Cost of Governance and Deficit Financing in Nigeria: An Application of Auto Regression Distributive Lag (ARDL) Model

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Abstract
This study examined the effect of cost of governance on deficit financing in Nigeria using the Auto Regression Distributive Lag (ARDL). Deficit financing was modeled as the function of Cost of general administration, cost of defence, cost of internal security and cost on national assembly. The study found that cost of general administration added 4.3 percent, cost of internal security added 7.8 percent, cost of defence added 2.1 percent while cost of national assembly added 22.2 percent at lag 1. From the above, the study concludes that cost of national assembly added the largest to deficit financing in Nigeria. The study recommends policies to reduce the cost of governance in order to manage the increasing rate of deficit financing in Nigeria.

Keywords: *Cost of Governance, Deficit Financing, Auto Regression Distributive Lag (ARDL), Cost On National Assembly, Cost of Internal Security, Cost of Defence, Cost of General Administration.*

INTRODUCTION

The history of Nigeria's deficit financing can be traced to 1961; the policy was justified during the post-independence era, largely because of the need to expand the economy then. From 1970, the country adopted the budgetary deficit policy because of huge public sector spending war reconstructions, wasteful spending, and mismanagement of the oil boom in the 1970's till the 1980's. From 1982, there was a decline in crude oil export earnings, this reduced the national reserves and resulted to heavy borrowing to finance public investments. The fiscal deficit increased public spending, while revenue declined. Thus, leading to deficit financing as a practise in which government spends more money than it receives. According to Collins (2003) the government planned to put more money into the economy than it takes out by taxation, with the expectation that increased business activity will bring enough additional revenue to cover the shortfall, it is also called deficit spending. In other words, it is the government spending in excess of revenues that a budget deficit is incurred which is financed by borrowing. It is known that the current public debt growth is larger than the growth of the economy for most of the developing countries. It is expected that the growing public debt will cause problems in relation to its services. Deficit financing is when government has a budget deficit; it is as result of government total revenue less total expenditure in a year. According to Atanasovki (2004) when government rather than using

tax borrows to finance her public investments. Gaber (2009) noted that deficit financing arises due to budgetary deficit this is when total revenue is less than total expenditure.

The fiscal deficit for 1990, 1995 and 2000 stood at N22.12 million, N1 billion and 103.78 billion respectively, and the corresponding external debt stood at N521 million, N1.37 billion, and N1.48 billion. Also, there was a dramatic increase from N47.38 billion in 2008 to N2.208 trillion in 2016 while external debt rose to N9.76 billion. In 2019, the Nigerian budget deficit stood at N1.92 trillion while external debt grew accordingly to N802.82 billion (Budget Office, 2020). Since there is no consensus in the literature yet about the net impact of deficit financing in developing economies, we need to undertake further studies by extending the period to 2019. Ariyo and Raheem (1990) showed that rising fiscal deficit has been a common characteristic of the Nigerian fiscal system and that there have been no identifiable and justifiable macroeconomics objectives for such. Moreover, Ariyo (1993) reported that fiscal deficit in Nigeria has become unsustainable since 1980 (Fasoranti, 2013). Nigeria's budget deficit dates back to 1961, and appeared justified during the immediate post-independence era, and since then till now, a huge percentage of Nigeria's budget runs on deficit (Nwanna & Nkiruka, 2019). The deficits over the years have been financed through external or internal borrowings thereby resulting in depletion of reserves. The phenomenon of external debts by Nigeria was dated back to 1958, when a loan of $US 28.0 million (N19.9 million) was contracted from the World Bank for railway construction (Ademola, Tajudeen & Adewumi, 2018).

The fiscal situation deteriorated drastically after 1982, as expenditures continually exceeded revenues between 1982 and 1995. By 1983, the Federal budget deficit amounted to 12 percent of GDP and this resulted in excessive borrowing from both domestic and foreign sources (Osinubi & Olaleru, 2006). The country's total debts also rose steadily after 1981, indicating the extent of gross fiscal imprudence by the government. Fiscal imbalances contributed to huge domestic and foreign debts as it was financed by borrowing, gradual depletion of international reserves. Also, by 1983 foreign reserves had declined to about one-sixth of a peak 1980 amount, as well as arrears in external commitments (Oluba, 2008). In 2007, the federal government sought for debt cancellation which led to a drastic reduction of the debt to the tune of about $US 3.4 billion (N427.8 billion) and despite this debt cancellation, Nigeria's debt acquisition has been on the increase since 2007. Furthermore, in 2018, the Nigerian government issued a $2.5 billion Eurobond which resulted in $US22.08 billion debt stock accumulation, with an external debt of N849 billion which later fell to N802.82 billion (Nwanna and Nkiruka, 2019). The culminating effect of the above has been a decline in the growth of GDP, external reserves and accelerated inflation.

Despite the introduction of the private sector led economy in 1986 using the Structural Adjustment Programme (SAP), the government seems to be one of the highest employers of skilled and semi-skilled labour in Nigeria. This and other related scenario have left public authorities both at the national and subnational levels with an ever-increasing administrative cost at the expense of developmental projects (Umaru, 2017). Whereas Nigeria recorded a balanced budget in 1995, followed by a fiscal surplus of N32.05 billion in 1996; the country has continued to run budget

deficits in subsequent years (CBN, 2018). In 2018, over 77.0 per cent of the federal government budget went into recurrent spending (DMO, 2020). While the total government expenditure in 2018 stood at N7.54 trillion, only N1.68 trillion was actually voted for capital expenditure, whereas fiscal deficit for that same year stood at N1.95 trillion (DMO, 2020). Thehuge and persistent annual deficit, has translated into a growing public debt for the country. The desire to achieve sustainable growth may prove difficult if this scenario continues. Economic growth is a quantitative expansion in the gross domestic product over a year, (Todaro & Smith, 2015). The growth rate of national output is one of the key performance indicators used in accessing the health status of an economy. Unfortunately, Nigeria's economic growth outcome in the recent past has been unimpressive. The highest growth rate from 1981 to date is 15.33 percent recorded in 2002 (World Bank, 2019). This figure fell significantly, to 6.44 percent in 2005, and remained around the same up to 2008 (World Bank, 2019). In 2012 however, the GDP growth rates further slumped to 4.23, and later to 2.65 percent in 2015 (World Bank, 2019). A critical look at the above showed that, fiscal deficit were more in the democratic era than the military era and this is associated with increasing cost of governance in the democratic era.

The president, the vice president, the senator present, ministers and other political office holders moves in convoy of at least Five SUV cars of not less than 50 million naira for each. Increasing cost of governance in the democratic region attracted the attention of both National and international institutions and the general public. There are 42 ministers of which 36 are cabinet ministers in direct cabinet responsibility. The Constitution stipulates that the President should appoint a Minister at least from each of the 36 states (El-Rufai, 2012). This implies that there will be at least 36 or 37 federal ministries to manage the affairs of the federal government. In addition, there are unspecific or unlimited number of special advisers and special assistants. It is believed that these categories of officials could be as high as 300. Nigerians have always associated security vote with governors and nursed the belief that it is prone to abuse, as well as, resulting to a duplication of the votes allocated to the security agencies in the budget. It is, however, astonishing to find security vote as an item running through all Ministries, Departments and Agencies (MDAs). More surprisingly, as found by Nzeshi (2012) even agencies whose primary functions revolves around security have security vote allocations in the budget.

Lamido Sanusi noted that Nigeria do not need 109 senators and 360 lower chamber members, he ran into troubled waters when he revealed that the National assembly, NASS alone gulps 26 per cent of their current expenditure in the 2010 appropriation Act. At the inauguration of the seventh Senate, David Mark, the president of the Upper Chamber, promised that the NASS would make laws to support reforms to reduce the cost of governance. When the forum of senators visited Pius Anyim, secretary to the government of the federation, SGF, one of the issues that came up was how to reduce the cost of government. In 2003, during President Obasanjo's administration, a staff audit showed that there were1.2 million federal civil servants, 1.500 political office holders (Ministers, special advisers and special assistants), 470 federal legislators and over 1.500 judicial officers. As part of his cost cutting measures, the Obasanjo administration reduced the number of federal ministries from 22 to16 by merging some of the ministries. Research report supports the observation made by the CBN governor about the high cost of governance. According to the research work of Stephen Ejuvbekpokpo published in the in 2012 entitled "Cost of governance on

economic development in Nigeria found that a unit rise in recurrent administrative expenditure would lead to a 0.52 unit fall in gross domestic product (GDP). Conversely, he found that a unit rise in capital administrative expenditure would cause grass domestic product to fall by0.45 units. Put in another way, if recurrent administrative expenditure rises by 100 percent, GDP will fill fall by 52 percent, just as if the capital administration expenditure surges by 100 percent, GDP will fall by 45 percent. From the above, this study examined the effect of cost of governance on deficit financing in Nigeria.

REVIEW OF RELATED LITERATURE

The Cost of Governance

The cost of governance is the money spends on administrative processes. It is also known as administrative expenditure. Adewole and Osabuohien (2007) decomposed cost of governance into two: recurrent administrative expenses and capital administrative expenses. They defined cost of governance as costs associated with the running of government. In other words, these are costs incurred by the government is running this affairs. The government helps to sustain the social contract that binds every member of the state. Similarly, Fluvian (2006) defined cost of governance as any expenditure in maintaining government administrative structures. He also equates cost of governance to total administrative expenditure, which is a part of total federal government expenditure in Nigeria. He said that the justification for using total administrative expenditure as cost of governance stems from the fact that administrative expenditures are incurred in governing processes. According to Drucker (2007) cost of governance is government budget allocated to both capital and recurrent expenditures on maintaining government administrative structures, which appears to be very enormous in Africa the question of efficiency in governance is, therefore, to ensure that public funds are spent judiciously, while public goods and services are sufficiently provided.

The distribution of public goods and services in Nigeria is based on the principle of equity. Natural and human resources may skew income distribution in favour of endowed groups when the market is allowed to be the principal mechanism for resource allocation. Free markets are, therefore, more likely to be hindered when pronounced disparities exist in the distribution of natural and human capital endowments among groups that exist in a particular society. This mostly explains why the nationalists of northern extraction did not agree at first with the idea of independence in Nigeria, since their limited investment in human capital would put them at a disadvantage in a post - independent Nigeria (Adewole & Osabudien, 2007). Nigeria, therefore, put up a political arrangement that ensured that the commanding heights of the economy were left in the domain of the public sector. With the benefit of hind sight, one could say this arrangement signaled the beginning of patronize activities that stifled the market and productivity, promoted rent seeking, brought an imbalance between efforts and rewards, and raised the cost of governance in Nigeria. Cost of governance, according to Afolugbo (2004), is therefore the cost incurred in running the government. It is the cost of performing political duties, and discharging civil services to the public.

Governance represents more than a means of providing common good, as it can be related to the government capacity to help the citizens' ability to achieve individual satisfaction and material prosperity. Therefore, governance could be compared to the management, supply and delivery of public services to a nation. According to Fluvian (2006), there are specific factors responsible for the rising cost of governance in Africa. First, there is the issue of inflation. Public project costs are unduly inflated by corrupt politicians. There should be equity. Adewole and Osaabwohien (2007) added that the rising cost of governance in Nigeria is a price we have to pay for undue consideration for equity. Similarly, the issue of misuse of public funds is another cause of the rising cost of governance in Nigeria (Warimen, 2007). Political leaders inflate the costs of public projects to embellish themselves. Adewole and Osabuohien (2007) noted that the supply of security beyond the optimal level will lead to limited prosperity. In other words, the excess money spent by government on particular set goods affects development, since resources are scarce and should be optimally utilized. Furthermore, there is population increase. An increase in population implies that there is pressure in the limited available the resources. Fluvian (2006) opined that increase in population implies that more demand for public goods and services, such as education, health services the need to give every ethnic group adequate representation is another reason for increasing cost of governance. Another major cause of the persistent rise in cost of governance in Africa vis-a – vis Nigeria is the extra-large civil service sector. This has been described as an institutional factor by Afolugbo (2004). Most public workers in Africa are redundant due to employment of excessive work staff to reduce unemployment. Employees are more than the optimal size, which led to inefficiency and unnecessary increase in cost.

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According to Iyoha and Oriakhi (2002), a larger than optimal civil service, dominated mainly by that section of the country with significant human capital deficiencies is bound to raise governance costs and institutionalize the mechanisms for rent extraction. This is a major problem in Nigeria. Another institutional factor that raises cost of governance is the provision of security by the state. For instance, a public good like law and order (security for short) has a high degree of public interest, upon which there is a broad consensus that it could be more cheaply provided by government, particularly by a central government, if we admit that in reality there is no pure public good, we should understand why profit maximizing firms could equally provide complementary security services. However, government provides that bulk of security services. Thus, the role of the private sector in the security sector is minimal. We recognize that the different levels of government would be able to organize security effectively (Ejuvbekpokpo, 2012).

According to Adewole and Osabuohien (2007) the absence of the centralization of security affects its efficiency and drives up cost of making security available. This model is drawn mainly from the insights provided by Olsen (1965) and Fates, et al (2002). In conventional economic theory, the state is a product of cooperation. In other words, rational human who live within a defined territory discover a net gain in cooperation rather than in competition. It could be likened to a group of many perfectly competitive firms who form a collusive unit called a monopoly. From a political economy perspective, the state is the by – product of rational individuals who believe that state formation would be better than living as individual or families. The state, therefore, as well as being the government's instrument of operation, is a natural monopoly, for no two organizations with equal powers of force over a defined territory can co-exist successfully and maintain relative peace. Lastly, the state is formed for the benefit of the people. It enables individuals to co-exist peacefully by avoiding violence and reducing tendency for communal and individual clashes.

Fates, et al (2002) added that if people can resist the temptation to steal, or extract rent for selfish reasons, there will be prosperity in the state. However, this is unlike the Nigerian situation. Most politicians are corrupt, selfish and passive. They specialize in looting public treasury. Consequently, pronounced poverty is a key feature of this kind of event. For there to be growth and development, resources must be channeled towards production. The Rising Cost of Governance in Nigeria Governance represents more than a means of providing common good, as it can be related to the government capacity to help the citizen's ability to achieve individual satisfaction and material prosperity. Therefore, governance could be compared to the management,

supply and delivery of public services to a nation. According to Fluvian (2006), there are specific factors responsible for the rising cost of governance in Africa. First, there is the issue of inflation.

Theoretical Review

One discovers three distinct schools of thought; these are Neoclassical, Keynesian, and Ricardian equivalence, each giving distinctive standards. Buderet (1989) gave a brief rundown of the three ideal models. The Neoclassical school considers people arranging, their consumption over their whole life cycle. By moving taxes to future eras, budget deficits increase current consumption by accepting full employment of resources; the neoclassical school contends that expanded consumption implies a decrease in saving. Interest rates must ascent to get balance the capital markets. Higher interest rates, thusly, result in a decrease in private investment. Moreover, there are Keynesian who provides a contention to develop as a result by making reference to the expansionary impacts of budget deficits. They contend that for the most part budget deficits result in an expansion in domestic which makes private investors more idealistic about the future course of the economy coming about them in investing more. This is as the crowd in effect. It is significant here that the conventional Keynesian perspective varies from the standard Neoclassical worldview in two crucial ways. To begin with, it allows the crowd-in effects are unemployed. Second, it presupposes the presence of an extensive number of liquidity compelled people. The second supposition ensures that aggregate consumption is exceptionally sensitive to changes in discretionary income.

Keynesians contend that deficits need not a crowd-out private investment. Webb (1998) is an example of this group, who suggests that increased aggregate demand enhance the profitability of private investments and leads to a higher level of investment at any given rate of interest. Subsequently, deficits may stimulate aggregate saving and investment notwithstanding the way that they raise interest rates. He presumes that the proof is in this manner that deficits have not crowded out investment. There has rather been 'crowding-in". It is important that it is contended that public capital crowds out or crowds-in private capital, contingent upon the relative quality of two contradicting powers: (1) As a substitute production for private capital, public capital tends to crowd out private capital; and (2) By raising the return to private capital, public capital tends to crowd-in private capital. Therefore, on parity, open capital will pack out or jam in private capital, contingent upon whether public capital will crowd-out or crowd-in private capital, depending on whether public and private capital are gross substitutes or gross complements, Furthermore, Webb argues, on the hand, that higher public investment raises the national rate of capital accumulation over the level chosen (in an assumed national manner) by private area specialists; in this way, public capital spending way crowd-out private expenditures on capital goods on an ex-basis as individuals seek to re-build up an ideal inter-temporal allocation of resources. On the other hand, public capital, especially infrastructure capital, for example, parkways, water framework, sewers, and airplane terminal, is liable to endure an integral association with private capital. Subsequently, the higher public investment may raise the marginal productivity of private capital and, in this manner crowd-in private investment.

Keynes evolution provided a framework on how fiscal deficit behavior should be analyzed. His earlier emphasis was on fiscal policy and deficit as components of aggregate demand. From this

viewpoint, the Keynesians found no compelling reason to adjust the financial plan amid times of subsidence. Rather, the thought of the consistently adjusted spending plan, that is, the financial backing ought to be in parity on the arrived at the midpoint of over the business cycle in surplus amid blasts also, in deficit amid subsidence was created as a standard for financial conduct. Taking after the subsidence of the risk of far reaching post bellum unemployment, in any case, the accentuation sparkled from the impact of financial arrangement on total interest to its impact on the parts of interest (Fisher & Easterly, 1990). There is the Ricardian equivalence approach advanced by Barro (1989), who argues "that an increase in budget deficits say due to an increase in government spending, must be paid for either now or later, with the total present value of receipts fixed by the total present value of spending. Subsequently, a cut in today's taxes must be matched by an expansion in future taxes, leaving interest rates, thus private investment, unchanged. This hypothesis, presented by David Ricardo (the acclaimed 40 English established financial analyst), expresses that far-seeing tax - payers will increase their savings in light of the increased government borrowing, and that would keep the interest rates stable. This thought is known as Ricardian equivalence and has been as of late created by the American financial specialist Robert Barro. Macroeconomists Bailey (1983); Carmishael (1982); among others are occupied with the relationship between private investment and public expenditure mainly because of the crowding-out effect of public spending. The crowding out impact reduces the capacity of the government to impact financial movement through fiscal measures.

Turnovsky (1989) argued that in the standard Neoclassical macroeconomic model, the method selected by the government to finance its spending program affects the levels of consumption, investment and net exports. Such models expect that aggregate consumption is higher and national (private in addition to public) saving lower, if a given government spending project is financed by issuing bonds instead of through current tax collection. If resources are fully employed, so that output is fixed, higher current consumption implies an equal and offsetting reduction in other forms of spending. In this way, investment and/or net fares must be complete crowded-out. It is significant that it is critical to recognize financial crowding-out which has been specified before and asset crowding-out which happens when the government contends with the private division on buying certain assets (gifted work, crude materials et cetera). At the point when the government segment grows, the private will contract in light of the expansion in costs of these assets because of an abundance request by the government, thus this prompts a fall in investment and consumption by the private part. Accordingly, the government part's development crowds out the private area. It is significant here too that asset crowding-out is an essential issue to consider particularly in developing nations where assets are rare even infrequently to the private division, so any excess demand for these assets by the government will severely impinge private sector productivity. Furthermore, Webb (1981) asserted that financing the budget deficit by borrowing from 'the public implies an increase in the supply of government bonds. In order to improve the attractiveness of these bonds, the government offers them at a lower price, which leads to higher interest rates. The increase in interest rates discourages the issue of private bonds, private investment, and private spending. In turn, this contributes to the financial crowding-out of the private sector

Some Post-Keynesian economists contend that deficit spending is vital, either to make the money supply (Chartalism) or to fulfill the demand for savings in abundance of what can be fulfilled by

private investment. Cartelists contend that deficit spending is consistently fundamental on the grounds that, in their perspective, fiat money is made by deficit spending: one cannot collect fiat money in taxes before one has issued it and spent it, and the measure of fiat money available for use is precisely the government debt- money spent however not gathered in deficiency spending starts things out. Cartelists argue that nations are fundamentally different from households. Governments in a flat money framework which just have debt in their own particular coin can issue different liabilities, their fiat money, to pay off their interest bearing bond debt. They cannot go bankrupt automatically on the grounds that this fiat money is what is utilized as a part of their economy to settle debt, while family unit liabilities are not all that utilized. This perspective is abridged as But it is difficult to see how the idea of "spending plan busting" applies to an government which as a finance issuer or its own currency, Proceeding in this vein, Chartalists contend that a basic deficit is important for financial development in an extending economy: if the economy develops, the money supply ought to also, which ought to be refined by government deficit spending. Private segment savings are equivalent to government area deficits, to the penny. Without adequate deficit spending, money supply can increment by expanding budgetary influence in the economy, the measure of bank cash develops, while the base money supply stays unaltered or develops at a slower rate, and in this manner the proportion (influence = credit/base) builds which can prompt a credit bubble and a money related emergency. Cartelism is a small minority view in financial matters; while it has had advocates throughout the years, and impacted Keynes, who particularly credited it, it is completely dismisses or overlooked by for all intents and purposes all contemporary standard business analysts. An eminent advocate was Ukrainian American financial expert Abba P. Lerner, who established the school of Neo-Cartelism, and supported deficit spending in his hypothesis of practical account. A contemporary focus or NcoCartelism is the Kansas City School of financial aspect.

Empirical Review

Sanya and Abiola (2015) study the relationship between fiscal deficit and macroeconomic stability (measured by real GDP) in Nigeria using ARDL model and found that fiscal deficit has a negative and significant impact on national output. The paper concluded that deficit financing is a major cause of macroeconomic instability in Nigeria. However, the results of the ARDL model, presented in Sanya and Abiola (2015) suffers from issues of reliability, since the unit root tests conducted indicate that all the variables included in their model were I(2). 26 Central Bank of Nigeria Economic and Financial Review June 2021 in a related study, Ali et al. (2018) examined the impact of deficit financing on economic growth in Nigeria using annual data from 1981 to 2016. Their ARDL analysis indicates that deficit financing (measured by domestic deficit financing) has a negative and significant impact on national output (measured by real GDP). Ezeabasili et al. (2014) examine the relationship between fiscal deficits and national output from 1970 to 2006 and opined that fiscal deficit has a negative impact on economic growth in Nigeria.

Idris and Bakar (2017) evaluated the effect of fiscal operation on macroeconomic growth in Nigeria using descriptive statistical analysis from 1980 to 2015. They argue that the fiscal operation (measured as a persistent budget deficit) has failed to provide an enabling environment for sustainable growth in Nigeria; and thus, recommended a reduction in the budget deficit.

Navaratnam and Mayandy (2016) investigate the impact of fiscal deficit on economic growth in five South Asian countries (Bangladesh, India, Nepal, Pakistan and Sri Lanka) using Johansson Cointegration and vector autoregressive models from 1980 to 2014. They find that fiscal deficit has a negative and significant impact on national output in all the countries except for Nepal where it has a significant positive impact. They further argue that fiscal deficit granger caused national output in Nepal, Pakistan and Bangladesh while the reverse was the case for India and Sri Lanka. They use VAR models on a country-by-country basis instead of adopting a more appropriate technique like fixed or random effect that is capable of bringing out the joint influence of the variables across the countries. Iqbal et al. (2017) examined the relationship between fiscal deficit and economic growth using the ARDL/bound testing approach to test the existence of co-integration on a series of data sets from 1972 to 2014. They argue that fiscal deficit has a negative and significant impact on national output in Pakistan and attributed the relationship to the fiscal deficit/GDP ratio which was far above the threshold level of 5.57 per cent. To reverse this trend, they recommend that the fiscal deficit/GDP ratio should be maintained within threshold level. The analysis was robust, but lacks post estimation tests to further ensure the robustness of the model.

Ojo (2014) examined the impact of deficit financing on economic growth in Nigeria from 1970 to 2010 using VAR model and argues that budget deficit has negative impact on national output. The main shortcoming of the analysis is that Umaru et al.: Budget Deficit and Economic Growth in Nigeria 27 the variables have different orders of integration, thus ARDL approach would have been more appropriate than VAR model. Furthermore, there was no post estimation diagnosis to ascertain the robustness of the results. However, Aero and Ogundipe (2018) used ARDL for a similar study in Nigeria and also suggest that fiscal deficit has a significant negative influence on national output. In contrast to the aforementioned, Oladipo and Ajisafe (2015) investigated the impact of deficit budget on national output from 1980 to 2012 using cointegration technique with a VAR model. They argue that, though budget deficit has been shown to have positive and significant impact on GDP, the impact has not succeeded in reducing poverty in Nigeria, because a large chunk of the deficit is used to finance consumption expenditure rather than the capital project. Although, the variables show no evidence of co-integration, the authors went ahead to estimate the long run relationship, which is not necessary. Umaru and Gatawa (2014) examined the links between fiscal deficit and a disaggregated government spending on national output in Nigeria using data from 1970 to 2011. They argue that total deficits financed spending not only induces real GDP positively but also granger causes national output unidirectionally. Maji and Achegbulu (2012) reported a strong and positive relationship between fiscal deficit and economic growth in Nigeria using ordinary least square (OLS) method of analysis. Similar outcome was also discovered in Pakistan (Goher, 2011). Ojong et al. (2013) in a related study, using data spanning from 1980 to 2008, employ OLS technique and discover that deficit budget has positive and significant impact on national output in Nigeria. However, the methodology applied is questionable because OLS technique is inappropriate for a time series data with the unit root problem associated with the series.

Edame and Okoi (2015) compared the impact of public deficit on economic growth under the Military and democratic system of government in Nigeria using the Chow Endogenous Break Test and conclude that fiscal deficit is growth inducing only under the democratic system. Ubi and Inyang (2018) further substantiated this by carrying out a descriptive appraisal of the impact of prolonged fiscal deficit on macroeconomic variables in Nigeria. Their findings suggest that fiscal deficit affects national output positively. Umeora (2013) scrutinized the link between budget deficit and macroeconomic variables in Nigeria using the OLS technique and discovers that public deficit is positively related to national output. This was further complemented in a study Central Bank of Nigeria Economic and Financial Review June 2021 by Akinola (2017) who also investigated the impact of budget deficit on macroeconomic performance in Nigeria from 1970 to 2013. The OLS result suggests that fiscal deficit is positively and significantly related to economic growth measured by per capita income. Their analysis, however, looks spurious, given that OLS is not suitable for series characterized by stationarity problems.

Buscemi and Yallwe (2012) carried out a panel study on the effect of fiscal deficit on sustainable growth and national savings in emerging economies consisting of China, India and South Africa from 1990-2009. Their analysis using generalised method of moment (GMM) shows that Fiscal deficit has positive effects on national output in the emerging economies. However, the time coverage is, rather, small and no post estimation test was conducted to ascertain the goodness of fit of the model. However, some empirical studies have shown no relationship between fiscal deficit and economic growth. Vuyyuri and Seshaiah (2004) examined the impact of budget deficit on macroeconomic variables in India from 1970 to 2002. Using co-integration technique with VEC model, they argue that fiscal deficit has no impact on national output. Wosowei (2013) in a related research, studied the impact of budget deficit on macroeconomic variables, in Nigeria, from 1980 to 2010, He observed that fiscal deficit has no significant impact on gross domestic product.

Andoni and Osmani (2017) observed the same scenario from 1993 to 2015 in Albania, using ARDL model. In addition, Tan (2006) analyses the relationship between fiscal deficit, inflation and economic growth in Malaysia, from 1966-2003, using Johansen Cointegration with VAR. The study suggests that no long run relationships exist between fiscal deficit and economic growth. Nevertheless, his variables have different orders of integration, suggesting that ARDL would have been more suitable than VAR model. Kesavarajah (2016) examined the growth effect of fiscal deficit for Sri Lanka from 1970 to 2015, using the VAR model and states that fiscal deficit (as a ratio of GDP) has no significant impact on GDP directly. He, however, argues that considering interest rate and GDP relation in Sri Lanka, fiscal deficit may have an adverse effect on GDP indirectly and therefore, recommends a gradual reduction in public deficit to achieve a desirable level of national output. Adam and Bevan (2002) examined the threshold level of fiscal deficit for 45 developing countries, using the bootstrap method. Their analysis put the optimal threshold of fiscal deficit to be about 1.5 per cent of GDP. They however pointed that the sign and magnitude of a unit change in fiscal deficit around the threshold level depend on the government expenditure increase or revenue reduction resulting from the deficit financing. Slimani (2016) examined the threshold of fiscal deficit in 40 developing countries from 1990 to 2012, using Hansen (1997)

method. The findings suggest that a double threshold effect exist for fiscal balances for the countries, and that the optimal threshold of fiscal deficit is 4.8 per cent, while the threshold for fiscal surplus is 3.2 per cent. He, however, added that the sign of relationship between government deficit and national output is determined by the level of aggregate investment in the economy (Slimani, 2016).

Onwioduokit (2012) attempted to establish a growth-inducing threshold level for fiscal deficit in West African Monetary Zone countries (Gambia, Ghana, Guinea, Nigeria and Sierra Leone) and stated 5.0 per cent as the optimal threshold. He, however, argues that the threshold level varies across countries. A year later, this claim was further corroborated in a study by the same author who analysed the optimal threshold for fiscal deficit in Sierra Leone and discovered it to be 7.0 per cent of the GDP (Onwioduokit, 2013). Aero and Ogundipe (2018) conducted a threshold analysis of fiscal deficit to economic growth in Nigeria from 1981 to 2014, using the threshold autoregressive model. They found the optimal threshold level of fiscal deficit to GDP in Nigeria to be about 5 percent. Onwioduokit and Bassey (2014) estimated the optimal threshold level of deficit for Gambia from 1980 to 2009 using the Threshold Autoregressive TAR Model with Hansen Approach of Residual Sum of Squares (RSS) and found increases of fiscal deficit beyond 6 percent of GDP, have negative impact on national output

METHODOLOGY

The research design for this study adopted the ex-post facto research design to examine the effect of cost of governance on defect budget in Nigeria. This design is chosen because it provides a structured and systematic framework for conducting rigorous analysis. Data for the study were sourced from Central Bank of Nigeria Statistical Bulletin

Model Specification

$$DF = \beta_0 + \beta_1 GAC + \beta_2 CD + \beta_3 CIS + \beta_4 CAN + \mu \quad (1)$$

Where

DF = Deficit financing

GAC = Cost of general administration

CD= Cost of defence

CIS = Cost of internal security

CAN = Cost on national assembly

β_0 = Regression Intercept

β_1 - β_4 = Coefficient of the independent variables to the Dependent variable

μ = Error term

Auto Regression Distributive Lag (ARDL)

To estimate the specified econometric models, the study will employ the Auto Regression Distributive Lag (ARDL) approach. The ARDL model, developed by Pesaran, Shin, & Smith (2001), is a widely used technique in econometrics for analyzing the long-run and short-run relationships between variables. It has gained popularity in applied research due to its flexibility

in accommodating mixed data types and addressing endogeneity concerns. The ARDL model is particularly suitable for analyzing the impact of infrastructure gaps on foreign investment, as it allows for the examination of both the immediate and delayed effects of infrastructural variables on investment. By incorporating lagged values of the dependent and independent variables, the ARDL model captures the dynamic nature of these relationships over time. Moreover, the ARDL approach provides a framework for estimating the long-run equilibrium relationship between deficit and cost of governance, as well as the short-run dynamics of adjustment towards this equilibrium. It offers valuable insights into the speed and magnitude of the response of deficit financing to changes in cost of governance thereby informing policy analysis and decision-making.

$$DF = \beta_0 + \beta_1 GAC + \beta_2 CD + \beta_3 CIS + \beta_4 CAN + \mu \quad (2)$$

In the long-run ARDL model, we examine the steady-state relationship between FI and the explanatory variables, including Cost of general administration, Cost of defence, Cost of internal security and Cost on national assembly on the other hand, the short-run ARDL model incorporates the short-term adjustments and dynamics in the relationship between deficit financing and the various cost of governance variables. By including lagged differences of the variables, this model captures the immediate response of deficit financing to changes in the explanatory factors.

Short-run ARDL model

$$\Delta DF\ (t) = \gamma 0 + \gamma 1 \Delta DF\ (t-1) + \delta 1 \Delta GAC\ (t-1) + \delta 2 \Delta CD\ (t-1) + \delta 3 \Delta CIS\ (t-1) + \delta 4 \Delta CAN\ (t-1) + \varepsilon \quad (3)$$

The short-run ARDL model captures the adjustments that occur in the immediate period following any changes in the variables. The model includes lagged differences (Δ) of the variables to account for their short-term dynamics, incorporating the lagged difference of DF and the lagged differences of the explanatory variables. This allows us to examine the immediate adjustments and responses of DF to changes in the explanatory factors. In both the long-run and short-run models, β0 represents the intercept, β1-β4 represents the coefficients for the respective variables, and ε represents the error term capturing any unexplained variation in the model.

Augmented Dickey-Fuller (ADF) Test

The ADF test is a commonly used test to assess the presence of a unit root in a time series. A unit root indicates that the series is non-stationary and exhibits a random walk pattern. The null hypothesis of the ADF test is that the series has a unit root, while the alternative hypothesis is that the series is stationary. The ADF test is conducted by regressing the differenced series on its lagged values. The general mathematical form of the ADF test equation is as follows:

$$\Delta y\_t = \alpha + \beta y\_\{t-1\} + \gamma\_1 \Delta y\_\{t-1\} + \gamma\_2 \Delta y\_\{t-2\} + \ldots + \gamma\_p \Delta y\_\{t-p\} + \varepsilon\_t \quad (4)$$

Where

Δ: denotes the first difference operator,
y_t: represents the time series variable
ε_t: is the error term.

The coefficient β is estimated and tested to determine if it is significantly different from zero. To interpret the results of the ADF test, the calculated test statistic (ADF statistic) is compared to critical values. These critical values depend on the sample size, level of significance, and the specific version of the test used (e.g., ADF-GLS, ADF-Fisher, etc.). The criteria for decision in the ADF test are as follows:

If the calculated test statistic is less negative than the critical value, we fail to reject the null hypothesis of a unit root, indicating non-stationarity. If the calculated test statistic is more negative than the critical value, we reject the null hypothesis and conclude that the series is stationary.

ARDL Bounds Cointegration Test

ARDL (Autoregressive Distributed Lag) Bounds Cointegration is a method used to test for the existence of a long-run relationship or cointegration between variables in a time series setting. The ARDL bounds test allows for the analysis of cointegration even when the variables may be integrated at different orders (i.e., some variables may be stationary, while others may be integrated of order 1 or higher). The ARDL bounds co-integration model can be represented as:

$Y_t = \alpha + \beta\_1X\_t + \beta\_2Z\_t + \varepsilon\_t$……..(5)

Where

Y_t: represents the dependent variable,
X_t:
Z_t: are the independent variables,
α: is the intercept,
β_1 and β_2: are the coefficients,
ε_t: is the error term.
To conduct the ARDL bounds test, the following steps are typically followed:

Determine the lag length: Choose an appropriate lag length for the model, usually based on information criteria such as the Akaike Information Criterion (AIC) or the Schwarz Information Criterion (SIC).Estimate the ARDL model: Use ordinary least squares (OLS) regression to estimate the coefficients of the ARDL model.Conduct the bounds test: Calculate the F-statistic for the joint significance of the lagged variables in the model. Compare the calculated F-statistic with the critical values from the bound tables provided by Pesaran, Shin, and Smith (2001) or Narayan (2005).At a significance level of 0.05, the decision criteria for the ARDL bounds co-integration test are as follows:

If the calculated F-statistic is greater than the upper critical value, the null hypothesis of no co-integration is rejected, indicating the presence of a long-run relationship between the variables.If the calculated F-statistic is lower than the lower critical value, the null hypothesis of no co-integration cannot be rejected, suggesting the absence of a long-run relationship.If the calculated F-statistic falls between the upper and lower critical values, no conclusive decision can be made, and further investigation is needed.The critical values for the ARDL bounds test are available in the works of Pesaran, Shin, and Smith (2001) and Narayan (2005) and depend on factors such as the lag length, sample size, and the type of test (e.g., level or first-difference).

RESULTS AND DISCUSSION

Table 1: Unit Root test Using Augmented Dickey-Fuller

Variable	ADF Statistic	Critical value @ 1%	Critical value @ 5%	Critical value @ 10%	Order of integration
DF	-5.121656	-3.769597	-3.004861	-2.642242	1(0)
GAC	-6.908519	-3.808546	-3.020686	-2.650413	1(I)
CIS	-4.639711	-3.886751	-3.052169	-2.666593	1(I)
CD	-5.458826	-3.857386	-3.040391	-2.660551	1(I)
CAN	-11.22379	-3.808546	-3.020686	-2.650413	1(I)

Source: Extract from E-view 9.0

To determine the degree of integration, a unit root test is carried out using the standard Augmented Dickey-Fuller (ADF) test. Moreover in applying ARDL model all the variables entered in the regression should not be integrated of order two. To check these conditions, unit root test is conducted before any sort of action taken. Even though the ARDL framework does not require per-testing variables to be done, the unit root test could convenience us whether or not the ARDL model should be used. The result in Table 1shows that there is a mixture of I (0) and I (1), this justifies the use of ADRL.

Table 2: Results of Bound test for Cointegration Growth ARDL

F-Bounds Test		Null Hypothesis: No levels relationship		
Test Statistic	Value	Signif.	I(0)	I(1)
			Asymptotic: n=1000	
F-statistic	9.071261	10%	2.2	3.09
k	4	5%	2.56	3.49
		2.5%	2.88	3.87
		1%	3.29	4.37
			Finite Sample:	
Actual Sample Size	21		n=35	
		10%	2.46	3.46
		5%	2.947	4.088
		1%	4.093	5.532
			Finite Sample: n=30	
		10%	2.525	3.56
		5%	3.058	4.223
		1%	4.28	5.84

Source: Extract from E-view 9.0

The bound test of co-integration with the null hypothesis of no long run co-integration exist is rejected since the F-statics (9.071261) above the upper bound (3.29) at one percent.

Table 3: Long Run ARDL Model Estimation

Variable	Coefficient	Std. Error	t-Statistic	Prob.*
DF(-1)	1.157236	0.181975	6.359297	0.0004
GAC	2.297178	1.921910	1.195258	0.2709
GAC(-1)	8.432109	3.319803	2.539942	0.0387
GAC(-2)	4.354404	3.174444	1.371706	0.2125
CIS	17.87644	7.153496	2.498980	0.0411
CIS(-1)	5.997978	2.902115	2.066761	0.0776
CIS(-2)	18.09569	8.041102	2.250399	0.0592
CD	4.214375	3.739380	1.127025	0.2969
CD(-1)	3.096605	3.997387	0.774657	0.4639
CD(-2)	12.15049	4.541540	2.675412	0.0317
CAN	8.348419	4.925297	1.695008	0.1339
CAN(-1)	12.29656	7.170946	1.714775	0.1301
CAN(-2)	22.23772	9.536053	2.331963	0.0525
C	313.6301	351.4882	0.892292	0.4019
R-squared	0.994717	Mean dependent var		-2200.781
Adjusted R-squared	0.984904	S.D. dependent var		2658.564
S.E. of regression	326.6431	Akaike info criterion		14.65033
Sum squared resid	746869.9	Schwarz criterion		15.34668
Log likelihood	-139.8285	Hannan-Quinn criter.		14.80146
F-statistic	101.3756	Durbin-Watson stat		2.435017
Prob(F-statistic)	0.000001			

Source: Extract from E-view 9.0

After confirming the existence of long-run co-integration relationship among the variables, the next step is running the appropriate ARDL model to find out the long run coefficients, which is reported in table 3 estimated of Cointegration and Long Run Coefficients using the ARDL Approach ARDL Selected Model: ARDL (1, 2, 1, 1, 2, 2, 2, 2) selected based on Akaike Information Criterion. The critical values reported for Pesaran*et al.* (2001) are the case with unrestricted intercept and no trend. As it is depicted in Table with an intercept and trend, the calculated F statistics (101.3756) is higher than both the Pesaran*et al.* (2001) and Narayan (2004) upper bound critical values at 1% level of significance. This implies that the null hypothesis of no long-run relationship is rejected; rather accept the alternative hypothesis (there is long-run relationship) based on the Pesaran*et al.* (2001) and Narayan (2004) critical values at 5% level of significance. Therefore, there is cointegration relationship among the variables in long run.The coefficient of determination (R-squared) is high explaining that about 98.4 percent of variation in the deficit finance were explained by cost of governance or attributed to variations in the explanatory variables in the model. The long run estimated result of the above table 3 showed, the cost of general administration has a positive impact on deficit financing and statistically significant at 1 percent significance level at 2.297178 coefficients positively. The coefficient of deficit financing (DF) is 1.157236. This indicates that, in the long run, holding other things constant, a 1 percent change in deficit financing change in during the study period. The result of cost of defence

is the result of positive relationship, at 5 present it is statistically significant and at 3.096605 coefficient positive relationship with deficit financing in period of study. Cost on national assembly, which is measured as percentage of total administrative cost has a positive relationship with deficit financing and statistically significant at 1 percent significance level at the 8.348419 coefficient while cost of internal security have a coefficient of 18.09569 which means the variable added 18 percent to deficit financing in Nigeria.

Table 4: Short Run Error Correction Model

ECM Regression				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
D(GAC)	2.297178	1.077624	2.131706	0.0705
D(GAC(-1))	4.354404	1.098765	3.962999	0.0054
D(CIS)	17.87644	3.089305	5.786559	0.0007
D(CIS(-1))	18.09569	3.749081	4.826699	0.0019
D(CD)	4.214375	2.124158	1.984022	0.0877
D(CD(-1))	12.15049	2.620104	4.637409	0.0024
D(CAN)	8.348419	1.338512	6.237088	0.0004
D(CAN(-1))	22.23772	3.325851	6.686326	0.0003
CointEq(-1)*	0.757236	0.027975	5.620509	0.0008
R-squared	0.913717	Mean dependent var		-433.2667
Adjusted R-squared	0.856194	S.D. dependent var		657.8754
S.E. of regression	249.4778	Akaike info criterion		14.17414
Sum squared resid	746869.9	Schwarz criterion		14.62180
Log likelihood	-139.8285	Hannan-Quinn criter.		14.27130
Durbin-Watson stat	2.435017			

Source: Extract from E-view 9.0

After the acceptance of long-run coefficients of the equation, the short-run ECM model is estimated. The error correction term (ECM), indicates the speed of adjustment to restore equilibrium in the dynamic model. It is a one lagged period residual obtained from the estimated dynamic long run model. The coefficient of the error correction term indicates how quickly variables converge to equilibrium. Moreover, it should have a negative sign and statistically significant at a standard significant level (i.e. p-value should less than 0.05). The error correction coefficient, estimated at -0.757236 is highly significant, has the correct negative sign, and imply a very high speed of adjustment to equilibrium. According to Bannerjee*et al*. (2003) as cited in Kidanemarim (2014), the highly significant error correction term further confirms the existence of a stable long-run relationship. Moreover, the coefficient of the error term (ECM-1) implies that the deviation from long run equilibrium level of deficit financing in the current period is corrected by 75.7% in the next period to bring back equilibrium when there is a shock to a steady state relationship. The coefficient of determination (R-squared) is high explaining that about 85.6 of variation in the deficit financing is attributed to variations in the explanatory variables in the model. In addition, the DW statistic does not suggest autocorrelation and the F-statistic is quite robust. Not only this but also in applying autoregressive distributed lag (ARDL) model, does not require testing for granger causality since, it considers an endogeneity problem in the model (Wessene,

2014). From the results presented in table 4, the independent variables have positive effect on deficit financing with cost on national assembly having the larges effect on deficit financing.

CONCLUSION AND RECOMMENDATIONS

Conclusion

The question of efficiency in governance is about ensuring that each amount of public funds is spent judiciously. In other words, every naira of public funds must be spent in a way that collective, not private welfare of citizens is maximized. In the absence of strong political institutions, the reduced cost of governance could only come if a benevolent set of public officers is in power. Since this is highly unlikely, we need to place institutional constraints on public office holders and technocrats in a way that minimizes the extraction of rent from the state. This is the better path to follow if the cost of governance is to be drastically reduced in Nigeria. Thus, no matter the quantum of financial resources in hands of the government, the desired objectives may not be achieve if cost of governance is not reduced to ensure revenue assurance in Nigeria. This is necessary to controlling costs and achieving the overall objectives of governance. This study examined cost governance and deficit financing in Nigeria. From the findings, the study conclude that cost of governance have positive and significant effect on deficit financing in Nigeria with cost of national assembly having the greatest effect on deficit financing.

Recommendations

i. There should be an optimal cabinet size to reduce cost of governance. The larger than optimal size of the executive cabinet and civil service sector are major causes of increasing cost of governance in Nigeria. It has also led to inefficiency in the public sector and waste of public fund.

ii. There is need to reduce the number of national assembly members, the National Assembly should be a single chamber and peopled by part time law makers. Constitutional amendments should be introduced urgently to reduce the size of the federal cabinet to not more than 18 to be appointed from the six geopolitical zones. In this regard the President and state governors should take the initiative in bringing about the necessary constitutional amendment for the reduction of the number of Ministers in the federal government. The approach to the issue has to be bi-partisan.

iii. The Nigerian legal system should be overhauled to achieve efficient dispensation of justice. This will help to reduce corrupt practices, such as inflation of costs of public projects kick-backs before contracts are awarded, abandoning of public projects also, property rights should be well defined to ensure the smooth operation of the free market system.

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