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EFFECT OF EXTERNAL DEBT BURDEN ON ECONOMIC GROWTH IN NIGERIA

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Abstract:
The study was aimed at exploring the effect of external debt burden on economic growth in Nigeria. For the purpose of estimating the variables under study, this uses a multiple regression (OLS) model. The data is firstly tested for stationarity using the Augmented Dickey-Fuller (ADF) tests. In order to test for co-integration, the Johansen co-integration technique is used for normality test (Jarque-Bera) and serial correlations were used. The variables are made up of real GDP, money supply and external debt. The result revealed that external debt burden had a negative and insignificant effect on the Nigeria economic growth (coefficient = -1.31, p-value = 0.27). Based on the findings the study recommends alternative sources of government revenue to be utilised fully for this will minimize over dependence of government on foreign debt and therefore foster economic growth.

JEL: F30, F34, F40

Keywords: economic growth, external debt burden, debt servicing and public investment

1. Introduction

Pertinently, in order to ensure growth, some developing countries such as Nigeria in their early stage of development need to borrow to enhance what they have domestically being that they are characterised by inadequate capital. So, they may generate huge gain higher than their equals in other countries when they invest wisely in some viable investment opportunities. Therefore, insofar as both the borrowed and internally generated money will be used effectively for investment project, it is important to acquire it. Hence growth is likely to be accelerated which will allow for future development. Eventually when the growth is sustained it increases the per capital income of the country.

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According to Umaru et al, 2013, when countries provide essential commodities and conducive environment for business to strive it will promote economic growth and development. Also, in other to raise fund for budget deficit as a way to increase financial market and sustain the increased public expenditure as suggested by Obudah and Tomboja (2013). Similarly, Pattilo, Ricci and Poirson (2002) suggests that reasonable rates of borrowing by the third world countries may induce its growth. According to Cheremy, (1996) governments borrow as to argument the dearth of resources available and narrow the investment gap (Dual Gap).

A study of the Nigerian external debt profile depicts a continuous increase since the current regime. Thus in 2015 the total external dearth stock was $10.7 billion then in 2016 it was $11.406 and in 2017 it was $15.047 billion which eventually increased to $22.44billion in 2018. The multilateral debt and bilateral loan amounted to $218.25 billion and $5.15 billion respectively from the Exim Bank of China credit to the federal government as presented by the National Bureau of Statistics (NBS). The intensification of the foreign debt is a common characteristic of the developing countries at their early stage of growth and development where the sum total of domestic savings is low, current account payment deficit is high and influx of capital from foreign country is needed to argument domestic resources. No government survives in isolation as it would need assistance of other nations in order to perform efficiently and effectively. The external debt becomes a major source of help to the borrowing nations.

Problem with foreign debt is when the burden accelerates so high that it negatively affects the growth and development of other sectors. Udeh (2013) highlighted that increased debt burden has led to the adoption of several measures capable of reducing the debt burden affecting the growth prospects of most countries that so much depend on foreign loan. These measures cover from debt rescheduling to outright cancellation. To worsen the situation, the resultant effect of debt serving leads to increase of increased deficit. This of course causes a great challenge to the economy as huge portion of the country's income is being used up. Hence, contributing to the imbalances in the country's balance or payment. With the above, the study was aimed at exploring the effect of external debt burden on the Nigeria economic growth.

2. Literature Review

2.1 Conceptual Review

2.1.1 Concept of External Debt

Foreign debt emerges as a result of the gap between domestic savings and investment (Ogbeifin, 2007). Therefore, nations perpetually borrow when the gap keeps widening. He further explained Nigerian foreign debt as the debt owed by both the government and private sectors of the Nigeria economy to foreigners which are repaid in foreign goods and services.

Sogo Temio (1999) sees the growing debt burden of the third world countries in two ways: first, is the overdependence of developing nations on foreign loan. Again, the inability to meet up with the debt servicing which of course are relatively very huge.

Ahmed, 1964 asserts that the causes of debt crisis arise from poor macroeconomic policies that are enacted by the government. He further explains that the third world countries are associated with dearth of mineral and agricultural resources while export depends so much on the mineral resources which are not sufficient. Domestic firms are not strong and so depend largely on the imported materials. Moreso, funds and other vital inputs which are used by these local firms flow from the developed nations which makes developing countries susceptible to foreign debt shocks.

Amone, Bandieva and Pesbitero (2005) defined foreign loan as that portion of a country's debt that was loaned from foreign lenders such as commercial banks, government or international financial organisations. This research conceptualised external debt as debt contracted by a country such as Nigeria from foreign country such as France.

2.1.2 Concept of Growth

The word growth is used in all areas of life. In economics growth is viewed in terms of economic growth. Solow (1956) in his growth models emphasised capital building, increase rate of change in the populace and technological advancement as the means of growth. Moreover, Romer (1986) asserts that long run growth is caused by economic incentives. Kuznet, cited in Todaro 1985 that economic growth is a long-term increase in capital to supply variety of economic commodities to her population. This growth level depends largely on the technological advancement and organisational and ideological adjustment that it is needed which means that economic growth is similar with sustained increase in national output, availability of sufficient economic goods, institutional and technological advancement and effective ideologies.

Anyanwu and Oaiklem (1995) defines economic growth as the rise overtime in an economic capacity of nation to provide goods and services needed to revamp the social welfare of the citizenry. The International Monetary Fund (2009) and CBN (2010) view economic growth as a rise of the total number of goods and services manufactured in a country for a given period of time. Thus, calculated as the percentage rate of increase in the real GDP. Growth is usually measured in real terms. Which means, inflation minus adjusted terms, so as to bring out the effect of inflation on the price of the manufactured goods and services. The rise of the real gross domestic product (RGDP) between 2004 and 2008 was caused mainly by the non-oil sector of the economy. Meanwhile, industrial product reduced by 2.2 percent as a result of poor performance of the oil sector (CBN, 2008).

2.1.3 Overview of Nigerian External Debt

External debt in Nigeria can be traced back to 1958, when Nigeria borrowed about 28 million US dollars from the World Bank for the Railway Construction. This loan was so much compared to the first jumbo loan which was up to the sum of $1.0 billion that Nigerian loaned from the international capital market in 1978 as reported by the debt management office (2004). From 1958 to 1977 the need for external debt was not much felt. However, the quest for it arose in 1978 as a result of down world slope in the oil

prices in 1978. The reduction in the oil prices had a negative impact on the revenue of the Nigeria government. Therefore, in order to combat the imbalances in the country's balance of payment and finance adequately some viable investment brought about the need for external loan. Debt management office further stated that from 1977, the total debt incurred by Nigeria has been on the rise from $0.768 billion to $5.09 billion in 1978 and $8.65 in 1980 which is about 73.96 percent increment. External loan rose to $35.94 billion in 2004.

Meanwhile, the debt relief in 2006 placed Nigeria in a better position, a time when Nigeria offset a large portion of its debt. Though it did not last and sooner than later the figure rose again. External loans increased further when the state government were permitted to embark in foreign debt. Thus, in the year 1986 Nigeria adopted a World Bank international monetary fund (IMF) sponsored structural adjustment programme (SAP) in expectation to improve the Nigerian economy. Of course, this assisted the country and it was able to repay some loans that were contracted (Ayadi and Agayi, 2008). Nigerian's total debt stock as at December 2014 is N12.4 trillion (Amaefule, 2015). The figure from international monetary fund (IMF) shows that the domestic borrowing by the government decreased from N12.589 trillion in December 2017 and N12.577 trillion in March 2017 and N12.151 trillion in June 2018. Recent figures from the trading economics have shown that foreign loan in Nigeria has risen to USD22083.44m in the second quarter of 2018 from USD22071.91m in the first quarter of 2018 and reduced to USD3627.5m in the first quarter of 2019. Omolaye et al (2006) assets that Nigerians holds the largest debt in Sub-Sahara Arica states.

2.1.4 Need for External Debt

External debt of course is vital and could lead to growth and development if effectively used for infrastructural development because of the predominant nature of poverty and dearth of capital and other resources. It becomes difficult to solely depend on savings for growth. Therefore, it becomes important that developing countries such as Nigeria seeks to obtain external loan in order to argument what is produced internally. Meanwhile, external debt is cheaper and so preferable than the domestic loan which are relatively high. Such that the rate charged by the internal monetary fund is as low as 5% for that which is charged domestically. In order to enjoy the benefit of external debt it has to be used for viable investments and not for consumption. However, the case of Nigeria is pitiable and has not yielded desired growth because our politicians siphoned the fund for their selfish aggrandisement.

2.1.5 Interaction between External Debt and Economic Growth

Inability of the developing countries to manage external debt properly has led to crisis and instability which hindered their growth. For analysing the effect of external debt burden economists have propounded the following theories, namely the crowding out effect theory and the debt overhang theory. Foreign debt can affect growth via increased debt servicing which are likely to "crowd out" both public and private investment Cohen (1993) and Clement et al (2003). Crowding out effect occurs when the nations funds that

are gained from foreign exchange are consumed in debt servicing. Which brings about reduction in the resources available for use by the local industries. The fund is used up in servicing debt burden and as such impedes development.

Tayo 1993 assets that the effect of debt servicing hinders growth due to debt incurred liquidity problems which contracts infrastructural and other developmental investment by the government. When the nation loses it focus on developing the domestic industries to settlement of debt burden liquidity problems occurs. So, the government will not have sufficient resources to create investment and social infrastructural that will lead to its growth. Debt overhang – when a nation acquires debt higher than it repayment ability, debt overhang takes place. Debt overhang takes place when the expected debt service amount is higher than the amount it was contracted for (Krugrian, 1982).

Borensztein (1990) opined that debt occurs when the gain obtained for by the borrowing nations are inimical. Overhang occurs when the gain derived from external debt by the nation are too low compared to returns on increased investment. So debt overhang refers to when increased debt burden deters private investors from embarking in viable projects as a result of huge payment of taxes imposed by the government (tax disincentive). When tax disincentive occurs, some investors give up out of fear and this is inimical for any growing nation because it slows down development.

Clement et al (2003) holds that increased external debt can promote investment up to a stage when debt overhang sets in and the willingness of the investors to provide resources begin to diminish. Audu (2004) holds that debt burden has hindered growth are aggravate some vices in Nigeria economy. Ekperiware et al (2005) opined that the useful resources that Nigerian would have used to improve domestic industries are being indirectly tax away via debt service payment. The dilemma is that both foreign investors are thrown to immerse risk and the domestic investors are not encouraged to thrive, so it becomes difficult if not impossible for the economy to grow.

2.2 Theoretical Framework

This study is based on dual gap theory. Chenery and Strout, (1966) governments borrows to augment their limited resources so as to bridge the savings investment. Dual gap theory holds that investment is a function of savings while development is a function of investment. Therefore, when there is insufficient savings that will bring about a desired level of investment needed for development to take place. The equivalent amount (Gap) could be borrowed and used for the desired investment.

Moreover, if foreign loans are to be added to the local resources the amount of import becomes greater than export that is M>E where M = import and E=export. Excess of investment over locally generated savings is equal to excess of import over export according to the National Income Accounting. It also holds that income is equal to consumption + import + savings. output = consumption + export + investment income = output.

2.3 Empirical Review

Izedonmi and Ilaboya (2012) conducted research on the impact of economic growth in Nigeria. Their work was based on time series data ranging from 1980 to 2010. The analysis applied was co-integration and error correction method. It estimated the relationship between economic growth and some other economic variables. The result shows a significant negative relationship between public debt burden and economic growth, while there was a negative and significant effect of debt service ratio to export on economic development. Their recommendation was that both the state government and other government parastatals should be banned from acquiring loan unless when it is mostly needed. To alleviate the effect of debt burden on economic growth, meticulous effort should be made on repayment of loans.

Ezeabasili, Isu and Mojekwe studied the relationship between Nigeria's external debt and economic growth. It used time series data from 1975-2006. In the analysis Johansen co-integration method, error correction approach and granger causality test were applied. Error correcting test shows that external debt had negative relationship with economic growth in Nigeria i.e. 1% increase of external loan brings about a decrease of 0.027% in GDP. Then 1% percentage increase in total debt services bring about 0.034 percentage decrease in GDP. However, both of them reflects a relationship of 10% significant level. The granger causality test shows that uni-directional causality exist between external debt servicing and economic growth at 10% significant level. Granger test revealed that external debt service payment is of 1% significant level. However, an interdependent relationship exists between economic growth and foreign debt. The writers recommended based on their findings that acquisition of debt for investment purposes should be via so many sources and that the repayment should be timely to avoid over dependence on debt.

Obademi (2012) studied the impact of economic growth in Nigeria. The augmented Douglas model was used for the analysis. To investigate the impact of foreign debt on economic growth co-integration method was applied.

The result revealed that in a long run, the impact of debt on economic growth was negative and quite significant while in the short run, the impact of debt in economic growth are positive. The Error Correction mechanisms revealed a slow speed in the rate with which short run equation moves to equilibrium in a long run. Based on the findings, the researcher concluded that it was poor management of debt that made the impact of debt on economic growth at long run to be negation because it was positive and yielded much fruits within the short run.

Suliman et al (2012) investigated the effect of external debt on the economic growth of Nigeria using the time series data from 1970-2010. Ordinary Least Squares OLS, Johansen co-integration, Augmented Dickey-fuller unit root test and Error connection techniques were applied. Co-integration test reveals a long run relationship within the variables while error correction model showed that foreign loan has a positive effect on the economic growth of Nigeria. Based on the findings, the researcher recommended that Nigeria should combat both economic and political instabilities in order to give room for adequate debt management. Audu (2004) studied the impact of external debt on the

economic growth and public investment in Nigeria using a time series data from 1970-2002. The analysis was done using Johansen co-integration test and vector error correction method. The result showed that Nigeria debt service burden had a significant and negative effect on economic growth and negative effect on public investment. Ogunmuyiwa (2011) investigated how external debt promotes the economic growth of Nigeria. It adopted a time series data from 1970-2007. Augmented Dickey-fuller test, Granger causality test, Johansen co-integration test and vector error correction econometric techniques were used for the analysis. From their findings no causality was seen between external debt and economic growth in Nigeria.

Ayadi (2008) investigated the impact of foreign loan with its servicing on the economy of Nigeria and South Africa. The econometric techniques employed were the Ordinary Least Square and Generalised Least Square Method. The result showed that debt payment/service requirement has a negative impact on the economic growth of both South African and Nigeria. Faraji and Makame (2013) studied the impact of external debt on Tanzanians economic growths. The study used a time series data from 1990-2010. Johansen co-integration technique was applied, and the finding revealed that external debt has a positive effect on the economies of both Nigeria and South Africa. Debt servicing was found to have a negative impact on both economies. The research recommended that an indebt research on the impact of foreign debt on foreign direct investment (FDI) and domestic revenue should be carried out.

Safdari and Mehrizi (2011) investigated the external debt and economic growth in Iran using a time series data from 1974 to 2007. Vector autoregressive model (VAR) technique was applied to find the relationships of some macroeconomic variables such as GDP, private investment, public investment, import and external debt. The result showed that external debt had a negative impact on the gross domestic product and private investment, but public investment had a positive impact on the private investment in Iran.

Ajayi and Okei (2012) carried out a study on foreign debt burden and economic growth and development of Nigeria. Ordinary least square technique was used for the analysis. The result showed that foreign debt burden had a negative effect on the national income and per capital income of Nigeria. It was also founded that huge level of foreign debt acquisition brought about the devaluation of the Nigeria currency, and other macroeconomic issues that include increase in retrenchment of workers, industrial strike action, poor educational system and poor economic growth. Based on their findings they recommended that foreign debt should be used strictly for investment that can generate the fund that will be used for its repayment and that the value of debt servicing payment should not exceed foreign exchange earnings.

Clements, Bhattacharya and Nguyen (2003) investigated the channels through which eternal debt affect growth in low income countries. The economy techniques used were the Johansen co-interesting test. It was founded that reasonable decrease in the external debt stock brought about a substantial increase in the per-capital income and economic growth. They recommended that debt service relief should be used for public investment.

3. Data and Methodology

In the estimation of variable under study, this study uses a multiple regression (OLS) model. The data is firstly tested for stationarity using the Augmented- Dickey-Fuller (ADF) tests. In order to test for cointegration, the Johansen cointegration technique is used. For Normality test (Jarque-Bera) and serial correlation were used.

3.1 Model Specification

The study modifies the model adopted by Ajayi and Okei (2012) they studied the effect of external debt burden on economic growth and development of Nigeria they adopted the regression analysis of OLS. In modifying the model in equation 1, this study adds two variables which are gross national income and exchange rate. The empirical model of the study, therefore, is specified as follows:

$$GDP_t = \beta 0 + \beta 1EXTDit + \beta 2MSt + \beta 3exrt + \varepsilon. \quad (2)$$

All the variables used in this study are converted to natural logarithms so as to minimize the impact of outliers and to obtain elasticity coefficients of these variables.
Where:
GDP = Real gross domestic product;
EXTD = External debt;
MS = Money supply;
EXR = External debt;
β0, β1, β2, β3 = coefficients of the parameter estimates;
ε.= Error term.

4. Results and Discussion

The study is aimed at exploring the implication of external debt burden on economic growth in Nigeria.

Table 1: Descriptive Statistics

	GDP	MS	EXTD	EXR
Mean	49398726	10936859	1314910.	168.1884
Median	49856099	9411112.	451461.7	149.5800
Maximum	69799942	28669585	4890270.	306.9200
Minimum	23688280	878457.3	10.71800	109.5500
Std. Dev.	16132189	9191006.	1747879.	65.25053
Skewness	-0.156065	0.578567	0.958119	1.452847
Kurtosis	1.599034	2.068538	2.272629	3.648464
Jarque-Bera	1.630936	1.746875	3.325822	7.016987
Probability	0.442432	0.417514	0.189586	0.029942
Sum	9.39E+08	2.08E+08	24983287	3195.580
Sum Sq. Dev.	4.68E+15	1.52E+15	5.50E+13	76637.37
Observations	18	18	18	18

Source: Author's computation from E-view 8.

Table 1 shows the basic aggregative averages like mean, median and mode for all the observations. The mean of the variables is 49398726, 10936859, 1314910 and168.1884. 4.68E+15, 1.52E+15, 5.50E+13 and 76637.37 are the spread and variations in the series. The table shows that EXR has degree of peakedness (kurtosis) in excess of 3.

4.1 Tests for Stationarity

Table 2: Summary of the ADF Unit Root Test

Variables	ADF Test Statistic	Critical Values at 5%	P Value	Order of Integration
GDP	-3.939501	-3.081002	0.0104	I(1)
EXTD	-3.516599	-3.065585	0.0216	I(1)
MS	-6.201680	-3.144920	0.0002	I(1)
EXR	-3.839008	-3.052169	0.0110	I(1)

The test for stationarity properties of the series following the Augmented Dickey Fuller statistics in Table 2 showed that all the series are stationary at order 1.

4.2 The Johansen Cointegration Test

Rank Test is not only used to confirm the existence of cointegration but would further unveil the number of cointegrating vectors.

Trend assumption: Linear deterministic trend
Series: GDP MS EXTD EXR
Lags interval (in first differences): 1 to 1

Unrestricted Cointegration Rank Test (Trace)

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None *	0.852914	68.55323	47.85613	0.0002
At most 1 *	0.723324	35.96867	29.79707	0.0086
At most 2	0.481568	14.12520	15.49471	0.0796
At most 3	0.159660	2.957131	3.841466	0.0855

Trace test indicates 2 cointegrating eqn(s) at the 0.05 level
* denotes rejection of the hypothesis at the 0.05 level
**MacKinnon-Haug-Michelis (1999) p-values

Unrestricted Cointegration Rank Test (Maximum Eigenvalue)

Hypothesized No. of CE(s)	Eigenvalue	Max-Eigen Statistic	0.05 Critical Value	Prob.**
None *	0.852914	32.58456	27.58434	0.0104
At most 1 *	0.723324	21.84347	21.13162	0.0397
At most 2	0.481568	11.16807	14.26460	0.1460
At most 3	0.159660	2.957131	3.841466	0.0855

Max-eigenvalue test indicates 2 cointegrating eqn(s) at the 0.05 level
* denotes rejection of the hypothesis at the 0.05 level
**MacKinnon-Haug-Michelis (1999) p-values

Maximum Eigen Value Test which did not only show evidence of cointegration but also confirmed the existence of two cointegrating vectors. This depicts a long correlation between the variables.

The hypotheses stated earlier in this research were tested using the following methods the Ordinary Least Squares and decision rule is if the coefficient estimate of the independent variable has a positive sign and its probability value less than 0.05, the null hypothesis is rejected and alternate hypothesis accepted. On the other hand, if the coefficient estimate of the independent variable does not have a positive sign and its probability greater than 0.05, the null hypothesis is accepted and alternate rejected.

Dependent Variable: GDP
Method: Least Squares
Included observations: 18

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	45643101	3721550.	12.26454	0.0000
MS	2.176576	0.409104	5.320348	0.0001
EXTD	-1.313025	1.006400	-1.304674	0.2117
EXR	-108941.9	45196.18	-2.410423	0.0292

R-squared	0.949629	Mean dependent var	49398726
Adjusted R-squared	0.939555	S.D. dependent var	16132189
S.E. of regression	3966198.	Akaike info criterion	33.40918
Sum squared resid	2.36E+14	Schwarz criterion	33.60801
Log likelihood	-313.3872	Hannan-Quinn criter.	33.44283
F-statistic	94.26338	Durbin-Watson stat	1.950204
Prob(F-statistic)	0.000000		

GDP = 45643101 + 2.18MS - 1.31EXTD - 108941.9EXR

The above regression showed that external debt burden had a negative and insignificant effect on economic growth in Nigeria from 2000-2018 (Coefficient = -1.31, p-value = 0.2). The relationship implies that a reduction in external debt burden by 1% will encourage economic growth by 45643101. Other accompanying variables like money supply showed

a positive and significant effect on Gross domestic growth while exchange rate showed a negative and significant effect on economic growth. This result partly agreed with the Safdari and Mehrizi, 2011) analyzed external debt and economic growth in Iran by observing the balance and long-term relation of five variables (GDP, private investment, public investment, external debt and imports). They employed time series data covering the period 1974-2007and the vector autoregressive model (VAR) technique of estimation was employed. Their findings showed that external that has a negative effect on GDP and private investment.

The R^2 which is a show of the goodness of fit of the model is 94% which means that 94% of variation in gross domestic product was explained by the regressors and about 6% of the relationship is explained by factors not captured by the model. The adjusted R^2 of about 93% takes account of a greater number of regressors if included and it will still explain 4% variation in the dependent variable.

5. Conclusions and Recommendations

The study was aimed at exploring the effect of external debt burden on economic growth in Nigeria. Therefore, the study concludes that external debt burden had a negative and insignificant effect on economic growth in Nigeria within 2000-2017. Money supply showed a positive and significant effect on GDP while exchange rate showed a negative and significant effect on economic growth. The study recommended that alternative sources of government revenue should be utilized fully for this will minimize dependence of government on borrowed funds to ratify the economy. Loans should be sourced internally so that when the principal and interest on the loans are paid back; it will serve as a crowd-in-effect which in turn further accelerates economic activities in the country. Finally, government should provide enabling environment so that micro, small and medium enterprises can drive for this will encourage domestic production and export.

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