On the Dynamics of the Oil Resource Curse in Nigeria: Theory and Implications

Paul Terna Gbahabo and Emmanuel Oduro-Afriyie

Department of development Finance,

Stellenbosch University, Cape Town South Africa

Abstract

The paper provides conceptual insights and in-depth analysis of the dynamics of the oil resource curse on the political economy of Nigeria. Using a combination of the resource curse and structural transformation theories, we highlight the perverse connections between oil dependence and weak institutional framework as well as low human development and its concomitant effect on conflict and political instability in Nigeria. We employ cross sectional data across selected countries in Sub-Saharan Africa and within Nigeria at various intervals under different groupings between the periods 2005 to 2016 to benchmark Nigeria's performance in terms of development indicators such as gross fixed capital formation; quality of governance and institutional capacity; level of inclusive human development; infrastructure performance and spread of the tax base. The study found that Nigeria compares abysmally poor in terms of the development indicators analyzed and therefore lags behind many countries in the region. We conclude in line with extant literature that to some degree the low development performance of Nigeria is symptomatic of the oil curse and common to many other mineral exporting countries in many developing regions of the world. The policy implications of this paper implies an urgent need for structural transformation of the economy from sectors with low productivity and net employment such as mineral exploration to sectors with high productivity and employment such as agriculture and manufacturing in order to stimulate the creation of better and productive jobs for the bulging population. The study also recommends an urgent need for institutional reforms that will strengthen the governance and administrative capacity of the country in order to foster a paradigm shift from a rentier economy to more inclusive and sustainable economy.

Keywords: Oil, Resource, Curse, Structural, Transformation, Nigeria

JEL Classification Numbers: 01, 04, 05, 055, 057, Q0, Y10

"More than any other group of countries, oil-dependent countries demonstrate perverse linkages between economic performance, poverty, bad governance, injustice, and conflict. This is not due to the resource per se, but to the structures and incentives that oil dependence creates" – **Terry Lynn Karl, 2004.**

"Nowhere are all the pathologies associated with oil as clearly manifest as in Nigeria. In past decades, Nigerian rulers may have plundered oil wealth to the tune of tens of billions of dollars. The explosion in windfall financed government expenditures also provided increased opportunities for kickbacks. All of these factors have contributed to poor growth but also to staggeringly destructive development outcomes. Thus, oil, and the institutional deterioration that it has led to,

has perhaps been the single most important cause of Nigeria's economic and political problems"- **Sala-I-Martin, March 2004**.

"Nigeria made a terrible mistake by becoming a mono-product economy hinged on oil and we are now in a volatile situation due to the crash in oil prices"- **President Muhammadu Buhari, May 2016.**

1. INTRODUCTION

Oil can be both a blessing and a curse to economic growth and development. With a per capita Gross Domestic Product of over $69,200 in 2016 and a Gini-coefficient of 0.26, Norway is effectively one of the most prosperous and most equal countries in the world. There is no doubt that oil windfall has been central to this economic miracle. On the other hand, Nigeria's economic development has been nothing short of a disaster. With a Gross Domestic Product per capita of $5942 which is below the regional average in Sub-Saharan Africa and a high incidence of poverty of 54% accounting for over 90 million of the population, Nigeria is one of the poorest and most unequal countries in the world despite earning billions of dollars annually in oil revenue (UNDP, 2015). The central puzzle is to determine what factors account for such widely divergent economic developments particularly with regards to human capabilities and infrastructural development between these two oil exporting countries. Why hasn't there been a trickledown effect on the living standards of a vast majority of the population of Nigeria, despite enormous oil export revenue over the years and why hasn't a consistent 5% economic growth over the last decade improve the lives of the lot? Why has oil revenues enabled Norway to prosper while sending Nigeria on a downward spiral with a myriad of development challenges as such weak and rent-seeking institutional framework, high unemployment, rising poverty and inequality, massive infrastructural decay and low tax culture.

The political economy of Nigeria has had a checkered history. During the colonial era and in the subsequent years following independence, agriculture was the central pillar of the Nigerian economy accounting for over 90% export and employing over 70% of the population. It is important to note that because government depended heavily on the export of agricultural commodities, priority was given to that sector of the economy which had positive social economic consequences on the wellbeing on the vast majority of the population. Given the small-holder-agriculture cultivation prevalent in the country, government had to mobilize a lot of her population to engage in agricultural production to enable government raise enough revenue to meet her social obligation of providing infrastructure and other basic services, and this by extension entailed massive job creation, low unemployment, low inequality and poverty ratio in the country. It was estimated at the time of independence in 1960, only less 19 million people were classified as poor contrast that with present over 90 million, (UNDP, 2015; Ayanwu, 1997).

The discovery of crude oil and gas marked a paradigm shift for the worse for Nigeria as the country completely neglected and abandoned both its fledging agricultural sector and nascent manufacturing industry to become overwhelmingly dependent on oil exports.

2. THEORETICAL FRAMEWORK; STRUCTURAL TRANSFORMATION AND MINERAL RESOURCE-GROWTH NEXUS

The theoretical framework in this paper explores a combination two theories, the resource curse thesis and the structural change theory and the impact the former have on the latter. The resource curse theory also known as the paradox of plenty states that there is an inverse association between natural resource abundance, especially minerals and oil, and the desirable structural change that is required for economic growth and development to take place in developing countries. In other words, minerals such as oil have an adverse and nonlinear effect on economic growth via its destructive impact on the institutional framework of a country (Sala-i-Martin and Subramanian, 2003; Karl, 2004). Other transmission channels through which mineral resources negatively impact on economic growth include the “Dutch disease effect- a strong currency arising from oil windfalls that impedes export of other commodities” and the effect of volatility of commodity prices on the economy. This association has been repeatedly observed to be so persistent in different time-series and cross-country analysis with different population size and income levels, type of government and composition. Specifically, it was found that countries without petroleum resources grew four times more than petroleum-rich countries (Ross, 1999; Auty, 2002; Sachs, 2001).

Empirical evidence from members of the Organization of Petroleum Exporting Countries (OPEC) between the period of 1965-1998 shows that OPEC members experienced an average decline of 1.3% in GNP per capita per annum during the period under review, whereas the combined average growth rate for developing countries with the similar income levels was 2.2% per year over the same period. Further research has revealed that the greater the dependency on oil, the worse-off a country becomes in terms of economic structural transformation (Karl, 2004; Sala-i-Martin and Subramanian, 2003; Stiglitz, 2012).

The structural change theory propounded by William Arthur Lewis (1954) also known as the two-sector-model states that for underdeveloped economies to become developed, they will need to transform their domestic economic structures from a heavy emphasis on traditional subsistence economy with a high supply of labour to a more modern, more urbanized and more industrially diverse manufacturing and service economy with higher productivity. A modification of this theory by Chenery and Taylor (1968) simply known as the patterns of development theory focuses on the sequential process an undeveloped economy must follow in other to become industrialized. These

sequential patterns of development emphasize a shift away from subsistence agriculture to industrial production, via the steady accumulation of physical and human capital from areas of low productivity to areas of higher productivity and value addition accompanied with changes in consumer demands from basic necessities to industrial goods and services. This shift in turn will stimulate rural-urban migration with concomitant consequence for demographic transition.

William Baumol (1967) also made his own contribution the structural change theory. In his version, for undeveloped economies to transform into a more industrially diverse manufacturing and service economy, there would have to be a transition from a stagnant sector that uses only labour as the input to a more progressive sector that uses new technology to stimulate growth and productivity in an economy. From a development finance perspective, it is pertinent to note that structural transformation does not only create GDP growth and higher productivity in an economy but also creates new employment in new areas of the economy thereby drastically reducing unemployment, poverty and inequality in the society (OECD, 2013). It is also important to view the stellar economic development experiences of China and Brazil in drastically reducing poverty for more than two decades this context (OECD, 2013).

The link between the resource curse theory and the structural transformation theory is that it is much more difficult for developing economies with oil resources to achieve the necessary structural transformation because there are no incentive for the government to proactively pursue policies that will structurally transform the economy due to the frequent large inflows of dollar-denominated revenue at almost zero cost generated from oil or minerals exports. Moreover, the presence of oil or minerals tend to very quickly destroy the socioeconomic and administrative institutions by turning the state into a rentier state where the state exclusively generates revenue from oil rents rather than from direct taxation, and therefore are likely not to tax the populations(Sala-i-martin and Subramanian, 2003; Karl, 2004). In other words, governments that have unrestricted recourse to oil rents do not have the necessary incentive to structurally transform the economy to other areas of wealth creation that they can subsequently tax; the population in turn, has less incentive to demand accountability and representation in government. These disconnect between taxation and representation reinforces a culture of rent-seeking and corruption leading to institutional failure of government with a concomitant adverse effect on the climate for investment and growth.

It is the authors' considered opinion that it is the combination of the resource curse and the failure to undergo structural transformation that has led the Nigerian state into its present quagmire of underdevelopment with high youth unemployment, rising poverty and inequality, dilapidated infrastructure, and consequent high insecurity.

3. CONTEXT AND BACKGROUND OF THE NIGERIAN ECONOMY

Nigeria is the country with the largest population in Africa with a population of over 180 million people comprising 18% of Africa's total population; it is safe to say 1 in every 6 Africans is a Nigerian. Following the 2014 Gross Domestic Product (GDP) rebasing, Nigeria emerged the largest economy on the continent with 2017 GDP estimated at $414.398 billion (National Bureau of Statistics, 2017). Since the year 2000, the Nigerian economy has been consistently growing above 5% on an annual basis but GDP growth contracted by -1.51% in the year 2016 recording a real GDP of N67, 984.20 billion for the year due to a fall in the value of crude oil in the international commodity market which Nigeria relies heavily upon for both government revenues and foreign exchange (Nigerian Bureau of Statistics, 2017). However despite having the largest economy on the continent and impressive growth rates, Nigeria is ranked as lower middle income country by the World Bank as well as low human development country by the United Nations Development Program due its poor performance in terms of per capita income and high multidimensional poverty (Organization of Economic Cooperation & Development, 2015).

Nigeria is a member of the Organization of the Petroleum-Exporting Countries which it joined in1971. With an estimated 2.5 million barrels of crude oil produced daily, Nigeria effectively qualifies as the 10th largest oil producer in the world, and is also home to the second largest oil reserves in Africa after Libya. Nigeria is also richly endowed in other valuable minerals, such as gold, iron ore and coal. Nigeria is heavily reliant on rents from oil production. According to the International Monetary Fund 2013 report, government revenues generated from the oil and gas sector accounted to 76% of total government revenue and approximately one third of GDP in 2011. Although the share of oil revenue to GDP is gradually declining, Nigeria remains a resource-intensive country according to the International Monetary Fund.

The return to democracy in 1999 ushered in a new wave of economic reforms chief amongst them include government disinvestment from State Owned Enterprises in order to break monopolies in strategic sectors of the economy such as telecommunications as well as banking sector reforms that strengthen the prudential regulation of the banking sector.

The agricultural sector is the second largest contributor to economic output in 2016 after the service sector, accounting for 24.43% of GDP, up from 23.11% in 2015. The agriculture sector provides employment for two-third of the country workforce and a major source of livelihood for nearly 90% of the rural population. Though agriculture once boasts being the mainstay of the economy (contributing over 60% of GDP and 90% of exports during the time of independence), the sector has long been abandoned since the commercial exportation of oil began. Though food imports have recently been declining, from $6.7 billion in 2009 to 4.35billion in 2013, Nigeria still remains a net importer of food and agricultural products due to the subsistence nature of

smallholder farming that preoccupies a large part of the population (Food and Agriculture Organization, 2012).

The services sector is the now effectively the largest contributor to total GDP accounting for 53.55% of GDP in 2016. The main drivers of growth in the services sector is financial services which has been performing very well since the 2009 banking reform which has led to a substantial improvement in liquidity thus making banks better placed to adequately provide financial intermediation in the economy. Other key drivers of growth in the services sector include telecommunication services as well as wholesale and retail trade. Nigeria telecommunication sector is the fastest growing on the continent. Similarly, the Information and Communication Technology (ICT) subsector has been experiencing rapid year on year growth of about 25% and contributing about 8.5% to GDP per annum in 2013 thus making it the fastest growing sector in the economy (Ministry of Communication, 2014).

The industrial sector constituting a third of the overall national GDP is dominated by the extractive industries. The manufacturing sector has been a bit unstable over the years fluctuating from 9.5% in 1985 to 2.5% in 2009 and experiencing a rebound to 9.5% in 2015 (World Bank, 2016).

Table 3.1: Facts about Nigerian economy at a glance

Variable	2000	2010	2015
GDP ($ billions)	46.4	367.1	486.80
GDP Growth (annual %)	-1.4	8.9	2.79
Value added in Agriculture (% of GDP)	38	41	23.1
Value added in Services (% of GDP)	44	43	53.2
Value added in Industry (% of GDP)	18	16	23.7
Export of goods & services (% of GDP)	18	22	10.7
Import of good & services (% of GDP)	26	49	10.8
Gross capital formation (% of GDP)	11	40	15.5
CPI Inflation (annual %)	6.9	13.7	9

Source: World Bank Indicators, 2016.

4. THE MAIN DEVELOPMENTAL CHALLENGES FACING NIGERIA

Any attempt to study the major developmental challenges confronting Nigeria is bound to fall short and run the risk of overgeneralization and oversimplification due to the large and diverse nature of the country. Although richly endowed in both human and natural resources, Nigeria has failed to make the most of its unique situation due to poor governance stemming from the trappings of oil windfall. Therefore, Nigeria is overwhelmed with a myriad of developmental challenges such as poor institutional quality, high rate of corruption and rent-seeking among public officials, massive

infrastructural deficit, high insecurity, high incidence of poverty, rising inequality, large peasant economy and hence low tax base.

For the purpose of this paper, we shall be focusing on the following; undiversified oil dependent nature of the economy that is constantly subjected to the volatility of the commodity; Poor governance and weak institutional framework that reinforces an atmosphere of rent-seeking and pork-barrel public service; the rising poverty and inequality as well as high rate of unemployment amongst the youth between the ages of 15-24 fuelling high crime rate and terrorism in the society; the deplorable nature of the infrastructure in the country especially electricity and economic impact on the economy; the vast untaxed population engaged in the informal sector as reflected in the low tax revenue base of the economy thus denying the government vital source of revenue to provide basic services.

4.1 Undiversified Oil-dependent economy

Crude oil has been a dominant source of government revenue since it was first exported in the 1960s, accounting for two-thirds of government revenue which is over 70 % of exports (Figure 4.1A). The conditions and episodes of growths of the economy tend to correlates with episodes of oil boom at the international commodity market. This therefore, calls into question the issue of sustainability. How sustainable is a growth model that is dependent on oil windfalls that are acutely sensitive to the volatility of a single product at the international commodity market? This development challenge has been recognized by successive governments in Nigeria; in fact the issue comes to the front burner of national discourse every time there is a decline in global oil price. The current Nigerian government policy pronouncement to diversify the economy due the crunch on national revenue as a result of the recent steep in oil prices by more than 65% (from a peak $112 per barrel to an all-time low of less than $39) since mid-2014 is one such incidence (Organization of Economic Cooperation & Development, 2015).

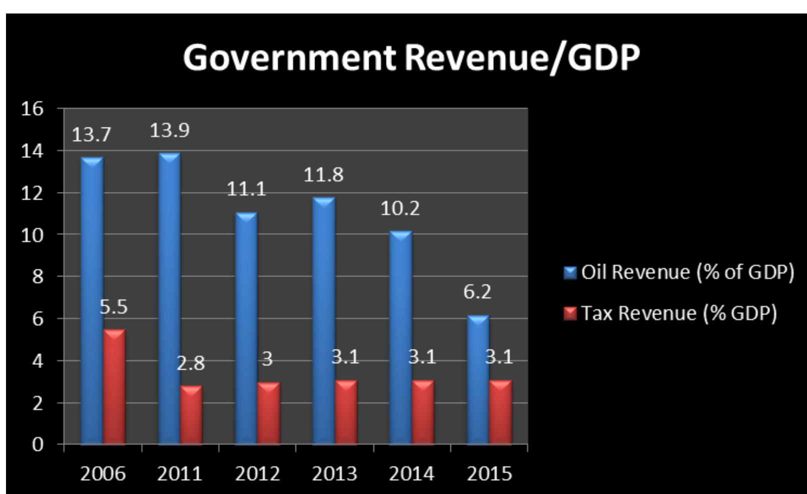
Perhaps the three well-known adverse effects of oil dependence on the Nigerian economy are as follows; The Dutch disease effect-during periods of oil boom between 1973 and early 1979 the Naira appreciated due to the huge inflows of oil revenue to the country and this had an adverse effect of impeding exports in other sectors of the economy such as the fledging agricultural sector and nascent manufacturing industry. The agricultural sector which employs the bulk of the population was neglected thus agricultural exports plummeted by nearly 50 % in value and by more than 50% in volume. This phenomenon whereby an oil exporting country becomes exclusively dependent it for exports and by extension rendering other sectors of the economy noncompetitive is referred to as the Dutch disease. The reduced competitiveness in other productive sectors of the economy in turn makes the diversification of the economy particularly unattractive thus reinforcing oil-dependence in the economy (Canagarajah and Thomas, 2001).

Secondly, the fact that oil mining and exploration is a capital intensive rather than a labour intensive industry compounds the situation thus creating what is known 'jobless growth' or 'growth without development' in the economy. Apart from the fact that the oil industry absorbs a very low percent of job per unit of capital employed, it mostly seeks high expatriate-skills as well as the very limited opportunities for technology diffusion thus fostering a weak linkage to the rest of the economy (Stiglitz, 2012).

Thirdly, the frequency oil price volatility of the international commodity market makes the Nigerian economy unstable and vulnerable to acute boom and bust cycles. Empirical evidence has shown that oil prices are twice as volatile as those of other commodities especially since the 1970s and that oil price volatility exerts strong adverse effect on fiscal discipline, public finances and state planning. Volatility also fosters disinvestment, inequality, and poverty due to frequent economic shocks that it exposes oil dependent economies to (Karl, 2004). The ravaging effect of the rent-seeking nature of Nigeria oil exploitation since its discovery and the failure to adequately reinvest oil proceeds into sustainable economic activities with stronger linkages to the rest of the economy such as Manufacturing and agriculture has led to a very low human development (Figure 4.1.B).

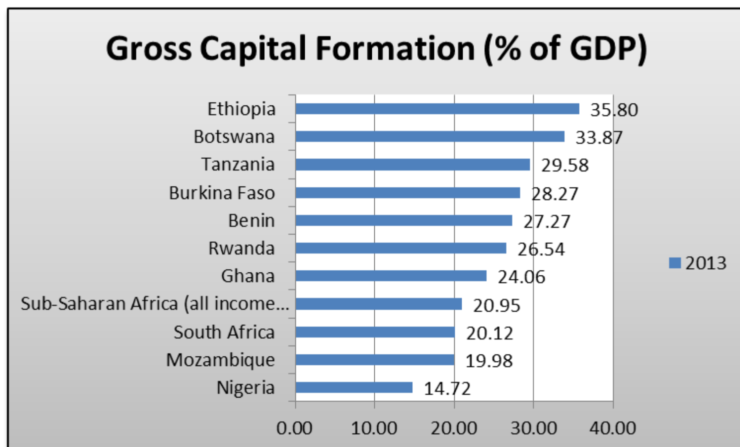
President Muhammadu Buhari of Nigeria for good reasons acknowledged during the 2016 national budget presentation to the parliament that one of the cardinal objectives of the budget is to diversify the economy and weaned it off its overreliance on revenues from a single and volatile commodity such as crude oil and gas.

Figure 4.1A: Trend of Nigerian Government revenue (% of GDP)



Source: Nigerian Bureau of Statistics, 2016.

Figure 4.1B: Gross Capital Formation (% of GDP) of 2013 for selected countries in SSA as well as the regional average.



Source: World Development Indicators, 2015.

4.2 Poor governance, Weak institutions and Corruption

Governance and institutions refers to any form of restraint on human interactions devised by society to maintain law and order (North, 1990). In the absence of effective and efficient institutions, there is bound to be poor governance in the sense that the outcome of human interactions becomes non-optimal. For institutions to be efficient there must be strict enforcement such that violation of rules and codes of behaviour must attract severe sanctions. The impact of weak state institutions on the economy can be seen through the absence of guarantee on property and contract rights as well as poor administrative capacity plagued with rent-seeking civil service. When property and contract rights are not well defined or properly enforced there is bound to be disequilibrium in the market giving rise to unemployment or stagnation in the economy (Chowdhury, 1999).

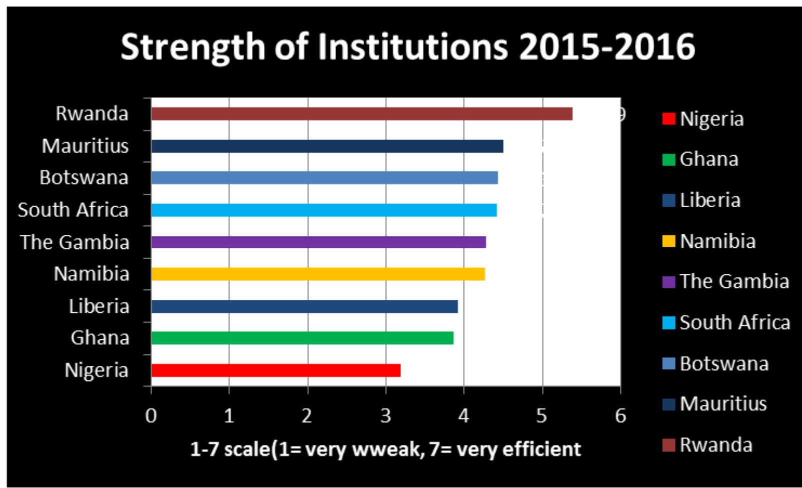
Ineffective and inefficient governance as well as weak state institutions is perhaps the major factor responsible for the scale of underdevelopment in Nigeria (Figure 4.2A). In fact many believe that it is the only problem with Nigeria. A quote from the famous late Nigerian novelist Chinua Achebe summed it all- “the trouble with Nigeria is simply and squarely a failure of leadership. There is nothing wrong with the Nigerian land or climate or water or air or anything else. The Nigerian

problem is the unwillingness or inability of its leaders to rise to their responsibility, to the challenge of personal example which is the hallmarks of true leadership".

The biggest manifestation of bad governance and weak institutions in Nigeria is official public corruption. There are many who believe that corruption is singularly the most important developmental challenge facing Nigeria today. This can hardly be faulted given the widespread nature of bureaucratic corruption in Nigeria where nearly 50% of the population has had to pay bribes to government officials in one time or another in return for public services (Figure 4.2B). Several empirical studies have detailed the adverse effects of corruption on almost every facet of the Nigerian society amidst socioeconomic implications. Some of these studies include the negative correlation between corruption and GDP growth (Gyimah-Brempong, 2002), the impact of corruption on poverty and inequality (Canagarajah and Thomas, 2001; Sala-I-Martin and Subramanian, 2003), the link between corruption and conflicts (Adebayo, 2014), corruption and underdevelopment (Agbiboa, 2012).

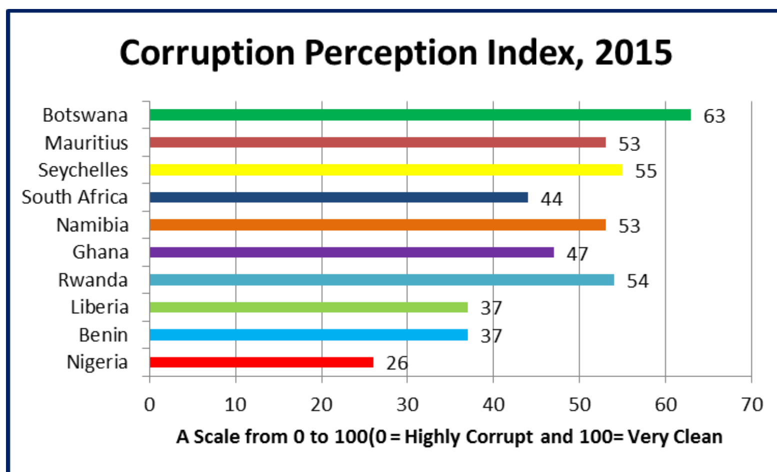
Some literature (Karl, 2004; Ojukwu and Shopeju, 2010) have attributed this poor governance and weak institutions to the resource curse via the transmission channel of deteriorating institutional framework. The argument is that the oil windfalls that accrue to oil exporting countries undermine the development of institutional framework by weakening state agencies administrative capacities. Another strand of this argument is that the members of Nigerian elite class who are benefiting from the weak institutional governance system by systematically plundering the oil rents continue to subvert the system so as to protect themselves. Huge amounts of oil revenue frequently go missing almost on a yearly basis. In 2013, it was reported that $6.8 billion dollars was stolen from a government programme meant to subsidise fuel for the masses in three years. Shady deals between public officials and refined-oil importing companies have gulped an estimated $29 billion dollars in the past decade. Yet more than half the population live in abject poverty and have little or no access to electricity due to collapse in the national grid. Moderate estimates suggest that at least $4 billion -8 billion is stolen every year, money that could be used to provide vital healthcare and education to the rural poor who are mostly worse off (Ojukwu and Shopeju, 2010; Agbiboa, 2012 The Economist, 2013, March 2nd).

Figure 4.2A: Benchmarking the strength of Nigeria's Institutions against the top performers in Sub-Saharan Africa for 2015-2016.



Source: World Economic Forum, 2015.

Figure 4.2B Perception of Corruption for selected Countries in Sub-Saharan Africa



Source: Transparency International, 2015.

4.3 Unemployment, Poverty and Inequality

No society can flourish and be happy, if a greater percentage of its population are poor and miserable. This statement attributed to Adams Smith in his 1776's inquiry into the wealth of Nations is as apt today as it was then. Perhaps, there is no better place to view the socioeconomic consequences of poverty and human deprivation in society at large than Nigeria (Figure 4.3A & B). Rising unemployment, poverty and inequality continues to take dangerous dimensions and threaten the corporate existence of the country.

Although Nigeria witnessed impressive growth rates above 5 % over the last decade, this growth has been no more than a 'jobless growth' or what is sometimes referred to as 'growth without

development' as extreme poverty continues to rise in spite of consistent economic growth. In 2010, Poverty rose by 3.5% below the national poverty line from 65.5% in 1996 to 69%. The Gini-coefficient as well as share of household consumption which are measures of inequality also deteriorated during the period as there was an increased from 0.43 in 2004 to 0.49 in 2014 and growth in consumption by the poorest 10% of the population fell by 12 per cent, while consumption by the richest rose by 18 per cent (Figure 4.3C). At the geopolitical level, inequality is even more visible. The 2010 Nigerian Poverty Profile estimated that about 70.4% of people in North-West were living on less than a dollar a day, whereas 69.1% in North-East, 59.7% in North Central , 59.2% in the South-East, 56.1% in South-South and 50.1% for the South-West (AfDB, OECD and UNDP, 2015).

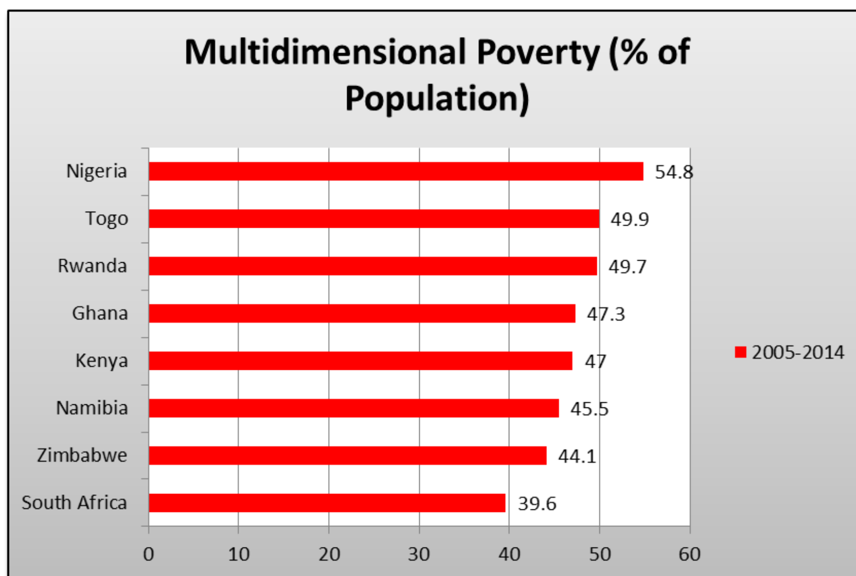
Nigeria's unemployment rate is one of the highest in the world ranking 171 out of 187 countries in terms of employment opportunities. According to official estimates unemployment situation in the country is deteriorating especially amongst the youth between the ages of 15-24 years which recorded 38% unemployment rate while the national average also worsened, rising up to 24% in 2011 from a low 21% in 2010. The national government has even acknowledged that the large youth unemployment in particular to be among the major causes of violence and insecurity in the country. In Northern Nigeria, extreme poverty and unemployment has led a lot of youth into religious terrorism and conflicts rendering an already bad situation intractable thereby perpetuating the regional inequality. Similarly, unemployment and social deprivation has led to high levels of oil bunkering and pipeline vandalism in the Niger Delta region.

According to the 2014 United Nations Development Human Development report, Nigeria is a low human development country due to its lack of inclusive growth ranking 12 places below its wealth category at 152 out of 187 countries with a score of 0.504 that is below the Sub Saharan African average score of 0.518. The low level of human development in Nigeria is at a crisis point and in dire need of intervention.

This little or no investment in human development in Nigeria over the years is not totally unconnected to the perennial problem of oil induced corruption. Oil dependence undermines and crowds out investments from other high impact job creating sectors by rendering them non-competitive. This in turn reinforces poverty and inequality. The agricultural sector, in which the vast majority of the population earn a living, was relegated as the fledging manufacturing sector which had the capacity to structurally transform the economy from exporting only primary commodities to processed valued-added industrial products thus creating modern urban jobs for the population. Worse still, the Nigerian government failed to reinvest those huge inflows from oil revenue into productive investments neither did they made any effort to carry out any form of equitable income distribution thus creating a situation of rising poverty and inequality that only became worse and evident during downturns.

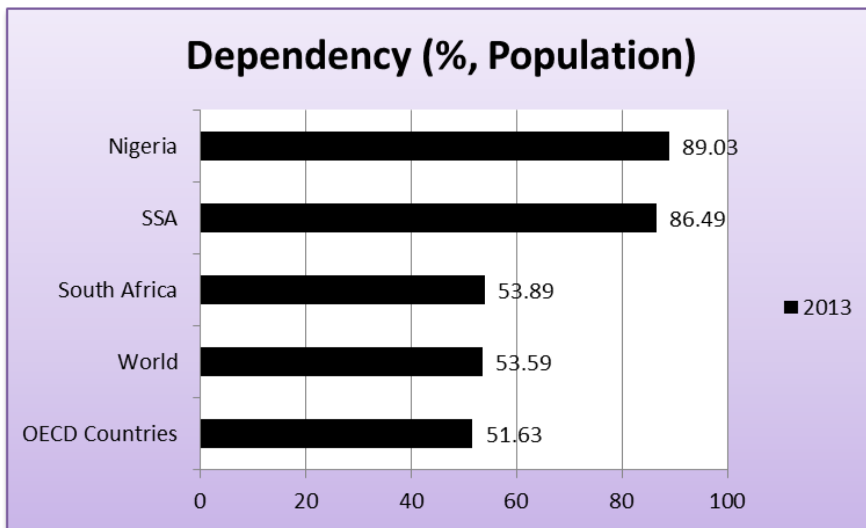
The weak linkage between the oil sector and the broad economy is also another reason for the low human development in Nigeria. In advanced oil exporting economies such as Norway, the growth of the petroleum sector tends to boost the output of the rest of the economy. In Nigeria, such effects are either weaker or non-existent. This explains a phenomenon whereby oil exports propelled real GDP growth rate of over 5% per year continues to have positive relationship with growth in unemployment instead of a negative relationship as unemployment skyrocketed from 15 per cent in 2005 to 25 per cent in 2011, and youth unemployment rates as high as 60 per cent according to some estimates.

Figure 4.3A: Multidimensional Poverty score for selected countries in SubSaharan Africa



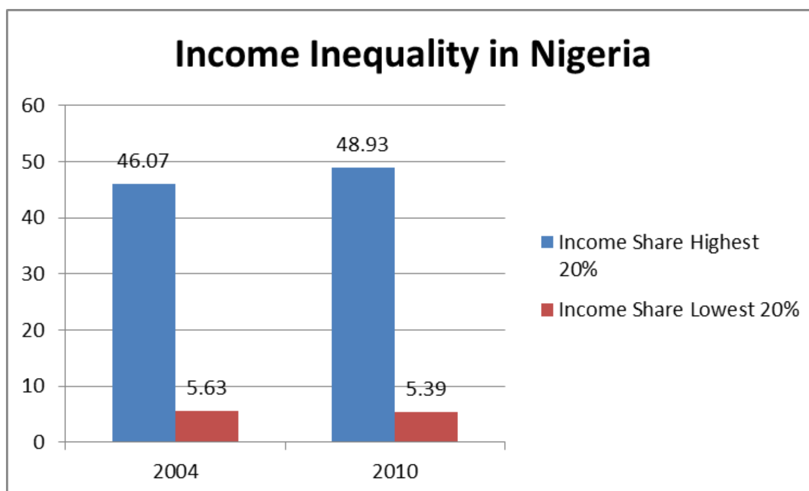
Source: UNDP Human Development Report, 2015.

Figure 4.3B: Percentage of population dependency against regional and global averages including South Africa



Source: World Development Indicator, 2015

Figure 4.3C: Showing Rising income inequality over time in Nigeria



Source: World Development Indicators, 2015.

4.4 Huge infrastructural deficit

Over the past decade, Nigerian economy has been growing at an annual rate of 5 per cent but electricity consumption capita has stagnated (Figure 4.4C). Nigeria suffers from a chronic case of

infrastructure decay with over 93 million of her population living in absolute darkness due to bad policy choices and poor governance issues. Vast amounts of public resources meant to improve the citizen's access to electricity often end up in foreign bank accounts of public officials. Empirical evidence has shown that good governance and policy choices more than national income are key determinants of effective provision of infrastructure. For example, consider Vietnam with lower levels of average income than Nigeria yet has almost achieved its target on universal rural electrification while Nigeria with higher levels of income have more than 60 per cent its population living in the rural areas with no access to electricity (World Development Indicators, 2015).

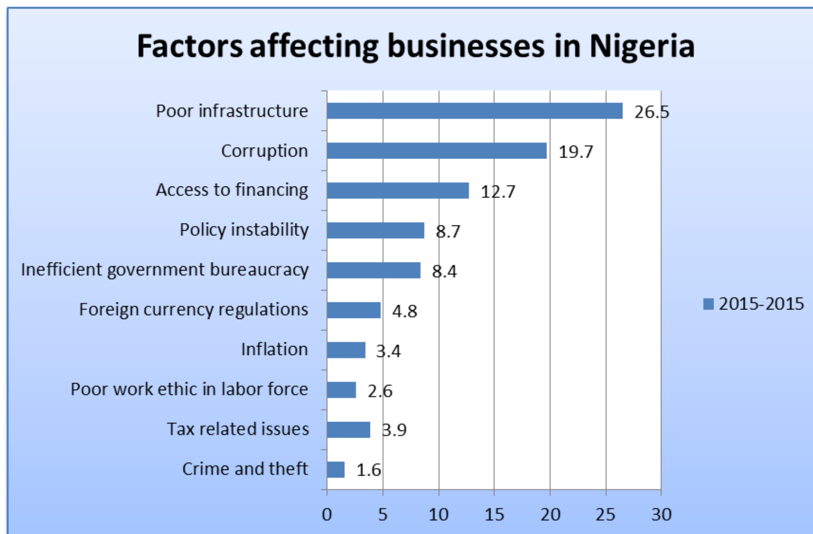
The gap in electricity access and consumption per capita between Nigeria and the other developing economies is even more shocking. For instance, benchmarking the electricity generation of Nigeria and that of Vietnam and South Africa respectively reveals a very alarming gap. The population of Nigeria is more than double that of Vietnam but struggles to generate less than one-quarter of the total electricity that Vietnam generates. Similarly, despite the fact that the population of South Africa is only one-third of the population of Nigeria, South Africa's per capita energy consumption is nine times more than Nigeria's. In another benchmark, we compare Nigeria versus India; While Nigeria has consistently outperformed India in terms of GDP growth in the last decade, India continues to maintain a significantly higher electricity consumption per capita (Africa Progress Report, 2015). Nigeria also suffers acutely from infrastructural deficit in other forms of energy as well as in the transportation sector and water supply, etc. Close to 50% of the population still cook with firewood due lack or epileptic supply of electricity. Privately drilled boreholes are the largest source of safe drinking water in Nigeria (National Bureau of Statistics-General Household Survey, 2013).

The lack of a stable access to electricity has a taken a debilitating toll on the Nigerian economy in several ways chief amongst which include the drop in the national capacity to generate wealth and employment in the country due to erratic power supply. The additional cost of providing a back-up electricity generating plant increases the cost of production thereby reducing the competitiveness and employment. According to George and Oseni (2012), the erratic and often inaccessible supply of electricity in Nigeria has often been one of the major factors influencing multinational corporations' decision to relocate production sites to other countries. Frequent power outage can affect output levels thus reducing manufacturing firm productivity especially for Small Median Enterprises that cannot afford self-provision of electricity (Figure 4.4A).

Over years, successive governments have neglected the infrastructural sector of the economy. From 2012 through to 2015, National budget allocation to infrastructure was less than 1% which also constituted only 1% of GDP (Figure 4.4B) as against the recommended 5-6% of GDP by development practitioners. The current government recognizing the huge infrastructural gap has

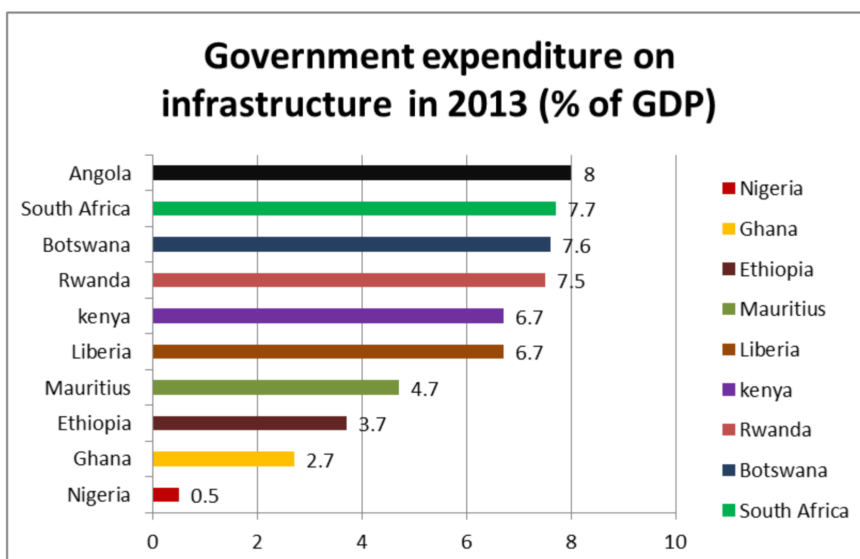
proposed an ambitious 23% increase in its infrastructure expenditure from the previous year (Nigeria National Budget, 2016).

Figure 4.4A: Shows weighted responses from Nigeria Enterprise survey on factors affecting business operations in Nigeria between the periods of 2015-2016.



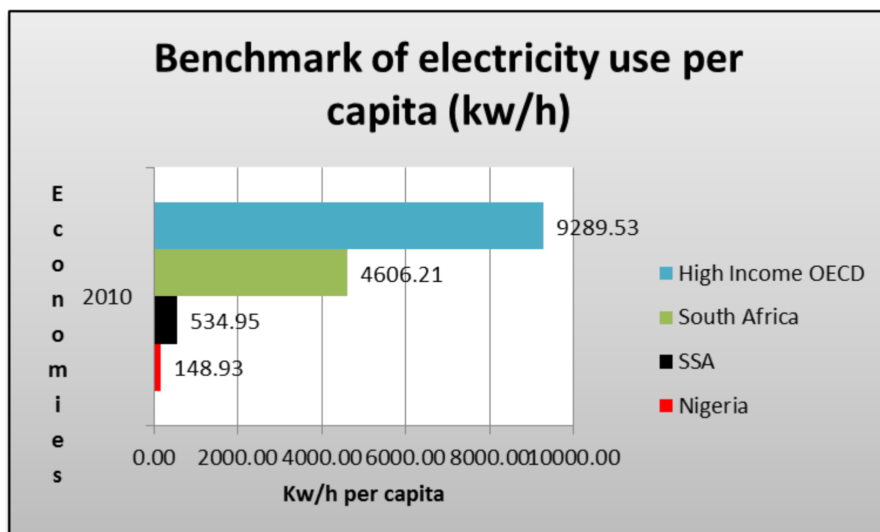
Source: World Economic Forum Global Competitiveness Index, 2015.

Figure 4.4B: Government expenditure on infrastructure to GDP in Sub-Saharan Africa.



Source: World Bank, 2015

Figure 4.4C: Benchmarking electricity use per capita



Source: World Development Indicators, 2015.

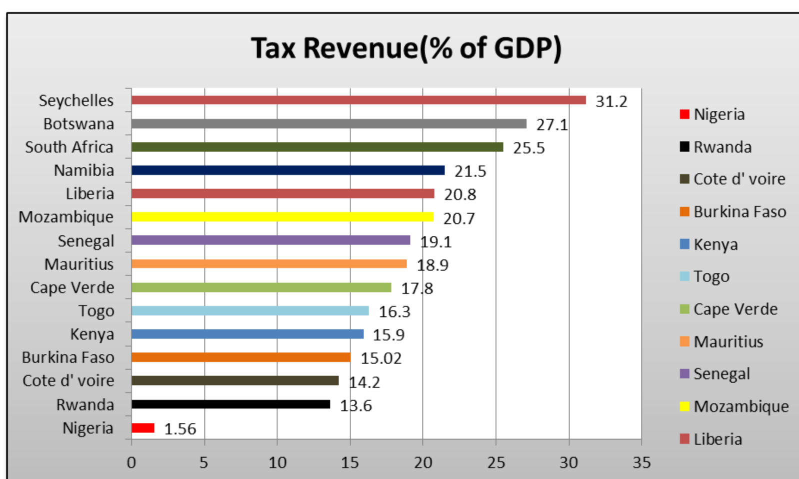
4.5. Large informal sector and low tax base

Nigeria has one of the lowest tax revenue to GDP ratios in Sub-Saharan Africa accounting to a meagre 1.5% in 2012 (Figure 4.5) compared that with Botswana's 27.1%, South Africa's 25.5% and the regional average of 13.83% (World Development Indicators, 2015).A number factor have been advanced as being responsible for this sorry state. The sudden inflow of dollar-denominated revenues from oil exports gave the Nigerian government little incentive to develop any non-oil sources of wealth or even to raise revenues through taxation. This consequently creates a situation of mutual dependence where the citizens being largely untaxed develop little or no incentive to hold government accountable (Sala-i-Martin and Subramanian, 2003; Karl, 2004). Another possible explanation will be that because Nigeria operates a dual economy with small modern sector and a relatively larger informal sector of the economy. Such a dualistic economy will have huge tax implication for the economy in a sense that a large part of the population is engaged in shadow economy and thus denying government vital tax revenues. A third argument which also seems plausible is that due the weak and corrupt bureaucratic institutional framework, public officials often collude with private businesses and divert tax revenues for their own private gains thus depriving the country of stable fiscal revenue.

The plethora of tax incentives and wavers often granted by government to businesses in order to attract investment is also another reason for the low tax base in the economy. Considering the large number of tax incentives and exemptions generously on offer in order to attract foreign direct investment in spite of ample empirical evidence suggesting that tax incentives are a necessary but

not sufficient a condition in attracting foreign investments but rather stable economic and political environment, a highly-skilled human capital, good infrastructure and a dependable rule of law. These ill-advised tax breaks are eroding the tax base and thus depriving the government precious little tax revenue. According to Action-Aid Nigeria country Director Dr. Hossain Abdul, it is estimated that between 1999- 2012, Nigeria lost almost $6.3 billion (averaging $448 million annually) on import and export duty waivers.

Figure 4.5: Tax revenue as percentage of GDP for selected countries in Sub-Saharan Africa for the year 2012



Source: World Development Indicators, 2015.

4 THE IMPACT OF OIL DEPENDENCY ON THE STRUCTURE OF THE NIGERIAN ECONOMY

The impact oil dependence on the structure of the Nigerian economy is overwhelmingly obvious as the oil sector has an overbearing influence on the economy. The economy experiences spells of growth in times of oil commodity boom and contracts in times of oil price shocks (Sala-I-Martin and Subramanian, 2003). Until recently, the oil sector has been the largest contributor to the national

output and the largest source of government revenue displacing the agriculture which was the central pillar of the Nigerian economy at the time of independence in 1960. Though the contribution of the oil and gas sector to the national output has been experiencing a steady decline, the sector still remains the largest export and source of revenue to the country.

The Nigerian economy is also characterised by large-scale subsidies due to the huge influence of oil generated revenue thus making government expenditure very large and unsustainable as is typical of many oil exporting countries. This subsidized economy with a lot of price controls creates inefficiencies in the economy by making many business activities uncompetitive and thus crowding out investments in the private sector (Karl, 2004).

Considering that the oil industry is capital-intensive and often require the employment of the expatriates, this means that the means of production in the sector with the most overbearing influence on the economy is exclusively controlled by foreign oil companies thereby limiting the level of local participation in a sector critical to the economy (Sachs and Warner, 2001).

Evidence abounds of the socioeconomic consequence of this nature of oil-led economic dependence which often results in high unemployment, poverty as well as rising inequality in many developing countries. For instance, Sala-I-Martin et al (2003) found that Nigeria's per capita GDP between 1965 and 2000 remained stagnant at $245 even though oil revenues per capita had increased from $33 to $345 between the same period amounting to $350 billion in oil revenues accruing to the government with little or no impact on the standard of living of the vast majority of population. Furthermore, poor governance and weak institutions are hallmark of oil dependent developing economies. Similarly, the oil curse is also not unconnected to the low tax base in the economy. The frequent inflow of large amounts of revenue into the economy from oil exports has disincentivized the government to raise tax revenue as well as diversifying the economy (Karl, 2004; Sala-I-Martin and Subramanian, 2003).

5 THE CONSEQUENCES AND RISK OF THESE CHALLENGES TO THE NIGERIAN ECONOMY

The consequences for maintain the present structure of economy that is undiversified and dependent on a commodity as volatile as oil is that Nigeria will continue to be plagued by the resource curse with all its ingredients. The effect of oil windfalls on the currency and its concomitant effect of rendering other sectors non-competitive is just one of the inherent risks in continuing on this path (Canagarah and Thomas, 2001).

Secondly the frequent fluctuations in the oil commodity and the capital flight that comes with it as portfolio investors pulled out their capital in times of downturn as well as the contracting effect and

instability on government revenues is another risk associated with being an oil dependent economy (Stiglitz, 2012).

Thirdly, the destructive effect of oil windfalls on the institutional quality is perhaps the most debilitating considering the primacy of institutions over other factors. Oil windfall allows public officials to have unrestricted access to slush funds thus creating an atmosphere of rent-seeking amongst state agencies of restraint (Sala-i-Martin and Subramanian, 2003).

Fourthly, another consequential risk that Nigeria is faced with due to the undiversified and oil dependent economy that it operates is raising unemployment amongst the youth. Considering that the oil mining and exploration industry is more of a capital intensive rather than a labour intensive industry and therefore cannot help in absorbing a significant percent of the population as compared to the agricultural and the manufacturing sector. Apart from the fact that the oil industry absorbs a very low percent of job per unit of capital employed, it mostly seeks high expatriate-skills as well as the very limited opportunities for technology diffusion thus fostering a weak linkage to the rest of the economy (Stiligtz, 2012).

Last but not least, growing conflicts and political instability and high crime rates are perhaps the strongest risk patterns that is emanating from the current economic system that Nigeria is operating. Even the national government has acknowledged the inherent risk in allowing poverty and high unemployment to fester amongst a large population of the youth and has attributed the rising wave of violence and insecurity in the country to youth unemployment. This risk is already manifesting in high incidence of terrorism in Northern Nigeria, kidnapping and militancy in the Southern Nigeria (Adebayo, 2014).

6 CONCLUSION

The current oil dependent nature of the Nigerian economy is absolutely unsustainable and favours only a few elites while the vast majority of the population languish in poverty. The myriad of problems facing Nigeria suggest Nigeria is practically at a crisis point and must adapt and find ways to foster inclusive growth as well strengthen the institutional framework in the country or implode like Somalia. Oil is at the heart of every development challenge in Nigeria; it has fuelled corruption, conflicts and institutional deterioration.

7 POLICY IMPLICATIONS

There is an urgent need for institutional reforms in Nigeria in order to strengthen the administrative capacity of the country civil bureaucracy from its present regime of parasitic and opportunistic plundering of state resources to an effective and efficient bureaucratic system where the rules of the game are well defined and enforced by an independent judiciary. This is perhaps the most important recommendation, given that without this particular reform government policies and

programmes will never achieve full optimality due to pervasive rent-seeking in the Nigerian public bureaucracy.

A set of targeted antipoverty interventions designed to directly improve the well-being of poor communities that takes into account the multidimensional nature of poverty by providing healthcare, education, microfinance and agricultural development programmes that can empower households in the community with special focus given to women and children.

The Nigerian government must proactively pursue policies that strengthen the weak linkages between the oil industry and the rest of the economy by reinvesting oil proceeds strategically to promote structural transformation of the economy especially focusing on sectors that have higher-job-creating impact such as agriculture, manufacturing and trade thereby diversifying the economy away from its perpetual state of oil dependence. Concerted efforts must be made by the government to ensure equitable distribution of oil revenue across society by providing basic services as well as improving the dilapidated infrastructure in the country in order to foster inclusive growth.

Government must also as a matter of urgency must design and pursue social inclusive programmes to mitigate the high incidence poverty, unemployment and rising inequality in the society. Considering that the most recent General Household Survey in Nigeria indicated that a vast majority of population are either employed in smallholder farming and petty trading, government should revive and strengthen the Agricultural Credit Guarantee Scheme as well as the Small and Median Enterprises Development Agency of Nigeria to provide soft loans and support to the many living at the fringe of society thereby boosting national productivity.

The Nigerian government must also as a matter of priority embark on structural transformation reforms of the economy that will create new and more productive jobs for the bulging youth population by moving a higher proportion of labour and resources from the present traditional low-productivity subsistence agriculture and petty trading areas to high-productivity sectors by stimulating and broadening the manufacturing base by attracting greenfield foreign direct investment (FDI) in the manufacturing sectors of the economy.

Nigeria is in dire in need of tax reforms that will strengthen the efficiency and capacity of the tax authorities so as to broaden the tax base of the country from its current less than 5% of GDP to at least the regional average of 15%. Another important component of this tax reform should overhaul the current massive and often shady tax incentives and wavers system that is draining government of much needed revenue for infrastructural development. The government must also consider increasing its Value Added Tax rate from a meagre 5% which is effectively one of the lowest in the world.

A combination of legislation and enforcement of progressive taxation on income, asset and wealth of the top 20% who control over 58% of the national income as well as direct transfer payments and expanded social spending on the poor will address both the rising inequality and create social safety net for the destitute population.

8 REFERENCES

Achebe, C., 1983. The problem with Nigeria. *Enugu: Forth Dimension Publishers*.

Adebayo, A.A., 2014. Implications of Boko Haram Terrorism on National Development in Nigeria, *Mediterranean Journal of Social Sciences, vol.5, no.16.*

Agbiboa, D.E., 2012. Between corruption and development: The political economy of state robbery in Nigeria. *Journal of business ethics*, *108*(3), pp.325-345.

Anyanwu, J.C., 1997. The structure of the Nigerian Economy (1960-1997). *Joanee Educational Publishers.*

Auty, R., 2002. Sustaining development in mineral economies: the resource curse thesis. *Routledge*.

Basedau, M. and Lay, J., 2009. Resource curse or rentier peace? The ambiguous effects of oil wealth and oil dependence on violent conflict. *Journal of Peace Research*, *46*(6), pp.757-776.

Baumol, W.J., 1967. Macroeconomics of unbalanced growth: the anatomy of urban crisis. *The American economic review*, pp.415-426.

Canagarajah, S. and Thomas, S., 2001. Poverty in a wealthy economy: the case of Nigeria. *Journal of African Economies*, *10*(2), pp.143-173.

Chenery, H.B. and Taylor, L., 1968. Development patterns: among countries and over time. *The Review of Economics and Statistics*, pp.391-416.

Chowdhury, A., 1999. Political economy of macroeconomic management: The need for institutional change. *International Journal of Social Economics*,*26*(1/2/3), pp.389-401.

FAO., 2012.'FAO Investment Policy Support: Foreign Agricultural Investment Profile, Nigeria', *Rome.*

FRN. 2016. Overview of the 2016 budget proposals; Budget of change, Muhammadu Buhari available at www.budgit.com.

George, E.O. and Oseni, J.E., 2012. The relationship between electricity power and unemployment rates in Nigeria. *Australian Journal of Business and Management Research*, *2*(2), p.10.

Gyimah-Brempong, K., 2002. Corruption, economic growth, and income inequality in Africa." *Economics of Governance* 3, no. 3: 183-209.

Karl, T.L., 2005. Understanding the Resource Curse; Covering Oil. *Open Society Institute, New York, pp.21-26.*

Lipset, S.M. and Lenz, G.S., 2000. Culture matters: How values shape human progress *.Corruption, culture, and markets. , 112, p.112.*

NBS.2013.'Nigeria's General Household Survey'. Available at www.nbs.ng

North, D.C., 1990. 'Institutions, institutional change and economic performance'. *Cambridge university press*.

OECD., 2015. 'The investment background in Nigeria and overview of main policy recommendations'. *OEECD Investment Policy Reviews*.

Ojukwu, C.C. and Shopeju, J.O., 2010.' Elite corruption and the culture of primitive accumulation in 21st century Nigeria'. *International Journal of Peace and Development Studies*, *1*(2), pp.15-24.

Ross, M.L., 1999. The political economy of the resource curse. *World politics*, *51*(02), pp.297-322

Sachs, J.D. and Warner, A.M., 2001. The curse of natural resources .*European economic review*, *45*(4), pp.827-838.

Stiglitz, J.E., 2012. 'From resource curse to blessing'. *Project Syndicate, August*, *12*.

Sala-i-Martin, X. and Subramanian, M.A., 2003. Addressing the Natural Resource Curse: An Illustration from Nigeria *(No. 3-139). International Monetary Fund.*

UNDP. 2015.'Human Development Report'. Available at http://.hdr.undp.org

World Bank, 2015. World Development Indicators Database, *http://data.worldbank.org/datacatalog/world-development-indicators.*

World Economic Forum 2015. Global Competitiveness Report 2013-2014, Geneva,

www.weforum.org/reports/global-competitiveness-report-2015-2016.