Effect of Public Debt on the Economic Growth of Nigeria (1986 – 2020)

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Abstract: **This study examined the effect of public debt on economic growth in Nigeria. Specifically, the effect of domestic debt and external debt on real gross domestic product was ascertained. This study applied a test of causation to determine the effect of public debt on economic growth in Nigeria from 1986 to 2020. The secondary data were obtained from the Central Bank of Nigeria (CBN) statistical bulletin of various issues. The dependent variable is economic growth measured by real gross domestic product, while the independent variable is public debt measured by domestic debt and external debt. The short-run relationship depicted that domestic debt has insignificant negative relationship with economic growth in Nigeria, whereas external debt has positive significant relationship with economic growth. With respect to the effect of domestic debt and external debt on economic growth, the granger causality test revealed that there is a bidirectional causal relationship between domestic debt and economic growth in Nigeria. This is to say that domestic debt has significant effect on economic growth. Similarly, it was also found that economic growth exerts significant effect on domestic debt. Though external debt would not be considered as an evil fiscal policy arrangement of the government, external loans contracted should be properly and efficiently channeled to capital expenditure which improves the manufacturing sector capacity, generates employments and reduced poverty which ultimately result in the acceleration of the pace of economic growth.**

***Keywords*: Public debt; economic growth, domestic debt, external debt, gross domestic product.**

I.INTRODUCTION

Public debt has continued in an upward trend, as experienced by many developing countries of the world, and is now attracting global attention. Public debt is been incurred mostly by borrowing, especially when the government is unable to raise enough revenue locally to carry out its obligation to its citizens. This implies that whenever there is a budget deficit most times the government resorts to borrowing in other to bridge the gap/shortfalls. Chinanuife, Eze, and Nwodo (2018) posits that the practice of borrowing is not bad if borrowed funds are used judiciously. Following the fall in oil prices, variation in the exchange rate, etc., which has brought adverse effects to some developing nations of the world such as Nigeria, it is therefore imperative to reflect on the economic implication of the country's growing debt record, and it is a very important issue which needs broad public debate. Therefore, increasing levels of the public debt of a country can be harmful to the growth of the economy of any country if not well utilized (Favour, Ideniyi, Oge & Charity, 2017).

Public debt, therefore, refers to the amount of money that federal government, state government, and local government owe at any time, which could manifest in any of the two major forms; internal (domestic) and external (foreign) debt and it accrues when the government is experiencing a budget deficit. In other words, all the money that government owes at all levels is defined as public debts. It can be in the form of services like pension payment owing to his employee both domestically or externally, or any contract entered by the government and could not pay. If the government is having a budget deficit and the government has a reputable economy and trusted system with strong economic indices, such government can generate revenue by issuing its bonds for other nations, individuals, and groups to subscribe to. Any government that lacks trust in the world to issue bonds for people to purchase will be left with no option than borrow from either external institutions or domestic institutions with an unfavorable or favorable interest rate (Akinwunmi & Adekoya, 2018).

When the budget deficit of any government rises, it will lead to an increase in public debt. Public debt can be classified into different types such as long-term debt and short-term debt. External debt refers to any financial resources which government, organizations are using that are borrowed from foreign counties or financial institutions other than the country's resources. Whether it is borrowing from Bank, investments from private individuals, or investment firms, it has merit and demerit, therefore anyone who wants to borrow from international institutions should consider the advantages and disadvantages associated with it before setting out to secure the fund (Akhanolu, Babajide, Akinjare, Oladeji & Osuma, 2018). Domestic Debt is defined as debt that the government borrowed within the country, it involves the same currency (Egbetunde, 2012). Therefore, all the amount of money that government owes internally such as Treasury Bills, Treasury Certificates, Federal Government Development Stock, Ways and Means Advances, and Treasury Bonds is regarded as domestic debt. Economic growth according to many economists refers to the total value of all final output that a country can produce within a year valued at market prices as adjusted for price changes plus the

imputed value of the economy's produced goods and services that do not pass through the market channel minus net income from abroad (Blake, 2015). This is observed as an increase in the country's productive capacity when measured up to one period of time to another. Therefore, growth in an economy is seen when the total output of goods and services increases when measured with the previous years. An upward growth (positive growth) simply means an increase in the output of that particular economy which is called a boom while downward growth (negative growth) means that the total output of goods and services produced in an economy in a particular year had fallen when compared to its value the previous years.

Obademi (2012) stated that the composition of a country's debt influences the citizens, government, private enterprises such as banks, and subsequently the entire economy. Therefore, all the sector of the economy is affected by public debt size and its means of repayment. So before borrowing money either externally or internally, the country in question should consider if the purpose of borrowing will lead to the growth of the economy. He opined that country borrow for the following three reasons: when government expected revenue is less than their proposed expenditure (a budget deficit) in a particular fiscal year and the country borrow to finance budget deficit; again, that debt arises as a result of the execution of productive investment and also that government borrowing to finance an important capital project like water dam, river basin development project, and agricultural development projects. So many economists and researchers are of the view that if a country borrows to a reasonable extent; it will increase national output while some economists think that high debt reduces growth. In light of the above disparity, this study focuses on identifying the effects of public debt on economic growth in Nigeria.

II. LITERATURE REVIEW

Public debt also referred to as government debt is conceptualized as the aggregate debts owed by a certain country to individuals, corporations, and countries within the country or abroad. Government debts typify all forms of government borrowings at all levels of government (Christabel, 2013). Public debt forms part of the finance approach adopted by governments all over the world, although this approach is often resorted to when all measures have been exhausted the measure is considered favorable relative to other measures which include the creation of money and the sale of national assets (Martin, 2009; Ajayi & Edewusi 2020). Also, debt overhang influences economic improvement and the effectiveness of monetary policies, export growth, and reduces the severity of trade policies thereby enhancing the friendliness of the market and by implication increasing trade openness. Economic growth occurs in an economy whenever a unit of production is successfully inputted into the economic system. Hence, we say that economic growth describes the number of goods and services created, with less concern about how the products or services are produced (Matiti & Muhtar, 2013). Notwithstanding, economic growth estimates growth in monetary terms and considers no other areas of development (Ayres & Warr, 2006). The effect of domestic debt is part of the complex issues influencing the structural stability of the Nigerian economy over time. Debt challenges are occasioned by debt servicing which consumes a noticeable part of savings created for public investment as well as the increasing uncertainty connected with the future increase in government financial crisis. Based on this premise, it is critically required for debt servicing to not reduce funds provided for the improvement of human development (Fadare, 2010). Albeit, this is a far cry from the situation in Nigeria, following the unfavorable situation of infrastructures, low level of employment, increasing poverty ratio, and high illiteracy level.

Literature have documented theories such as the Keynesian theory of public debt, the classical theory of public debt, and the Ricardo theory of public debt among others. This study was restricted to the Ricardo theory of public debt. The theory was postulated by Ricardo in 1819. Ricardo's theory of public debt holds that financing public expenditure could be productively attained by sourcing funds from sectors and communities with excess economic resources to reduce inequality. He stated that the reason for this is because the prioritization of a certain sector for the settlement of public expenditure does not impact positively on the growth of the economy but rather it impoverishes the state despite large amounts of public debts and taxes raised. Similarly, this research argued that the payment of interest of debt extorts a significant amount of wealth from the society to a different economy thereby impoverishing the state.

Akhanolu, Babajide, Akinjare, Oladeji, and Osuma, (2018) evaluated the effect of public debt on economic growth in Nigeria. The quantitative research technique was adopted, secondary data from 1982-2017 was gathered. Inferential analyses were conducted and findings from the study demonstrated that internal debt exerts a positive impact on economic growth while external debt revealed an inverse relationship with economic growth. Premise on the findings, the study suggested that borrowed funds particularly external debt should be minimized.

Favour, Ideniyi, Oge, and Charity (2017) assessed public debt and economic growth in Nigeria. Specifically, the study investigate the extent to which foreign debt impacts national output in Nigeria; ascertained if domestic debt significantly impacts national output in Nigeria; determined the degree of causal relationship existing between the explanatory variables and national output in Nigeria. The study adopted the quantitative research method. Secondary time series data spanning forty-five years (1970-2015) was amassed in the study from the Central Bank of Nigeria. Results stemming from the study revealed that external debt has a significant negative impact on economic growth within the period under study; domestic debt (DMD) has a significant negative relationship with economic growth within the period

under consideration and external debt and domestic debt granger cause RGDP in Nigeria with causality running from external debt and domestic debt to RGDP. Premise on the result, the study suggested the government should reduce external debt and the ones obtained should be strictly used for purposes intended to ensure the positive effect and the government should cut down on domestic borrowing.

Udeh, Ugwu and Onwuka (2016) ascertained the impact of external debt on economic growth in Nigeria. Ex-post facto research design was adopted for the study. While data on Gross Domestic Product (GDP), External Debt Stock and External Debt Service Payment were obtained from World Bank International Debt Statistics, Exchange Rate data were collected from Central Bank of Nigeria Statistical Bulletin, 2013. The period of study was 1980-2013. Model was formulated and data were analysed using Ordinary Least Square. Diagnostic tests were conducted using Augmented Dick Fuller Unit Root Test, Co-integration and Error Correction Model. The independent variable was GDP, while the explanatory variables were External Debt Stock, External Debt Service Payment and Exchange Rate. They discovered that External Debt had a positive relationship with Gross Domestic Product at short run, but a negative relationship at long run. Also, while External Debt Service Payment had negative relationship with Gross Domestic Product, Exchange Rate had a positive relationship with it.

Onyekwelu, Okoye and Ugwuanyi (2014) evaluated external debts management strategies in developing economies and its implications on some key economic indices using Nigeria as a case study. The study adopted both the content analysis and the empirical approach. Data for this study were basically secondary data. The quantitative data for analysis were gathered from the statistical bulletins/releases of relevant government agencies like the Debt Management Office, Central Bank and the Office of the Accountant General of the Federation. The qualitative information was sourced via textbooks, and scholarly journal publications accessed through the internet. Data were analysed using the Linear Regression and Analysis of Variance (ANOVA). The linear regression showed that there is a positive and significant relationship between the size of External Debts and Gross Domestic Product (GDP), Capital Expenditure, External Reserves and Exports. However, the Analysis of Variance (ANOVA) reveals a negative correlation between External Debts and the variables studied. The study attributes this anomaly to mismanagement of credit facilities, unfavourable loan terms characterized by capitalization/compounding of interests, weak economic base, poorly co-ordinated statistics on loans and overdependence on foreign aids among others.

Imimole, Imoughele and Okhause (2014) ascertained the extent to which Nigeria's external debt relates to indices of ability to pay in order to ascertain the sustainability of it and to identify the main determinants of her external indebtedness for the period 1986 to 2010. Based on available data and the use of statistical methods, they observed that Nigeria's external debt is not sustainable in terms of willingness and ability to pay, and that the country's external debt is characterised by capital flight as a results of external debt accumulation which is evident in the ratio of the country's reserves to external debt. The result from cointegration test showed presence of long run relationship between external debt and the explanatory variables. The study also found that the main determinants of Nigeria's external debt are gross domestic product, debt service and exchange rate.

Emerenimi and Anyanwu (2015) evaluated the effectiveness of external debt on economic growth within a span of 1981-2012. The data were collected from CBN Statistical Bulletin 2010 and the Debt Management Office (DMO) quarterly report. The Engle and Granger Cointegration and Ordinary Least Square (OLS) were employed in the cause of this study. The result of the analyses showed that rising external debt stock inhibits the pace of economic growth of Nigeria by increasing the cost of its servicing beyond the debt sustainability limit while external debt servicing was found not to impair economic growth.

Obademi (2015) examined the impact of public debt on economic growth using Nigeria as a case study. An analysis of the long-run relationship and impact of debt from the perspective of the value impact and proportional impact was done. The proportional impact variables are ratios of the value impact to the gross domestic product (GDP). An augmented Cobb Douglas model was used and subsequently a dynamic version of the functional relationship was estimated using Cointegration technique to capture the long-run impact of debt variables on economic growth. The result showed that the joint impact of debt on economic growth is negative and quite significant in the long-run though in the short-run the impact of borrowed funds and coefficient of budget deficit is positive.

Ijeoma (2013) assessed the Impact of Debt on selected macroeconomic indicators in Nigerian economy for the period 1980-2010. Data for the study were collected from Debt Management Office, CBN Statistical Bulletin, and internet materials and analysed with Linear Regression. The study found that Nigeria's external debt stock has a significant effect on her economic growth. It also revealed that there is a significant relationship between Nigeria's Debt service payment and her Gross Fixed Capital Formation.

Gabdo and Aminu (2013) analysed the impact of external on economic growth in Nigeria. The time series data were derived from various secondary sources such as: the Central bank of Nigeria statistical bulletins, Economic and Financial Review and Annual reports, statement of accounts and Federal Office of Statistics (FOS)and Debt Management Office (DMO) publications and website from 1992-2012. The estimated techniques includes the Ordinary Least Square (OLS) method, Augmented Dickey- Fuller (ADF) unit root

test, Johansen Co-integration test and Error Correction Method (ECM). The results revealed that external debt impacted positively on the economic performance of Nigeria.

Egbetunde (2012) examined public debt and economic growth in Nigeria. The study employed the quantitative research method. Secondary time series data spanning forty years (1970-2010). Data gathered in the study was analyzed using Augmented Dickey-Fuller and Philip Perron test. Results stemming from the study revealed that public debt exerts a long-run impact on economic growth. The findings of the VAR model also demonstrated that there is bi-directional causality between public debt and economic growth in Nigeria. Based on this finding, the study recommended that the Nigerian government should source for loans within the economy.

III. METHODOLOGY

This study applied a test of causation to determine the effect of public debt on economic growth in Nigeria from 1986 to 2020. The secondary data were obtained from the Central Bank of Nigeria (CBN) statistical bulletin. The study employed the Granger Causality framework to estimate the model. The choice of this method of estimation is that it is well suited to predict the ability of one variable to affect or cause another to move at a specified direction. Before estimating the model, we first determined the unit root properties of the data using the Augmented Dickey-Fuller (ADF) tests. This is to provide support that the data are free from stationarity defect that may cast a dent on the reliability of the regression output. The ADF test were performed at level and first difference however, it was the result of the first difference that was reported due to the fact that most time series data are not stationary at level form. Secondly, we ascertained the short-run and co-integration/long-run relationship between economic growth and public debt by applying the Autoregressive Distribute Lag (ARDL)/Bound test technique. This is on the argument that the ARDL fundamentals take into consideration the different order of integration of time series data. The dependent variable is economic growth measured by Real Gross Domestic Product (RGDP), while the independent variable is public debt measured by Domestic Debt (DD) and External Debt (ED). It is expected that domestic debt and external debt should have a negative relationship with real gross domestic product in Nigeria. This is hinged to the available report from the Debt Management Office (DMO) on the rising cost of Nigeria's debt profile. A modified model of Egbetunde (2012) was adapted. The original model of Egbetunde (2012) is expressed as:

$$RGDP = f(PUD) \qquad Equ.1$$

Having modified Egbetunde (2012) model, the model of this study is econometrically stated as:

$$RGDP_t = \beta_0 + \beta_1 DD_t + \beta_2 ED_t + \varepsilon_t \qquad Equ.2$$

Where:

$RGDP$ = Real gross domestic product

DD = Domestic debt

ED = External debt

β_0 = The constant term

$\beta_1 - \beta_2$ = The coefficients of the independent variables

ε = the random disturbance term

IV. RESULTS AND DISCUSSION

This study applied the Augmented Dickey-Fuller (ADF) unit root test determine the stationarity properties of the data to avoid the problem of spurious regression. Due to the mixed order of integration of the variables, Table 1 presents only the unit root result of the variables at first difference. As can be seen from the ADF result, the variables are all stationary at first difference, hence the result of the regression output would be deemed to be reliable in statistical perspective.

Table 1: ADF Test Result

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

Source: Statistical Output from E-views 10.0

P-values are in parenthesis, while * and ** represent 1% and 5% level of significance respectively

The bound testing technique was used to evaluate the long-run relationship between public debt and economic growth in Nigeria. The result in Table 2 shows that there is a long-run relationship between public debt and economic growth in Nigeria. This assertion is deduced on the basis that the f-statistic of 6.79 is higher than the upper and lower critical bond values of 3.87 and 3.10 respectively. An implication that economic growth, domestic debt and external debt are significantly related in the long-run at a significant value of 5%.

Table 2: ARDL Bounds Test

T-Test	5% Critical Value Bound		Remark
F-Statistic	Upper Bound	Lower Bound	
6.797005	3.87	3.1	Null Hypothesis Rejected

Source: Statistical Output from E-views 10.0

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

debt significantly leads to reduction in economic growth by a factor of 1.06. This disagrees with the findings of Akhanolu, Babajide, Akinjare, Oladeji, and Osuma, (2018) that domestic debt has positive relationship with economic growth but is in affirmation with Favour, Ideniyi, Oge, and Charity (2017) that domestic debt is negatively related to economic growth in Nigeria. A unit increase in external debt has the tendency to rising economic growth by a 40.09%. Put differently, the higher the external debt the higher the gross domestic product of Nigeria. This supports the work of Onyekwelu, Okoye and Ugwuanyi (2014) and Gabdo and Aminu (2013) that external debt is positively related to gross domestic product of Nigeria. However, is conflicts with the finding of Akhanolu, Babajide, Akinjare, Oladeji, and Osuma, (2018), Udeh, Ugwu and Onwuka (2016) and Emerenimi and Anyanwu (2015) and on the negative effect of external debt on economic growth of Nigeria.

Table 3: ARDL Short-Run Relationship

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

Source: Statistical Output from E-views 10.0

The adjusted R-square reveals that 99.82% changes economic growth was attributable to the joint fluctuation in domestic and external debt. This is supported by the p-value (0.0000) of the f-statistic (1726.157) which is significant at a level of 5%. The Durbin Watson value of 1.75 is within the acceptable range of no autocorrelation in the estimated model.

With respect to the effect of domestic debt and external debt on economic growth, the granger causality test in Table 4 reveals that there is a bidirectional causal relationship between domestic debt and economic growth in Nigeria as causality runs in both direction at a significant level of 5%. This is to say that domestic debt has significant effect on economic growth on one hand, while on the other hand, domestic debt is significantly affected by economic growth. This supports the findings of Favour, Ideniyi, Oge, and Charity (2017) that domestic debt granger cause economic growth in Nigeria. On the contrary, external debt has no significant effect on economic growth in Nigeria because causality does not flow in either direction that is, from external debt to economic growth or from economic growth to external debt. This also of Favour, Ideniyi, Oge, and Charity (2017) who study revealed that external debt has significant effect on Nigeria economic growth.

Table 4: Granger Causality Test

Null Hypothesis:	Obs	F-Statistic	Prob.	Remarks
DD does not Granger Cause RGDP	34	27.8249	0.0000	Causality
RGDP does not Granger Cause DD		8.80673	0.0057	Causality
EX does not Granger Cause RGDP	34	1.46826	0.2348	No Causality
RGDP does not Granger Cause ED		2.75836	0.1068	No Causality

Source: Statistical Output from E-views 10.0

V.CONCLUSION AND RECOMMENDATIONS

Nigeria's debt crisis can be attributed to both exogenous and endogenous factors such as the nature of the economy, economic policies, dependency on oil, dwindling foreign exchange receipts etc. The origin of Nigeria's external debt dates back to 1958. Debt service payments were within manageable limits until 1982, but became unmanageable in 1983 because of the preference for private lending. However, Nigerian political leaders need to develop home grown policies to enhance the country's competitive advantage in the international market in this era of globalization. Besides, conscious efforts must be made to secure total exit from all forms of commercial debts that exposes the country to another regime of debt overkill. Nigeria must also explore and

develop more export products outside crude oil. Though external debt would not be considered as an evil fiscal policy arrangement of the government, external loans contracted should be properly and efficiently channeled to capital expenditure which improves the manufacturing sector capacity, generates employments and reduced poverty which ultimately result in the acceleration of the pace of economic growth. The government of Nigeria can follow the framework of debt swap in order of reduce the large percentage of her revenue used in repaying loans of default on debt service payment. In this scenario, the government can negotiate creditor organization or institutions to reduce the debt owed and invest the reduced amount into agreed sustainable projects for economic growth and development using the local currency.

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APPENDIX

Table 5: Data for Analysis

Year	Real Gross Domestic Product ₦'Billion	Domestic Debt Outstanding ₦'Billion	External Debt Outstanding ₦'Billion
1986	15,237.99	28.44	41.445
1987	15,263.93	36.79	100.79
1988	16,215.37	47.03	133.96
1989	17,294.68	47.05	240.39
1990	19,305.63	84.09	298.61
1991	19,199.06	116.20	328.45
1992	19,620.19	177.69	544.26
1993	19,927.99	273.84	633.14
1994	19,979.12	407.58	648.81
1995	20,353.20	477.73	716.87
1996	21,177.92	419.98	617.32
1997	21,789.10	501.75	595.93
1998	22,332.87	560.83	633.02
1999	22,449.41	794.81	2,577.37
2000	23,688.28	898.25	3,097.38
2001	25,267.54	1,016.97	3,176.29
2002	28,957.71	1,166.00	3,932.88
2003	31,709.45	1,329.68	4,478.33
2004	35,020.55	1,370.33	4,890.27
2005	37,474.95	1,525.91	2,695.07
2006	39,995.50	1,753.26	451.46
2007	42,922.41	2,169.64	438.89
2008	46,012.52	2,320.31	523.25
2009	49,856.10	3,228.03	590.44
2010	54,612.26	4,551.82	689.84
2011	57,511.04	5,622.84	896.85
2012	59,929.89	6,537.54	1,026.90
2013	63,218.72	7,118.98	1,387.33
2014	67,152.79	7,904.03	1,631.50
2015	69,023.93	8,837.00	2,111.51
2016	67,984.20	11,058.20	3,478.91
2017	68,490.98	12,589.49	5,787.51
2018	69,799.94	12,774.40	7,759.20
2019	71,387.83	14,272.64	9,022.42
2020	70,014.37	16,023.89	12,705.62

Source: Central Bank of Nigeria Statistical Bulletin 2020