approaches to planning and budgeting which allow implications of resource prospects over an extended period to be taken into account in making decisions on projects and programs.		1. Adopt a rolling multi-year budget:										
		a. Begin with a two year rolling budget.	▬						●	●		
		b. Expand to a three-year rolling budget.			▬				●		●	
		2. Adopt a core-type approach to planning of capital, investment relating it to the rolling multi-year budget.	▬							●		

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL 1	OTHER SALS	OTHER BANK LENDING OPERATIONS
PUBLIC ENTERPRISE POLICIES Improve overall efficiency of parastatals and reduce their heavy dependence on the Government for financial support. Privatize commercially oriented parastatals	1. Appointment of Study Group on Parastatals (1984). Report submitted. 2. Decision to divest of public holdings in commercially oriented enterprises (agricultural production, hotels, food, beverages, breweries, distilleries, distribution electrical electronic appliances and all non-strategic industries). Also, consideration to be given to reducing public holdings without losing control in banks, insurance companies and other financial enterprises. 3. Direction to parastatals to improve accounting practices and to issue timely financial reports. Accounts to be audited and published.	1. Prepare a Statement of Policy on Public Enterprises.										
		2. Restructure and strengthen e.g., Ministry of Finance Incorporated (MOFI) to effectively support the Ministries in planning and executing public enterprise reforms.										
		3. Within the context of sector strategies (see V - sector policies) carry out a rationalisation program for parastatals.										Parastatel sector loans Project loans
		a. Classify parastatals according to whether they should be left largely unchanged, restructured, privatized or liquidated. Indepth studies required for some enterprises.										
		b. Establish priorities and timetable for rationalization.										
		c. Prepare and implement restructuring sub-program.										
		d. Prepare and implement privatization and liquidation sub-program.										

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
FINANCIAL SYSTEM POLICIES Reduce Government intervention in financial markets and allow more discretion to the financial institutions in their operations.	1. Announcement to review financial system with the aim of its restructuring. To include (i) review of barriers to entry in banking and finance (ii) overhaul of operations of Agriculture Credit Guarantee Scheme and the Nigerian Agricultural and Cooperative Bank (NACB), with emphasis on decentralization and closer cooperation of NACB with the commercial banks.	1. Prepare and implement program for restructuring the financial sector. To include means to (i) reduce barriers to entry (ii) encourage branch expansion in rural areas (iii) further develop capital markets as a source of long-term finance and (iv) improve existing agricultural credit delivery system.	[redacted]						●	●		Financial sector loans
	2. Announcement to narrow gap in the margin and spread of interest rates.	2. a. Adjust interest rates to reflect positive real and scarcity yields.	[redacted]						●	●		
		b. Phase out interest differential among sectors.	[redacted]						●	●		
	3. Credit allocation system simplified by reducing number of sector with ceilings from 8 to 4.	3. Simplify further credit allocation system with the ultimate objective of eliminating it.										
		a. Aggregate ceilings.	[redacted]						●	●		
		b. Replace monthly reports with semi-annual reports.	[redacted]									
		c. Eliminate ceilings.			[redacted]				●	●		

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
SECTORAL POLICIES Prepare medium term development strategies for each sector, taking cognizance of broad policy reforms (as relevant), and address the specific policy and institutional reforms required to achieve development objectives in an efficient way as well as the appropriate schedule of public expenditures to support them. Special focus on the removal of bottlenecks and constraints affecting the efficient development of productive sectors.		1. Prepare strategy for agricultural sector (see also I, II, III, and V) and IV).										
		a. Prepare statement of policy on agriculture and water resource development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.	[redacted]							●		Agriculture sector, Multi-state ADP project loans.
		b. Create the APP to carry out necessary studies on agricultural product prices, marketing and incentives.	[redacted]							●		
		c. Ongoing revision and implementation of sector strategy.	[redacted]							●	●	
		2. Prepare strategy for oil and gas sector (see also I, II, III, and IV.										Oil and gas sector and project loans.
		a. Prepare statement of policy on oil and gas development, incorporating principles for public investment, and parastatal operations in the sector.	[redacted]							●		
		b. Ongoing revisions and implementation of sector strategy.	[redacted]							●	●	

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
SECTOR POLICIES (Continued)												
	Establishment of Industry and Trade Policy Analysis Unit (ITAP) expected soon under World Bank Industry Technical Assistance Project loan to the Government. Will work in collaboration with ATPG to carry out trade and incentive policy analysis.	3. Prepare strategy for the manufacturing sector (see also I, II, III and IV).										
		a. Prepare statement of policy on manufacturing development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.	[redacted]							●		Industry sector loans
		b. Designation of high level interministerial body for guiding and counseling the trade and incentive policy reforms (for both manufacturing and agriculture).	[redacted]							●		
		c. Key industry studies to be carried out as part of the work of ITAP, with aim of: (i) identifying and formulating measure to overcome regulatory constraints and market imperfections affecting efficient development; (ii) reassessing approach to public involvement in the industries and (iii) providing information base for promotion of private investment. Priority to be given to studies of refineries, petrochemicals, steel, and pulp and paper.	[redacted]							●		
		d. Ongoing revisions (especially in light of findings of industry studies) and implementation of sector strategy.	[redacted]							●	●	

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD						VEHICLE FOR CONDITIONALITY				
		ACTIONS TO BE TAKEN	TARGET COMPLETION DATE					IMF PROGRAMS		SAL PROGRAMS		OTHER BANK LENDING OPERATIONS
			YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	SOLE COND.	JOINT COND.	SAL I	OTHER SALS	
SECTOR POLICIES (Continued)		4. Prepare strategies for education and health sectors (see also II, III, IV and V).										Sector and project loans.
		a. Prepare statements of policy incorporating federal/state responsibilities, and principles for cost-recovery, public investment and recurrent expenditures.	[redacted]									
		b. Prepare multi-year public expenditure program (categorize core, reserve core, non-core) consistent with policy statement, budget constraints and principles underlying structure of public expenditure program. Relate program to state responsibilities.	[redacted]									
		c. Ongoing revisions and implementation of strategies.	[redacted]									
		5. Prepare, revise and implement strategies for other sectors.	[redacted]									Sector and project loans

Annex B

NIGERIA: Policy Actions in First Year of Adjustment Program

Policy Action	At Commencement	During First Year
I. Exchange Rate, Trade and Incentive Policies		
Exchange Rate.		
1. Initial discrete devaluation (at least 50%).	X	
[2. Review formula for crawling adjustments to exchange rate to allow margin for changes in real rate as well as reflecting domestic - international inflation differentials.]	X	
[3. Adjust Naira value regularly (monthly) on basis of revised formula.]		X
[4. Allocate 5 percent (at least) of oil export proceeds to second tier foreign exchange market.]		X
Import Controls and Taxes		
1. Modify customs tariff schedule, narrowing rates to 15 to 35% range (with clustering in narrower band of 20 to 30%).		X
2. a. Liberalize import controls on raw materials and spare parts through their transfer to open general licence status.		X
b. Formulate a plan for the phased liberalization of remaining import restrictions.		X
Internal Trade Controls and Taxes		
1. a. Relax ex-factory price controls on all goods.		X
b. Formulate approach for shift to crop pricing structure which reflects market forces. Re-examine role of the six commodity market boards to setting of support prices for domestic crops (APP to be responsible.)		X
c. Adjust petroleum product prices in line with exchange rate adjustments.	X	X
2. a. Restructure excise tax on ex-factory production of all goods to fall within range of , say, 5 to 25%.	X	
b. Apply additional excise taxes to both locally produced and imported luxury goods (say, 50 or 100%).	X	
Export Incentives		
1. Review and modify appropriate customs drawback scheme and other fiscal export incentives with aim of ensuring (with some exceptions) (i) exemption (or equivalent) from tariffs and excise taxes on inputs directly and indirectly incorporated in export production; (ii) exemption from excise taxes on export sales; (iii) compensation for discriminatory effect of import protection regime and exchange rate policy on value added; (iv) simplication of the fiscal export incentive package and of its administration. Appropriate incentives for export traders would form part of this review.		X X

Policy Action	At Commencement	During First Year
Investment Incentives		
1. Carry out studies to finalize coverage, design and administration of a package of fiscal investment incentives (under taken jointly by the teams involved with ITAP and APP).		X
2. a. Commence work to improve operations of the Industrial Development Coordinating Division (to become effective one-stop shop for industrial approvals and investment promotion).		X
b. Review and amend, where necessary, investment policies and guidelines to promote desirable foreign investment. This would include increased ownership flexibility in some areas.		X
II. Public Expenditure Policies		
1. Maintain restraints on public sector wage increases and extend freeze on recruitment to all but the most critical skills.	X	X
2. In 1987 budget, reflect move to (i) restore levels of supplies nature and manpower; (ii) give priority to routine and periodic maintenance over new investment; and (iii) further reduce in transfers to commercially-oriented parastatals (basis to be agreed within context of a rolling budget - see 4 below.)	X	
3. Agree on restructured public investment program with context of sector strategies and (i) specify principles for the setting of priorities for completing ongoing capital projects; (ii) re-assess ongoing and proposed new projects (with completion costs over ₦30 million) against these principles; and (iii) categorize projects into "core", "reserve core" and "non-core" within context of agreed budget constraints and incorporate into rolling budget estimates.	X	
4. Adopt a rolling multi-year budget. Begin with a two year rolling budget.	X	
III. Public Enterprise Policies		
1. Prepare a Statement of Policy on Public Enterprises.	X	
2. Restructure and strengthen Ministry of Finance Incorporated (MOFI) or some other agency of Government to effectively support the Ministries in planning and executing public enterprise reforms.		X

Policy Action	At Commencement	During First Year
3. Within the context of sector strategies (see V - sector policies) carry out a rationalization program for parastatals.		
a. Classify parastatals according to whether they should be left largely unchanged, restructured, privatized or liquidated. Indepth studies required for some enterprises.	X	
b. Establish priorities and timetable for rationalization.	X	
c. Prepare and commence implementation of restructuring sub-program building into it: (i) increased autonomy of public enterprices in making operating decisions (management, procurement, staffing, etc.) and improved accountability; (ii) further autonomy of public enterprises in setting tariffs and prices (where relevant); (iii) improved accounting practices, financial controls and management in public enterprises; and (iv) rehabilitation requirements.		X
d. Prepare and commence implementation of privatization and liquidation sub-program.		X
IV. Financial System Policies		
1. Prepare program for restructuring the financial sector. To include means to: (i) reduce barriers to entry; (ii) encourage branch expansion in rural areas; (iii) further develop capital markets as a source of long-term finance; and (iv) improve existing agricultural credit delivery system.		X
2. Adjust interest rates to reflect positive real and scarcity yields.		X
3. Simplify further credit allocation system: (i) aggregate ceilings; and (ii) replace monthly reports with semi-annual reports.		X
V. Productive Sector Policies		
1. Prepare strategy for agricultural sector.		
a. Prepare statement of policy on agriculture and water resource development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.	X	
b. Create the APP to carry out necessary studies on agricultural product prices, marketing and incentives.	X	
2. Prepare strategy for oil and gas sector. Prepare statement of policy on oil and gas development, incorporating principles for public investment and parastatal operations in the sector.	X	

Policy Action	At Commencement	During First Year
3. Prepare strategy for the manufacturing sector.		
a. Prepare statement of policy on manufacturing development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.	X	
b. Designation of high level interministerial body for guiding and counseling the trade and incentive policy reforms (for both manufacturing and agriculture).	X	
c. Industry studies for refineries, petrochemicals, steel and pulp and paper to be carried out as part of the work of ITAP, with the principal aim of reassessing approach to public involvement in the industries.		X

Annex C

NIGERIA: Sector Policies

I. Productive Sectors

Agriculture

1. Sustained growth of the agricultural sector requires that comparative advantage be the primary criteria for the crop and technology choices that have to be made. Food crops are and must remain central to the development strategy for the sector and should continue to be given strong support from the Government in areas such as research. However, increased support should be given to export crops and import competing non-food commercial crops. Success in developing a strong agricultural base will depend on a careful mix of public expenditure programs with policies that create an environment of incentives favorable to private enterprise. The extensive information and analysis now available on agriculture must be drawn together to frame a more coherent sector strategy.

2. Prices and Subsidies. It will be important to shift farmer incentives from input subsidies, which place an undue burden on the Government's budget, to a crop pricing structure which reflects market forces and requires minimal intervention. Prices of both inputs and outputs should generally be allowed to be determined within the context of Nigeria's overall trade policies, with the use of input subsidies being continued only for promotional or other specifically directed short term objectives. An export incentive package should be introduced so that export crops are not unduly discriminated against.

3. Parastatals. Both Federal and state governments should continue to divest themselves of production-oriented parastatals, or enter into joint ventures to enlist private management skills in restoring enterprises to profitability. The role of the commodity trading boards should be reviewed. Financially unviable enterprises should be liquidated and steps taken to improve the efficiency of enterprises which will remain within the public sector.

4. Irrigation and Integrated Rural Development. Budget constraints mean that resources will have to be concentrated on maximizing the returns from existing investments. In this respect, allocations for irrigation should not be used for large scale dam and water diversion structures but should instead emphasize down-stream delivery systems where the incremental costs are within reach, with even greater emphasis on the development of smaller scale low-cost irrigation schemes. The ADPs will continue to justify a sizeable proportion of expenditure, although their components need to be examined in the light of recent indications of the absence of an economic response to fertilizer applications on sorghum and wheat.

5. Support Investments and Recurrent Expenditures. The Government should actively pursue applied research programs which will expedite the adoption of new varieties and technologies from the national and international research centers and establish their appropriateness at the

farm level. While such research should encompass all aspects of agricultural cropping, it should give priority to rain-fed farming in the lower rainfall areas. In addition, the Government should consider the advantages that could be achieved by moving the country's research activities under the Ministry of Agriculture. Forestry development will also remain critical to meet long term national wood and pulp needs and to combat serious natural resource degradation. A large share of planned expenditures should thus be directed to protection and resource conservation (e.g., shelter belts, arid zone afforestation and rural forestry). It will be necessary to restore an appropriate balance between overheads, maintenance and manpower expenditures at both the federal and state levels if agricultural officials are to carry out their work effectively.

Oil and Gas

6. Investment Policy. It will be important for the joint venture companies to maintain investment in oil exploration and development at levels that will ensure satisfactory oil reserve/production ratios. To minimize its investment burden in the petroleum subsector, the Government should consider entering into production sharing agreements outside of the Delta. Desirable revisions of NNPC's own investments in oil exploration should be aimed at minimizing expensive exploratory domestic drilling over the adjustment period. At the same time, the investment program needs to be scrutinized very closely and refocussed on areas such as gas utilization and LPG extraction, which would cushion the effects of falling oil prices.

7. Gas infrastructure development should be given priority to enable power stations and selected industrial users to substitute gas that is presently being flared for the more expensive fuel oil. The highest priority is the construction of the Warri-Lagos pipeline and the corresponding development of the gas field of Utorogu. This program could also be related to the gathering of associated gas. This gas would also be used for LPG, initially for export and eventually for domestic markets once they are developed. While the prices for domestic products were dramatically increased in the 1986 budget, agreements for gas producer and consumer prices are still needed to promote the substitution of gas for liquid fuels, primarily in the power sector.

8. The approach adopted in the LNG project is a strategic one and allows for a great degree of flexibility with respect to the scope of the project, its starting date and phasing, and the degree of private sector participation. The project would have the highest chance of success if it were set up on a joint venture basis, with at least a 40 percent share for foreign companies and with an experienced operating company in charge of management. The project should only be embarked upon if purchase contracts can be guaranteed.

9. Joint Ventures. Earlier this year, basic agreements on oil taxation and lifting regulations were concluded between NNPC and its joint venture partners which, although they may need to be renegotiated soon, give Nigeria more flexibility to react to the volatile international oil

market. NNPC should rely on joint ventures in all facets of oil and gas production, but it should be reorganized as a holding company with largely independent subsidiaries and divest itself of its petroleum product distribution companies.

Manufacturing

10. The broader exchange rate, trade and incentive policy reforms will serve to encourage desirable private investment and production in manufacturing. However, subsectoral strategies will need to be prepared for steel, petrochemicals and pulp and paper, which constitute major areas of Government investment in the sector. With the projected severe resource constraints and the poor performance and high costs of past public investments, there is a need to reduce considerably the role of the public sector in industrial development. Increased domestic and foreign private investment and production in line with Nigeria's comparative advantage would need to be encouraged as a basis for future sustained industrial growth. Meanwhile, public sector efforts could be redirected towards strengthening industrial infrastructure and support services.

10. Strategy for Public Sector Investment. The focus should be limited to timely completion of economically viable ongoing projects yielding the highest and most immediate returns, particularly in terms of net foreign exchange savings. This will involve extremely difficult choices because of the number, scope and implementation status of the projects. The extent of the resource constraints will be such that even certain potentially viable ongoing projects will need to be deferred for completion, rephased or reshaped to reduce their costs. Continued funding of projects of marginal or negative viability should be limited to covering the minimum costs entailed in suspending, mothballing or discontinuing them. The necessary scaling down of public expenditures in the sector should be achieved as follows. In steel, given the inadequate market for its products, its high costs and doubtful viability, construction of the Ajaokuta steel works should preferably be discontinued or deferred indefinitely. Further expenditures to complete the Delta Steel complex should be held to minimum necessary levels. No new projects (including the flat products plant, special alloys plant and foundry) should be started. In petrochemicals, priority should be given to the completion of the plants to produce polypropylene, carbon black and synthetic detergents ("Phase I"), but with a restructuring plan for the latter two plants. The first phase ("Phase IIA") of a proposed large polyolephine based complex to produce thermo-plastic should be deferred. In refineries, the debottlenecking projects at the Kaduna and Wassi refineries should be compelted as soon as possible but the Government should reconsider its decision to proceed with the proposed Harcourt II refinery given its unacceptably low economic rate of return. In pulp and paper, the Iwopin project should be reappraised to test its viability and explore alternative design options.

11. Restructuring of Public Enterprises. Many public sector industrial projects have weak and under-capitalized financial structures. Some are unable to service their debt and are expected to incur substantial operating losses. Where these projects are potentially viable, they will

require restructuring to make them financially self-sustaining. In-depth operations audits should be conducted for each enterprise by independent technical consultants to determine feasible cost-saving efficiencies and identify production restructuring needs. In this context, increased private sector participation could usefully provide necessary specialized technical know-how, management and marketing expertise where it is presently lacking in the public sector (e.g., in petrochemicals). It would be important to ensure maximum autonomy of management of all public sector industrial enterprises so that they could be run along commercial lines. However, in line with the Government's announced intentions most public sector industrial projects should be privatized. The Federal Government will have to write-off part (or in some cases all) of its investment in a number of cases.

2. Infrastructure Sectors

Electrical Power

12. Actions aimed at improving generation, transmission and distribution systems through a rehabilitation program and better balancing of generation and distribution capacities are of utmost priority in the development of the power sector. In parallel, steps have to be taken to reduce system losses, improve collections and restore financial viability.

13. System Expansion. To meet the expected deficit in power balances through 1995 and avoid further expansion of auto producer capacity, the rehabilitation of existing generating plants, completion of the on-going Egbin steam project and the construction of the gas pipeline (which would service gas fueled capacity at the Egbin plant) are essential. A satisfactory power balance could be achieved through the mid-1990s if these programs can be completed in a timely fashion, allowing the deferral of work on Shiroro hydro, Delta IV thermal and other power generation projects until after 1991. The Delta Steel combined cycle plant would also not be required. If additional financial resources were to become available over the 1987-91 period, then the completion of the Shiroro project could be brought forward since it is economic on a fuel saving basis. The plant rehabilitation program must be completed because it is the only measure that can economically provide additional power supplies during the next couple of years as well as contribute to the improvement of NEPA's financial position through increased sales, lower systems losses and more efficient generation. The Egbin plant should have priority because, in conjunction with the gas pipeline, it would be the least cost means of meeting generating requirements up to 1995. Priority also has to be given to the strengthening of communications and control facilities, the reinforcement of the transmission and subtransmission systems, and the rehabilitation and expansion of the distribution system to handle the expected demand.

14. Financial Recovery. NEPA's financial situation is extremely weak. A phased 50 percent increase in tariffs should be sought over the next two to three years. NEPA also needs to step up its on-going efforts

to improve bill collections and reduce operating costs. The Government should also consider a capital restructuring of NEPA. By converting a proportion of Government loans to equity, NEPA would be absolved of some of the heavy debt burden to the Government thus reducing the amount of tariff increase required.

Telecommunications

15. Critical for the effective functioning of the sector and its future development will be the formulation of a long term strategy. Essential components of the strategy would be: (i) the specification of an appropriate network development program in which investment priorities recognize the constraints imposed by the availability of financial resources and implementation capacity; (ii) a reorganization of the institutional structure and the development of effective management systems in all functional areas; and (iii) the achievement of financial viability through improved operating efficiencies, reduced capital costs and a revised tariff structure.

16. Network Development Program. Planned extensions to the system should be postponed until the existing facilities are more effectively utilized and financial viability is achieved. Top priority should be accorded to the rehabilitation, upgrading and maintenance of existing facilities. The most immediate requirement is to bring the vast existing and ongoing plant investments to their full revenue earning status. This will mean the deferral or rephasing of some installations where it appears unlikely that contractual obligations can be financed using available resources. The progressive use of digital technology should be a feature of the program over the longer term.

17. Institutional Structure and Management Systems. The amalgamations of the telecommunications arm of P&T with NET into the new entity NITEL is a positive step. However, the parameters for the reorganization need to be established, with particular attention being paid to ensuring that NITEL has adequate autonomy (especially in areas of financial management, staffing and procurement) and that it is endowed with the requisite managerial and technical ability to effectively implement the network development program and achieve financial viability. Since it will take some time for the amalgamation to be fully effective, immediate steps should be taken to streamline the functions of P&T and NET. The steps should include: (i) the elimination of non-compatible exchanges through increased coordination; (ii) a reduction in the present high ratio of staffing per installed line, particularly in the clerical and administrative areas; and (iii) improved management planning, reporting and information systems.

18. Financial Viability. The sector should aim to break even on current account (excluding depreciaiton and debt service) by the end of 1987, with increasing surpluses being accrued after that date for debt service and investment purposes. On the revenue side, high priority should be given to a comprehensive review of the tariff structure with the aim of increasing installation fees and rentals to more realistic levels. Equally

important will be an effort to substantially upgrade the billing and collection system, with immediate steps being taken to collect overdue accounts receivable. To bring capital costs under control, improved procedures for procurement and installation supervision are essential. The reliance on turnkey contracts for capital works should be reduced, particularly for the next major phase of development which should be the progressive introduction of digital transmission and switching technology.

Transport

19. The key objectives for the transport sector are to protect and better utilize existing facilities, improve the performance of transport parastatals and increase cost recovery throughout the sector. Improvements in urban public transport and road safety are also viewed as sector objectives.

20. Directions for Investment. Future expenditures should continue to concentrate on roads, which account for the overwhelming proportion of the domestic transport spending. However, road expenditure needs to be substantially reoriented toward rehabilitation and maintenance. There is scope for rail to play a much larger role than in the past, but only if the efficiency of operations is significantly improved and efforts are focussed on the activities in which rail enjoys a comparative advantage. In order to meet even the demands presently placed upon it, the National Rail Commission (NRC) urgently needs locomotive spares (and, less urgently, wagon spares). If performance improves accordingly, this could then be followed up by more substantial funding towards the end of the decade for truck and communication materials and some limited acquisition of new locomotives and rolling stock. By virtue of the significant investment in ports and airports in the latter 1970s, basic capacity is adequate in these modes and only limited funds are required for ancillary equipment and repair work. In aviation operations the private sector should be allowed full scope in order to minimize the need for public funding of Nigerian Airways.

21. Parastatal Reforms. Despite recent staff cuts, there is substantial scope for the introduction of further cost saving measures. Capital restructuring and the setting of financial targets are also required to make the enterprises more self sufficient. There needs to be more accountability by and with the enterprises, and inherently non-viable operations need to be eliminaited unless the Government specifically directs otherwise, in which case the enterprise should be compensated for its "social obligations", so that clear commercially based financial performance targets can be specified. Serious consideration should be given to truncating NRC by closing some branch lines, terminal sections, and stations on the main lines (90 percent of NRC's revenue originates from 10 percent of its stations). A minimum rail tariff increase of around 50 percent needs to be immediately implemented, with agreed principles on further increases over time to attain full cost recovery. Over the next three years, a staff reduction of around 30 percent should be pursued. The National Ports Authority (NPA) should initially reduce its staff by 10

percent over the next year through the divestiture of workshop operations in the secondary ports. Port tariffs should also be increased.

22. The idea of privatizing transport parastatals has been receiving serious attention, but no decisions have yet been taken. Existing information suggests that a number of such parastatals could indeed be fully privatized. These would include the National Freight Company, the Government Coastal Agency, the National Cargo Handling Company and perhaps the Central Water Transport Company. In other cases, privatization of selected functions appears warranted, particularly workshops and support activities for computers. In this regard, the recent trend away from contracting out services and undertaking these 'in-house', while understandable in the light of abuse of contracts, is almost certainly going to decrease effective performance of these services. The answer may lie instead in tighter control and supervision of contracts.

Water Supply

23. In order to maximize the return on any future investment in the water supply sector, the key objectives have to be to protect and better utilize existing facilities, and to balance supply capacity and distribution capability. Provision of new water supply systems in urban ares (including expansion of such systems) and in rural areas should only be made where the need is critical and the potential beneficiaries clearly demonstrate their willingness to pay. Increased efficiencies in the operations of state water utilities and those agencies responsible for rural water supplies must be essential components of any sector development program. The state water utilities are capable of fulfilling the required role in the urban areas provided the Government assists in the setting of common standards and in training. It is not feasible for any one government agency, at either federal or state level, to be responsible for all aspects of the operation and maintenance of rural water supply installations. The transportation requirements alone dictate that a rural community served by an installation must be largely responsible for its maintenance.

24. Investment Priorities of State Governments. First priority must be given to the rehabilitation of water supply systems to enable them to operate at their design capacity. The majority of the investment required for rehabilitation is for replacement of defective electrical and mechanical equipment, such as pump motors, starters, valves and diesel generators. In the rural areas, the communities served should be responsible for the operation and maintenance of point supply sources (principally handpumps). Government support should be limited to the provision of spare parts, technical advice and training. Provision of any new rural water supply installation should be limited to those communities which are willing to pay an appropriate amount of the construction cost prior to work commencing and would agree to be responsible for operation and maintenance. For those large urban areas in Nigeria where the economic cost of a grossly insufficient water supply system is a major constraint to development and where the population is prepared to pay the full cost of providing a reliable supply (including a contribution towards capital

cost), the provision of new and the expansion of existing systems should proceed. The financial performance of the concerned state water utility should be a major factor in the decision of whether or not to provide finance for new works.

25. Institutional Reforms. Tariffs need to be reviewed and increased in almost all state water utilities. Billing and collection targets also need to be set. Guidelines should be provided by the Federal Government to the states on the establishment of appropriate tariffs, budgeting and accounting procedures, and staffing levels. In the rural water supply sub-sector all activities, including existing installations, should be brought under the control of one agency in each state. At the same time, a system will have to be established which will enable the rural communities with a point supply source to obtain (at a charge) spare parts, assistance in maintenance and training.

26. Federal Financial Support. It would be a helpful incentive for development of the sector if Federal Government financial support was available up to a specified percentage of the cost of water supply schemes. To qualify, schemes would have to be prepared in accordance with federal guidelines.

Housing and Urban Development

27. The growing financial constraints facing states, coupled with dramatic population increases in the older, larger and most economically active urban centers calls for a reassessment of how best to deal with urban growth. These same cities are also suffering from acute and rising deficiencies in basic urban services and infrastructure, which must be brought up to aminimum level if they are to function efficiently as centers of administration and production, contribute to the productivity of the Nigerian economy and to offer safe and healthy environments in which to live. The amount of investment needed to overcome Nigeria's urban problems is so vast that priorities have to be set carefully.

28. Role of the Federal Ministry of Works and Housing (FMWH). The above concerns have led the FMWH to explore more efficient approaches to the management of urban growth. It has confirmed sites an services as the approach to be adopted in meeting the demand for housing. Simultaneously, it has indicated that the Federal and state governments should not construct housing, but rather provide the land and infrastructure to promote private sector shelter delivery. The importance of financial independence, the necessity to promote local resource mobilization and improved fiscal management is also recognized. There thus seems to be a clear appreciation of the need to reshape the Federal Government's role in the provision of housing, with a greater emphasis on policy setting and technical support and away from the direct provision of finished units. However, the FMWH will have to develop action programs rooted in these general principles and support them by: (i) the issuance of a Housing Policy Paper that emphasizes the continuing shift towards the Sites and Services concept, reinforced by selected demonstration projects that involve the States and promotes the role of the private sector; (ii) the

issuance of an Urban Policy Paper that clarifies the roles of the Federal, State and Local Authorities; (iii) setting standards for planning, land use, infrastructure and building; and (iv) training its staff to be better equipped for these tasks. While FMBN has the authority to finance shelter investment, no counterpart mechanism for identifying, appraising and financing sound urban infrastructure investment exists.

29. Urban Infrastructure Development Fund. For this purpose, an Urban Infrastructure Development Fund should be established. The broad objectives of the Fund would be to provide state and local governments with the means to increase investment in technically and financially sound urban infrastructure projects, and to improve municipal services. The Fund's operating procedures would establish certain actions on the part of borrowers (e.g., passage of financial reform legislation, preparation of detailed feasiblity studies) as prequalification criteria. In parallel, the local and state governments should find better and more effective ways of generating and collecting revenues - including improved cost recovery measures - to support their infrastructure investments.

30. National Capital. Abuja is a national investment that has yet to pay a return. One view would hold that the sunk cost should be written off, and the move from Lagos to the new Capital be put on hold until higher priority and more cost effective programs have been funded. The opposing view is that the need to utilize the sizeable past investment is urgent for political as well as economic reasons. However, Abuja will continue to grow whether or not the capial is moved. Clearly, the funding is not available for a massive shift of all government functions all at once and a phased shift would seem to be the most viable. What is needed is an "operations research" oriented study of the costs and benefits that would be attached to the alternate scenarios for the move. The "no move" scenario would be scrutinized along with the alternative. Given the funds invested to date in Abuja, the cost of such a study would be small compared to the benefit of selecting an effective least cost plan of action based on careful analysis. While the study is under way, Abuja could be used by the FMWH as a test site for public/private sector joint ventures. Sites and service projects could be commenced and market demand for alternative plot sizes and basic layouts could be tested.

3. Social Sectors

Education

31. The Government should adopt a series of fundamental policy reforms designed to accomplish structural adjustments in the education sector. The overall strategy should embrace: (i) restoring the materials-manpower ratios by increasing the proportion of funds allocated for non-wage recurrent expenditures at all levels of education, such that productive efficiency is ensured; (ii) increasing the level of cost recovery in secondary and post-secondary institutions relative to current cost-recovery levels in primary schools in a way consistent with productive efficiency and distributive justice; (iii) improving maintenance and rehabilitation of educational plant, such that minimally acceptable

standards are achieved; (iv) improving staffing and equipment for technical training; and (v) using price incentives at the senior secondary and post-secondary levels to increase the proportion of students in science and technology subjects. The rationalization of previous heavy investments in the sector should constitute a major objective of the strategy.

32. Primary Education. There should be a reassertion by the Government that the nation's principal objective in the education sector is to provide primary education of sufficient quality in all states to yield the high social rates of return traditionally produced by this subsector. Towards this end, consideration should be given to upgrading the state institutions responsible for primary schooling.

33. Secondary Education. A national policy on tuition at the secondary level should be introduced which enables schools to recover a defined portion of per-student costs, part of which would be spent at the discretion of the individual school and could be directed towards crucial (e.g., non-salary) inputs. The acceleration of "deboarding" should continue through the conversion of student hostels to classrooms, laboratories and workshops. Whenever boarding is retained (e.g., in the unity schools of the Federal Government), charges should be levied on parents on a full cost recovery basis. The private provision of secondary education under rigorous state set standards should be encouraged.

34. Post-Secondary Education. Priority should be given to a program to improve and strengthen polytechnics. Further, the course emphasis in the polytechnics should shift from business to technical subjects, with advanced technical courses being offered in some to train technical teachers and higher level skilled workers for industry (a function not presently being performed in the country). The aim by 1991 should be to adjust polytechnic enrollments upwards by around 20 percent, holding university enrollments constant.

35. Cost Recovery. Fees for tuition should be established for all post-secondary institutions, setting fuller cost recovery for universities (say 60 percent of total recurrent costs per student) than for polytechnics (say 40 percent). At the university level, fees for science and technical based disciplines should be set at lower and arts-based at higher than average levels. In addition, full cost recovery for boarding facilities should be instituted in a phased manner. As a corollary, consideration should be given to the introduction of both a merit-based scholarship scheme and needs-based student loan scheme to ensure that access to post-primary institutions for low income students is at a minimum preserved - and preferably enlarged - during the period of heightened cost recovery.

Health

36. A bold and pragmatic policy framework has begun to emerge in the Government's strategy for the health sector which envisages a public/private partnership where the Government assumes principal responsibility for preventative care and the private sector for curative care. High priority is to be given to reducing fertility and the rate of

population growth. The Federal Ministry of Health envisions its long-term roles as addressing basic preventative health care (water quality, waste disposal and health education), helping to set standards and monitor achievements and to participate in the international health community.

37. Under the new policy framework, all levels of government would have its health care responsibilities shaped by the following principles: (i) public participation in the implementation of health service programs organized at the village and local government levels; (ii) encouragement of the private sector and private-public partnerships; (iii) expanded emphasis on preventive care; (iv) promotion of a system, based on primary care facilities, to help address community level health problems; (v) financing of curative health services by a mix of public and private expenditures including fees, drug sales contributions, retainer contracts and insurance schemes; (vi) training in the health professions to be undertaken at the individual's expense; (vii) increased efficiency in the delivery of health services through appropriate manpower and material balances and economies in the purchase of materials; and (viii) limited integration of qualified traditional healers and modern health providers.

38. Disengagement. The process of transfer of certain governmental activities to the private sector will have to be spelled out. The Hospital Management Boards have been envisioned as the vehicles for effective public disengagement from higher-level curative care. However, there will continue to be a requirement (though diminishing) for public funds to support the institutions in the hospital subsector - and the formula for setting the level of these funds and the conditions attached to them will need to be determined at an early stage to avoid ongoing conflicts. In parallel, a decision will have to be made on the approach to the ownership of, and operational responsibility for, clinics and dispensaries. One approach could be to transfer the ownership and operational responsibility to general hospitals, while other routes would be to develop local health authorities or to allow their absorption by village health associations. Policies relating to licensing of private sector facilities and the setting of standards of practice will also have to be reviewed. The reconciliation of the conflict in the government's desire to have curative services available in unserved areas on the one hand, and to disengage itself form providing the services on the other, will also have to be addressed.

39. Access and Public Participation. The high costs associated with shifting public preventive health care to unserved areas dictate a gradual reduction in geographical disparities. One avenue which could be explored for both cost reductions and increasing the access to care is the further promotion of health programs through schools, especially in presently unserved areas. Schools could increasingly become the locus of a range of preventive health care services for catchment populations. Village and local government health associations would also be important avenues for mobilizing community involvement in the provision of health services. The positive role they can play in cost recovery and control over expenditures should be recognized, as well as their ability to encourage contributions from villagers (such as labor and land) for the construction and maintenance of infrastructure. The establishment of a fund, in cooperation

with the individual states and with support from local banks, to provide start-up support for health programs to village and local government health associations would be helpful.

40. Cost Recovery and Insurance. The Government aims to move towards cost recovery in health care services. The pricing of curative health care services will increasingly come under the ambit of the private sector, although the Government will need to continue playing a role to help contain costs. In parallel, a health insurance scheme is proposed, which is seen as providing principally employee-paid financing of ambulatory and institutional curative care in both government and private facilities. Major technical issues will need be resolved before the scheme can be implemented, e.g., target population, basis for setting premium and collecting them, and equity issues.

41. Implementation. The Federal and State Ministries of Health will require sophisticated planning skills and adequate resources to efect the structural adjustments sought in the new health policy framework. The information, management and date collection systems will need to be strengthened and streamlined, and a "bottom up" approach to record keeping instituted. Specific information on health finance will be required, e.g., compartive unit costs to facilitate sound decision making. Special attention will need to be given to strengthening the financial and administrative capacity of local governments in dealing with health issues. Many of the new policies will not have an immediate impact on the capital budget as they will need to be introduced over a number of years, although the proposed privatization of curative care -- which implies at a minimum shifting hospitals to the private sector -- will eventually eliminate the need for public sector construction or expansion of hospitals. In any event it will take years, especially in the North, before the smaller health facilities -- dispensaries, maternities, health clinics, etc. -- can be privatized. The new policies on cost recovery will also have to be introduced cautiously and are unlikely to work without additional investments to improve services. Cost recovery will have to be partial outside of curative care and its more immediate effect is likely to be the easing of recurrent budgets (e.g., through revolving funds being developed by some of the states for the purchase of drugs).

Annex D

NIGERIA: Bank Lending and ESW Programs

A. Lending Program 1986-90 ($millions)

Core Program		Reserve List	
FY 86			
Lagos Solid Waste	72		
Industry TA	5		
Imo Urban	53		
Livestock II	81		
Transport Parastatals	22		
	=======		
	233		
FY 87		**FY 87**	
Forestry II	72	Industrial Rehab.	200
(S) Southern Borno ADP	25		
Road Rehabilitation	75-200		
(S) Multi State ADP	162		
	=======		
	334-459		
FY 88		**FY 88**	
Public Ent. TA	35	Oil Palm V	100-80
(S) Urban Infrastructure	80-150	SAL	400
(S) Lagos Water Supply	90-150	Education	50
Imo Population & Health	50		=======
Power VII	100-200		100-530
	=======		
	355-585		
FY 89		**FY 89**	
(S) Multi State ADP II	120-220	Rural Water	80-130
(S) Water Rehabilitation	75-150	Industry Manpower	50
(S) Agriculture Manpower	50-150	Industry Rehab.	400
Population/Health (Nat'l)	80		=======
(S) ELP	80-130		80-580
	=======		
	405-655		
FY 90		**FY 90**	
(S) Water Supply	100-150	Agric. Credit	50-150
Urban Development	70-120	Roads	100-200
(S) Population (State)	100	Industrial Imports	300
(S) Irrigation	75-150		=======
(S) Telecommunications	25-150		150-650
(S) Agric. Res.	75-120		
	=======		
	445-790		

Total FY 86-90: 1772-2722

B. Indicative Economic Sector Work Program

ESW Category	Staff Weeks 1987	1988	1989
1. Economic Work			
A. Structural Admustment Process	118	170	170
Financial Restructuring - External	(35)	(40)	(40)
Financial Restructuring - Internal	(47)	(80)	(80)
Public Expenditure	(17)	(20)	(20)
Other Macroeconomic Dialogue (incl. trade & incentive policies)	(19)	(40)	(40)
B. Economic Reporting and Strategy Papers	27	30	30
	====	====	====
Total Economic Work	147	200	200
2. Sector Work			
A. Agriculture	79	50	30
B. Energy	29	20	10
C. Industry	12	10	10
D. Education	34	30	30
E. Other Sectors	36	110	140
	====	====	====
Total Sector Work	190	220	220
3. Other ESW	45	80	80
Total Economic and Sector Work	380	500	500

Notes: (1) 1977 work program based on restricted levels now proposed by Bank management.

(2) 1978 and 1979 Work Program staff weeks assume restoration to previous levels and reflect work associated with the Medium Term Adjustment Program.

Annex E

NIGERIA: Assumptions and Results of Financial Assessments

1. Tables 1-8 summarize the results of the various projections made of Nigeria's external balance. Table 1 presents the debt outstanding as of the end of 1985. Table 2 shows the import levels that would result if Nigeria pays all debt service as scheduled (i.e. no reschedulings) and receives new commitments only from IBRD and ADB. Table 3 presents these debt service obligations in more detail. Table 4 shows the effect on import levels of assuming a 30% limit on debt service payments (the austerity policy scenario). Table 5 presents the import levels that would result from the adjustment policy scenario. Table 6 compares the two scenarios and displays the sources of the higher import levels in the adjustment policy scenario. Tables 7 and 8 describe the changes in exposure of the various creditors that would result from the adjustment policy scenario. The detailed assumptions used to make these estimates are described below

2. Oil Exports. Oil price assumptions are from EPD as of the end of January. While the world oil price projections are much lower than previous forecasts, they are not as low for 1986 as current spot prices both because average selling prices are above spot prices at the moment and because markets may stabilize later in the year. Oil prices could be several dollars lower than in these projections, especially in the next few years. It is assumed that OPEC quantities will be higher in the future than they have been in recent years because the lower prices will stimulate demand and because non-OPEC supplies will be less forthcoming at these lower prices. In that environment, EPD assumes that Nigeria's share of OPEC production would decrease from 8.6% in 1985 to 8.1% (their official share) by 1988.

3. Nigeria's production increases from 1.50 m.b./day in 1986 to 1.71 in 1990 to 2.0 in 1995.

4. Nigeria's price (including a $1 premium above the world oil price) is $21 in 1986, $24 in 1990, and $40 in 1995.

5. We based our estimates of domestic consumption on our best data for 1985 (.25 m.b./day) followed by a decrease to .23 m.b./day in 1986 due primarily to the higher prices. This grows to .29 in 1990 and .35 in 1995. On that basis we calculated export quantities and therefore total oil export revenues. However, domestic oil consumption is endogenous in our macro model. To keep oil export revenues insulated from the macro runs, we decided to keep export quantities fixed and accommodate slight run-to-run variations in domestic consumption by varying total production accordingly. Therefore, quantity exported in our projections is 1.27 m.b./day in 1986, 1.42 in 1990, and 1.65 in 1995.

6. Non-Oil Exports. We have taken these numbers from the macro model. The estimate for 1986 is $356 million in both scenarios compared to $330 million in 1985 -- most of that growth is in cocoa. From 1987 onwards the growth in real terms for manufacturing exports is 0% through 1989 and -2% thereafter in the austerity policy scenario and 2% growing gradually to 12% in 1985 in the adjustment policy scenario. Other agricultural exports grow very little in either case. Cocoa increases from 180,000 tons to 220,000 tons in the adjustment policy scenario while actually decreasing from 1987 onwards in the austerity policy scenario. Gas exports of $100 million have been added in both cases from 1990 onwards. By 1990 the difference between the two cases in non-oil exports is $114 million. By 1995 the difference is $471 million ($272 million in 1985 dollars).

7. Export NFS are assumed to be 3% of total goods exports.

8. Import NFS. This is comprised of two major parts: freight, insurance, and other services which vary with imports and repatriated profits which depend mostly on oil exports. Based on historical figures, the relationship has been 10% of imports + 4% of oil exports. In order to try to capture the recent changes in profit retention rules for the oil industry, we have used 10% of imports + 5% of oil exports for our projections.

9. Other Balance of Payments Items. Travel is assumed to be included in the NFS imports. Direct foreign investment grows at zero per cent in real terms in 1986 in both scenarios and by zero per cent in nominal terms throughout the rest of the austerity policy scenario. In the adjustment policy scenario, the growth is zero per cent in real terms through 1987 and 2% in 1988, 3% in 1989, 4% in 1990, and 5% thereafter. Net transfers are constant in real terms in both cases.

10. MUV. The manufacturing unit value index (MUV) is used to deflate imports to a constant dollar value. The projections for the different countries are from EPD's latest estimates, but the weights used correspond to the shares of those countries in Nigeria's imports. The index that results grows by 6.7% in 1986, 6.0% in 1987 and 1988, 6.2% in 1989, 6.3% in 1990 and then falling gradually to 4.3% in 1995. The cumulative MUV to produce 1985 dollars values is 1.35 in 1990 and 1.73 in 1995.

11. MLT Debt. All figures on MLT debt are from EPD unless specified otherwise in these notes. Interest due, amortization due, and disbursements scheduled are provided for Paris Club, London Club, Multilateral Creditors, and other MLT for 1986-1995. EPD also provides end 1985 DOD. Our only change is to take out the World Bank and ADB figures from the MLT and replace them with our assumptions on disbursements for the different cases. This requires adjusting the interest and amortization due to the World Bank and ADB.

12. Arrears. The MLT figures already include $1.7 billion that represents the arrears that had been converted to MLT as of end 1985. From

the remaining claims we assume the following amounts will be recognized and paid off as indicated.

Amount	Date of Recognition	Retroactive interest to Jan. 1, 1984 paid	Principal Repayments Due	
			Austerity*	Adjustment
$ 1.8	Jan. 1, 1987	1987	1987-1990	1987-1996
$ .5	Jan. 1, 1988	1988	1988-1991	1988-1997
$ .5	Jan. 1, 1989	1989	1989-1992	1989-1998

The interest rate in both cases is 1% above LIBOR. The principal is to be repaid over 3½ years in the austerity policy scenario and 10 years in the adjustment policy scenario.

* Note that the arrears will not actually be paid off in this period in the austerity policy scenario because of the 30% limit on debt service.

13. Short-Term Debt. After lengthy discussions, EPD felt the stock as of end 1985 was $1-2 billion, IMF felt the number was not much over $750 million. We have settled on $1 billion, yielding interest payments of $100 million per year. There are no payments on principal and no increase in exposure (not even with inflation) in either case.

14. Private Debt. All figures on private debt are from EPD. The stock at end 1985 is about $1 billion. There are some disbursements in the first few years, but amortization payments scheduled exceed disbursements in all years. We treat private debt the same as public MLT insofar as de facto rescheduling is concerned. In the 30% case, only part of the principal payments are made, and debt service on private debt is included in the 30%. This means that public debt service is more like 29% of exports in the early years in the austerity policy scenario. In the adjustment policy scenario, all amortization to private creditors is paid on schedule.

15. De Facto Rescheduling. In the austerity policy scenario, we assume that total debt service (public MLT, private, short-term, and arrears) is limited to 30% of total exports of goods and services. Payments are made in the following order.

1. interest and principal to multilateral creditors.
2. all other interest (including interest on rolled-over principal).
3. all other principal including rolled over unpaid principal from previous years.

Total debt service payments equal 30% of exports provided the sum of debt service owed, including rolled-over interest and principal, equals or exceeds that amount. As a result, the rolled-over balance is eliminated in 1993 the first year debt service falls below 30%.

16. World Bank and ADB Loans. For the austerity policy scenario we have assumed that the Bank would continue to maintain a positive net transfer of resources to Nigeria; at a minimum, commitments are expected to be about $230 million in FY86, rising gradually over the ten years to reach $750 million in 1995. Should the medium-term framework improve over our austerity policy scenario without spectacular breakthrough on the policy front, we could conceive of a more rapid increase in lending. Under a best policies scenario, with significant movements on the exchange rate and on import liberalization, our project lending would increase over the years to $1.1 billion in 1995 plus a SAL and other quick disbursing loans averaging $500 million from 1987 to 1995. Total new commitments from the SAL and quick disbursing Bank loans would be $4.5 billion over the period. In all cases, we assume the African Development Bank will provide $200 million per year in new commitments beginning in 1987.

17. IMF Loans. We assume IMF loan disbursements to be 60% of quota in 1987-1990 followed by a fifth year disbursement equal to amortization due in 1991. The 60% is applied to the present quota and that amount ($510 million) is used without adjustments for inflation. Because of the first repayment coming due in 1990 the IMF exposure reaches a peak of 220% of quota (4 x 60 - 20) in 1990 and 1991 declining rapidly thereafter. All IMF loans are repaid by 1994.

18. Official Rescheduling. In 1986 we assume the 30% limit would apply exactly as in the austerity policy scenario. The unpaid principal which is rolled over to 1987 becomes eligible for Paris and London Club rescheduling.

19. For both the Paris Club and London Club, we reschedule 100% of the principal due 1987-1992. Paris Club interest is not rescheduled. This would not actually be in the form of a six-year agreement. We assume it would be in the form of a two-year agreement or even two one-year agreements followed by a four-year agreement. The difference is important in practical terms because of the closer monitoring and the ability of the creditors to cancel the agreement if progress is not satisfactory. For estimating the effects assuming progress is satisfactory, however, the multiple agreements are equivalent to a single six-year agreement. Repayment of the rescheduled amounts does not begin until 1993. All rescheduled amounts are repaid by 1997 in five even installments.

20. In the adjustment policy scenario, we assume the arrears will be repaid over ten years rather than the 3½ years that have been the terms agreed to in the past. We assume no rescheduling of private debt or other MLT (mostly COMECON countries) except that the unpaid principal arising from the 30% limit in 1986 is all assumed to be rescheduled in 1987.

21. New Commercial Money. In the adjustment policy scenario, we add additional borrowing to all of the other assumptions in order to reach a particular path of imports considered to be consistent with the macro-economic estimates for that scenario. New money is assumed to come from London Club banks, Paris Club creditors, and others. The terms are

three-years grace and then four years to repay. The total disbursements over the period for this new money is $5.8 billion.

22. Reserves. Foreign exchange reserve assets are estimated at about $1.1 billion at the end of 1985, about 1.6 months of imports of goods in that year. In both cases, we assume that this percentage is increased to two months of imports of goods. In the adjustment policy scenario, we assume this happens in 1987. In the austerity policy scenario, we assume this is done gradually over the period 1987-1989. Thus reserve assets in nominal terms increase from $1.1 billion at the end of 1985 to $1.3 billion in 1980 and $3.1 billion in 1995 in the austerity policy scenario and $1.7 and 2.7 billion in the adjustment policy scenario.

TABLE 1

Debt Outstanding and Disbursed
($ Million as of 12/31/1985)

Public 1/ Medium and Long-Term	13,225	
Paris Club Creditors		(4,733)
London Club Creditors		(4,516)
Multilateral Institutions		(1,339)
Other 2/		(2,637)
Short-Term	1,000	
Private	1,081	
Total Debt Outstanding	15,306	
Trade Credit Arrears (not yet recognized)	2,800	
Total debt including unrecognized arrears	18,106	

1/ Includes public and publicly guaranteed debt.

2/ Primarily bilateral loans from COMECON countries and trade credit arrears already recognized and issued.

TABLE 2

Nigeria External Balance
(Debt Paid as Scheduled, i.e. No Action Taken)

- No rescheduling
- No new loans (except minimal World Bank and ADB)
- (Millions of current US$)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Oil Export Revenues	11,150	9,735	10,578	10,775	11,081	12,439	13,666	15,270	17,765	21,207	24,090
Other Exports & NFS	674	659	723	770	800	846	912	975	1,062	1,177	1,277
Total Export Revenues	11,824	10,393	11,301	11,545	11,881	13,285	14,577	16,245	18,827	22,383	25,367
+ Disbursements	2,636	1,924	1,382	1,069	650	528	464	505	557	605	659
- Interest Due	1,502	1,440	1,862	1,316	1,122	672	545	485	453	445	457
- Amortization Due	3,547	3,891	3,780	3,813	3,438	2,273	1,332	1,002	761	571	468
+ Other Balance of Payments Items	-165	108	334	-54	-43	-58	-420	-272	-315	-393	-500
Imports Goods & Services	9,246	7,095	7,375	7,431	7,928	10,811	12,745	14,991	17,855	21,579	24,601
Imports Goods	8,000	5,963	6,175	6,216	6,653	9,206	10,903	12,865	15,394	18,557	21,160
Imports Goods (1985 dollars)	8,000	5,689	5,460	5,185	5,226	6,802	7,614	8,524	9,682	11,195	12,239
Debt Service/Exports	43%	51%	50%	44%	38%	22%	13%	9%	6%	5%	4%
Total Debt Outstanding & Disbursed at years end	18,106	16,139	13,741	10,996	8,209	6,464	5,597	5,100	4,896	4,930	5,122

TABLE 3

Nigeria's Debt Service Obligations

- No rescheduling
- Arrears = $4.5 billion
- (Current US$ millions)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Interest											
Public	1407	1263	1081	903	713	571	505	472	449	442	455
Paris Club	331	390	361	301	230	169	120	80	48	25	11
London Club	508	416	318	223	134	68	34	19	8	1	1
Multilateral 1/	105	123	141	155	167	179	193	206	221	237	256
Short-term	100	100	100	100	100	100	100	100	100	100	100
Other	363	234	161	124	82	55	58	67	72	79	87
Private	95	89	74	56	40	26	14	7	4	3	2
Arrears	0	88	707	357	369	75	26	6	0	0	0
Total 2/	1502	1440	1862	1316	1122	672	545	485	453	445	457
Amortization											
Public	3302	3603	3242	3012	2551	1332	970	816	747	559	457
Paris Club	743	1056	1181	1123	961	649	508	397	309	202	88
London Club	1400	1510	1369	1155	859	407	181	116	103	3	2
Multilateral	54	82	112	149	158	175	191	213	240	269	296
Other	1105	955	580	585	573	101	90	90	95	85	71
Private	245	288	281	216	158	140	76	43	14	12	11
Arrears	0	0	257	586	729	800	286	143	0	0	0
Total	3547	3891	3780	3814	3438	2272	1332	1002	761	571	468
Total Debt Service As % of Exports											
Disbursements											
Public	3577	1795	1307	1036	636	528	464	505	557	605	659
Paris Club	1174	849	486	301	206	84	2	0	0	0	0
London Club	560	498	356	321	17	2	0	0	0	0	0
Multilateral	276	285	287	270	280	314	325	359	397	435	486
Other	267	163	178	144	133	128	137	146	160	170	173
Private	359	129	75	33	14	0	0	0	0	0	0
Total	2636	1924	1382	1069	650	528	464	505	557	605	659
Net Flows											
Public	-1132	-3071	-3016	-2879	-2628	-1375	-1011	-783	-639	-396	-253
Paris Club	100	-579	-1056	-1123	-985	-734	-626	-477	-357	-227	-99
London Club	-1348	-1428	-1331	-1057	-976	-473	-215	-135	-111	-4	-3
Multilateral	117	80	34	-34	-45	-40	-59	-60	-65	-71	-66
Short-term	-100	-100	-100	-100	-100	-100	-100	-100	-100	-100	-100
Other	-1201	-1026	-563	-565	-522	-28	-11	-11	-7	-6	15
Private	19	-248	-280	-239	-184	-166	-90	-50	-18	-15	-13
Arrears	0	-88	-964	-943	-1098	-875	-312	-149	0	0	0
Total	-2413	-3407	-4260	-4061	-3910	-2416	-1413	-982	-657	-411	-266
Total Net Flows/GNP											

1/ Includes only IBRD for this draft.

2/ Total consists of Public, Private and Arrears.

TABLE 4

Nigeria's External Balance
(Austerity Policy Scenario)

- Billions of current US$.
- Limit on debt service equals 30% of exports.
- No new loans (except ADB and World Bank).

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Exports Goods and Services	11.8	10.4	11.3	11.5	11.9	13.3	14.6	16.2	18.8	22.4	25.4
+ Disbursements	2.6	1.9	1.4	1.1	.7	.5	.5	.5	.6	.6	.7
- Interest Paid	1.5	1.6	2.3	2.0	2.0	1.6	1.3	1.1	.7	.5	.5
- Amortization Paid	3.5	1.5	1.1	1.5	1.5	2.4	3.0	3.8	5.0	1.0	.5
+ Other Balance of Payments Items	-.2	.1	.1	0	0	.1	-.1	-.1	-.2	-.3	-1.1
= Imports Goods & Services	9.2	9.3	9.4	9.1	9.0	9.9	10.5	11.8	13.5	21.3	24.0
Imports Goods	8.0	8.0	8.0	7.8	7.6	8.4	8.9	9.9	11.4	18.3	20.6
Imports Goods (1985 dollars)	8.0	7.5	7.1	6.5	6.0	6.2	6.2	6.6	7.2	11.0	11.9
Memo Items											
Percent of Interest Paid	100	100	100	100	100	100	100	100	100	100	100
Percent of Principal to Preferred Creditors Paid	100	100	100	100	100	100	100	100	100	100	100
Percent of Other Principal Paid 1/	100	40	30	39	44	100	100	100	100	100	100
Cumulative Unpaid Principal	0	2.3	5.0	7.3	9.3	9.1	7.4	4.6	.4	0	0
Debt Service/Exports	43%	30%	30%	30%	30%	30%	30%	30%	30%	6%	4%
Total Debt Outstanding and Disbursed 2/	18.1	18.5	18.7	18.3	17.5	15.6	13.0	9.7	5.3	4.9	5.1

1/ Does not include rolled-over principal from previous years.
2/ Includes trade arrears not yet recognized.

TABLE 5

Nigeria's External Balance
(Adjustment Policy Scenario)

- (Billions of current US$)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Total Export Revenues	11.8	10.4	11.3	11.6	11.9	13.4	14.7	16.5	19.1	22.8	25.8
+ Disbursements	2.6	1.9	2.2	2.3	3.0	2.0	2.0	2.4	2.8	1.7	1.4
- Interest	1.5	1.6	2.3	2.1	2.3	2.0	2.0	2.0	2.0	1.8	1.5
- Amortization	3.5	1.6	1.2	1.2	1.2	.9	1.1	1.7	3.6	3.9	4.1
- Other Balance of Payments Items	-.2	.1	-.1	.1	.1	.1	.1	.1	.1	.2	0
Imports Goods and Services	9.2	9.3	10.0	10.7	11.5	12.5	13.7	15.2	16.3	19.0	21.7
Imports Goods	8.0	8.0	8.5	9.2	9.9	10.7	11.7	13.1	14.0	16.2	18.5
Imports Goods (1985 dollars)	8.0	7.5	7.5	7.7	7.8	7.9	8.2	8.7	8.8	9.8	10.7
Debt Service/Exports	43%	30%	31%	28%	29%	22%	21%	22%	29%	25%	22%
Total Debt Outstanding + Disbursed*	18.1	18.5	19.5	20.7	22.6	23.6	24.5	25.3	24.4	22.3	19.6

* Includes trade arrears not yet recognized.

TABLE 6

Comparing Scenarios

- Billions of 1985 US$.

	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
COMPARING CASES (Imports of Goods)										
No Action	5.6	5.5	5.2	5.2	6.8	7.6	8.5	9.7	11.2	12.2
Austerity Policy Scenario	7.5	7.1	6.5	6.0	6.2	6.2	6.6	7.2	11.0	11.9
Adjustment Policy Scenario	7.5	7.5	7.7	7.8	7.9	8.2	8.7	8.8	9.8	10.7
NET RELIEF										
De Facto Rescheduling	1.9	1.4	1.3	.7	-.7	-1.6	-2.1	-2.4	-.2	0
Official Rescheduling 1/		1.7	1.4	.9	.4	-.2	-.4	-1.5	-1.5	-1.5
IMF Loans		.4	.3	.3	.1	-.1	-.4	-.3	-.3	-.2
Higher IBRD Loans		.1	.3	.3	.3	.3	.3	.2	.1	.1
Other New Loans		.1	.3	.8	0	.1	.3	.3	-.3	-.6
Higher Non-Oil Exports					.1	.1	.1	.2	.2	.2
Other Items 2/		-.3	.2	.2	.1	.4	.2	.2	.4	.4
Total Net Relief Adjustment Policy Scenario	1.9	2.0	2.5	2.6	1.1	.6	.2	-.9	-1.4	-1.5

1/ Includes longer repayment period for trade arrears.

2/ Includes differences in reserves, foreign investment, transfers, and travel.

TABLE 7

Composition of Exposure
(Adjustment Policy Scenario)

- (Billions of US$)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
World Bank	1.3	1.5	1.8	2.3	3.0	3.8	4.6	5.4	6.2	6.9	7.7
IMF	0	0	.5	1.0	1.5	1.9	1.9	1.4	.9	.4	.1
Arrears *	2.8	2.8	2.6	2.4	2.1	1.8	1.6	1.3	1.0	.7	.4
Paris Club	4.7	5.5	6.0	6.3	6.5	6.5	6.5	6.5	5.6	4.5	3.5
London Club	4.5	4.9	5.3	5.6	5.6	5.6	5.6	5.6	4.7	3.8	2.7
Other (includes some multilaterals)	2.7	1.9	1.5	1.0	.6	.6	.7	.7	.8	.9	1.0
Other New Loans	0	0	.2	.6	1.9	2.2	2.5	3.2	4.2	4.0	3.1
Short-Term and Private	2.1	1.9	1.7	1.5	1.4	1.2	1.2	1.1	1.1	1.1	1.1
Total	18.1	18.5	19.5	20.7	22.6	23.6	24.5	25.3	24.4	22.3	19.6

* Includes arrears not yet recognized.

TABLE 8

Year to Year Growth in Exposure
(Adjustment Policy Scenario)

- (% change in current US$)

	85-86	86-87	87-88	88-89	89-90	90-91	91-92	92-93	93-94
London Club only	9	7	6	0	0	0	0	-16	-20
Paris Club only	16	9	5	3	1	0	0	-15	-19
London Club + Other	9	11	13	21	3	5	9	1	-13
London Club + Paris Club	12	8	6	2	1	0	0	-15	-19
London Club + Paris Club + Other New Loans	12	10	9	12	2	2	5	-6	-15

Average Growth Rates

London Club + Other New Loans	1985-1989	=	14% per year
	1985-1992	=	10% per year
London Club + Paris Club and Other New Loans	1985-1988	=	11% per year
	1986-1989	=	10% per year

Annex F

NIGERIA: Assumptions and Results of Macro-Economic Assessments

Principal Policy Assumptions

1. In order to illustrate economic consequences of different policy options open to the Government, economic performance under two illustrative scenarios -- one labelled the "Austerity Policy Scenario" and the other labelled "Adjustment Policy Scenario" -- which differ as far as policies pursued are outlined below. 1/ Both scenarios assumes an initial period of economic reform momentum -- characterized by some reforms to address Nigeria's structural adjustment problems -- for somewhat more than a year following the steps announced in the 1986 budget. Thus, developments in 1986 is projected to be the same in the two scenarios. After this period policies and economic performance will start to diverge.

- The "Austerity Policy Scenario" assumes that political and economic pressures on government which led to poor policies over the past decade will reassert their influence after this initial period; as a result, Nigeria will again begin to pursue basically inward oriented policies, relying mainly on austerity measures and administrative controls in its attempts to achieve external and internal economic balance. The real exchange rate is assumed to continue on its appreciating trend under this scenario. Another main characteristic of this scenario is a unilaterally set debt service target by the Nigerians ("cold rescheduling").

- The "Adjustment Policy Scenario" in contrast, assumes that the Government continues to build on the initiatives already taken in the 1986 budget and embraces a medium-term adjustment program along the lines outlined in Section II.

2. World Price Parameters. These assumptions are taken from EPD. When there is an interval with no explicit EPD projections data available (as between 1990 and 1995) prices are assumed to change at a constant rate (given by a compound growth formula). The only variable for which an exact equivalent to the EPD projections does not exist is aggregate MUV. EPD's MUV is the weighted average for five countries (United States, Britain, France, Germany and Japan) with these countries' shares in world trade as

---

1/ An extended version of the World Bank's standard RMSM model, adjusted to the specific characteristics of the Nigerian economy, has been used in these scenarios. The scenarios are to be interpreted neither as forecasts for most probably development nor as plans for the most desirable. The ambition is limited to an attempt to present consistent analyses of the consequences of different assumptions about the future. The results are perhaps best described as conditional forecasts, the fundamental condition lying in the structure of the model and the assumptions about economic strategies followed by the authorities.

weights. The aggregate MUV used here is also a weighted average of the same countries' MUVs but instead using Nigeria's import structure as the weighting system. This results in slightly different aggregate MUV.

3. Exchange Rates, Domestic Prices and Money Supply. In the Austerity Policy Scenario concerns over impacts on prices and standards of living (for mainly the urban population) are assumed to constrain the Government to offset (through devaluations of the nominal exchange rate) only half of the impact on the real exchange rate 1/ of differences between domestic and international inflation; thus gradually deteriorating policies after 1986 are assumed to result in a continued gradual real appreciation of the exchange rate. The Adjustment Policy Scenario, in contrast, assumes a fast adjustment of the real exchange rate to levels that again makes non-oil tradeables internationally competitive; the real exchange rates is assumed to go down to an "equilibrium value" of ₦0.3 = $1 in 1989 (as against ₦1 = $1 in 1985) through adjustments in the nominal exchange rate. A flexible policy is assumed to be pursued thereafter in order to keep the real exchange rate at this level. Thus, while the Austerity Policy Scenario treats the exchange rate as endogenous, it is a policy parameter in the Adjustment Policy Scenario. The introduction of a second-tier foreign exchange market together with an increase in export retention to 25 percent for non-oil exports in 1986 is estimated to correspond to a 10 percent real devaluation.

4. The domestic prices level (inflation) is given endogenously in the model through a specific equation which "explains" prices as a function of some constant level of inflationary expectation (10 percent throughout the projection period in the Austerity Policy Scenario; 7.5 percent from 1990 onwards in the Adjustment Policy Scenario), previous year's inflation, import availability, and nominal exchange rate. The Austerity Policy Scenario assumes that no adjustments in (nominal) energy prices are made in addition to those announced in the 1986 budget; thus in real terms, energy prices would decline with inflation in this case. The Adjustment Policy Scenario assumes that domestic energy prices are maintained at above world levels (as the exchange rate is adjusted). Money supply in the model is a function of the current account balance, government deficit plus an exogenous "growth parameter" of 15 percent which is progressively lowered to 10 percent by 1991 in the Adjustment Policy Scenario as a proxy for monetary restraint.

5. Production. The model identifies five sectors in the production block of the economy: agriculture, industry, oil, construction and services.Most of the agricultural subsectors are assumed to be relatively insensitive to foreign exchange constraints, the impact of the latter being felt mainly via impacts of lack of fertilizers, pesticides, etc., on output. Given this, and since initial food shortages and the resort to QRs in a Austerity Policy Scenario is assumed to result in high prices, growth

---

1/ The real exchange rate in the model is defined as the change in nominal exchange rate adjusted for the difference between domestic (CPI) and international inflation (MUV).

performance for food crops (including livestock) is not assumed to be too different in the two scenarios. Of course, incentives do matter; a policy case is therefore assumed to result in higher growth for this subsector than the erratic incentives created by political lobbyism and QRs. The better incentives in the Adjustment Policy Scenario are assumed to result in successively higher growth rates towards the end of the decade. Growth rates for agriculture in the Austerity Policy Scenario are assumed to peak at 2.3 percent annually in the late 1980s/early 1990s and decline to 2.0 percent by 1995. The Adjustment Policy Scenario assumes agricultural growth will accelerate to a peak of 4.5 percent in 1989 in response to improved policies and settle down at its steady state growth rate of 3.8 percent in the early 1990s. (Thus, the growth rate for agriculture are exogenous in the models.)

6. Given its very high import dependence, industrial growth in the short term is essentially dependent on the availability of imported raw material inputs. Because of the presently very low capacity utilization, about 25-35 percent, supply factors are not assumed to be a significant constraint; a doubling of capacity over 9 years (1987-95) would therefore be possible and consistent with very low ICORs. The elasticity of industrial production with respect to raw material availability is assumed to be one at the present. In the Adjustment Policy Scenario some supply response and more efficient use of imports are projected to result in successively higher elasticities (of 1.3) in the 1990s. Not all industrial growth, however, is projected to come from better capacity utilization: gross capital formation, does allow for some new capacity creation (as well as repair and maintenance expenditure). The Austerity Policy Scenario assumes that the starting elasticity of one will remain throughout the period. 1/

7. Oil production is used for domestic consumption and exports. Assumptions for total production has been agreed upon with EPD and is, therefore, exogenous. It is assumed that due to short-term demand in elasticity domestic oil consumption never declines. Whenever non-oil GDP increases, the domestic consumption grows with an elasticity of .3 in the Adjustment Policy Scenario and .6 in the Austerity Policy Scenario. The reason for these differences is that this single elasticity is a proxy for both income and price impacts. Since a relatively high elasticity is offset by a relatively low growth rate in the Austerity Policy Scenario while a rather low elasticity is combined with high growth in the Adjustment Policy Scenario, domestic oil consumption and oil exports is roughly the same in the two scenarios.

1/ The growth performance for industry is rather different in the two scenarios due to: (i) relatively better availability of foreign exchange in the Adjustment Policy Scenario (maybe the most important element in the early part of the projection period in the Adjustment Policy Scenario; the Austerity Policy Scenario performance will be determined mainly by this factor over the whole projection period) and (ii) positive incentives in the Adjustment Policy Scenario.

8. Construction output is determined by investment via an elasticity (same in the two scenarios).

9. The services sector is split in two parts as regards the way output is determined: (i) government service output (linked to public consumption in the public finance block); (ii) "private" services (including public parastatals) linked to changes in non-oil GDP (based on regression estimates) with some ad hoc adjustments to reflect differences in policy environment. Growth is projected to be fairly low for the next two years before picking up to 3 percent in the Austerity Policy Scenario and 3.5 percent in the Adjustment Policy Scenario. The idea is that in the long run this sector will probably have to keep up with demand (population) growth.

10. Oil exports (about 95 percent of total) are assumed to be the same in the Austerity Policy Scenario and the Adjustment Policy Scenario. The principal component of non-oil exports is cocoa. In the policy case, cocoa export is assumed to grow from 125 thousand tons in 1986 to 180 thousand tons in 1990. This growth should continue, but at a lower pace in the 1990s with exports at 220 thousand tons by 1995. As a result of recent policy announcements of increased export earnings retention, cocoa exports have preliminary been assumed to initially increase also in the Austerity Policy Scenario, reaching 150 thousand tons in 1988-90 before going back to about 120 thousand tons in 1995 because of the deteriorating economic environment. Raw materials and manufactures account for only minor shares of export revenues. Both subsectors are assumed to grow at fairly high rates, averaging 7 percent per year during the projection period, in the Adsjustment Policy Scenario. These exports do not change between 1984 and 1990 in the Austerity Policy Scenario; in the 1990s, these exports are assumed to decline due to declining policy environment.

11. Total imports in the Austerity Policy Scenario are derived from what remains after meeting the 30 percent target for debt service payment, given total export revenue. The Austerity Policy Scenario assumes that capital good imports will continue to be favored and that the nature of investment will be typified by capital and import-intensive projects with often very low (or negative) rates of return. Food and consumer goods imports are assumed to grow by an average of 6 and 7 percent respectively. This behavior will, given the very depressed levels of total imports under this strategy, leave intermediate goods imports too low to allow for any industrial growth.

12. In the Adjustment Policy Scenario, import composition reflects investment and raw material needs compatible with sufficient industrial growth. Food and consumer goods imports are assumed to increase by 50 and 30 percent, respectively, in 1987 to offset inflationary impacts of exchange rate adjustments and to grow only slowly thereafter. Total imports will, however, be constrained not only by the balance of payment constraints but also by the need to build up reserves for the difficult years 1989-93. Capital goods imports are determined by the amount of gross fixed capital formation. The import content of investment is assumed to be 60 percent. Raw material imports, finally, are adjusted to achieve the needed industrial growth rates.

13. Gross investment is composed of changes in stocks, federal, state, and private investment, respectively. Changes in stock and private investment are endogenous and a function of level of economic activity. State investment (about 8 percent of the total) goes up by an exogenous growth rate. Federal investment in the Adjustment Policy Scenario is broadly in conformity with the Public Expenditure Program Review report and averages 2800 million naira during the rest of the 1980s, increasing significantly during the 1990s. The numbers in the Austerity Policy Scenario are not widely different, except that the less favorable economic environment results in lower private investment and higher (inefficient) public investment.

14. The 1986 federal budget implies a deficit/GDP ratio of 2.0 in 1986. The Austerity Policy Scenario assumes that this ratio will increase again towards 1990 (to fall somewhat thereafter as higher oil prices and lower debt service will again permit return to high spending while at the same time keeping budget deficits within reasonable limits). The Adjustment Policy Scenario in contrast, assumes gradual reduction of federal budget deficit towards the end of the decade, staying at low levels through the first part of the 1990s, reflecting continued fiscal discipline.

Table A: Key Variables

(%, Constant 1984 Naira unless shown)

	1984	1985	1986	1987-91 (Average)	1991	1992-95 (Average)	1995
PRODUCTION INDICATORS :							
GDP Growth Rate		1.1	0.0	3.4	3.5	4.2	3.6
-Oil Production Growth		7.0	0.7	3.2	2.3	3.4	0.0
-Non-Oil GDP Growth		-0.3	-0.1	3.5	3.8	4.4	4.6
Agriculture		3.5	2.5	3.9	3.8	3.8	3.8
Industry		-22.1	-9.7	6.9	5.5	8.3	10.0
GDP per Capita (Constant $)	796.4	780.2	754.7	751.8	759.2	776.6	785.5
GNP Growth Rate		1.3	0.0	3.5	3.6	4.2	3.7
GNP per Capita (Constant $)		766.6	741.6	739.9	748.0	766.3	775.7
DEBT INDICATORS (ALL IN CURRENT PRICES) :							
Total DOD ($ Billion)	13.7	18.1	18.5	22.2	24.5	22.9	19.6
Debt/Exports	111.0	140.4	178.1	177.2	166.7	114.1	76.1
Debt/GDP	18.5	24.7	27.9	53.8	56.5	41.3	29.5
Interest/GDP	1.4	2.0	2.4	5.2	4.6	3.3	2.3
Debt Service/Exports							
-Including Rescheduled	24.8	39.2	30.0	44.6	26.1	25.5	21.8
-Excluding Rescheduled	24.8	39.2	29.1	25.5	19.4	22.7	20.6
Interest/Exports	8.7	11.7	15.1	17.4	13.7	9.2	6.0
INVESTMENT, SAVINGS, AND CONSUMPTION INDICATORS :							
Investment/GDP	12.9	13.4	12.5	11.3	11.9	13.9	15.1
-Public Investment/GDP	9.9	10.6	9.8	7.8	7.6	8.6	9.0
-Private Investment/GDP	3.0	2.8	2.7	3.6	4.3	5.4	6.1
Savings/GDP	15.3	18.3	14.2	12.2	12.7	15.8	17.5
Private/Public Investment	30.7	26.8	27.7	46.6	56.2	62.5	68.1
Consumption/Capita Growth		-6.5	-4.3	0.3	-0.2	0.3	0.9
TRADE INDICATORS :							
Exports Growth Rate		10.3	3.8	2.7	1.6	3.7	-0.2
-Non-Oil Export growth		-24.6	35.4	7.9	4.6	4.9	5.2
Exports/GDP (Current)		17.6	15.7	30.3	33.9	36.7	38.8
Exports/GDP (Constant)		21.1	21.9	21.2	21.2	21.1	20.7
-Non-Oil Exports/Exports		2.1	3.4	4.1	4.3	4.1	3.9
Imports Growth Rate		-12.2	-9.3	2.5	3.7	7.0	9.4
Imports/GDP (Current)		12.5	13.6	28.2	31.3	31.4	32.2
Imports/GDP (Constant)		14.4	13.0	12.9	12.4	12.9	13.8
OTHER INDICATORS :							
Ex-post ICORs							
-GDP (non oil)				3.5	3.6	3.7	3.9
-Agriculture				2.7	2.7	2.7	2.7
-Industry				2.9	3.5	4.3	5.0
-Services				4.1	4.0	3.8	3.8
Ex-Post Import Elasticity (w.r.t. non-oil GDP)				0.9	1.0	1.7	2.6

Note: Inconsistencies may exist between current a constant ratios as a result of exchange rate adjustments.

02-Mar-86 WAINI, Austerity Policy Case Run for Loan Committee Paper, Scenario: 30% debt service cap.

Table A: Key Variables

(%, Constant 1984 Naira unless shown)

	1984	1985	1986	1987-91 (Average)	1991	1992-95 (Average)	1995
PRODUCTION INDICATORS :							
GDP Growth Rate		1.1	0.0	1.5	1.9	3.1	2.5
-Oil Production Growth		7.0	0.7	3.2	2.3	3.4	0.0
-Non-Oil GDP Growth		-0.3	-0.1	1.0	1.8	3.1	3.2
Agriculture		3.5	2.5	2.3	2.3	2.1	2.0
Industry		-22.1	-9.7	-9.0	-9.0	9.1	10.0
GDP per Capita (Constant $)	796.4	780.2	754.7	717.2	698.4	692.5	693.7
GNP Growth Rate		1.3	0.0	1.5	2.0	3.2	2.5
GNP per Capita (Constant $)		766.6	741.6	705.3	687.3	682.2	683.9
DEBT INDICATORS (ALL IN CURRENT PRICES) :							
Total DOD ($ Billion)	13.7	18.1	18.5	16.6	13.0	6.5	5.1
Debt/Exports	111.0	140.4	178.1	135.9	89.4	33.7	20.2
Debt/GDP	18.5	24.7	27.9	20.1	9.6	2.2	0.6
Interest/GDP	1.4	2.0	2.4	2.2	1.0	0.2	0.1
Debt Service/Exports	24.8	39.2	30.0	29.7	30.0	17.5	3.7
Interest/Exports	8.7	11.7	15.1	14.8	8.8	3.4	1.8
STMENT, SAVINGS, AND CONSUMPTION INDICATORS :							
Investment/GDP	12.9	13.4	12.5	11.2	11.3	12.4	13.0
-Public Investment/GDP	9.9	10.6	9.8	9.0	9.3	10.3	10.9
-Private Investment/GDP	3.0	2.8	2.7	2.3	2.0	2.1	2.1
Savings/GDP	15.3	18.3	14.2	14.2	14.8	14.8	13.7
Private/Public Investment	30.7	26.8	27.7	25.3	22.0	20.1	19.8
Consumption/Capita Growth		-6.5	-4.3	-2.4	-1.5	1.3	1.5
TRADE INDICATORS :							
Exports Growth Rate		10.3	3.8	2.6	1.3	3.3	-0.7
-Non-Oil Export growth		-24.6	35.4	2.4	-3.5	-3.7	-3.7
Exports/GDP (Current)		17.6	15.7	14.3	10.8	5.6	2.9
Exports/GDP (Constant)		21.1	21.9	21.8	22.4	22.9	22.5
-Non-Oil Exports/Exports		2.1	3.4	3.6	3.3	2.6	2.1
Imports Growth Rate		-12.2	-9.3	-3.3	-0.3	19.5	15.1
Imports/GDP (Current)		12.5	13.6	11.1	7.8	4.4	2.8
Imports/GDP (Constant)		14.4	13.0	11.0	10.3	13.9	17.9
OTHER INDICATORS :							
Ex-post ICORs							
-GDP (non oil)				16.3	7.1	5.2	4.5
-Agriculture							
-Industry							
-Services							
Ex-Post Import Elasticity (w.r.t. non-oil GDP)				Negative	-0.2	5.4	6.0

Note: Inconsistencies may exist between current and constant ratios as a result of exchange rate adjustments.

→ Nigeria BR.

FORM NO. 75
(6-83)

THE WORLD BANK/IFC

ROUTING SLIP	DATE: 2/10/86
NAME	ROOM NO.
Messrs. Alisbah, Obrien, Isenman	
Eccles, Humphrey, T. Husain,	
Choksi, Obidegwu, Rischard,	
Rajapatirana, Swayze, Tallroth	

	APPROPRIATE DISPOSITION		NOTE AND RETURN
	APPROVAL		NOTE AND SEND ON
	CLEARANCE		PER OUR CONVERSATION
	COMMENT		PER YOUR REQUEST
	FOR ACTION		PREPARE REPLY
	INFORMATION		RECOMMENDATION
	INITIAL		SIGNATURE
	NOTE AND FILE		URGENT

REMARKS:

Enclosed is working Paper No. 2. Grateful for your comments as soon as possible.

FROM:	ROOM NO.:	EXTENSION:
T. Allen	E327	78056

VD gave this to Myers to make comments

Draft
TAllen:pm
Job: Baker Report
Disk: ALLEN
February 5, 1986

NIGERIA: BAKER INITIATIVE COUNTRY REPORT

Working Paper No. II

Adjustment Policy Package

1. To achieve the objectives set for the medium term adjustment program, it is necessary for the Government to supplement its demand management measures 1/ with structural adjustment policies aimed at increasing the efficiency of investment, improving domestic savings and stimulating desirable tradeable good production, particularly of non-oil exports. The highly uncertain and tight financial situation will require the Government to reduce its heavy reliance on public expenditures as the propulsive force of development and to make more use of macro-economic and sectoral policies that will inter alia stimulate efficient and increased private investment and production. The Government should build on the budget initiative already taken, with the further reforms focussing principally on: (i) correcting the still grossly misaligned prices through reforms in the exchange rate, trade and incentive policies; (ii) overcoming the considerable public sector inefficiencies through restructured public expenditures and continued rationalization of the parastatal sector; (iii) reducing the severe imperfections in the financial system through less Government intervention in the operations of the financial markets and improved financial intermediation; and (iv) removing the sectoral supply constraints which discourage private initiative and inhibit responses to favorable market conditions. The essential elements of the package of outlined below, noting that it assumes that an arrangement is consummated between the IMF and the Government which is acceptable to all the parties involved. Annex A summarizes recent policy actions of the Government and the timing of further actions over the adjustment period, while Annex B

1/ There are no further demand management measures proposals apart from those also regarded as structural (e.g. interest rate policy) and debt management (the subject of a separate working paper). It is expected that as part of the Adjustment Policy Package, the Government would continue to place tight constraints on the budget deficit with the aim of eliminating it completely by the end of the adjustment program period. While improved revenue measures should continue to be pursued - especially at the state Government level through appropriate cost recovery mechanisms - this should not be seen as a substitute for a slimmer bureaucracy and a reduced government presence in productive activity.

summarizes the actions which would take place in the first year of the adjustment program.

Exchange Rate, Trade and Incentive Policies

2. The thrust of the policy reforms in this area should be towards a market determined exchange rate and the dismantling of trade controls. Provided the underlying trade taxes and incentives are structured correctly, the principal impediments to efficient resource allocation - and to non-oil exports and the utilization of local raw materials - will be removed and the inducements to engaged in parallel black market activities minimized.

3. It is most unlikely that the Government would agree to an immediate devaluation of the Naira of a magnitude sufficient to reflect the true scarcity value of foreign exchange. It is also unlikely the Government would agree to the immediate and complete liberalization of import controls. The concern is that the lifting of all import restrictions would cause pent up and speculative demands to place considerable pressures on the still limited amount of foreign exchange and although this would force further reductions in the value of the Naira, it runs the danger of essential good losing out in the process. While the injection of additional foreign exchange resources would serve to relieve this pressure, it is extremely doubtful that sufficient resources would be forthcoming in a short enough period of time (on terms acceptable to the Government) to avoid a political backlash associated with shortages of essential goods which could do irreparable harm to the adjustment program.

4. While the removal of controls on imports would thus have to be phased (preferably over at most a three year period) the dismantling of controls on prices and marketing could be achieved within a relatively short period of time. Immediate action can also be taken to ensure that the system of foreign and internal trade taxes (including fiscal export and investment incentives) provide the desired medium to longer term signals to producers and consumers. Although their effect on resource allocation will be minimal while the import controls are still in force, they will at least be in place by the time the controls are removed. The early reforms in this area will provide a clear indication to the private sector as to the future parameters they will face, allowing them to plan ahead with some certainty. Those basic reforms should be clearly distinguished from transitory trade tax and other measures used to compensate - at least partially - for the unfavorable effects of the distortions caused by the continued use of import controls and the corresponding overvalued Naira.

5. Exchange Rate. A process has to be set in motion through which the phased dismantling of trade controls and other reforms affecting foreign exchange demands and supplies would allow the exchange rate to move towards a realistic level with minimum disruptive effects. An initial large and discrete devaluation should take place, and a more flexible exchange rate policy adopted. [As an interim measure during the period in which trade controls are being dismantled, the Government could review the formula it is presently using to make crawling adjustments to the exchange rate to ensure its allows regular (monthly) adjustments based on a formula reflecting domestic-international inflation differentials and a

margin for further changes in the real rate (with further discrete adjustments being made to coincide with the phasing of liberalization of import controls). The margin could start, say, at three to four percent and be gradually stepped up as the import and other controls are relaxed. In parallel, the scope of the newly established second-tier foreign exchange market to be operated by the commercial banks (in which the value of the Naira is market determined) could be expanded through the Government allocating an increasing share of oil export proceeds to the market (at least 5 percent in the first year of the adjustment program), supplementing the limited amounts sourced from the foreign currency domicialiary accounts system (the values established in the market should also be used to guide the extent of discrete and regular adjustments to the exchange rate). However, the second-tier market should be integrated into the 'formal' market as soon as possible, at the latest by the time the trade and incentive reforms are fully in place (at the end of the third year of the program) with the Naira then being allowed to find its own level.] 2/

6. Export Controls and Taxes. There are no taxes of significance on non-oil exports and this situation should be maintained. The Government has recently abolished the list of prohibited exports (expect for a limited number of goods whose importation has been banned) and simplified export licensing requirements for the 36 affected products (procedures now limited principally to the collection of necessary statistical information). The export monopoly power of the six commodity boards (rubber, cocoa, palm produce, cotton, groundnuts and grains) was also abolished, with the private sector being allowed to market externally these products.

7. Import Controls and Taxes. The medium term aim should be for customs tariffs to be the only form of direct intervention in import trade (exceptions would be for import controls on a small number of products for security and safety reasons). While accepting the customs tariffs are an important source of easily collectible revenues, their structure should be designed principally with their resource allocation effects in mind. This would suggest a relatively low and uniform level of rates with limited exemption provisions. A new customs tariff schedule was promulgated in 1984 representing a first step in this direction. 3/ The reforms involved a considerable narrowing of the range of rates (10 to 60 percent with some exceptions) and the abolition of schemes providing zero or concessionary rates to a large group of favored importers not involved in export trade. However, further modifications to the schedule should be made to narrow even more the range of rates (probably 15 to 35 percent, with a clustering of rates in a narrower band of 20 to 30 percent). This would seem to be a reasonable range for the final structure of the custom tariff schedule

---

2/ These recommended exchange rate actions are interim thoughts of the Ban
k only. Firm recommendations will be formulated after the IMF completes in reviews in March/April 1986.

3/ This schedule was developed by the Government with the assistance of the Bank and was to form part of the conditionality of the proposed SALI of 1984.

taking account of the Government's insistence on some continuing protection for import replacement activities, the level and structure of excise taxes and revenue considerations (in the case of luxury goods, high levels of excise taxes on production are also proposed to be applied to imports - see para 11). The appropriate modifications should be made at the time of the initial devaluation, with further modifications over the adjustment program period being limited to the correction of anomalies and the simplication of the rate structure where required.

8. As indicated earlier, the dismantling of quantitative restrictions on imports should be phased over a maximum three year period. Initial priority should be given to liberalizing the import controls on raw materials and spare parts (with some exceptions) through their transfer to open general licence (OGL) status, noting that the changes made in the custom tariff sub-heading descriptions for the new schedule introduced in 1984 facilitate the distinction of raw materials and spare parts from other goods. This would coincide with the initial devaluation and would serve to rejuvenate local production and relieve to some extent the growing problem of unemployment. 4/ During the first year of the adjustment program, studies should be undertaken to develop more fully a medium term plan for liberalizing the remaining import controls (with the exception of a limited number of goods restricted for security and safety reasons). The plan should include measures to counteract dumping and trade restrictions imposed by other countries and to streamline import licensing and foreign exchange allocation procedures. Priority should be given to liberalizing (at the beginning of the second year of the program) restrictions which have important distortionary and protective effects and on most capital equipment. The liberalization should apply not only to goods on the prohibited list and those subject to import licensing, but also to foreign exchange allocations of the Central Bank as applicable. The Government has already taken steps to simplify the "two queue" system of import controls by decentralizing approval power to foreign exchange dealers, harmonizing the issuance of import licenses with the foreign exchange budget, and abolishing the system of global and monthly allocations of foreign exchange for trade transactions to authorized dealers.

9. The "across the board" temporary import surcharge of 30 percent 5/ recently introduced by the Government serves as an implicit devaluation (on the import side), allows the Government to capture some of

---

4/ Some form of reserve powers will have to be devised to allow the Government to intervene if there should be excessive speculative imports detrimental to the overall reform program. The proposed high levels of excise taxes on luxury goods (applicable to both imports and local production) would serve to constrain expenditures on imported inputs for this production.

5/ Inclusive of the previously applicable surcharge of 6.02 percent but additional to all existing customs tariffs. The proceeds of the surcharge are to be used principally for strengthening the program of non-oil export promotion and export incentives (see paras 12 to 14).

the "quota rents" associated with the goods under import restrictions and provides additional resources to the exchequer. Based on the monitoring of the initial effects of the reforms and in the context of the medium term plan to liberalize the remaining quantitative restrictions, a decision should be made at the end of the first year of the adjustment program as to whether or not the surcharge should continue to be applied. Preferably its effects should be captured through an equivalent exchange rate adjustment (which may be required under an IMF program, since such a surcharge is regarded as an unfavorable multiple exchange rate practice).

10. Internal Trade Taxes and Controls. The Government should take steps to withdraw its direct interventions in price setting. Immediate action should be taken to relax the controls on ex-factory prices in order to shift incentives away from trading to production, to signal relative scarcities and to increase the effective yields and elasticity of the excise tax system. Also it would be highly desirable to shift farmer incentives from input subsidies to a crop pricing structure which reflects market forces, and to re-examine the role of the six commodity marketing boards (see para 6) and the approach to the setting of support prices for domestic crops with the aim of minimizing Government intervention. The recently created Agricultural Prices and Tariffs Group (APTG), which absorbs the Technical Committee on Producer Prices would be responsible for the formulations of recommendations in these areas for implementation in the second year of the adjustment program. The Government has recently adjusted petroleum product prices (except for kerosine) to remove implicit financial subsidies, although it should continue to adjust these prices in line with the exchange rate adjustments.

11. Excise taxes on production for the local market should be structured so as to be consistent with principles for the setting of custom tariff levels. They should be set at a lower level than custom tariffs (within the range of 5 to 25 percent but clustered in the 10 to 20 percent range) to reflect a reasonable net degree of import protection. However, high additional excise duties (say 50 and 100 percent) should be applied to the local production of luxury goods (and selected other consumer items) as well as to imports of them. The appropriate rates for industrial products (including mining) and any required offsetting provisions should be determined prior to the commencement of the adjustment program and be put in place at the same time as the desired tariff schedule, 6/ although some fine tuning may be required later in the adjustment period. The approach to the taxation of agricultural and forestry product should be reviewed by the APTG and policies formulated for implementation in the second year of the adjustment program.

12. Export Incentives. A package of fiscal incentives should be introduced which removes as far as possible the impediments to non-oil export production inherent in the system of trade taxes and controls. Even

---

6/ The Government broadened the excise tax system in 1984 in parallel with the introduction of the revised customs tariff schedule. This broadened system provides a good basis for future reforms.

when import controls have been completely removed and the exchange rate has been adjusted to its market clearing level, the trade taxes in force will still mean that compensatory export incentives will be required.

13. To attempt to provide the right level of export incentives during the period when import controls are being dismantled and substantive real exchange adjustments are continually being made would be a complex, and perhaps unnecessary, task. The base level of export incentives should be set to reflect the situation at the end of the import liberalization period, although the temporary import surcharges on inputs into export production would be refunded while they are in force during the import liberalization period. Budgetary considerations and GATT regulations would need to be taken into account in determining the nature, level and coverage of the incentives, but the package could include: (i) the recently reactivated customs drawback scheme, but extended and adapted to include exemption (or equivalent) from customs tariffs and excise taxes on all inputs directly and indirectly incorporated in export production (the present scheme only covers excise duties on exports and customs tariffs and import surcharges on imported inputs directly incorporated in export production); and (ii) a negotiable tax credit on export production set at a level to offset, as far as possible, the distortionary effects of the import protection system and exchange rate policy on value added in non oil export production (the ability to sell a portion of foreign exchange earned in the second tier foreign exchange market goes part of the way towards overcoming the discriminatory effects of the exchange rate policy - see paras. 5 and 14). It would be important to ensure that the administrative mechanisms for making the incentives available are simple and straight forward, which will require a redesign of the existing customs drawback scheme so that it is less cumbersome and allows timely refunds to exporters. It is proposed that the studies required to finalize the coverage, design and administration of the incentive be undertaken jointly by the team involved in the Industry Technical Assistance Project (ITAP) and the ATPG during the first year of the adjustment program for implementation in the second year. The design of appropriate incentives for export traders and service exports would form part of the review.

14. Other Measures. Recent measures introduced by the Government to promote non-traditional exports include: (i) activation of the already created export guarantee and insurance scheme; (ii) extension of the foreign exchange retention scheme to allow exporters to retain 25 percent of foreign exchange earnings, which can be used to purchase priority inputs (although an import license not valid for foreign exchange still has to be obtained) or be sold in the second tier foreign exchange market; and (iii) assistance in export costing and pricing (nature yet to be specified). Steps have also be taken to overcome the deficiencies in the operations of the Nigerian Export Promotion Council, to encourage the establishment of the Export Zones in selected parts of the country and to require authorized foreign exchange dealers to set up export desks for export promotion activities.

15. Investment Incentives. A review of the fiscal investment incentives being granted by the Government to industry should be undertaken with a view to: (i) making them more meaningful to investors without creating an undue burden on the Government budget; (ii) ensuring, while

acting as a compensatory measure for remaining market imperfections and failures, they do not create new distortions in themselves and are consistent with, and reinforce, the Government's development objectives (especially employment generation and regional dispersal); and (iii) ensuring their simplicity in administration, including minimal discretion in their application. 7/ This will also involve the specification of guidelines for their availability. The review should be carried by the ITAP team at the same time as the studies for the fiscal export incentives, with changes being implemented concurrently in the second year of the adjustment program.

16. Other steps to be undertaken to improve investment promotion during the first three years of the adjustment program would include (i) the establishment of the existing Industry Development Coordinating Division of the Industrial Policy Review body as an effective "one stop" agency for industrial approvals and investment promotion; (ii) streamlining the regulatory measures relating to the operations of enterprises and investment, including the removal of inconsistencies in prevailing laws and regulations and minimizing the overlapping jurisdictions among agencies; and (iii) amending, where necessary, investment policies and guidelines to generate further desirable foreign investment. The latter should include increased ownership flexibility in some areas. To encourage increasing private interest in medium and large scale commercial farming, it will also be necessary to review the land tenure arrangements. There is a need to strengthen promotion and support services for the private sector, including pre and post-investment services, statistical and business information services, applied agricultural research programs and extension and technical support services. A conscious effort should be made to ensure continuous and effective dialogue with the private sector, and to seek their active participation in formulating and implementing investment policies and promotion programs.

Public Expenditure Policies

17. The highly constrained public resource situation - particularly of foreign exchange - will mean that difficult decisions regarding both the level and structure of public expenditures will have to be taken. The requirement is to cut back on the expenditures in a way which does least damage to the economy and ensures that maximum net benefits flow from them. To achieve this, the composition of federal and state expenditure over the five year adjustment period should support the macroeconomic policy reforms and reflect basic economic principles, with allocations at the sectoral level being made within the context of clearly articulated sectoral development strategies. However, there is also a need to put in place a

---

7/ While the present investment incentives offered in Nigeria have had little impact (the import protection system having the dominating influence on investment), a properly constructed system of fiscal investment incentives can be an extremely powerful took for encouraging desirable investment in industrial activities, as the experience of other countries has shown.

system of public expenditure planning and budgeting which recognized the revenue uncertainties - resulting mainly from the unpredictability of oil markets - and can alleviate their negative impact.

18. Critical Principles in Determining the composition of Public Expenditures. The principles which should guide the Federal and State Governments in their budgetary and planning decisions over the five year adjustment program are as follows. First, the public wage bill should be stabilized. The Government recently reduced the salaries of public servants and should restrain attempts for levels to be restored over the next three years at least. The Government's present freeze on hiring should be maintained and extended to all but the most critical skills. Over the longer run, the emphasis has to be on eliminating overstaffing through a judicious combination of attrition and redeployment, and on allowing wages for different skill categories to reflect scarcity values. Second, constrained supplies and maintenance expenditures have greatly impaired the efficient delivery of public services. Restored levels of supplies will be essential in a number of sectors (particularly health, education and agriculture) if reasonably modest standards of services are to be achieved. Also, both routine and periodic maintenance must have priority over new investment to prevent the rapid deterioration of infrastructure. Third, transfers to parastatals to cover operating deficits and capital expenditures have to be reduced, with efforts made to ensure that the commercially oriented public enterprises are increasingly able to support their own capital expenditure programs (see paras 21 to 25). The Government has already taken steps in this direction by reducing transfers to all economic and quasi-economic parastatals to 50 percent of present (1985) levels, requiring the parastatals to obtain the balance of their needs from tariff increases and increased operating efficiencies. Finally, priorities should be set for the completion of the large number of capital projects on the basis of their economic viability and costs to complete, with across-the-board cuts being avoided so that the economy is not burdened by a proliferation of incompleted and weak projects. Those which are clearly not economically viable, even on a sunk cost basis, should be cancelled and the necessary penalties paid. For projects in the early stage of implementation, possibilities for reshaping the scope and/or timing to reduce costs and increase benefits should be assessed, especially where large sums remain to be spent. Completing viable ongoing projects should have priority over new projects, the latter not being commenced unless their economic viability is beyond question and fund can be assured both for their timely completion and to meet their ongoing costs.

19. Agreement would be reached with the Federal Government on how these principles would be reflected in the budgetary and planning process. The mechanisms for this would be agreement on the initial composition and subsequent criteria for updating the proposed rolling multi year budget and core investment program (see para. 20). It will also be important for the principles to be reflected in State Government expenditures, although the means for ensuring this still have to be determined.

20. Public Expenditure Planning and Budgeting. The most important institutional reform to be pursued should be the adoption of a rolling multi-year budget which allows the implications of resource prospects over an extended period to be taken into account in making decisions on projects

and programs. The system should be introduced in a phased manner, beginning with a selective two-year rolling budget to be put in place for the first year of the adjustment program. This should be supplemented with a core type approach to the planning of capital investments. The essential features of the approach would be the division of projects into two categories: (i) those that would proceed immediately; and (ii) those that would go ahead if and when additional resources would be available. The former set of projects (core list) would be fully funded each year in line with the amounts need for efficient implementation. No funding would be provided for any of the projects on the standby list unless adequate resources were available to guarantee their full funding to completion. 8/ The first steps in this direction have already been taken through the findings of the special inter-ministerial committee set up late in 1983 to review all projects involving completion cost of ₦30 million or more. Subsequent public expenditure and project reviews of the Government and the World Bank can also be used as deriving the initial rolling budget. Underlying all these actions, would be a move away from the present "shopping list" nature of the Five Year Development Plan to one which is more indicative and policy oriented, with sectoral development strategies (see paras. 30 to 38) forming the principal means for establishing capital and recurrent expenditure priorities within each sector.

Public Enterprise Policies

21. Substantive policy reforms relating to parastatals are required to improve their overall efficiency and to reduce their heavy dependence upon Government financial support. In recent years the Government has taken steps to ensure some public enterprises to operate along more commercial lines and has commissioned several studies of their problems. Certain enterprises, mainly in agricultural activities, have been privatized. However, despite these measures and the findings of officially backed investigations - including the Onosode Commission in 1981 and the

Study Group on Parastatals in 1984 - the Government has not been able to articulate a cohesive program of policy reforms, although it has recently announced its intent to divest of public holdings in commercially-oriented enterprises (agricultural production, hotels, food, beverages, breweries, distilleries, distribution, electrical and electronic appliances etc.). Such a program should be prepared with the utmost urgency, being completed with the first year of the adjustment program and incorporate actions along the lines outlined below. The reforms would be implemented over the five year adjustment period, with the timetable being finalized once the program has been formulated.

8/ There would clearly need be some additional ranking of priorities on the standby list. Placing a project on the standby list would serve to signal to the relevant line ministry that the project is on the point of being approved and that it should move ahead to complete project preparation, design and so on.

22. Rationalization of the Parastatals. Within the context of the development strategies for the sectors in which they operate, parastatals should be examined and classified according to whether they should be left largely unchanged, restructured, privatized or liquidated. Certain enterprises slated for privatization may require prior financial restructuring and perhaps some rehabilitation. In-depth studies of a number of enterprises will be required before a final decision can be made on them. The sector ministries should be given the responsibility for completing this task, with a restructured and strengthened Ministry of Finance Incorporated (MOFI) playing a supporting role. Plans for restructuring should include rehabilitation requirements as well as financial and organizational changes. As part of the financial restructuring, outstanding loans to the enterprises would have repayment, grace and interest terms specified; 9/ in some cases, outstanding loans could be converted to equity. Also, guidelines should be developed that will permit certain enterprises to privatize selected aspects of their operations (e.g. trading companies). Financial constraints facing the Government will mean that priorities will have to be set for restructuring.

23. Autonomy and Accountability. Public enterprises should immediately be given autonomy in making operating decisions relating to, for example, day-to-day management, procurement and staffing. However, the Government, through the supervision ministries, should take parallel action to establish clear objectives and performance targets with the board and chief executive officer of each enterprise, and to assist in drawing up action plans to achieve these targets. Also, MOFI should be made responsible for monitoring the financial performance of the enterprises, making recommendations on their investment programs where access to budgetary resources and external financing is involved, and for ensuring that they produce timely and adequate accounts audited according to appropriate Nigeria standards. Close liaison of MOFI (or whatever oversight agency is chosen for this role) with the supervisory ministries will be required, especially in the formulation and review of objectives and plans for each enterprise. 10/

24. Commercial Orientation. Greater autonomy should be given to enterprises to determine their tariff and pricing structures. Where Government approval of tariffs is required (especially of monopolies or quasi-monopolies), they should be review frequently to reflect cost and financial return considerations, taking cognizance of enterprise efficiencies. Tariff adjustments of key utilities should be also be linked

---

9/ Similarly, all future loans should have clearly specific terms and conditions. Public enterprises should also be expected to settle outstanding payment obligations vis-a-vis other public enterprises and Government agencies.

10/ MOFI and the liaison office in each supervisory ministry will need to be strengthened. MOFI in particular should be provided the additional staff resources necessary for it to carry out its functions effectively.

to clearly defined targets for the reduction of budgetary transfers to them. Where enterprises are fulfilling non-commercial objectives of the Government, they should be compensated through special budgetary provisions based on estimates of the costs involved. However, cost curtailment and improved operating efficiency should be the first order of business for most parastatals. The adoption of improved accounting practices and financial controls should be encouraged. Technical assistance should receive particular attention. the appointment of high caliber top management will be essential.

25. Approach to State Parastatals. A similar approach could be adopted for state public enterprises. In this case, the scope of intervention and required policy reforms would be less demanding since, for the most part, the states are principally involved in the industrial sector and the bulk of their holdings are relatively small-scale. These enterprises are targets for privatization. The most substantive holding of state Governments tend to be jointly owned with the Federal Government and thus would be covered in the reforms at that level.

Financial System Policies

26. The increased mobilization of financial savings and the more efficient allocation of financial resources will be essential components of the adjustment program. In general, the Government should reduce its intervention in the operation of financial markets - particularly in credit allocation and the setting of interest rates - and allow more discretion to the financial institutions in their operations. Encouragement should be given to the establishment of new banks and branch expansion, and to the development of the domestic capital market.

27. Restructuring the Financial Sector. The Government has recently announced its intention to review the financial sector with the aim of its restructuring. The review, which should be completed by the end of the first year of the adjustment program, should result in the articulation and subsequent implementation of a strategy which includes means to: (i) reduce barrier to entry in banking and finance (which could include liberalization of ownership laws); (ii) encourage branch expansion in rural areas; (iii) further develop capital markets as a source of long-term finance; and (iv) improve existing agricultural credit delivery systems. The latter would include an overhaul of the operations of the Agriculture Credit Guarantee Scheme and the Nigerian Agricultural and Cooperative Bank (NACB), with emphasis on decentralization and closer cooperation of NACB with the commercial banks.

28. Credit Allocation. The credit allocation system gives the banks little discretion in credit allocation across sectors and imposes on them extensive reporting requirements. A timetable for the removal of the

percentage credit allocation ceiling should be agreed upon 11/ with the initial steps being a further aggregation of the sectors (and subsectors) for which the ceilings are imposed and the replacement of monthly reports by the bank with semi-annual (on at-most quarterly) reports.

29. Interest Rates. An immediate move should be made to adjust the level of interest rates to reflect a positive real yield on holding financial assets, and it should be flexible to take into account the frequent changes in the rate of inflation and balance of payment conditions. Also, the differential interest rates applied to the preferred sectors should be eliminated.

Productive Sector Policies

30. As indicated earlier, intra-sectoral breakdowns of public expenditure should be determined within the context of medium term development strategies for each sector. the strategies should take cognizance of the broader macroeconomic and related policy reforms (as relevant), and address the specific policy and institutional reforms required to achieve sectoral development objectives in an efficient way as well as the appropriate schedule of public expenditures to support them.

31. Special focus should be placed on the removal of bottlenecks and constraints affecting the efficient development of the productive sectors. While the basic trade and incentive policy reforms will go a long way in this direction, there are a number of policy and non-policy originating distortions which are only recognizable at the sectoral level (e.g. local content programs for specific industries, lack of particular work force skills) on which action must be taken to ensure the realization of comparative advantage and efficient resource allocation. Further, there are various market imperfections (e.g. lack of data and of knowledge by potential investors - particularly foreign - of investment opportunities in some industries) which require Government initiatives to correct. Such actions would be consistent with the aim of seeing the Government's role in the productive sectors changing from a regulatory one to a promotional one, as well as from one which emphasizes Government direct investment and intervention to one supportive of private initiatives.

32. The strategies proposed for each sector should be completed before the commencement of the reform program so as to form the basis for the specification of sectoral level policy reforms and actions over the the adjustment period. They would be updated on a regular basis and would be an important input into the formulation of the rolling multi-year budgets. The following represents key elements which should be incorporated in the strategies for the major productive sectors viz. agriculture, oil and gas, and manufacturing.

11/ The Government recently took steps towards simplification by grouping activities into four sectors (previously of eight sectors) for which percentage credit allocation ceiling are set. However, within some sectors, sub-sector ceilings have been set.

33. Agriculture. Sustained growth of the agricultural sector requires that comparative advantage be the primary criterion for the crop and technology choices that have to be made. Food crops are and must remain central to the development strategy for the sector, and should continue to be given strong support from the Government in areas such as research. However, export crops and other non-food commercial crops must also play an increasing role over time as reliance on oil exports decreases; in this connection, increasing Government support should be given to these crops.

34. Budget constraints will require difficult allocative decisions on the public investment program in the sector. Resources should be concentrated on maximizing the returns from existing investments. In this respect, allocations for irrigation should not be used for large scale dam and water diversion structures but should instead emphasize down-stream delivery systems where the incremental costs are within reach, with even greater emphasis on the development of smaller scale, quickly implementable, low cost irrigation schemes. The ADPs will continue to justify a major proportion of expenditure. However, a change in policy to promote crops for export and industrial crop import substitutes would require public funds to support appropriate commercial tree and field crop development projects. The rapid reduction of fertilizer and other input subsidies, through a full cost pricing policy, would free up public funds for these essential services. The Government should also give priority to agricultural research. It should actively pursue applied research programs which will expedite the adoption of new varieties and technologies from the national and international research centers, and establish their appropriateness and applicability at the farm level. While such research should encompass all aspects of agricultural cropping, it should give priority to rain-fed farming in the lower rainfall areas. Forestry development will also remain critical, not only to meet long term national wood and pulp needs, but also to combat serious natural resource degradation. Finally, in livestock, the decline in the national herd must be arrested, veterinary services strengthened and domestic meat production expanded to replace imports.

35. Oil and Gas. It will be important for the joint venture companies to maintain investment in oil exploration and development at levels that will ensure satisfactory oil reserve/production ratios. To minimize its investment burden in the petroleum subsector, the Government should consider entering into production sharing agreements for new acreage outside of the Niger Delta area. Desirable revisions of NNPC's own investments in oil exploration should be aimed at minimizing expensive exploratory domestic drilling over the adjustment period. The highest priority is the construction of the Warri-Lagos pipeline and the corresponding field development of Utorogu. It is most unlikely that further field development would be required before the end of the eighties so plans to invest in an associated gas gathering system in the western Niger Delta could be postponed. Other "core" capital expenditures over the adjustment period should be limited to the commencement of the development of the LNG project infrastructure for LPG distribution and NNPC's own expenditure on oil exploration activity. A consistent pricing policy for oil and gas should support the investment program (see para 10).

36. The approach adopted in the LNG project is a strategic one and allows for a great degree of flexibility with respect to the scope of the project, its starting date and phasing, and the degree of private sector participation. The project would have the highest chance of success if it were set up on a joint venture basis, with at least a 40 percent share for foreign companies and with an experienced operating company in charge of management.

37. Manufacturing. The broader exchange rate, trade and incentive policy reforms will serve in particular to encourage desirable private investment and production in manufacturing. However, subsectoral strategies will need to be prepared for the key sectors of steel and petrochemicals which constitute major areas of Government investment in the sector. With the projected severe resource constraints and the poor performance and high costs of past public investments, there is a need to reduce considerably the role of the public sector in industrial development. Increased domestic and foreign private investment and production, in line with Nigeria's comparative advantage, would need to be encouraged as a basis for future sustained industrial growth. Meanwhile, public sector efforts could be redirected towards strengthening industrial infrastructure and support services.

38. The necessary scaling-down of the public expenditures in the manufacturing sector should principally be achieved as follows. In steel, given the inadequate market for its products, its high costs and doubtful viability, construction of the Ajaokuta steel works should be discontinued or deferred indefinitely. Further expenditures to complete the Delta Steel complex should be held to minimum necessary levels. No new projects (including the flat products plant, special alloys plant, special alloys plant and foundries) should be embarked on. In petrochemicals, priority should be given to the effective completion of Phase I projects, but this should include the implementation of a restructuring plan for the carbon black and synthetic detergent plants. The Phase II A project should be deferred until after the adjustment period. In refineries, the debottlenecking projects at the Kaduna and Wassi refineries should be completed as soon as possible, and the Government should reconsider its decision to proceed with the proposed Port Harcourt II refinery given its unacceptably low economic rate-of-return.

Annex A
Nigeria: Policy Actions [illegible]

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN (TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD)	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	IMF PROGRAMS: JOINT COND.	SAL PROGRAMS: SAL I	SAL PROGRAMS: OTHER SALS	OTHER BANK LENDING OPERATIONS
I. EXCHANGE RATE, TRADE AND INCENTIVE POLICIES												
A. Exchange Rate: Move to a realistic level appropriate to the reformed trade policy environment.	1. Reconfirmation of policy of crawling adjustment of the exchange rate to reduce overvaluation of Naira.	1. Substantial initial devaluation and adoption of a more flexible exchange rate policy.	●					●				
	2. Proposal to establish a second tier foreign exchange market.	2. Move towards unification of the second-tier foreign exchange market with the 'formal' market.		●	●	●	●	●				
	3. Implicit Devaluation through introduction of import surcharge (see I C 3 - Action recently taken) and export incentives (see I E - Actions recently taken).											
B. Export Controls & Taxes: Remove export controls and marketing restrictions on desirable non-oil exports.	1. Abolition of list of prohibited exports (with some exceptions).											
	2. Simplification of export licencing procedures.											
	3. Abolition of export monopoly power of the six commodity boards.											
C. Import Controls & Taxes: Dismantle import controls and move to a situation in which a relatively moderate and uniform customs tariff is the only form of direct intervention in import trade (with limited exceptions).	1. a. Promulgation of new customs tariff (1984) narrowing range of tariffs (10 to 60% w some exceptions). Adjustments made (post-1984) to correct anamolies.	1. Modify further customs tariff schedule, narrowing rates to 15 to 35% range.	●					●		●		
	b. Abolition of approved user and other schemes (1984) providing zero or concessionary rates to favored importers.	2. a. Liberalize import controls on raw materials and spare parts.	●					●		●		
	2. a. Simplification of "two queue" system of import controls and introduction of measures to remove administrative abuses and block leakages in granting import licences.	b. Formulate a plan for the phased liberalization of remaining import restrictions.	●					●		●		
	b. Rationalization of priorities for issuance of import licences, with increased emphasis on (i) imports to support food production and (ii) raw materials and spare parts for manufacturers.	c. Implement liberalization plan.		●	●	●	●	●				
	c. Creation of new category of import licences not valid for foreign exchange for approved priority imports.											

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL I	OTHER SALS	OTHER BANK LENDING OPERATIONS
C. Import Controls & Taxes (Continued)	3. Introduction of a temporary import surcharge of 30%.	3. Import surcharge to be replaced by appropriate exchange rate action.										
	4. Abolition of compulsory advance deposit requirement for imports.											
D. Internal Trade Controls and Taxes: Withdrawal of Government from direct intervention in price setting. Excise taxes used as a major revenue measure, with coverage, structure and level being consistent with the principles for the setting of custom tariff levels.	1. Adjustment of domestic petroleum product prices to remove financial subsidy (except kerosine).	1. a. Relax ex-factory price controls on all goods.										
	2. Expansion of excise tax base (1984), with taxes re-structured to be consistent with new customs tariff schedule. Further modifications post 1984.	b. Formulate and implement approach for shift to crop pricing structure which reflects market forces. Re-examine role of the six commodity market boards and approach to setting of support prices for domestic crops.										Agricultural sector and project loans.
	3. Creation of Agricultural Prices and Tariff Group (APTG) to be responsible for recommendations regarding price support and other trade policies relating to agriculture.	c. Adjust petroleum product prices in line with exchange rate adjustments.										Transport sector and project loans.

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL I	OTHER SALS	OTHER BANK LENDING OPERATIONS
D. Internal Trade Controls and Taxes (Continued)		7.a. Restructure excise taxes on ex-factory production of all goods to fall within range of, say, 5 to 25%.										
		b. Apply additional excise duties to both locally produced and imported luxury goods (say 50 or 100%).										
		c. Formulate (AIPG) and implement policies for taxation of forestry and agricultural products.										

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL I	OTHER SALS	OTHER BANK LENDING OPERATIONS
E. Export Incentives: Introduce a package of fiscal incentives which removes impediments to exports and restores competitiveness of non-oil export production. Adopt other non-distortionary measures to promote non-oil exports.	1. Reactivation and modification of custums tariff drawback scheme.	1.a. Review and modify appropriately Customs Tariff Drawback Scheme and other fiscal export incentives.	[redacted]						[redacted]		[redacted]	
	2. Assistance on export costing and pricing (nature yet to be specified).											
	3. Extension of the Foreign Exchange Retention Scheme to allow exporters to retain 25% of foreign exchange earnings.	b. Adjust these and other export incentives as needed (including phasing out transitory elements of the package) to reflect progress of exchange rate and other trade policy adjustments.	[redacted]								[redacted]	
	4. Activation of an already created Export Credit Guarantee and Insurance Scheme.											
	5. Encouragement of establishment of Free Export Zones in selected part of the country. Revitalization of the Export Promotion Council. Requirement for authorized foreign exchange dealers to set up export desk for a export promotional activity.											

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL I	OTHER SALS	OTHER BANK LENDING OPERATIONS
F. Investment Incentives: Introduce a set of fiscal investment incentives which are meaningful to investors, minimally distortionary and simple in their administration. Also improve other efforts to promote foreign and local investment in desirable production activities.		1.a. Carry-out studies to finalize the coverage, design and administration of a package of fiscal investment incentives.										
		b. Introduce incentive package.										
		2. Undertake other measures to improve investment promotion including:										
		a. Improve investment promotion operations of the existing Industrial Development Coordinating Division of the Industrial Policy Review Body.										
		b. Streamline regulatory measures relating to operations of enterprises and investment.										
		c. Review and ammend where necessary, investment policies and guidelines to promote desirable foreign investment.										
		d. Strengthen support services to the private sector (information, applied research, etc.).										Industry and Agricultural sector and Project loans.

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL I	OTHER SALS	OTHER BANK LENDING OPERATIONS
II. PUBLIC EXPENDITURES POLICIES												
A. Level and Structure of Public Expenditures: Curtail public expenditures in a way which does least damage to the economy and ensures that maximum benefits flow from them. Composition of federal and state expenditures over the five-year adjustment period should support the macro-economic policy reforms and reflect basic economic principles, with allocations at the sectoral level being made within the context of clearly articulated sectoral development strategies (see also V - Sectoral Policies).	1. Reduction of salaries of public servants (1985). Freeze on hiring new public service staff in a wide range of positions (1984). Reduction of fringe benefits to public servants.	1. Stabalize public wage bill. (limits to be determined within the context of the rolling three-year budget see II B.1).										
	2. Reduction of non-statutory transfers to all economic and quasi-economic parastatals to 50% of present (1985) levels. Balance of needs to be obtained from increases in tariffs of parastatals.	2. Restore levels of supplies relative to manpower and give priority to routine and periodic maintenance over new investment (basis to be agreed within the context of the rolling three-year budget).										
	3. Major ongoing investment project (over N30 million to complete) reviewed by Inter-Ministerial Committee (with World Bank Technical Assistance - 1984).	3. Continue to reduce and ultimately eliminate transfers to commercially-oriented parastatals to cover their operating deficits and capital expenditure programs (with limited exceptions - see also III below).										
		4. Restructure Federal public investment program: within context of agreed (i) sector strategies (see V); (ii) principles for setting priorities and (iii) budget constraints.										

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL I	OTHER SALS	OTHER BANK LENDING OPERATIONS
PUBLIC EXPENDITURES POLICIES (Continued)		b. Review public investment program annually in light of current revenue considerations, ensuring consistency with principles and sector strategies.	■	■	■	■	■			●	●	Sectoral and project loans.
B. Public Expenditure Planning and Budgeting: Improve budgetary process by adopting approaches to planning and budgeting which allow implications of resource prospects over an extended period to be taken into account in making decisions on projects and programs.		1. Adopt a rolling multi-year budget:										
		a. Begin with a two year rolling budget.	■						●	●		
		b. Expand to a three-year rolling budget.				■			●		●	
		2. Adopt a core-type approach to planning of capital, investment relating it to the rolling multi-year budget.	■							●		

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD — TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY — IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL I	OTHER SALS	OTHER BANK LENDING OPERATIONS
III. PUBLIC ENTERPRISE POLICIES												
Improve overall efficiency of parastatals and reduce their heavy dependence on the Government for financial support. Privatize commercially oriented parastatals	1. Appointment of Study Group on Parastatals (1984). Report submitted.	1. Prepare a Statement of Policy on Public Enterprises.	[redacted]							[redacted]		
	2. Decision to divest of public holdings in commercially oriented enterprises (agricultural production, hotels, food, beverages, breweries, distilleries, distribution electrical electronic appliances and all non-strategic industries). Also, consideration to be given to reducing public holdings without losing control in banks, insurance companies and other financial enterprises.	2. Restructure and strengthen Ministry of Finance Incorporated (MOFI) to effectively support the Ministries in planning and executing public enterprise reforms.		[redacted]						[redacted]		
		3. Within the context of sector strategies (see V - sector policies) carry out a rationalisation program for parastatals.										
		a. Classify parastatals according to whether they should be left largely unchanged, restructured, privatized or liquidated. Indepth studies required for some enterprises.	[redacted]							[redacted]		
	3. Direction to parastatals to improve accounting practices and to issue timely financial reports. Accounts to be audited and published.	b. Establish priorities and timetable for rationalization.	[redacted]							[redacted]		
		c. Prepare and implement restructuring sub-program.		[redacted]						[redacted]	[redacted]	
		d. Prepare and implement privatization and liquidation sub-program.		[redacted]						[redacted]	[redacted]	

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	ACTIONS TO BE TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD — TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY — IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL I	OTHER SALS	OTHER BANK LENDING OPERATIONS
IV. FINANCIAL SYSTEM POLICIES Reduce Government intervention in financial markets and allow more discretion to the financial institutions in their operations.	1. Announcement to review financial system with the aim of its restructuring. To include (i) review of barriers to entry in banking and finance (ii) overhaul of operations of Agriculture Credit Guarantee Scheme and the Nigerian Agricultural and Cooperative Bank (NACB), with emphasis on decentralization and closer cooperation of NACB with the commercial banks.	1. Prepare and implement program for restructuring the financial sector. To include means to (i) reduce barriers to entry (ii) encourage branch expansion in rural areas (iii) further develop capital markets as a source of long-term finance and (iv) improve existing agricultural credit delivery system.										
		2. a. Adjust interest rates to reflect positive real and scarcity yields.										
	2. Announcement to narrow gap in the margin and spread of interest rates.	b. Phase out interest differential among sectors.										
	3. Credit allocation system simplified by reducing number of sector with ceilings from 8 to 4.	3. Simplify further credit allocation system with the ultimate objective of eliminating it.										
		a. Aggregate ceilings.										
		b. Replace monthly reports with semi-annual reports.										
		c. Eliminate ceilings.										

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD					VEHICLE FOR CONDITIONALITY				
		ACTIONS TO BE TAKEN	TARGET COMPLETION DATE					IMF PROGRAMS		SAL PROGRAMS		OTHER BANK LENDING OPERATIONS
			YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	SOLE COND.	JOINT COND.	SAL I	OTHER SALS	
V. SECTORAL POLICIES Prepare medium term development strategies for each sector, taking cognizance of broad policy reforms (as relevant), and address the specific policy and institutional reforms required to achieve development objectives in an efficient way as well as the appropriate schedule of public expenditures to support them. Special focus on the removal of bottlenecks and constraints affecting the efficient development of productive sectors.		1. Prepare strategy for agricultural sector (see also I, II, III, and V) and IV).										
		a. Prepare statement of policy on agriculture and water resource development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.										Agriculture sector, Multi-state ADP project loans.
		b. Create the ATPG to carry out necessary studies on agricultural product prices, marketing and incentives.										
		c. Ongoing revision and implementation of sector strategy.										
		2. Prepare strategy for oil and gas sector (see also I, II, III, and IV.										Oil and gas sector and project loans.
		a. Prepare statement of policy on oil and gas development, incorporating principles for public investment, and parastatal operations in the sector.										
		b. Ongoing revisions and implementation of sector strategy.										

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD: ACTIONS TO BE TAKEN	TARGET COMPLETION DATE: YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	VEHICLE FOR CONDITIONALITY: IMF PROGRAMS: SOLE COND.	JOINT COND.	SAL PROGRAMS: SAL I	OTHER SALS	OTHER BANK LENDING OPERATIONS
SECTOR POLICIES (Continued)												
	Establishment of Industry and Trade Policy Analysis Unit (ITAP) expected soon under World Bank Industry Technical Assistance Project loan to the Government. Will work in collaboration with ATPG to carry out trade and incentive policy analysis.	3. Prepare strategy for the manufacturing sector (see also I, II, III and IV).										
		a. Prepare statement of policy on manufacturing development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.										Industry sector loan
		b. Designation of high level interministerial body for guiding and counseling the trade and incentive policy reforms (for both manufacturing and agriculture).										
		c. Key industry studies to be carried out as part of the work of ITAP, with aim of: (i) identifying and formulating measure to overcome regulatory constraints and market imperfections affecting efficient development; (ii) reassessing approach to public involvement in the industries and (iii) providing information base for promotion of private investment. Priority to be given to studies of refineries, petrochemicals, steel, and pulp and paper.										
		d. Ongoing revisions (especially in light of findings of industry studies) and implementation of sector strategy.										

ACTION PARAMETERS	ACTIONS RECENTLY TAKEN	TIMETABLE FOR ACTIONS OVER THE ADJUSTMENT PERIOD									VEHICLE FOR CONDITIONALITY				
		ACTIONS TO BE TAKEN	TARGET COMPLETION DATE					IMF PROGRAMS		SAL PROGRAMS		OTHER BANK LENDING OPERATIONS
			YEAR 0	YEAR 1	YEAR 2	YEAR 3	YEARS 4 & 5	SOLE COND.	JOINT COND.	SAL I	OTHER SALS	
SECTOR POLICIES (Continued)												
		4. Prepare strategies for education and health sectors (see also II, III, IV and V).										Sector and project loans.
		a. Prepare statements of policy incorporating federal/state responsibilities, and principles for cost-recovery, public investment and recurrent expenditures.		[redacted]								
		b. Prepare multi-year public expenditure program (categorize core, reserve core, non-core) consistent with policy statement, budget constraints and principles underlying structure of public expenditure program. Relate program to state responsibilities.	[redacted]	[redacted]								
		c. Ongoing revisions and implementation of strategies.		[redacted]								
		5. Prepare, revise and implement strategies for other sectors.		[redacted]								Sector and project loans

Annex B

NIGERIA: Policy Actions in First Year of Adjustment Program

Policy Action	At Commencement	During First Year
I. Exchange Rate, Trade and Incentive Policies		
Exchange Rate.		
1. Initial discrete devaluation	X	
[2. Review formula for crawling adjustments to exchange rate to allow margin for changes in real rate as well as reflecting domestic - international inflation differentials.]	X	
[3. Adjust Naira value regularly (monthly) on basis of revised formula.]		X
[4. Allocate 5 percent (at least) of oil export proceeds to second tier foreign exchange market.]		X
Import Controls and Taxes		
1. Modify customs tariff schedule, narrowing rates to 15 to 35% range (with clustering in narrower band of 20 to 30%).		X
2. a. Liberalize import controls on raw materials and spare parts through their transfer to open general licence status.		X
b. Formulate a plan for the phased liberalization of remaining import restrictions.		X
Internal Trade Controls and Taxes		
1. a. Relax ex-factory price controls on all goods.		X
b. Formulate approach for shift to crop pricing structure which reflects market forces. Re-examine role of the six commodity market boards to setting of support prices for domestic crops (ATPG to be responsible.)		X
c. Adjust petroleum product prices in line with exchange rate adjustments.	X	X
2. a. Restructure excise tax on ex-factory production of all goods to fall within range of , say, 5 to 25%.	X	
b. Apply additional excise taxes to both locally produced and imported luxury goods (say, 50 or 100%).	X	
Export Incentives		
1. Review and modify appropriate customs drawback scheme and other fiscal export incentives with aim of ensuring (with some exceptions) (i) exemption (or equivalent) from tariffs and excise taxes on inputs directly and indirectly incorporated in export production; (ii) compensation for discriminatory effect of import protection regime and exchange rate policy on value added in non-oil export production; (iii) simplication of the fiscal export incentive package and of its administration. Appropriate incentives for export traders would form part of this review.		X X
Investment Incentives		
1. Carry out studies to finalize coverage, design and administration of a package of fiscal investment incentives (under taken jointly by the teams involved with ITAP and ATPG).		X
2. a. Commence work to improve operations of the existing Industrial Development Coordinating Division of the Industrial Policy Review Body (to become effective one-stop shop for industrial approvals and investment promotion).		X
b. Review and amend, where necessary, investment policies and guidelines to promote desirable foreign investment. This would include increased ownership flexibility in some areas.		X

Policy Action	At Commencement	During First Year
II. Public Expenditure Policies		
1. Maintain restraints on public sector wage increases and extend freeze on recruitment to all but the most critical skills.	X	X
2. In 1987 budget, reflect move to (i) restore levels of supplies nature and manpower; (ii) give priority to routine and periodic maintenance over new investment; and (iii) further reduce in transfers to commercially-oriented parastatals (basis to be agreed within context of a rolling budget - see 4 below.)	X	
3. Agree on restructured public investment program with context of sector strategies and (i) specify principles for the setting of priorities for completing ongoing capital projects; (ii) re-assess ongoing and proposed new projects (with completion costs over ₦30 million) against these principles; and (iii) categorize projects into "core", "reserve core" and "non-core" within context of agreed budget constraints and incorporate into rolling budget estimates.	X	
4. Adopt a rolling multi-year budget. Begin with a two year rolling budget.	X	
III. Public Enterprise Policies		
1. Prepare a Statement of Policy on Public Enterprises.	X	
2. Restructure and strengthen Ministry of Finance Incorporated (MOFI) to effectively support the Ministries in planning and executing public enterprise reforms.		X
3. Within the context of sector strategies (see V - sector policies) carry out a rationalization program for parastatals.		
a. Classify parastatals according to whether they should be left largely unchanged, restructured, privatized or liquidated. Indepth studies required for some enterprises.	X	
b. Establish priorities and timetable for rationalization.	X	
c. Prepare and commence implementation of restructuring sub-program building into it: (i) increased autonomy of public enterprices in making operating decisions (management, procurement, staffing, etc.) and improved accountability; (ii) further autonomy of public enterprises in setting tariffs and prices (where relevant); (iii) improved accounting practices, financial controls and management in public enterprises; and (iv) rehabilitation requirements.		X
d. Prepare and commence implementation of privatization and liquidation sub-program.		X

Policy Action	At Commencement	During First Year
IV. Financial System Policies		
1. Prepare program for restructuring the financial sector. To include means to: (i) reduce barriers to entry; (ii) encourage branch expansion in rural areas; (iii) further develop capital markets as a source of long-term finance; and (iv) improve existing agricultural credit delivery system.		X
2. Adjust interest rates to reflect positive real and scarcity yields.		X
3. Simplify further credit allocation system: (i) aggregate ceilings; and (ii) replace monthly reports with semi-annual reports.		X
V. Productive Sector Policies		
1. Prepare strategy for agricultural sector.		
a. Prepare statement of policy on agriculture and water resource development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.	X	
b. Create the ATPG to carry out necessary studies on agricultural product prices, marketing and incentives.	X	
2. Prepare strategy for oil and gas sector. Prepare statement of policy on oil and gas development, incorporating principles for public investment, and parastatal operations in the sector.	X	
3. Prepare strategy for the manufacturing sector.		
a. Prepare statement of policy on manufacturing development, incorporating principles for public investment, recurrent expenditures and parastatal operations in the sector.	X	
b. Designation of high level interministerial body for guiding and counseling the trade and incentive policy reforms (for both manufacturing and agriculture).	X	
c. Industry studies for refineries, petrochemicals, steel and pulp and paper to be carried out as part of the work of ITAP, with aim of: (i) identifying and formulating measure to overcome regulatory constraints and market imperfections affecting efficient development; (ii) reassessing approach to public involvement in the industries (as appropriate; and (iii) providing information base for promotion of private investment.		X

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

→ Nigeria RB.

DATE February 4, 1986

TO See Distribution Below

FROM William Humphrey, Division Chief, WAlNI

EXTENSION 78058

SUBJECT NIGERIA: Baker Initiative Country Report

1. It is proposed that the first draft of the above report be circulated for comment and discussion sometime during the week commencing February 17, with the aim of producing a final draft by March 7. The report will then be subject to review by Mr. Husain followed by Mr. Stern.

2. The proposed outline for the report is attached (see Annex A). The Main Report is expected to be 15 to 20 pages, supplemented by a limited number of concise annexes.

3. In preparing the report, the Nigeria Division is receiving valuable assistance from the various interested Departments in the Bank. It has also embarked on a series of informal, working level consultations with the Fund. Throughout the course of the forthcoming two weeks, it is intended to circulate some background working papers with the aim of soliciting early comments and views to be incorporated into the first draft of the report. The topics to be covered by the Working Papers and their expected circulation dates are attached (see Annex B). The first of the working papers is enclosed.

4. The tight timetable is dictated by the need for early action. Please feel free to make comments, verbal or by memo, on any of the papers. These comments could be directed to Tom Allen (extension 78056).

Attachments

Distribution:

Messrs. O'Brien, Eccles, T. Husain, Choksi, Obidegu, Rischard, Rajapatirana.

Cleared with & cc: Mr. Isenman.

cc: Messrs. Alisbah, Isenman.

TAllen:pm

DRAFT

Annex A

Nigeria: Baker Initiative Country Study

Draft Outline of Report

(See also Working Paper No. 1)

Main Report (15 to 20 pages)

1. Recent Economic Developments (2 to 3 pages)

1.1. Macroeconomic Performance
1.2. External Debt
1.3. Policy Issues and Response

- o Stabilization
- o Structural
- o Directions for Reform

2. Medium Term Adjustment Program (10 to 15 pages)

2.1. Objectives and Requirements

- o Growth and External Debt Objectives
- o Implications for Investment, Savings and Exports

2.2 Adjustment Policy Package

- o Demand and Debt Management Policies
- o Exchange rate, Trade and Incentive Policies
- o Public Expenditures Policies
- o Public Enterprise Policies
- o Financial System Policies
- o Sectoral Policies

2.3. The External Financial Package

- o Finance Requirements
- o Financial Restructuring Options
- o World Bank Lending Program

2.4. Institutional Responsibilities and Monitoring

- o Role of Institutions
- o Monitoring Requirements - Procedures

3. Impact of the Adjustment Program (2 pages)

- o Economic Performance without Medium Term Adjustment Program
- o Economic Performance with Medium Term Adjustment Program

Annexes (all very brief)

A. Matrix of Policy Actions over Adjustment Program Period
B. Matrix of Policy Actions in First Year of Adjustment Program Period
C. Sector Programs
D. Bank Lending Program
E. Macroeconomic and Financial Assessments - Parameters and Results

Annex B

Nigeria: Baker Initiative Country Report

Series of Working Papers to be Circulated

Working Paper No. 1: Nigeria - Parameters for Report

Executive summary of parameters for and of conclusions to emerge from the report.
(Circulate February 4).

Working Paper No. 2: Nigeria - Adjustment Policy Package

Nature and phasing of policy reforms over the five year adjustment period.

Annex A: Matrix of Policy Actions over Adjustment Period.

Annex B: Matrix of Policy Actions in First Year of Adjustment Program.
(Circulate February 5).

Working Paper No. 3: Nigeria - The Financial Package

Financing requirements and restructuring options.
(Circulate February 6).

Working Paper No. 4: Nigeria - Macroeconomic Assessments

Economic Performance with and without Medium Term Adjustment Program.

Annex A: Assumption and Results for Base Case.

Annex B: Assumptions and Results for Policy Case.
(Circulate February 7)

Working Paper No. 5: Sector Programs

Agriculture
Industry
Energy
Other Sectors
(Circulate February 10)

Draft
PIsenman/TAllen:pm
Job: Baker Report
Disk: ALLEN
February 3, 1986

NIGERIA: BAKER INITIATIVE COUNTRY REPORT

Working Paper No. I

Overview of Themes for the Report

1. Nigeria stands at the crossroads. It has found the political will for austerity and, in its new budget, even the political will to make a strong beginning on structural change. But it has made the decision not to reach an agreement with the Fund, which has become an issue of political pride; this, though, is considered essential by the Paris and London Club financiers before they would agree to a rescheduling of Nigeria's considerable external debts to them. While Nigeria could unilaterally reschedule the debts, such a step would cut off access to the additional new funds needed to support structural reforms and to establish firm foundations for future growth. It is also unclear how long Nigeria would stick to a major and largely unpopular reform program in the absence of some broader compact with the international community and of Fund surveillance. The depressed oil markets make the situation more urgent.

2. Our recommended strategy calls for working with the Nigerian Government to build on the initiatives they have already taken and embrace a more comprehensive adjustment policy package aimed at renewing growth and improving creditworthiness, although it would be perhaps a decade before the full fruits of the program are observable. To facilitate the mobilization of the necessary financial support to implement the package over the medium term, we would encourage the Government to enter into a dialogue with the Fund as soon as is feasible, and encourage all the parties concerned to be flexible concerning the form of an acceptable Government/Fund relationship.

3. Policy Package. The policy package is a comprehensive and detailed one, based on a substantial amount of ESW and previous SAL preparation. It is aimed at increasing the efficiency of resource use, stimulating non-oil exports and improving savings and growth. It builds on the extensive initiatives already taken by the Government in the new budget and focuses principally on: (i) correcting the grossly misaligned prices through reforms in exchange rate, trade and incentive policies; (ii) overcoming the considerable public sector inefficiencies through restructured public expenditures and the rationalization of the parastatal sector; (iii) reducing the severe imperfections in the financial system through less Government intervention in the operations of financial markets and improved financial intermediation; and (iv) removing the constraints which discourage private initiative and inhibit supply responses to favorable market conditions. Poverty issues are addressed partly through

the public expenditure and agriculture programs and partly through the effects of growth on employment, incomes and Government programs. The principal substantive issue will revolve around the desirable speed of devaluation and import liberalization, which will be central to any agreement with the Fund.

4. Financial Package. To meet reasonable growth and creditworthiness objectives, the Government will require additional external financial support both through a rescheduling of its existing debts with the Paris and London Clubs financiers and through new money commitments (including World Bank quick dispersing loans). In order to keep new money requirements within feasible limits, consolidation of a group of maturities under a multi-year rescheduling would be necessary (e.g. through a two step NYRA). However, Nigeria's abnormally large trade arrears pose difficulties in keeping new money requirements to reasonable levels (noting the level of legitimate trade arrears outstanding is still uncertain), while the uncertainties in the oil market require some 'cushion' in new money requirements.

5. The Two Major Policy Scenarios. We see the current period of internally generated policy reform (but of uncertainty regarding the implementation of a full policy package blessed by the Fund) as lasting about 12 to 18 months. We think it would take a minimum of 9 to 12 months for Nigeria to be willing politically to reach an agreement with the Fund. On the other hand, we see 12 (perhaps 18) months as the maximum time that the reformers in the Nigerian Government can maintain the pace of reform without external financial support. By that time, if not sooner, the other political and economic influences on Government, which have led to poor economic policies for a number of years, would be likely to have reasserted their influence and policies would be likely to have deteriorated. Thus, our reform and non-reform scenarios remain the same for the first 12 months. After 12 months, the two scenarios diverge. In the Policy Scenario a full policy package is undertaken, accompanied by substantial multi-year rescheduling from creditors and a substantially expanded Bank program. In the Non-Policy Scenario pricing and other policies gradually deteriorate, leading to lower efficiency, lower external capital flows, lower savings and lower growth. This is a case of gradual deterioration, though, not a "scare" case. We also do various sensitivity analyses, such as a Fund-blessed program but without Fund lending and lower oil prices.

6. Bank Lending Program. To encourage the Nigerian Government to maintain the policy progress begun under their new budget, we would keep up a reasonable project lending program of around $400 million per year. We should still, though, be cautious on commitment and would give the Government roughly 12 to 18 months to work things out. Of course, if policies deteriorate sharply before 12 months, we would have to react accordingly. This would consist of cutting down our lending to a notional core program of about $200 million per year, partly because of concerns about creditworthiness and partly as a strong signal in the policy dialogue. If the momentum for policy reform continues, the Bank would be ready to put in place quick disbursing 'program-type' assistance such as a second fertilizer loan. If a full medium term adjustment program is

embraced, we would be ready to increase our lending program substantially (to near $1 billion per annum), including a series of SAL's.

7. The Next Steps. We plan to build on the on-going policy dialogue we have had with the Government, and seek their reaction to the adoption of a medium term adjustment package along the lines to be outlined in the Report. We would continue our efforts to convince them of the necessity of having some form of agreement with the Fund and explore means through which this could be achieved. We need to approach the Fund at the highest level to get them to cooperate to the extent feasible, and sound out with them (and the Paris and London Clubs) alternative approaches which recognize the sensitive issues involved. We would in any event counsel the Nigerian Government on what is needed to continue the progress it has already made, even if neither the Government or the Fund are yet willing to indicate a willingness to get together on terms acceptable to each other.

→ Nigeria RSB

February 11, 1986

Mr. Paul Isenman, WAIDR

Dear Paul,

Thank you for your note.

There seems to be a major difference in our viewpoints -- perhaps one worth discussing at length. On the surface, the difference concerns how much "commercial" (including IMF upper traunch) balance of payments support Nigeria can usefully absorb in the next few years. At a second level, our difference seems to relate to what constitutes evidence of the occurrence of economic adjustment as opposed to evidence of adjustment of policies and intentions only. At a most fundamental level, I feel we differ on how important higher domestic interest rates and less corruption are to the successful use of "expensive", balance of payments support.

If I may make the usual distinction between "domestic" and "foreign" resources, Nigeria's problem is a poor allocation of domestic resources. Until this improves, and we need hard evidence that it has, Nigeria cannot make good use of expensive foreign resources. It is most important that incorrect incentives which still exist in economy, that is, those causing the major misallocation of domestic resources, be removed. Two most serious causes for such distortions are low domestic interest rates and excessive corruption. If real interest rates were to rise, importantly by reducing public deficits and reforming the financial system, and corruption decrease, I feel sure you would see a much better allocation of domestic resources in Nigeria. Evidence of

improvements in allocation would be: (i) a shift toward investment in working capital for increasing capacity utilization, and (ii) a decrease in government investment, or more importantly, in the cost of government investment projects. Since much of the working capital is for imports, evidence of (i) would include relatively more imports going to working capital. This would probably require a price allocation system for foreign exchange although, better, less corrupt administrative allocation might also work. Evidence for (ii) would be, at a minimum, a "feeling" that corruption surrounding government investments has decreased. More elaborate financial tests might include showing that a government procurement price index has declined and/or demonstrating that yields on government investments have risen considerably.

It is important to note that my main concern is Nigeria's ability to absorb "commercial", balance of payments support over the next few years; that is, until adjustment has occurred. After adjustment, or, after evidence of improvements in domestic resource allocation has surfaced, absorptive capacity will probably be quite high.

I do not downplay the beneficial role which a significant amount of Bank project lending could play even in the present, unadjusted circumstances. As long as new Bank projects are "financially free-standing" or not dependent on the government budget and foreign exchange allocation systems for finances, they will most likely help in both the adjustment and growth processes in Nigeria. There is, therefore, a large scope for Bank lending activity for projects, as long as they are productive and have sufficient user charges and covenants

regarding foreign exchange availability so that financing needs can be obtained outside of the government budgetary process. There is an interesting exception to this last point about removing dependency on recurrent budgetary support. Bank projects would benefit if they receive a government capital grant through the budget, "up front" or at the start of the project.

Sincerely,

Bob

Bob Myers.

cc: F. S. O'Brien (WANVP)
W. Humphrey (WA1NI)
L. Squire (CPDRM)
A. Choksi (CPDTA)
T. Allen (WA1DR)

RM:cmb

→ Nigeria RB

January 22, 1986

Note to Mr. Myers.

Bob,

I have read with great interest your paper on domestic adjustment and foreign borrowing in Nigeria. It really makes one stop and think to read that "new external commercial borrowing, including that obtained via rescheduling will probably be low or nil for the next few years". I assume that you have purposely overstated your conclusions to reemphasize the important policy point you want to make on avoiding excessive external borrowing. Sometimes, though, a good point can be carried too far by excluding other relevant points. I hope you would agree with me that the objective of borrowing is increased present value of output (setting aside borrowing for health, etc.) -- whether that comes from increased investment or through increased output from existing capacity. As you know well, a key objective of our structural adjustment programs in Nigeria and elsewhere is to encourage greater efficiency in the use of resources, with an emphasis on increased output from existing capacity.

In further work you do for us or CPD on this issue, you may want to note that borrowing for fertilizer or other current inputs may well have higher returns than borrowing for new investment per se. In addition, you may want to take account of oil price cycles. Both theory and practice suggest that marginal returns to investment and borrowing rise when investment and import capacity are low. Thus, once a structural adjustment program is in place, borrowing whould be counter-cyclical, not pro-cyclical. Oil price prospects will, of course, affect how much borrowing can prudently be afforded. However, the structure of Nigeria's debt and likely prospects for oil markets in the 1990s suggest that the key debt issue for the longer term will not be the debt-service ratio (liquidity), but the economic return on the use of the borrowed funds that you rightly emphasize in your paper. None of this is to say that Nigeria should, even if it could, try to borrow its way out of the income loss resulting from the decline in oil prices. Rather it needs to adjust; and it should be risk-averse in its assumptions about how much of the price decline is cyclical and how long the cycle will be. Still, the basic point about higher returns now remains.

At the present time, stocks of imports are down to very low levels in Nigeria. And, as you know, current over-production is wreaking havoc in oil markets. The point at debate is how far it is prudent -- from the point of view of the present value of growth or of the political stability needed to sustain a reform program once begun -- to cut Nigerian imports further below the more than halving that has already taken place. This is a question that calls for analysis and judgment on a number of difficult issues.

Regarding the focus of the Nigeria structural adjustment program, I have asked Tom Allen to send you a set of documents on this. One might get the misconception from looking at memos on the financing issue alone that the main focus of the SAL/EFF adjustment program was not a comprehensive set of reforms (affecting, inter alia, savings) to get production up and to reduce the inefficiency that has contributed so much to the low returns on investment (and foreign borrowing). Your reminder on the importance of the savings issue is timely, though, now that we will have to increase our emphasis on interest rates and other issues that were to have been handled primarily by the Fund.

Paul Isenman

cc: Messrs. W. Humphrey (WAINI)
L. Squire (CPDRM)
A. Choksi (CPDTA)
T. Allen (WAIDR)

Draft
R. Myers
1/10/86

DOMESTIC ADJUSTMENT AND FOREIGN BORROWING IN NIGERIA

INTRODUCTION

1. This note sets out a vision of what a restructured, but internationally integrated Nigerian economy would look like in about 20 years'time. It assumes that the ultimate goal of Nigerian governments (Federal and State) is to use policy variables and foreign borrowing to improve Nigeria's per capita consumption over the long-run. The paper begins with a quick summary of the basic principles applicable to adjusting the domestic economy so as to make optimum use of future foreign borrowing opportunities. Two points are crucial: first, the governments should focus much more on adjusting domestic saving to investment and foreign borrowing targets; second, in establishing these targets, the government should use the fundamental principle that returns to investments, at the margin should be equal to an upwardly adjusted marginal cost of foreign borrowing. The adjustments to the marginal cost of foreign borrowing will raise its domestic cost above the international interest. This will reflect possible exchange rate depreciations and the extra risk which the country as a whole undertakes when private individuals borrow.

2. The country's past experiences with domestic policy and foreign borrowing are then reviewed. The government did not control external borrowing so that its costs (interest rate) were below the marginal benefits or yields on domestic investments. As a result, the country overborrowed, or, in other words, governments' management of the

domestic economy was inconsistent with the amount of foreign borrowing undertaken by the country.

3. The third section of the paper presents a discussion, item by item, of the likely developments in Nigeria's major structural parameters. The main conclusion, derivable from this section, is that current discussions on adjustment and foreign borrowing by Nigeria place relatively too much emphasis on the importance of exchange rate devaluations and immediate inflows of greater amounts of external loans. The significance of upward adjustments to domestic interest rates and of improvements in the country's, and particularly the Federal and State governments', domestic saving efforts are, conversely, underemphasized. If the policy focus is redirected somewhat toward the latter issues, new external commercial borrowing, including that obtained via rescheduling will probably be low or nil for the next few years. It could rise significantly thereafter, however, if changes in domestic policies and the government's planning procedures are enacted.

Basic Principles

4. There are two basic principles, one relating to ensuring that there are welfare gains from foreign borrowing and the second concerning ensuring that the country is always creditworthy in foreign lenders' eyes. Regarding the first, foreign borrowing will increase welfare and consumption if the real marginal benefits from investments to be financed with such borrowing are below real average benefits in the economy but above the real marginal cost of foreign borrowing. This marginal, or basic investment and borrowing rule applies both to the

public and private sector and to both domestic and foreign borrowing. Unfortunately, correct application of this basic rule is very difficult when foreign borrowing is involved. The real social cost of foreign borrowing is affected by real international interest rates, exchange rates and divergence of social from private costs of foreign borrowing. This divergence plus the likelihood of a devaluation over a "borrowing cycle" means that the domestic cost of foreign borrowing will be significantly above real international interest rates.

5. Ensuring continuing creditworthiness is ultimately dependent on the success of applying the first, or basic investment and borrowing rule. For any particular period or loan, however, creditworthiness is not so much affected by the first principle as by the ability of a borrower to mobilize the resources needed to service debt. Thus, even unwise borrowing (that for which the marginal benefits are below the marginal cost) must be serviced by tradeable resources obtained from somewhere. This second principle applies, therefore, to borrowers' ability to save, or to raise, via pricing, taxing, or domestic borowing, the tradeable output needed to service foreign debt.

6. A sensible approach to simultaneously carrying out these welfare and creditworthiness principles is to adopt some long term investment and foreign borrowing targets and then adjust domestic savings, or the capability to mobilize resources domestically, accordingly. The former can be done using knowledge of a country's investment characteristics, including rough notions of average and marginal yields. Establishing foreign borrowing targets involves first

estimating the long run average and marginal real interest cost of the foreign loans likely to be made available and then imposing a sensible long run "cap" or debt to GDP target. This long run debt/GNP target can then be used, alone with shorter term fluctuations in the yields on investments and costs of foreign borrowing to establish appropriate paths for annual current account deficits and domestic savings.

Past Foreign Borrowing by Nigeria

7. Between 1973 and 1983 the dollar value of Nigeria's current account deficits, net of surpluses, was $23 billion. Of this total increment in foreign liabilities about half can be accounted for as having been borrowed by the Government and/or taken over by the Central Bank from the private sector. During this period Nigeria's terms of trade improved dramatically, a situation which normally does not call for such large increments in foreign debt. Nigerians adjusted expenditure expectations upward even faster, however. It therefore appears that the borrowing was not undertaken as a result of a specific plan or strategy, but in order to finance a very rapidly expanding investment program in the face of lower than expected oil revenues. In contrast to most other developing countries, nearly all of this borrowing occurred between 1978 and 1982 at variable commercial interest rates. This caused Nigeria's real interest cost to rise to extremely high levels as real international interest rates rose.

8. Nigeria's past application of basic investment and borrowing rule was poor and/or non existent. This meant that welfare gains from such borrowing were low, or more likely, negative. Rough aggregate data

for the country as a whole suggest that the marginal benefits from investment and foreign borrowing were well below the marginal cost of such activities. Real marginal rates of return for 1975-80 were about 3%. Although initially negative, real interest rates rose quickly to 15%-20%, or well above the rates of return to investment. Real borrowing costs were even greater than 15% to 20%. Strict quantitative limits on oil exports ensure that increments in debt service must now be paid with domestically produced non-oil tradeable output. Domestic prices of this output have risen significantly, both compared to former levels and compared to the prices of non tradeables. This depreciation in the real exchange rate has further raised the cost of debt servicing above the real international rates facing Nigeria.

9. The real cost of foreign borrowing apparently exceeded real returns to investment throughout the economy, and particularly across both the public and private sectors. This latter suggests the counterintuitive result that even the private sector did not or could not correctly apply the basic borrowing and investment rule. Also, in both sectors, investment was heavily concentrated in the production of non tradeables. Apparently, returns to these investments, though low, were much higher than those for tradeable investments. Because of this it is likely that the real exchange rate depreciations required to capture tradeable output for debt servicing will be very significant.

10. The overborrowing, or incorrect application of the basic investment and borrowing rule seems primarily to be the responsibility of Government planners. Managers of the economy or plan implementers,

to the extent that they are different from planners, are also culpable. For the public sector the extent by which the cost of foreign borrowing exceeded the benefits from investments was partly the result of the low yields on public investments. These yields appeared to have been low both because too much public investment was undertaken and because of poor project choice. The excessive levels of public investment severely strained the public sector's absorbtive capacity thus lowering the returns even for those projects which would have had higher rates of return if they had been undertaken sequentially. Planners seem not to have considered this "adding up" problem. Instead they assumed that the yields on each project separately would be achieved no matter how many projects were undertaken simultaneously. Poor project choice was also significant and occured because non economic criteria, such as political motives, potential for personal gain, etc., prevented selection of those projects with the highest rates of return.

11. Public sector overborrowing occured for two additional, important reasons. There appears to have been little appreciation of the cost of the public investment resources generated via (oil related) taxes and foreign borrowing. In addition, the need to improve the resource mobilization facilities of the Government as foreign borrowing increased was not appreciated. Since Nigeria's oil is an exhaustible resource, sold internationally, planners should have considered the long-run opportunity cost of leaving it in the ground to be equal to likely long-run real international interest rates. This point was not

appreciated by Nigeria's planners. Neither was the link between public resource mobilization capabilities and the extent and maturity structure of foreign borrowing. Creditworthiness cannot, at all times, be maintained unless the Government has the capability to obtain tradeable output to service debts even when the output stream from investments financed by foreign borrowing is delayed and/or insufficient. This lack of appreciation of the limited capability to expand Government resource mobilization has, in fact, led to the present debt service crisis.

12. All these problems, except the last or resource mobililzation one, befell the private sector as well. Inattention by the private sector to the importance of these issues does not appear to explain this, however. Instead distorted price and cost incentives led the private sector to overborrow from abroad. The primary reason for these price distortions is the absence of effective price competition. This is, in turn, due to Government policies and practices which prevent or do not encourage price competition. Government procurement procedures, for instance, result in excessive financial profits for suppliers. Even though some of these profits may be used for gratuities, the effect is to transfer oil revenues and foreign borrowing to the private sector for non productive behavior. Government's behavior as a supplier is also non-competivite. Most Government services are sold on a cost plus (or more usually cost minus) basis. Effective prices charged by the Government, or prices adjusted for low collection of revenues, are lower

still. Together these result in an enormous transfer of purchasing power to the private sector.

13. The absence of price competition both within the private sector and between the private and Government sectors has created the distortions to private incentives. Financial returns, particularly to non tradeable output such as trading activity, construction and other services are well above the real returns to such activities. Financial costs, on the other hand, many of which the Government controls, tend to be well below true resource costs. This is particularly true of the domestic cost of credit and foreign exchange both of which are allocated administratively.

14. Pervasive distortions have led the private sector to overborrow from abroad. The sector has, however, succeeded in shifting the cost of the real losses resulting from this overborrowing to the Government. This has occurred because the Government has accepted the responsibility to repay external arrears. The private sector will continue, as it has in the past to treat foreign debt similarly to domestic debt and to repay it with domestic currency. The build-up in arrears occured when foreign debts were settled in domestic currency terms but not in tradeable output. Now, the Government must repay these arrears with tradeable output the domestic cost of which has increased considerably.

15. Distortions and lack of price competition in Nigeria have had a particularly devastating effect on the real returns to investment in the last two years. During this time, investment cutbacks have centered heavily on working capital investment instead of on investment in fixed

plant and equipment. Variations in working capital investment cause changes in capacity utilization of existing plant and equipment. Such investment should ideally be financed domestically and would, in perfectly functioning credit markets, always have higher real yields than investment in new plant and equipment. As a result, in a competitive system, existing producers could compete the credit away from those desiring it for new plant and equipment. Imperfections in Nigeria's credit markets have prevented this from occurring thus providing an exceptional argument for financing working capital from abroad. This borrowing would finance the highest yielding investments presently available but would not increase the welfare of the country. Instead, the borrowing would minimize the losses associated with poor investment in plant and equipment in the past.

16. The inadequate application of the basic borrowing and investment rule in Nigeria has lowered potentially achievable consumption to levels which are probably below those which would have occurred without so much foreign borrowing. This need not have caused a debt service crisis had the country's ability to mobilize and use resources been flexible enough to lower consumption in order to obtain the tradeable output needed to service the debt. For the Government increased taxes or domestic borrowing could have accomplished this. Alternatively, if additional revenues could not be collected, the Government might have decreased public consumption in order to accommodate larger debt service payments. Unfortunatley, as with the first principle, the requisite matching of the ability to adjust

consumption with the extent of foreign borrowing did not occur. One reason for this was that the Government's debt recording and processing procedures were so poor that the domestic financing requirements of a mounting foreign debt were obscured. A second reason was a lack of appreciation of the limited ability to lower consumption by capturing domestic product for debt service payments. These limits exist in both the fiscal (Federal and State) and financial systems. Fiscally, domestic taxes, even for petroleum, can/will not be raised sufficiently. Financially, neither domestic interest rates nor government bond sales are high enough to have much of an impact on private sector savings.

CHANGES IN BASIC STRUCTURAL PARAMETERS

The Appropriate Time Horizon

17. It is likely that twenty years is a more appropriate time horizon than two or five years for a domestic adjustment and foreign borrowing program. This is not because it will take twenty years to implement improved policies. Instead, this longer time period is a more realistic estimate of the amount of time it will take for policies implemented over the next three to five years to become fully effective.

18. The longer time horizon could also enable avoidance of policies, based on a short time horizon, which might make matters worse later on. For example, Nigeria might react to past overborrowing by borrowing, more, for instance, via rescheduling agreements, without making significant domestic policy reforms. Such borrowing or

rescheduling might lessen reductions in consumption in the short run, but might be very costly in terms of much larger amounts of consumption which will have to be foregone in the future.

The Foreign Borrowing Target

19. The foreign borrowing target or desired debt (DOD)/GDP ratio is established in order to give a notional indication of appropriate current account deficits over time. This foreign borrowing or DOD/GDP target should be a sensible one based on Nigeria's investment opportunities, likely cost for foreign borrowing and capacity to increase domestic savings. If real interest costs on foreign borrowing average four percent per year for Nigeria, or somewhat above the norms for LDCs generally, then a sensible DOD/GDP target for Nigeria for 2005 is about 30% - 40%. This is about what the ratio is now. Therefore, such a target implies an average current account deficit each year of one third of the GDP growth rate. Thus, for example, a long run GDP growth rate of three percent per year implies that DOD also grows at 3 percent or that current account deficits average one percent of GDP each year given that the DOD/GDP ratio is to remain about 35 percent.

20. More important from a short term policy perspective is the appropriate path of current account deficits. For most countries, including Nigeria, it is not particularly sensible to adopt a single target for the current account deficit/GDP ratio. Establishing a single target, or a straight line path for current account deficits ignores the fact that there will be fluctuations in the yields on Nigeria's marginal investments and in the domestic cost of foreign borrowing. It also

ignores present lender imposed credit constraints and the possibility of future domestic or external shocks to the economy. It is, therefore, more appropriate for Nigeria, in the absence of shocks, that current account deficits be below this norm for the next several years. Thereafter, they can be above the norm, i.e. greater than one third of increments in GDP, as long as adjustments to the domestic economy have occurred. A borrowing path which is at first below and then above 30 percent of the growth in GDP would recognize the existence of lender imposed credit constraints and the fact that the impact of adjustments to domestic economy will not occur immediately.

Domestic Interest Rates

21. Policy adjustments should cause real domestic interest rates in Nigeria to both rise above international ones and play a bigger role in allocating credit for investment. The simultaneous occurrence of both of these will signal improvements in yields on investment and indicate that welfare gains from foreign borrowing are possible. More sophisticated and efficient domestic financial markets and government controls on external capital flows are necessary conditions. If the domestic financial system is liberalized, domestic interest rates should rise, as long as credit goes to higher yielding investments. Accomodating government monetary and fiscal policy is also needed, however.

22. The appropriate level of domestic interest rates depends on likely average real international interest rates which will face Nigeria. It was previously estimated that these would average about

four percent over the next 20 years. To this rate should be added the impact of likely real devaluations of the Nira and a margin to reflect the fact that the social costs of foreign borrowing exceed the private ones. Even though much of the real depreciation of the Nira appears to have occurred already, it is likely over the next "borrowing cycle", or twenty years, that some further depreciation will occur. In light of this, real domestic interest rates of something like 7 to 8 percent seem to be a reasonable target.

Yields on Investment in Plant and Equipment

23. Yields on investment in plant and equipment must rise. This should occur partly because of fewer, better planned government investments. Lower capital/labor ratios for new investment, if coupled with wage restraint, will also be a factor. Over time, private investment will most probably increase relative to public investment and become more productive. This is based on a presumption that there are a large number of high yielding investments in Nigeria which are currently not undertaken. Financial distortions, a lack of incentives and/or the presence of disincentives, and poor credit allocation have discouraged private investment and/or directed it to areas in which the real returns are low. Removal of these problems should encourage private investment in higher yielding ventures.

24. The implications of the above discussions on likely real foreign and domestic interest rates is that real yields on marginal investment in Nigeria should be about eight to nine percent. Yields on intramarginal investments should be above this so that the average

yields on investments approximate something like twelve percent. A rough rule of thumb (taken from an empirical study in Senegal) is that about 40 percent of the reciprocal of sectoral ICOR's represent the real rate of return to investment in those sectors. Although this percentage would vary somewhat with the captial/labor ratio, it appears to be a good approximation for yields in Nigeria. That is, this rate (0.4/ICOR) if coupled with an ICOR of 5 would imply a real yield on the marginal project of 8 percent or about equal to real domestic and adjusted foreign interest rates. Yield on intramarginal projects should be above this so that average yields are on the order of 12 percent. This implies that Nigeria's ICORs for investment as a whole should average between 3 and 3.5.

25. This discussion of the adjusted real cost of foreign borrowing and target marginal and average yields for investments has assumed significant devaluations of the real exchange rate. This suggests that real yields on tradeable investment will improve significantly so that the investment pattern will shift toward more tradeable investments. In light of this, one would expect over the twenty year period the ratio of non oil tradeable to non tradeable investment to rise significantly. It is not clear, however, that non oil tradeable investments should be concentrated heavily in foreign exchange earning exportable production. Certainly investments of this type would have the largest impact on Nigeria's future creditworthiness. However, given the fact that Nigeria has a large domestic market, it is not clear that price incentives will favor export projects over investment in import

substitution industries. It is not possible, therefore, to be categorical about the likelihood that increments in non oil tradeable production will concentrate in the export sector.

Domestic Taxes

26. Two important structural changes should occur to the country's domestic tax system. First, the Federal and state governments should adjust taxes so that their consumption and debt servicing requirements are completely covered by recurrent revenues collected in a non distortionary fashion. Second, the Federal government should impose a tax on foreign borrowing by state governments and the private sector in order to accurately reflect the true social cost of such borrowing. The long run structural significance of the first point is that Nigeria's tax system will shift away from dependency on imports and oil exports and toward taxation of income and/or private domestic consumption expenditures. These taxes should began to replace taxes on oil exports in importance. Oil export derived revenues may decline if prices and/or volumes fall, but, in any event should be used more and more either for investment or for foreign debt service payments rather domestic consumption. The extent to which oil export tax revenue is used for domestic investment vs external debt service payments will depend on whether higher yielding investments in tradeables are for export or import substitution. If the latter, then virtually all oil revenues will have to be used to make debt service payments on external debt.

27. Desirable structural changes in the tax system would not only reduce the distortions of the present system but also increase the

levels and flexibility of government saving. Given the strong relationship between fiscal and current account deficits, control over government saving is the primary way that the Federal government can ensure that general purpose foreign borrowing will be used primarily for financing domestic investment rather than consumption.

28. Imposing a tax or on-lending wedge on foreign borrowing by state governments and the private sector would be significant addition to the Federal government's fiscal responsibility. The tax is important for reducing the volumes of foreign credits borrowed by these units. The revenue should ideally cover the risk of default which the Federeal government bears on behalf of state and private borrowers. In the absence of specific quantitative notions of what this risk is, it is probably appropriate to began by imposing a tax or on-lending wedge of one percentage point in real terms. This could be adjusted depending on experience. Such a tax or on-lending wedge would also increase the accuracy of debt recording in Nigeria, thus improving the likelihood that future debt servicing requirements can be anticipated and adhered to.

Anyone, → Co. Study Box.
Gobind left this. Looks going to be Their contribution to the debt study.
Bob Myers

Draft
GNankani:pm
Job: LC Paper
Disk: GN1

NIGERIA

Loan Committee Paper
Pre-Summary

1. Revised analysis of oil prospects, arrears and imports implies that an expanded World Bank package combined with a standard IMF package for 1986-87 would imply a net gap for rescheduling/new money of about $4.5 billion, and a similar gap of $3 billion in 1988-90, totaling $7.5 billion. Without IMF funding, but with expanded Bank lending (i.e. $6.3 billion commitments - 1986-90), the total gap would be about $8.5 billion, with $5.5 billion of it needed in 1986-87.

2. Preliminary analysis suggests that about $5 billion could be raised through reschedulings leaving $3.5 billion for additional money from the IMF and commercial banks. Of this latter amount, an insignificant amount would be needed in 1986-87. This assumes core real imports at $6 and $7 billion for 1986-87, and $7.5 billion thereafter (adjust for imports in current dollars).

3. Therefore, a workable package could be:

i) Major policy reforms in the areas of exchange and trade policies, public expenditure policies, financial sector reforms, public enterprises, public sector management, key pricing policies and continued fiscal/monetary restraint,

with clear agreement on their design, levels and timing for the 1986-87 period, and broad agreements for the 1988-90 period.

ii) An expanded World Bank lending program for 1986-87 (at a level of $6.3 billion for 86-90);

iii) three year rescheduling of Paris and London Club debts, with the third year requiring re-validation; similar terms for uninsured arrears;

iv) IMF 'green light' plus, if acceptable to Nigeria, IMFSBA (for additional import financing).

v) No new commercial bank lending in 1986-87; new lending may be warranted in 1988-90 depending on policy reform and oil developments;

vi) ECA lines of credit consistent with above import levels.

4. Further analysis of the above package may reveal that new money may be necessary even in 1986-87, but this appears unlikely at present.

5. The action plan following from the above would be:

i) Allow for a modest increase in World Bank lending

conditional as policy actions in 1986-87, and policy thrust of reforms in 1988-90;

ii) Completion of an IMF review, allowing Nigeria to avail itself of an SBA;

iii) Major effort at rescheduling;

iv) Continuous monitoring.

THE WORLD BANK/INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

Mrs. Alyssia Stumpf

Ma. Thalwitz

Sounds fine
ES
12/3

B.A
cc G.N ✓
T.A
P.F.

DATE November 25, 1985

TO Mr. Ernest Stern, SVPOP

FROM Wilfried P. Thalwitz, RVP, WAN

EXTENSION 72063

SUBJECT NIGERIA: Balance of Payments Forecasts, Reform and External Financial Support

1. Thank you for your reactions (attached) to my memorandum on Nigeria's balance of payments prospects over the 1986-90 period. They are well taken and consistent with the evolution of our own thinking. As you say, the prospects are indeed dismal and it is fairly clear that our Nigerian friends do not yet realize how bleak the picture is. It is, therefore, important that in our next round of discussion with them, we try to help them understand their predicament, go over again the policy package needed to address their problems and give them some indication of the kind of support they might expect from the international financial community - both in debt rescheduling and new inflows - if they adopt appropriate policies.

2. As you have suggested, we are now preparing a paper for the Loan Committee, covering these issues. We had earlier discussed with Shahid Husain doing a paper on Nigeria along the lines of those being written for Argentina, Brazil, Chile, Columbia, Mexico and Morocco. We will use the same paper for the Loan Committee. We would modify the structure proposed for the other papers in order, as you suggest, to give less emphasis to a five-year financial plan. Instead we would adopt an approach to the problem that is conditional on significant policy reforms plus a commitment on the part of all parties concerned to continue to deal with the problem as we go along. Thus, the overall picture we would be presenting to the Loan Committee would be a revised version of that in the balance of payments memorandum, adding a description of the adjustment package distinguishing between a first stage (two years) for which there would be a detailed adjustment program, and a second stage (three years) for which there would be a preliminary program. In addition to covering policy packages and external financial requirements, the Loan Committee paper would discuss any implications for Bank lending as well as monitoring procedures, Bank-Fund collaboration and lending instruments. ✓

3. On some of the more specific points raised in your note, I would make the following comments at this stage. First, on import data, after we took account of the influences of relative prices and QRs, it became possible to explain satisfactorily the apparent fluctuations in import/GDP elasticities. Even so, we are looking further at the economic consequences of trying to compress imports further. Second, our projections are entirely consistent with the Fund's except on oil prices and volumes. The net impact of these differences on total oil revenues is insignificant. In reconciling our data, there is likely to be little disagreement with respect to Nigeria's oil exports. However,

if the net difference is insignificant, and forecasts are uncertain, why figure

it will not be surprising if we fail to get full agreement on oil price projections, given the uncertainty in which the oil market continues to be shrouded. Third, it turns out that Mr. Agarwala's debt data (dated November 2, 1985) are not defined to include trade arrears, although his most recent data (dated November 5, 1985) do include an estimate of these arrears. Finally, we are working closely with Mr. Wood's staff on alternative workout schemes. They have suggested that it would also be useful to explore alternative schemes involving the trade-off between rescheduling and additional capital needs in a systematic way as has recently been done by FPA for Ivory Coast and Jamaica.

4. Could you please confirm that you think our proposed approach to the Loan Committee paper makes sense. We would aim to get it up by end-December. We also plan, as you suggest, to send an updated version to the OPSC no later than March which would also deal with our levels of lending -- especially if there is no significant movement on policy reform.

cc: Messrs. Alisbah, Humphrey, Isenman, Agarwala, Rischard,
Mrs. Federigan
WAlNI Staff

Attachment

GNankani/WSHumphrey:pt

Attachment

Draft
GNankani:pm
Job: LC Outline
Disk: GN1

NIGERIA

Loan Committee Paper
Annotated Outline

I. Background (BT/RM)

i) A brief statement of the current state of affairs and how Nigeria got into it (1975-85), and how it has responded, so far. (CEM Chapter I).

ii) Describe our 'vision' of a restructured Nigeria, in which oil complements other sectors in the development strategy (see SAL Green Cover, Agriculture, Non-Oil Exports and Oil-Market related reports).

iii) Use (i) and (ii) to identify major policy issues required to establish creditworthiness and resume growth as: exchange and trade policies, public expenditure policies and strategies, financial sector policies, improved public sector performance, pricing policies for key sectors (energy, commodities under boards) institutional reforms relating to the private sector's role and economic management.

II. Balance of Payments Prospects (AD/IA/VC)

i) Overview of macroeconomic projections 1985-95 (growth, inflation exchange rate, investment/savings, exports, imports, debt servicing etc.).

ii) Balance of Payment analysis, with a two-stage approach - identify more certain gap for 1986-87 and a more uncertain gap (a range) for 1988-90. This should address issues of oil, arrears, imports in as refined a way as possible, including for critical ambiguities, some sensitivity analysis (e.g. for $1 premium on oil, international inflation, etc.).

iii) Conclude with an estimate of minimum financing package needed to resume growth in 1986-87, and in 1988-90. Compare to currently expected levels from World Bank, IMF and identify gap that would need to be filled by a combination of debt rescheduling and new lending.

III. Adjustment Policy Package and its Phasing (1986-87/88-90) (GN/TA)

i) Exchange and trade policies.

ii) Public Expenditure policies and major sectoral strategies.

iii) Public Enterprise policies.

iv) Key pricing policies.

v) Other public sector management policies.

vi) Financial sector policies.

vii) Continued fiscal/monetary restraint.

viii) Institutional reforms - private sector role, economic management.

IV. The Financial Package (GN/TS/VC/FPA)

i) Alternative ways of closing the remaining gap (i.e. rescheduling, new money). This will involve, inter alia discussion of rescheduling, increased Bank lending, role of the IMF, increased commercial bank lending, new instruments etc.

ii) Institutional issues: new instruments, monitoring procedures, Bank-Fund collaboration.

V. A Suggested Action Plan

i) Summary of major constraints

ii) FMGN's role.

iii) The role of the Bank

iv) The role of other international institutions: IMF, Paris and

London Clubs, commercial banks, AFDB, ECAs, private creditors (uninsured arrears).

Duncan

THE WORLD BANK · INTERNATIONAL FINANCE CORPORATION

OFFICE MEMORANDUM

Basil –
As discussed, I would appreciate your comments by 9:30 AM on Tuesday.
Paul
10/25

DATE October 24, 1985

TO Mr. Wilfried P. Thalwitz, RVP, WAN

FROM Bilsel Alisbah, Director, WA1

EXTENSION 78051

SUBJECT NIGERIA - Balance of Payments Prospects and Debt Servicing Capacity

1. I attach a note on Nigeria's balance of payments prospects and debt servicing capacity, which we have prepared so that it can be sent to Mr. Stern soon after his return. You will see that its main focus is the problem which Nigeria will face if it adopts the IMF/SAL program and then only gets a "normal" financing package. Without more generous debt rescheduling and additional financing, Nigeria would not be able to maintain even the austere level of imports expected for 1985. The paper discusses ways in which additional relief might be provided over and above the "normal" package. It concludes with a discussion of Nigeria's creditworthiness for Bank lending in the absence of the kind of measures which would permit the IMF/SAL package to go forward. Although what is contained here does not constitute a complete creditworthiness analysis - we are still working on the picture in the 1990's - it does make a strong case for continued Bank lending for a "core" program.

Wilfried
We spoke about this already.
Basil

2. I also attach the letter I have signed to the Minister of Finance and sent in yesterday's pouch to the Resident Mission. If you feel any changes are needed, we can ask Ishrat to make them before passing it on to the Finance Minister.

Attachments

cc: Messrs. Fuchs, O'Brien, Eccles, T. Husain, Isenman, Allen, Todd, Husain, Innes (Lagos), WA1NI staff.

WSHumphrey:pt

P-1866

The World Bank
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL DEVELOPMENT ASSOCIATION

1818 H Street, N.W.
Washington, D.C. 20433
U.S.A.

(202) 477-1234
Cable Address: INTBAFRAD
Cable Address: INDEVAS

October 23, 1985

Dr. Kalu I. Kalu
Minister of Finance
Federal Ministry of Finance
Federal Secretariat
Ikoyi
Lagos, Nigeria.

Dear Dr. Kalu:

It was a great pleasure seeing you and the other members of the Nigerian delegation at Seoul. You asked there to have our analysis of Nigeria's balance of payments prospects and their consequences, even if this work was still in a fairly rough state. We have given top priority to this work and would like to take this occasion to share our preliminary findings with you.

The first conclusion is that the balance of payments financing problem will indeed be a serious one. The key numbers on this are quite straightforward, if subject to substantial uncertainties. They are summarized in Tables A and B, which are accompanied by notes on their assumptions. Reorganizing the data in Table A yields the following discouraging picture.

(US$ million)

	1986	1987	1988	1989	1990	Total (1986-90)
Oil exports:	9,837	9,736	10,238	11,800	13,490	55,102
Import Capacity with no new financing: 1/	4,815	5,066	5,262	6,959	10,055	32,157
Net rescheduling and new financing needed to keep imports at likely 1985 real level ($7.5 billion)	3,655	3,973	4,527	3,371	583	16,108

1/ This is equivalent to the amount that would be available for imports of goods, given existing commitments, on the assumption that no new finance is available.

The above assumes rescheduled trade arrears at $6 billion. If -- though this appears unlikely -- the rescheduled arrears were to amount to as little as $4 billion, the total financing requirement over the period would be about $2.7 billion lower (or conversely, the import capacity would be about $2.7 billion higher).

This financing crisis arose, of course, mainly from the decline in (present and prospective) oil prices and volumes and from the increasing debt service burden, including that from the large trade arrears. We note that the Government is trying for a substantially lower level of imports in 1985 and agree that it is highly desirable to do so as a temporary response to the current financing emergency. However, our quantitative analysis of import requirements suggests that for the period 1986-1990, even $7.5 billion is quite low by historical standards. At that level, (real) imports per capita would be slightly below those of 1971-73; also, in order to prevent a further decline in GNP per capita, an exceptional increase in the efficiency of use of imports would be required. In addition, some would consider our estimates of oil earnings, always notoriously difficult to predict, to be on the high side. (We have used estimates from the World Bank's Commodity Division; annual price and volume assumptions are included in the notes to Tables A and B.)

There are a few major conclusions that virtually leap out of these numbers. The first is that Nigeria should be planning on a low level of imports indeed over the next several years; and its related policies, such as its planning for public expenditures, should take account of this. Our report on Public Expenditure, of which we gave you a draft in Seoul, is based on an assumption of ₦10 billion of federal public investment over the five years 1986-90. With present oil projections, even this may be on the high side.

The second is that it is imperative to reach agreement with the IMF quickly, to have access not only to to Fund resources themselves, but also to other sources of financing, such as (medium and long-term) debt rescheduling, and new lending from members of the Paris and London clubs. I respect and appreciate the desire in Nigeria now not to repeat the errors of the past regarding the accumulation of unaffordable debts and arrears. However, inability to achieve at least minimum levels of imports would raise serious problems for economic development. In the absence of an IMF agreement and an associated financing package, balance of payments prospects anywhere near those suggested by the figures above could well cause lenders to try to reduce the risk of default by cutting back on their exposure. This could extend to normal trade financing; and I would even have a hard time defending any substantial amounts of new Bank lending to our senior management, given the Bank's concerns about the effect of country creditworthiness on its own borrowing capacity.

The third conclusion is that substantial policy reforms are urgently needed to bring about structural adjustment. This is necessary not just to permit the IMF program and other resource flows that would follow from it, but to increase substantially the efficiency of utilization of very scarce foreign exchange and of the economy in general. It is unfortunate that these reforms -- particularly a change in the value of foreign exchange -- are often viewed

in Nigeria as only a condition for a Fund program, and not as something that Nigeria needs to do for itself even in the absence of a Fund program. Regarding the exchange rate, the sharp worsening of the balance of payments situation has direct implications for the size of the change needed. The change needed to discourage excess demand for imports and allocate them efficiently and to encourage emphasis on efficient import substitution and on non-oil exports is going to be substantially more than was the case as recently as 12-18 months ago. And to the extent that the Government decides to restrain imports even below $7.5 billion over the next five years, the change in the exchange rate would have to be that much greater. Without such a policy adjustment, the economy would get more and more permanently enmeshed in import and other controls. These may succeed in holding down import levels, but the costs, both immediate and longer term, to growth and anti-inflation objectives would be severe.

We are now in the early stages of work on possible scenarios to judge the feasibility of financing at least the 1985 level of imports through the rest of the decade, as well as of allowing an improved situation beginning by about 1990. By an improved situation, we mean an increasing trend in real import levels combined with a declining trend in the proportion of exports going to service external debt. As part of this work, we are looking at financing and reform packages that have been put together in other countries. From preliminary work to date, I believe that a package meeting these two objectives is feasible, although the work has not yet advanced to the stage where we can attach specific amounts to each major source of financing.

What is clear already, though, is that a "normal" financing package may well not be enough. Such a "normal" program would include moderate levels of IMF financing over four years, increased Bank lending (including the introduction of Structural Adjustment Loans), and debt relief for three years from the Paris and London Clubs. Based on our initial estimates this "normal" program would probably raise "only" about $6.6 billion (in net relief) over the five years, by no means enough to meet the requirements noted above. Also, it would provide net relief only in the first three years, still leaving a large gap in 1988, 1989 and 1990, as repayments of principal as well as interest become due. What will be needed is an "extraordinary" program, generous both in amounts provided and in the length of its maturities. New medium-term lending from commercial sources would also be required. Any improvement in oil revenues, whether on the price or volume side, would obviously also help. If the "extraordinary" program is to be feasible at all, it will require a correspondingly strong reform program on the Nigerian side -- one which is no more difficult than that undertaken by a number of other countries, but which would not allow much room for half-way measures or lengthy delays. At the end of the day, Nigeria will, of course, have to adjust -- in its imports and in its pricing and other policies -- to make the best of whatever import-financing capacity it is able to achieve. As noted above, the lower the amount of import financing, the bigger the devaluation and other policy changes that will be necessary.

I am asking Ishrat Husain, who has been in close contact with those working here in Washington on the numbers, to deliver this letter to you and

to be available to you and your colleagues to discuss both the numbers and their implications. We are in the process of transferring to his office the relevant computer diskettes, so that he and his staff will be able to do "what if" calculations quickly for you based on whatever alternate assumptions you specify, as well as to show your staff how to run this program themselves.

Yours sincerely,

Bilsel Alisbah
Director
Western Africa, Country Programs I

Table 8

NIGERIA: EXTERNAL FINANCING BALANCE

(Based on existing commitments, assuming no new financing and arrears at US$ 6 billion)

(millions of current US dollars)

	1985	1986	1987	1988	1989	1990	Total (1986-1990)
Current Account							
Exports FOB	11373	10406	10346	10890	12498	14237	58376
(of which Oil)	10841	9837	9736	10238	11800	13490	55102
Imports FOB	-7500	-8025	-8587	-9231	-9942	-10697	-46481
Merchandise Trade Balance	3873	2381	1759	1659	2556	3540	11895
Net Services	-3160	-4247	-3198	-2973	-2736	-2661	-15815
(of which interest on loans already committed)	-1615	-2600	-1437	-1082	-701	-472	-6292
Current Account Balance	712	-1866	-1439	-1314	-180	879	-3920
Capital Account							
Loan Disbursements (from commitments to date)	2837	1630	1018	450	284	151	3532
Loan Amortisation (on commitments to date and including rescheduled trade arrears of US $ 6 billion)	-3350	-3816	-3883	-3952	-3683	-1826	-17160
Other (including foreign investment)	388	459	395	364	290	301	1808
Capital Account Balance (incl. Reserve changes)	259	-1789	-2534	-3213	-3191	-1462	-12189
Net Financing Requirement (-)	1 / 0	-3655	-3973	-4527	-3371	-583	-16108

Footnote: 1 / The recent downward revision in the expected level of imports (from $ 8 billion to $7.5 billion)would imply a surplus in the balance of payments. We assume that this would be used in building up reserves to a more reasonable level of about 2 months worth of imports (rather than 1.5) and in import financing.

Source: IBRD staff estimates unless otherwise specified in the attached notes.

Table B

NIGERIA: EXTERNAL FINANCING BALANCE 1986-90

(Based on existing commitments, assuming no new financing and arrears at US $ 6 billion)

(millions of current US$)

	1985	1986	1987	1988	1989	1990	Total (1986-90)
Merchandise Trade F.O.B. (net)	3873	2381	1759	1659	2556	3540	11895
Total Exports	11373	10406	10346	10890	12498	14237	58376
of which: Petroleum	10841	9837	9736	10238	11800	13490	55102
Other	532	569	609	652	697	746	3274
Total Imports	-7500	-8025	-8587	-9231	-9942	-10697	-46481
Services (Net)	-3160	-4247	-3198	-2973	-2736	-2661	-15815
1. Freight & Insurance	-450	-482	-515	-554	-596	-642	-2789
2. Travel	-150	-158	-169	-181	-195	-210	-912
3. Other Goods & Services Income	-450	-482	-515	-554	-596	-642	-2789
4. Investment Income	-1825	-2827	-1678	-1340	-977	-768	-7591
a) On Direct Pvt. Investment	-263	-281	-301	-323	-348	-374	-1627
b) Interest on MLT Debt	-1615	-2600	-1437	-1082	-701	-472	-6292
c) Interest on Reserves	52	54	59	65	71	78	327
5. Net Transfers	-285	-299	-320	-344	-371	-399	-1733
CURRENT ACCOUNT BALANCE	712	-1866	-1439	-1314	-180	879	-3920
Capital Account							
Direct Investment (Net)	308	323	339	356	374	393	1785
Oil							
Non-oil							
Medium & Long Term Capital (Net)	-513	-2187	-2865	-3502	-3399	-1676	-13628
Gross Borrowing (from commitments to date)	2837	1630	1018	450	284	151	3532
Financial Institutions	2451	1309	780	286	180	67	2622
Multilateral IBRD	222	204	163	131	104	83	685
IBRD SAL							
IMF							
Private	164	117	75	33	0	0	225
Amortisation Due (on commitments to date)	3350	3816	3883	3952	3683	1826	17160
Arrears US $ 6.0 billion 1/	0	571	1143	1429	1714	571	5429
Financial Institutions	3047	2919	2389	2201	1691	987	10188
Multilateral IBRD	53	81	111	147	157	168	664
IBRD SAL							
IMF							
Private	250	245	240	175	120	100	880
Short Term Capital	81	136	56	8	-84	-92	24
Oil	-39	92	9	-46	-143	-155	
Other	120	44	47	54	59	63	
Commercial Banks	0	0	0	0	0	0	
Net Errors and Omissions							
OVERALL BALANCE	587 2/	-3594	-3908	-4452	-3289	-496	-15739
Financing	-587	3594	3908	4452	3289	496	
Level of Reserves	1581	671	736	810	892	979	
Assets	865	926	991	1065	1147	1234	
Liabilities	-255	-255	-255	-255	-255	-255	
Reserve Availablity	384	161	-65	-74	-82	-87	
FINANCING REQUIREMENT	0 2/	-3655	-3973	-4527	-3371	-583	-16108

Footnotes: 1/ If arrears were as low as US $ 4 billion, this would reduce the debt service by the following amounts:

	1986	1987	1988	1989	1990	1986-1990
Current US $ million	744	440	551	649	324	2708

2/ The recent downward revision in the expected level of imports (from $ 8 billion to $ 7.5 billion) would imply a surplus in the balance of payments. We assume that this would be used in building up reserves to a more reasonable level of about 2 months worth of imports (rather than 1.5) and in import financing.

Source: IBRD staff estimates unless otherwise specified in the attached notes

Notes To Tables A and B

1. Tables A and B present several hypothetical projections of Nigeria's external balance. These projections are not "worst case" scenarios. Some of the assumptions are, if anything, quite optimistic. In brief, these projections suggest that, given our assumptions on oil exports, in order to keep total imports over the next five years at their 1985 level (quite low by historical standards), Nigeria would have to borrow or reschedule very large amounts.

2. These projections depend heavily on the assumptions about oil exports. It is possible that unforseen developments in world oil markets could cause Nigeria's oil export earnings to be much larger than shown here. In the absence of any such indication, however, it would be best to plan for the next few years on the assumption that oil markets will stay pretty much as they are. This is far from the worst that could happen. If all current producers were to compete openly, the price could easily fall to the $20 per barrel range.

3. Our first calculations project the external financing gap under the following assumptions:

a) Imports (of goods) are held constant in real terms at the level estimated for 1985 ($7.5 billion in 1985 prices).

b) Oil exports are taken from the latest World Bank Commodity Division projections. Their estimates are similar in aggregate oil earnings to those of the International Monetary Fund. The quantities and prices of these two estimates are given below.

	1986	1987	1988	1989	1990	Total 1986-1990
IMF Informal Estimates						
Oil sold (mb/d)	1.15	1.20	1.25	1.30	1.35	
Price of oil US$	24.00	24.00	24.00	24.00	24.00	
Value of oil exports	10,074	10,512	10,950	11,388	11,826	54,750
World Bank Commodity Division Estimates						
Oil sold (mb/d)	.98	.97	1.02	1.06	1.10	
Price of oil US$	27.50	27.50	27.50	30.50	33.60	
Value of oil exports	9,837	9,737	10,266	11,800	13,490	55,130

Thus, the IMF estimates have lower prices but higher volumes than the Commodity Division estimates. The IMF projections are noticeably higher in 1987 and 1988, and lower in 1989 and (particularly) 1990. Scenarios with other prices will be run on request.

c) Non-oil exports were taken from World Bank projections, averaging US$655 million per year over the five year period.

d) Short term arrears were assumed to be $6.0 billion at the end of 1984. It was assumed these would be formally recognized in April 86 with interest payable from January 1, 1984, and principal payments beginning July 1986 for the uninsured credits and July 1988 for the insured credits.

e) The amounts of medium and long term debt and the current terms of those loans were taken from the World Bank's External Debt Division. Total MLT debt was $12.7 billion as of December 1984, according to those records.

f) To project new financing needs, it is assumed that no new loan commitments have been obtained. Existing loan commitments are disbursed on normal schedules.

g) Regarding services, items like freight, insurance, and other goods and services are taken as fixed proportions (based on historic trends) of imports of goods. Other items under "services" grow by a modest rate of 5 percent in 1985-86 and by the IBRD estimates of international inflation rates thereafter.

h) Direct investment is assumed to increase by 5 percent per year.

i) Medium and long-term debt data is taken from the IBRD External Debt Reporting System. World Bank disbursements are based on Nigeria Division estimates.

j) Data on short-term capital have been obtained from the IMF.

k) It is assumed that Nigeria will maintain a reserve level of 1.5 months of imports of goods. Liabilities are kept constant at 1984 level.

NOTE ON NIGERIA'S BALANCE OF PAYMENTS PROSPECTS AND DEBT-SERVICE CAPACITY

Due to worsening oil prices and volumes, together with sharply increasing debt service payments, Nigeria now faces a severe balance of payments crisis. Even to hold imports (of goods) at their expected 1985 real level of $7.5 billion -- compared to an annual average of $15.5 billion in the peak period 1980-1982 -- throughout the remaining part of the 1980's would require an extraordinary rescue and reform package. There is no magic in this $7.5 billion number. Nigeria will in fact have to try to adjust to whatever is available. However, as discussed below, $7.5 billion is already at the low end of what appears consistent with a reform program that is likely to stand the test of time. Without such a rescue and reform package, the Nigerians will have only three options: hoping for better oil markets -- a chancy process at best; cutting imports much further, thus jeapordizing chances for any meaningful growth and for sustainability of the reform program; or some combination of arrears and default. It is not even clear at this point that the extraordinary package needed could be put together. But it is clearly worth the effort to explore such a package, given the importance of development in this country that comprises half the population of West Africa, and given the broader adverse consequences of a major default.

The key numbers are summarized in Table A, which is accompanied by notes explaining the basis of its major assumptions. The main reason we have become much more concerned than we were just six months ago is the decline in projected world oil prices and, even more importantly, in the

volumes that (in the view of the Commodity Division) Nigeria can expect to export. This reemphasizes the extreme dependence of the Nigerian economy on international oil markets, which are notoriously difficult to predict. Thus, our estimates of financing requirements are inevitably subject to a high degree of uncertainty. An improvement in world oil prices and the volume of Nigeria's oil exports would reduce the financing problem to more manageable proportions, but it would take a dramatic change (a 40 percent increase in oil earnings) to meet all new financing requirements. On the other hand, a further sharp decline in oil prices could make Nigeria's balance of payments crisis unmanageable -- to the point of large-scale default, and of such a sharp compression of imports that economic and political stability would become highly questionable. The level of new financing needed, over and above existing commitments, on the basis of stable oil revenues is presented below. (This financing requirement is not a "financing gap", as usually thought of in the Bank, since much of the needed new funding is potentially readily available).

New financing needed in order to keep imports at their real 1985 level

	1986	1987	1988	1989	1990	Total 1986-1990
Financing Requirement (-): (US$ million)	-3,655	-3,973	-4,527	-3,371	-583	-16,108

What can be done to meet this requirement? Without a program of structural adjustment, hardly anything. Clearly, a full structural adjustment program is needed, with at least normal support from the Bank and Fund, and at least normal levels of debt rescheduling. The "normal" package would include: $5.3 billion in total Bank commitments 1986-1990, of which $2.0 billion in SALs; an IMF program of 70 percent of quota

shoot for more

annually 1986-1989; annual rescheduling of debt over 3 years on the optmistic assumption of 85% percent financing of principal and interest from the Paris Club and 100% of principal from the London Club, with a grace period of 3 years. But as shown below, this "normal" level of adjustment assistance -- itself implying a major reform effort on the part of the Nigerians -- would not provide nearly enough, particularly for the period 1988-1990.

Net Financing from "normal" package: 1/

(US$ million)

	1986	1987	1988	1989	1990	Total 1986-1990
- Bank	96	335	474	530	598	2,033
- Fund	578	533	488	443	-372	1,667
- Rescheduling	2,459	2,125	1,553	-1,342	-1,873	2,922
Total	3,132	2,993	2,514	-369	-1,647	6,622
(Memo item: initial Financing Requirement)	(-3,655)	(-3,973)	(-4,527)	(-3,371)	(-583)	(-16,108)
Remaining Financing requirement (-):	-523	-980	-2,012	-3,740	-2,231	-9,486

What more can be done? A key issue is whether an "extraordinary" package could be put together. Even thinking of such a package implies a corresponding extra reform effort on the part of Nigeria. To date, its performance on austerity has been fine, and prospects for agreement on public investment and public enterprise reform are fairly good; the real question, though, is how far Nigeria will be willing to go on the exchange

---

1/ Disbursements from new commitments, minus debt service on the new commitments.

rate and related trade liberalization. The main differences between the "extraordinary" and the "normal" packages are: a two-year sequential rescheduling followed by three years, (totalling five years rather than a total of three-years) with a grace period of five rather than three years; Fund access at up to 90 percent (rather than 70) of quota annually over 1986-1989, preferably on EFF terms for at least three years, with a one year standby after that and a rollover of principal in 1989 (and partial rollover in 1990); and a modest increase in IBRD commitments of $1 billion over the five years, to show that we are not simply asking everyone else to make a special effort. This package is, of course illustrative. It errs on the side of optimism to underline both that there is a need for something well beyond the ordinary and that even with optimistic assumptions a substantial residual gap would still remain. We have discussed these proposals with central staffs who indicated that while they were quite optimistic, they were not impossible or outlandish.

Financing from "extraordinary" package: 2/

(Disbursements, US$ million)

	1986	1987	1988	1989	1990	Total 1986-1990
- Bank	287	604	621	660	710	2,883
- Fund	736	679	622	564	-475	2,126
- Rescheduling	2,459	2,125	1,553	774	-30	6,880
Total	3,482	3,408	2,795	1,998	205	11,888
(Memo item: Initial Financing Requirement)	(-3,655)	(-3,973)	(-4,527)	(-3,371)	(-583)	(-16,108)
Remaining financing requirement (-):	-173	-565	-1,731	-1,373	-379	-4,220

The remaining gap is still large, and is now even more concentrated in 1988 and 1989. Putting the crisis off for two years may give some breathing room to see what happens to oil markets; but it is not only undesirable but probably also infeasible. Without a viable medium-term financing plan, neither we nor other lenders would participate; nor would Nigeria be likely to undertake a highly unpopular major devaluation when it would be transparent that Nigeria would have merely shifted the crisis out a bit. (Of course, shifting fixed debts out far enough to reach the period of substantially higher oil revenues, expected to begin in roughly 1990, is a more viable proposition.)

How can this remaining gap be closed? One possibility -- a logical extension of the extraordinary package -- would be increased commercial borrowing. Commercial lenders are understandably reluctant even

---

2/ For ease of exposition, the table covers the gross amounts, and not just the increments over the "normal" package.

to maintain their exposure in Nigeria. The projections above assumed a substantial reduction in this exposure as debts and arrears are paid off. With the "extraordinary package", there would be no payments on principal during this period for the 70-80% of total MLT debt covered by the Paris and London Clubs. However, there would still be a substantial net outflow in interest on commercial debt. It would be conceivable for the Fund and Bank to take a fairly tough line, making the case to commercial lenders that extending additional credit is a necessary part of getting existing debts repaid (and having access to the Nigerian market in the longer run, which some bankers tell us is still important to them). 3/ In addition, some new funds should be available through supplier credits. This could come through renewed Paris Club guarantees, or because the total profits on the sale of goods (e.g. 35 percent rather than the e.g. 3 percent margins on lending per se) make Nigeria, with a major rescue and reform effort, worth the risk.

A second possibility is producing more oil, through being accorded a larger share of OPEC production. Given the current weakness of oil markets and of OPEC, this is more plausible for the outer years. As oil markets begin to firm, though, it is not unreasonable to expect OPEC to permit, or at least turn a blind eye, to a modest increase in Nigerian

---

3/ We have assumed that commercial lines of credit would be fully used in the year they are granted; for example they can be used directly for debt servicing. Regarding maturities, we have assumed a 100% balloon repayment in the fourth year, which we are advised would be the likely price of the volume of borrowing and 3 years' grace period we seek. Other combinations of commitments and maturities could also yield a similar disbursement pattern.

sales. We estimate that total revenues could plausibly be 7% higher in 1988 and 10% higher in 1989 and 1990, than assumed in the projections above. We also considered the possibility of substantially increased non-oil exports, but there are problems of the low base and of the relatively long lead times to produce more of such things as tree-crops and energy-based products. Growth in non-oil exports is vital, however, for the longer term.

A rough estimate of what might be yielded by these two steps is given below:

(US$ million)

	1986	1987	1988	1989	1990	Total 1986-1990
Increased oil revenues:	0	0	800	1,100	1,200	3,100
Incremental commercial borrowing:						
- (disbursements -- 100% of commitments)	(250)	(750)	(1,000)	(750)	(750)	(3,500)
- net relief	238	688	850	275	-250	1,800
Total:	238	688	1,650	1,375	950	4,900
(Memo item: previous financing requirement)	(-173)	(-565)	(-1,731)	(-1,373)	(-379)	(-4,220)
Remaining financing requirement (-):	64	123	-81	2	571	680

This would at first glance more than eliminate the gap over the period. However, not all the steps described above can be counted on to happen -- or to yield at least the amounts suggested, since some of them are purposely optimistic. Rather, in order to assure imports at the highly compressed level of 1985 -- let alone to permit some import growth to

encourage output growth -- the sum of potential new financing should preferably exceed actual requirements by a substantial amount.

There is one further important point already identified for further investigation. It is unclear whether the total amount of trade arrears (insured and uninsured) that will finally be rescheduled (including those on which promissory notes have already been issued) will be in the range of $6 billion, as we have conservatively assumed, or in the range of $4 billion, as some others assert to be the case. Total claims are significantly higher than $6 billion, but some of them are apparently fraudulent or based on gross overinvoicing; and some other claims may not be cleared, because of technical or substantive flaws, by Chase (the Government's agent on validating arrears claims). Using the lower figure of $4 billion would have a noticeable effect (with reduced payments on both principal and interest).

	1986	1987	1988	1989	1990	1986-1990
Reduced service on arrears:	744	440	551	649	324	2,708

This would be an encouraging result. However, the odds are that the trade arrears will be closer to $6 billion than to $4 billion.

To the extent that not all these steps are possible to the extent projected here and a substantial gap remains, the only real major possibility left -- if default is to be avoided -- would be cutting imports further. This would be highly undesirable from a growth point of

view. An import level of $7.5 billion is extremely low by historical standards. Imports per capita would be back to the level of 1971-73, although the structure of production and consumption has become much more import-intensive since then. The 1985 level was $2 billion below its expected value from regression analysis. However in this case necessity will have to be the mother of structural change. At this level, even to keep GNP -- let alone GNP per capita -- from declining would require an exceptional increase in the efficiency of use of imports. In addition, there should preferably be some real growth in imports, say 3 percent a year, from this very low base to encourage real growth in GDP. This would add about $3 billion to financing requirements in current prices if growth starts in 1987.

Overall, it might be possible -- just barely -- to put a minimum feasible rescue package together. This assumes, inter alia, that we can walk the fine line with the Nigerians of convincing them on the one hand that the problem is so serious that they must reach agreement on the best possible package they can get (including full support of the Fund), but on the other, that it is not so hopeless that it is in any event doomed. The latter perception would likely lead them either to inaction -- putting off politically difficult steps that will leave them with an unviable situation -- or default. We will be doing more work on the numbers and on the likely feasibility and magnitude of elements of a possible rescue program. We will continue to work closely with the Fund on this.

We are also giving consideration to the implications of the current situation for Nigeria's continuing creditworthiness for Bank

lending. A potentially serious problem could arise, particularly if no action is taken toward a major rescue and reform effort. In that case, as shown in Table A, Nigeria's debt service would be 62 percent in 1986, declining fairly rapidly thereafter; the 1987 and 1988 levels would still be above 45 percent, though. However, even these high levels would be below those of some major Latin American borrower countries. More to the point, Nigeria has just gone through a balance of payments crisis in which it first built up trade arrears and then slashed imports in half; in spite of these serious problems it has shown a striking commitment to keeping current on medium and long-term debt service in general, and in debt service to the Bank in particular. They have had little difficulty in keeping payments current -- surprisingly so, given the general inefficiency of the Government on other matters relating to loan processing, etc. And even if Nigeria did default on some MLT debt service over the next few years, it would probably default on (rescheduled trade arrears) to private uninsured creditors first, and to the Bank only after other creditors.

In addition, if there is no agreement with the Fund, the much lower lending and rescheduling in the latter part of the 1980s would mean lower debt service due in the early 1990s. The cost, in terms of reduced imports and growth and perhaps some defaults, would have been great; but with lower debt service and with the improved oil market expected for the first half of the 1990s, the risk of default to the Bank after 1990 would be relatively low. And no repayments under loans made from now on would become due before 1991. This is not to say that there are no concerns about short-term creditworthiness if there is no rescue and reform program. For example a prolonged crisis might lead to a change of government and to

a weakening of the very high priority given to meeting MLT debt servicing obligations. On the other hand, given the Nigerian record to date on MLT debt service and its close relations with the Bank, this would hardly be the time to cut back our new lending even further. Such a cutback would at best be likely to reduce opportunities for arriving at the reforms and resultant financing that would assure that we, and other lenders, get repaid over the next several years; in fact, a sharp cutback from our current, essentially "core", program, even risks creating a self-fulfilling prophecy of an increased chance of default. Although the cutback in our program was originally for country strategy rather than creditworthiness reasons, it serves for the latter as well. For the time being, we are concentrating our efforts on the policy dialogue -- particularly with Finance Minister Kalu, who is sympathetic to the need for reform and for an accommodation with the Fund. A copy of a letter to him on the financing problem and the need for strong action is attached. This letter, by the way, mentions the creditworthiness problem on Bank lending that would arise if there is no agreement with the Fund. If developments over the next few months are not positive, the OPSC strategy update planned for the early spring will focus heavily on the creditworthiness issue. Even if progress is good and we are working actively on the "extraordinary program", we will also continue to monitor the creditworthiness issue.

PIsenman/ADuncan/JTodd/VChandra:pjc

Table A

NIGERIA: EXTERNAL FINANCING BALANCE

(Based on existing commitments, assuming no new financing and arrears at US$ 6 billion)

(millions of current US dollars)

	1985	1986	1987	1988	1989	1990	Total (1986-1990)
Current Account							
Exports FOB	11373	10406	10346	10890	12498	14237	58376
(of which Oil)	10841	9837	9736	10238	11800	13490	55102
Imports FOB	-7500	-8025	-8587	-9231	-9942	-10697	-46481
Merchandise Trade Balance	3873	2381	1759	1659	2556	3540	11895
Net Services	-3160	-4247	-3198	-2973	-2736	-2661	-15815
(of which interest on loans already committed)	-1615	-2600	-1437	-1082	-701	-472	-6292
Current Account Balance	712	-1866	-1439	-1314	-180	879	-3920
Capital Account							
Loan Disbursements (from commitments to date)	2837	1630	1018	450	284	151	3532
Loan Amortisation (on commitments to date and including rescheduled trade arrears of US $ 6 billion)	-3350	-3816	-3883	-3952	-3683	-1826	-17160
Other (including foreign investment)	388	459	395	364	290	301	1808
Capital Account Balance (incl. Reserve changes)	259	-1789	-2534	-3213	-3191	-1462	-12189
Net Financing Requirement (-)	1 / 0	-3655	-3973	-4527	-3371	-583	-16108
Debt Service Ratio	43.7	61.7	51.4	46.2	35.1	16.1	42.1

Footnote: 1 / The recent downward revision in the expected level of imports (from $ 8 billion to $7.5 billion)would imply a surplus in the balance of payments. We assume that this would be used in building up reserves to a more reasonable level of about 2 months worth of imports (rather than 1.5) and in import financing.

Source: IBRD staff estimates unless otherwise specified in the attached notes.

Table B

NIGERIA: EXTERNAL FINANCING BALANCE 1986-90

(Based on existing commitments, assuming no new financing and arrears at US $ 6 billion)

(millions of current US$)

	1985	1986	1987	1988	1989	1990	Total (1986-90)
Merchandise Trade F.O.B. (net)	3873	2381	1759	1659	2556	3540	11895
Total Exports	11373	10406	10346	10890	12498	14237	58376
of which: Petroleum	10841	9837	9736	10238	11800	13490	55102
Other	532	569	609	652	697	746	3274
Total Imports	-7500	-8025	-8587	-9231	-9942	-10697	-46481
Services (Net)	-3160	-4247	-3198	-2973	-2736	-2661	-15815
1. Freight & Insurance	-450	-482	-515	-554	-596	-642	-2789
2. Travel	-150	-158	-169	-181	-195	-210	-912
3. Other Goods & Services Income	-450	-482	-515	-554	-596	-642	-2789
4. Investment Income	-1825	-2827	-1678	-1340	-977	-768	-7591
a) On Direct Pvt. Investment	-263	-281	-301	-323	-348	-374	-1627
b) Interest on MLT Debt	-1615	-2600	-1437	-1082	-701	-472	-6292
c) Interest on Reserves	52	54	59	65	71	78	327
5. Net Transfers	-285	-299	-320	-344	-371	-399	-1733
CURRENT ACCOUNT BALANCE	712	-1866	-1439	-1314	-180	879	-3920
Capital Account							
Direct Investment (Net)	308	323	339	356	374	393	1785
Oil							
Non-oil							
Medium & Long Term Capital (Net)	-513	-2187	-2865	-3502	-3399	-1676	-13628
Gross Borrowing (from commitments to date)	2837	1630	1018	450	284	151	3532
Financial Institutions	2451	1309	780	286	180	67	2622
Multilateral IBRD	222	204	163	131	104	83	685
IBRD SAL							
IMF							
Private	164	117	75	33	0	0	225
Amortisation Due (on commitments to date)	3350	3816	3883	3952	3683	1826	17160
Arrears US $ 6.0 billion 1/	0	571	1143	1429	1714	571	5429
Financial Institutions	3047	2919	2389	2201	1691	987	10188
Multilateral IBRD	53	81	111	147	157	168	664
IBRD SAL							
IMF							
Private	250	245	240	175	120	100	880
Short Term Capital	81	136	56	8	-84	-92	24
Oil	-39	92	9	-46	-143	-155	
Other	120	44	47	54	59	63	
Commercial Banks	0	0	0	0	0	0	
Net Errors and Omissions							
OVERALL BALANCE	587 2/	-3594	-3908	-4452	-3289	-496	-15739
Financing	-587	3594	3908	4452	3289	496	
Level of Reserves	1581	671	736	810	892	979	
Assets	865	926	991	1065	1147	1234	
Liabilities	-255	-255	-255	-255	-255	-255	
Reserve Availablity	384	-61	-65	-74	-82	-87	
FINANCING REQUIREMENT	0 2/	-3655	-3973	-4527	-3371	-583	-16108

Footnotes: 1/ If arrears were as low as US $ 4 billion, this would reduce the debt service by the following amounts:

	1986	1987	1988	1989	1990	1986-1990
Current US $ million	744	440	551	649	324	2708

2/ The recent downward revision in the expected level of imports (from $ 8 billion to $ 7.5 billion) would imply a surplus in the balance of payments. We assume that this would be used in building up reserves to a more reasonable level of about 2 months worth of imports (rather than 1.5) and in import financing.

Source: IBRD staff estimates unless otherwise specified in the attached notes

Notes To Tables A and B

1. Tables A and B present several hypothetical projections of Nigeria's external balance. These projections are not "worst case" scenarios. Some of the assumptions are, if anything, quite optimistic. In brief, these projections suggest that, given our assumptions on oil exports, in order to keep total imports over the next five years at their 1985 level (quite low by historical standards), Nigeria would have to borrow or reschedule very large amounts.

2. These projections depend heavily on the assumptions about oil exports. It is possible that unforseen developments in world oil markets could cause Nigeria's oil export earnings to be much larger than shown here. In the absence of any such indication, however, it would be best to plan for the next few years on the assumption that oil markets will stay pretty much as they are. This is far from the worst that could happen. If all current producers were to compete openly, the price could easily fall to the $20 per barrel range.

3. Our first calculations project the external financing gap under the following assumptions:

a) Imports (of goods) are held constant in real terms at the level estimated for 1985 ($7.5 billion in 1985 prices).

b) Oil exports are taken from the latest World Bank Commodity Division projections. Their estimates are similar in aggregate oil earnings to those of the International Monetary Fund. The quantities and prices of these two estimates are given below.

	1986	1987	1988	1989	1990	Total 1986-1990
IMF Informal Estimates						
Oil sold (mb/d)	1.15	1.20	1.25	1.30	1.35	
Price of oil US$	24.00	24.00	24.00	24.00	24.00	
Value of oil exports	10,074	10,512	10,950	11,388	11,826	54,750
World Bank Commodity Division Estimates						
Oil sold (mb/d)	.98	.97	1.02	1.06	1.10	
Price of oil US$	27.50	27.50	27.50	30.50	33.60	
Value of oil exports	9,837	9,737	10,266	11,800	13,490	55,130

Thus, the IMF estimates have lower prices but higher volumes than the Commodity Division estimates. The IMF projections are noticeably higher in 1987 and 1988, and lower in 1989 and (particularly) 1990. Scenarios with other prices will be run on request.

c) Non-oil exports were taken from World Bank projections, averaging US$655 million per year over the five year period.

d) Short term arrears were assumed to be $6.0 billion at the end of 1984. It was assumed these would be formally recognized in April 86 with interest payable from January 1, 1984, and principal payments beginning July 1986 for the uninsured credits and July 1988 for the insured credits.

e) The amounts of medium and long term debt and the current terms of those loans were taken from the World Bank's External Debt Division. Total MLT debt was $12.7 billion as of December 1984, according to those records.

f) To project new financing needs, it is assumed that no new loan commitments have been obtained. Existing loan commitments are disbursed on normal schedules.

g) Regarding services, items like freight, insurance, and other goods and services are taken as fixed proportions (based on historic trends) of imports of goods. Other items under "services" grow by a modest rate of 5 percent in 1985-86 and by the IBRD estimates of international inflation rates thereafter.

h) Direct investment is assumed to increase by 5 percent per year.

i) Medium and long-term debt data is taken from the IBRD External Debt Reporting System. World Bank disbursements are based on Nigeria Division estimates.

j) Data on short-term capital have been obtained from the IMF.

k) It is assumed that Nigeria will maintain a reserve level of 1.5 months of imports of goods. Liabilities are kept constant at 1984 level.