Nigeria Development Update

Nigeria’s Choice

December 15, 2022
Nigeria's Choice

Country Economic Memorandum
Charting a New Course
NIGERIA STANDS AT A CRITICAL JUNCTURE, WITH A CHOICE TO MAKE

Source: NBS, WDI, and World Bank estimates.
PART 1: A TASTER OF THE NIGERIA COUNTRY ECONOMIC MEMORANDUM

Seven observations about Nigeria’s growth record
Seven observations about Nigeria’s growth record

1. Macroeconomic stability and policy predictability have deteriorated over the past decade, eroding growth potential

2. Economic performance across different periods is directly linked to the pace of reforms, which relates to the strength of institutions

3. Nigeria lacks large and mid-sized formal productive firms, pointing to labor misallocation that hinders productivity growth

4. Oil dominance: boom-bust oil cycles and low investment have hindered economic diversification, as oil continues to dominate exports

5. Structural transformation and job creation have been slow

6. More jobs are needed to employ a fast-growing labor force and a demographic dividend is not yet in sight

7. The economy is not generating enough pathways out of poverty, due to the lack of better jobs and economic transformation

Source: NBS, CBN, WDI, and World Bank estimates.
1. Macroeconomic stability and policy predictability have deteriorated over the past decade, eroding growth potential

A macroeconomic stability index comprising inflation, fiscal and external balances shows steady deterioration

Nigeria’s potential output growth is now below population growth

Source: NBS, CBN, WDI, and World Bank estimates.
2. Economic performance across different periods is directly linked to the pace of reforms, which relates to the strength of institutions

From 2001 to 2008, the Nigerian Government implemented a series of bold reforms

- 2001: Liberalization of telecoms
- 2003: First fiscal rule introduced
- 2004: (i) Central Bank Act (ii) Excess crude account
- 2005: (i) Privatization of state-owned enterprises and deregulation of government activities. (ii) Debt forgiveness
- 2006: Civil service reforms
- 2007: (i) Trade reforms (ii) The Fiscal Responsibility Act and the Public Procurement Act (PPA) were enacted

However, the appetite for reforms has decreased over the past decade

Source: NBS, NCS, CBN, and World Bank estimates.
3. Nigeria lacks large and mid-sized formal productive firms, pointing to labor misallocation that hinders productivity growth

Small firms dominate the business landscape...

...but report the lowest productivity

4. Oil dominance: boom-bust oil cycles and low investment have hindered economic diversification, as oil continues to dominate exports

Investment has played a limited role in economic growth. Nigeria has one of the least complex economies in the world.

Source: NBS, CBN, Observatory of Economic Complexity, and World Bank estimates.
5. Structural transformation and job creation have been slow

The non-oil economy has shifted increasingly towards low-productivity services, although agriculture still dominates.

TFP growth has declined sharply

The move out of agriculture into other sectors has increased productivity, but agriculture remains the main employer.

Source: NBS, CBN, ILO, and World Bank estimates.
6. More jobs are needed to employ a fast-growing labor force and a
demographic dividend is not yet in sight

Job creation, especially of full-time, high-quality jobs, has not kept up with a fast-growing population (even before the 2020 recession)

Even in 2050, for every young dependent in Nigeria, on average only 1.5 family members will be of working age - much lower than comparator countries

Source: NBS, CBN, UN World Population Prospects, and World Bank estimates.
7. The economy is not generating enough pathways out of poverty, due to the lack of better jobs and economic transformation

Merely being in work does not guarantee a path out of poverty, and wage work is scarce

Employment in agriculture is more prevalent among the poor

Only 16.7 percent of working Nigerians have a wage job

RECAP OF THE LONGER-TERM DEVELOPMENT PATH: INDONESIA

Steady growth of the pie punctuated by occasional setbacks

Annual growth

Real GDP per capita (US$)

Source: WDI.
RECAP OF THE LONGER-TERM DEVELOPMENT PATH: NIGERIA

Little sustained progress other than during the 2000s, then two recessions associated with 2015 oil shock & COVID-19
NGERIA’S GROWTH SINCE 2001: A WIDER COMPARATIVE PERSPECTIVE

Source: NBS, CBN, WDI, and World Bank estimates.

2001 GDP per capita

Turkey
Russia
Mexico
China
Brazil
South Africa
Egypt
Indonesia
India
Ghana
Bangladesh
Pakistan
Nigeria

GDP Per Capita (US$, 2017 PPP)
Nigeria’s GDP per capita gains over the last two decades are the lowest among middle-income peers.

**Source:** NBS, CBN, WDI, and World Bank estimates.

**GDP Per Capita (US$, 2017 PPP)**

- **2001**
- **Additional GDP per capita generated between 2001 - 2021**

**2001 GDP per capita**

**2021 GDP per capita**

Source: NBS, CBN, WDI, and World Bank estimates.
PART 2: THE URGENCY OF NIGERIA’S CHOICE (OR: WHAT’S DIFFERENT THIS TIME)

Increasing fragility

Macro-fiscal indicators are flashing red despite a global oil price boom

Coming to a head: why has Nigeria not benefited from the oil price boom?
INCREASE IN CONFLICT AND VIOLENCE

The nexus between lack of economic opportunity and conflict is intensifying

2012

Source: ACLED.
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Increasing fragility

Macro-fiscal indicators are flashing red despite a global oil price boom

Coming to a head: why has Nigeria not benefited from the oil price boom?
MACRO-FISCAL SITUATION: GLOBAL ENERGY PRICES BOOMED IN 2021-22

Prices are well above the average of the last two decades

Average 2000 – 2019: US$68

Source: World Bank
YET DESPITE BEING AN OIL EXPORTER, NIGERIA’S RECENT ECONOMIC GROWTH RATE HAS BEEN LOW

It has been more like that of South Africa, an *oil importing* country hit very hard by the pandemic.

Source: World Bank estimates based on Haver data
THE BASE CASE IS FOR GDP GROWTH TO REMAIN WEAK NEXT YEAR

Oil output has continued to contract, and non-oil output growth has fallen

Source: NBS, World Bank estimates.

Nigeria’s growth outlook has been revised downwards

Source: NBS, World Bank estimates.
INFLATION HAS SURGED OFF AN ALREADY HIGH BASE

Nigeria’s high, structural inflation pre-dates the global supply and price shocks of 2021-22 and has worsened.

INFLATION REACHED ITS HIGHEST LEVEL IN 17 YEARS IN OCTOBER 2022, INCREASING POVERTY & FOOD SECURITY CONCERNS

Inflation pushed an estimated 5 million more Nigerians into poverty in the first 10 months of 2022

- Before price shock
- After price shock (2020-2021)
- After price shock (2022)

Number of poor people (millions)

Source: World Bank estimates based on NBS data.

Average prices of locally-produced staples have increased faster than average inflation

- Yam tuber (1 tuber)
- Bread (500g)
- Rice (1kg)
- Wheat (1kg)

Source: NBS.
PUBLIC FINANCES ARE UNDER SEVERE PRESSURE

Fiscal deficits have increased, forcing a rapid increase in borrowing from the CBN

Due mainly to slumping net oil revenues, the fiscal deficit has widened...

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...causing a ramp-up in expensive and inflationary CBN financing

Sources: BOF and OAGF

Sources: CBN and OAGF and World Bank estimates.
FX DISTORTIONS HAVE INCREASED
This is deterring investment due to uncertainties firms face in accessing FX and related costs to doing business

N/US$

CF premium = 22%

CBN discontinues sales of FX to BDC

Currency redesign announcement

Parallel exchange rate

FX premium = 72%

I&E exchange rate

Source: CBN, BDC.
FX RESERVES HAVE DECLINED IN 2022, DESPITE HIGHER OIL EXPORT REVENUES WHICH HAVE PUSHED THE CURRENT ACCOUNT INTO SURPLUS

- Reserves accumulation in a context of increasing oil prices and less rigid FX management
- Interventions to keep the naira stable and increasing fuel imports and petrol subsidy
- Oil price shock
- COVID and oil price shocks
- I&E window created
- Declining reserves in a context of high oil prices
- Additional SDR allocation
- Reserves excluding additional SDR
NIGERIA’S RISK PREMIUM HAS INCREASED IN GLOBAL CAPITAL MARKETS, INCREASING BORROWING COSTS

Source: JP Morgan.
GROWTH & MACROECONOMIC CHALLENGES HIT HOME: HOUSEHOLDS’ PURCHASING POWER HAS SLUMPED...

₦ 30,000
Nigeria's minimum wage in nominal naira in 2019

2019

The cumulative inflation between 2019 and 2022 was 55 percent

₦ 19,355
The real minimum wage in naira in 2022, after discounting for inflation

N 30,000
Nigeria's minimum wage in nominal naira in 2019

2019

US$82
Nigeria’s minimum wage in nominal US dollars in 2019

The parallel market exchange rate depreciated from 367 to 750 Naira/US$

2022

US$26
Nigeria’s real wage in US dollars in 2022, after discounting for both inflation and exchange rate depreciation

Source: NLSS, NBS, CBN, and World Bank estimates.
PART 2: THE URGENCY OF NIGERIA’S CHOICE (OR: WHAT’S DIFFERENT THIS TIME)

Increasing fragility

Macro-fiscal indicators are flashing red despite a global oil price boom

Coming to a head: why has Nigeria not benefited from the oil price boom?
OIL REVENUES HAVE DECOUPLED FROM OIL PRICES

For the first time in Nigeria’s history, rising oil prices are not filtering into net revenues

Source: OAGF, World Bank estimates based off NNPC annual statistical bulletins for oil production from 2015 to 2019, government oil production reports for 2020 and 2021, and World Bank commodity annual prices for Brent crude oil.
THE DECOUPLING IS PARTLY DUE TO LOWER CRUDE OIL PRODUCTION

In H1 2022, oil production was the lowest in three decades

Source: NNPC annual statistical bulletins for oil production from 2015 to 2019, government oil production reports for 2020 and 2021, OPEC.

- High production costs
- Oil theft and insecurity
- Federation arrears in Joint Ventures
- Lack of investment

Average 2010 – 2019: 2.1 mbpd
BUT MAINLY DUE TO THE COSTLY AND REGRESSIVE PETROL SUBSIDY

Source: OAGF, NETI, and World Bank estimates.

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross Oil and Gas Revenue</th>
<th>Petrol Subsidy</th>
<th>Other Deductions</th>
<th>Net Oil and Gas Revenues</th>
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<tbody>
<tr>
<td>2020</td>
<td>4098</td>
<td>-107</td>
<td>-1024</td>
<td>2967</td>
</tr>
<tr>
<td>2021</td>
<td>5631</td>
<td></td>
<td>-1430</td>
<td>-1171</td>
</tr>
<tr>
<td>2022 Projected</td>
<td>9102</td>
<td></td>
<td>-4800</td>
<td>-1918</td>
</tr>
<tr>
<td>2023 Projected</td>
<td>8605</td>
<td></td>
<td>-5000</td>
<td>-2100</td>
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</table>

<table>
<thead>
<tr>
<th>Year</th>
<th>2020</th>
<th>2021</th>
<th>2022 Projected</th>
<th>2023 Projected</th>
</tr>
</thead>
<tbody>
<tr>
<td>Naira, billion</td>
<td>2020</td>
<td>2021</td>
<td>2022 Projected</td>
<td>2023 Projected</td>
</tr>
</tbody>
</table>

Source: OAGF, NETI, and World Bank estimates.
REFORMS TO BOOST NON-OIL REVENUES HAVE PREVENTED AN EVEN WORSE FISCAL SQUEEZE

The Strategic Growth Revenue Initiative has helped prevent a steeper decline in revenues

<table>
<thead>
<tr>
<th>Year</th>
<th>Net Oil Revenues</th>
<th>Non-Oil Revenues</th>
<th>Total Revenues</th>
<th>Additional Non-Oil Revenues from Reforms</th>
</tr>
</thead>
<tbody>
<tr>
<td>2020</td>
<td>2.0</td>
<td>4.5</td>
<td>6.5</td>
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<tr>
<td>2021</td>
<td>1.8</td>
<td>4.6</td>
<td>6.4</td>
<td>0.5</td>
</tr>
<tr>
<td>2022</td>
<td>1.3</td>
<td>4.5</td>
<td>5.8</td>
<td>0.5</td>
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<tr>
<td>2023</td>
<td>0.6</td>
<td>4.7</td>
<td>5.3</td>
<td>0.8</td>
</tr>
</tbody>
</table>

Source: World Bank estimates based on data from NEITI, BOF, and OAGF
GOVERNMENT HAS BEEN FORCED TO BORROW MORE AND THE COST OF DEBT IS SURGING

Interest costs and principal repayments are rising fast, crowding out spending on productive sectors

Source: World Bank estimates based on data from OAGF and DMO
INFLATION: FUELED BY A COMBINATION OF SHOCKS AND POLICIES

Recent domestic & external price shocks

Flooding in farming areas has impacted the harvest of crops such as rice and corn and will reduce agriculture production in 2023

The war in Ukraine has increased global food and fuel prices

Policies

Suboptimal exchange rate management fuels inflation by constraining FX supply, complicating the operating environment for businesses, and pushing up the parallel exchange rate which is closely associated with inflation

Import and FX restrictions restrict the supply of food and staple products, increasing their prices and those of associated goods

Monetary & fiscal policy settings: The increase in the Monetary Policy rate (500bp since May 2022) is a step in the right direction, but the effectiveness of monetary policy is compromised by subsidized interest rates and the monetization of the FG fiscal deficit which in turn is partly due to the fiscal burden imposed by the PMS subsidy
PART 3: CHOOSING TO RISE TO POTENTIAL
## KEY CHOICES: A PRIORITIZED SET OF REFORMS FOR THE SHORT AND MEDIUM-TERM

<table>
<thead>
<tr>
<th>Time horizon</th>
<th>Macroeconomic and Institutional Enablers</th>
<th>Investment Accelerators</th>
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<tbody>
<tr>
<td><strong>Sprints</strong></td>
<td>- Adopt a single and market-reflective exchange rate</td>
<td>- Facilitate trade and boost domestic value added by removing import and foreign exchange restrictions</td>
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<tr>
<td></td>
<td>- Increase non-oil revenues by raising VAT and excise rates and strengthening tax administration</td>
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<tr>
<td><strong>Medium-distance runs</strong></td>
<td>- Eliminate the petrol subsidy by establishing a compact which also protects the poor and vulnerable</td>
<td>- Increase access to finance by strengthening the institutional infrastructure for financial intermediation</td>
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<td></td>
<td>- Contain inflation by reducing the federal government's recourse to CBN financing</td>
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<tr>
<td><strong>Marathons</strong></td>
<td>- Boost competition by embedding it into policy, enhancing enforcement, and simplifying rules to lower costs</td>
<td>- Boost power generation by investing in infrastructure to reduce technical and commercial losses</td>
</tr>
<tr>
<td></td>
<td>- Reduce insecurity by strengthening the rule of law</td>
<td>- Facilitate transport connectivity by reducing interstate transportation costs</td>
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</table>
WHAT DOES SUCCESS LOOK LIKE? TRANSFORMATIVE GAINS

Federal and state-level reforms could unlock 6.7 percentage points of additional annual growth over the next 20 years.

The success of Nigeria’s growth strategies will largely depend on the establishment of a strong implementation mechanism that promotes performance and accountability.

Implementation is the result of consensus among the political elite about the direction of policy, the allocation of fiscal resources, the role of the state and the space for private sector initiatives.
Thank You

Grass to Grace
By Millicent Osumuo
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