

UNDERSTANDING THE NIGERIAN DOMESTIC DEBT

Abstract:

The Internal debt or domestic debt of a nation is the part of the total government debt in a country that is owed to lenders within the country. The internal and external debt stock makes up a country's public debt profile. In Nigeria, the domestic debt profile is currently experiencing an upward trend and as such created issues such as debt over-hang, increased debt service, exchange rate instability, and crowding out effects on the private sector, etc in the economy. The creation of a separate public debt management office like the DMO was therefore aimed at achieving the following advantages: good debt management practices, prudently raising financing to fund government deficits at affordable costs and manageable risks in the medium- and long-term; achieving a positive impact on overall macroeconomic management, including monetary and fiscal policies.

Keywords: public debt profile, macroeconomic management, domestic debt, exchange rate instability

1.0 INTRODUCTION

The existence of a market for government borrowing systems in Nigeria can be traced to the financial reforms introduced by the then colonial government in 1958. These reforms led to the creation of the Central Bank of Nigeria (CBN) and the creation of marketable Public Securities to finance the fiscal deficit. According to paragraph 35 of the Central Bank of Nigeria (CBN) Ordinance 1958, the bank shall be entrusted with the issue and management of Federal Government Loans publicly issued in Nigeria upon such terms and conditions as may be agreed within the Federal Government and the Bank.

Since the beginning of the debt crisis in 1982 which broke out as a result of misjudgments in the conduct of economic policies, there has been a lot of attention given to developing countries' debts, in terms of both total debt burden and governments' ability to repay and service such obligations.

Huge public debt is one of the biggest economic policy concerns plaguing many countries' economies, particularly developing and poor countries around the world. In general, these long-term developments have prompted major concerns among international financial institutions and bilateral lenders, prompting several efforts. However, the issue of domestic debt in emerging countries has the potential to significantly affect economic growth, government budgets, macroeconomic stability, and private-sector credit in any given economy.

In Nigeria, the domestic debt profile is currently experiencing an upward trend and as such created issues such as debt over-hang, increased debt service, exchange rate instability, and crowding out effects on the private sector, etc in the economy. This can be attributable to why in the recent past, academics, policymakers, and other analysts started focusing their interest in the area of domestic debt as it affects growth and development in global economies, particularly the severely externally indebted nations. It was in 1986, at the inception of Structural Adjustment Program (SAP) the level of external debt for the first time became larger than the level of domestic debt, (Asogwa, 2009). Ever since then, the stock of external debt has consistently been larger than domestic debt. Alison et al (2003).

However, President Olusegun Obasanjo's government in October 2005 attempted to reduce drastically the country's debt overhang. This was effectively achieved through the exit from the Paris Club of Nations. Nigeria and the Paris Club announced a final agreement for debt relief worth \$18 billion, thus resulting in an overall reduction of Nigeria's debt stock by \$30 billion and reducing the country's debt-to-GDP ratio.

The threshold ratios of debt to Gross Domestic Product (GDP) of countries vary from country to country depending on their debt sustainability. For instance, in Nigeria, according to the 2015 Debt Sustainability Analysis (DSA), the threshold was about 40 percent of GDP in the country currently attained about 25 percent which was within the range of the threshold at that time. Currently, as of November 2023, the debt-to-GDP ratio of Nigeria was 38.79 percent, which is still below the average of 56.3% for Sub-Saharan Africa.

The national debt of Nigeria has implications for the country's economic and social development, as well as its relations with other countries and international organizations. If this threshold

exceeds the threshold, the country could run into domestic debt-servicing problems and the associated effects on other macroeconomic goals. Hence, this will further lead to rescheduling the domestic and public debt on a non-market basis (Guidotti and Kumar, 1992).

2.0 WHAT IS DOMESTIC DEBT:

The Internal debt or domestic debt of a nation is the part of the total government debt in a country that is owed to lenders within the country. The internal and external debt stock makes up a country's public debt profile. Commercial banks, other financial institutions, and other members of the public, etc constitute the sources of funds for the domestic debts owed by a government; (money a government borrows from its citizens) is part of the country's national debt. Governments usually borrow by issuing securities, government bonds, and bills. It is a form of fiat creation of money, in which the government obtains cash not by printing it, but by borrowing it. The money created is in the form of treasury securities or securities borrowed from the central bank. These may be traded but will only rarely be spent on goods and services. In this way, the expected increase in inflation due to the increase in national wealth is lower than if the government had simply printed the money and increased the more liquid forms of wealth (i.e., the money supply). This is, however, different from the external debt a country borrows directly from a supranational organization (e.g. the World Bank, IMF) or International Financial Institutions.

3.0 TREND IN THE NIGERIA'S DOMESTIC DEBT PROFILE

After Nigeria's exit from the Paris Club of the nation, the external Debt began to experience consistence decline, while the domestic debt stock has grown continuously over the years to date, see chart below. Nigeria's domestic debt stock in 2000 stood at about N833,382.47 billion, while the external stock was N2,031,897.80 billion. After the exit of the Paris Club of Nations in 2005, both categories of debt declined while the domestic stock grew much more than the external debt. As of the end period of 2015, the domestic debt had risen to about N8,836,995.80 billion from N833,382.47 billion recorded in 2000.

The domestic or internal debt stock at the end of 2020 had risen significantly from N16,023,885.33 billion to about N22,210,364.595 billion at the end of 2022. The figure astronomically rose to about N50,196,102.87 billion as of September 2023. This significant

change can be attributable to the securitization policy of the federal government where all outstanding government's Ways and Means Advances issued by the Central Bank over time to the Federal Government were converted to the country's current domestic debt stock.

Table 1: Nigeria's Total Debt outstanding (2015-2023) N'Million

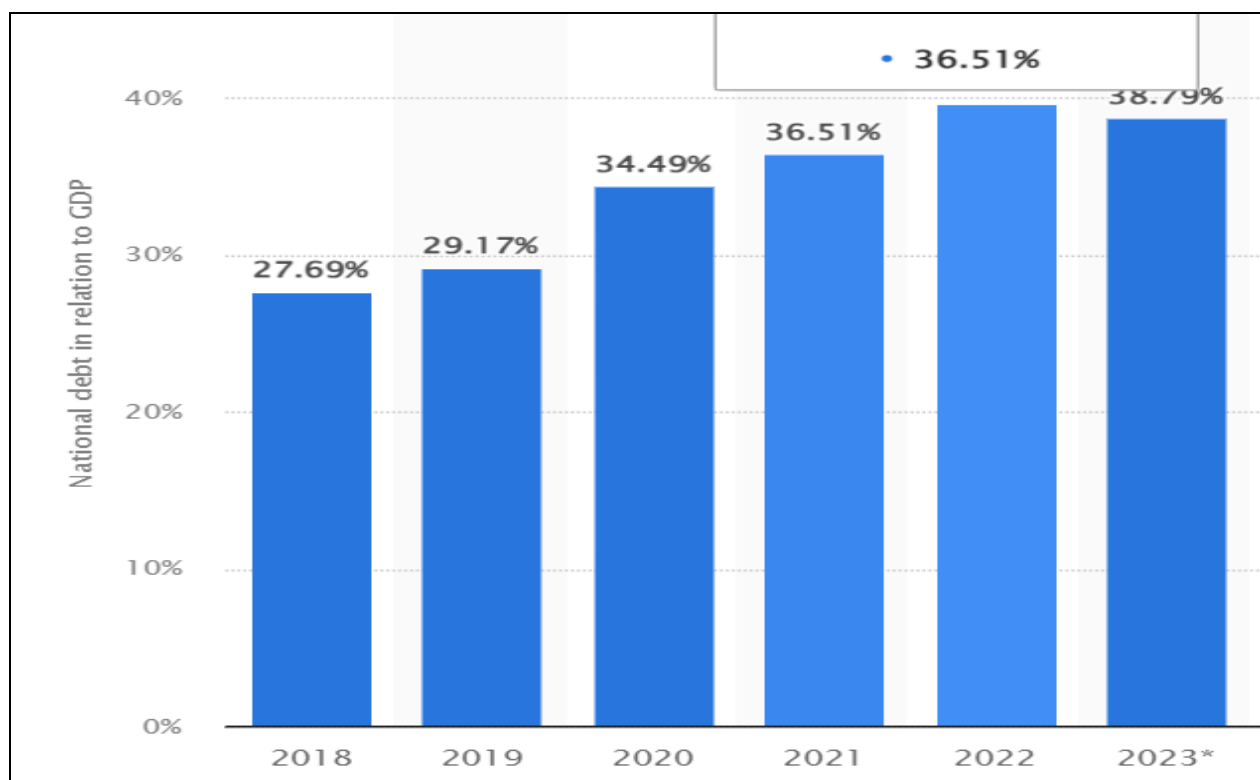
Nigeria's Total Public Debt Outstanding(2015 - 2023, N' Million)					
	<i>2015</i>	<i>2020</i>	<i>2021</i>	<i>2022</i>	<i>2023</i>
Domestic Debt %of total	8,836,995.85	16,023,885.33	23,700,801.25	22,210,364.60	50,196,102.87
External Debt %of total	2,111,530.71	12,705,618.00	15,858,231.26	18,702,251.88	31,980,000.00

The external debt as of the end of 2015 stood at about N2,111,530.71 million from the N1,016,721.69 million recorded in 2012. The value, however, rose significantly to about N12,705,618.00 million in 2020, and about N18,702,251.88 million as at end 2022. Due to intense borrowing of the government, especially from Multilateral agencies, the Nigeria's external stock rose to an all-high figure of N31.98 trillion, representing about 36.38 percent of Nigeria's total debt profile.

3.0 RISING TREND OF RATIO OF DOMESTIC DEBT TO GDP IN NIGERIA

One can analyze the evolution of the domestic debt from its size or by considering its different components. The stock of government debt is measured relative to national output. Since the early 1980s, the ratio of domestic government debt to gross domestic product (GDP) in Nigeria has risen sharply. By 1964, the level of domestic debt was 5.5 percent of GDP. A decade later (by 1974), this ratio went up slightly to 6.9 percent of GDP. But by 1984, the domestic debt /GDP ratio was over 40 percent.

Figure 1: Nigeria's Debt to GDP Ratio (2018-2023)



Sources: Statista 2024

Although it declined slightly in the 1990s, it has since 2000 moved upwards. The Country has been experiencing escalating levels of government domestic indebtedness, and the country's domestic debt-to-GDP ratio is clearly on the high side. For instance, the ratio rose from 27.69 percent in 2018 to 29.17 percent in 2019, 34.49 percent in 2020. It further experienced consistent rise from 36.51 percent in 2021 to 36.67 percent in 2022, and 38.79 percent in 2023, respectively.

If this threshold exceeds the threshold, the country could run into domestic debt-servicing problems and the associated effects on other macroeconomic goals.

4.0 COMPONENTS OF DOMESTIC DEBT STOCK IN NIGERIA

Domestic debt is defined as debt denominated in local currency. The management of domestic debt in Nigeria has hitherto been conducted by the Central Bank of Nigeria (CBN), but in recent time the issuance of the debt instruments are regulated by the Debt Management Office (DMO), while the Central Bank of Nigeria acts as the Issuing House and the Registrar. Therefore,

government domestic debt refers to debt instruments issued by the government and does not include contractor debts and supplier credit by the government, Asogwa & Ezenma (2014). The debt instruments consist of the following:

FGN Bond:

The FGN Bond makes up the majority percentage of the domestic borrowings of government in recent times, representing a proportion of about 86.02 percent of total domestic debt. In which the commercial banks and discount houses accounting for the larger share amount of the domestic debt components. DMO has been regulating the activities of the FGN bonds market, while the Central Bank of Nigeria acts as the Issuing House and the Registrar

Table 2: Federal Government Domestic Debt Stock as at September 2023

FEDERAL GOVERNMENT DOMESTIC DEBT STOCK BY INSTRUMENT AS AT SEPTEMBER 30TH, 2023		
INSTRUMENT	AMOUNTS IN NAIRA	% PROPORTION
FGN Bonds	43,177,327,421,592.00	86.02
Nigerian Treasury Bills	4,722,716,799,000.00	9.41
Nigerian Treasury Bonds	25,988,000,000.00	0.05
FGN Savings Bond	33,924,610,000.00	0.07
FGN Sukuk	742,557,000,000.00	1.48
Green Bond	15,000,000,000.00	0.03
Promissory Notes	1,478,589,036,250.26	2.95
TOTAL	50,196,102,866,842.30	100.00

The FGN bond is considered as the safest of all investments in domestic currency securities market because it is backed by the ‘full faith and credit’ of the government. They have no default risk, meaning that it is virtually certain your interest and principal will be paid as and when due. The income you earn is exempt from state and local taxes.

Figure 2: Holders of Federal Government Domestic Debt



Source: Debt Management Office, Nigeria

Nigerian Treasury Bills: Treasury Bills are short term debt instrument usually a not more than a year issued by the Central Bank of Nigeria (CBN) on behalf of the federal government. The investment is backed by the full faith and credit of the Federal Government of Nigeria, hence, it is considered one of the safest forms of investment. This instrument is the second most common debt instrument after the FGN Bond, representing about 9.41 percent of the total debt instruments. The Federal Government of Nigeria through the Central Bank of Nigeria (CBN) issues T-bills to provide short-term funding for the government budget deficit.

Promissory Notes:

A promissory note, sometimes referred to as a note payable, is a debt instrument, in which one party promises in writing to pay a determinate sum of money to the other, either at a fixed or determinable future time or on demand of the payee, under specific terms and conditions. Nigeria's debt stock is increasing due to a combination of several factors, including the continued issuing of promissory notes by the federal government.

FGN Sukuk:

Sukuk is an investment certificate that represents the ownership interest of the holder in an asset or pool of assets. The certificate entitles the holder to receive income from the use of the assets. The Sukuk program is designed to support the construction and rehabilitation of key economic infrastructure such as roads across the six geopolitical zones in Nigeria.

FGN Saving Bond

The Federal Government of Nigeria Savings Bond (FGNSB) is a government bond backed by the full faith and credit of the Federal Government of Nigeria (FGN) and listed on the Nigerian Stock Exchange. Licensed and accredited stockbrokers such as FBNQuest Securities are authorized to issue units of this offer to investors.

Nigerian Treasury Bond

These are long-term maturity instruments (over 10 years) with fixed interest rate debt security issued and backed by the 'full faith and credit of the Federal government.' They are contrary to the NTBs that have a less than one year maturity the T-bonds are regarded as the safest form of marketable investment. They have an active secondary market and usually pay semi-annual interest.

Green Bond

Green bonds are a type of debt issued by public/private institutions to finance themselves and, unlike other credit instruments, they commit the use of the funds obtained to an environmental project or one related to climate change. This is, however, specific for financing or refinancing projects that contribute positively to the environment and/or climate. The bond is alternatively known as a climate bond.

- **Ways and Means Advances:** These are temporary overdrafts issued to the Federal government by the CBN which are meant to be repayable within a year. ways and means advances are not marketable but held solely by the CBN. However, these advances were never defrayed by the federal government but refinanced by the floatation of treasury bills and treasury certificates. Only recently all outstanding ways and means owed by federal government have been converted to a long-term domestic debt instrument through securitization.

5.0 INSTITUTIONAL FRAMEWORK FOR SUPERVISING AND REGULATION DEBT IN NIGERIA

The Debt management office (DMO) was established in October 2000 to centrally coordinate the management of Nigeria's debt, both domestic and Foreign which was hitherto being done by a myriad of establishments in an uncoordinated fashion. The diffused debt management strategy was very cumbersome and inefficient. For instance, prior to the establishment of the Federal Ministry of Finance (FMF) alone had, various units/departments which was saddled with the

responsibility for managing and servicing external debt such as the Paris Club debts, and other creditor Multilateral Institutions like International Monetary Funds, (IMF), African Development Bank (AFDB) etc. The central bank of Nigeria, however, at that time, was also responsible for managing external debt.

The creation of a separate public debt management office like the DMO was therefore aimed at achieving the following advantages: good debt management practices, prudently raising financing to fund government deficits at affordable costs and manageable risks in the medium- and long-term; achieving a positive impact on overall macroeconomic management, including monetary and fiscal policies. etc.

6.0 REASONS/USES OF GOVERNMENT DOMESTIC BORROWINGS

- **Financing of Government fiscal Operations (budget deficit financing)** - Government debt is one of the major sources of financing government fiscal operations, Governments can also create money to monetize their debts, thereby removing the need to pay interest. In most annual budgetary estimates of the federal government, the projected revenue (government receipts) falls below expectation, this is however, often occasioned by continuous huge government obligations in on spending on procurement of public utilities. Consequently, the fiscal operations of the Federal Government usually resulted in large deficits. This development often leads to a huge gap between fiscal revenue and expenditure. Hence the need for the government to look for sources of financing the gaps. Such borrowing can come from internal and/or external sources. This is necessary in order to boost domestic investment and hence accelerate economic growth and development.
- **Governments also borrow to finance major infrastructure projects** like railways, roads, and public utilities. These investments are expected to have long-term economic benefits that can offset the cost of borrowing.
- **Economic Stimulation** - Borrowing can be used to boost economic growth during challenging economic downturn, this is done by injecting borrowed funds into the economy, the government can stimulate demand, create jobs, and support businesses, ultimately leading to increased tax revenue. For example, during the Covid-19 Pandemic,

the Nigerian government borrows funds from several multilateral organizations to stimulate the economy.

- **Domestic debt can be used to achieve monetary policy targets** - This is particularly the case in countries with large balance of payments surpluses, created by large aid inflows or oil exports, for example. In those situations, the inflows of foreign exchange increase liquidity which could undermine macroeconomic stability and the central banks often decide to intervene by selling government or central bank bills to stem inflationary pressures from excess liquidity. In this case, public domestic borrowing acts as an anti-inflationary measure by mobilizing surplus money in people's hands. Apart from budget deficit financing, and for implementing monetary policy, another reason for domestic debt is for developing the financial sector.
- **Develop the financial instrument to deepen the financial markets** - As Johnson (2001) argued, to develop and deepen the Nigerian financial markets, there needs to be a steady supply and range of financial instruments to be traded. Usually, at the beginning of this process, the government offers short-term Treasury bills, which provide a secure return and boost investor confidence in government debt instruments. Thereafter, financial market deepening can be achieved by offering longer-dated instruments with different interest rate structures, i.e. fixed and floating rates.
- **To meet Government Financial needs**; generally, as government revenue declines, the government borrows from the Central Bank through the instrument of ways and means advances. These advances were never defrayed by the Federal Government but refinanced by the floatation of treasury bills and treasury certificates. These are rolled over by issuing new ones to pay holders of maturing debt instrument contributing to the continued growth of the debt stock.

7.0 CONCLUSION AND RECOMMENDATIONS

One of the biggest problems with economic policy that many nations, particularly developing nations like Nigeria, are currently facing is the issue of enormous public debt. Generally, these developments over a long time have raised serious concerns among international financial institutions and bilateral lenders, resulting in several initiatives. However, the problem of domestic debt in developing nations can have a big impact on macroeconomic stability, private

sector lending, government budgets, and economic growth in many economies. For this reason, it is essential that every government make an effort to implement measures to reduce the rate at which the nation's public and private debts exponentially increase.

Based on the above issues discussed, it is recommended that the government should:

- ✚ *Borrowing should be done on a needs and purpose basis.*
- ✚ *Government issuance of debt instruments should be done in an harmonized calendar by the DMO and CBN to avoid prompting liquidity issues.*
- ✚ *The government should attempt to restructure borrowings from short tenured to long tenured Loans facilities.*
- ✚ *Reduction in government Spending and cutdown of government budgeting process.*
- ✚ *Adopt debt refinancing, where a new loan or debt instrument that has better terms than a previous contract can be used to pay down the previous obligation.*
- ✚ *Government should employ a determined debt-reduction strategy for the economy.*
- ✚ *Maintaining interest rates at low levels helps stimulate the economy, generate tax revenue, and, ultimately, reduce the national debt.*

References:

1. Adofu, I. and Abula, M. (2010). "Domestic Debt and the Nigerian Economy". Current Research Journal of Economic Theory. 2(1): 22-26, 2010
2. Anyanwu, J. C. and Erhijakpor, A. E. O. (2004). "Domestic Debt and Economic Growth: The Nigerian Experience"
3. Asogwa, R. C and Ezema, C. C. (2014). "Domestic Government Debt Structure, Risk Characteristics and Monetary Policy Conduct: Evidence from Nigeria. Final Research Report Submitted for the "International Research Project on Macroeconomic Policy Challenges for Low Income Countries". Department of Economics University of Nigeria
4. Ngozi Okonjo-Iweala e'tal (2003); "the Debt Trap in Nigeria: Towards a sustainable Debt Strategy" Africa world press incorporation
5. Peter N. M., Denis N. Y. and Chukwuedo S. O. (2013). Analysis Of Domestic Debt: Implication for Economic Growth in Nigeria. Global Journal of Social Sciences Vol 12, 2013: 1-9. Issn 1596-6216
6. Adebisi, W. K. and Olowookere, J. K. (2013). 'Managing Nigerian Debt: The Practical Solutions". Research Journal of Finance and Accounting, ISSN 2222-1697 (Paper) ISSN 2222-2847 (Online) Vol.4, No.19

7. DMO 2013 Annual Report and statement of Accounts, 2013
8. DMO's Full Report of the Annual National Debt Sustainability Analysis (DSA)
9. DMO's Full Report on the programme for the establishment of Debt management departments and domestic debt data reconstruction in the 36 states of the federation and the FCT (2008-2012), December 2012
10. <https://fbnquest.com/securities/solutions/fgn-savings-bond-offer/>
11. Nigeria's Medium –Term Debt Management Strategy (2012-2023)
12. www.dmo.gov.ng

UNDER PEER REVIEW