Nigeria Economic Alert:

Nigeria's Economic Recovery and Growth Plan (ERGP): a strategy for economic diversification & sustainable growth

24 April 2017

The ERGP: A policy response to the economic downturn

Nigeria's economic downturn has prompted a response by the Federal Government in form of a National Development Plan which covers a four year period from 2017 to 2020. The Economic Recovery and Growth Plan is aimed at strengthening economic diversification by focusing on three broad objectives: restoring sustainable growth, building a globally competitive economy, and investing in human capital development. The ERGP is structured to leverage private sector participation through the creation of an enabling policy and business environment to attract private sector finance targeted at infrastructure development and industrialisation.

Continuity is fundamental to the success of the ERGP

Whilst the objectives of the ERGP are laudable, its vulnerability to political disruptions is a key risk which impacts the sustainability and enforceability of the development plan. Aisen and Veiga (2016) using a case study of 169 countries show that such disruptions may not only truncate the impact of a development plan, but also hinder the growth prospects of an economy through lower productivity growth[1].

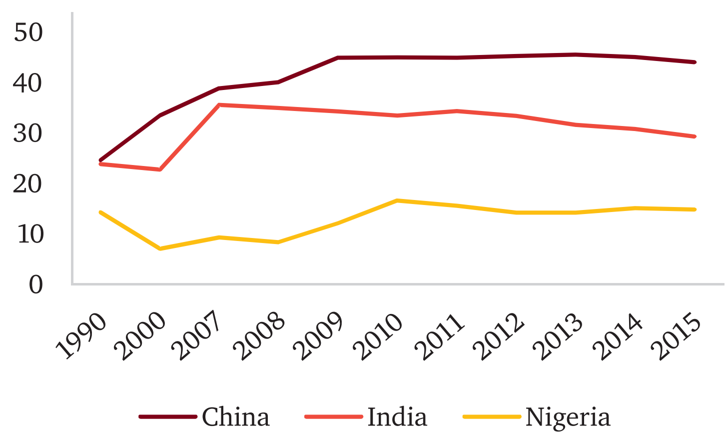
Nigeria can limit the impact of political disruptions through the institutionalisation of its development plans. Specifically, there is a need to accelerate the enactment of the existing Development Planning and Project Continuity Bill, an offshoot of Vision 20:2020, which was initiated in 2011 to insulate present and future plans from political uncertainties.

Scaling up private financial flows is key to closing the investment gap

According to the ERGP, an investment of USD 3 trillion is required for infrastructure development over the next 30 years. This implies a funding requirement of USD 400 billion over the implementation period of the ERGP.

The ERGP only plans for a Federal Government borrowing of USD 30 billion, which represents 7.5% of the funding required. Considering the traditional sources of government financing are stretched, massive amounts of private investment will be required to bridge the shortfall. Yet, private investment has remained sluggish in the past decade. Over this period, gross fixed capital formation as a percentage of GDP averaged below 15% compared to an average of 43.3% and 32.8% in China and India respectively. Consequently, Nigeria's infrastructure stock as percent of GDP[2] remains low at 35%*, far below the emerging market average of 70%*. Similarly, FDI into Nigeria in recent years has been lackluster after reaching a peak of USD8.6 billion in 2009, declining 48.8% to USD4.4 billion in 2016 on the back of deteriorating business conditions.

Gross Fixed Capital Formation (% of GDP)



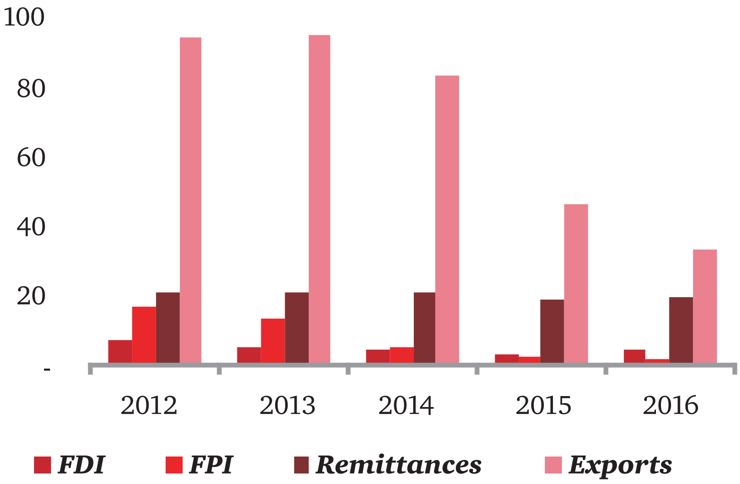
Source: World Bank, PwC Analysis

Improving business environment and a sustainable FX regime are key to unlocking private investment

Nigeria faces significant challenges in building a stable business environment. Between 2008 and 2017, its Ease of Doing Business ranking worsened from 108 (of 178 countries) to 169 (of 190 countries), More recently, the Federal Government has signaled its commitment towards easing constraints in the business environment by establishing the Presidential Enabling Business Environment Council (PEBEC), chaired by the Vice President of the Federal Republic of Nigeria, Professor Yemi Osinbajo GCON and approving the implementation of a 60-day national action plan which commenced February 21, 2016. So far, there appears to be significant progress in delivering on reforms relating to: starting a business, dealing with construction permits, getting credit, trading across borders and dealing with the entry and exit of people. To broaden the impact of these reforms however, there is an urgent need to replicate a similar action plan across all states since over 60% of capital spending occurs at the sub-national level.

Similarly, the Foreign Exchange regime has been a major impediment to doing business in Nigeria. In particular, the unavailability of Foreign Exchange through the official market has resulted in challenges in meeting dollar obligations for both importers and investors. Thus, there is an urgent need to implement a flexible exchange rate structure, which allows for a wider autonomous interbank market, thus providing a more liquid market for price discovery, as the exchange rate will be market determined rather than managed.

Nigeria's FX inflows (2012 - 2016)



Source: Central Bank of Nigeria, NBS; PwC Analysis

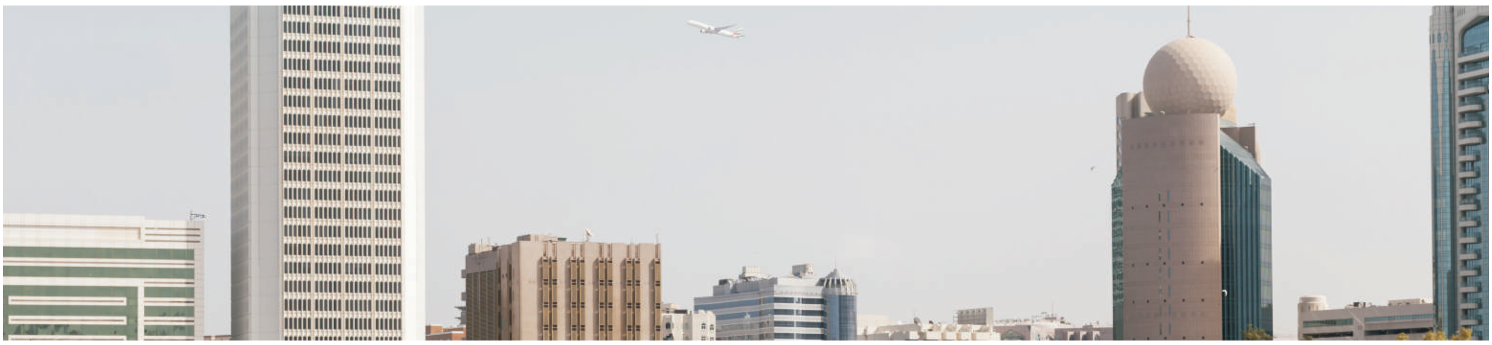
Newly introduced FX window could improve dollar inflows

On Friday, the Central Bank of Nigeria (CBN) published guidelines on the introduction of a new Foreign Exchange (FX) window for investors and exporters to boost FX liquidity and ensure timely settlement of transactions. Supply to the window is expected to be from portfolio investors, exporters, Authorised Dealers and other parties, including the CBN. In addition, exchange rate would be determined through a transparent polling system that allows for price discovery. Even as this development could be positive for dollar inflows through increased FDI and portfolio investments, the implementation of the framework could be a challenge as the existence of multiple exchange rates leaves room for arbitrage. In addition, the role of the CBN should not signal an interference in price discovery, as this could undermine the success of the reform.

Implementing the ERGP could increase Nigeria's Human Development Index (HDI) score

In 2016, PwC published a report which argued that national policies should be guided not only by improvements in GDP but also a broader measure of development, proxied by the Human Development Index (HDI)[3]. The report goes further to identify through empirical analysis, three critical levers to improving Nigeria's HDI from 0.51 in 2014 to 0.73 in 2030, which will mean an attainment of "high human development" status by 2030. The levers were identified as: improving the ease of doing business, enhancing labor productivity and reducing the overall level of corruption. We believe that the implementation of the ERGP will result in significant improvements in these three levers thus leading to faster and more inclusive growth.

** 2012 estimates*
1 Aisen and Francisco (2010) Does Political Instability Affect Economic Growth? IMF working paper WP/11/12
2 Economic and Growth Recovery Plan (2017)
3. PwC (2016) " The Future of Nigeria: Three critical levers for improving HDI" http://www.pwc.com/ng/en/assets/pdf/the-future-of-nigeria-improving-hdi.pdf



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