

GLOBAL ECONOMIC CRISIS AND NIGERIA: POLICY RESPONSES AND AGENDA FOR LONG TERM GROWTH

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Abstract

This paper examined the impact of global economic crisis on the Nigerian economy from macroeconomic perspective. It traced the origin of the crisis to the collapse of Sub-prime mortgage lending in the USA following complex banking problems that developed over time from housing and credit markets mis-match, poor judgement by borrowers and lenders, and over speculation of very risky mortgage products regarded as financial innovations. The paper provided the highlights of what the global economic crisis meant for Nigeria, the channels through which the crisis spread to the sectors thereby affected the domestic economy, the strategies adopted by Government to counter and mitigate the effects on the populace, among others. Some of the immediate effects were dwindling government revenue occasioned by sharp drop in commodity prices, particularly crude oil which is the main source of government revenue, decline in stock market valuations leading to loss of financial wealth, depreciation in Naira exchange rates, capital flight, etc. The paper also discussed Nigeria's policy response to the crisis starting with the inauguration of a Presidential Steering Committee on the Crisis and a package of incentives designed to ginger production, increase domestic demand and generate employment opportunities. To facilitate economic recovery and long term growth, the paper recommended strengthening the Sovereign Wealth Fund to accumulate foreign reserves during high oil prices, improved mobilization of domestic non-oil resources for development and the need for vertical cooperation among the three tiers of government. Finally, the paper suggested strategies to counter the effects of the global economic crisis in Nigeria.

1. INTRODUCTION

The last global economic crisis was the second round of the financial crisis which began in U.S. in August 2007. The crisis has its roots in a banking practice called sub-prime mortgage lending in the USA. It is traceable to a set of complex banking problems that developed over time, caused specifically by housing and credit markets mis-match, poor judgement by borrowers and/or the lenders, inability of home owners to make mortgage payments, speculation and overbuilding during the boom period, risky mortgage products (financial innovations with concealed default risks), high personal and corporate debt profiles and weak central bank policies.

The benign environment then led investors, firms and consumers to expect a bright future and underestimate risk. Housing and other asset prices went up in U.S. as several risky mortgages were approved and sold as being nearly riskless. So, when housing prices fell and subprime mortgages and securities based on them reduced in value, the stage was set for a crisis. The crisis became contagious and quickly moved across assets, markets and economies in view of global integration and connections among financial institutions.

It is therefore relevant to ask: What does the global economic crisis mean for Nigeria? What are the channels through which the crisis is spreading and affecting Nigeria? What are the strategies that can be used to counter the effects of the global economic crisis on Nigeria? The aim of this paper is to examine the macroeconomic implications of the global economic crisis for the Nigerian economy. In order to enhance the understanding of the implications of

the crisis, the relevant concepts are clarified and an overview of past and present global economic crises is presented. This is followed by the implications of the global economic crisis on the Nigerian economy.

2. CONCEPTUAL FRAMEWORK

a. Conceptual clarification

Global: This is a synonym of the word worldwide which relates to the entire world. It means covering or affecting the whole world. It also mean comprehensive. It has been argued that global has replaced international as a way of referring to issues, processes and structure.

Economic Crises: Economic means „connected with the economy of a country or an area“ in aspects like production, trade, services, and development of the wealth of the society. **Crisis** on the other hand refersto a time of difficulty or confusion when problems must be solved or important decisions made. Therefore, economic crisis relates to difficulties which affect the growth and performance of the economyin question unlike financial crisis which mainly involve financial institutions or assets suddenly losing a large part of their value. Crises will mean different periods of economic crisis.

Relationship between Concepts: An economic phenomenon is global in outlook when it is worldwide in character and wide spread influence. Hence, global economic crises refer to economic problems which affect the economies of several countries.

b. Analytical framework

The global economy is a network of economic linkages. The domestic economy has three markets through which it is linked to the economy of the rest of the world. These are: goods market, factor market and assets market (money and credit market)². Activities in the rest of the world influence the domestic economy through each of these markets. The extent to which this occurs depends on the extent to which the domestic economy is integrated to the economies of the rest of the world in these markets.

The most obvious link of the domestic economy with other economies is through exports and imports of goods and services. The rest of the world influences the prices at which trade takes place and the quantities (for some goods) traded in the world markets. Thus, the effects of the rest of the world on the domestic economy are essentially through:

- i. prices and quantities of exports and imports.
- ii. terms of trade (price of exports divided by price of imports)
- iii. purchasing power of exports (terms of trade X export volume)

The terms of trade measure is one of the most important indicators of external shocks to the economy. An improvement in terms of trade is a good thing but deterioration is adverse. In the case of the factor market of a domestic economy, it is linked to the other economies through two channels: international mobility of labour and international capital movement. The effects of labour movement, whether short-term or long-term/permanent, are through 1). Influence on labour supply in the home country; and 2.) Influence on home country“s income through remittances.

The third link between the domestic economy and other economies in the world is through the market for assets, the money and credit market. In this respect, people decide on where they want to invest their capital or keep their wealth. Some people may choose to hold their

wealth abroad despite obstacles – legal and physical – while others may prefer the local economy. In any event, capital tends to flee countries with unstable finances and where the rewards associated with holding assets (e.g. interest rates and dividends) are relatively low. This link between asset markets is perhaps the most immediate and the strongest of the three linkages. For instance, domestic prices misalignment relative foreign prices may take sometime to have effect on the economy. But when interest rates, adjusted for exchange rate depreciation, get out of line, there is an immediate, highly visible pressure from capital flight. External reserves will fall or the country's exchange rate will depreciate.

A financial crisis can metamorphose into a global economic crisis manifesting in deepening recession, contraction of growth, employment and, hence, aggregate demand in a number of developed countries and some emerging market economies.

3. OVERVIEW OF GLOBAL ECONOMIC CRISES

The world has witnessed several financial and economic crises. Notable among them is the **Great Depression of 1929-33** which is regarded as the worst of modern times. It reflected previous excesses and subsequent incompetence. A short list of some major financial crises since 1980 includes:

- Latin American debt crisis of 1980s which began in Mexico
- U.S. Savings and Loans crisis in 1989-91
- Nordic Banking and Economic Crises, 1990-94
- The 1994 – 95 Mexican Economic Crisis
- The Asian Financial Crisis in 1997 – 98
- 1998 Russian Financial Crisis
- 1999 – 2002 Argentine Economic Crisis
- 2008 U.S. Financial Crisis

The U.S. Savings and Loans (S&L) Crisis of the 1980-91 was a massive collapse of the thrift industry. S&Ls financed long-term fixed-rate residential mortgages with savings and time deposits at a restricted interest rate. This maturity mismatch exposed S&Ls to considerable interest rate risk when inflation rose in the 1970s and monetary policy was tightened. S&Ls experienced enormous losses of net worth in 1979 – 82, and the early 1980s recession exacerbated the problem. From 1986 to mid-1995 about one half of all S&Ls (1,043) holding \$519 billion in assets were closed or otherwise resolved. The resulting slowdown in the finance industry and the real estate market may have contributed to the 1990 – 91 economic recession in America. However, the recession was short-lived and relatively mild.

The three Nordic countries (Norway, Sweden and Finland) experienced banking and economic crises in the early 1990s though the timing and severity of the crisis were different but there were important common elements. The crisis in Norway preceded the other two as it was closely linked to international oil price fluctuations while the crises in Finland took the form of a severe depression (cumulative GDP fell by 14 percent over 1990 – 94 and the unemployment rate exploded from 3 to 20 percent over that period).

In the case of the Asian financial crisis, the slowdown in the East Asia region during the crisis had global repercussions. The global economy witnessed slow growth and fall in commodity prices. The drop in oil prices adversely affected the export earnings and economic growth rates of oil-exporting countries such as Nigeria. The financial crisis also

affected the other non-oil producing Sub Saharan African (SSA) countries through the declining prices of key non-oil export commodities such as cotton, timber, etc. However, the financial effect of the East Asian financial crisis was effectively limited to South Africa because it was the only country in SSA with sophisticated financial markets and substantial capital inflows. So, it was the only one fully exposed to contagion from the world financial crisis. In recent years, however, some SSA countries, such as Nigeria, have liberalized their financial sectors and internationalized the capital markets thus making the economies highly vulnerable to the financial contagion.

The present global economic crisis started as a global financial crisis emanating from crisis in the U.S. mortgage sector. A major factor in the financial crisis is the failure of regulation and supervision against the backdrop of careless financial liberalization. Minimal or no government regulation was being extolled as virtues while self-regulation was equally extolled as a framework for banks under Basle II. The mortgage market crisis quickly spread to the entire financial sector and entire economy leaving in its wake serious recession. The crisis spread to Europe through the channels of financial globalization, with European banks having also experienced losses as a result of their engagement with securities linked to the U.S. housing market. When the real estate bubble busted in the US and Europe, investors moved to commodities, where experts expected a continuous increase in prices. The commodity bubble peaked in mid 2008, with a subsequent collapse, that only decelerated by the end of the year. In the second half of the year commodity prices declined by some 45 percent; in particular, losses were large in the case of metals and oil. The crisis spread like wild fire to the rest of the economy and to the rest of the developed world through financial contagion. The financial crisis has turned into a global economic crisis with most parts of the developed world experiencing deep recession which some analysts have described as the biggest global economic crisis since the Great Depression of the 1930s.

Contagion relates to the transfer of financial effects across countries more strongly than economic fundamentals can explain. This means that, as a result of various channels of linkages with the rest of the world, even a country that has strong macro-economic fundamentals, good regulatory frameworks and has managed its economy well can be a victim of global financial crisis through contagion. In the highly interdependent world economy, any adverse global or regional shock is rapidly transmitted to other economies through mechanisms such as declines in import volumes and/or changes in real prices of commodities (e.g. oil, copper, timber, etc). Also, as financial markets have become highly integrated, they tend to transmit global, regional or local shocks much more rapidly than in the past decades when financial markets were less integrated.

The current global economic crisis is unprecedented in history in terms of scope and severity. Because of the crisis, global capital flows have largely frozen; credit crunch persists despite massive global liquidity injections; global aggregate demand has fallen sharply (about \$50 trillion value lost through capital markets, housing etc); commodity prices have collapsed; world trade shrinking and major global banks recapitalized by governments. International financial institutions are without adequate resources to intervene, leading to global coordination failure.

The general perception when the problems were affecting only the United States and a few other developed countries was that Asia, the largest regional emerging market group, and Latin America, the second largest, as well as other regions were doing so well that in a

wishful way most thought they had “decoupled” from the advanced economies, and wealth would grow with few restrictions³.

The previous sense of strength and invulnerability is now gone. Commodity prices have declined by about one and half percentage point from their peak; demand for manufactured goods is declining sharply world wide; stock market valuations have declined by about one and half percentage point or more; and currencies in many emerging countries have depreciated, as capital flows reversed seeking to find a safe heaven. Governments were reasonably careful with their policies, but private enterprises held “toxic” assets to an unexpectedly large extent, with serious effects for their own financial health as well as that of their countries. The loss of financial wealth is enormous, and the consequences for the economies of the world, will be unfortunately commensurate⁴.

Compared with some other African countries, Nigeria appeared at first better positioned to weather the storm created by the global financial crisis, thanks to its large official reserves, improved policy frameworks, and generally robust banking sector.⁵ By 2008, the prospects for the Nigerian economy looked so promising that the economy was projected to grow at the rate of 6.1 per cent. However, because of the current crisis, the growth forecast was reduced to 4.0 per cent. As it has now become an economic crisis, the implications for Nigeria are far-reaching unlike if it was just a financial crisis

4. IMPLICATIONS OF GLOBAL ECONOMIC CRISES FOR NIGERIA

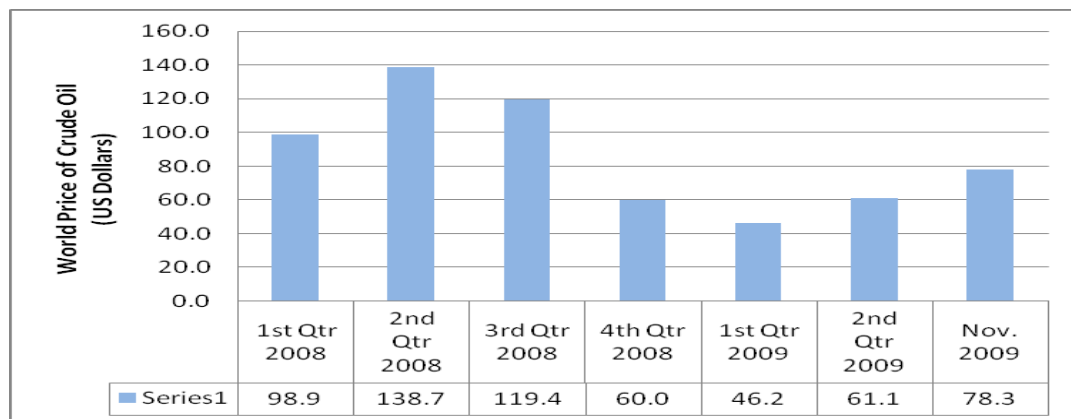
In the first few months of the global crisis, there was the view that the impact on Nigeria would be minimal because of its low integration into the global economy. Furthermore, Nigeria tends to have very small inter-bank markets which should shield the country from the direct effects of the global financial crisis. Recent developments have, however, shown that the negative contagion effects of the crisis are already evident in Nigeria. The real effects of the crisis in the region are not simply due to the nature of macroeconomic policies and governance in Nigeria. Indeed, the crisis represents a serious setback for Nigeria because it is taking place at a time when the country is making progress in economic performance and macroeconomic management. The implications of the economic crisis on Nigeria can be examined in terms of impact on different aspects of the Nigerian economy.²

i) Effects on Government Internal Finance

The global economic crisis has serious negative implications for government revenue and spending in Nigeria. This is the most visible aspect of the impact because of the heavy dependence of the Nigerian economy on foreign trade, particularly, crude oil exports for government revenue and foreign exchange earnings. The reduced demand for oil as a result of the global recession has led to the crashing of crude oil prices in the world market from about US\$146.2 per barrel of Nigeria Bonny Light on July 4, 2008 to US\$39.9 in the first week of January 2009. Crude oil experienced price declines of more than 50 per cent between February 2008 and February 2009. This has had negative impact on government finances. For instance, allocation to the three tiers of government dropped to N285 billion in January 2009 as against N435 billion in December 2008. This represents a difference of N150 billion and 34.5 per cent fall. The market is yet to fully recover as crude oil prices generally fluctuated within US\$ 40.0 per barrel and US\$53.0 per barrel between January and March 2009.

Because of the anticipated shortfall in oil revenue in 2009, a huge fiscal deficit of N1.09 trillion, or 3.95 percent of GDP was projected in the 2009 Federal budget. Unlike in many other economies, government spending is quite significant as the public sector is the major driver of the economy. This is why stakeholders (including the private sector) eagerly await government budget every year before meaningful economic activities can be embarked upon. Adverse effect of dwindling finances on government spending led to significant recessionary effect on the rest of the economy in 2009. Apart from this, public funds which would have been used for developmental purposes will be spent to mitigate the effect of the crisis in Nigeria. Thus, such crisis can be very costly financially and developmentally⁶. Indeed, not much progress was made by government in addressing infrastructures (energy, water, communication and transportation) due to funding inadequacy.

Figure 1: Trend of World Price of Nigeria's Bonny Light Crude Oil



Source: Central Bank of Nigeria

ii) Macroeconomic Effects

Already the global economic crisis is having far-reaching effects on macroeconomic variables in Nigeria. The effects on economic growth, balance of payments, the naira exchange rate, inflation, interest rates, and external debt are briefly discussed below.

Growth:

The Nigerian economy may experience significant reduction in output contrary to the optimism of senior government officials; however, it may not go into outright economic recession if the tempo of interventions in the various sectors is sustained. The high growth rates recorded in the past few years may slow down significantly. In 2004-2007, the economy witnessed real GDP growth averaging 6.3 per cent. The growth of the non-oil sector upon which much hope is placed by government may slow down because of the problems in the oil sector. In effect, the growth projections of between 7 - 9 per cent in the 2009 Federal budget could not be realised as the economy grew by 6.7 per cent.

Balance of Payments and Exchange rate:

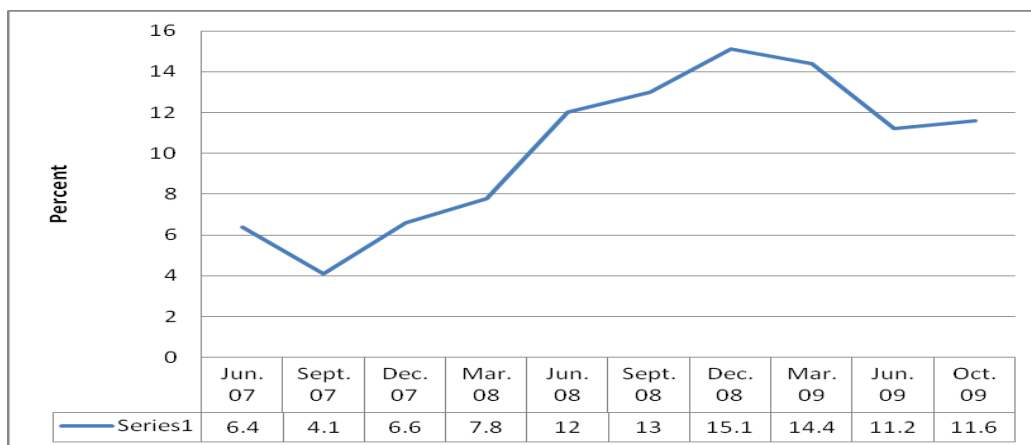
Another macroeconomic implication of the global economic crisis in Nigeria is the possibility of balance of payments crisis and exchange rate crisis. Already Nigeria has witnessed increased outflow of capital, particularly portfolio investment. Many portfolio investors have liquidated their funds, leading in part to the collapse of the Nigerian stock market. As a result of this also, foreign exchange reserves fell continuously for some time. Nigeria's stock of foreign exchange reserves which stood at over US\$60.0 billion by the

middle of 2008 currently stand at about US\$37.95 billion as at end of first quarter of 2010. Consequent to the shortfalls in foreign exchange earnings and supply along with intensified capital flight, the naira has since early December, 2008 been experiencing continuous pressure in the foreign exchange market. At some point in 2009, the exchange rate stood at N160: US\$1.0, a depreciation of 27.5 per cent compared to the level of N116.0: US\$ 1.0 as at end of November 2008. At N146.0: \$1.0, the rate of depreciation was 20.6 per cent. The depreciation of the naira has increased the exchange rate risks faced by domestic firms and increased the likelihood that they will default on loans owed to domestic banks, thereby increasing the vulnerability of these banks.

Inflation and Interest rates

Exchange rate depreciation usually comes with higher domestic prices. Even though the prices of foreign goods remain unchanged, traders will have to charge higher prices as they require more domestic currency to get the needed foreign exchange for their imports. Conversely, exporters are favoured as they will have more naira for their exports. The problem here is just that demand for such exports may be low due to the economic recession in the foreign countries. In addition, production of such exports depends on some imported foreign inputs and thus higher costs of production. It is not only due to exchange rate depreciation that inflation may worsen, another factor is the financing of the fiscal deficits arising from the declining government revenue. Available data shows that inflation rose from 7.8 and 12.0 per cent respectively, in the first and second quarters of 2008 to 14.6 per cent in December 2008.

Figure 2: Inflation Rate in Nigeria, 2007/2009



Source: National Bureau of Statistics [NBS]

Normally, the global economic crisis may make interest rates to rise in Nigeria considering the depreciating naira, fiscal deficit and rising inflation. This is unlike in some countries where interest rate is falling due to low demand for credit. It is not surprising that banks still charge high interest rates despite the reduction of the monetary policy rate by the central bank and the directive to reduce their lending rates. Investors will want to have positive interest rate. So, as inflation rises deposit rate has to rise. Lending rate has to be higher than the deposit rate.

External Debt:

In the case of external debt, Nigeria became free from the burden of external debt in 2006 following the relief obtained from the Paris Club. However, declining government revenue

due to the global economic crisis is making the government plan to borrow US\$500.0 million from the International Capital Market in 2009 to finance the part of its budget deficit. The loan has been approved by the National Assembly. Thus, this may be the beginning of rising and burdensome external debt in Nigeria as it is not clear if our nation has learnt any lesson from the past.

iii) Effect on the Nigerian Financial Sector

The Nigerian financial sector was liberalized in the late 1990s. Several portfolio investors have been attracted to the capital market because of the recent oil boom and high returns on investment. Following the bank consolidation exercise, the banks have become highly capitalized and have larger amounts of shareholders' funds with them than ever before. Furthermore, some of them have developed strong links with the global financial system and have been able to borrow from some financial institutions abroad. In sum, links have been established with the global financial system through borrowing from abroad and investment in Nigeria. Now, with the global economic crisis, there has been some withdrawal of funds/placements by many international banks/institutions that extended credit to Nigerian banks and businesses. Recall of funds by foreign banks intensified capital flight in Nigeria and is compounding the downturn in the capital market. Some banks in Nigeria have already started introducing belt-tightening measures as part of strategy to minimize impact.

It is noteworthy that the economic crisis will significantly weaken investor confidence in Nigeria, both in the capital and money markets. In view of the Bearish features of the capital market, 23 per cent or N2.9 trillion in market capitalization has already been lost since March, 2008 resulting in the CBN granting reprieve to banks that has large portfolio of margin facilities to re-structure for longer periods.

iv) Effect on the Real sector

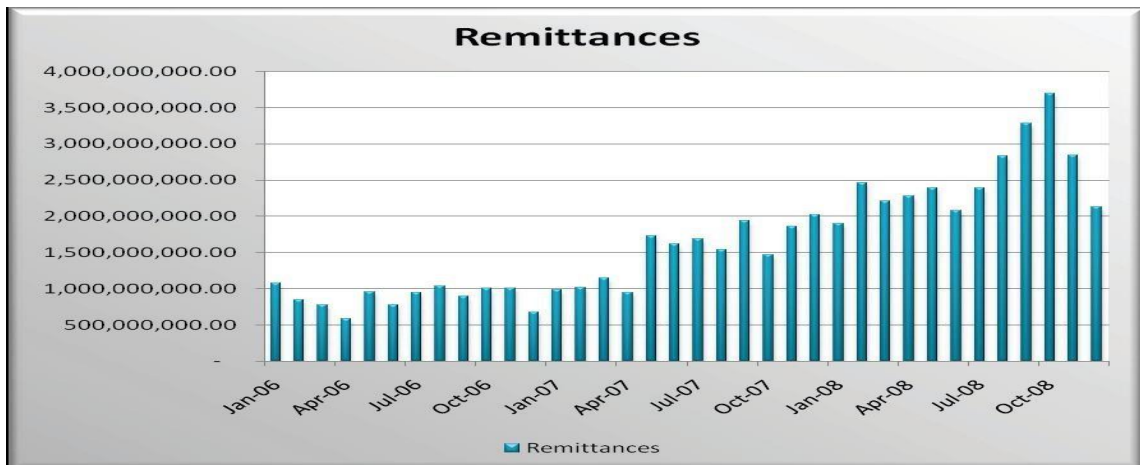
The real sector, particularly, the industrial sector, has been facing numerous problems before now. The problems include high cost of production, poor state of infrastructural facilities, high interest rates, multiple taxes, insecurity, etc. With the global economic crisis, indeed the sector's problems are being compounded by depreciating naira in the foreign exchange market, rising interest rates, rising cost of diesel, etc. In addition, the Nigerian manufacturing sector is import dependent and is therefore currently finding it difficult to establish letters of credit due to the fall in the value of the naira, rising interest rates and low foreign exchange supply in the market. Operators in the sector are jittery anticipating more hard times in terms of lower investment, lower profits and possible factory closure and retrenchment of workers. This is the more so, in view of the slowing down of global demand. Those of them that strive to export manufactured goods would be negatively affected. Added to these challenges facing producers in the Nigerian real sector is the difficulty is securing credit facilities for their operations.

v) Social effects

The impact of the global economic crisis may make the level of unemployment to rise in Nigeria while salaries of those that are able to remain in employment may be reduced. In addition, the amount of money remitted home by Nigerians working abroad to family members have dwindled because of the hardship they are facing too. Workers' remittances have played an important role in development finance in Nigeria recently. Such inflows finance household consumption and hence have a direct effect on poverty. In fact, there is some concern that some of the Nigerian migrant workers in Europe, North America and the

Gulf States may have been laid off and returned home thereby increasing the number of those in the unemployment market further. The lower household income may increase the rate of poverty and undesirable social vices like corruption, crime, prostitution, etc. Already, about 54.4 per cent of the Nigerian population are living below the international poverty line.

Figure 3: Monthly Remittances to Nigeria, 2006-2008 (Naira)



Source: CBN (2009)³

Thus, the country faces a greater challenge in meeting the MDG's target of halving the number of people below the poverty line by the year 2015. It is equally reasonable to expect the decline in fiscal space due to the drying up of traditional sources of development finance to also make it more difficult for Nigeria to fund health, education, infrastructure and nutrition programmes.

5. NIGERIA'S POLICY RESPONSES TO THE CRISIS AND OUTCOMES

The immediate response of the Federal Government to the global economic crisis was the inauguration of a Presidential Steering Committee on the Global Economic Crisis on January 16, 2009. The terms of reference of the Committee were:

- To assess the impact of the global economic crisis on the Nigerian economy with particular reference to the annual budget, as well as the financial and commodity markets.
- To recommend appropriate macro-economic policy responses that can further stimulate the economy.
- To identify practical measures aimed at shoring up the confidence of investors and the general populace in the economy, and increasing growth in the real sector.
- To examine the related issues of unemployment, poverty, global food crisis, and ensuring a sustainable debt position.
- To consider and make general recommendations on any other relevant issues.

Further, the Federal Government reconstituted the National Economic Management Team to design and implement a new economic framework. The new national economic management framework was expected to provide a more holistic and well-coordinated response to the economic recession. Accordingly, the team was mandated to come up with measures to curb the contagion effect of the global financial meltdown on the domestic economy. A number

of palliative measures were proposed on the short, medium and long terms to mitigate the effects of the global economic crisis on the country. What was worked out was a package of incentives that would ginger production, increase the purchasing power of the ordinary man on the street and help generate employment opportunities. In the medium- and long-term strategies, aside infrastructural development, the government sought to boost agriculture through commercial farming, not only for food security but for employment generation. In the oil sector, the local content guidelines would be reviewed as a component of the reforms to give more leverage to Nigerians.

Fiscal Responses

The government responded to the global economic recession by reducing the crude-oil price benchmark in the 2009 budget from US\$59.00 to US\$45.00 per barrel. In addition, projects in the budget were prioritized. Some expenditure virements were approved and supplementary budget was approved as well in late 2009. In addressing the global economic slowdown through fiscal measures, the Federal Government increased expenditures in the areas it considered fiscally sustainable during the trying times to ameliorate the situation. The Federal Government provided the sum of N1.435 trillion to help cushion the effects of the economic crises in Nigeria. The various interventions are N620 billion banks bail out, N460 billion for food security, N26 billion for road construction, N29 million for NDE to train in 14 trades in six geo- political zones and N100 million for cotton and textile garment. The government planned to investment

\$5.3 billion in the Nigerian integrated power project. Also, a N200 billion Commercial Agricultural Credit Scheme was introduced as part of the stimulus package. Other measures designed to execute the relief plan are: support for the National Youth Employment Scheme; clearing verified pension arrears to boost disposable income; increasing the N70 billion injected by the government in February 2009 to revive the textile industry and expanding it to cover the garment industry; and the payment of local contractors.

In consideration of the need to stimulate the economy following the unintended liquidity and credit crunch faced by the various tiers of government due to the banking sector reforms, the sum of USD 2 billion was withdrawn from the Excess Crude Account and distributed to the various tiers of government. In view of the unfavourable crude oil production and market price, the Federal Government also augmented collections from the excess crude account to shore-up the monthly allocation to the three tiers of government.

Monetary Responses

Liquidity management - The expansionary fiscal policy response to the crisis was complemented with relaxed monetary policies pursued by the Central Bank of Nigeria. Some of the monetary policy measures introduced included: i) reduction of the monetary policy rate (MPR) by 50.0 basis points from 10.25 per cent to 9.75 per cent and later to 8.0 per cent (below the inflation rate); ii) reduction in the cash reserve requirement (CRR) for banks from 4.0 to 2.0 per cent; and iii) cutting the liquidity ratio from 40.0 to 30.0 per cent and further to 25 per cent. In addition, the CBN gave a directive to banks that they had the option to restructure the already crystallized margin loans up to 2009. The CBN also expanded the discount window which allowed banks to borrow for up 360 days. It also suspended the aggressive mop-up of liquidity since late 2008. As these actions did not seem

to yield the desired economic outcomes in time, the CBN resorted to direct control measures involving interest rate caps and the re-introduction of exchange control measures.

In an attempt to reduce pressure on inter-bank rates, the CBN reduced the Expanded Discount Window (EDW) rate to a maximum of 500 basis points above MPR beginning from March 16, 2009. This measure is expected to help reduce the problems of banks facing temporary liquidity crisis. Moreover, the bankers' committee pegged the maximum deposit and lending rates at 15 percent and 22 percent respectively, effective from April 1, 2009 until end of 2009, so as to promote the growth of real sector of the economy.

Foreign exchange management - Under foreign exchange and exchange rate management, the CBN adopted an exchange rate adjustment that would help to preserve the country's foreign exchange reserves. To this end, it moved from the Whole Sale Dutch Auction System (WDAS) to Retail Dutch Auction System (RDAS) and to checking the speculative demand for foreign exchange, as well as introducing a band of plus or minus 3 percent to ensure stability. Also, the CBN also restructured Bureaux de Change (BDC) operations by categorizing them into Classes „A“, „B“ and „C“. In addition, sale of cash foreign exchange was limited to bank operated BDCs, and eligible transactions under the RDAS window were revised and enlarged.

Bank Regulation/ Supervision - In response to the global financial and economic crises, the monetary authorities adopted various measures for proper supervision and regulation, as well as ensure soundness of the financial (and banking) system. In order to properly regulate and supervise the banks, the CBN deployed resident examiners to the banks with effect from January 2009. This was in addition to „standby teams“ of target examiners that would be deployed to any bank at any time to identify those that did not observe the accepted code of corporate governance. This was expected to inject discipline and restore confidence in the system. The CBN also rendered advisory service to banks on risk management. This included extra conservation during time of crisis, capital conservation, cost minimization, de-emphasis on size, salaries and or bonuses, to mention just a few. Furthermore, the CBN also strengthened institutional coordination through the Financial Sector Regulatory Coordinating Committee (FSRCC). The CBN has continued to emphasize the use of e-FASS as a tool for banks' returns analysis for speedy identification of early warning signals.

A major reform implemented in the banking sector following the enhanced banking regulation and supervision was the CBN takeover of five commercial banks in the country in a move to save them from imminent collapse. The CBN also sacked the management of the banks and appointed new ones, citing alleged financial and operational misconduct against the former managements as basis for its action. The apex bank also published the names of individuals and organizations that were indebted to the troubled banks and sent the country's anti-graft agency, the Economic and Financial Crimes Commission (EFCC), after them to recover non-performing loans, which were put at about N2.8trillion.

Realizing that the change in the senior management of the banks alone would not solve the distress in the industry, the CBN injected six hundred and twenty billion Naira (equivalent to \$4.0 billion), to reinvigorate the ailing banks. According to the apex bank, the banks had become so weakly capitalized that they posed a systemic threat to the Nigerian economy.

6. AGENDA FOR STRONG ECONOMIC RECOVERY AND LONG-TERM GROWTH MACROECONOMIC POLICY AND STRUCTURAL REFORMS

The macroeconomic policy and structural reforms implemented in Nigeria, particularly over the last decade, have served the country well. However, there is a need to deepen the economic reforms further. This would help minimize the effects of the crisis and lay the foundation for sustainable growth in the country.

Establish the Nigeria Sovereign Wealth Fund and accumulate foreign reserves during high oil prices.

The current crisis underscores the need for Nigeria to design and establish a more formal framework such as Sovereign Wealth Fund [SWF] for the management of oil savings currently held in the Excess Crude Account at the Central Bank of Nigeria as well as and other monies received from other sources. Proper management of such a fund with clear rules to guide investment and withdrawal is required. The fund will insulate the economy from shocks arising from poor management of oil savings. Investment of such funds over a long term would build a strong financial base for the benefit, prosperity and security of future generation of Nigerians even after the nation's exhaustible resources like oil are depleted. It would also mitigate the effect of natural and environmental disasters as well as cushioning the impact of a fall in world oil prices. Among the policy issues that arise during mineral resource booms are the capacity of the economy to absorb fiscal surplus and its impact on the growth rate of the economy, its inflation rate, and matters involving investment policies. To what extent should the current population benefit, to what extent should future generations benefit, and how the two should be linked through investment funding?

Moreover, there is the issue of revenue instability which can be short-term or long-term. Short-term instabilities are a result of drastic volatility of commodity prices. Concerns related to long-term instabilities arise for non-renewable commodities such as oil and gas, which are subject to depletion and cannot be indefinitely exploited. Renewable commodities are affected by long-term instabilities for two reasons. First, long-term prices for commodities relative to manufacturing tend to fall, and with them revenue earnings from those commodities. Second, some commodities, particularly raw material commodities, have increasingly faced the threat of substitution due to new scientific developments in biotechnology and nanotechnology.

Short-term revenue instability presents serious challenges for macroeconomic planning, particularly for fiscal policy management. If expenditure patterns follow revenue patterns, cycles of booms and busts in commodity prices get translated into cycles of booms and busts in fiscal expenditures. As a result, fiscal policy becomes pro-cyclical, implying that spending goes up (and taxes go down) in periods of booming prices and spending goes down (and taxes up) in periods of price busts. Such patterns of expenditure are common in developing countries, and are associated with poor fiscal management. The macroeconomic and fiscal policy challenges are further pronounced by the uncertainties surrounding the long-term sustainability of some natural resources.

Improve and Effective mobilization of domestic resources for development

The financial crisis has diminished prospects for private capital flows to Nigeria. FDI often responds to growth with a lag and so it is not surprising that the full impact of the crisis on

flows to Africa will be felt more in 2009 and beyond. Other forms of private capital flows have also been affected by the crisis. Presently, Nigeria is facing difficulties issuing bonds in international capital markets. The financial crisis has increased the risk premiums that Nigeria has to pay in international capital markets. Accordingly, the country had to cancel its plans to raise funds from the international capital markets.

The drying-up of this source of external finance is a serious setback for development in the country as the money raised would have been used to finance infrastructure development and boost growth. The private sector is also facing challenges in raising funds in international capital markets. The current difficulties in obtaining funds from the international capital markets suggest that Nigeria should learn to effectively mobilize domestic resources to finance development. The need to depend on domestic financing sources is also amplified by the withdrawal of funds by many international banks that extended credit to Nigerian banks and businesses. As mentioned earlier, recall of funds by foreign banks intensified capital flight in Nigeria and was compounded the downturn in the capital market. Therefore, it is important to use the opportunity of the current crisis to introduce reforms aimed at boosting domestic resource mobilization, may be not to increase the tax base but certainly to boost revenue collection.

Desired macroeconomic policy responses Policy Coordination:

There is need to ensure better fiscal and monetary policy coordination now for macroeconomic stability. Essentially, monetary and fiscal policies need to target long-term macro-stability rather than quick wins that take the focus off the path to sustainable development. Single digit inflation need not be a priority in the short term. It is important to decide what level of inflation, interest rate and exchange rate adjustments are tolerable in the short term as a compromise for sustaining high growth. In the long term, low and stable inflation may be achieved with growth and poverty reduction.

Vertical Cooperation among Tiers of Government

The achievement and sustenance of macroeconomic stability also require vertical cooperation among the three tiers of government in fiscal matters, not only in spending, but also in resolving the cases of multiple taxation among them. There is an expansive agenda of policy actions and investments to be undertaken. Hence, it is important for the leadership to be persistent, focused, and determined in order to make the difference. More importantly, the fact of federalism, marked by the overlapping of economic and political responsibilities among tiers of government, makes intergovernmental cooperation essential, if not inevitable, to achieve the goals of macroeconomic stabilization. In the Nigerian federation, the 36 states, the Federal Capital Territory as well as 774 local governments share about 45 percent of consolidated revenue. However, the Federal Government has no statutory powers to control the sub-national governments for the purposes of macroeconomic stabilization. Thus, adoption of cooperative approach to governance is essential.

Development of the Productive Non-oil Economy

There is need for Nigeria to invest heavily in infrastructural development in order to create the enabling environment for a non-oil economy. In this regard, the provision of steady power and water supplies as well as good road and communication networks are very crucial. It is also important for Nigeria to fully explore the ways of reviving its huge

agricultural potential which has been neglected in addition to exploiting its rich untapped solid mineral deposit in order to promote diversification of the economy away from a mono-cultural product base.

Boost Nigeria's Export Competitiveness

To build a solid foundation for sustained high growth, it is important to create an environment for high levels of investment. Both savings and investment have historically been low relative to more rapidly growing economies. Indeed, poor investment efficiency suggests that "effective" investment may even be lower. Evidence shows that savings have not been scarce and neither a binding constraint on investment nor the main factor in the Nigeria's low growth record. Low access to finance and high and volatile interest rate seem to be more serious constraints to economic operators. In particular, term financing is scarce. Low return on investment appears to be the root cause of low investment and low growth in Nigeria. High returns are only evident in few sectors like oil, banking and the food and beverage industry. The high returns on investment in the oil industry are not surprising considering the fact that the industry operates at a high level of efficiency comparable to global standards. In the case of the banking sector, the high returns seem to be primarily from foreign exchange transactions and investment in government securities and not from lending. Regarding the food and beverage industry, it is mostly the multinational operators like Cadbury and Nestle that are expanding their operations and undertaking new investments.

Low returns to investment in Nigeria result directly from the severe infrastructure bottlenecks experienced by firms. Presently, the poor state of infrastructure in Nigeria reduces the productivity and competitiveness of firms in two main ways: it adds to firm costs and reduces competition in the economy. Key among the infrastructure constraints are power and land transportation. Poor access to power forces firms to invest in generating their own power thereby substantially reducing funds available for productive reinvestment. Such self-provision of infrastructure may add as much as 20 per cent to firm costs. In addition, high transport costs due to poor roads, port and rail conditions significantly increase the cost of doing business in Nigeria and increases time to market. Clearly, this environment increases cost of doing business in Nigeria and reduces the ability of firms to appropriate returns.

The immediate focus of the government's growth strategy should be on reforms and investments that will improve investment returns, particularly improving power supply and enhancing the access to and quality of physical infrastructure. Next, policymakers need to institute reforms that will increase the ability of firms to appropriate returns to investment. Principal among the required reform is the need to ensure macroeconomic stability, particularly from oil revenue volatility, and improve the institutions and regulations to guide investment behaviour. Further, enhancing access to capital, especially term finance, is important to facilitate the process of effective intermediation of Nigeria's vast resources in support of non-oil sector growth. However, Nigeria requires significant improvement in the quality of human capital to successfully change the composition of economic activities towards higher productivity areas and integrate the economy more fully into the global market.

7. Strategies to Counter Effects of Global Financial Crises in Nigeria

A good crisis should not go unexploited, and Nigeria should exploit the current crisis to reshape its policies towards its poor and its potential for future growth. Also, we need to manage the current crisis to ensure that it does not reverse progress made recently and reduce the prospects of achieving the Millennium Development Goals (MDGs).

Several strategies can be used to counter the effects of the global economic crisis in Nigeria. These are explained below.

- i) Government need to play active roles in economic management for the development and stability of the economy. The visible hand of the government must assist the invisible hand of the market. It is now clear that if left unchecked, market forces, with all their limitations and inadequacies, can lead to damaging outcomes. Relying on the market cannot provide an effective agenda against poverty.
- ii) Another strategy that is required now is stronger regulation and more professional supervision of the Nigerian financial institutions and strict enforcement of existing financial rules, regulations and laws. Noteworthy is the fact that failed regulatory policy in America contributed immensely to the present crisis just as in the case of the East Asian crisis of 1997/98. May be Nigeria should separate the banking and supervisory/regulatory functions of the Central Bank of Nigeria. Another institution may be established to perform the regulatory functions more effectively.
- iii) There is need to put in place a contingency plan for possible bail-out of any distressed financial institution. This may take the form of injection of funds into such ailing banks through government acquisition of shares which would be bought back when they recover. This approach can aid recovery from recession and ensure safety of jobs, savings and pensions.
- iv) It is not justifiable to use public money to bail out the Nigerian capital market. By nature, share prices are dynamic. Eventually, share prices will rise through the operation of the market mechanism as the other sectors of the economy recover. As people have more money, they will buy shares thereby leading to an increase in the values of the shares. Clearly, the recovery of the Nigerian capital market largely depends on developments in other sectors.
- v) Increase spending, particularly on infrastructure development, even though this would increase budget deficits, to do otherwise would increase poverty. This increased spending will mean Nigeria would be in a better position to increase growth after the current crisis.
- vi) Even though we need to stimulate aggregate demand for goods and services by public spending, such government expenditure must be very productive. A situation of unimplementable budgets whereby funds meant for capital projects are returned to the treasury at the end of the year will make it difficult to counter the adverse effects of the global economic crisis in Nigeria. Hence, profligate, corrupt and inefficient public spending should be discontinued or sanctioned more seriously.
- vii) The CBN sometime ago announced a number of expansionary monetary policy measures: reduction of Monetary Policy Rate, slashing of liquidity ratio, cutting down of cash reserve ratio, etc. These are in the right direction. But these must be complemented with fiscal policy measures also aimed at boosting aggregate demand

and avoiding economic recession.

- viii) The current global economic crisis presents a golden opportunity to take decisive steps to reduce the current precarious dependence of the economy on just one product for revenue and foreign exchange earnings. In the periods of oil windfall, the country had missed golden opportunities to diversify the economy and develop a robust infrastructure base. Rather, oil revenues were largely squandered and mismanaged by the ruling class. A diversified economy has some in-built mechanism to withstand external shocks.
- ix) In the interim, there is need for an aggressive non-oil revenue drive starting from 2010 to bring all taxable adults who had been evading and avoiding tax into the tax net. It is only non oil revenue that can guarantee us sustainable development. Also, there is need to strive for improved revenue through improvement in the efficiency in collection and administration of existing taxes.
- x) Another important strategy necessary to counter the effects of the global economic crisis in Nigeria is to build confidence in the Nigerian banking sub-sector which has shown some resilience towards the global financial crisis. The recent floating of bonds in the capital market by both the Federal Government and Lagos State Government point to government's confidence in the market. Given the high degree of capitalization of the banks, their continued posting of huge profits, and their strategic moves at the moment, they should be able to withstand shocks. They should equally endeavour to boost confidence in the capital market by enhancing the liquidity of that market.
- xi) Adequately fund and reform the National Bureau of Statistics. Government must make deliberate efforts at successfully implementing the new Statistical Master Plan to boost production and dissemination of quality, reliable, robust and timely data for planning and business forecast.
- xii) Government must come up with policy framework for gradual transformation of the large informal sector of the Nigeria economy. Unofficial sources have claimed that the informal sector of the domestic economy constitute about 40 per cent of economic activities thereby leading to gross under estimation of Nigeria's gross domestic product. Besides, the formalization of the underground economy will boost government revenue through widening of tax base and also provide veritable information for strategic management of industrial development of Nigeria.

8. CONCLUSION AND RECOMMENDATIONS

The current global economic crisis is the second round of the financial crisis which began in USA in August 2007. The crisis has its roots in a banking practice called sub-prime mortgage lending in the USA. The crisis has become contagious moving quickly across assets, markets and economies in view of global integration and connections among financial institutions. This paper examines the implications of the global economic crisis for the Nigerian economy. The paper concludes that the impact of the crisis is already manifesting in Nigeria with greater effects likely afterwards. The following steps are recommended for action:

Restore confidence by Strengthening risk management

With slowing growth, corporate default rates and non-performing loans can be expected to rise. Banks exposed to sectors which are very vulnerable to the slowdown like the export-oriented sectors, may be at greater risk. Supervisors will need to ensure that banks properly classify loans and conduct full scale evaluation of all financial institutions to assess their balance sheets. The strengthening of the regulatory structure and cautious risk management would restore confidence in the banking system.

Standing ready to recapitalize the banking system, if necessary

In view of the possibility of a larger than expected wave of corporate defaults leading to bank failures, authorities should consider contingency plans, if public funds are required to prop up the capital base of financial institutions.

Increase demand

Economic crises are more painful to developing countries like Nigeria which have no social safety nets to cushion the impact of recession. Therefore, the Nigerian governments need to provide safety nets to the citizenry to lessen the effect of the crisis on the people. The fiscal package should be timely, large, lasting and sustainable: timely, because the need for action is immediate; large, because the current and expected decrease in private demand is very large; lasting because the downturn will last for some time; and sustainable, so as not to lead to a debt explosion and adverse reactions of financial markets. Fiscal packages such as spending increases, and targeted tax cuts and transfers, are likely to have the highest multipliers. General tax cuts or subsidies, either for consumers or for firms, are likely to have lower multipliers.

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