A focus on citizens' well-being would recalibrate investment priorities

Reforms and infrastructure in Nigeria

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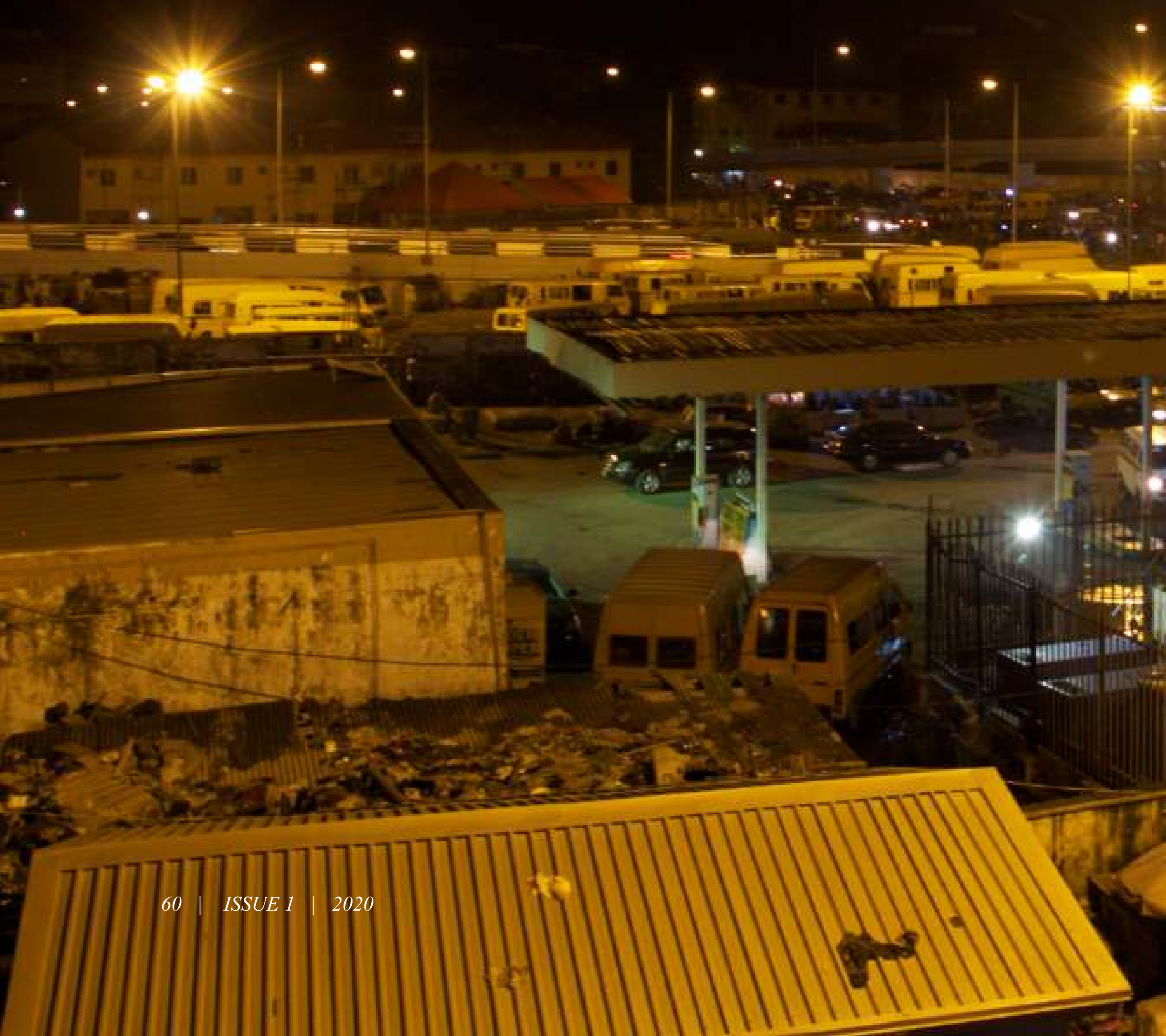
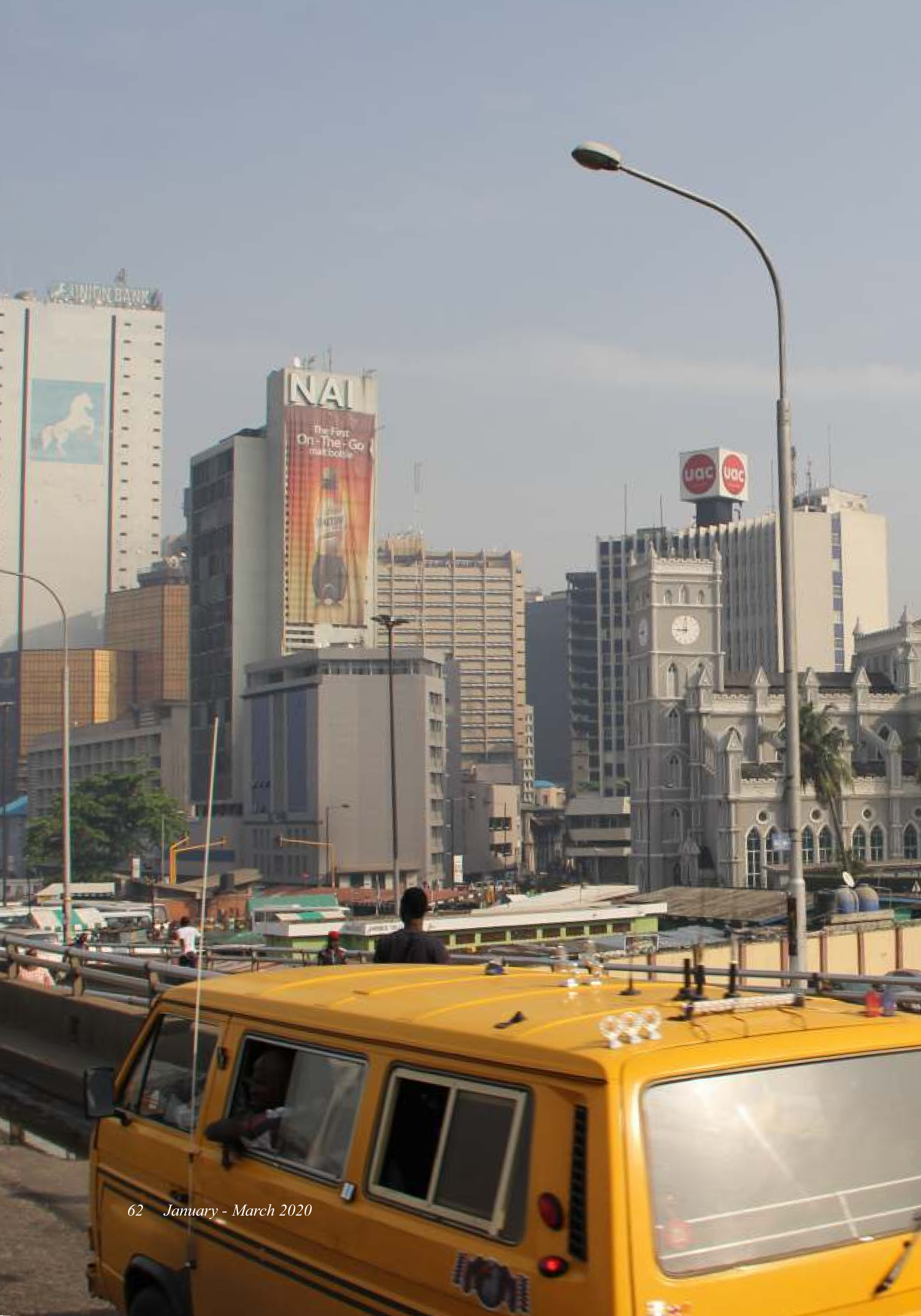


Key Recommendations

- Nigeria should reduce the public sector's stranglehold on the "commanding heights" of the economy, especially the Federal Government's operational control of sectors like infrastructure.
- There is need to drastically reduce the time needed for procurement along with easier methods for the private sector to undertake PPPs and JVs with the Federal Government on key infrastructure projects.
- Liberalisation of entry by private sector players into the infrastructure sectors and easing of regulations and bureaucratic control will enable market forces to determine pricing for the benefit of public finance, the infrastructure stock and broader economy.
- Urgent policy changes are needed to make it easier and profitable for informal sector businesses to formalize, enter national data and the tax net, and the enhancement of systems for paying and interrogating all business taxes, etc. Beyond streamlining business registration, more supportive measures are needed to encourage growth of SMEs.

Nigeria's need for fundamental and sustained economic reform is magnified by deeply worrisome key economic indices. The country's population is approaching 210 million, while real gross domestic product (GDP) growth, which was 6.2% per year at its 2014 peak, now stands at 2.3%, which in turn is below the population growth rate of 2.6%. The national debt stood at $73.2 billion on 30 June 2018, or 19% of GDP, driven significantly by an increase in external debt from $4.6 billion in 2015 to $22.8 billion in 2018. This has been magnified by the approximately 60% devaluation of the naira during the same period. Taken alone, these numbers would not be so bad if they reflected sustainable national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investments in physical (land, air, sea transport, electricity and natural gas) infrastructure or an exponential increase in Nigeria's non-oil exports. Unfortunately, this has not been the case.

This paper contends that in the past 45 years two major factors have arisen to challenge Nigeria's socio-economic growth. One is the total dominance by the Federal Government of Nigeria (FGN) of the key levers of the national economy – commanding the commanding heights, as it were. The other is Nigeria's cultural devaluation, signified by its descent from an ethos of national excellence to a constant squabble driven by the lowest parochial denominators of tribe, tongue and religion. As *The Economist* recently noted, “acquired social codes also influence individual choices, and thus broader economic activity”. While it is not the focus of this paper, this latter factor, its negative effect on the political economy and how to remedy it is surely a necessary discussion that Nigeria can no longer avoid. Nevertheless, the negative effects of both factors on the country have continued to play a major role in the deficit in its infrastructure growth.

Considering that practically the entirety of Nigeria's vital infrastructure stock is tightly held by the FGN, the country's most urgent economic policy imperative surely is to loosen the federal public sector's hold on the commanding heights of the economy. This is particularly true of key infrastructure assets, which will enable private sector investment in target sectors by the fastest means possible. This urgency is driven by three harsh realities. First, the FGN has inadequate revenue streams - achieving barely 50% ($31.3 billion) of expected revenues of approximately $60 billion during the past three fiscal years. Second, there is the massive debt profile summarised earlier, which is now probably higher than $80 billion. Third, the debt service-to-revenue profile went from 32.7% in 2015 to 69% in 2018. According to the Budget Office of the Federation, this looks set to grow to 82% by 2022.

What has worked and why?

In the past four years it has been hard to find what has worked; in other words, policies that have led to increased investment and economic growth. It is even harder when physical infrastructure is considered. Projects - such as there are - in roads, rail, ports, electricity, natural gas are all at best works in progress. The FGN's primary focus on the fight against corruption, the fight against Boko Haram, the execution of social welfare programmes (school feeding, N-

Power, Trader Moni, Market Moni, etc.), the defence of the naira by the Central Bank of Nigeria, and several separate policy initiatives in the infrastructure space, have all so far produced suboptimal results.

The evidence can be discerned across several infrastructure clusters. First, in terms of roads**,** total dependence on a depleted national budget meant that no new federal roads were added. At the same time, maintenance of the existing stock continues to fall behind demand. A few key initiatives – the Kaduna-Kano Expressway, the Second Niger Bridge, Onitsha, and the Lagos-Ibadan Expressway resurfacing – seem to have gained some momentum and are now underway. This situation makes even more glaring the many other projects, literally in every state, that are not being considered at all. The situation is worsened by the slow implementation of the capital budgets for roads and the abysmally lower proportion of funds released, hovering between 10% and 15% over the past three years.

Second, in the rail sector, the massive effort to mobilise Chinese bilateral funding to construct a standard gauge railway network across the country has yielded mixed results. The Abuja-Kaduna standard gauge link was commissioned but remains entirely dedicated to carrying passengers. So far, the construction of a standard gauge line from Lagos to Kano is assured only of getting to Ibadan and hopefully being commissioned in 2020. It is not clear whether funds are available to extend it to Kano. The story is similar for the Port Harcourt-Maiduguri Eastern Line. It is also unclear whether the loan terms for some of these projects will not push the country into a debt trap. The effort to concession the legacy national narrow gauge rail system to a consortium of international companies continues to wind its tortuous way through a complicated procurement process.

Third, Nigeria's ports still perform sub-optimally and thus create a viable business case for ports like Cotonou and Lome to act as alternatives to the Lagos Port Complex. On the other hand, projects such as the Lekki Port/Lagos Free Trade Zone have succeeded in mobilising capital for a new deep-water port project that has proven itself to be fully bankable on stringent engineering and commercial parameters. It is no coincidence that the promise of great things in Lagos comes from private sector activity. This is only because state actors have refrained from going directly into business themselves and instead focused on creating an enabling environment for private investment.

Fourth, Nigeria's electricity sector, together with natural gas, is yet to fulfil its promise. Electricity reforms between 2005 and 2013 slowly went through the planned stages of unbundling, corporatisation, the establishment of a fully autonomous sector regulator and finally privatisation. Yet geometric growth in electricity consumption per capita has not materialised. Rather than blame privatisation, as some have done, a closer study will show that energy sector (electricity and gas) growth has been hindered by suboptimal, even negative, regulation and policy-making. It also does not help that natural gas and electricity transmission is controlled by two FGN parastatals with dissimilar purposes and strategies, controlled or supervised by two separate ministerial portfolios.

Finally, efforts to improve the ease of doing business in Nigeria are showing results, which ironically are almost unnoticed or insufficiently appreciated. The FGN's focus on upgrading Nigeria's ease of doing business rankings has had some success, as have similar efforts in some states like Lagos. Yet this is only one part of the comprehensive policy package needed to make Nigeria's business environment truly viable. A necessary complement is enhancing the prospects of entrepreneurs' running and growing their businesses successfully, which remain difficult in Nigeria. Two features of the country's economic landscape make this task even more difficult. These are the negative, almost predatory, policy/bureaucratic/regulatory environment in which Nigerian businesses, big and small, operate, and the high, multiple fiscal impositions such as taxes and levies.

What can be done?

The FGN must undertake several key actions to prevent Nigeria from finding itself far adrift of its peers and the region it should be leading.

<u>1. Make it easier and profitable to formalise</u>: Nigeria's informal sector was responsible for a massive 75% of GDP in 2010, according to a study by Mgbabor and Malaolu (2013). They note that “unemployment, [the] tax burden, government regulation and inflation are the most important drivers of informality in Nigeria”. Of these, the tax burden and predatory regulatory practices are the most important factors that the FGN can control. Indeed, if these two are eased and informal small and medium enterprises (SMEs) are encouraged to formalise, they will in turn help to reduce the inflation

significantly. The ease of upgrading into the formal sector and the even more important need to ease running and growing a small business will create a wider baseline and stream of tax revenues to help ameliorate the unsustainable debt-to-revenue profile that the FGN currently carries.

So, while it is good to focus on improving the country's ease of doing business ratings, it is now more important to focus on improving the indices around the ease of managing and growing SMEs. In addition, recognising that the heavier tax burden that formal companies face is a huge disincentive to their growth, the Joint Tax Board should work to streamline state and federal taxes, reduce rates and develop a simple and user-friendly system for informing taxable individuals and entities of their tax liability and enabling them to pay their taxes and interrogate tax authorities easily.

<u>2. Reduce procurement time and foster infrastructure partnerships and joint ventures</u>: Senior public servants may want to ask private sector players a simple question a lot more often: "How may I help?" A common answer would be: "Let go of underutilised and undercapitalised assets and do it quickly." In this regard, the National Assembly has a vital role to play. Three pieces of legislation have turned out to be suboptimal and a major brake on the speed at which assets can be turned over to private sector investment. These are the Public Procurement Act, the Public Enterprises (Commercialisation and Privatisation) Act and the Infrastructure Concession and Regulatory Commission Act. Often when the idea of a joint venture between private interests and a relevant FGN Ministry, Department, and Agency (MDA) is mooted, at least two, sometimes all three, of these acts come into play, easily adding 18-24 months or more to a transaction timetable.

The political reality is that the process of getting a major project past the initiation, negotiation and transaction documentation stages is often protracted. This is a disincentive to even start in the first place, during a single ministerial or presidential tenure that may not be renewed. As a result there has been gravitation towards a short-term policy and planning perspective. The National Assembly should work with the Executive Branch to create a limited window for temporary exemptions to the application of aspects of these laws. Alternatively, new legislation can also grant powers to the President-in-Council to cut short compliance times and/or exclude certain critical projects from strict compliance with said laws. This would enable projects with significant value-for-money potential to be executed rapidly if certain simpler technical, commercial and financial parameters can be met.

Thus, joint ventures and concessions could be proposed, studied, negotiated and concluded in roads, land transport, aviation (particularly in airport and airspace operations/management), electricity and natural gas processing/transmission. Given the few precedents in private investment in infrastructure, it is certain that speeding up transaction times can only have a positive effect on the national economy.

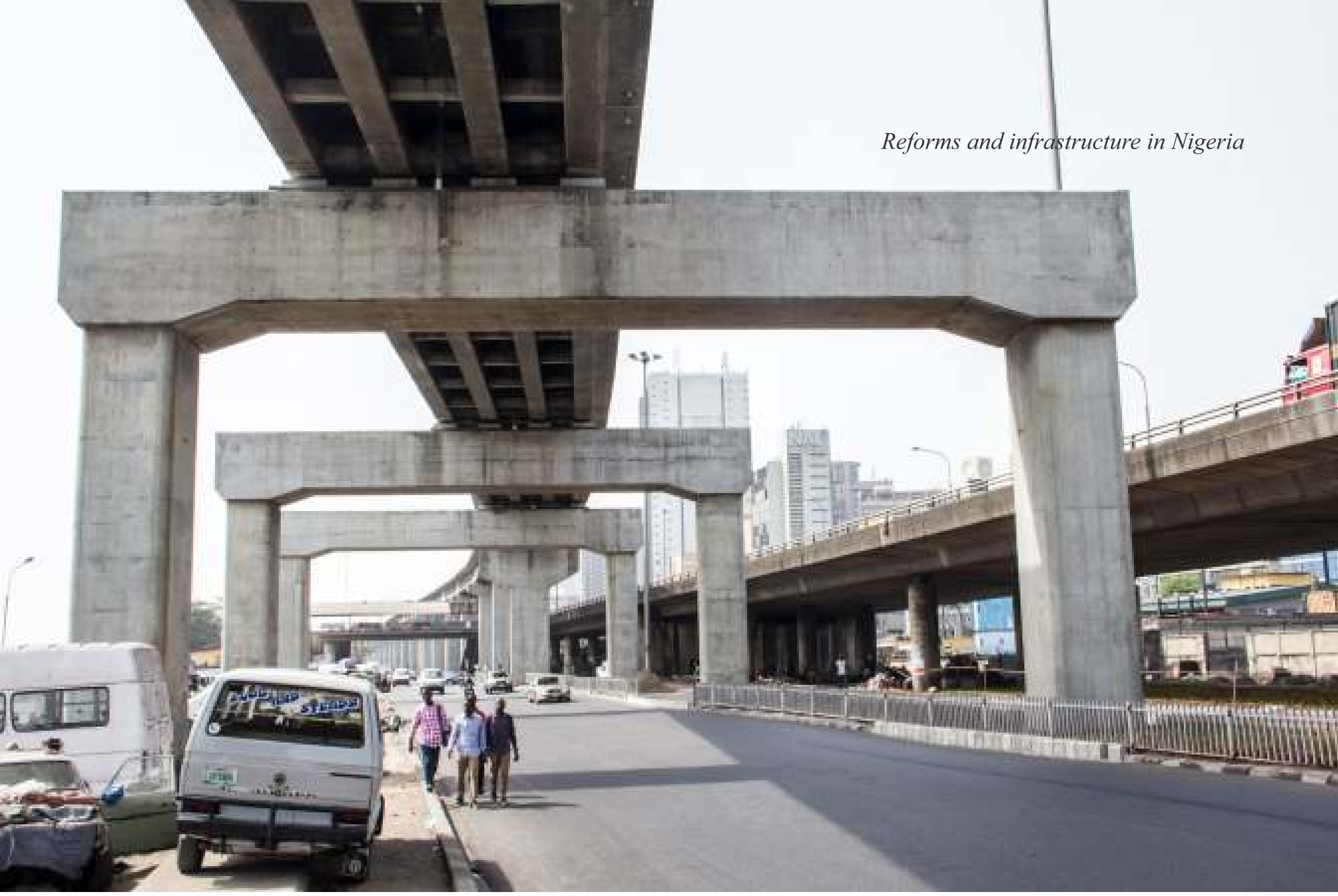
3. De-regulate infrastructure sectors: "De-regulate" is used here to mean liberalising entry into these sectors by reducing the number and cost of the various current barriers to entry. It is also important to reduce the many unwieldy rules and regulations with which players in the infrastructure sectors must contend. Two issues here are of particular interest. The first concerns the need to significantly reduce reporting requirements of regulatory agencies like the Nigerian Electricity Regulatory Commission (NERC), Nigerian Communications Commission (NCC) and Department of Petroleum Resources (DPR) to the minimum. To this end, the Presidential Ease of Doing Business Council (PEBEC) should be mandated to investigate this question and identify regulations for which compliance should be suspended or even terminated.

Another option is to permit market forces to come more into play in pricing infrastructure services. For instance, the Minister of Power could issue a policy directive to NERC under section 33 of the Electric Power Sector Reform Act, 2005, to fully deregulate electricity tariffs and foster a true willing buyer-willing seller electricity market. If the right tariffs are set, distribution companies (DISCOs) would enter into more supply contracts and all the players in the electricity value chain – generation, transmission, distribution, natural gas (exploration, processing, supply and transport) – would be incentivised to invest in revamping and expanding their asset base and growing steadily once again. This can rapidly augment the current grossly insufficient average daily output of 3 900 MW delivered to the national grid.

<u>4. Foster devolution through contracts with state governments</u>: One of the key elements of the electoral platform set out by the ruling party, the All Progressives Congress (APC), is the devolution of exclusive federal powers to the states. Typically, this would be via a convoluted constitutional amendment process involving the 37 national and state legislative houses. This would take years to design and more years to execute, which is simply not a politically viable option. A better way to devolve responsibility for speedily initiating and contracting major infrastructure public-private partnerships (PPPs) would be for the FGN to enter into "administrative contracts" with State Governments. In this way, the FGN and the three or four states, for instance, through which a long stretch of a major federal road (trunk "A") passed could enter into a contract whereby responsibility for contracting a PPP was devolved to these states. Certain simple preconditions could be set for these states to meet, such as the express intent by credible private sector financial and operating entities and development finance institutions (DFIs) to work with the states in designing, financing and procuring such PPP projects. Those states would then undertake a much faster process of project development, capital raising and project contracting. Apart from preparing the grounds for constitutional devolution, this would be a practical way to get much-needed investment to where it is needed.

Conclusion

Since 2015, economic reform in Nigeria and the growth that it seeks to foster have slowed considerably. The FGN has been occupied with maintaining macroeconomic stability (at an increasingly great cost), as well as waging an anti-corruption war (which has in no way addressed the institutional causes of



corruption) and a war in the Northeast (which has hugely distracted national governance and leadership).

The true focus of national security ought not to be regime security or the wellbeing of the president of the day or the maintenance of the FGN's dominance of the commanding heights. Rather, it should be the wellbeing of the citizen. The strategic elements of national security – military, diplomatic, intelligence and economic – must be singularly focused on this. If the economic reform ideas briefly discussed here are examined in further detail, a focused economic strategy for loosening the hold of the FGN on major infrastructure assets that straddle the commanding heights of Nigeria's economy can be developed and implemented.

The direct result of such a strategy would be to catalyse direct investment into the country's grossly inadequate infrastructure stock and various other sectors of the national and state economies. This would yield positive effects on the wellbeing of Nigeria's citizens and, ultimately, the advent of a peaceful and progressive Nigeria that has been so long in the making yet never realised.