
Committee on Balance-of-Payments Restrictions

REPORT ON THE FULL CONSULTATION UNDER
ARTICLE XVIII:12(b) WITH NIGERIA

1. The Committee met on 24 and 25 May 1993, under the Chairmanship of Mr. P. Witt (Germany) to conduct a full consultation with Nigeria, pursuant to the provisions of Article XVIII:12 (b) and the 1979 Declaration on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205). The International Monetary Fund was invited to participate in the consultation, pursuant to the provisions of Article XV:2.

2. The Committee had the following documents before it:

Basic document supplied by Nigeria

BOP/313

Background paper prepared by the Secretariat

BOP/W/151 and Rev.1.

International Monetary Fund, Recent Economic Developments, dated 19 February 1993.

3. The opening statement by the representative of Nigeria is contained in Annex I.

4. The statement by the representative of the IMF is contained in Annex II.

(i) Balance-of-payments position and prospects; alternative measures to restore equilibrium

5. The Committee noted that, since the last consultation, Nigeria's macroeconomic situation had deteriorated significantly and that the outlook was unfavourable. Economic growth had slowed markedly, financial performance had weakened, export growth had slowed down, the rate of inflation had accelerated sharply and the external balance had come under severe pressure. From a large surplus in 1990, the current account had moved progressively into deficit, reaching 2 per cent of GDP in 1992; the deficit on capital account had widened, partly due to substantial capital flight; the debt burden had increased and gross official reserves had fallen to about one month of imports.

6. Members of the Committee expressed serious concern about developments in Nigeria's macroeconomic management since late 1990, which they considered to be the main cause of the country's economic decline. The vulnerability of the Nigerian economy to weakening oil prices and the economic difficulties caused by a sharp drop in oil prices in 1992 were recognized. Members stressed, however, that declining oil prices had not been met by appropriate adjustments in domestic macroeconomic and financial policies. Relaxation of fiscal and monetary policies had led to increasing fiscal and external imbalances and a resurgence of inflation. Members expressed the view that a return to steady economic growth and the solution of the country's balance of payments difficulties required rapid and decisive adjustment in domestic macroeconomic and financial policies; this would facilitate reaching an agreement with the country's creditors on servicing Nigeria's high external debt. Members also questioned the economic rationale of the subsidies granted by Nigeria on domestic oil consumption.

7. Members of the Committee welcomed the abolition of the ban on wheat imports and encouraged Nigeria to intensify the process of trade liberalization. Concern was, however, expressed about recent developments in the foreign exchange market, which appeared to reverse the liberalization measures introduced in March 1992.

(ii) System, methods and effects of restrictions

8. Members called attention to the large number of products which had long been subject to import bans and the lack of transparency regarding their legal justification under the General Agreement. It was not clear which import restrictive measures were maintained under Article XVIII:B. Several import bans seemed to protect domestic production rather than safeguard the balance of payments; their justification under Article XVIII:B was therefore questionable. One member stated that Nigeria's import bans violated both Article XII:3(c) and Article XVIII:(10) of the GATT, which provides that import restrictions should "avoid unnecessary damage to the commercial interests of any other contracting party" and should not be applied as to "prevent unreasonably the importation of any description of goods in minimum commercial quantities". Some members encouraged Nigeria to use price-based restrictions rather than quantitative limits, to allow greater competition in the Nigerian market.

9. Several members pointed out that Nigerian tariffs were fluctuating and their application involved a great deal of unpredictability; import duties on a number of items had recently been increased. Members asked Nigeria to provide a time-table for future tariff reductions. It was also noted that recent changes in Nigeria's foreign exchange régime had led to delays in import payments. Questions were asked about the economic and legal justification for the 7 per cent import surcharge, and the application of high anti-dumping duties by Nigeria. Concern was expressed by the Committee about smuggling and other forms of illicit trade which was encouraged by the trade restrictions and some other measures applied by Nigeria.

10. The Committee requested Nigeria to notify the GATT justification of its remaining import restrictions, including their justification under Article XVIII:B of the General Agreement on a tariff-line basis by the end of July 1993. Members asked Nigeria to intensify import liberalization and prepare a time-table for the disinvocation of Article XVIII:B.

11. In reply, the representative of Nigeria stated that his country's economic problems were caused mainly by the country's heavy dependence on oil exports; quantity of oil production and oil prices were not under Nigeria's control. Capital flight took the form of overinvoicing, a practice followed by multinational companies. The Transitional Government was considering under the Economic Blueprint scheme how to change the present situation. Reducing of government spending is difficult because debt servicing accounted for more than 50 per cent of all spending and decrease of social spending had strict limits. Domestic oil price was considered by the Government as an political issue; a comprehensive oil and gas policy was under consideration.

12. Import bans in Nigeria were maintained for various purposes including not only balance of payments but also health, security and moral considerations. At present, Nigeria was not in a position to indicate the exact legal justifications for all the restrictions, but it was ready to notify them on a tariff line basis by 31 July 1993. It was the intention of Nigeria to reduce its import restrictions; however, this would take a longer period. The list of restrictions would be subject to revision in two years. Nigeria recognized that price-related import restrictive measures should enjoy priority over quantitative measures. There was no time-table for tariff changes; however, the present tariff régime would expire in 1994. Since the last consultation Nigeria had made changes in its tariffs; some

tariff rates were reduced, while others had been increased. Changes in the foreign exchange régime could not cause delays in payments, as banks were allocated foreign exchange on a pro-rata basis. To prevent commercial malpractice, the Government had established a Committee which investigated offences in this field. The 7 per cent import surcharge mainly covered port handling charges; it was not applied for balance-of-payments reasons, but its purpose was to raise revenue for improving port infrastructure.

(iii) Conclusions

13. The Committee recognized that since the last consultation, Nigeria's external and internal economic balances had deteriorated significantly. From a large surplus in 1990, the current account balance had moved progressively into deficit, reaching 2 per cent of GDP in 1992. Simultaneously, there was a significant deterioration in the capital account. As a result, the level of reserves had declined to around one month of imports.

14. While recognizing the vulnerability of the Nigerian economy to weakening oil prices, the Committee expressed particular concern about the relaxation of fiscal and monetary policies in this period, which had brought about large and increasing fiscal and external imbalances and a resurgence of inflation. It was felt that, to return to a path of steady economic growth, rapid and decisive adjustment in domestic macroeconomic and financial policies was required. The Committee emphasized that this would be a key element in the solution of Nigeria's balance of payments difficulties, including the necessity of reaching a durable solution for servicing external debt. The burden of debt service weighed heavily on both the fiscal and external accounts despite progress on debt and debt service reduction vis-à-vis commercial creditors. Debt agreement with official creditors, however, was awaiting reversal of the policy slippages of the past period and the return to a credible reform and macroeconomic policy programme.

15. The Committee urged Nigeria to intensify the process of trade liberalization, in order to complement the necessary corrective macroeconomic and financial adjustment measures. Specifically, an appropriate incentive structure, including market-oriented exchange rates, would bring important elements of trade back into official channels, helping to redress both the fiscal and trade balances.

16. Although the ban on wheat imports had been abolished, fourteen other broad product groups remained under import prohibition. Doubt was expressed whether the remaining import prohibitions could be correctly justified under Article XVIII:B. The Committee welcomed Nigeria's readiness to notify the reasons for such measures and, where appropriate, their justification under XVIII:B on a tariff-line basis by end July 1993.

17. Concern was also expressed about the possible trade effects of the temporary change in the foreign exchange régime introduced in February 1993. Other concerns were voiced with regard to tariff changes; the use and effects of anti-dumping measures; the fiscal and economic impact of oil subsidies; and the effects of, and justification for, the import surcharge. The Committee noted Nigeria's statement that the import surcharge was established not for balance-of-payments reasons but mainly for the development of port facilities.

18. The Committee, being unable to determine which measures were maintained for balance of payments purposes, decided to revert to this question after having received the notification referred to in paragraph 16.

Annex I

Opening Statement by the Delegation of Nigeria

In March 1991, Nigeria consulted with this Committee under the simplified procedures. It was the view of this Committee that the liberalization of trade and exchange restrictions introduced by Nigeria were commendable and should be continued. I wish to assure this Committee that the liberalization policies which Nigeria introduced in July 1986, in the context of the Structural Adjustment Programme, are still in place and continued to be reinforced. We have implemented a number of measures aimed at resuscitating the economy and diversifying the productive base. These include the acceleration of privatization, and commercialization of certain government enterprises, removal of foreign ownership requirements for scheduled sectors, and the adoption by the CBN of indirect approach to monetary management.

The measures were adopted with a view to meeting basic economic objectives outlined by government, such as the reduction in the level of inflation, stimulation of private sector investment, generation of employment and reduction in the pressure on the external sector. The results have so far been modest. The GDP at 984 factor cost increased by 5.2, 8.3 and 4.4 per cent in 1989, 1990 and 1991, respectively. Agricultural production recorded an increase of 4.8, 7.7 and 5.5 per cent for the same period, while industrial production increased by 9.4, 11.1 per cent in 1989 and 1990, respectively. The rate of inflation which was 50.5 per cent in 1989 fell to 7.4 per cent at the end of 1990, but rose to 13.0 and 46.0 per cent in 1981 and 1992, respectively. This development can be traced to surfeit liquidity in the economy, uncertainty surrounding the exchange rate and increase in the cost of production.

The management of the external debt situation continued to be handled through rescheduling meetings with our creditors. Efforts to reduce the debt burden are continuing. Among the initiatives adopted are capital repayments, and debt to equity conversion programme. The debt conversion programme has recorded some positive progress in achieving the objectives of increased investment in the productive sectors of the economy.

So far, Nigeria rescheduled her debt totalling US\$19.3 billion with the London and Paris Clubs Creditors and obtained debt cancellation amounting to US\$106.4 million from the governments of Canada and the United States. Consequently, there is a significant decline in our country's external debt stock from US\$33.36 billion at the end of 1991 to US\$27.56 billion at the end of 1992. Furthermore, the sum of N58.4 billion or 52.09 per cent of the 1993 budget has been set aside for debt servicing.

The focus of the exchange rate management continued to be centered on the need to get a realistic value for the Naira. However, the increased pressure on the national currency arising from expansionary fiscal operation, speculative biddings and some other malpractices continued. In order to eliminate these problems, government introduced new reforms in 1992, whereby the rates would be freely determined by the banks directly executing the order of their clients.

- i - the Central Bank of Nigeria has discontinued the practice of allocating foreign exchange to banks on predetermined quotas;
- ii - banks are free to procure foreign exchange from any source and to sell such foreign exchange to clients on presentation of approved documents currently in use;

- iii - banks are free to sell their foreign exchange at rates they like with no rice controls but subject to a maximum spread of 1%. Authorized dealers are required to publish such rates, and the CBN shall note the areas for future sales to such dealers;
- iv - banks dealing in foreign exchange shall report such statistical purposes to the CBN on the prescribed forms;
- v - current restrictions on capital transfers are abolished. However, in all cases, evidence of importation and exportation has to be provided to the authorities;
- vi - borrowing money for the purpose of repatriating funds is prohibited and strict debt equity ratios are enforced on all foreign investors in Nigeria; and
- vii - transactions on all bills for collection, open accounts and such other modes of trades, other than imports under letters of credit are to be reviewed.

In the area of fiscal policy Government has put in place the following:-

- i - the extension of the duty-free concessions and reductions in tariffs on selected items introduced in March 1992 to 31 December 1993;
- ii - the introduction of Modified Value Added Tax (MVAT) to replace the existing sales tax;
- iii - the abolition of excise duties on all locally manufactured products except tobacco and alcohol;
- iv - the retention of 5% customs duty rate on sugar;
- v - the removal of cassava derivatives such as industrial starch, pellets and chips, from the Export Prohibition list; and
- vi - the lifting of total ban on wheat importation.

In order to address the persistent problem of budget deficit, government has established a budget monitoring Committee. Government has also recognized the need for a stable macro-economic environment to facilitate planning by private sector operators and win the confidence of foreign investors. The monetary and fiscal policies outlined above, therefore have been put in to achieving these objectives.

Finally, the oil and gas sectors will continue to play a major rôle in the Nigerian economy for the foreseeable future. In this connection, Government is considering the development of a comprehensive oil and gas policy to facilitate full realization of potentials of that sector in the Nigerian economy.

Annex II

Statement by the Fund Representative
to the GATT Balance of Payments Committee

Nigeria is heavily dependent on the oil sector for exports and government revenue, making its economy vulnerable to developments in world oil markets. Policies during the period of buoyant oil revenue did not contribute to increasing the robustness of the economy. The sharp drop in world oil prices in the mid-1980s, therefore, caused serious economic difficulties, including major strains on the balance of payments, which were not met by appropriate adjustments in domestic macroeconomic and financial policies. Following a severe economic decline, however, Nigeria launched a structural adjustment program (SAP) in mid-1986, which was supported by three stand-by arrangements from the Fund over the period 1987-92. The basic objectives of the SAP were to redress the country's large financial and structural imbalances, and hence establish a firm basis for sustained economic growth. In a sharp departure from past policies, the SAP emphasized reliance on market forces, instead of administrative controls. Accordingly, the exchange and trade system was liberalized, most price controls eliminated, marketing boards abolished, a large number of public enterprises privatized or commercialized, and steps were taken to encourage private domestic and foreign investment. Efforts were also made to diversify the economy by promoting agricultural and other non-oil sector activities.

These reforms improved the framework of incentives in the economy, and generally strengthened the country's international competitiveness. Aided by the implementation of appropriate financial policies, albeit inter-mittently, and a significant recovery in world oil prices, Nigeria's overall economic performance improved appreciably during the period 1988-90: the growth of real GDP averaged 8.4 percent a year; the rate of inflation, as measured by the consumer price index on an end-of-period basis, decelerated to 3.5 percent by end-1990; and the external current account balance moved from a large deficit to a sizable surplus.

Against the backdrop of a highly volatile world oil market and the requirements of the transition to civilian rule, however, Nigeria's economic and financial performance has weakened since late 1990. Economic growth slowed markedly, the rate of inflation accelerated sharply, and the external position came under severe pressure, involving a substantial accumulation of external payments arrears as well as a large loss of reserves. Slippages in financial policies, at a time when oil export prices were declining, caused a sharp deterioration in the external current account balance, from a surplus equivalent to about 8 percent of GDP in 1990 to a deficit of 2 percent of GDP in 1992. By 1992 oil export prices had fallen some 20 percent below their 1990 level, while the volume of oil exports had increased only moderately. Export earnings fell for two consecutive years, while import payments continued to rise. With few new commitments from bilateral and multilateral sources, disbursements of loans continued the declining trend that began in 1990, and the deficit in the capital account widened to US\$5.7 billion in 1992. Gross official reserves declined sharply, from the equivalent of about 5 months of imports in 1990-91 to only 1 month of imports in early 1993.

At the core of Nigeria's macroeconomic imbalances has been the recent expansionary stance of fiscal policy, which has been driven by large extra-budgetary outlays. The Federal Government's overall fiscal deficit more than tripled from 1990 to 1992, reaching an estimated 10.6 percent of GDP. In addition, the growing subsidies on domestic petroleum consumption have not only had a major distortionary impact on the economy, but have also exacerbated the country's fiscal problems.

Since 1986, Nigeria has continued to liberalize its exchange and trade system. The bulk of the demand for foreign exchange continued to be met through weekly auctions conducted by the Central Bank, while foreign exchange bureaus, which were introduced in August 1987, contributed to a liberalization of the exchange system. In December 1990 the foreign exchange auction system was rationalized by eliminating the guaranteed allocation of foreign exchange on the basis of dealer banks' quotas. During 1991 and early 1992, as domestic inflationary pressures mounted, the spread between the foreign exchange bureau and official rates widened, from 16 percent in December 1990 to 78 percent in February 1992; during the same period, the official exchange rate of the naira vis-à-vis the U.S. dollar depreciated by 17 percent, whereas the bureau rate depreciated by 80 percent. Subsequently, on March 5, 1992, the foreign exchange auction was replaced by an interbank system, under which the official rate was determined in the interbank market; with that action, the official rate depreciated from N 10.56 to N 18.48 per U.S. dollar, and the spread between the foreign exchange bureau and official rates narrowed markedly. Nevertheless, the expansionary fiscal policies continued to exert pressure on the naira, which prompted the Central Bank to suspend the supply of foreign exchange to the interbank market on several occasions toward the end of 1992 and in early 1993. The Central Bank reintroduced on February 18, 1993, on a temporary basis, an auction system for the allocation of foreign exchange, and the naira depreciated further to N 25 per U.S. dollar, compared with N 20.6 per U.S. dollar at end-January. Since February 25, 1993, the Central Bank has allocated foreign exchange on a pro-rata basis at a fixed exchange rate. In response, the naira moved up to N 23 per U.S. dollar and the spread between the official and the foreign exchange bureau rates widened with the latter being quoted at about N 35 per U.S. dollar.

As regards the trade system, important liberalization measures have been taken since 1986, including the elimination of all import licensing requirements, the removal of the 30 percent import surcharge, and a sharp reduction of the number of prohibited imports, first from 74 to 16, and most recently to 14. In January 1988 a new tariff system was adopted, which was designed to rationalize the tariff structure over a seven-year period. It was envisaged that the tariff structure introduced in 1988 would remain in force until 1994 and that during the 1992-94 period the dispersion of tariffs would be narrowed. In the aftermath of the March 1992 exchange reform, Nigeria took several measures aimed at cushioning the effects of the devaluation, through a selective lowering of import duties, mainly on vehicles, spare parts, and components, as well as a relaxation of import restrictions on pharmaceuticals. In addition, in 1992, import duties on inputs for cement production were lowered, while the five-year-old ban on wheat imports first was suspended with effect from October 22, 1992, and then abolished in April 1993. Despite these measures, the commitment to reforms is not yet well-rooted, and the trade system continues to feature import prohibitions (on 14 product groups, including poultry, vegetables, textiles, beer, rice and maize), export bans (on certain crops and timber), and high import taxes for both fiscal and domestic protection purposes. The Fund has urged a relaxation of these controls as part of the process of removing the structural impediments to growth.

In view of the very heavy debt service burden, Nigeria's balance of payments outlook will, in all likelihood, remain very difficult, with financing gaps projected at about US\$2 billion a year during the remainder of the 1990s. Debt service relative to exports of goods and nonfactor services would decline over this period, but still average some 33 percent, despite the recent completion of a significant debt and debt service reduction operation with commercial banks. Thus, Nigeria faces considerable challenges in the period ahead. The political transition process has so far constrained the authorities' ability to take bold corrective actions, notably on the fiscal side, although it is clear that the country cannot afford to wait much longer to address its serious difficulties. Financial imbalances have once again assumed alarming proportions. In addition, in the absence of a stable policy environment, a durable solution which would address the heavy external debt service burden is not in sight.

The transitional government that took office in early January 1993 has expressed its intention in the context of the new budget to follow the economic strategy launched under the SAP. However, it still needs to formulate and start to implement soon a strong and comprehensive adjustment program, with a view to correcting the existing imbalances, bringing inflation under control, allowing the exchange rate to reflect market conditions, and making further progress in the liberalization of the exchange and trade régime. Such a program would also be necessary to mobilize the support of bilateral creditors in finding a lasting solution to Nigeria's debt problem, and to close the large financing gaps that are in prospect for 1993 and the medium term.