Fiscal Policy and Economic Growth: The Nigerian Experience (1970-2014)

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ABSTRACT
This study investigated the relationship between fiscal policy and economic growth of the Nigerian economy, for the period 1970 to 2014. The relationship between economic growth proxied by percentage changes in gross domestic product and fiscal policy (percentage changes in government expenditure, tax revenue and fiscal deficit) were modelled and analysed with the aid of ordinary least square method (OLS), Johansen co-integration, and error correction model. Government expenditures were segregated into four major sectors of administration, economic service, social and community service, and transfer sectors, and the result revealed that government expenditure on economic service (GEXPE) and fiscal deficit (FD) are positively and insignificantly related to gross domestic product, while government expenditure on social and community service (GEXPS) and tax revenue (TR) relates positively and significantly with gross domestic product, also government expenditure on administration and transfer were revealed to be related negatively and insignificantly with economic growth. Unit root test results indicate that all the variables were stationary at level, while Co-integration result revealed that there exist a long-run equilibrium relationship between economic growth and fiscal policy variables in Nigeria. The estimated ECM model which is rightly signed and statistically significant indicates that 92% disequilibrium in our explained variable can be corrected with changes in our explanatory variables over a year. As such, the study recommends among others that; Government should adopt fiscal mechanism that will encourage increment in revenue through tax instead of borrowing and over dependent on oil revenue.

Keywords: *Fiscal policy, Government expenditure, Tax revenue, fiscal deficit, Economic growth and Nigeria.*

Introduction

The achievement of macroeconomic goals namely; full employment, stability of price level, high and sustainable economic growth and external balance have been a policy priority of every economy whether developed or developing, given the susceptibility of macroeconomic variables to fluctuations in the economy. The realization of these goals is not automatic but requires policy guidance, and as such (Olawunmi & Ayinla 2007) opined that it is this policy guidance that represents the objectives of economic policy. According to Onoh (2007), "the need for

government intervention in the stabilization of the economy at critical times was recognised, especially when the private sector had lost focus, market forces de-mechanised, industries shut down, and interest rate plunging vertically towards zero as firms divest and no longer borrow to expand production and employment".   But the complexion of the argument as to whether government intervention is necessary or not changed in favour of government intervention following the appearance of Lord Keynes and his new deficit fiscal policy in 1930s; the fall out of which according to Jumbo (2010), became a great influence on both economic and political thinking; and this, revived government interest in the area of prediction and management of the economic environment in a bid to achieve economic growth and other macroeconomic objectives.

The question then is, why has it been unproductive in Nigeria despite its demonstrated efficacy in other economies as an effective policy that exerts influence on economic growth and development? The answer to this question forms the major aim of this paper.

Theoretical unpinning

According to Zhattau (2013), Growth comes from the accumulation of capital (both human and physical) and from innovations which lead to technical progress and raises the productivity of inputs into production and increase the potential level of output. Neoclassical growth models imply that government policy can affect only the output level but not the growth rate. However, endogenous growth models incorporate channels through which fiscal policy can affect long-run growth (Barro-Sala-i-Martin, 1991). In the incorporation of the channels, the model classifies generally the fiscal policy instruments into; (i) distortionary taxation, (ii) non-distortionary taxation; (iii) productive expenditures and (iv) unproductive expenditures, (Masson, 2000). Based on the model, all things being equal, it then follows that increase in productive spending financed by non-distortionary taxes will increase growth, while the effect may be disastrous on the economic growth if distortionary taxation is used.

Kennedy et al (2004) opined that an increase in non-productive spending financed by non-distortionary taxes will be neutral for growth, while if distortionary taxes are used, the impact on growth will tend to be negative. However, some government expenditures whether productive or non-productive are been provided by other means outside tax whether distortionary or non-distortionary and as such has effect on economic growth. Although Medee and Nebee (2011) assert that financing of fiscal deficit by reducing the available funds to private investors is very likely to retard economic growth. But on the other hand, some scholars argued that growth enhancement effect of fiscal deficit is not dependent on the manner of its funding rather on the manner of its spending, as such they are of the opinion that fiscal deficit as a tool of fiscal policy in spite of how it is financed, as long as it is being used to build infrastructure and provide support services, creates a conducive climate for private investment and will improve the prospect of economic growth.

Review of related works

According to Zhattau (2013), developing world government has little choice but to undergo several fiscal retrenchments in this face of rising debt burdens, falling commodity prices, growing trade imbalances, and declining foreign private public investment inflows. This meant cutting government expenditures (mostly on social services) and raising revenues through increased or more efficient tax collection (Torado and Smith 2009).

Medee and Nebee (2011) observed that despite the lofty place of fiscal policy in the management of the economy, the Nigerian economy is yet to come on the path of sound growth and development, which conforms the assertions of Agiobenebo (2003), Gbosi (2002) and Okowa (1997). Okpanachi (2004) pointed out that the poor performance of government policies in achieving desired macroeconomic targets in Nigeria stemmed largely from the lack of recognition on the part of policy makers of the structure of the economy vis-à-vis the interrelationships between government's own fiscal activities and macroeconomic variables. He went further to conclude that there is the need to overhaul the entire process of budgetary formulation, implementation and control. Olawunmi and Ayinla (2007) concluded in their study that, the achievement of sustainable economic growth through fiscal policy in Nigeria has remained a mirage.

Medee and Nenbee (2011) investigated the impact of fiscal policy variables on economic growth in Nigeria between 1970 and 2009. They employed the use of acrane method of Vector Auto Regression (VAR) and error correction mechanism (ECM) techniques, and their result revealed that there exist a mild long-run equilibrium relationship between economic growth and fiscal policy in Nigeria for the period studied. Wosowei (2013) employed the use of ordinary least square method in evaluating the relationship between fiscal deficit and macroeconomic performance in Nigeria over the period 1980 to 2010. The empirical findings show that fiscal deficit even though met the economic a prior in terms of its negative coefficient, yet did not significantly affect macroeconomic output within the period studied. In the same line, Ezeabasili, Wilson and Tsegba (2012) studied the effect of fiscal deficits on economic growth in Nigeria over the period 1970 to 2006. Using ordinary least square method of estimation, their result indicates that there is a negative effect of fiscal deficit on economic growth of Nigeria for the period and as such support the findings of Gummel (2001) in Ezeabasili et al (2012). Adefeso and Mobalaji (2010) analysed the fiscal-monetary policy and economic growth in Nigeria. With the aim of re-estimating and re-examining the relative effect of fiscal and monetary policies on economic growth in Nigeria over the periods 1970-2007. Employing the Error correction mechanism and co-integration technique, they found that the effect of monetary policy is much stronger than fiscal policy. And as such, they suggested that there should be more emphasis and reliance on monetary policy for the purpose of economic stabilization in Nigeria. Oni et al (2014), investigated the joint impact of total capital expenditure and total recurrent expenditure on economic growth in Nigeria through the use of ordinary least square multiple regression analytical method. Their result shows that total capital expenditure and total recurrent expenditure are important determinants of economic growth in Nigeria.

Methodology
This research work adopts the econometric framework of multiple regression, co integration and error correction methodologies, the variable are based on Gupta et al (2005) and Tanzi and Zee (1997) fiscal policy is viewed from three basic stand points: the fiscal policy stance; fiscal deficit or surplus, Tax revenue and, composition of federal government expenditures. The relationships are therefore modelled, first in its functional form thus:

GDP=F (GEXPA, GEXPE, GEXPS, GEXPT, TR, FD)…………………(1)

Equation (1) can be expressed Econometrically as,

GDP = GDP = $\beta_0 + \beta_1$ GEXPA + β_2 GEXPE + β_3 GEXPS + β_4 GEXPT + β_5 TR + β_6 FD + Ut …. (2)

b1, b2, b3, b4 b5, b6 > 0

Where:
GDP = Gross domestic product
GEXPA = government expenditure on administration
GEXPE = government expenditure on economic services
GEXPS = government expenditure on social community services
GEXPT = government expenditure on transfers
TR = tax revenue
FD = fiscal deficit
$\beta 0$ = Constant.
$\beta 1- \beta 6$= Regression coefficients.
Ut = Error Term.

Aprioi expectations
Following the theoretical positions, we expect all our explanatory variables to relate positively with gross domestic product as represented.
For the purpose of detecting the presence or otherwise of a unit root in our time series data which is a prerequisite for co-integration, we conducted a unit root test which is postulated by Markov first-order autoregressive scheme, usually denoted as AR(1) as follows:

$$Yt = \alpha Yt\text{-}1 + \mu t \text{.................................... (3)}$$

Where:
Yt =   Real GDP at time t.
α =   Coefficient of one period lagged value of real GDP.
$Yt\text{-}1$ =   One period lagged value of real GDP.
μt =   White noise error term assumed statistically independent and randomly distributed with zero mean, constant variance and serially not correlated.
Therefore, the model for testing the existence of unit root of a time series data is specified as follows:

$$\Delta Yt = \beta 1 + \beta_{2t} + \square Y_{t\text{-}1} + \sum_{i=1}^{m} \alpha i \, \Delta Y_{t\text{-}i} + \mu t \text{ .... (4)}$$

Where:
Y = variable of choice
$\beta 1$ = intercept
Δ = first difference operator
$\beta 2$ = constant parameter
$\square$ = coefficient of lagged $Yt\text{-}1$
μt = white noise error term
Following this, the implied hypothesis to be tested will be:
Ho: $\square = 0$, the time series data is non-stationary.
H1: $\square \neq 0$, the time series data is stationary.
Note, we will reject the null hypothesis if the absolute value of the ADF calculated is larger than the absolute value of the Mackinnon critical value.

Results Estimations and analysis
Table 1: stationarity result

Variables	ADF-statistics	Critical value	Order of integration
GDP	-4.077261 (0.0001)	1% level -2.618579 5% level -1.948495 10%level -1.612135	stationary at level $I(0)$
GEXPA	-6.091117 (0.0000)	1% level -2.618579 5% level -1.948495 10% level -1.612135	stationary at level $I(0)$
GEXPE	-5.233944 (0.0000)	1% level -2.618579 5% level -1.948495 10% level -1.612135	stationary at level $I(0)$
GEXPS	-6.991104 (0.0000)	1% level -3.588509 5% level -2.929734 10% level -2.603064	stationary at level $I(0)$
GEXPT	-2.794480 (0.0063)	1% level -2.619851 5% level -1.948686 10% level -1.612036	stationary at level $I(0)$
TR	-5.094468 (0.0000)	1% level -2.618579 5% level -1.948495 10% level -1.612135	stationary at level $I(0)$
FD	-3.099035 (0.0027)	1% level -2.619851 5% level -1.948686 10% level -1.612036	Stationary at level $I(0)$
RESIDUAL	-6.362868 (0.0000)	1% level -2.618579 5% level -1.948495 10% level -1.612135	Stationary at level $I(0)$

Source: author's computation.
Following the ADF result as shown in table 4., all the variables were seen to be stationary at level (they are integrated at order zero; I(0)).

Test for short run relationship
Table 2: Regression result
Dependent Variable: GDP
Included observations: 45

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.155078	0.047717	3.249955	0.0024
GEXPA	-0.013204	0.090187	-0.146409	0.8844
GEXPE	-0.045340	0.068094	-0.665846	0.5095
GEXPS	0.061932	0.035276	1.755632	0.0872
GEXPT	-0.091237	0.104873	-0.869971	0.3898
TR	0.436567	0.085181	5.125173	0.0000
FD	0.002729	0.005302	0.514658	0.6098
R-squared	0.503850			

Adjusted R-squared	0.425510		
F-statistic	6.431619	Durbin-Watson stat	1.711699
Prob(F-statistic)	0.000097		

Source: author's computation

Discussion of table 2, regression analysis
The coefficient of government expenditure on administration is negative (-0.013204), implying that the relationship existing between government expenditure on administration and GDP is negative and statistically insignificant in contrast to our apriori expectation. Based on the result, it means that 1% increase in government expenditure on administration will bring about 1.3% decrease in gross domestic product; this deviation from what we expected could, be as a result of expenditures in these sector being spent on consumables and most at times by political office holders in addition to the fact that most of the recorded misappropriation cases were witnessed in this sector. However, the implication of this relationship is that if the reduction in political office holders' salaries as has been announced by some of them is done with all circumspection, it will likely spur the growth of the economy. And wastages are cubed, the funds are spent for the right purposes, misappropriation are dealt with. Then we can have the desired result.

Expenditure on economic services
Government expenditure on economic services has a coefficient of -0.045340 with probability of 0.5095 implying that the relationship is negative and statistically insignificant. The result indicates that 1% increase in government expenditure on economic services will lead to approximately 5% decrease in gross domestic product holding other variables constant. This is against our apriori expectation but could be justified as a result of over dependency of economic services activities and expenditures on oil sector at the detriment of other economic sectors like agriculture and others.

Expenditure on social and community services
The 0.061932 coefficient of government expenditure on social and community services indicate a positive relationship between government expenditure on social and community services and gross domestic product which support our expectation. Holding other variables constant, a percentage increase in government expenditure on social and community services will bring about 6% increase in gross domestic product. This is explained by the fact that increases in government spending on productive services will increase output of the nation following theory; and interestingly, it was found to be statistically insignificant as evidenced from the probability of 0.0872. This means that over the years, the government have not done enough even though this sector has the potential to grow the economy.

Expenditures on transfer
Government expenditures on transfer has a coefficient of -0.091237, indicating a negative relationship between government expenditure on transfer and gross domestic product in Nigeria for the period under study; this implies that 1% increase in expenditure on transfer will lead to 9% decrease in gross domestic product holding other variables constant. This result although against our expectation may be due to mismatch in government revenue and expenditures and also as a result of too much external borrowings; since debt servicing attracts the major aspect of transfer expenditures. However, it is statistically insignificant based on its probability of 0.3898.

Government tax revenue

With the coefficient of 0.436567 and the probability of 0.0000, the result indicates a significant and positive relationship between government tax revenue and gross domestic product. Holding other variables constant, a percentage increase in tax revenue increases gross domestic product by 44% approximately. This agrees with our apriori expectation because an increase in government tax revenue through her expenditure will lead to increase in nation's output. Even as this result is as expected, government should be careful about over taxing the people, else it will be counterproductive if it is not matched with commensurate productive expenditure.

Fiscal deficit

The coefficient of fiscal deficit is 0.002729, implying a positive relationship between fiscal deficit and gross domestic product in Nigeria for the period under study. It indicates that 1% increase in fiscal deficit will lead to approximately 0.3% increase in gross domestic product. This confirms our expectation because theory (Keynesian) asserts that government expenditure especially fiscal deficit could provide a short-term stimulus to help halt a recession or depression. Although, it statistically insignificant judging by its probability of 0.6098.

Global statistics:
F statistic

Since at 5% level of significant and df of 4, 40, our F-calculated of 6.431619 is greater than the F-tabulated of 3.29, we reject the null hypothesis and conclude that the model demonstrated a good fit.

Co-efficient of Determination R2

The 0.503850 Co-efficient of Determination is an indication that our explanatory variables explained 50% of the total variation in our dependent variable.

Test for long run relationship
Table 4. 3 Co-integration
Trend assumption: Linear deterministic trend (restricted)
Series: GDP GEXPA GEXPE GEXPS GEXPT TR FD
Lags interval (in first differences): 1 to 1

Unrestricted Cointegration Rank Test (Trace)

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None *	0.656822	189.8399	150.5585	0.0000
At most 1 *	0.601367	143.8511	117.7082	0.0004
At most 2 *	0.516732	104.3034	88.80380	0.0025
At most 3 *	0.499284	73.03450	63.87610	0.0070
At most 4 *	0.392978	43.29068	42.91525	0.0458
At most 5	0.293249	21.82549	25.87211	0.1470
At most 6	0.148277	6.901215	12.51798	0.3549

Trace test indicates 5 cointegrating eqn(s) at the 0.05 level

* denotes rejection of the hypothesis at the 0.05 level
**MacKinnon-Haug-Michelis (1999) p-values

Based on the above Johansen co-integration statistics result, the trace statistics indicates 5 co-integrating equations, which by implication means that there is an existence of long-run co-movement among the observed variables. From the table, the co-integration among the variables is evidenced on the trace statistics value of 189.8399 which is greater than the critical value of 150.5585. The 0.00000 probability of trace statistics which is also less that the critical value probability of 0.05 is an additional prove of existence of co-integration among the variables; and as such, we reject the null hypothesis of no co-integration. The theory of Granger representation opines that if variables are co-integrated, the relationship can be expressed as ECM. Therefore, due to the existence of co-integration among our variables, we need to carry out an error correction model as depicted below in order to ascertain the speed of adjustment to the equilibrium.

Table 4.4: Error correction model result

Dependent Variable: D(GDP)				
Method: Least Squares				
Date: 12/03/15 Time: 00:17				
Sample (adjusted): 1971 2014				
Included observations: 44 after adjustments				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.011162	0.031402	-0.355449	0.7243
D(GEXPA)	0.018029	0.064383	0.280027	0.7811
D(GEXPE)	-0.075585	0.050872	-1.485792	0.1460
D(GEXPS)	0.063825	0.021238	3.005296	0.0048
D(GEXPT)	-0.094843	0.063216	-1.500292	0.1423
D(TR)	0.475569	0.056147	8.470020	0.0000
D(FD)	0.004725	0.003663	1.289724	0.2054
ECM(-1)	-0.922877	0.158143	-5.835721	0.0000
R-squared	0.793613	Mean dependent var		-0.008589
Adjusted R-squared	0.753482	S.D. dependent var		0.419208
S.E. of regression	0.208139	Akaike info criterion		-0.138252
Sum squared resid	1.559591	Schwarz criterion		0.186146
Log likelihood	11.04155	Hannan-Quinn criter.		-0.017950
F-statistic	19.77563	Durbin-Watson stat		1.788588
Prob(F-statistic)	0.000000			

From the error correction model, the R^2 indicates that approximately 79% variation in economic growth is been explained by our selected explanatory variables; also the result shows that ECM is rightly signed, that is, it is negative and statistically significant with about 92% speed of

adjustment, if there was a distortion in the short run. This result shows long run relationship and reasonable dynamics of GDP to the explanatory variables.

The co integration analysis shows the existence of long run equilibrium relationship among variables, it does not give us information about the direction of the relationship or the patterns. To assess the direction or pattern of the relationship, we conducted a causality test thus;

Table 4.5 Granger causality test

Pairwise Granger Causality Tests
Date: 01/16/16   Time: 08:33
Sample: 1970 2014
Lags: 2

Null Hypothesis:	Obs	F-Statistic	Prob.
GEXPA does not Granger Cause GDP	43	1.13431	0.3323
GDP does not Granger Cause GEXPA		1.30298	0.2836
GEXPE does not Granger Cause GDP	43	3.05921	0.0586
GDP does not Granger Cause GEXPE		3.51764	0.0397
GEXPS does not Granger Cause GDP	43	1.73991	0.1892
GDP does not Granger Cause GEXPS		1.74504	0.1883
GEXPT does not Granger Cause GDP	43	0.62163	0.5424
GDP does not Granger Cause GEXPT		1.38084	0.2637
TR does not Granger Cause GDP	43	1.02939	0.3670
GDP does not Granger Cause TR		0.35538	0.7032
FD does not Granger Cause GDP	43	0.17092	0.8435
GDP does not Granger Cause FD		1.01442	0.3722

Source: author's computation

From the result of granger causality test depicted above, the employed variables failed to prove the existence of directional relationship among the variables with the exception of GDP and GEXPE where a unidirectional relationship was found flowing from GDP to government expenditure on economic services. This implies that the increase in output of goods and services in the Nigerian economy will boost government's spending on economic services.

Conclusion

From our findings and discussions above, we can conclude therefore that for the period under study, social and community service expenditure and government tax revenue positively relates with gross domestic product in Nigeria with only the latter being significant. Also fiscal deficit relate positively but insignificantly with gross domestic product in the country over the years of our study, while government expenditures on economic services, transfer, and administration relate negatively and insignificantly with gross domestic product over the years of our study. Also, the study conclude that there is an existence of equilibrium relationship between our employed variables and that 92% disequilibrium in economic growth (GDP) can be corrected

with changes in our explanatory variables over a year; and as such, we recommend based on the findings and discussions above as follows:

1. Government should adopt fiscal mechanism that will encourage increment in revenue through tax instead of borrowing and over dependent on oil revenue.
2. Government should make effort to ease the process of tax collection and also ensure the effectiveness of punishment for tax defaulters and evaders.
3. Government should depend less on external borrowing with high service rate and central bank in financing its deficit, rather depend much on internal borrowing which   has   no inflationary tendency.
4. Government should make effort to diversify the economy by investing more on social and community service and economic service sectors so as to limit over dependency on oil sector that cannot boast of accommodating 0.001% of Nigerian population.
5. Fiscal policy should always be applied in synchronization with monetary policy in order to avoid conflict of macroeconomic objectives.
6. Government should at all times avoid financing capital investment with short-term debt and vice versa (fund mismatch).
7. Government needs to endeavour to diversify the economy away from the over dependence on the oil sector, judging from the poor performance of the sector in recent times.

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