Dynamics of Fiscal Policy on the Growth of Nigeria Economy

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Abstract

The study examined dynamics of fiscal policy on the growth of Nigeria Economy. The objectives were; to examine the effect of government revenue on the growth of Nigerian Economy, to examine the effect of government expenditure on the growth of Nigeria Economy and to ascertain the effect of government borrowing and employment on economic growth in Nigeria. Secondary data was sourced from Central Bank of Nigeria Statistical Bulletin and ordinary least square of multiple regression were used to establish the relationship between dependent and independent variables. The findings revealed that government revenue had no significant effect on gross domestic product. Also shown that there was a significant effect of government expenditure on gross domestic product. It was discovered that government borrowing had a significant effect on gross domestic product and employment had a significant effect on gross domestic product. It was recommended that government should harmonise the tax system and taxes should be spent on productive sector of the economy. The study recommended that efforts should be made to increase the economy because of its direct consequences on fiscal policy.

***Keywords**: Fiscal Policy, Government Revenue, Government Expenditure, Government Borrowing, Employment, Economic Growth*

Introduction

Fiscal policy is one of the policies made by government to regulate the level of spending. Fiscal policy is used to fine-tune and direct the economy to achieve the goals of price stability, which employment policies use in the developing countries like Nigeria. Anyanwu (1993) view it as part of government policy concerning the raising of revenue through taxation and other means and deciding on the level and pattern of expenditure for the purpose of influencing economic activities. Fiscal policy promote and maintain high employment as well as stabilizing the economy. The function of fiscal policy is to alleviate unemployment and enhance economic stability. Also it is generally known as an institutional framework which the government undertakes its fiscal operations in the form of taxation, spending and borrowing the Keynesians posit that fiscal policy exerts greater influence on economic activities. Fiscal policy as a tool for macroeconomic management has been seen as a purposeful use of government revenue and expenditure to manipulate the level of economic activities in a country. The implementation of fiscal policy is essentially routed through government budget. Budget as a fiscal policy is conceived as a structure that balances the changes in government revenue and expenditure over a period of time. The intent of fiscal policy is to stimulate economic and social development by pursuing a policy stance that ensures a sense of balance between taxation, expenditure and borrowing that is consistent with sustainable growth. Fiscal policy has a significant influence on the growth and operation of the economy, it plays prominent roles in the pursuit of macro-economic stabilization in Nigeria. In the context of Nigeria, it deals with taxation, revenues, public borrowing, public expenditure aimed at influencing economic activities on the achievement of certain desirable or macro – economic goals.

Theoretical framework

This study is anchored on John Maynard Keynes (1883 – 1946). He posit that an increased level of government intervention in the economy, especially through budget deficits and fiscal policy is to fine-tune or manage aggregate demand in order to achieve the best policy performance. This theory focuses on the rate of spending in the economy and what determines the level of employement and production of output and income in the economy. Gwartney and Stroup (1982) contended that classical economists from Adam Smith (1723-1790) to the time of Keynes focused their analysis on economic efficiency and production. In other words, classical economics is a synthesis of theories put forth by numerous individuals from Adam Smith's time (the late 1700s) to the early twentieth century. Keynesianism became associated with an increased level of government intervention in the economy, especially through budget deficits and fiscal policy to fine tune or manages aggregate demand in attempt to achieve the best policy performance.

Empirical Literature

Many studies were revealed on fiscal policy on the growth of economy in developed and developing countries. Farner (2009) investigated on the effectiveness of fiscal policy on the growth of Nigeria economy between 2000 – 2015. Secondary source of data was employed in this study. Multiple regression statistical tools were used in the study. The finding showed that fiscal policy positively affected the growth of Nigeria economy. The study recommended that private expenditure should be properly managed in order to restore full employment. Bodunrin (2016) investigated the impact of fiscal and monetary policy on Nigerian economic, growth from 1981 to 2015. Time series data were collected from the central bank of Nigeria (CBN). A vector autoregressive model (VAR) was applied. The VAR model revealed that fiscal policy distorted real GDP but died out after one year, while monetary policy had no significant impact on real GDP while the impact of recurrent expenditure was insignificant. The study recommended that fiscal policy leadership and harmonization between the fiscal and monetary authority, with emphasis on channeling resources to where they are most needed Adefeso and Mobalayi (2010) investigated on the fiscal-monetary policy and economic growth in Nigeria. Their major objective was to re-estimate and re-examine the relative effectiveness of fiscal and monetary policies on economic growth in Nigeria using annual data from 1970 to 2007. The error connection mechanism and co-integration techniques were used to analyze the data drawn policy inferences. The result showed that the effect of monetary policy is much stronger than fiscal policy. The study recommended that there should be more emphasis and reliance on monetary policy for the purpose of economic stabilization. Olawunmi and Ayinia (2007) examined the contribution of fiscal policy in the achievement of sustainable economic growth in Nigeria using slow growth model estimated with the use of ordinary least square (OLS) method. It was found that fiscal policy has not been effective in the area of promoting sustainable economic growth in Nigeria. They however, stated that factors such as wasteful spending, poor policy implementation policy evident in Nigeria, which are indeed capable of hampering the effectiveness of fiscal policy have made it impossible to come up with such a conclusion. Ogbole, Amadi and Essi (2011) assessed fiscal policy and its impact on economic growth in Nigeria (1970-2006). The study involves comparative analysis of the impact of fiscal policy on economic growth in Nigeria during regulation and deregulation periods. Econometric analysis was adopted, results revealed that there is a difference in fiscal policy in stimulating economic growth during and after regulation period. Adeoye (2006) analyzed the impact of fiscal policy on economic growth in Nigeria in 1970 to 2002. The finding shows that public investment negatively affects output growth implying that public expenditure has a crowding out effect on private investment.

Literature review

Fiscal policy is one of the measures by which government adjusts its level of spending in order to influence a nation's economy. Government uses fiscal and monetary policies in order to influence money supply in a nation such as Nigeria. According to Reem (2009), fiscal policy is used along with monetary policy in different combination to direct a country's goal. He further stated that governments can influence macroeconomic productivity levels by increasing or decreasing tax levels and public spending. Fiscal policy describes changes to government spending and revenue behavior in an effort to influence the economy. However, expansionary fiscal policy can result in raising interest rate, growing trade deficits, and accelerating inflation particularly if applied during healthy economic expansions. Fiscal policy is a sister strategy to monetary policy through which a central bank influences a nation's money supply. It is a policy that maintains the condition of full employment, economic stability and to stabilize the rate of growth. For an underdeveloped economy, the main purpose of this policy is to accelerate the rate of capital formation and investment.

Fiscal policy is an important tool for managing the economy because of its ability to affect the total amount of output produced, that is, gross domestic product. The first effect it does is to raise the demand for goods and services. The tools of fiscal policy are taxes and spending. Taxes influence the economy by determining how much money government has to spend in certain areas and how much money individuals should spend. For the developing countries like Nigeria, the usefulness of fiscal policy is to quicken the rate of capital formation and investments for the goals of development and growth. It is very effective during recession where monetary policy is insufficient to boost demand. For example, if the government pursue expansionary fiscal policy, but interest rates rise and the global economy is in a recession, it may be insufficient to boost demand.

Research methodology

The focus of this study has been and fiscal policy on the economic growth of Nigeria. In this study, the exploratory design is employed to identify the factors that contribute to fiscal policy on the economic growth of Nigeria. Based on the objectives of the study, secondary sources are employed in this research. In analysing the data generated for this work. Multiple regression model was employed to establish the relationship between dependent variable and independent variables. The study employed ordinary least square (OLS) model to statistically analyze the relationship between government revenue, government expenditure, borrowing, employment and economic growth using GDP as a proxy. Based on this, the model below has been developed for the study.

GDP = F(GOVERV, GOVEXP, GOVB, EMP)

Where:

GOVERV = Government revenue
GOVEXP, = Government expenditure
GOVB = Government borrowing
UEMP = Employment

Therefore, the functional relationship is linearized into ordinary least square (OLS) model.

$GDP = b_o + b_1\ GOVREV + b_2GOVEXP + b_3GOVB + b_T\ EMP + e$

Where:

Dependent variable = GDP
Independent variable = GOVREV, GOVEXP, GOVB,EMP
Regression constant = b_o
Regression parameters = $b_1 – b_4$
Stochastic error term = e

Analysis of data

The regression results of fiscal policy on Nigeria economy is presented and analysis below. The estimation technique used as the ordinary square (OLS) methods.

Presentation of result

LGDP = -0.631441 + 0.322118 + 0.279075 + 0.578713 + 3.456

The coefficient of multiple determination (R^2) is 0.988884 and an adjusted R^2 of 0.987255. The later indicates that 99% of variations in the observed behaviour of GDP is jointly explained by the independent variables namely: GOVREV, GOVEXP, BOR and EMP. This shows that the model fits the data well and has a tight fits. Also, the f-statistic is used to test for the significant of such good or tight fit. The model reports that high f-statistic value of 620.7068 is greater when compared with the table value.

TABLE 1

Dependent variable: LGDP

Variable	Coefficient	Std.error	t-stat	Prob
C	-0.631441	0.569086	-1.109571	0.2797
LGOVREV	0.322118	0.241727	1.332570	0.1970
LGOVEXP	0.279075	0.145656	1.915980	0.0691
LBOR	0.578713	0.206180	2.806834	0.0106
LEMP	3.456777	2.748494	1.257698	0.0000

Source: Contingency table extracted from Appendix

R^2 = 0.98848 R^2(adj) = 0.9877255

F-stat = 620.7068

DW = 1.386156

Using this criterion, therefore government expenditure is significant at 5 percent level specially, a 1 percent increase in GOVEXP (0.27%), BOR (0.57%) and GOVREV (0.32%), EMP(3.45) will prop up the economy. The DW statistical (1.386) is used to test for the serial correlation in the residuals of the model. The calculated DW is 1.386. The decision rule is that if the calculated Dw falls outside du and 4-du (1.66 and 2.34) then there is a serial correlation in the residuals. This shows that our calculated Dw = 1.386 falls outside and this indicates that the estimates should be taken with caution. The goodness of fit of the models indicated by the adjusted R – square shows as good fit of the model that the model fits the data well, the total variation in the observed behaviour of gross domestic product (GDP), used as a measure of economic growth, is jointly explained by variation in government revenue, government expenditure and borrowing. For the overall significance of the model, the ANOVA on the F-statistic is used. To test for the individual statistical significance of the parameter, the t-statistic of the respective variables were considered. Considering their probability values, computer software shows the constant term is negative while independent variables are statistically significant (GOVEXP, BOR, EMP). The a prior expectations about the signs of the parameter estimates are confirmation to economic theory.

Summary of findings

Based on the analysis of the study, the research work is carried out to assess fiscal policy on the Nigeria economy. In order to validate the work, theoretical and empirical literature relevant to study were reviewed. The findings of the study include that: Government revenue had a positive impact on Nigeria economy and it was statistically insignificant. Government expenditure had a positive and was statistically significant. It therefore means that funds government spend on defence, health etc contributed positively to the performance of Nigeria economy. Government borrowing and employment had a positive and statistically effect on the growth of Nigeria economy.. There were factors that affected the performance of Nigeria economy. Based on the result, it was shown that these variables were statistically significant on the performance of the economy as well as unemployment

Conclusion/Recommendations

Fiscal policy deals with the manipulation of government expenditure, government revenue and borrowing with a view to influence macroeconomic variable such as gross domestic product toward a desired direction. It deals with the aggregate effect of government expenditure and taxation on income, production, employment and other economic activities. The following recommendations are made;

1. Government should harmonize the tax system and money realized from taxes should be spent on productive sector of the economy.
2. Agencies responsible for implementation of fiscal policy measures should be given necessary support and free hand in the discharge of their duty to improve efficiency.
3. Government should implement effective policies on how to generate revenue in order to enhance the growth of the Nigeria economy
4. Government should control funds that are allocated to other sectors of the economy in order to minimize misappropriation of funds and misplacement of capital flight

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