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Resilience through Reforms

Nigeria Development Update
June 2021

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Acknowledgements

The *Nigeria Development Update* (NDU) is a World Bank report series produced twice a year that assesses recent economic and social developments and prospects in Nigeria, and places these in a longer-term and global context. The NDU also provides an in-depth examination of selected policy issues and medium-term development challenges in Nigeria. It is intended for a wide audience, including policy makers, business leaders, financial market participants, and the community of analysts and professionals engaged in Nigeria's evolving economy.

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Structure

The Nigeria Development Update (NDU) has three sections:

1. **Recent economic developments and outlook:** A review of the most salient economic developments over the previous 6 months and the outlook for the following two years, including a set of short-term and medium-term policy recommendations.

2. **Taking a closer look:** A topical review of a selection of issues that have "risen to the surface" in the previous 6 months.

3. **Spotlight on Nigeria's development agenda:** A long-term view on key challenges and opportunities for Nigeria's development agenda, including a set of actionable policy recommendations.

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Abbreviations and Acronyms

bps	Basis points
CAD	Current Account Deficit
CBN	Central Bank of Nigeria
DMO	Debt Management Office
FX	Foreign Exchange
GDP	Gross Domestic Product
GHS	General Household Survey
IEFX	Investors' & Exporters' Foreign Exchange
MSMEs	Micro, Small, and Medium Enterprises
NASSP	National Social Safety Nets Program
NBS	National Bureau of Statistics
NDU	Nigeria Development Update
NLPS	National Longitudinal Phone Survey
NPL	Non-Performing Loans
OMO	Open-market operations
SSA	Sub-Saharan Africa

Overview

In 2020, Nigeria experienced its deepest recession in four decades, but growth resumed in the fourth quarter as pandemic restrictions were eased, oil prices recovered, and the authorities implemented policies to counter the economic shock. As a result, in 2020 the Nigerian economy experienced a smaller contraction (-1.8 percent) than had been projected when the pandemic began (-3.2 percent). As part of its response, the government carried out several long-delayed policy reforms, often against vocal opposition. Notably, the government (1) began to harmonize exchange rates; (2) began to eliminate gasoline subsidies; (3) started adjusting electricity tariffs to more cost-reflective levels; (4) cut nonessential spending and redirected resources to COVID-19 responses at both the federal and the state levels; and (5) enhanced debt management and increased public-sector transparency, especially for oil and gas operations. By creating additional fiscal space and maximizing the impact of the government's limited resources, these measures were critical in protecting the economy against a much deeper recession and in laying the foundation for earlier recovery.

However, several critical reforms are as yet incomplete, which threatens Nigeria's nascent recovery. In the baseline scenario, Nigeria's economy is expected to grow by 1.8 percent in 2021. Despite the current favorable external environment, with oil prices recovering and growth in advanced economies, reform slippages would hinder the renewed economic expansion and undermine progress toward Nigeria's development goals. In a risk scenario, in which the government fails to sustain recent macroeconomic and structural reforms, the pace of economic recovery would slow, and GDP growth could be just 1.1 percent in 2021. Gasoline subsidies have re-emerged with the recent rise in oil prices, and a reversal of fiscal consolidation efforts on the revenue side is an especially threatening risk. Failure to sustain the reform momentum would threaten both macroeconomic sustainability and the government's policy credibility and would further limit the government's ability to address gaps in human and physical capital—all of which would discourage private investment. Slow growth would put more pressure on the financial sector: nonperforming loans (NPLs), which have yet to reflect the impact of the COVID-19 shocks due in part to regulatory forbearance granted by the Central Bank of Nigeria (CBN), would likely rise as forbearance is withdrawn. Moreover, Nigeria is experiencing a rise in insecurity. A tepid or uneven recovery could exacerbate social tensions, which would further dampen investor enthusiasm and could lead to political instability, and more conflict.

High inflation rates are worsening poverty and depressing economic activity. Driven by a steep increase in food prices, since September 2019 headline inflation has risen dramatically. Although inflation declined slightly in April 2021, it is still the highest in four years. In contrast to previous inflationary episodes in Nigeria, the current trend arises from multiple demand and supply shocks, compounded by policy distortions and the exigencies of the pandemic. On the supply side, a combination of unfavorable weather, insecurity and conflict, and pandemic-related shocks affecting food production and market access are pushing food prices up. Trade restrictions, including the closure of land borders in August 2019, have also pushed up prices for both food and nonfood consumer goods. On the demand side, the lack of a credible monetary anchor encourages firms and consumers to expect shock-induced price increases and incorporate their expectations into their investment and consumption decisions. The impact of higher inflation is severe: In 2020, rising prices alone—even without incorporating the direct impacts of COVID-19 on welfare—may have pushed an estimated 7 million Nigerians into poverty.

Limited employment opportunities pose both economic and security challenges. As in other developing countries where informality is high, Nigeria's official unemployment rate is a poor indicator of labor-market outcomes because unemployed workers receive little public support and the incentives to remain employed are compelling, even in marginal activities that generate low returns. In Nigeria agriculture has long served as an employer of last resort; family farms absorb excess labor during economic downturns Yet the periodic influx of displaced urban workers into the rural economy keeps agricultural wage rates depressed and generates uncertainty that discourages investment in productive capital. The informal service sector also provides employment, but it also typically offers low wages and limited job security or labor protection. In addition to their negative economic consequences, rising levels of unemployment and underemployment are both a cause and a consequence of conflict and insecurity. Marginally employed workers become prime recruiting targets for criminal organizations and insurgent groups like Boko Haram. Intensifying violence and widespread criminality further erode the labor market, contributing to a vicious cycle of underemployment and instability. Creating adequate productive employment is thus a priority not only for economic policy but also for national security.

Adopting a sequenced program to protect the lives and livelihoods of poor and vulnerable Nigerians—with immediate attention to reducing inflation—is vital to sustain the recovery. This edition of the *Nigeria Development Update* proposes near-term measures designed to reduce inflation while protecting the poor and supporting the recovery. Policy proposals are organized around three priority objectives: (1) Reduce inflation by adopting policies to support macroeconomic stability, inclusive growth, and job creation. (2) Protect poor households from the impacts of inflation. And (3) Facilitate access to sustainable financing for small and medium enterprises in key sectors to mitigate the effects of inflation and accelerate the recovery. Accomplishing these goals will require a big push in areas as varied as exchange-rate management, monetary policy, trade policy, fiscal policy, and social protection:

- **Exchange Rate Management:** Make the Nigeria Autonomous Foreign Exchange (NAFEX) rate[1]—now the anchor rate for all formal foreign exchange (FX) transactions—more flexible in order to reduce real exchange rate misalignments, boost Nigeria's competitiveness, and narrow the spread between the NAFEX rate and the parallel market rate, with a positive effect on inflation dynamics.

- **Trade Policy:** (1) Fully reopen land borders to trade and strengthen regional cooperation in combating smuggling. (2) Facilitate imports of staple foods and medicines by removing them from the list of FX restrictions, and replace import bans with tariffs that align with the ECOWAS Common External Tariff. (3) Review all FX and import restrictions currently applied to nonfood goods and assess the pros and cons of replacing them with tariffs. (4) Do not add any products to the list of import and FX restrictions. (5) Control oil-related inflationary pressures by reducing gasoline smuggling.

- **Fiscal Policy:** (1) To help control growth of the money supply, establish mechanisms to monitor and report the federal government's stock of CBN overdrafts. (2) Identify more flexible options for borrowing to finance the federal government deficit. (3) Totally eliminate the fuel subsidy. (4) Design a sequence of reforms to mobilize domestic non-oil revenue in a way that does not affect recovery of the economy, such as increasing "sin taxes," charging fees for electronic money transfers, rationalizing tax expenditures, removing loopholes in tax laws, and improving tax compliance by building up revenue administration.

- **Monetary Policy:** (1) Clearly define monetary-policy priorities and objectives, with price stability specified as the primary goal. (2) Resume naira-denominated open-market operations (OMOs) based

1 NAFEX is the reference rate for FX transactions in the Investors' & Exporters' FX Window. It is also referred to as the IEFX rate in other parts of this Report.

on a transparent issuance schedule, and signal to markets that OMOs will use short-maturity securities to control banking system liquidity. (3) Reduce CBN subsidized lending to medium and large corporates, expanding the scope for commercial banks to intermediate funds at a risk-adjusted lending rate. (4) Phase out excessive reliance on the cash-reserve ratio as a high-frequency liquidity control tool and an instrument to finance quasi-fiscal CBN operations.

- **Social Protection:** (1) Leverage the National Social Safety Nets Program (NASSP) to provide transfers to more households and temporarily increase transfers to current beneficiaries. (2) Complement NASSP with the National Home-Grown School Feeding Program (NHGSFP) to strengthen the food security of vulnerable households. (3) Rapidly implement the COVID-19 Action Recovery and Economic Stimulus program to support households, farmers, and firms.

How COVID-19 is affecting the labor market and how inflation is affecting poverty

The continuing effects of the COVID-19 crisis on welfare and work: The pandemic continues to profoundly affect employment and household welfare in Nigeria. Data collected in the February 2021 COVID-19 National Longitudinal Phone Survey indicate that the number of people working in February 2021 was similar to the number in September 2020—much higher than would be expected if employment were following typical seasonal patterns. The higher share of people working was more concentrated among women and people from poorer households, which indicates an "added worker effect": more members take on work to help the household to cope with economic shocks. Moreover, the commerce and service sectors have expanded beyond what would be expected given previous seasonal patterns, especially for women. Accompanying these labor market shifts, incomes for some households have increased since before the crisis, although this is far from universal. Yet even if incomes are stabilizing, households are feeling the impact of rising prices, which erodes their purchasing power and means that food insecurity is still widespread.

Poverty and inflation in Nigeria: Inflation is exacerbating poverty. The headline inflation rate reached a four-year high in March 2021, and in 2020 food prices accounted for 63 percent of the total increase in inflation. Most of the food that households consume is purchased rather than self-produced, even among poor agricultural households in rural areas; food-price inflation is thus a major threat to purchasing power and household welfare. Food insecurity is more widespread than it was before the COVID-19 crisis, and in November 2020 about 56 percent of households reported that adults had skipped meals in the previous 30 days. Expanding social protection programs to provide time-bound support will alleviate the immediate effects of inflation. Over the long term, however, the Nigerian authorities need to address the sources of inflation through a mix of monetary, exchange-rate, fiscal, and trade policies, complemented by reforms that support job creation.

Spotlights on the power sector and on mobilizing domestic revenues

Igniting economic growth by reforming the power sector: Nigeria's revenue-side challenges may be diffuse, but on the spending side the electricity sector is a clear priority for reforms. An estimated 43 percent of Nigeria's population (85 million people) lack access to an electricity grid—the largest energy-access deficit in the world. Privatization efforts have not delivered their intended outcomes, and the power sector is now under severe stress. Distribution companies report aggregate technical, commercial, and collection losses of about 50 percent, far above the 15 percent benchmark for international good practice. The inefficiencies, combined with uneven reforms of tariffs, have led to a breakdown in the sector's payment chain. For instance, in 2020 alone, Federal government support for the electricity sector exceeded its total health budget. Recognizing that power sector underperformance threatens Nigeria's post-pandemic recovery, the authorities have already begun implementing some critical actions specified in the Power Sector Recovery Programme (PSRP) and the National Electrification Project (NEP) to improve sector performance and increase access to reliable electricity throughout the country. For example, in November 2020, the government raised electricity tariffs from 56 to 80 percent of cost while moving to a regime of service-based tariffs and ensuring that the increases in average tariffs do not adversely impact those poor and low-income households hat do have access to grid electricity. To complement the tariff reforms, the government issued regulations to stop arbitrary estimated billing, accelerate mass metering, and enforce payment discipline for the distribution companies—all actions to improve the financial sustainability of the sector. There is now a need to deepen these actions through a combination of financial and policy interventions upstream and technical, operational, and investment interventions downstream.

Options to raise revenues in a time of crisis: Tax revenues are necessary to run essential services, provide security to citizens, help tackle hunger and poverty, and deliver critical health and education services. Nigeria may be Africa's biggest economy but at just 4 percent it has Africa's lowest tax-to-GDP ratio. Together the COVID-related economic slowdown and the steep fall in oil prices in 2020 brought into clear focus the need to increase non-oil revenue even when investment, jobs, and growth also need to increase. This calls for a carefully calibrated set of policy and administrative measures that can grow revenues without discouraging investment. That rules out any increases in traditional ad valorem taxes like the value-added tax but it does afford an opportunity to fully apply tax policies already adopted and reform tax administration to seal compliance gaps. Focusing on low-hanging, revenue-yielding fruits could yield substantial gains: increasing "sin taxes," charging fees for electronic money transfers, rationalizing tax expenditures, removing loopholes in tax laws, and improving tax compliance with more disciplined revenue administration. In the next three years such measures can raise the tax-to-GDP ratio to about 7 percent and bring in as much as ₦10 trillion. In the longer term, fundamental reforms of the tax system will be necessary to stimulate post-pandemic investment and economic growth. As Nigeria tries to "build back better" after the COVID crisis, a more strategic approach to revenue mobilization will also be necessary: not just taxing more, but taxing better; not just how much to collect, but how to collect, what to collect, and from whom.

Part 1: Recent Economic Developments and Outlook for Nigeria

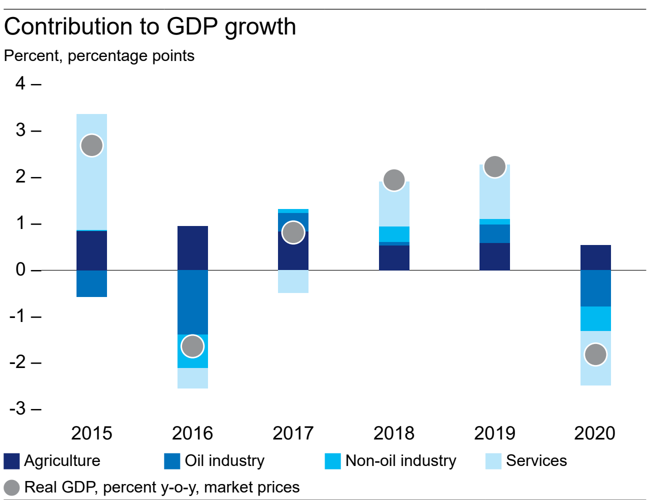
Economic Growth: Past the pandemic-induced recession, but not yet on the road to solid growth

In 2020 the Nigerian economy shrank by 1.8 percent. The COVID-19 crisis drove the economic slowdown; the external context was marked by capital outflows, intensified risk aversion, low oil prices, and shrinking remittances. In March 2020, the federal government imposed a lockdown on Lagos and Ogun states and the Federal Capital Territory, and state governments set similar restrictions. These measures, combined with precautionary firm and consumer behavior, put the brakes on manufacturing and services activity; essential sectors like food, agriculture, and financial services continued to operate, but at diminished levels.

While heavily affected trade and investment are still guarded, private consumption is showing signs of resilience. In 2020 exports declined by 27.0 percent, imports by 23.3 percent, and fixed capital formation by 7.6 percent—the worst declines since the global financial crisis of 2009 and its aftermath. Nevertheless, private consumption went up by 2.2 percent. Although the data on GDP is still preliminary, the resilience of private consumption may be explained in part by workers moving out of services, which were severely impacted by the pandemic, to agriculture, which was less affected.[2]

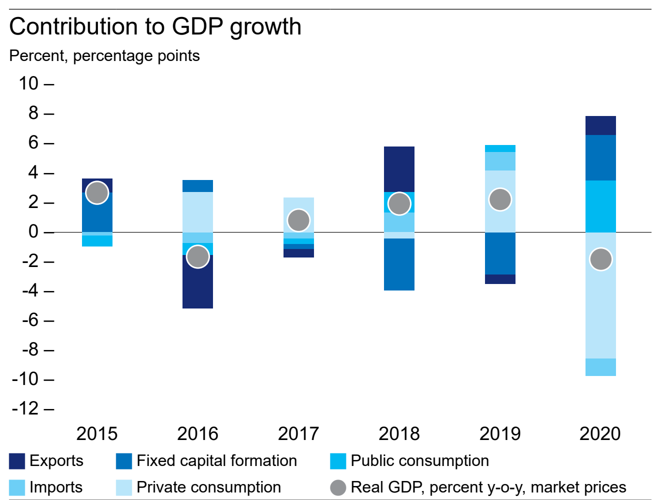
Timely government support helped shore up consumption and prevented an even larger contraction. The government launched a COVID-19 spending program and, in contrast to previous practice, this program was budgeted and combined with measures to enhance procurement and conduct independent audits of the spending. In addition, the Central Bank of Nigeria (CBN) provided ample support to agriculture and manufacturing. For instance, during the pandemic the agricultural sector received funding through the CBN Anchor Borrowers' Programme and its Agribusiness Small and Medium Enterprises Investment Scheme, the Nigeria Incentive-Based Risk Sharing System for Agricultural Lending, and other targeted programs. In 2020 Q4, oil prices and remittances

Figure 1.1. Services and oil led the contraction in 2020.



Source: NBS and World Bank estimates.

Figure 1.2. Private consumption remained quite stable.

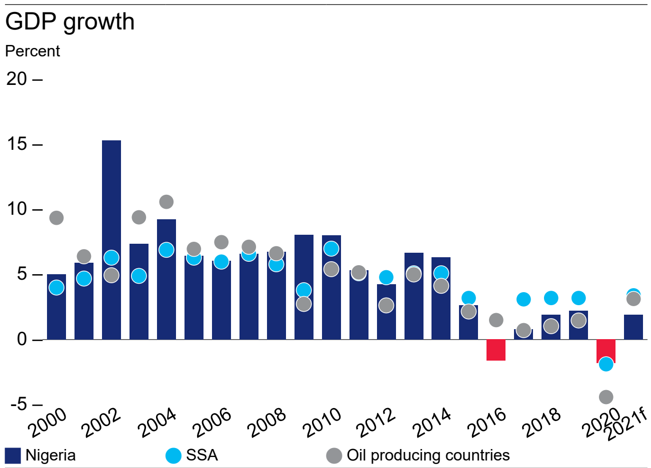


Source: NBS and World Bank estimates.

2 These issues were discussed in more detail in the December 2020 edition of the *Nigeria Development Update*.

rebounded, though not to their pre-pandemic levels. In this improving external context, the economy outperformed expectations, and by the end of the year the Nigerian economy was no longer in recession.

Figure 1.3. Nigeria's performance in 2021 is expected to be below the averages for Sub-Saharan Africa and for oil-producing countries.



Source: NBS, World Bank, and IMF estimates.

The positive growth in agriculture in 2020 was offset by severe contractions in services and the oil and nonoil sectors.

- **In 2020 agricultural output went up by 2.2 percent, slightly below 2019's 2.4 percent growth.** Crop production, which represents 90 percent of total agricultural production, drove the expansion, especially staple foods like rice, corn, beans, and cassava for domestic consumption. Agriculture was the sector least affected by COVID-19, and production expanded in the second half of the year. Its growth was supported by farmers returning to work after July and the movement of workers from services to agriculture.[3]

- **Oil production in 2020 contracted by 8.9 percent.** A tighter OPEC quota and the disruption of oil production in the first three quarters resulted in a combination of lower oil prices and smaller production volumes, which diminished revenues for both the public and the private sectors as the decline in oil output accelerated a contraction in services, investment, and credit growth. For the last 40 years, growth of Nigeria's GDP has closely tracked oil prices, and the economy continues to depend heavily on sales of crude oil. In 2019, for example, although oil represented just 10 percent of GDP, it accounted for over 80 percent of exports and more than 50 percent of consolidated revenues.

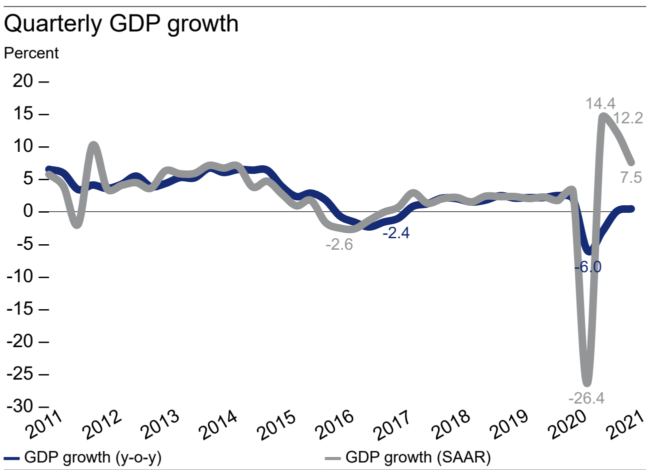
- **The nonoil industrial sector, including manufacturing and construction, shrank by 3.9 percent.** Lockdown measures and slowing economic activity caused a contraction in much of the nonoil industry except for cement production, processed foods, and chemical and pharmaceutical products. Even after firms had resumed operations, most nonoil industries were confronted by lower demand and excess inventories. Despite rising costs of inputs and a shortage of foreign exchange, in Q4 industrial activity recovered slightly, driven by construction and coinciding with the reopening of the economy, but at under 50 percent, capacity utilization was a full 15 percentage points (pp) below the 2019 average.

- **Services output declined by 2.2 percent in 2020, but trends across subsectors were uneven.** Information technology and communications expanded by 13.2 percent as household and firm consumption of data and broadcasting services spiked as a result of both mobility restrictions and precautionary behavior. Financial services grew by 9.4 percent as CBN monetary stimulus and lower interest rates drove expansion of credit to the private sector. Health services expanded by 2.2 percent due to higher COVID-related demand. However, all other services subsectors—which are the main sources of urban employment—contracted sharply. Trade declined by 8.5 percent, accommodation and food services by 17.8 percent, transportation and storage by 22.3 percent, and real estate by 9.2 percent. Moreover, total employment in services has fallen below pre-pandemic levels.

3 The movement of labor between sectors in Nigeria—and the role of agriculture as an employer of last resort—are described in Section 2: "The Continuing Effects of the COVID-19 Crisis on Work and Welfare."

Nigeria exited the recession in Q4 2020, but the pace of recovery remains subdued. In Q1 2021, GDP grew by 0.4 percent, the lowest GDP growth rate recorded in a first quarter since 2017 (-1.0 percent). When adjusted by seasonality, GDP grew by 7.5 percent in annualized terms, below the rates observed in Q4 and Q3 in 2020, indicating a deceleration. As in previous quarters, agriculture continued to be the most resilient sector in the economy and grew by 2.3 percent, led by higher crop production. Industrial activity also grew by 0.9 percent, due to a recovery in the production of cement and a more dynamic construction sector. In contrast, oil GDP declined by 2.2 percent, although at a lower pace than in the previous quarters (-13.4 percent on average in the last three quarters). Services declined by 0.4 percent due to the contraction of all its components but information and communication services (6.5 percent), real estate (1.8 percent), and health services (4.6 percent). The decline in services shows that in the first quarter the economy continued to be affected by the COVID-induced pandemic: transportation contracted by 21.9 percent, accommodation and food services by 4.6 percent, and trade by 2.4 percent.

Figure 1.4. The pace of quarterly GDP growth after the recession is subdued.



Source: CBN data and World Bank estimates.
Notes: TRAMO-SEATS methodology is used for seasonal adjustment.

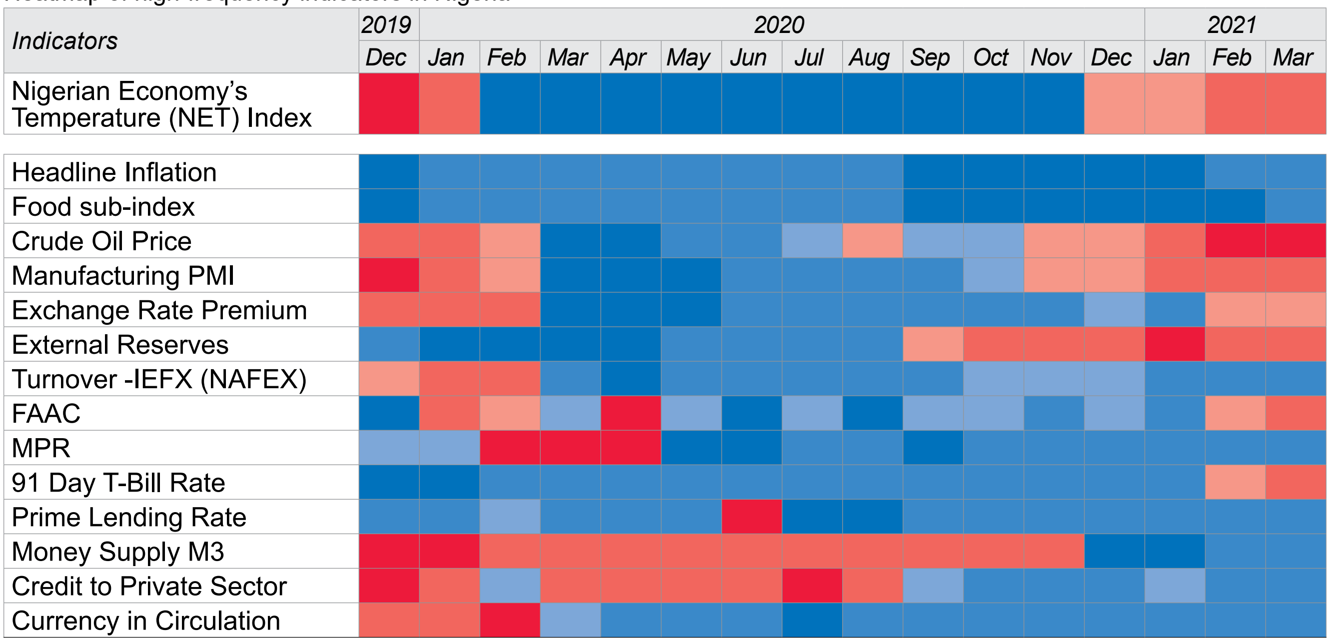
Increasing mobility and rebounding oil prices are supporting recovery, and while its magnitude remains uncertain, 2021 Q2 is expected to host a substantial rebound in economic activity. The projected rebound is based on assessment of high-frequency indicators in Nigeria, which suggest that nonoil GDP began to recover as early as mid-2020; it also considers statistical base effects. Last year, each week of suppressed economic activity represented a loss of about 0.2 pp of GDP growth, but fewer restrictions are expected in the second half of 2021. The Nigerian Purchasing Manager's Index for manufacturing moved into positive territory in Q1, suggesting a rebound in industrial activity during the first half of this year. If oil prices hold steady for the rest of the year, GDP growth in 2021 is expected to be among Nigeria's fastest in the last seven years.

Uncertainty about the trajectory and duration of the COVID-19 pandemic will continue to influence household consumption and private investment. The COVID-19 crisis is far from over, and while the second wave of cases appears to have peaked and receded, how the pandemic will evolve is still unclear. Indeed, the December 2020 Business Expectation Survey Report and the CBN Consumer Expectations Survey for Q4 of 2020 reveal high, though easing, uncertainty and risk aversion among consumers and firms. The rollout of vaccines will likely impact the pace of the recovery, but immunization in Nigeria is not expected to be widespread in 2021.

The Nigerian economy is expected to grow by 1.8 percent in 2021, though again there is high uncertainty about the outlook. The recovery would be driven by rises in oil exports and in domestic demand. However, Nigeria's recovery is expected to underperform those of other oil producers, and an unexpected shock to oil prices could threaten the modest growth projected. Although oil prices have increased, oil production is expected to remain relatively low at an average of 1.7 million barrels a day, down from an average of 1.9 million barrels between 2016 and 2019. GDP per capita is also projected to continue declining because the economy is forecast to grow more slowly

Figure 1.5. High-frequency indicators suggest that Nigeria's economy will recover in the first half of 2021.

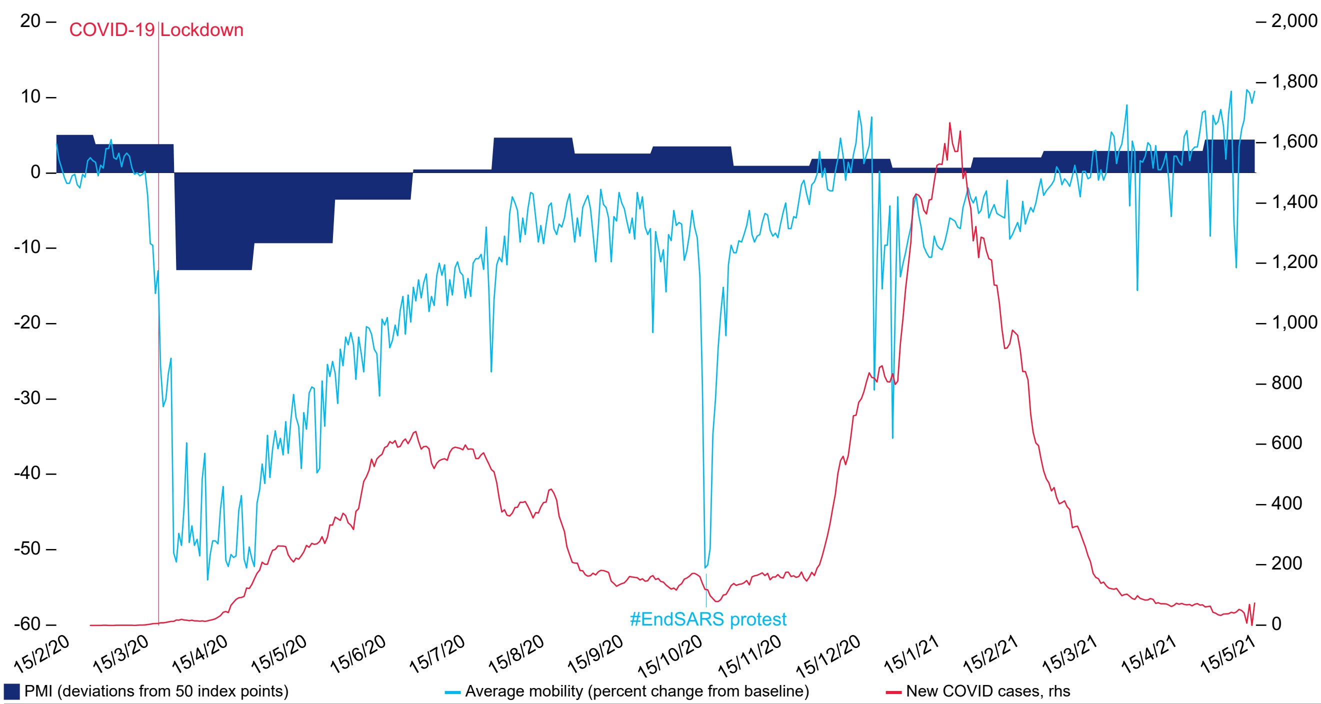
Heatmap of high-frequency indicators in Nigeria



Source: CBN, NBS, Financial Markets Dealers Quotation (FMDQ), Aboki FX, and World Bank estimates.
Notes: The NET Index is a synthetic indicator built to measure the temperature of the Nigerian economy based on a set of 14 high-frequency indicators - Headline inflation, Crude oil price, Manufacturing PMI, Treasury Bill rate, Diesel price, Petrol price, Currency in circulation, Exchange rate premium (Parallel - NAFEX) and M2. NET highly correlates with quarterly GDP. The index does not provide a point estimate, but a qualitative assessment of whether the overall economy is heating up (red) or cooling down (blue). Color coding is based on the deviations of standardized values of each indicator relative to a 5-years mean. Red represents growth above the mean (the economy is heating); darker shades of red represent stronger growth. Blue represents the opposite.

Figure 1.6. As mobility restrictions eased and the number of COVID-19 cases declined from its peak in early 2021, economic activity has begun to recover.

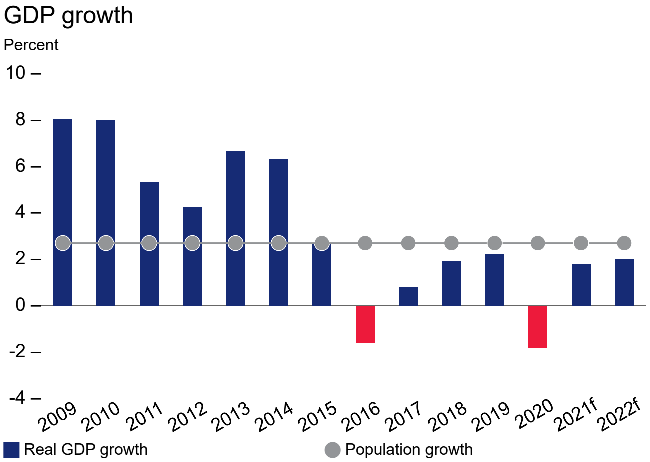
PMI index, average mobility, and new COVID-19 cases



Source: CBN, Stanbic, Google, and Nigerian authorities.

than the population. Moreover, high inflation and high unemployment exacerbate the macroeconomic risks, and activity in the tertiary sector will not fully normalize unless COVID-19 is contained. By the end of 2021, Nigeria's GDP is likely to approach its 2010 level, thus reversing a full decade of economic growth.

Figure 1.7. Growth in GDP per capita is expected to remain subdued in 2021.



Source: NBS and World Bank estimates.

Nigeria's economy continues to be acutely vulnerable to both external and domestic shocks. When the pandemic materialized, the Nigerian economy was still recovering from the 2016 recession. Multiple foreign-exchange rates, trade restrictions, and CBN financing of the public deficit had worsened the business environment, compounding longstanding development challenges related to mobilizing public revenue, building human capital, and a variety of concerns about infrastructure, and governance. Although the authorities carried out bold reforms in 2021, further action is necessary to address Nigeria's structural challenges and accelerate GDP growth in the short and medium term. The government has an opportunity to accelerate the recovery by deepening recent reforms that focus on enabling private investment. Even in a best-case scenario for the global economy, an appropriate domestic policy response will be crucial to lay the foundation for broad-based and sustainable post-crisis recovery.

Despite the projected recovery, the 2020 recession is expected to have lasting effects on poor and vulnerable households. As explained in Section 2 of this report, the recession disproportionately impacted Nigeria's poorest households; workers were forced to move from higher- to lower-productivity sectors; and economic uncertainty and food insecurity were heightened even among workers who returned to regular employment. Questions about income are limiting the investments households are willing to make in education and health services, undermining prospects for long-term GDP growth. In total, the pandemic-induced recession of 2020 is estimated to have increased poverty in Nigeria.

Box 1.1. Rising insecurity poses severe economic risks.

Nigeria faces intensifying conflict and insecurity on multiple fronts. In 2020, Nigeria was added to the World Bank's List of Fragile and Conflict-Affected Situations due to repeated instances of civil unrest, rising crime rates, intercommunity violence in central Nigeria, and the ongoing Boko Haram insurgency in the northeast, among other factors. Moreover, the situation has been worsening over the last years. The Armed Conflict and Location Event Data (ACLED) Project estimates that the number of conflict events in Nigeria increased by 150 percent between 2018 and 2020, and the number of such events between January and April 2021 has already exceeded the total for 2018. In April 2021, Amnesty International estimated that the mass kidnappings of schoolchildren by Boko Haram, which have resulted in hundreds of children being killed, raped, forced into "marriages" with insurgents, or compelled to join the group, have resulted in the closure of over 600 schools, with educational losses for tens of thousands of children. Conflicts between farmers and

Box 1.1 continued

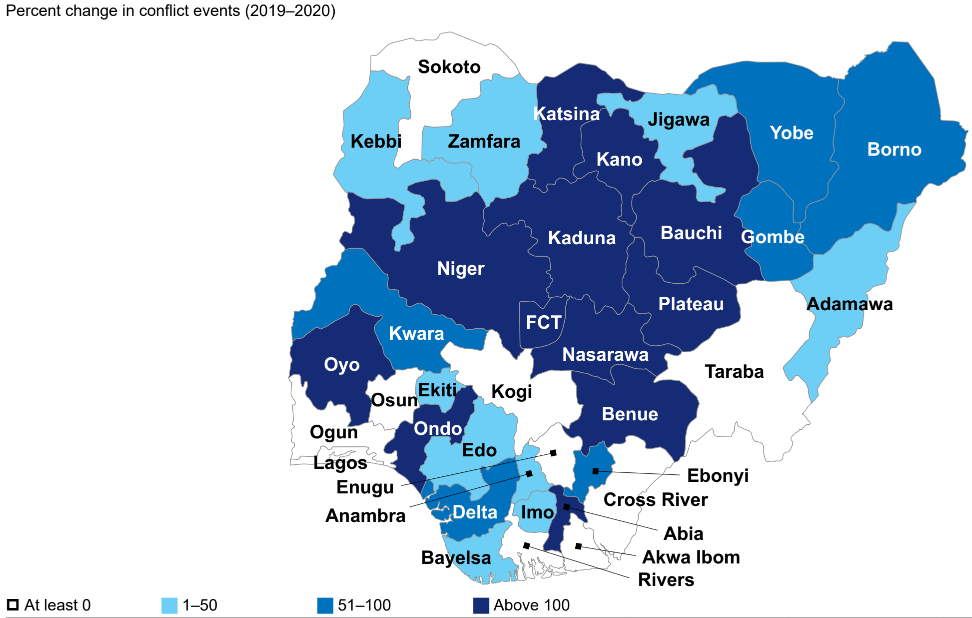
pastoralists, which first emerged in the middle belt, have spread to other parts of the country, and escalated to armed banditry, with kidnapping for ransom becoming increasingly common.

The COVID-19 pandemic has aggravated several key preexisting insecurity challenges in Nigeria. The initial lockdown during the second quarter of 2020 and the subsequent economic slowdown led to widespread unemployment and underemployment. The August 2020 Nigeria COVID-19 National Longitudinal Phone Survey (NLPS) revealed that even though many Nigerians had returned to work after the early phase of the crisis, most households remained in an economically precarious situation, with more than two-thirds of respondents reporting lower incomes than in the previous year. High and rising inflation has also exacerbated economic insecurity. These factors have greatly incentivized crime as a means of earning income and made participation in an insurgent movement a more viable alternative to conventional employment.

Figure B1.1.1. Conflict and violence in Nigeria have intensified.

Change in conflict events in Nigeria (2019–2020)

Percent change in conflict events (2019–2020)



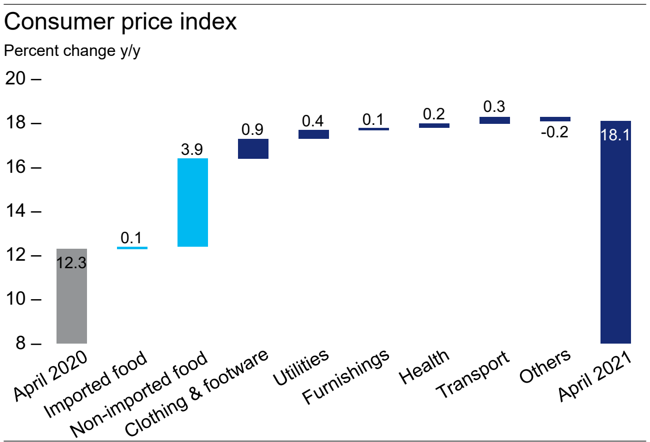
Source: World Bank estimates based on ACLED.

Instability and violence are also slowing economic growth and job creation—resulting in a vicious cycle. Insecurity is driving internal displacement and crippling the economic activities of vulnerable communities. Clashes between farmers and pastoralists have severely damaged agricultural output in north-central Nigeria in recent years, contributing to rising food insecurity and food-price inflation. The latest poverty data for Nigeria (2019) indicates that the northeast and northwest of the country, which have the highest incidences of conflict events, also have the highest poverty rates. Insecurity is a powerful disincentive to both domestic and foreign investment, compounding the negative effect of weak governance and poor infrastructure. Moreover, the growth of a lucrative criminal industry centered on kidnapping for ransom is presenting appealing opportunities for young workers, especially those facing dim prospects in a weak and unstable labor market.

Prices: Inflationary pressures are becoming more difficult to manage

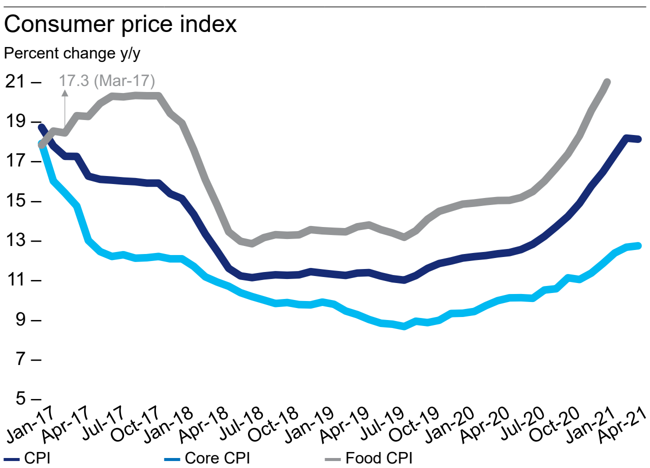
The rate of inflation rose steadily throughout 2020 and by March 2021 had reached a four-year high (Figure 1.8). The rise has been driven primarily by surging food prices (Figure 1.9). By April 2021, the consumer price index was up 18.1 percent, year-on-year (y/y); the increases were comparable in urban centers (18.7 percent) and rural areas (17.6 percent). The composite food index reached 22.7 percent, slightly below the 22.9 percent recorded in March 2021 (the highest rate in 15 years), due to higher prices for such staples as bread and cereals, potatoes, yams and other tubers, meat, fish, fruits, and oils and fats. COVID-19 restrictions prevented seasonal migration during harvest time, and the resultant disruption of supply chains was compounded by security issues, border closures, and limited access to markets. The surges in domestic food prices accounted for almost 70 percent of the total 12-month increase in inflation. The general increase in food prices masks both the price spikes for certain staple goods and significant disparities between regions (Figure 1.10 and Figure 1.11). The core inflation rate also increased, reaching 12.7 percent in April 2021, led by rising prices for passenger air and road transportation, medical services, pharmaceuticals, and motor vehicles.

Figure 1.8. Food prices have driven the surge in inflation over the past 12 months.



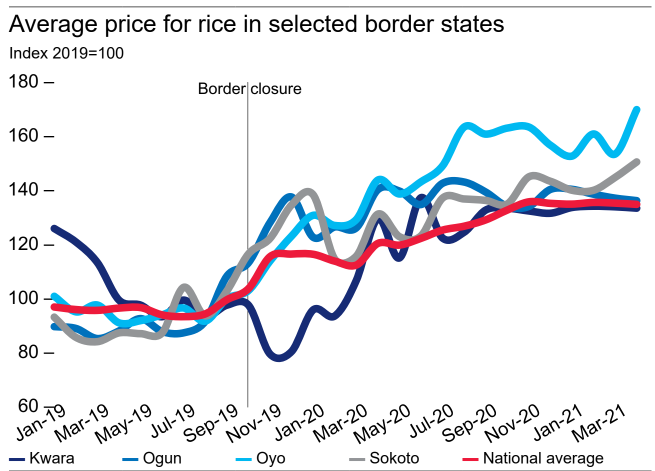
Source: NBS data and World Bank estimates.

Figure 1.9. In March-April, headline inflation rate has reached its highest level since March 2017.



Source: NBS data and World Bank estimates.

Figure 1.10. Prices for staple goods have gone up more in border states.

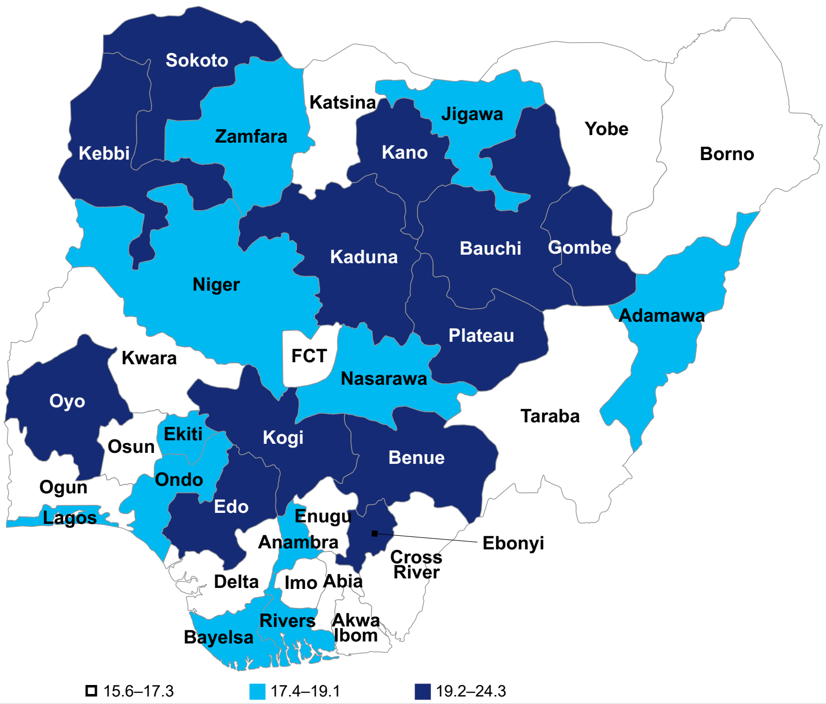


Source: NBS data and World Bank estimates.

Figure 1.11. Price increases have been unevenly distributed across states.

Inflation rates across Nigerian states

April headline inflation, percent



Source: NBS data and World Bank estimates.

Inflationary pressures are expected to persist for the next six months, and for 2021 inflation is expected to exceed 16 percent. Even if domestic food production increases and supply and distribution constraints are eased, a combination of exchange-rate management problems, shortages of hard currency, border closures, expansionary monetary policy, and the monetary funding of the fiscal deficit will continue to generate inflation pressures. In the first quarter of 2021 inflation accelerated in many Sub-Saharan African countries; however, other countries with high inflation rates, such as Zambia and Zimbabwe, have tightened their monetary stance to mitigate the pass-through effect of exchange-rate depreciation and to anchor inflationary expectations. In Nigeria, absence of a credible anchor has caused the inflationary expectations of both professional forecasters and businesses to spike. In 2020, Nigeria's inflation rate was the seventh highest in Sub-Saharan Africa, but by the end of 2021 it is expected to rise to fifth highest, behind only Zimbabwe, Zambia, South Sudan, and Angola.

In 2021 elevated inflation rates are expected to further exacerbate poverty and dampen growth. As discussed in Section 2, high inflation is expected to frustrate Nigeria's economic recovery and erode the purchasing power of households, which will increase both the poverty rate and the number of people living below the poverty line. Prices trending upward in a weak economic recovery will limit CBN options for alleviating inflationary pressures. With firms and consumers both expecting inflation to remain high in the next 12 months, even with conventional inflation targeting monetary policy would be of little effect. In addition to worsening poverty and undermining development outcomes, a slow recovery with few jobs created could erode investor confidence in the capacity of the authorities to sustain adequate macroeconomic activity to support the post-pandemic recovery.

Box 1.2. Drivers of inflation in Nigeria in 2020–21.

The upswing in inflation rates is proving especially hard to control because inflationary pressures are being generated by multiple demand and supply shocks. The pressures are compounded by policy factors related to containment of the pandemic and to the spending necessary to counter its effects. In addition to supply-side factors affecting food production and marketing, lack of a credible nominal anchor on the demand side is buttressing the price-shocks uncertainty that firms and consumers face when making investment and consumption decisions. The month-to-month pattern of price changes also differs from the patterns seen in previous inflationary episodes, as lockdown prevention of seasonal migration meant that food-price inflation in 2020 was disconnected from the agricultural seasonality that typically drives food prices.

Exogenous factors:

- **Insecurity and conflict in food-producing areas,** especially northern and central Nigeria, have destroyed crops and forced farmers to abandon their land. Reduced food production exerts a cost-push force on prices, especially in conflict-affected areas and regions with limited transportation and storage infrastructure.

- **The COVID-19 crisis and associated containment measures** have disrupted production and supply chains while preventing seasonal migration during harvest time.

Policy factors:

- **Trade restrictions,** including the closing of land borders starting in August 2019, have contributed to rising prices for food and consumer goods. Food prices are especially sensitive to trade restrictions; domestic supply cannot adjust quickly to offset a decline in imports.

- **Foreign currency restrictions** are further pushing up prices of food and agricultural inputs like fertilizer. Imports of over 40 goods, including many staple foods, are currently ineligible for foreign exchange (FX) through formal windows.

- **Nigeria's exchange rate management** has contributed to the rise in inflation because currently there is in effect a cap on the price of foreign currency (nominal exchange rate) and its supply (the FX supply available in the IEFX and other windows where the central bank intervenes) in the formal markets. Even though the nominal IEFX rate has been depreciating, which has helped to alleviate inflationary pressures, it has not been doing so fast enough to equilibrate the FX market. When there is a divergence between the official/IEFX rate and the parallel FX rate, the parallel rate is the one most associated with food price dynamics. Unable to access FX in the IEFX window, businesses seek it through the parallel market and other alternative sources and factor in the parallel rate in business decisions, so that it eventually passes through to market prices for goods and services.

Box 1.2 continued

- **Nigeria's monetary policy** is not consistent with prioritizing efforts to curb inflation. The tools that CBN use to achieve its policy goals sometimes contradict each other. For example, keeping the exchange rate de facto stable, promoting growth, and containing inflation. This weakens effectiveness of monetary transmission mechanisms to contain demand inflationary pressures.

- **Expansionary monetary policy and financing of the fiscal deficit** add more upward pressure on inflation rates. The y/y growth rate of M2 jumped from 6.3 percent in 2019 to 31.9 percent in 2020 as the CBN played a major role in funding a widening government deficit. This coupled with a decline in the stock of open-market securities used to control the system's liquidity. The rapid expansion of M2 occurred in a context of contracting economic activity and minimal growth in credit to the private sector. Since June 2020, the growth in CBN loans to the federal government have accounted for 48 percent of the increase in M2.

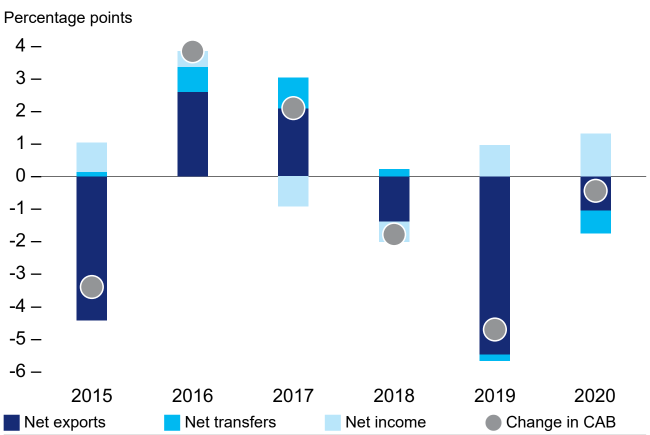
The External Sector: Nigeria's outlook improves as oil prices recover

The COVID-19 crisis intensified pressure on Nigeria's balance of payments (BoP). In 2020 the current account deficit (CAD) widened from 3.7 percent of GDP in 2019 to 4.2 percent as oil exports and remittances—the two largest current account inflows—together fell by almost 30 percent (Box 1.1 describes Nigeria's longstanding vulnerability to oil price volatility). Total exports plunged by 43 percent, but imports also fell, by 28 percent, reflecting pandemic-related economic disruptions, slack demand, and a shortage of foreign exchange (FX). Due to the substantial drop in imports, Nigeria's CAD did not widen as dramatically as those of other oil major exporters, such as Libya, Iraq, Kuwait, and Sudan, but the crisis had a dampening effect on capital inflows, especially portfolio investment. Throughout 2020, high global risk aversion, uncertainty about Nigeria's foreign exchange policies, and a low-interest-rate regime resulted in net portfolio outflows. Meanwhile, foreign direct investment (FDI) to Nigeria, already low compared to peer countries, shrank by 25 percent.

The CAD and the portfolio outflows put intense pressure on the naira, but the impact on external reserves was contained due to the CBN's FX management strategy. Nigeria's stock of gross external reserves initially declined at the outset of the pandemic but then held relatively steady for the rest of the year, partly due to the CBN's exchange rate management strategy and partly to support from the International Monetary Fund. By yearend-2020, gross FX reserves were US$35 billion, equivalent to 5.9 months of imports. Unwilling to allow substantial depletion of the external reserves because of higher foreign outflows, the CBN deployed its FX demand-management strategies by, e.g., continuing to exclude various items from the

Figure 1.12. Falling oil exports and foreign remittances widened the CAD in 2020…

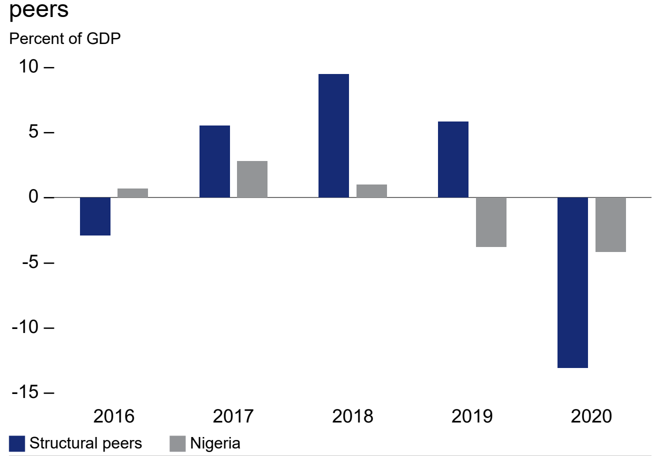
Contribution to changes in Nigeria's Current-Account Balance



Source: CBN

Figure 1.13. …but a steep decline in imports kept Nigeria's deficit narrower than those of its structural peers.

Current-Account Balance as a share of GDP, Nigeria and peers



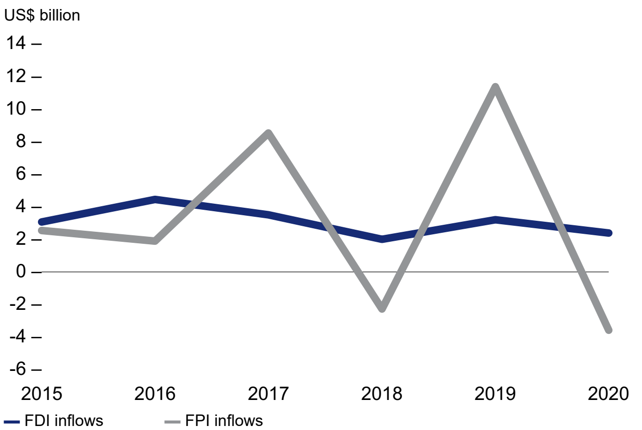
Source: CBN and World Bank estimates.
Note: Nigeria's structural peers are countries in which crude oil exports exceed 85 percent of total merchandise exports. Among them are Azerbaijan, Iraq, Kuwait, Libya, Qatar, and Sudan.

FX market (now 45 items) and temporarily interrupting the supply of FX to *Bureaux de Change* (BDCs) and the Investors' & Exporters' FX (IEFX) window. The CBN resumed IEFX sales in September but barred commercial banks from processing FX purchases for transactions routed through buying agents or other third parties. As a result, demand for FX rose in the parallel market, which eventually led to depreciation of the parallel market rate.

In 2021 the CAD is expected to narrow to about 0.5 percent of GDP as oil prices rebound and the global economy recovers. Since January 2021, commodity prices have risen substantially; in mid-March oil prices surged by 30 percent, to US$68 per barrel. The recovery of commodity prices reflects resurgent global demand, driven in part by robust fiscal stimulus in the United States and other advanced economies, as well as supply-side factors, especially the recent OPEC+ production agreements. Inbound remittances are also expected to recover as rising vaccination rates and effective containment measures strengthen foreign labor markets.

Figure 1.14. Portfolio outflows and contracting FDI intensified pressure on the balance of payments.

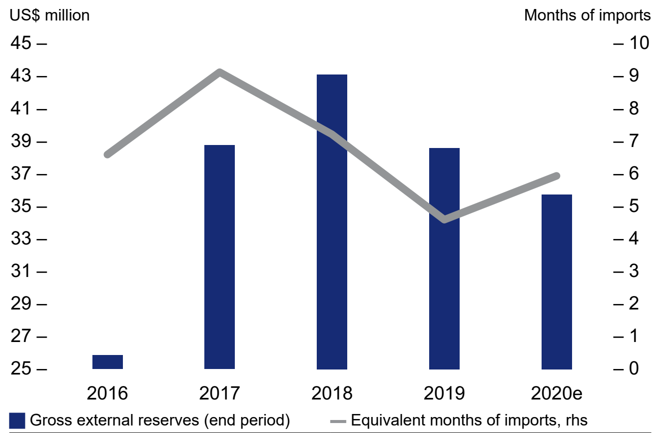
Foreign Direct Investment and Foreign Portfolio Investment inflows



Source: CBN.

Figure 1.15. The CBN continued to apply demand-management strategies to preserve its FX reserves.

Foreign exchange reserves



Source: CBN.

Box 1.3. Accelerating export diversification to relieve Nigeria's external volatility.

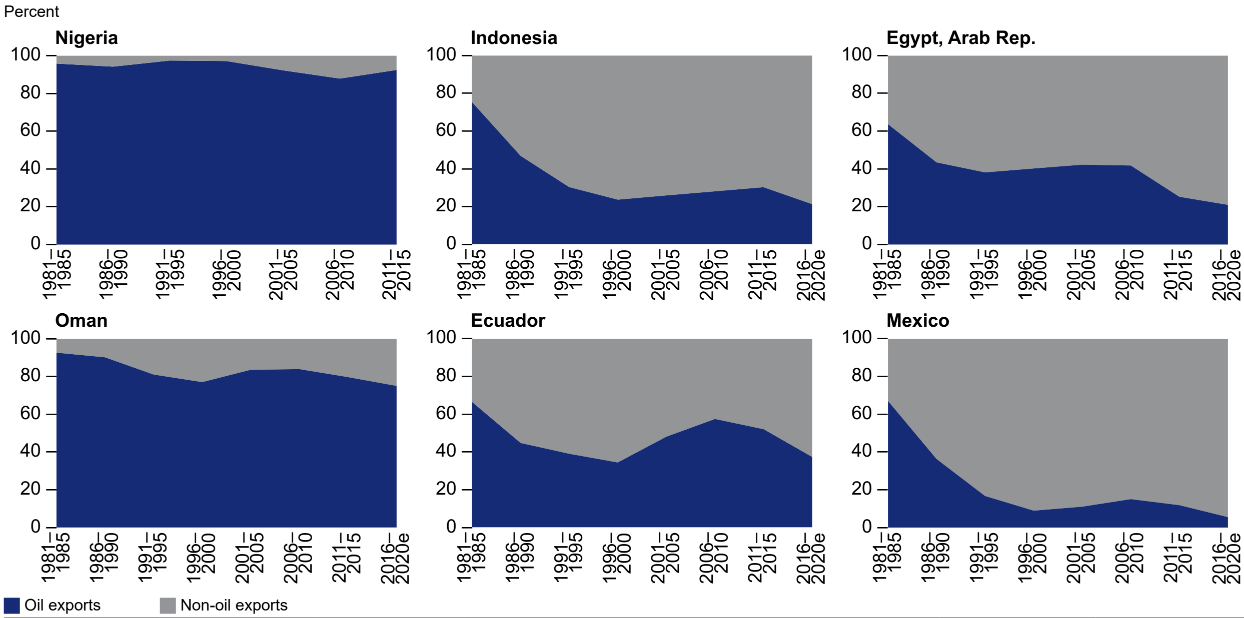
Since the 1970s, Nigeria's economy has become heavily focused on oil production, and formerly robust nonoil sectors have atrophied. Previously, Nigeria exported a broad range of primary commodities, including a substantial share of the world's cocoa, palm oil, groundnuts, cotton, hides, skins, rubber, and coffee, as well as coal, tin, and other minerals. However, the discovery of commercial-scale oil reserves in 1956 spurred a surge in the 1960s of foreign investments in Nigeria's oil industry; within a decade Nigeria's daily oil output had reached 2.3 million barrels. Oil exports drove steady appreciation of the real effective exchange rate, eroding the competitiveness of the nonoil sectors. Agricultural exports slumped, and oil expanded from an average of 12 percent of total exports in the early 1960s to 95 percent 20 years later.

Box 1.3 continued

Over the last several decades, oil has consistently represented more than 90 percent of Nigeria's total exports, resulting in a high degree of external volatility. In 2017, Nigeria had the world's 9th most concentrated export structure (UNCTAD 2017); and its overwhelming dependence on oil exports has left the terms of trade and balance of payments highly vulnerable to shocks. Nigeria has tried both fixed and managed-float exchange-rate regimes, and repeated oil-price-driven boom/bust cycles have forced the authorities to make large exchange-rate adjustments or deal with erosion of external reserves and depreciation of the naira. During the 2008/09 global financial crisis, the global price of crude oil fell by over 70 percent; then, from mid-2014 through early 2016, global crude prices again plunged by 70 percent. In 2020, the COVID-19 pandemic set off a worldwide economic slowdown that caused the global price of oil to once again to plummet by 70 percent between January and April. In each cycle, faltering oil exports weakened confidence in the economy, resulting in diminished or even negative net capital inflows, which intensified pressure on the naira, further discouraged investment, and slowed growth.

Figure B1.2.1. Over the last several decades, Nigeria has remained far more dependent on oil exports than the average of other oil-rich countries.

Relative shares of oil and nonoil exports, Nigeria and comparators



Source: World Bank estimates.

Despite repeatedly experiencing the adverse consequences of the lack of diversity in its export base, Nigeria has made little progress in reducing its dependence on oil. Successive national development plans, most recently the 2017–20 Economic Recovery & Growth Plan (ERGP),[1] have stressed the need to diversify exports and fiscal revenues away from the oil sector, but these efforts have met with little success. As

1 The ERGP identified six priority economic sectors: agriculture, manufacturing, solid minerals, services, construction and real estate, and oil and gas. In addition, the Zero Oil Initiative of the National Export Promotion Council and the Ministry of Budget and National Planning is designed to boost the supply of foreign exchange from nonoil sectors by encouraging the growth of 11 export products: cotton, rice, leather, gold, soya, sugar, cocoa, petrochemicals and fertilizer, palm oil, rubber, and cement.

Box 1.3 continued

of 2017, Nigeria's score on the UNCTAD export concentration index[2] was more than twice that of regional comparators like Uganda and Benin and global comparators like the United Arab Emirates and Oman. Uganda reduced its dependence on coffee exports by broadening its portfolio of manufactured goods, and Benin reduced its dependence on cotton by diversifying into commodities like oil, gas, and gold. The United Arab Emirates and Oman have made enormous efforts to diversify away from hydrocarbons by fostering the growth of manufacturing and high-value services.

Nigeria can break the cycle of oil-induced volatility by diversifying its export basket. In addition to increasing macroeconomic vulnerability, international experience shows that an excessive focus on extractive industries and other sectors with limited scope for productivity gains can slow employment creation and income growth. Thus, diversification into manufacturing, commercial agriculture, and knowledge-intensive services can help stabilize the macroeconomy while stimulating structural transformation, fostering the creation of high-quality jobs, and building new competitive advantages. Numerous World Bank analyses have highlighted Nigeria's potential to accelerate growth and promote export diversification through increased private investment in sectors like agribusiness, mining, manufacturing, and the digital economy. Agribusiness, for example, could prove transformative for Nigeria, especially in conflict-afflicted areas like the North East. Furthermore, given robust demand for raw materials and intermediate goods, the production of chemicals, leather, and construction materials could boost exports, accelerate job creation, and facilitate structural transformation by absorbing excess labor from the agricultural sector.

2 Export concentration index scores range from 1, when a single product accounts for all exports, to 0, indicating that exports are distributed across an infinite range of products. In 2017, Nigeria's index score was 0.8; the scores for comparator countries were below 0.4.

Monetary Policy and Exchange Rate Management: Adjustments remain critical to Nigeria's recovery

Since 2020, the CBN has focused more on funding the government and easing financial conditions to soften the impact of the COVID-19 crisis than on stabilizing prices. Although inflation accelerated in 2020 and further in 2021, led by rising food prices, the CBN progressively lowered the monetary policy rate (MPR), citing—as its rationale—the need to support economic recovery. The MPR has been held at 11.5 percent since September, and the CBN has kept the cash reserve requirement at 27.5 percent and the liquidity ratio at 30 percent since January 2020. The CBN has also expanded its interventions to mitigate the pandemic's economic impact on households and businesses: (i) it lowered interest rates on all its subsidized interventions, (ii) suspended interest payments on borrowed funds under these interventions, and (iii) introduced at least five new lending facilities (Figure 1.18). It also directly financed one-third of the federal government's fiscal deficit in 2020 through measures that included extensive use of overdrafts exceeding the CBN charter's statutory limit of 5 percent of the previous year's government revenue. Supporting renewed growth was also part of the CBN's official explanation for these policy actions.

The CBN limited its use of open-market operations (OMO) bills to manage liquidity and shore up the value of the naira, slashing its use of them from the first quarter of 2020 through the first quarter of 2021. After the 2015 oil-price crash, the CBN opened the market for OMO securities to foreign portfolio investors, who ultimately held up to one-third of the bills to take advantage of their high yields. In October 2019, the CBN allowed only banks and foreign investors to see OMO bills, excluding domestic institutional investors and the public. When the collapse of yields on OMO securities drove repatriation of returns by foreign portfolio investors, pressure on the FX market intensified. In response, in 2020 the CBN cut OMO issuances by 70 percent and in the first three months of 2021 by almost 60 percent.

Prolonging the CBN's accommodative monetary policy would risk further entrenching high inflation and exacerbating financial outflows. Monetary policy may remain accommodative in the near term, but the authorities should be ready to tighten the CBN's stance if pressure on the external accounts intensifies as EU and US bond rates continue to rise and inflation accelerates. The headline inflation rate is currently far above the upper limit of the CBN's 6–9 percent target band (see the Inflation section).

As exchange rate stability continues to be a key policy objective, the CBN has pursued this by continuing to manage FX demand and employing other means to strengthen the value of the naira. More recently, it has taken further steps to unify the exchange rates**.** Although the CBN devalued the official exchange rate by 15 percent in March 2020 and by another 5 percent in August while also allowing the Importers' and Exporters' Foreign Exchange (IEFX) rate to depreciate, it was hesitant to allow further slides in the rates. However, its limited interventions in the IEFX window, which reduced the FX supply, and its restriction on access to FX for 45 items pushed up demand in the parallel market, where an estimated 90 percent of manufacturers' current FX needs are sourced. Significant spreads between the official, the IEFX, and the parallel exchange rate persisted throughout 2020[4] and as of April 2021, the spread between the official and the IEFX rate was estimated at 8 percent and between the IEFX and the parallel rate, reached 18 percent (the spread between the

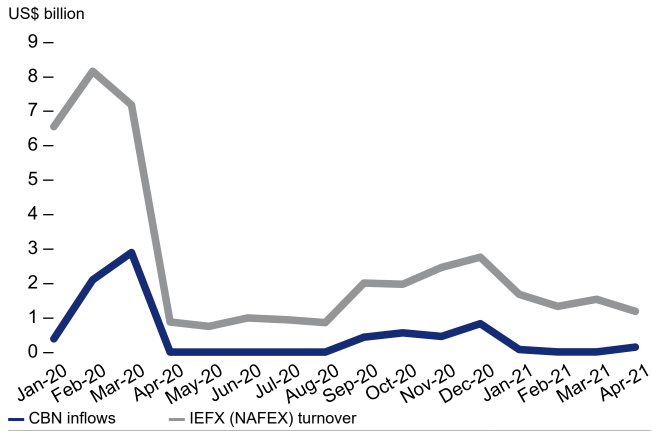
4 Between March and December 2020, the average spread between the official and the IEFX rates was 5 percent and between the IEFX and the parallel rate was 19 percent; the average spread between the official and the parallel rate was 24 percent

official and the parallel rate was 27 percent). The way the exchange rate was managed limited access to FX and thus adversely affected investor confidence and investment appetite. In May 2021, the CBN formally took concrete steps towards rates unification between the official and IEFX rates. However, the IEFX rate continues to be managed and is not fully reflective of market forces. Furthermore, there remains a 20 percent premium between this unified rate and the parallel market rate. The two-month naira-for-dollars scheme introduced by the CBN in March 2021 to serve as an incentive for increased remittance inflows through formal channels was extended indefinitely in May and was preceded by regulatory directives in December 2020—that mandated all licensed operators to pay remittances in dollars. While this may indeed encourage the use of the formal channels, it is not clear that incentive payments will increase remittances to the country.

While the CBN has taken steps towards operationalizing unification of exchange rates, greater flexibility will be necessary to support the recovery. Until oil companies are allowed to sell FX receipts to IEFX bank participants, CBN would still have an important role to play as supplier of FX. In this scenario, participating banks in the FX market will start to play an expanded role that goes beyond just executing buy/sell orders of its clients to start acting as market makers, meaning that they start to quote two-way prices buying and selling on its own behalf and carrying a stock of FX. With increased flexibility, the CBN could start intervening only to smooth large fluctuations, and work toward ensuring a single, market-driven rate. Keeping market stakeholders fully informed of such efforts would help attract both domestic and foreign investment. The right mix of exchange-rate flexibility and expanded supply (e.g., through banks and FX agents) would enable the FX market to efficiently allocate resources, which would allow the CBN to focus its interventions on smoothing large and disruptive FX fluctuations.

Figure 1.16. CBN FX sales in the IEFX window have been limited.

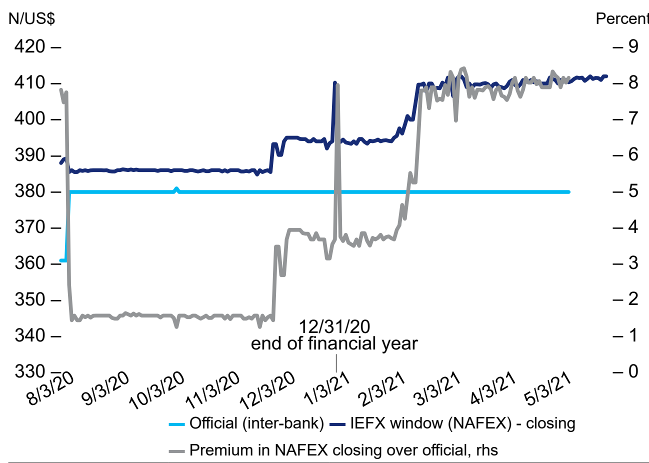
CBN IEFX interventions and market turnover



Source: FMDQ.

Figure 1.17. The premium between the official and the IEFX rates widened before the formal move towards unification of both rates in May 2021.

FX market rates



Sources: CBN and FMDQ.

Figure 1.18. The CBN intensified its development finance interventions in 2020 in response to the COVID-19 crisis.

Timeline of new CBN interventions, 2020

March 2020	*May 2020*	*August 2020*	*September 2020*
₦50 billion targeted facility	Healthcare research and development grant	National gas expansion project	Family homes financing initiative
Purpose: to cushion the effect of COVID-19 pandemic on households and SMEs. 1. Households: • Term loan: Maximum of ₦3 million at 5 percent p.a. • Tenor: Maximum of 3 years with at least one-year moratorium 2. SMEs: • Term loan: Maximum of ₦25 million at 5 percent p.a. • Tenor: Maximum of 3 years with at least one-year moratorium	*Purpose:* to help strengthen the public healthcare system with innovative financing of research and development in new and improved drugs, vaccines and diagnostics of infectious diseases. 1. Research activities: • Maximum of ₦50 million • Timeframe: Not more than 2 years from the date of release of fund 2. Development/ manufacturing activities: • Maximum of ₦500 million • Timeframe: Not more than 1 year from the date of release of fund	*Purpose:* to improve access to finance for private sector investments in domestic gas value chain. 1. Manufacturers, processors, wholesale distributors: • Term loan: Not more than ₦10 billion per obligor, at not more than 5 percent p.a. up to Feb. 2021, and thereafter 9 percent p.a. • Tenor: 10 years with maximum of 2-year moratorium on principal only 2. SMEs, retail distributors, households: • Term loan: ₦50 million per obligor, at not more than 5 percent p.a. up to Feb. 2021, and thereafter 9 percent p.a. • Tenor: 5 years with maximum of 2-year moratorium on principal only	*Purpose:* a construction finance facility to implement the federal government's social housing programme. • Term loan: Cumulative maximum limit of ₦200 billion at not more than 5 percent p.a. • Tenor: 3 years
₦100 billion credit support for health sector			Solar connection facility
Purpose: to cushion the effect of COVID-19 pandemic on the economy. • Term loan: ₦2 billion per obligor, at not more than 5 percent p.a. up to Feb. 2021, and thereafter 9 percent p.a. • Tenor: Maximum of 10 years with a 2-year moratorium on principal			*Purpose:* to expand energy access to 25 million individuals. 1. Upstream participants: • Term loan: Maximum of 70 percent of project cost, at maximum of 9 percent p.a. • Tenor: Maximum of 10 years 2. Downstream participants (mini grid developers: • Term loan: Maximum of 70 percent of project cost, at maximum of 10 percent p.a. • Tenor: Up to 7 years 3. Home solar systems retailers and distributors: • Term loan: Maximum limit of ₦500, at 10 percent p.a. • Tenor: Up to 5 years

Source: CBN.

The Financial Sector: Nigeria avoided a credit crunch but the banking system is showing signs of stress

Despite the harsh operating environment, the banking system has proven generally resilient, but signs of stress are beginning to appear. The financial system must continue to deal with the COVID-19 crisis, rising inflation, the collapse of crude oil prices in 2020 H1, a surge in unemployment, and a protracted disruption in the supply of foreign exchange. In comparable countries, this combination of shocks has caused bank balance sheets to rapidly deteriorate, yet in Nigeria in February 2021 the nonperforming loan (NPL) ratio was still 6.3 percent, largely unchanged from a year earlier. The system is also still well-capitalized, with a capital adequacy ratio (CAR) of 15.2 percent in February 2021, up about 30 basis points (bps) from a year earlier.[5] Dollar funding tightened abruptly in 2020, but the system's overall liquidity position appears comfortable; in February the 40.5 percent liquidity ratio was well above the prudential minimum.[6] Importantly, access to international capital market has opened up for Nigerian banks, and two of them placed 5-year Eurobonds raising US$650 million in recent months which would help ease FX liquidity strains and extend funding maturities. It is expected that more financial intermediaries in Nigeria will tap international markets to issue foreign currency denominated securities or syndicated foreign currency denominated financing in order to partially meet the growing foreign currency needs as well as upcoming foreign currency denominated maturities.

Thus far, the CBN's policy initiatives and development-finance interventions have helped prevent a severe credit crunch in the private sector. The CBN cut its monetary policy rate by 100 bps in May 2020 and by another 100 bps in September. Regulatory forbearance for the restructuring of pandemic-affected exposures is now in effect until March 2022. The CBN has softened the terms of its development-finance interventions, and the new terms have been extended through March 2022; it has also launched a range of new development-finance initiatives at subsidized interest rates in an attempt to ease the impact of COVID-19 on households and SMEs. It is also helping pharmaceutical companies, health practitioners, and SMEs respond to the pandemic by injecting up to ₦400 billion in loanable funds.[7] The new funding is equivalent to about 2 percent of private sector bank credit.

The regulatory forbearance granted by the CBN for restructuring loans impacted by COVID-19 was crucial to keep the banking system sound, but in the next few quarters NPLs are expected to rise. While the average NPL ratio may be slow to respond to recent disruptions, sectors with higher loan dollarization and those directly exposed to crude-oil prices, such as oil and gas and construction, have started to see a decline in loan quality.[8] In other sectors the impact of the crude-oil price shock on loan quality will take several quarters to fully register. Meanwhile, forbearance is expected to be withdrawn, some corporate business models will cease to be financially viable, and with growth prospects for

5 Banks with international authorization licenses have a minimum CAR requirement of 15 percent—with a 1 percentage point add-on for domestically systemic banks; banks with national authorization licenses have a minimum CAR requirement of 10 percent.

6 Between March 31 and September 30, 2020, the system's dollar funding declined by some US$2.6 billion (₦986 billion), with similar losses in deposits and loans; and total foreign-currency-denominated liabilities as a share of total banking system liabilities dropped from 24.3 to 20.4 percent.

7 ₦100 billion is available from the Health Sector Intervention Facility and ₦300 billion from the Targeted Credit Facility. In November 2020, disbursements were ₦61 billion from the former and ₦149 billion from the latter. The initial funding for the Targeted Facility was ₦50 billion which was raised three times, reaching ₦300 billion in March 2021.

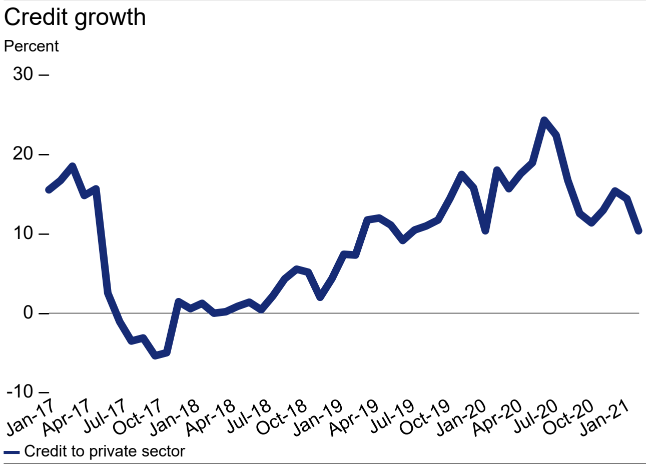
8 For example, at year end-2020 the NPL ratio was 17.7 percent in the construction sector, up 567 bps year on year, and 7.9 percent in oil and gas (upstream and downstream), up 306 bps. According to the NBS, in April 2019 the loan-dollarization ratio in construction was 23 percent and in oil and gas 60 percent respectively, in April 2019 (NBS e-library—"Selected Banking Sector Data: Sectoral Breakdown of Credit, ePayment Channels and Staff Strength (Q1 2019)".

2021 more muted, the repayment capacity of borrowers would be under pressure, which is also likely to affect loan quality. Profitability is falling due to, among other factors, compression of net interest margins, a dramatic slowdown in credit origination, and rising impairment charges. Several banks, both large and small, now have capital cushions that are only slightly above the minimum requirements. Corporate lending exposures account for most of the credit portfolio and are concentrated among the largest borrowers; as their leverage increases, so does the risk associated with corporate lending exposures.[9] In this context, latent material credit-risk vulnerabilities could emerge in the next few quarters. Indeed, the IMF Article IV Consultation report of December 2020 noted that recent CBN stress tests simulating the migration of 25 percent of the unrestructured loan portfolio to NPL status could cause the system's CAR to drop below 10 percent.

The continuing surge in inflation has been accompanied by a contraction in real credit to the private sector. Although in the first three months of 2021 demand deposits continued to expand at an average real rate of 35 percent, real quasi-money deposits started to fall as negative real interest rates persisted, illuminating the risk of financial disintermediation. Meanwhile, microfinance banks drove a rapid expansion in nominal credit, which in 2020 grew by 82 percent year-on-year, supported also but to a lesser extent by development-finance institutions.[10] More positively, since March 2021 the prime lending rate of commercial banks has fallen by some 360 bps, with the maximum rate lower by 274 bps as deposit funding costs dropped by 200–400 bps across different maturities. As Nigeria lays the groundwork for a sustained post-pandemic recovery, if resilient, broad-based growth and job creation are to be ensured, broadening access to credit should be a priority.

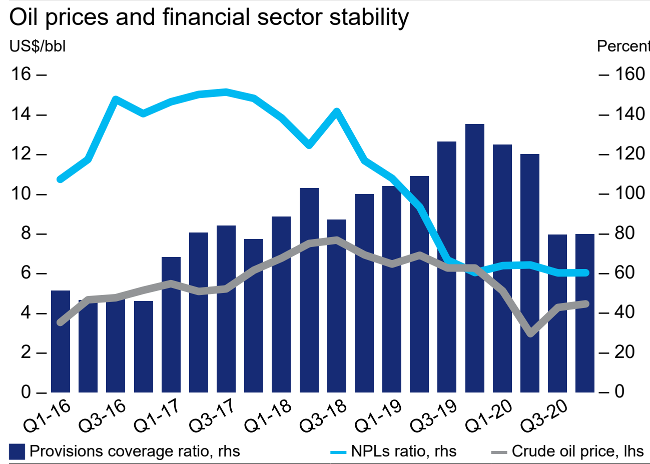
Different credit segments are expected to recover at different speeds, and the authorities must take special care in managing the process of withdrawing forbearance and other pandemic-related support measures. Reversal of the bank-debt repayment moratorium and forbearance measures present distinct risks to CBN as supervisor of banks and of other financial institutions. Policymakers must balance continued support for businesses and households against the risk that low-quality (impaired) assets will become entrenched in the system, intensifying liquidity risks and eroding the culture of loan repayment.[11] Moreover, rolling back pandemic-related support measures will reveal previously hidden deterioration in asset quality, raising solvency risks for more thinly capitalized

Figure 1.19. Credit growth has decelerated.



Source: NBS, CBN and World Bank estimates.

Figure 1.20. Nigeria's financial sector is vulnerable to oil price volatility.



Source: NBS, CBN, and World Bank estimates.

9 The 100 largest borrowers accounted for 47 percent of total credit in April 2019 (NBS e-library), and most large banks reportedly serve the same small group of corporations.
10 At the end of Q3 2020 microfinance institutions accounted for less than 2 percent of financial system assets.
11 On March 3d, 2021, the CBN announced that it would extend the reduction from 9 to 5 percent of the interest rate on its development intervention facilities for one year through February 28, 2022, and that a one-year extension of the repayment of credit facilities would be considered case-by-case.

banking institutions. Managing the consequences of this process will test the adequacy of the processes for dealing with banks in distress and resolving bank insolvency. Prompt regulatory development of the procedures authorized in the recently amended Banks and Other Financial Institutions Act will be critical to ensure effective application of the revised law, as will further development of the capacity of the Nigeria Deposit Insurance Corporation to assess and execute resolution plans for systemically important domestic banks. Upgrading regulation could attenuate reliance on public support, direct or indirect, from the CBN or the Asset Management Corporation of Nigeria by providing efficient tools to resolve bank insolvency while enabling the authorities to move away from regulatory forbearance when dealing with undercapitalized entities. If inflation continues to accelerate, pressures in the FX market fail to subside, or both, the CBN will likely need to raise policy rates. Accelerating inflation tends to be associated with higher inflation volatility, which in turn makes credit risk assessments less reliable and banks more cautious about lending.

Fiscal Policy: Despite rising oil prices, Nigeria's fiscal position is tenuous, highlighting the need to sustain reforms

In 2020 reforms of the power sector, reduced gasoline subsidies, and higher VAT rates were fundamental in expanding the government's restricted short-term fiscal space. These measures, combined with greater transparency, are expected to bolster revenues and enhance the allocative efficiency of public spending. Mobilizing more revenue is vital for public services and social programming, and over the longer term such funds can be used to counter the harm inflation does to household welfare, expand the social safety net, increase the supply of health care, and accelerate recovery of consumption by vulnerable households. Enhanced transparency will also provide crucial information for assessing debt sustainability and fiscal risks, which is critical to ensure that Nigeria can issue commercial debt at a manageable cost.

The government's fiscal reforms were timely, but consistency will be critical to support a strong recovery beyond 2021. Before the pandemic, a combination of low revenues and heavy dependence on oil threatened Nigeria's fiscal stance: in 2018–19, revenue reached just 8 percent of GDP, among the lowest levels in the world, yet sales of crude oil represented 80 percent of exports, 30 percent of banking-sector credit, and 50 percent of general government revenues. Revenues from other sources, such as nonoil taxes, had stagnated at about 4 percent of GDP due to costly tax incentives, a suboptimal VAT system, low tax rates, weak tax administration, and burdensome compliance requirements for taxpayers. Nigeria's public-revenue-to-GDP ratio is the lowest among similar oil producers, and a lack of fiscal resources has resulted consistently in low and inefficient spending. Public spending averages just 12 percent of GDP and estimates of its efficiency are far below the levels of comparable middle-income economies. In addition, regressive and opaque subsidies for fuel and electricity create economic distortions and reduce the fiscal space for development spending. By addressing some of these issues, at least in part, the government's recent reforms are expected to increase Nigeria's fiscal and macroeconomic resilience.

In 2020, the fiscal deficit of the general government widened to 5.4 percent of GDP, the largest gap in two decades. Following the twin shocks of the COVID-19 pandemic and concurrent decline in oil prices, general government revenues fell from 7.4 percent of GDP in 2019 to 6.5 percent of GDP in 2020. Plunging oil prices during the first half of the year reduced oil revenue from 2.8 percent of GDP in 2019 to 2.0 percent in 2020, while nonoil revenue dropped from 4.7 percent of GDP to 4.5 percent as economic activity slowed. The Federal Government and all State Governments adopted amended budgets between July and September of 2020, which prioritized spending to accommodate ₦500 billion (0.3 percent of GDP) in fiscal support for COVID-19 response and adjusted the budgeted oil price from US$57 to US$28 per barrel. Nevertheless, non-oil revenues in 2020 underperformed relative even the revised budgetary expectations, especially the evolution of nonoil revenues, while oil revenues slightly outperformed expectations due to rebounding prices in the second half of the year. Although the oil-savings in Excess Crude Account have been depleted prior to the COVID-19 shock, the federation account revenue distribution was boosted by distribution of various revenues savings (particularly from the past exchange rate differences), which supported the fiscal inflows for both the federal and subnational governments.

Table 1.1. Key Reforms implemented by Nigerian authorities.

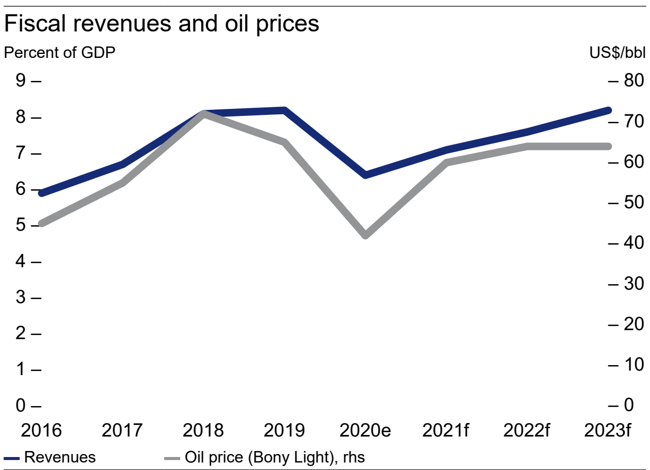
Oil-Revenue Transparency		**Power Sector**	
In June the Nigerian National Petroleum Corporation (NNPC) published independently audited financial statements for 20 subsidiaries and corporate units for fiscal year (FY) 2018. In October NNPC published audited financial statements for 22 units for FY2019, along with the consolidated group statement. The NNPC has published detailed monthly reports for the first half of 2020, including information on the volumes and values of oil and gas delivered, fiscal payments made, in-kind oil payments made, and deductions offered by NNPC.	Status: On track	In November 2020, electricity tariffs were adjusted from an estimated 56 percent of production cost to over 80 percent, and a regime of service-based tariffs was established to ensure that the higher average cost of electricity does not adversely impact poor and low-income households. However, further tariff adjustments have been delayed, and full cost recovery will not be achieved in 2022.	Status: Paused
Gasoline Subsidies		**Debt Transparency**	
In March 2020, the government established a market-based gasoline-pricing mechanism though the regulations were not detailed. In mid-November, the government raised the price band from the level that had prevailed from 2016 to mid-March 2020, signaling its intention to sustain market-based pricing. However, the government lowered the gasoline prices in December 2020 against the backdrop of rising world oil prices. Retail prices have yet to be adjusted to reflect the rise in benchmark prices in 2021.	Status: Paused	In June 2020, for the first time, the Debt Management Office (DMO) published detailed information on loans to the federal government that have been signed but not yet disbursed. This information was disaggregated by creditor and by project. The DMO also committed to continue publishing this information twice a year. The government has also improved its reporting of fiscal risks.	Status: On track
VAT		**Budgeting practices**	
In November 2019, the government approved a Finance Bill designed to raise enough federal revenue to meet the government's 2020 budget targets, align Nigeria's budgets with international standards, support small businesses, and encourage investments in infrastructure. The VAT rate was also raised, from 5 to 7.5 percent, though that is still low by international standards.	Status: On track	In May 2020, the federal government adopted an amended budget for the year that cut nonessential spending and raised the borrowing ceiling. Although fiscal federalism does not compel states to be fiscally transparent and accountable to the federal government, all 36 states have passed amended 2020 budgets.	Status: On track

As in previous crises, reduced fiscal space constrained the government's capacity to deliver adequate services and to invest productively. While as in previous crises, the estimated[12] government capital spending declined from 3.1 percent of GDP in 2019 to an estimated 2.8 percent in 2020, the decline has been less pronounced, in part due to amended budgets that increased the realism of both revenue and financing inflows. By contrast, recurrent expenditures grew from 8.0 percent of GDP in 2019 to 8.5 percent in 2020, as state and federal government adjusted personnel costs in line with new minimum wage law, and booted by the rising cost of debt service at the federal government level, which increased from 2.0 percent of GDP to 2.4 percent over the period.

Although rising oil prices are easing fiscal pressures, Nigeria remains highly vulnerable to external and domestic shocks. The performance of the public finances depends heavily on oil revenues, but the impact of oil-price changes is not symmetrical. A US$10 increase in the price of a barrel of oil could reduce the fiscal deficit by 0.4 percent of GDP in absence of fuel subsidy, but a similar decrease could widen the fiscal deficit by more than 0.4 percent of GDP. In the baseline scenario, general government revenues are projected to remain below 7 percent of GDP 2021, with oil revenue increasing from 2.0 to 2.5 percent of GDP as average oil prices rise from US$42 per barrel in 2020 to US$60 per barrel in 2021 while oil production remains subdued at 1.7 million barrels per day observed in late 2020. However, this revenue increase will be insufficient to balance the budget. Nonoil revenue is also expected to rise moderately, driven by greater VAT collection following the public financial reforms of 2020, which increased the VAT rate from 5.0 to 7.5 percent; phasing out of the tax relief measures, and the implementation of Finance Act 2020. Gradual fiscal consolidation over time is expected to be supported by expenditure savings arising from the phasing out of electricity and fuel subsidies. Recurrent spending is expected to remain rigid, with continued implementation of minimum wage law and sustained debt service costs. Overall, the general government's fiscal deficit is expected to narrow only marginally from 5.4 percent of GDP in 2020 to [about 5 percent] percent in 2021, and Nigeria's fiscal position is projected to remain tightly constrained.

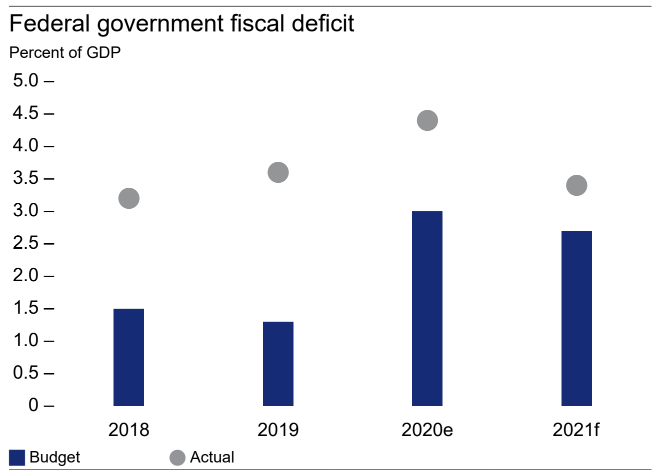
Despite the faster-than-expected economic recovery, the revenue projections in the 2021 Budget are unlikely to be met. The budget assumes that the benchmark oil price will recover from US$28 to US$40 per barrel, below the level of US$64 observed in April 2021, and that aggregate oil production will rise from

Figure 1.21. Higher oil prices are expected to boost public revenue in 2021...



Source: Office of the Accountant-General of the Federation (OAGF) and World Bank estimates.

Figure 1.22. ...but revenue outturns are expected to continue underperforming.



Source: 2018–2021 Budget Proposals, Office of the Accountant-General of the Federation (OAGF) and World Bank estimates.

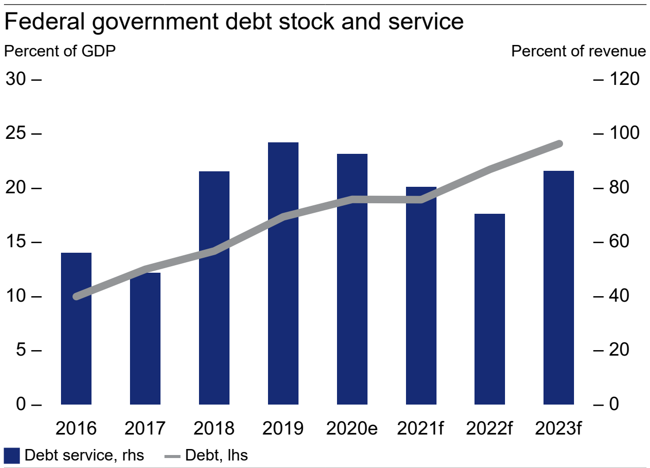
12 Federal Government actual spending figures are available; state capital spending is estimated.

1.8 to 1.9 million barrels per day. The proposal also assumes an official exchange rate of ₦379/US$, an annual GDP growth rate of 3.0 percent (above the current average market expectation of 2.1 percent), and an annual inflation rate of 12.0 percent, though the rate would have to drop below 10 percent in the second half of the year to reach this target. Reflecting these assumptions, the 2021 Budget net oil revenue projections are 98.0 percent higher than those included in the 2020 Amended Budget, and total budgeted federal government spending is expected to increase by 11.0 percent.

In the absence of sound fiscal buffers, the additional expenditure needs arising from the COVID-19 crisis have required increased borrowing. Excess crude savings were depleted before 2019, and low oil prices have not allowed the government to rebuild them. The resulting lack of fiscal buffers (beyond savings from past exchange rate differences and other funds) Combined with falling and underperforming revenues led to increase borrowing, including from the CBN. Consequently, Nigeria's deficit financing needs have steadily driven up the debt stock, and the rising cost of debt service is outpacing revenue growth and eroding the government's fiscal space. Higher borrowing limits in the Amended Federal Government Budget 2020 allowed for more transparent borrowing from both domestic and external sources but were not sufficient to avoid tapping into the Central Bank financing. The total debt stock (including the estimated borrowing from the Central Bank) 23.6 percent in 2019 to 27 percent in 2020The timely passage of the amended budgets at both the Federal and State levels helped limit recourse to central bank financing, though it remained significant at 2.8 percent of GDP.

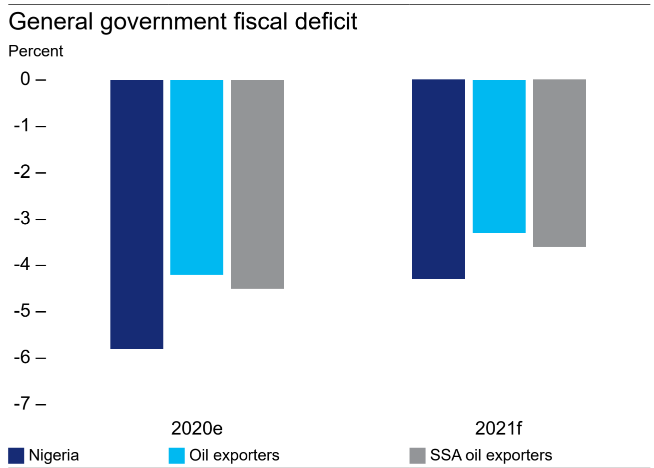
The high cost of debt service is increasing fiscal rigidity, but Nigeria's public debt stock remains moderate by international standards. While faster-than-expected GDP growth, higher oil prices, will ease some debt sustainability concerns, the debt continues to rise, projected to exceed 30 percent of GDP after 2021. Nigeria's public debt is expected to remain largely domestic and mostly issued by the Federal Government. While debt levels remain relatively moderate, debt growth outpaces the growth in revenues. Given Nigeria's chronically low revenues, the debt-service-to-revenue ratio at the general government level is continue rising, averaging about 30 percent by the end of 2021, further constraining an already limited fiscal envelope. These pressures are particularly acute at the federal government

Figure 1.23. Debt dynamics remain sustainable, but debt service consumes most of Nigeria's fiscal revenue.



Source: Office of the Accountant-General of the Federation (OAGF) and World Bank estimates.

Figure 1.24. Despite higher oil prices, Nigeria's fiscal deficit is expected to be one of the largest among oil-producing countries.



Source: World Bank Macro Poverty Outlook.

level: as it contracts most of the public debt, it bears most of the debt service costs, systemically requiring more than 50 percent of its retained revenues (and nearly 100 percent in 2020). Despite this high ratio, a January 2021 IMF assessment determined that Nigeria's debt stock would remain sustainable under a variety of individual macroeconomic shocks, though it remains highly vulnerable to a combination of shocks. In the fourth quarter of 2020, the Nigerian legislature approved a medium-term expenditure strategy for 2021–23 that includes about US$18 billion (US$6 billion annually) in support from international financial institutions and Eurobond issues. The government has raised its public debt limit to 40 percent of GDP to incorporate increased budget shortfalls over the medium term and to accommodate the securitization of CBN deficit financing as long-term debt, which will increase debt transparency and may reduce debt servicing costs, the government's use of CBN overdrafts is more expensive than other financing options. Repeated recourse to large-scale central bank financing could hinder the CBN's ability to curb inflation.

Economic Outlook

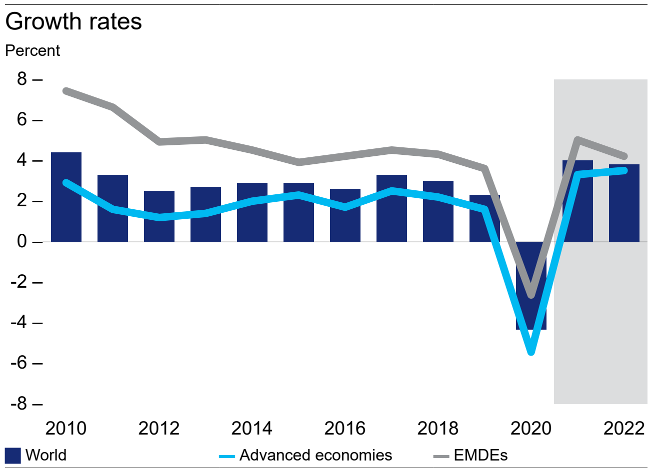
The Global Economy: Beginning to recover, but new waves of COVID-19 could threaten the outlook

Like much of the world, Nigeria's economic outlook still depends on the trajectory of the COVID-19 pandemic. Despite major progress on vaccine distribution, COVID-19 continues to spread, with some countries now confronted by outbreaks of more contagious variants of the virus. A combination of vaccines and containment measures has helped slow the spread of the virus, in particular, in advanced economies. However, vaccinations have been heavily concentrated in advanced and emerging economies, with less than 1 percent of total vaccinations administered in Sub-Saharan Africa as of early June.

Global economic activity is accelerating, but the recovery is far from solid. After contracting by 4.3 percent last year, in 2021 aggregate global growth is projected to recover to 4 percent (Figure 1.25). However, the renewed expansion will not be sufficient to offset the deep recession of last year, and the recovery is expected to be uneven. Rapid growth is projected for the United States, China, and some advanced economies, but many middle- and low-income countries are expected to trail their high-income counterparts. However, the global recovery should strengthen over the medium term as widespread vaccinations bolster confidence and consumption and trade flows are gradually released.

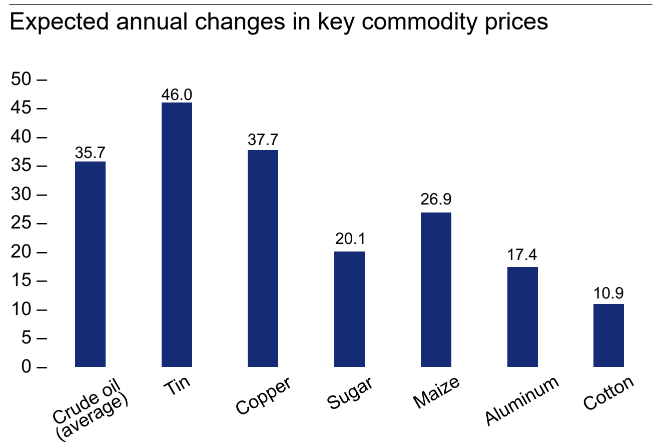
Despite the improving outlook, for 2022 aggregate global economic growth is likely to be 4.4 percentage points below pre-pandemic projections. Near-term prospects for lower-income countries (LICs) are especially grim, with the gap between pre- and post-pandemic growth projections almost twice as large as that gap for advanced economies. After contracting by an estimated 3.7 percent in 2019, aggregate GDP growth in SSA is projected to rebound modestly, to 2.7 percent in 2021 and 3.3 percent in 2022. Over the long term, the pandemic's corrosive effects on human and physical capital accumulation are expected to leave deep scars

Figure 1.25. The pandemic induced a deep global recession, but a faster-than-expected recovery appears to be underway.



Source: World Bank.

Figure 1.26. A combination of supply- and demand-side factors is driving global recovery of commodity prices.



Source: World Bank Commodity Markets Outlook.

on global output, especially in LICs. By disrupting education, undermining health outcomes, crowding out investment, and compelling households to adopt coping strategies that are economically detrimental, the pandemic has created barriers to achievement of critical development goals for many years to come.

Rising prices are expected to accelerate the recovery of commodity exporters. Commodity prices have shot up since the start of 2021, in response to resurgent global demand supported by positive supply-side factors. In particular, for oil exporters, prices are expected to average \$56/bbl in 2021 before rising to \$60/bbl in 2022. This path reflects the improved outlook for global economic growth and a more gradual increase than previously expected in production by OPEC and its partners (OPEC+). However, further slippage in oil demand, perhaps arising from a renewed outbreak of COVID-19, could put considerable additional pressure on the OPEC+ production agreement. An end to the agreement and a sudden rise in global production could push oil prices far lower than currently expected. A further risk is the response of U.S. shale to higher prices—an unexpectedly fast recovery in U.S. production would also put heavy pressure on the OPEC+ producers.

Nigeria's Outlook: Sequenced policy reforms are crucial if there is to be a strong and resilient recovery

There is considerable uncertainty about Nigeria's economic outlook because it is so dependent on the evolution of the COVID-19 pandemic, the global economic recovery, oil prices, and the speed of reforms in Nigeria. A renewed global surge in COVID-19 cases, driven by more transmissible strains, has intensified the already massive uncertainty about the duration of the pandemic and the pace of vaccination, and the uncertainty will continue to influence private investment and household consumption. Moreover, while oil prices have rebounded to pre-pandemic levels, Nigeria's modest projected recovery could be threatened not only by the continuing uncertainty but also by oil-sector volatility—unexpected shocks to oil prices or production, weaknesses in the financial sector, high inflation, and worsening unemployment. Even in the most favorable global context, an effective policy response will be crucial to lay the foundation for robust recovery. Especially vital to Nigeria's recovery will be revenue-focused fiscal consolidation, reprioritizing spending, better management of spending and debt, reforms to stabilize the financial sector, and gradual adoption of a more flexible foreign-exchange regime.

In the baseline scenario, growth in Nigeria's GDP is projected to recover only slightly in 2021, to an annual average of 1.8 percent, before gradually rising over the medium term. As international borders gradually reopen, telecommunications services, trade, agriculture, and construction are expected to drive growth; oil prices would remain close to pre-pandemic levels; and mobility restrictions would be lifted. Though agricultural output should benefit from an influx of displaced urban labor, its growth will come at the expense of other sectors. In the baseline scenario, the Nigerian authorities sustain the 2020 reforms, especially reforms to electricity and fuel subsidies, which are necessary to generate the fiscal space needed to continue supporting the COVID-19 response. However, the reforms do not address the two main sources of macro imbalances in 2021: exchange rate mismanagement and high inflation. Thus, reforming the management of the exchange rate is not expected, so there will be more pressure on the parallel exchange rate; the CBN will have less flexibility to clear the FX backlog—and foreign investors will have less appetite to invest in Nigeria. Inflation is expected to continue accelerating even if supply constraints are adequately managed, and the vicious cycle of high parallel FX rates (which means high premiums) and high demand-driven inflation is likely to make monetary policy less effective. If inflation expectations are not anchored, investment and consumption decisions will continue to be suboptimal. Thus, Nigeria's vulnerabilities are likely to stay high. While the higher oil prices should result into higher reserves (although despite higher exports they did not go up much in the first quarter of 2021), low levels of public and private investment would continue to contain growth. In such a scenario, concerns about poverty and the direction of the economy can be expected to increase.

In an alternative scenario in which the government undertakes a sequenced program to stabilize inflation and protect the livelihoods of poor and vulnerable households, over the medium term Nigeria will be in a better position to support faster economic recovery. This scenario assumes that the authorities adopt much-needed exchange-rate management reforms; advance monetary, fiscal, and trade measures that help control inflation; and opt for policies that support macroeconomic stability, inclusive growth, and job creation (Table 1.2). Easing import and FX restrictions, which lead to higher prices for both imported goods and domestic substitutes, would contribute to price stability. Improved exchange-rate management would reduce pressure on external accounts and improve the business environment, thus encouraging private investment, both domestic and foreign. Programs that expand access to financing for micro, small, and medium enterprises (MSMEs) would accelerate domestic investment and spur robust recovery. Furthermore, building up the delivery of social protection programs will help ease the immediate impact of inflation on poor and vulnerable households. In this scenario, annual GDP growth is also projected to average 1.8 percent in 2021 because at first the positive impact of the proposed growth-enabling measures would be counterbalanced by inflation control and stabilization measures, which explains why in the alternative reform scenario growth is not higher: in order to control inflation, the authorities would need to rein in expansive monetary policy and CBN financing of the government deficit. The impact on inflation is not expected to be immediate. However, starting in 2022 expected GDP growth and inflation dynamics would contribute to a more adequate macro financial framework: growth is expected to reach 2.5 percent in 2022, and surpass population growth in 2023, and inflation would average 12.0 percent in 2022 before falling to 10.0 percent in 2023.

In a third scenario, in which the policy assumptions of the baseline scenario are reversed and the global context is unfavorable (lower commodity prices and a persisting global health crisis), the economic recovery would be significantly slower. This scenario assumes the reversal of revenue-based fiscal consolidation efforts, such as reducing electricity and gasoline subsidies; reversal would diminish foreign and domestic investment, significantly dampening Nigeria's growth prospects. Less public spending would widen Nigeria's already substantial gaps in human and physical capital, worsen public service delivery, and damage investor confidence. As a result, GDP growth would reach only 1.1 percent in 2021; thanks to a base effect; inflation rates would be higher, job creation weaker, and poverty would rise.

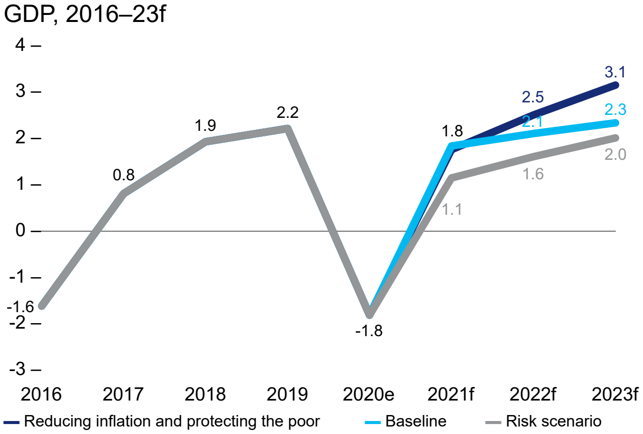
Policy Options: Sustained reform momentum is critical to reduce inflation, support a robust recovery, and protect livelihoods

The COVID-19 pandemic has exacerbated underlying structural challenges in the Nigerian economy, resulting in a combination of low growth and high inflation; if recovery is to be rapid and broad-based, continued reforms will be necessary. Efforts to protect the welfare of poor and vulnerable Nigerians and accelerate the resumption of economic activity need to include measures to stabilize inflation. In 2020 alone, poverty is expected to increase due to a combination of COVID-19-related price shocks, depressed economic activity, and rapid population growth. Moreover, food insecurity has increased. At its current elevated level, even a stable inflation rate for the rest of 2021 could continue pushing more Nigerians into poverty.

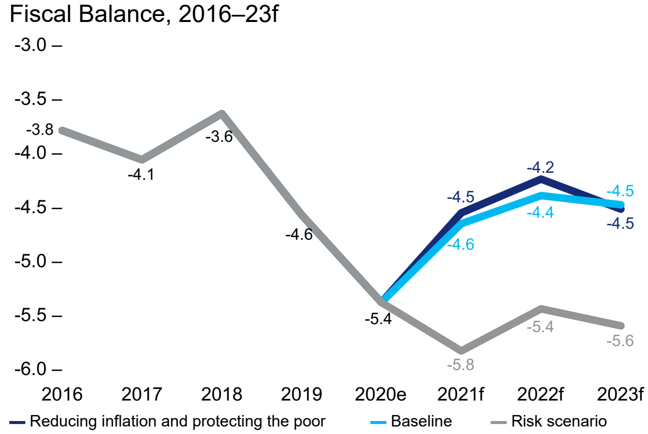
Table 1.2. Nigeria's Economic Outlook: Three scenarios.

Scenario 1: Baseline	*Scenario 2: Reduce inflation and protecting the poor*	*Scenario 3: Risk scenario*
Assumptions		
Policy: The authorities sustain current reform efforts in key macroeconomic policy areas, including revenue-based fiscal consolidation, expenditure reprioritization, debt management, and financial-sector stability, but fail to advance measures to make exchange-rate management more flexible and lower inflation. ***Oil price:*** Oil prices average US$56 per barrel in 2021 and US$60 in 2022. ***COVID-19:*** No third wave and vaccine deployment speeds up in 2022.	***Policy:*** The authorities sustain current reform efforts in key macroeconomic policy areas and advance reforms to stabilize inflation and promote inclusive growth and job creation, for example by promoting a fully flexible exchange-rate, trade policies, and social protection measures. ***Oil price:*** Oil prices average US$56 per barrel in 2021 and US$60 in 2022. ***COVID-19:*** No third wave and vaccine deployment speeds up in 2022.	***Policy:*** The authorities fail to sustain recent reforms, including changes to electricity and gasoline subsidies, and no adjustments are made to the nominal exchange rate. ***Oil price:*** Oil prices average US$56 per barrel in 2021 and US$56 in 2022. ***COVID-19:*** No third wave and vaccine deployment speeds up in 2022, but the global health crisis does not abate in most emerging and developed economies throughout the first half of 2022.

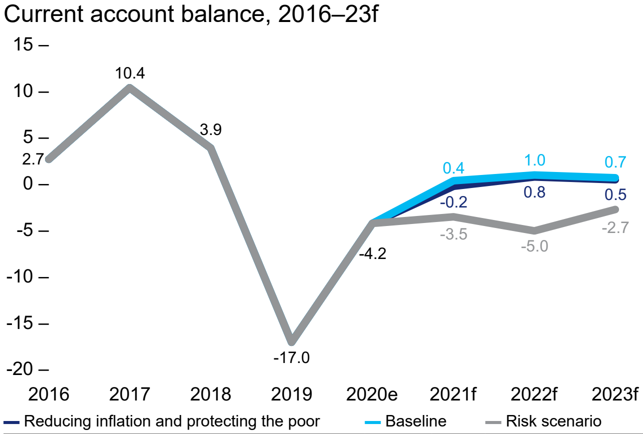
GDP, 2016–23f



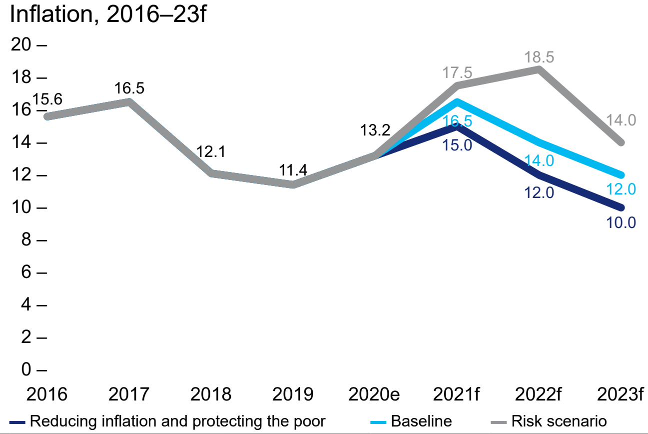
Fiscal Balance, 2016–23f



Current account balance, 2016–23f



Inflation, 2016–23f



This edition of the *Nigeria Development Update* proposes immediate policy actions to stabilize inflation, restore growth, and protect the lives and livelihoods of Nigerians. Because inflationary pressures arise from multiple sources, stabilizing and reducing inflation will require a sequenced and coordinated package of reforms that encompasses exchange-rate management and monetary, fiscal, and trade policy. Because such action could hit poor households hard in the short term, social protection systems must be reinforced to prevent any further deterioration in consumption and welfare. Half-measures will not be enough to divert the current inflationary trend and lay the foundation for robust recovery—and policy reversals pose a major risk to Nigeria's economic outlook.

Table 1.3. Policy options to reduce inflation, protect the poor, and support the recovery.

Area	*Immediate Priorities (Next 3 to 6 months)*	*Medium-Term Priorities (Next 6 to 18 months)*
1. Reduce inflation by adopting policies that support macroeconomic stability, inclusive growth, and job creation		
Exchange Rate Management	• To build credibility, communicate the exchange-rate management strategy. For example, assure market participants using the Secondary Market Intervention Sales (SMIS) and IEFX windows of a well-defined schedule of FX auctions (e.g., for the next 3 months and then on a rolling basis), consistent with projections for FX inflows. The amounts to be auctioned should respond to the CBN's need to rebuild the stock of international reserves to safer levels. • Regulate the auction processes, at least initially, by using pre-defined exchange-rate bands to control possible immediate overshooting. These bands could be relaxed as the market develops and the system gains credibility. Reserve extraordinary FX interventions (e.g., unscheduled auctions) for episodes of intense market volatility.	• Carry out measures to deepen the FX market, such as re-establishing the dollar interbank market and again enabling commercial banks to trade FX on their own behalf and not solely to fill client orders. This would help increase the depth and liquidity of the FX market while improving price discovery. Banks would also be able to absorb some unexpected FX demand and supply shocks, gradually lessening the need for CBN interventions. Banks would still be subject to net open position limits and other prudential requirements. The reestablishment of the dollar interbank market would also help participants reallocate FX liquidity and comply with prudential standards. • Merge all exchange-rate windows into a single window that reflects market fundamentals.

Table 1.3. Policy options to reduce inflation, protect the poor, and support the recovery. (continued)

Area	*Immediate Priorities (Next 3 to 6 months)*	*Medium-Term Priorities (Next 6 to 18 months)*
Trade	• Fully reopen land borders to trade and strengthen regional cooperation to combat smuggling. Extend to Benin the ECOWAS Customs Mutual Assistance Agreement that Nigeria is currently piloting with Niger. • Facilitate imports of staple foods and medicines by removing them from the list of FX restrictions and replacing import bans with tariffs that reflect the ECOWAS Common External Tariff. • Review the FX restrictions and import bans currently applied to nonfood goods and assess the implications of replacing them with tariffs. This analysis should include effects on households, firms, and public revenues, as well as on the desired policy outcome of protecting domestic producers without incentivizing smuggling. • Refrain from adding any new products to the list of import bans and FX restrictions. • To control oil-related inflationary pressures, reduce gasoline smuggling by (1) better monitoring exports and imports; (2) publishing guidelines for fuel products sold in Nigeria to ensure that they reflect import-parity and do not incentivize smuggling; and (3) making arrangements to ensure that sales of crude oil to domestic refineries and domestic sales of refined fuel products reflect market-based prices that are aligned with international prices and market exchange rates.	• Based on the results of the analysis of nontariff measures, replace import bans with tariffs, which will increase revenues, lower domestic prices, and reduce smuggling and criminality along the border. • Finalize plans to implement the African Continental Free-Trade Area Phase 1 protocols and annexes and identify a mechanism for addressing the cost of trade adjustments to workers. Compile a list of excluded products. • Put in place high-priority measures to reduce trade and transportation costs by addressing delays in border and port clearance. Such measures include simplifying and harmonizing documents, streamlining and automating procedures, and making more information available.
Fiscal Policy	• To help contain the growth of the money supply, establish mechanisms to monitor the federal government's stock of CBN overdrafts (i.e., the historical stock of accumulated ways and means), the flow of the overdraft facility (i.e., its monthly use), and its servicing cost (i.e., interest payments). • Adopt a mechanism to increase flexibility between borrowing options to finance the federal government deficit. Currently, the legislature approves a fixed ceiling for each domestic and external loan contracted to finance the domestic deficit; when external financing falls short of approved plans, domestic borrowing is not automatically increased to cover the shortfall, resulting in recourse to CBN financing, which accelerates the growth of the money supply and can lead to higher inflation.	• To help contain the growth of the money supply over the medium term, analyze the cost of the fiscal-subsidy elements of the CBN's quasi-fiscal interventions, including: (i) power-sector financing; and (ii) subsidized CBN lending schemes for agriculture, industrial development, COVID-19 response, etc. • To further reduce the federal government's recourse to CBN financing, improve the accuracy of budgetary revenue forecasting. Overoptimistic revenue forecasts and the resulting shortfalls lead to larger-than-anticipated deficits, creating additional financing needs for which borrowing has not been approved by the legislature, which encourages the use of CBN financing. • Adopt a mechanism to allow increased borrowing to cover additional financing needs arising from revenue shortfalls.

Table 1.3. Policy options to reduce inflation, protect the poor, and support the recovery. (continued)

Area	*Immediate Priorities (Next 3 to 6 months)*	*Medium-Term Priorities (Next 6 to 18 months)*
Monetary Policy	• Clearly define key monetary-policy priorities and objectives and signal the government's commitment to price stability as the primary objective while remaining aware that in the next few months the CBN will continue to support both economic recovery and a limited funding of the government as the country emerges from the COVID-19 crisis. • Resume naira-denominated open-market operations (OMOs) with a transparent schedule for issuing securities and a clear message that OMOs will use short-maturity securities to achieve price stability. • Reduce CBN lending to medium and large corporates under its subsidized funding schemes to expand the scope for commercial banks to intermediate funds at a risk-adjusted lending rate. • Phase out excessive reliance on the cash-reserve ratio as a "high-frequency" liquidity control tool and an instrument to finance the CBN's quasi fiscal operations, as it implicitly taxes financial savings mobilization.	• Establish a Monetary and Fiscal Policy Coordination Council to clarify joint policy objectives and identify areas of coordination. The council should focus on eliminating unsustainable monetary and quasi-fiscal interventions while strengthening debt sustainability and advancing Nigeria's development priorities. As in other emerging markets, the council should be chaired by a high-ranking official, and it should include the CBN Governor, the Federal Minister of Finance, Budget, and National Planning, and independent experts.
2. Protect poor households from the impacts of inflation		
Social Protection	• Leverage the National Social Safety Nets Program 1 (NASSP 1) and the proposed NASSP II which is under discussion, with a plan to provide cash transfer support to additional 5 households in the NSR in rural areas and possible expansion of the Rapid-Response Register (RRR) of vulnerable beneficiaries in urban and peri-urban areas to include another 7.2 million households in addition to the two million already targeted by the COVID-19 response effort. These proposed measures would allow the program to cover 16.2 million already poor, newly poor, and vulnerable households in all 36 States and the Federal Capital Territory. • Rapidly implement the CARES program to support households, farmers, and firms. By the end of 2022, the CARES program aims to support approximately two million households, 750,000 farmers, and 70,000 firms.	• Given the government's current fiscal and macroeconomic challenges, a public expenditure review could shed light on whether the resources allocated to Nigeria's Social Protection and Jobs Programs and other untargeted programs are adequate and are being used in the most cost-effective and pro-poor manner. The results could provide useful guidance on how to strengthen expenditure management and reform the subsidy regime. • Integrate the NHGSFP and other social assistance programs into the National Social Register (NSR) and State-level social registers. Expand the NSR and State-level social registers so that other existing and future social programs could use the available data to quickly identify and enroll households for future support and ensure that programs effectively reach targeted groups. • Augment social protection programs with improved mechanisms for payment delivery, such as that developed through the NASSP, which could be enhanced by using digitization to facilitate payment delivery and strengthen accountability. • Graduate existing NASSP beneficiaries into productive-inclusion activities such as workforce training, asset and livestock transfers, and livelihood grants.

Table 1.3. Policy options to reduce inflation, protect the poor, and support the recovery. (continued)

Area	*Immediate Priorities (Next 3 to 6 months)*	*Medium-Term Priorities (Next 6 to 18 months)*
3. Facilitate access to financing for MSMEs in key sectors to mitigate the impact of inflation and accelerate the recovery		
MSMEs and Job Creation 	• Identify criteria for enabling MSMEs to access appropriate forms of equity financing and launch a scoping exercise to enroll and screen eligible MSMEs, develop parameters for debt restructuring, and create performance indicators for viable delinquent MSMEs. • Screen and enroll eligible MSMEs and build their capacity for debt restructuring.	• Roll out financing for targeted MSMEs while monitoring enrollment and assessing the reliability of the streamlined process, and without increasing CBN's interventions. Develop a streamlined process that offers clear incentives to formalize and register informal MSMEs. • Implement targeted labor-intensive public works and infrastructure microprojects to support employment while bolstering the capital stock. • Issue guidelines for adapting procurement procedures to support and encourage SMEs to participate in public procurement.

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Part 2: Taking a Closer Look

The continuing effects of the COVID-19 crisis on welfare and work

Summary: *The share of people working in February 2021 is similar to the share in September 2020, which is much higher than would be expected if working rates followed typical seasonal patterns. The higher share of people working is concentrated among women and people from poorer households, which suggests an "added worker effect," in which additional household members increase their labor supply in order to cope with economic shocks. Also, the commerce and service sectors have expanded beyond what would be expected given previous seasonal patterns, especially for women. Accompanying these labor market shifts, incomes for some households have increased since before the crisis, although that is far from universal. Yet even if incomes are stabilizing, households are feeling the impact of rising prices, which erodes their purchasing power and means that food insecurity remains widespread.*

New high-frequency data provide an updated picture of how the COVID-19 crisis is affecting the Nigerian labor market

Using new data, this brief builds on the previous edition of the Nigeria Development Update (NDU) by asking whether the post-lockdown return to work has been sustained and whether household incomes remain precarious. Since the COVID-19 crisis began, Nigeria's National Bureau of Statistics (NBS) has collaborated with the World Bank to collect data each month to track the economic and health impacts of the crisis through the Nigeria COVID-19 National Longitudinal Phone Survey (NLPS). Using these data, the previous NDU demonstrated that the share of household heads—the main income earners in each household—who were working plunged as lockdown restrictions were introduced in April and May 2020, but rose and stabilized as restrictions were eased. However, many household heads shifted to agriculture as they returned to work. Meanwhile, widespread reports of declining income and heightened food insecurity suggested that households remained economically precarious. Using new data collected in the February 2021 NLPS, it is now possible to verify whether these labor market trends have continued. These data not only provide more up-to-date information on the labor market but also include all household members of working age rather than just one respondent in each household.[13]

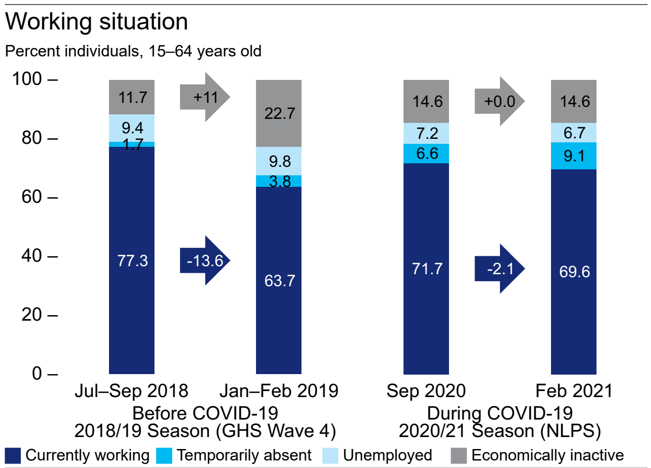
The share of people working in February 2021 was higher than would be expected, especially among women and people from poor households

In February 2021, about 69.6 percent of working-age Nigerians were working, similar to the level in September 2020 but much higher than would be expected for this time of the year. Usually, the share of people working in July–September is higher than in January–February: surveys from previous years show a regular and significant seasonal contraction between the July-September post-planting season and the January-February post-harvest season of the agricultural cycle. For example, the share of people working dropped by 13.6 percentage points (pp) between July/September 2018 and January/February 2019, but by only 2.1 pp between September 2020 and February 2021 (see Figure

13 Working age refers to all individuals aged 15 to 64.

2.1). Similar patterns were observed for people who are out of the labor force—those economically inactive. Between July/September 2018 and January/February 2019 the number of people who were economically inactive rose by 11.0 pp, but between September 2020 and February 2021 there was no increase at all. As such, individuals who would not normally work in the post-harvest season are instead continuing to work.

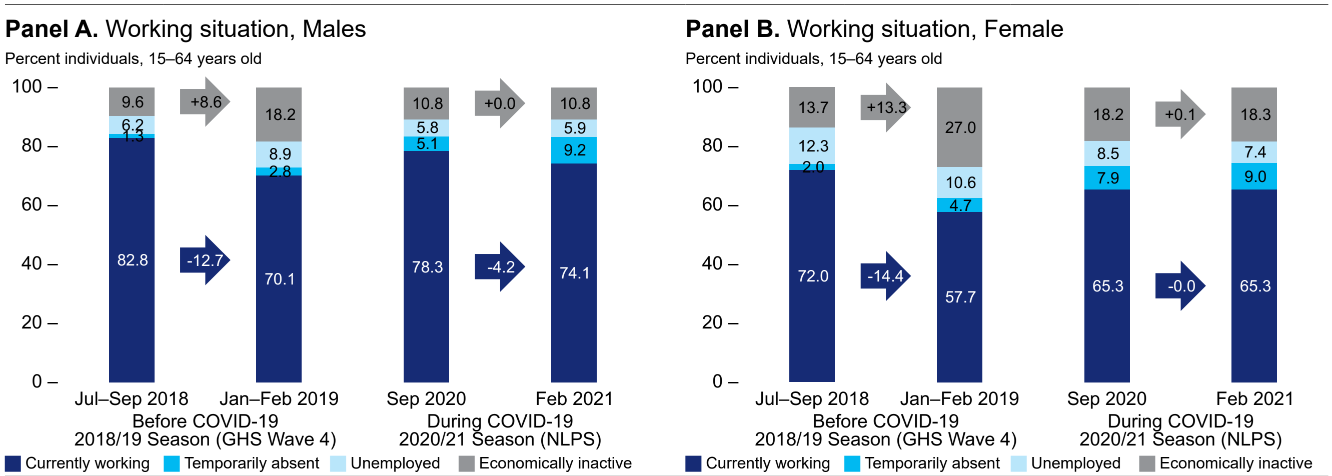
Figure 2.1. The share of people working is much higher than would be expected from previous seasonal patterns.



Source: Nigeria General Household Survey (GHS), Wave 4; Nigeria COVID-19 National Longitudinal Phone Survey (NLPS)
Note: This figure includes 4,018 observations that represent households with information for all rounds (GHS-W4 Post Planting, GHS-W4 Post Harvest, NLPS R5 and NLPS R10).

Women and poorer households are contributing more to the relatively high share of people working, which is consistent with an "added worker effect," where more household members participate in the labor force in response to economic shocks. In the pre-COVID agricultural cycle,[14] the share of men working contracted by 12.7 pp between the post-planting and post-harvesting seasons, but by only 4.2 pp in the current 2020/21 agricultural cycle (see Figure 2.2, A). Yet for women the difference in seasonal changes was even larger: in the pre-COVID agricultural cycle, the share of women working contracted by 14.4 pp, but in 2020/21 there was virtually no change in the share of women working (Figure 2.2, B). Similar gender differences emerge when examining how the seasonal expansion in the share of women and men who were out of the labor force entirely (economically inactive) changed from before the crisis to the present agricultural cycle. Moreover, the relatively high share of people working is also concentrated in households in the poorest quintiles of the pre-crisis consumption distribution. These patterns of heightened labor supply are consistent with the added worker effect.

Figure 2.2. The increase in the share of people working is higher among women.



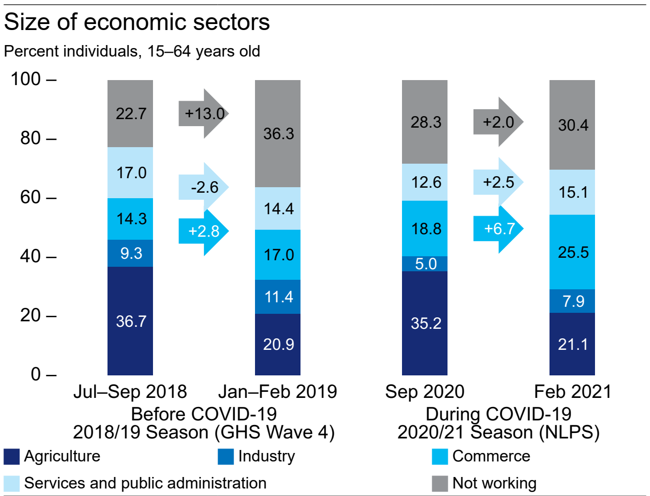
Sources: GHS and NLPS data.
Notes: This figure is based on 4,018 observations for households surveyed in all rounds (GHS-W4 Post Planting, GHS-W4 Post Harvest, NLPS R5 and NLPS R10).

14 The agricultural cycle was measured from July-September 2018 for the post-planting season to January–February 2019 for the post-harvest season for the pre-COVID period. The agricultural cycle was measured from September 2020 for the post-planting season to February 2021 for the post-harvest season for the crisis period.

The commerce and service sectors have expanded

The share of Nigerians engaged in commerce and services expanded more than would have been expected between September 2020 and February 2021. Between July/September 2018 and January/February 2019, the share of working-age Nigerians engaged in commerce rose by 2.8 pp, but between September 2020 and February 2021, the share rose by 6.7 pp (see Figure 2.3). In "services and public administration," between July/September 2018 and January/February 2019 the share of workers contracted by 2.6 pp, but between September 2020 and February 2021 the share expanded by 2.5 pp. This expansion appears to have been driven mainly by women. Two factors may explain these differences. First, the commerce and service sectors were more adversely affected at the onset of the COVID-19 crisis in 2020 due to both lockdown restrictions and social distancing. Second, during the post-harvest season, only sectors other than agriculture can absorb additional labor.

Figure 2.3. The commerce and service sectors expanded more than would be expected from previous seasonal patterns.

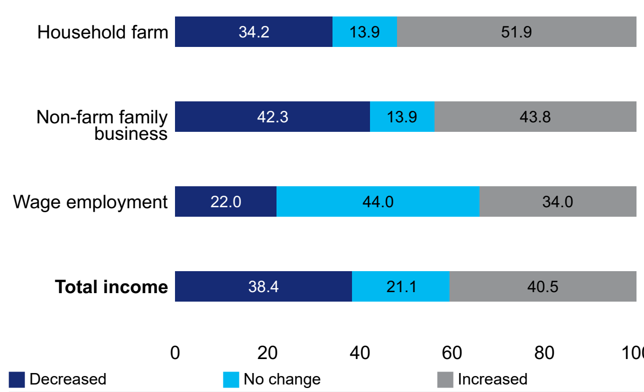


Sources: GHS and NLPS.
Notes: This figure is based on 4,018 observations for households surveyed in all rounds (GHS-W4 Post Planting, GHS-W4 Post Harvest, NLPS R5 and NLPS R10).

Any increase in incomes may be offset by rising prices, leaving the welfare of households precarious

Accompanying these labor market shifts, incomes for some households, though far from all, have improved. About 40.5 percent of households reported that their income had gone up between the August 2019–January 2020 and the August 2020–January 2021 periods. Incomes from agricultural work were even more likely to have improved: 51.9 percent of farm households indicated that their incomes had gone up in the second period, perhaps because rising food prices benefit some food producers.[15] Yet nonfarm enterprises—many of which may be in the commerce and service sectors that expanded—fared worse: about 42.3 percent of households relying on non-farm enterprises indicated that enterprise income had decreased (see Figure 2.4).

Figure 2.4. Incomes for some households have improved.



Source: NLPS, Round 9.
Notes: This figure includes 4,018 observations of households with information for all rounds (GHS-W4 Post Planting, GHS-W4 Post Harvest, NLPS R5 and NLPS R10). Bars represent households that had earned income from the indicated source in the previous 12 months. "Decreased" includes the small share of households that did not receive any income from that source between August 2020 and January 2021, despite normally doing so.

Even if incomes for some households are stabilizing, this may not be enough to offset rising inflation, which is limiting purchasing power and leaving households food insecure. As the section on 'Inflation and Poverty' demonstrates, throughout 2020 inflation, especially for food items, accelerated substantially. These price increases may negate any increase in nominal income that households are reporting, because for both

15 See section on 'Poverty and Inflation in Nigeria' for a further discussion of rising food prices and overall price inflation.

poor and non-poor households, the majority of food items are purchased rather than produced at home. Indeed, this could explain the added worker effect seen in the NLPS data: poorer households may be experiencing steeper declines in their purchasing power and are coping by becoming more active in the labor force. Moreover, despite having abated somewhat since the peak of the COVID-19 crisis in April/May 2020, food insecurity is still widespread: for example, in November 2020, in 56.1 percent of households' adults had skipped meals in the previous 30 days. With incomes uncertain, prices rising, and food insecurity elevated, the welfare of Nigerian households is far more precarious than it was before the COVID-19 crisis.

Poverty and inflation in Nigeria

Summary: *Inflation reached a 4-year high in March 2021, with food prices accounting for 63 percent of the total rise in inflation in 2020. Even among poor agricultural households, most of the food that households consume is purchased rather than produced at home, so inflated food prices are a major threat to purchasing power and welfare. Food insecurity is more widespread than it was before the COVID-19 crisis: in November 2020, in 56.1 percent of households, adults had skipped meals in the previous 30 days. In the short run, expanding social protection to provide time-bound support could alleviate the effects of inflation. In the medium and long run, however, it will be vital to address the sources of inflation through a mix of monetary, exchange rate, fiscal, and trade policies as well as effecting reforms to support job creation.*

Inflation's climb to a 4-year high in March 2021 was driven by both supply and demand factors

Driven by a surge in food prices, inflation reached a 4-year high in March 2021. Between March 2020 and March 2021, inflation for all items in the CPI basket rose from 12.3 percent to 18.2 percent, while for food items it rose from 15.0 percent to 22.9 percent, the highest level of food price inflation recorded in the last two decades. Indeed, the rise in food prices accounts for 63 percent of 2020's total rise in inflation. In 2019 and 2020, Nigeria had the 7th highest inflation rate in Sub-Saharan Africa.

A combination of supply and demand factors, some of which resulted from policy decisions, explain the rise in inflation. On the supply side, food production was affected by factors restricting access to markets and by declining crop yields. On the demand side, arguably the main explanation is that firms and consumers expect prices to rise during shocks and incorporate those expectations into their investment and consumption decisions (see Chapter 1 on recent economic developments, section on Inflation). The pattern of inflation measured month-to-month is different from previous years because in 2020 rising food prices were not connected to agricultural seasonality patterns as they had been before. Inflation threatens economic activity and job creation, jeopardizing prospects for a sustainable recovery. The combination of inflationary pressure and the contraction in the real economy witnessed in 2020 is projected to leave per capita income, in inflation-adjusted terms, close to what it was in 1980. High inflation distorts the consumption, investment, and saving decisions of the government, households, and firms, as well as their long-term borrowing and lending decisions, which ultimately threatens macro-fiscal and financial stability.

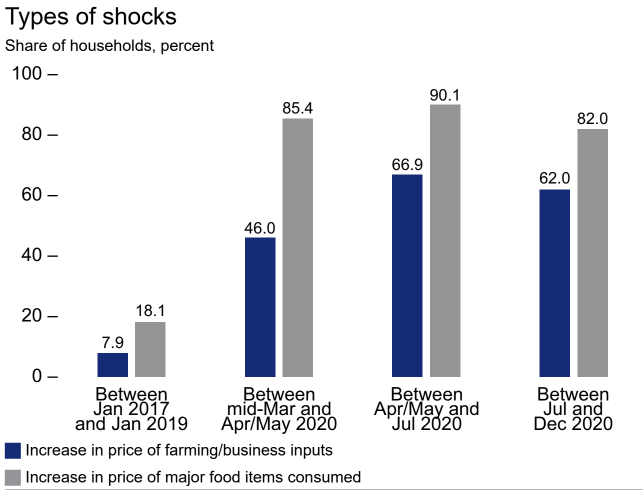
Increasing prices threaten household purchasing power

Nigerian households are directly feeling the effects of accelerating inflation. According to the monthly Nigeria COVID-19 National Longitudinal Phone Survey (NLPS), between July 2020 and December 2020, 82.7 percent of households saw rises in the prices of the major food items they consume, compared with 18.5 percent of households reporting such a shock between January 2017 and January 2019 (see

Figure 2.5). Moreover, about 62.0 percent of households also reported an increase in the prices of farming or business inputs.

Most of the food that Nigerians consume is purchased. According to the 2018/19 NLSS, about 24.1 percent of the consumption basket comes from own-produced food for households in the bottom 40 percent of the consumption distribution compared with 12.9 percent for the top 60 percent (see Figure 2.6).

Figure 2.5. Price shocks during the COVID-19 crisis, percent of Nigerian households.



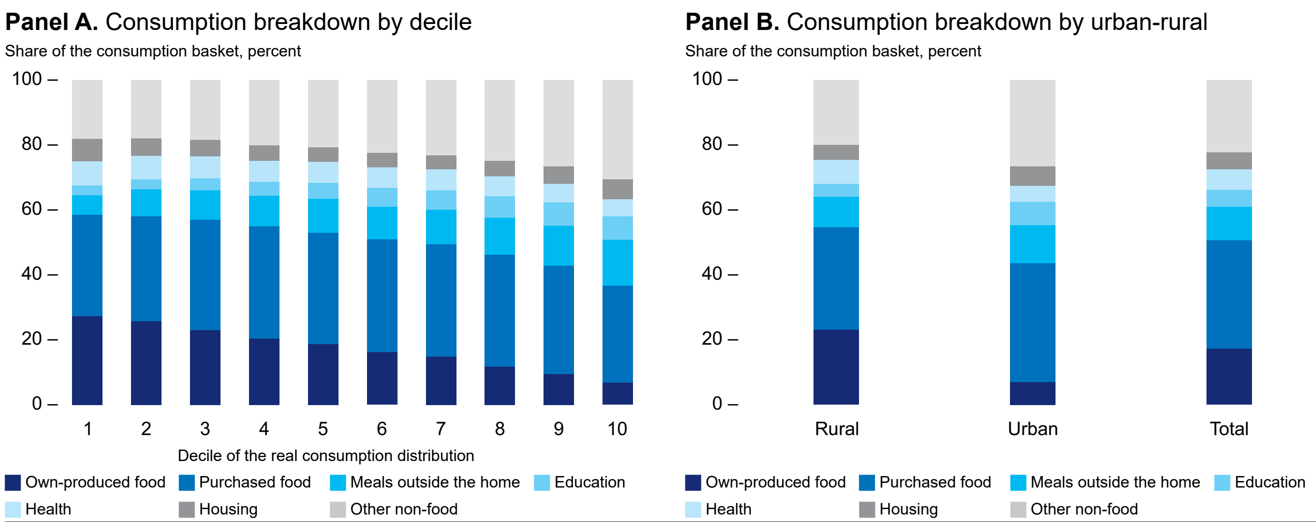
Source: 2018/19 GHS, NLPS, and World Bank estimates.

Yet both poor and non-poor households still buy most of the food they consume: about 33.1 percent of the consumption basket comes from purchased food for households in the bottom 40 percent, compared with 33.6 percent for the top 60 percent. Similarly, while rural households produce more of their own food than urban households, the majority of the food that they consume is also purchased.

Falling purchasing power could increase poverty and food insecurity

Falling purchasing power could push 7 million more Nigerians into poverty. The welfare losses associated with the price rises in 2020 can be calculated by assessing how much the cost of households' consumption baskets increased (see Annex for details). Consumption for the average Nigerian would need to rise by 4.9 percent to maintain the same level of welfare as before the 2020 price rises, which corresponds to just under 9,500 naira per person per year in nominal 2018/19 terms. By calculating the different welfare losses for each decile of

Figure 2.6. Most of the food that Nigerians consume is purchased, even for poor households and rural dwellers.

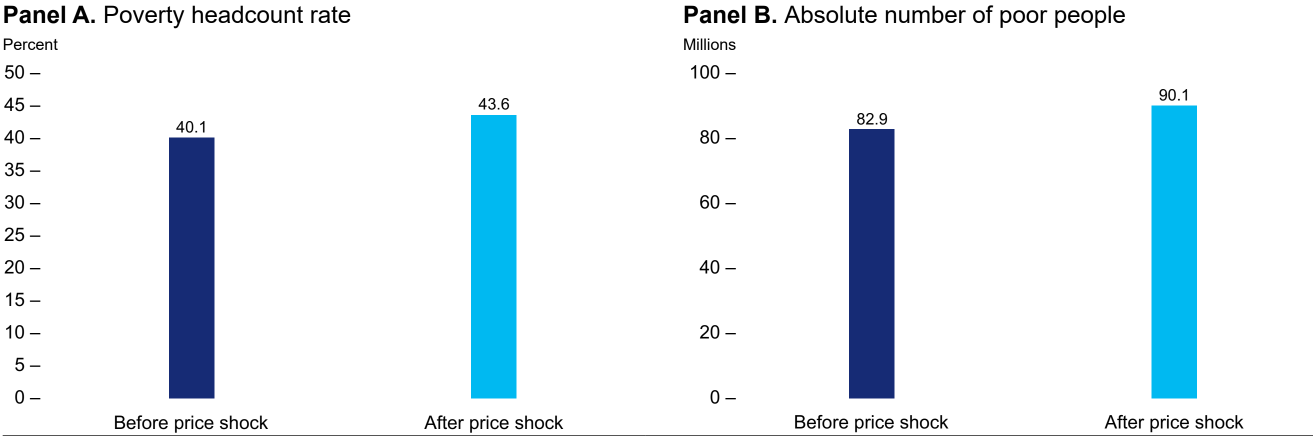


Source: 2018/19 NLSS and World Bank estimates.
Note: Estimates exclude Borno. Individual weights are used so charts represent full population. Bars show the share of the consumption basket devoted to each type of good, including zeroes (so the basket adds up to 100 percent). Deciles created using temporally- and spatially deflated consumption aggregate.

the consumption distribution, it is possible to ascertain how poverty would change when prices rise. It emerges that the 2020 price increases could push up the poverty headcount rate by as much as 3.5 pp—7.2 million people per the population estimates in the 2018/19 NLSS (see Figure 2.7).

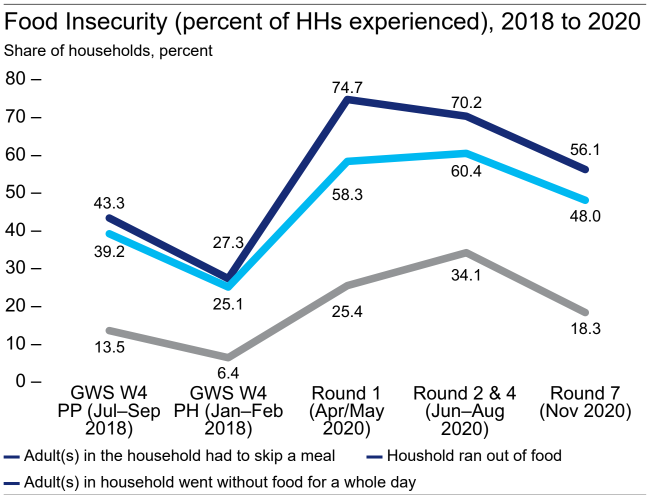
With purchasing power reduced, food insecurity is more widespread than it was before the COVID-19 crisis. The NLPS data confirm that Nigerian households adopted negative coping strategies in response to the 2020 price shocks. Between July 2020 and December 2020 about 58.3 percent of households dealt with the price shocks by consuming less food; 26.3 percent reduced their non-food consumption. The relatively high share of people who are working (see section on employment) may also be a signal that households are increasing their labor supply to offset lost purchasing power. It is therefore not surprising that food insecurity continues to be more prevalent than it was before the pandemic struck: in November 2020, adults in 56.1 percent of households had skipped meals in the previous 30 days and 48.0 percent of households ran out of food entirely (see Figure 2.8).

Figure 2.7. The rising prices witnessed in 2020 could increase the number of poor people by 7 million people.



Source: NBS price data, 2018/19 NLSS, and World Bank estimates.
Note: Estimates exclude Borno. Poverty calculated using national poverty line. Population taken from the sum of the 2018/19 NLSS weights.

Figure 2.8. Food insecurity is more widespread than it was before the COVID-19 crisis.



Source: 2018/19 GHS, NLPS, and World Bank estimates.

Policy options

Expanding social protection in the short run to provide time-bound support could alleviate the effects of inflation. In particular, the flagship social transfer program, the National Social Safety Nets Project (NASSP), could be scaled up both horizontally, by adding new beneficiaries, or vertically, by increasing benefits. The expansion could go beyond current efforts to scale up NASSP and other programs in urban areas in response to the COVID-19 crisis through the Rapid Response Register. Both rural and urban areas could be selected using Nigeria's new poverty map, which uses Big Data and machine learning techniques to construct granular measures of welfare for each ward in Nigeria. One concern is that cash transfers might intensify inflationary pressures more than in-kind transfers, especially in remote areas where the supply of goods and services is limited. Yet evidence from similar contexts suggests that cash transfers may in fact boost the consumption of non-recipient as well as recipient households—leading to spillover effects—without substantially increasing local price inflation (Egger, Hausehofer, Miguel, Niehaus, & Walker, 2019).

In the medium and long run, however, it will be vital to address the sources of inflationary pressures. This requires a sequenced and coordinated mix of monetary, exchange rate, fiscal, and trade policies to reduce inflation while laying foundations to control inflation over the following 6 to 18 months. Attempts to ease inflationary pressure should be accompanied by policies to boost job creation (see section on employment) because the labor market will be the main vehicle for sharing any proceeds from growth to individuals and households and for sustainably reducing poverty.

References

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Annex: Approach and caveats for welfare calculations

One way to understand the extent of the welfare losses caused by higher prices and reduced purchasing power is to calculate the money needed to maintain household welfare at the same level even as prices rise—the "compensating variation." Household exposure to price shocks depends on the share of overall consumption they devote to each good, which is captured by the 2018/19 Nigeria Living Standards Survey (NLSS). Calculating the compensating variation then hinges on mapping the item-level price data published by the Nigerian National Bureau of Statistics (NBS) into the consumption basket from the 2018/19 NLSS. To gain a more granular picture of welfare losses for different types of households, the approach can be applied separately to each decile of the consumption distribution.

While these calculations make clear how severely inflation affects welfare, they are subject to many caveats, which underlines the need for more data:

- The NBS data on which the analysis is based comprise just 43 food items for which prices are made public, covering less than one-third of the average Nigerian consumption basket. Prices were likely increasing for other items in the basket, which would deepen the effects on purchasing power, welfare, and poverty.
- As prices rise, households may purchase less expensive items, which could reduce some of the measured impacts: the analysis does not capture this type of substitution.
- The analysis focuses only on overall consumption, without separating purchases from own production, and does not consider the effects of price rises on the earnings of households that are net producers. For example, households that sell the goods for which prices are rising may enjoy higher profits.

Part 3: Spotlights on Nigeria's Development Agenda

Spotlight 1: Igniting economic growth by reforming Nigeria's power sector

Summary: *Electricity not only fuels productivity, it is a vital catalyst in health, education, and other forms of social development. According to the latest Tracking SDG7 report, 85 million Nigerians (43 percent of the population) have no access to electricity. Lack of reliable power stifles economic activity; in Nigeria, annual economic losses from lack of reliable power are estimated at 5 to 7 percent of GDP—at a cost of US$25 billion). The transition to a largely privately owned sector did not bring about the outcomes expected. Distribution companies (DISCOs) report inefficiencies measured by aggregate technical, commercial and collection (ATC&C) losses at about 50 percent, far above the 15 percent that is international good practice. The inefficiencies combined with the irregularity in applying the tariff policy have led to a breakdown of the electricity payment chain. The cumulative shortfalls in tariff collections for 2015–19 were estimated at ₦1,678 billion (~US$6.0 billion). In 2019 the tariff shortfall rose to ₦524 billion (~US$1.7 billion), which was more than the total Federal Government of Nigeria (FGN) health budget.*[16] *It was also fiscally unaffordable. The FGN has recognized that the severely underperforming power sector threatens Nigeria's recovery from the oil price shock and the COVID-19 crisis; in 2020 it began to take critical action to help turn the sector around.*

The country that currently has the least access to electricity in the world needs a power sector capable of meeting demand as it grows

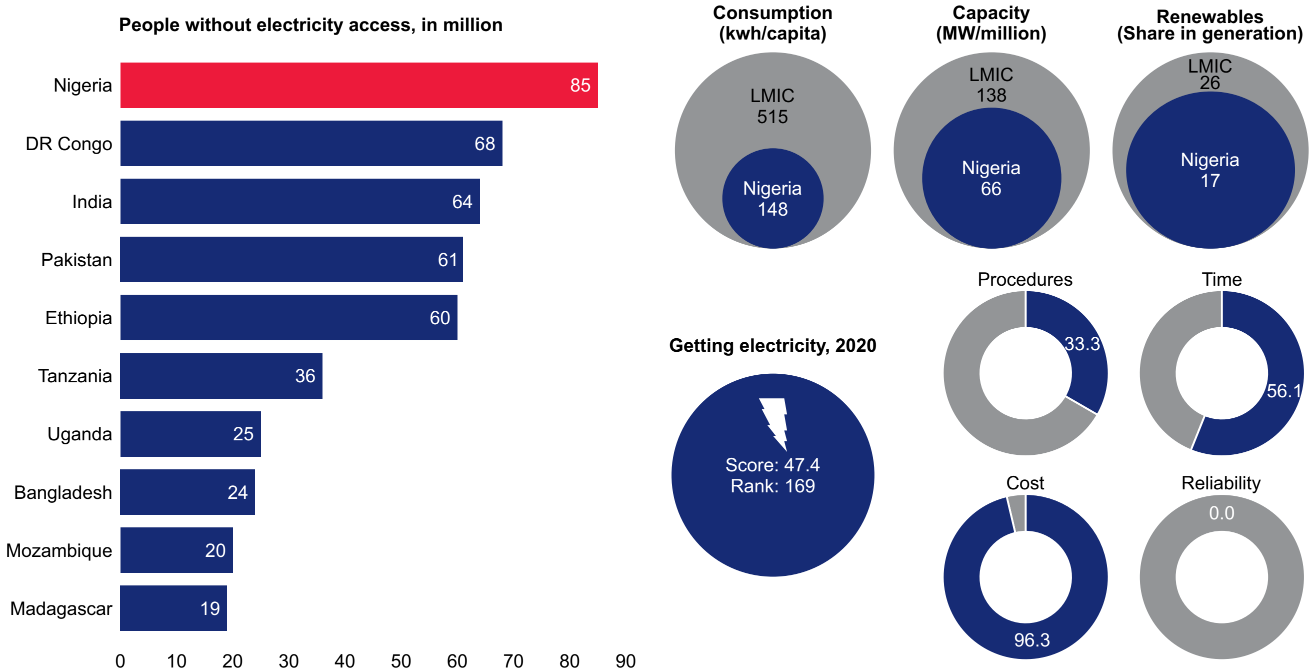
Nigeria's power sector problems have serious repercussions for economic growth. With 43 percent of the population (85 million people) lacking access to grid electricity, Nigeria has the world's largest energy access deficit (Figure 3.1). Nationwide, for the poorest 40 percent of the population, access to grid electricity is an abysmal 31 percent. Similar disparities exist between regions and between rural and urban areas. Even those who are connected to the grid cannot rely on the supply; they must deal with frequent outages. Firms cite lack of reliable power supply as the top constraint to their business. In the 2020 *Doing Business Report*, of the 190 countries surveyed, Nigeria ranked 169th globally on the *getting electricity* indicator, and it was 33rd of the 46 countries in SSA. In the report the reliability of its electricity scored 0.

With the electricity supply unreliable and insufficient, businesses and wealthy homes have turned to expensive gasoline-run generators. It is estimated that in Nigeria over 22 million gasoline generators ("gensets") power about 26 percent of all households and 30 percent of MSMEs; their net capacity is eight times more than the national grid. Inhalation of smoke from gensets is linked to about 1,500 deaths annually. In 2018 alone the FGN is estimated to have spent ₦490–₦670 billion (US$1.6–2.2 billion) on subsidizing gasoline consumption for them. On top of that, ordinary Nigerians spent an estimated ₦3.7 trillion (~US$12 billion) on purchase and operation of gensets. Annual economic losses from the unreliable electricity

16 In 2019 the tariff shortfall was ₦524 billion; the FGN budget for health was ₦428 billion.

Figure 3.1. Nigeria's unreliable, and for many inaccessible, power supply is a threat to economic growth.

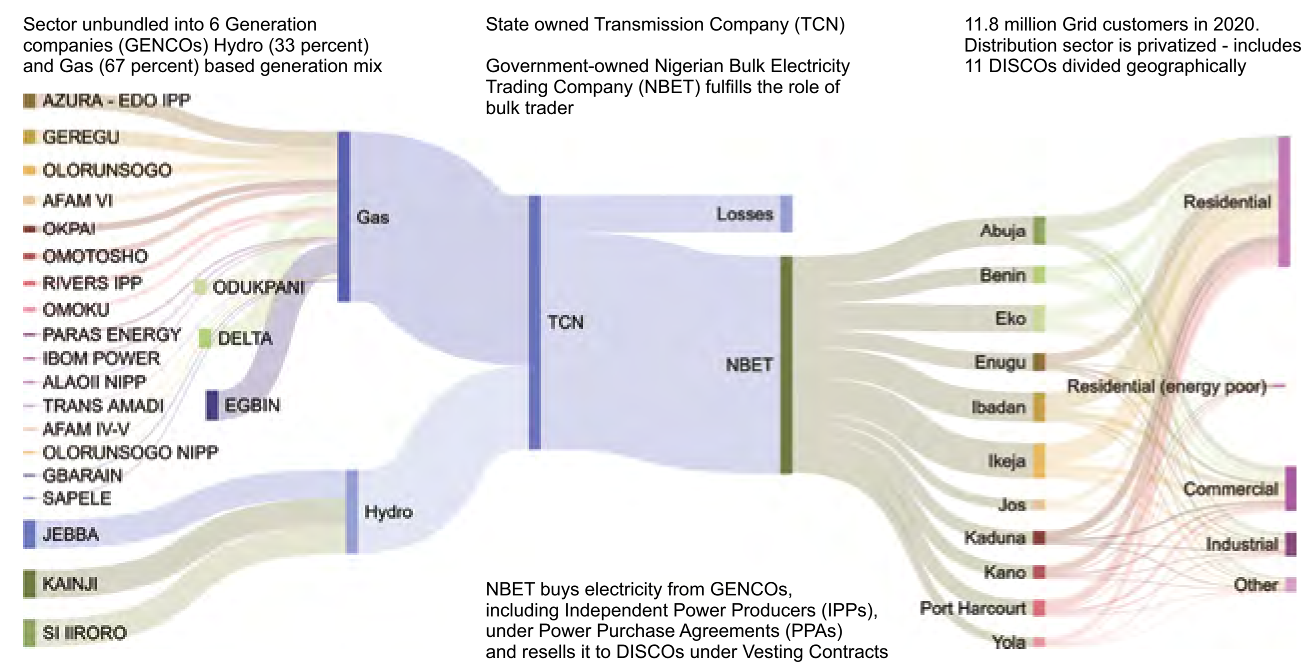
Nigeria's consumption per capita, installed capacity, renewable share, access to electricity and on the Getting electricity indicator in the Doing Business Report



Source: Consumption, capacity and renewables from IEA and EIA. People without alectricity access from Tracking SDG7, 2020. Getting electricity from Doing Business 2020.

Figure 3.2. The power sector is unbundled and largely privately owned.

Electricity grid



Source: World Bank 2020.
Note: Thickness of the curved bars indicate volume of energy (GWh) flowing.

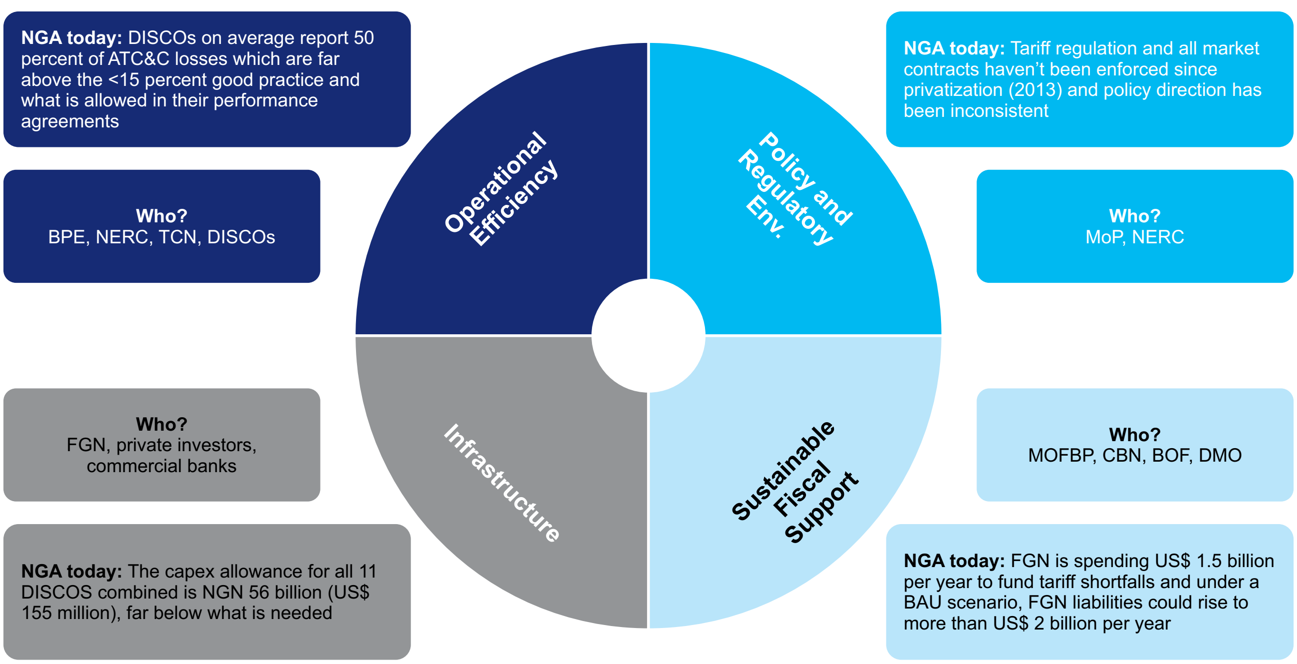
supply are estimated at about ₦7–10 trillion (~US$25 billion)—5–7 percent of the GDP.

Nigeria's power sector is unbundled and since 2013 has been largely privately owned, but the transition did not produce the expected results. After the Electric Power Sector Reform Act was passed in 2004, the sector was unbundled into six generation companies (GENCOs), eleven distribution companies (DISCOs), and the Transmission Company of Nigeria (TCN). By 2013 the DISCOs and GENCOs had all been privatized. Three of the five thermal GENCOs, which use natural gas as fuel, were sold in their entirety to new owners, and three hydro GENCOs were transferred to private operators through concession contracts. TCN is still a government-owned monopoly. In the current stage of market development, known as the Transitional Market,[17] the government-owned Nigerian Bulk Electricity Trading Company (NBET) fulfills the role of bulk trader. NBET buys electricity from GENCOs, including independent power producers (IPPs), and resells it to DISCOs. The transition from a publicly-owned to a largely privately-owned power sector did not bring the expected performance and service quality outcomes. Government ministries and agencies, the Nigeria Electricity Regulatory Commission (NERC), and the private sector have all fallen short of their expected contributions to the sector turnaround.

Inconsistent application of tariff policy has made sustainable electricity operations difficult. Although sector regulator NERC periodically issues Multi-Year Tariff Orders (MYTOs[18]) they are not actively enforced, with frequent delays often due to external factors like litigation. This delay causes the financial situation of sector companies, especially DISCOs, to deteriorate and leaves NERC unable to enforce the contractual obligations of the privately-owned GENCOs and DISCOs. There is also a lack of clarity about how to reduce losses and meet the capital expenditure targets specified in the Performance Agreements between

Figure 3.3. The power sector must deal with four different types of problems.

Comprehensive measures to move Nigeria's power sector forward sustainably are needed



Source: World Bank 2020.

17 This is an intermediate step consisting of a bulk buyer (to interface between GENCOs and DISCOs) envisaged ass leading ultimately to a fully functioning willing-buyer (DISCO) and willing-seller (GENCO) with no intermediary.

18 The MYTO methodology followed in Nigeria uses an incentive-based regulation that seeks to reward performance above certain benchmarks.

DISCOs and the Bureau of Public Enterprises (BPE), which are used to determine the tariff policy.

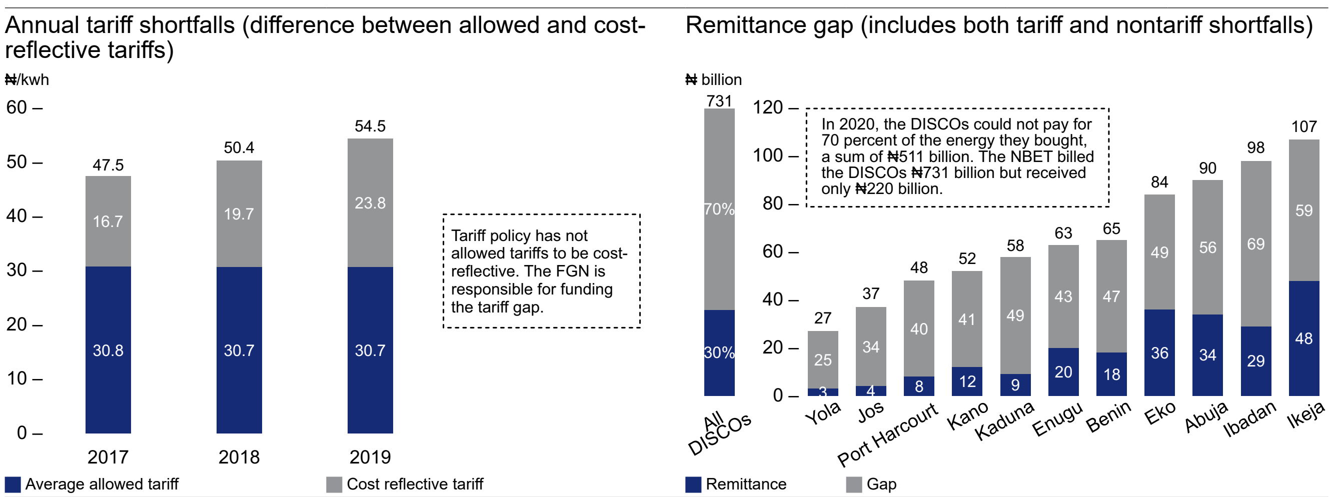
The distribution segment is struggling with exceptionally high losses and low collections. The sector's aggregate technical, commercial, and collection (ATC&C) losses are extremely high, with DISCOs reporting on average 50 percent in 2020, versus 26 percent allowed by NERC in the tariff policy. These high losses are exacerbated by inadequate metering of end-use customers and the failure of many ministries, departments, and agencies (MDAs) of federal, state and local governments to pay their electricity bills. The high losses, coupled with lack of payment discipline by DISCOs and inadequate contractual enforcement of those payments by NBET and NERC, results in low remittances to NBET by the DISCOs (Box 3.1).

Lack of cost-reflective tariffs since 2012 and low remittances of DISCOs to NBET forced the FGN to intervene and cover the shortfall—a significant fiscal burden. The FGN is responsible for funding the tariff shortfalls, which are the difference between allowed and cost-reflective tariffs. Since 2012, the tariff shortfall widened significantly because allowed tariffs stayed flat but cost-reflective tariffs shot up due to foreign exchange depreciation and domestic inflation. The cumulative shortfalls for 2015–19 were an estimated ₦1,678 billion (US$6.0 billion). To ensure that the GENCOs and gas suppliers received enough payments to continue generating electricity, since 2017 the FGN has borrowed a total of ₦1,301 billion (US$4.2 billion). In 2019 total FGN support reached N524 billion (US$1.7 billion), 0.4 percent of GDP—higher than the ₦428 billion budget for health and just 20 percent less than the ₦650 billion budgeted for education.

The FGN wanted to keep electricity tariffs low to protect the economically disadvantaged, but most of the benefits went to the relatively wealthy. Every Nigerian who receives electricity from a DISCO pays less[19] for electricity than the cost of supplying it. However, 80 percent of the spending on tariff shortfalls benefits the richest 40 percent of the population; only 8 percent benefits the bottom 40 percent, and of this less than 2 percent benefits the poorest 20 percent. Significant resources spent on funding tariff shortfalls disproportionately benefit the relatively wealthy who have access to the grid and use more electricity, so that ultimately a big chunk of government support goes to those who do not really need help with paying bills.

The need to turn the power sector around has long been recognized by all parties—the government, the electric supply industry, the private sector, and international partners—as one of Nigeria's most

Figure 3.4. The Government has had to step in to cover shortfalls and let the energy flow.

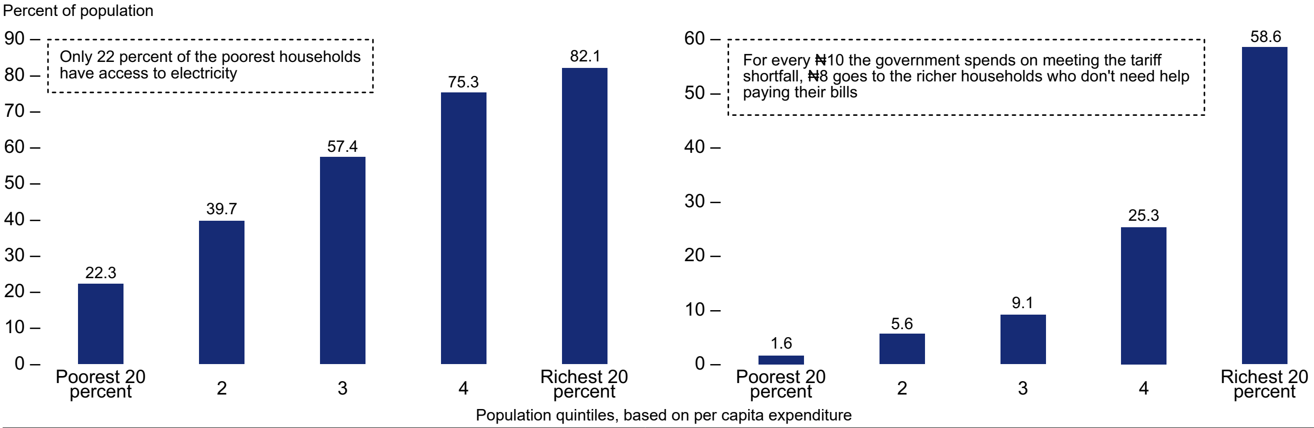


Source: Nigerian Electricity Supply Industry (NESI) data, NERC.

19 This excludes the amount spent by consumers on gasoline, gensets, solar and other alternatives to augment the unreliable supply.

Figure 3.5. Keeping tariffs low benefits the rich more than the poor.

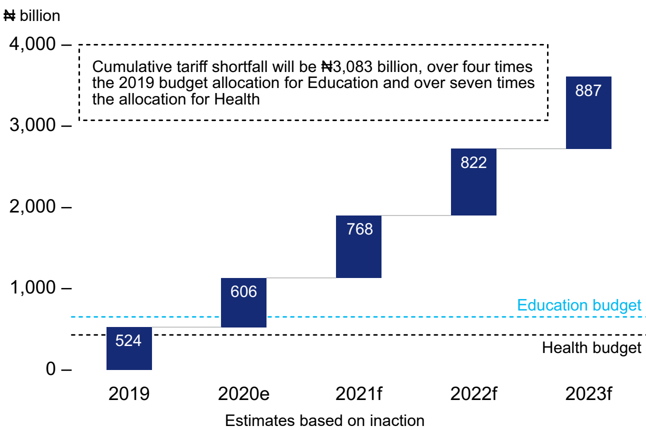
Distribution of government spending to meet the tariff shortfall



Source: World Bank 2020.

Figure 3.6. Early in 2020, it was predicted that through 2023 there would be another ₦3,082 trillion of tariff shortfalls.

Estimated new annual tariff shortfalls 2020–23 *if* tariffs remained unchanged



Source: NESI Data, NERC, and FGN Budget 2019.

critical development priorities. The cost of inaction is very high. At the start of 2020, it was estimated that if the sector continued its current performance and tariffs stayed not only flat but far below cost-recovery, through 2023 the FGN would have to provide another ₦3.082 trillion[20] (US$7.94 billion) in regressive subsidies that benefit mainly the wealthiest consumers. And this massive spending would not have bought any improvements in service quality. Apart from taking money away from other important social development efforts, the power sector itself would continue being a serious barrier to economic growth and a threat to fiscal sustainability.

The FGN is committed to reducing annual tariff shortfalls and in November 2020 took a significant step by introducing a service-based tariff (SBT),[21] which effectively increased tariffs by an average of 38 percent. The FGN has targeted reducing new tariff shortfalls from ₦502 billion in 2020 to less than ₦300 billion in 2021 in its PSRP Financing Plan as it moves power sector towards full cost recovery and a fair electricity pricing policy. The transition to the SBT and the increased payment discipline will enable DISCOs to increase collection efficiency and remittances to NBET and TCN, further improving the sector finances and enabling increased, better quality electricity supply to Nigerians. Reducing the tariff shortfall to improve financial and fiscal sustainability is one of the comprehensive reforms needed to turn the power sector around (see next section).

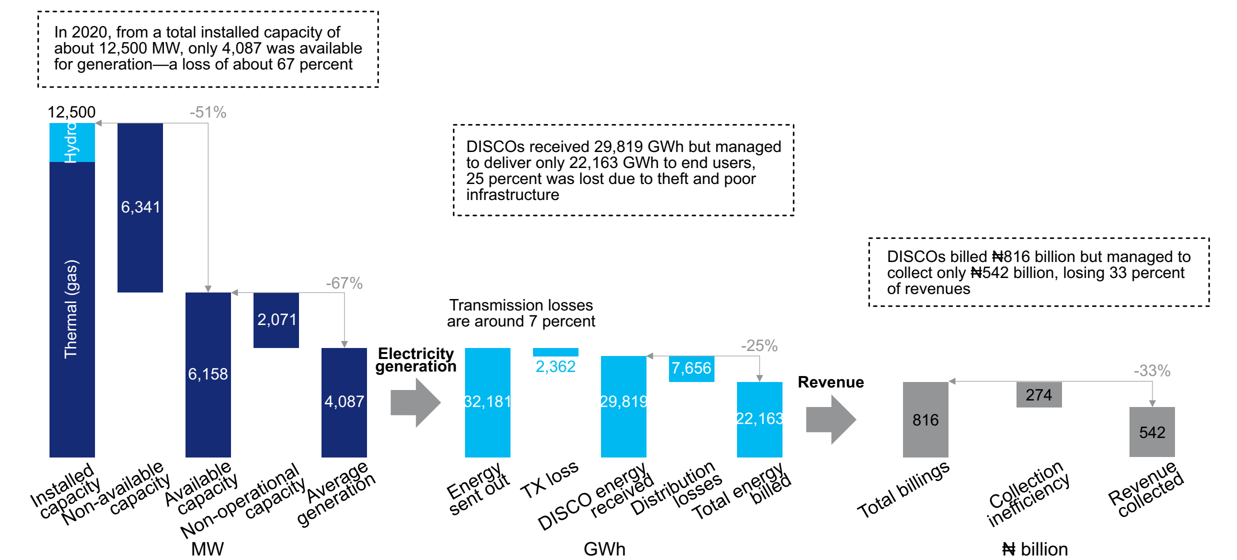
20 This analysis/scenario assumes no action on part of FGN in addressing tariff shortfalls. In reality, FGN did move in 2020 to narrow tariff shortfalls.
21 The SBT was introduced on September 1,2020 and suspended for October, but has been in effect since November 1, 2020.

Box 3.1. Understanding operational inefficiencies and their impact.

Operational inefficiencies in the sector are numerous. To understand their extent and the impact they have on sector finances, it is helpful to travel along the supply chain using 2020 data from NERC:

Generation: Nigeria has about 12,500 MW of installed capacity, dominated by natural gas (88 percent) with hydro making up the rest. However, just over 51 percent of this capacity was not available in 2020 due to maintenance and repair work. Of the 6,158 MW available during the year, an average of just 4,087 MW was actually used for generation, because of both insufficient gas supply, transmission and distribution constraints, and the inability of DISCOs to purchase power. As a result, in 2020 only 33 percent of installed capacity was used.

Figure B3.1.1. From Generation to Retail: Inefficiencies in the Nigeria power sector.



Source: NESI data, NERC.

Transmission and Distribution: The 4,087 MW of generation capacity available was used to generate 32,181 gigawatt hours (GWh) of electricity. This was sent to DISCOs, which received just under 30,000 GWh—a transmission loss of 7 percent, about 3 percent above benchmarks. Distribution network losses are also quite high. The DISCOs delivered only 75 percent of the electricity they received, losing 7,656 GWh to poor infrastructure and theft. In all 32 percent of electricity is lost during transmission and distribution.

Retail: DISCOs could bill 22,163 GWh of electricity to their customers (60 percent of whom are not metered). This should have ideally generated ₦816 billion in revenue for the DISCOs, but they were unable to collect only 33 percent of these revenues leading to collection of only ₦542 billion in 2020. Thus, inefficiencies in the distribution sector contribute a significant portion of the 50 percent aggregated technical, commercial and collection (ATC&C) losses.

A holistic approach integrating comprehensive measures is necessary to address Nigeria's power problems sustainably

Addressing problems of power sector offers Nigeria an opportunity to tackle longstanding challenges and give the economy a boost. To address the economic challenges that have arisen from the oil price shock and COVID-19, in July 2020 the FGN launched a ₦23 trillion (US$5.9 billion) Nigerian Economic Sustainability Plan (NESP). The NESP lays out an ambitious package of policy measures and programs to stimulate activity and create jobs through investments in agriculture, roads, renewables, and housing. But any economic recovery program will be severely challenged by minimal access to electricity, an insufficient power supply, and a financially unviable power sector. However, the focus on kickstarting the economy, and the general push to place it on a stronger and more sustainable recovery path, provide a new impetus to reforms in the sector.

There is a broad political consensus and real commitment to start turning around the sector by taking critical actions set out in the Government's Power Sector Recovery Programme (PSRP), some of which has already been done. The PSRP is a comprehensive package of financial, operational, governance, and policy interventions for restoring the sector's financial viability, improving service delivery, reducing its fiscal burden on the government budget, strengthening sector governance and transparency, and ensuring that contracts are enforced and reforms communicated. Given how urgent it is to address the multiple challenges in the sector, a Presidential Working Group has been created to coordinate and monitor the sector reforms. The FGN has chosen to undertake critical PSRP actions in all four areas: (a) policy and regulatory environment; (b) fiscal and financial sustainability; (c) operational efficiency; and (d) network infrastructure. It will not be easy to reverse many of the important regulatory actions, such as NERC requiring DISCOs to prepare and carry out performance improvement plans (PIPs), issuance of the order to cap estimated billing, and launching the extraordinary MYTO review to set new conditions for DISCOs and TCN. There is also widespread agreement within the government that improvements in sector performance are necessary conditions for future public funding, i.e., no more unconditional funding.

Increasing the capacity and reliability of the transmission network is critical to the sector's financial viability. Insufficient investment in transmission has curtailed the network's capacity to transport power, contributing to the fact that only 33 percent of the installed capacity is usable. There is a clear need to refurbish the transmission infrastructure to enhance system stability and ensure that the grid can dispatch generation at lower cost while increasing the supply. At the same time, Nigeria is a critical member of the West Africa Power Pool (WAPP), the regional market launched in 2018, which can significantly improve the electricity supply not just in Nigeria but throughout all of West Africa. By the mid-2020s it is expected that all 14 countries in the WAPP will be interconnected; efforts are already underway to increase the capacity of the network and to reinforce it in order to increase domestic supply and accrue the benefits of regional trade.

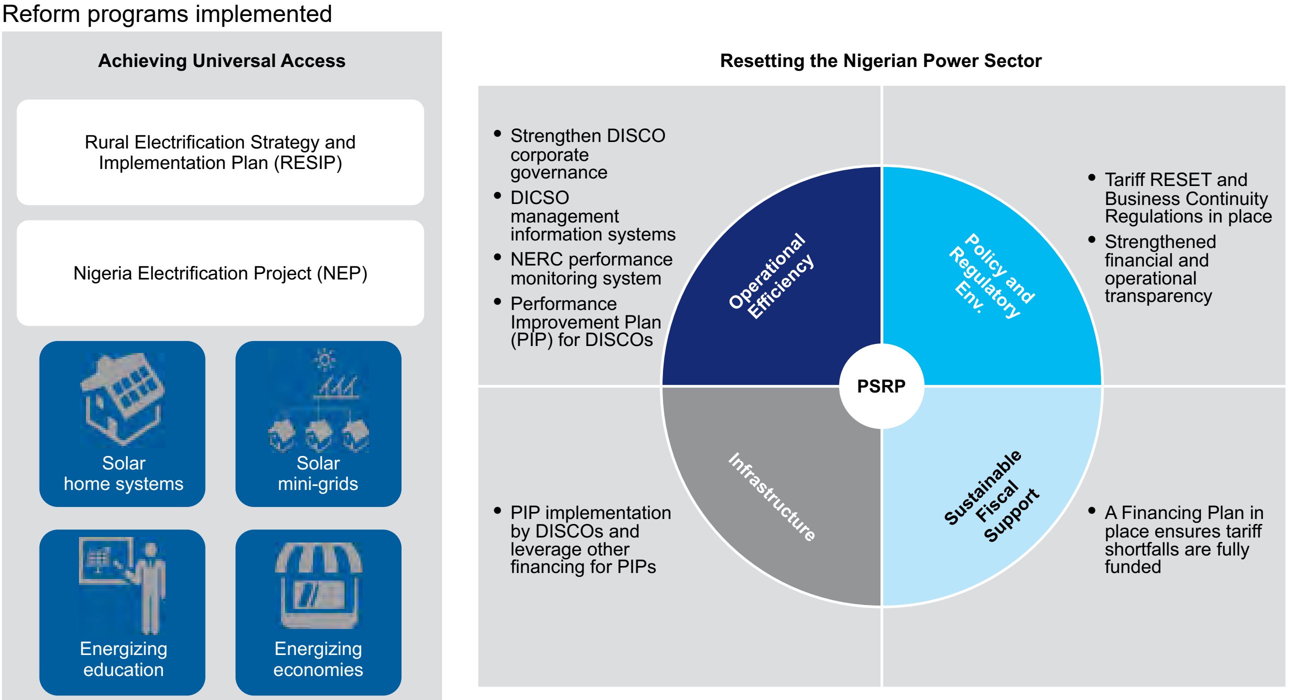
Because DISCOs own and operate the Nigerian distribution network, they are central to the turn-around of sector performance. The PSRP recognizes poor revenue collection and remittances, as well as insufficient investment, as factors in the inadequacy of DISCO performance. Recognizing the critical need to improve distribution and transmission networks the FGN has provided ₦240 billion to improve services and resolve transmission and distribution bottlenecks. Programs such as the National Mass Metering Program aim to increase metering significantly to help DISCOs increase their billing transparency and collection efficiency. PIP preparation and activation under NERC guidelines will ensure that investment planning is fact-based rather than speculative. Timely adherence to PIPs will improve the technical and financial performance, and the governance, of DISCOs, reducing ATC&C losses, increasing collection rates, and connecting more customers to the grid. This will eventually enable the sector to end FGN assistance and fill its investment needs by accessing private financing.

Increasing operational efficiency and improving infrastructure are essential for a transition to clean energy. The energy sector is the largest contributor to Nigeria's greenhouse gas (GHG) emissions. The country has committed to cutting its GHG emissions by 45 percent by 2030, primarily from the energy sector; 22 percent of the targeted emissions can be met by replacing the more than 20GW of gasoline-based generator capacity that Nigerians use to supplement grid-based electricity. In the short to medium term, distributed solar-based solutions for homes and rooftops, and mini grids, can be used to replace the gensets using innovative business models and financing that meets the needs of end-users, developers, and local finance institutions. In the long run, grid-connected solar capacity is a critical component of the least-cost generation path that can keep the sector in line with the Nationally Determined Contribution targets. A framework that addresses credit risk for buyers and allows market-based mechanisms for bilateral deals between generators and DISCOs will be required if grid-based solar is to take off.

There is widespread acknowledgment that increasing access to electricity is critical to Nigeria's plans for recovery from COVID-19 and the oil price shock. To achieve universal access to electricity by 2030, Nigeria would need to connect 500,000 to 800,000 households every year. Both grid-extension and off-grid solutions will be needed to provide timely quality services to unserved and underserved households and businesses, especially as the country recovers from the impact of the pandemic. Recognizing the need for action outside the grid-connected areas that the DISCOs currently service, the FGN launched the Rural Electrification Strategy and Implementation Plan and the Nigeria Electrification Project to focus on underserved rural populations and

Figure 3.7. FGN is already responding to the policy priorities for the power sector.

Reform programs implemented



Source: REA and FGN.

rural institutions. The Rural Electrification Agency has since established the Rural Electrification Fund. Additionally, the FGN launched the Solar Power Naija initiative in April 2021 that aims to roll out 5 million solar connections in communities that are not connected to the grid.

Key policy options for the power sector

Why Reforms Are Needed	*Which Reforms Are Critical*	*What Impact these Reforms Could Have*
Strengthening the Policy and Regulatory Environment		
• One of the biggest challenges in the sector is inadequate enforcement of sector contracts. Delays in issuance of MYTOs on tariff reviews and effective application of their outcomes hurt the sector. Performance targets for DISCOs under current MYTOs fall short.	• Carry out an extraordinary tariff review for all DISCOs and before year end 2021 issue new MYTOs to set the revenue requirements for these companies for 2022–25. *Who:* NERC • Include in revenue requirements allowances for capital and operating expenditures and estimated total aggregated technical and commercial losses in supply, based on Performance Improvement Plans (PIPs) approved by the Regulator. *Who:* NERC • Sector institutions fully commit to adhere effectively to sector contracts and regulations. *Who:* NERC, TCN, NBET, FGN • Improve the investment climate, including economic procurement of generation capacity pursuant to a Least Cost Development Plan (LCDP) and clarification of the monetary and fiscal policies that provide incentives for private investments in the power sector. *Who:* FGN	• DISCO payment discipline is strengthened and enforced. • Regulatory conditions are predictable and defined through 2025. • The investment climate improves.

Why Reforms Are Needed	*Which Reforms Are Critical*	*What Impact these Reforms Could Have*
Achieving Fiscal and Financial Sustainability		
• The FGN cannot afford the more than ₦500 billion (over US$1 billion) of new tariff shortfalls annually. DISCOs do not pay up to 70 percent of their invoices to NBET.	• Move toward full cost recovery with tariff adjustments through new MYTOs, accompanied by measures to protect the poor and enforce payment discipline. *Who:* NERC • Implement the PSRP Financing Plan to fully fund new tariff shortfalls and clear historical arrears with sustainable sources of funds. *Who:* FGN (Federal Ministry of Finance, Budget and National Planning - Budget Office of the Federation)	• Tariff shortfalls are fully funded and gradually reduced to zero. • The fiscal burden of the power sector on the FGN is reduced. • The financial situation of DISCOs improves as tariffs come to better reflect current conditions and the costs of efficient service delivery.
Improving Operational Efficiency		

• Operational inefficiencies in the system result in massive financial as well as economic losses. There is an immediate need to ensure that the transmission and distribution networks receive at least the minimum level of supply that allows the grid stability and reduction of system outages.	Address constraints in the transmission and distribution segments and maintenance issues in generation.
	• Implement PIPs[22] approved by NERC in late April 2021, to be reflected in MYTOs of extraordinary review for 2022–25.
	Who: DISCOs
	• Systematically oversee DISCO performance after MYTOs are issued, and adopt corrective action (including license revocation) when DISCOs fail to adhere to PIPs and deliver on MYTO provisions.
	Who: NERC
	• Follow corporate governance and transparency best practices.
	Who: DISCOs
	• Increase accountability and transparency:
	  • Timely publish financial statements of DISCOs audited according to International Financial Reporting Standards.
	  Who: DISCOs
	  • Publish key operational and financial performance data of the sector every quarter.
	  Who: NERC
		• Minimum supply necessary for grid stability is achieved.
		• The distribution network is increasingly reliable.
		• Operations in all business areas of DISCOs are efficient, transparent, and accountable.
		• Investor confidence increases as DISCOs emerge as credible commercial partners.
		• Sector credibility and investor confidence both increase.

22 DISCOs prepared PIPs based on guidelines issued by NERC in 2019 that could incorporate tools (information systems, revenue protection programs, etc.) to improve efficiency and enhance transparency and accountability in operations.

<table>
<tr><th>Why Reforms Are Needed</th><th>Which Reforms Are Critical</th><th>What Impact these Reforms Could Have</th></tr>
<tr><td colspan="3">Expand and Improve Infrastructure</td></tr>
<tr><td>• Substandard infrastructure is a major factor in sector inefficiencies. There is an urgent need to improve and expand the network to improve the quality of supply.
• Poor access to electricity severely impacts the economic prospects of all Nigerians. About 43 percent (~85 million people) of the population has no access to electricity.</td><td>• Define technical and operational interventions required to turn-around operations.
• Identify the capital investments required to do so in the PIPs.
Who: DISCOs
• To close the metering gap, effectively implement programs for metering of customers.
Who: DISCOs
• Tackle electricity theft and bill collection to reduce the critically high ATC&C losses.
Who: DISCOs
• Upgrade, rehabilitate, and reinforce transmission lines.
Who: TCN
• Adopt a dual strategy to expand access to electricity service that involves off-grid access solutions, such as mini grids and solar home systems. Focus on underserved rural populations and rural institutions, such as schools, health centers, and administrative buildings as well as rural businesses, farms, and enterprises for job creation and economic development.
Who: FGN, REA</td><td>• ATC&C losses are reduced from an unsustainable 50 percent.
• Quality of service improves.
• Better collection increases revenues
• Increase i transfer capacity of the transmission network.
• Dispatch least-cost generation and enhance regional trade to optimize costs.
• Increase access.</td></tr>
<tr><td colspan="3">Clean Energy Transition</td></tr>
<tr><td>• The energy sector is the largest contributor to GHG emissions. Over 20GW of gasoline genset capacity is employed by households and small businesses, about 8 times more than the national grid.</td><td>Short and Medium Term
• Create enabling regulatory and policy for unlocking Distributed Photovoltaic (DPV) solar market.
Who: NERC, FGN, State Governments, CBN, DFIs
• Identify innovative-use cases and business models for scaling up DPV.
Who: Private sector, DFIs, FGN

Long Term
• Define enabling conditions for development of large-scale grid connected solar projects.
Who: NERC, FGN, DISCOs, GENCOs</td><td>• Renewables comprise a larger share of the generation mix.
• GHG emissions from the power sector are reduced.</td></tr>
</table>

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IEA, IRENA, UNSD, World Bank, WHO. 2020. *Tracking SDG 7: The Energy Progress Report*. World Bank, Washington DC

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Spotlight 2: Options to raise revenues in a time of crisis

Summary: *Nigeria is Africa's biggest economy but has the lowest tax-GDP ratio on the continent of just 4 percent. Tax revenues are necessary to ensure essential services, provide security to citizens, help tackle hunger and poverty, and deliver critical health and education services. The COVID-related economic slowdown coupled with the plunge in oil prices in 2020 brought into sharp focus the need to increase non-oil revenue in a time of crisis when investment, jobs, and growth also need to increase. This calls for policy and administrative measures that are carefully calibrated to grow revenues without negatively impacting investment. This rules out any increases in traditional ad valorem taxes like the value-added tax (VAT) but opens a window to fully implement the already existing tax policies and reform tax administration to seal compliance gaps. There is potential for harvesting revenue-yielding fruits such as increasing "sin taxes," charging fees for electronic money transfers, rationalizing tax expenditures, removing loopholes in tax laws, and improving tax compliance by reinforcing revenue administration. Over the next three years, measures like these could raise the tax-to-GDP ratio to about 7 percent, bringing in an additional ₦10 trillion. In the longer term, fundamental reform of the tax system is needed to stimulate post-pandemic investment and economic growth. As Nigeria tries to "build back better" after the COVID crisis, the approach to revenue mobilization needs to be more strategic: not just taxing more, but taxing better; not just how much to collect, but how to collect, what to collect, and from whom.*

Africa's biggest economy also has Africa's lowest tax-to-GDP ratio: Nigeria must mobilize far more revenue if it is to capitalize on its immense economic potential

To achieve sustainable, and inclusive, growth; build a resilient economy; and achieve the aspirations of its people, Nigeria must address its perennially low revenue mobilization. Its 2019 tax-to-GDP ratio of 4.2 percent was less than one-third of the SSA regional average. This is the product of many years of overreliance on resource revenues from oil and gas, a strategy that is no longer viable due to the volatility of oil demand and prices and to inefficiencies in the oil sector. The inefficiencies have perpetuated a vicious cycle of under-investment, low human development, and low incomes.

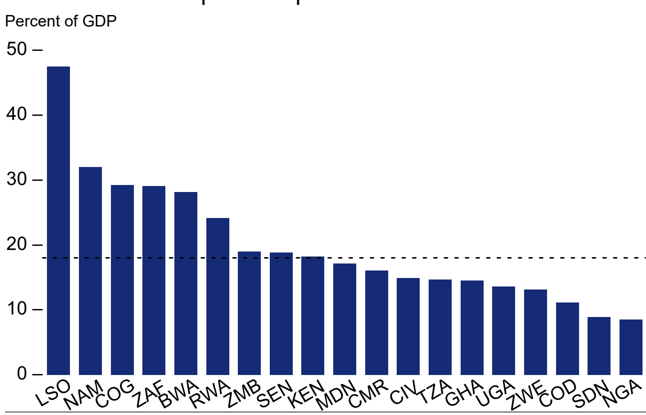
The COVID-19 pandemic has added more pressure on already subdued domestic revenue and threatens to push Nigeria further into deficit. In addition to the drop in oil and gas revenue, as economic activity slowed. and, in some cases stalled, the pandemic has also had adverse impacts on other revenue streams. Households consumed less, and corporate profits fell, reducing VAT collections and corporate income tax (CIT)—two of the largest sources of non-oil revenue. The pandemic has also reduced the scope for tax administration enforcement actions; and minimal use of automation in tax administration precluded any leveraging of technology to improve compliance.

While COVID-19 wrought many challenges, it also brings about a rare opportunity to make changes that could give revenues a major boost in the long run. Further pressure on oil prices and diminished demand forces the Nigerian government to seek alternative sources of revenue that are easy to tap into at minimal disruption to the economy. Normally, the ease of collecting resource revenues renders alternative sources secondary. In other words, the continuing COVID-19–related economic challenges may have a silver lining. The revenue streams suggested below and administrative reforms to bridge compliance gaps are likely to be sticky beyond the pandemic. This would be a boon to the economy, especially if resource revenues recover.

However, avenues for accelerating DRM should be limited to those that do not jeopardize investment, growth, or jobs. While Nigeria's economy has performed better than expected, in 2020 it was hit by the deepest recession in almost four decades, and growth this year is still expected to be moderate. Revenue-raising policies and administrative actions must be carefully chosen so as not to undermine an already weak growth recovery path.

Figure 3.8. Nigeria's revenue collection is far behind that of peers.

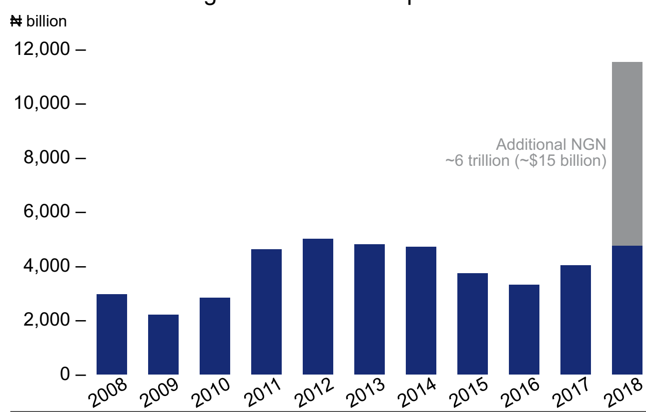
Total revenue compared to peers



Source: Federal Inland Revenue Service (FIRS) and IMF *2018 Revenue Statistics*.

Figure 3.9. Revenue can be doubled with minimal disruption of the economy.

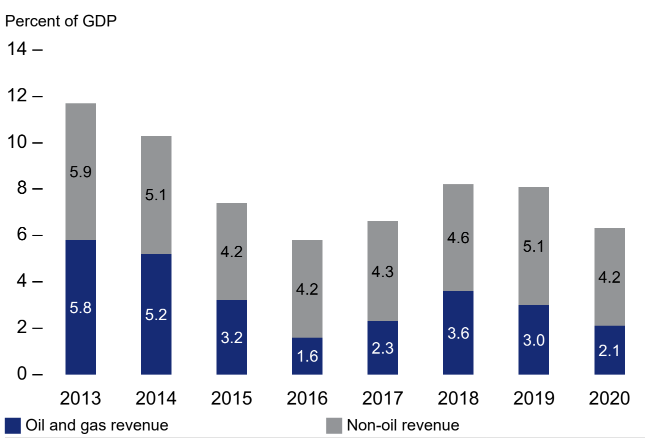
Potential revenue gains at median of peers



Source: FIRS and IMF *2018 Revenue Statistics*.

Figure 3.10. Driven by crises, general government revenue continues to fall.

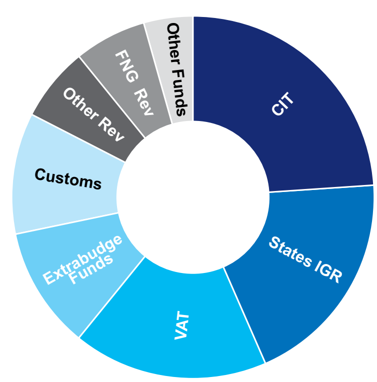
Trend in oil and non-oil revenue



Source: FAAC data from the FIRS.

Figure 3.11. CIT and VAT are the largest sources of non-oil revenue.

Share of non-oil revenues sources in 2020



Source: FAAC data from the FIRS.

Figure 3.12. Sequenced reforms will best mobilize revenue.

Immediate	Medium Term	Long Term
Enhance excise rates on "sin goods" and establishing ecise on petrol and diesel at a token rate. **Implement the Electronic Money Transfer levy.** This revenue source is sustainable and is likely to grow in coming years. **Improve overall tax compliance** with focus on VAT. Complemented by measures to enhance the efficiency of FIRS through ICT capacity, HR management and training of staff, organizational reforms and process improvements.	**Rationlize tax expenditure:** Nigeria offers a wide range of tax concessions that cover a range of taxes, with the largest impact being in CIT and VAT. Nigeria does have a legislative framework in place for measurement and grant of tax expenditures (the Fiscal Responsibility Act, 2007), which can be leveraged to rationalize ineffective tax incentives. **Reforms key tax statutes at the Federal level,** i.e. the Corporate Income Tax Act (CITA) and the Value Added Tax Act (VATA), including plugging loopholes, rationalization of the treatment of expenditures (CITA) and credits (VATA), and development of anti-fragmentation rules.	**Improve revenue from cross border transactions and other international tax measures.** These range from improvement of personal income tax from undisclosed overseas deposits and illicit financial flows through better use of information gained under exchange of information, to VAT on online transactions, and CIT from accurate application of transfer pricing rules. **Enhance Internally Generated Revenues (IGR).** Efforts are needed to improve States' collection of PIT and other taxes such as the property tax.

The economy has adequate space for administrative and policy reforms that do not negatively impact investment and growth

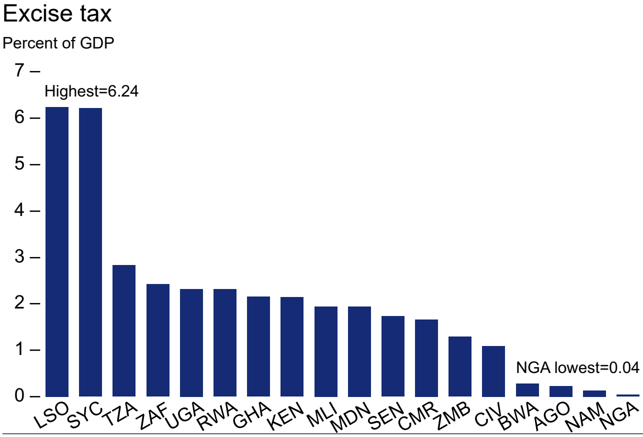
World Bank estimates that Nigeria's non-oil revenue potential is more than twice what it currently collects; with the right reforms, it should be possible to reach a tax-to-GDP ratio comparable to regional peers like Ghana and Uganda at 12 percent and Kenya at 15 percent. The government has already taken major steps to reform the VAT, and has prepared its first tax expenditures statement. There is now an opportunity to build on this momentum, especially given the urgent need to marshal resources for post-COVID recovery. In view of the complex political economy and the administrative and legal constraints that obtain in Nigeria, a sequenced reform approach is likely to achieve the best outcome.

Excises can help lower the cost of environmental pollution, improve health prospects, and boost tax revenue by up to 1 percent of GDP

Although the rates were increased in 2017, at 0.04 percent of GDP, Nigeria's excise taxes are among the world's lowest. While the primary purpose of an excise is to internalize the social costs of harmful goods like alcohol and tobacco, their revenue contribution can also be important. Nigeria does not subject liquid fuel to tax, which is unfortunate since excises could capture the cost burden of fuel on the environment, and this revenue source is inherently stable because demand for fuel is inelastic.

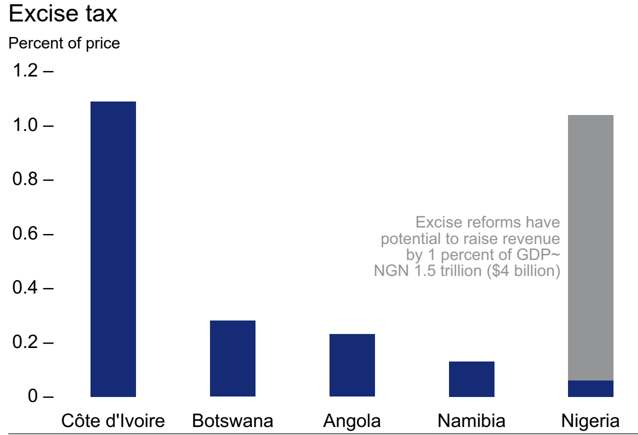
Enhancing the excise regime offers an immediate opportunity for revenue increases; an appropriate excise rate on beer alone could raise up to

Figure 3.13. Nigeria's excise tax revenue is among the lowest in Sub-Saharan Africa.



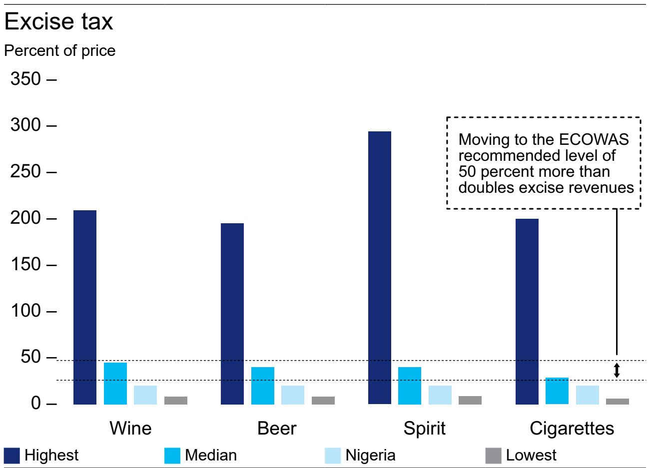
Source: IMF World Revenue Longitudinal Data.

Figure 3.14. Marginal improvement has consequential revenue implications.



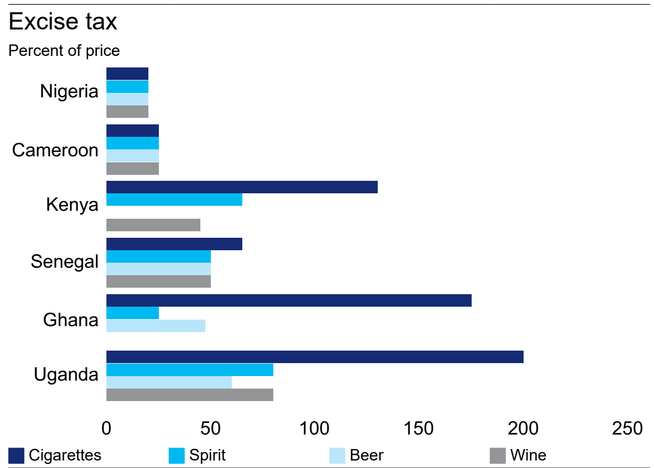
Source: IMF World Revenue Longitudinal Data.

Figure 3.15. There is ample space to raise excise rates for alcohol and cigarettes.



Source: PWC Worldwide Tax Summaries.

Figure 3.16. Nigeria's excise rates are lower than those of its peers.



Source: PWC Worldwide Tax Summaries.

₦600 billion. On alcohol and tobacco, Nigeria applies an ad valorem rate of 20 percent, which is less than half the median of its African peers. To effectively tap into this revenue source, Nigeria could retain the current ad valorem excises but augment them with specific ones. World Bank estimates show that retaining the current rates and gradually increasing the specific duty component to achieve tax incidence consistent with regional peers will generate additional revenue of ₦955 billion in the first year. Specific excises are preferable because they are simpler to administer and less vulnerable to avoidance through undervaluation.

The electronic money transfer (EMT) levy is a stable revenue source with potential to raise up to ₦462 billion in 2021

The EMT levy, introduced in the Finance Act 2020, which amended the Stamp Duty Act, taps into the growth in electronic funds transfer in Nigeria and can be administered at low cost. To maximize its impact, Nigeria must promptly issue regulations for the imposition, administration, collection, and remittance of the levy. Because the levy is quite wide in scope and presents interpretation problems, regulations should specify exclusions from the scope and specify in detail processes for administering the levy. Enforcement of some elements of the charge, such as inter-bank transfers, could be challenging in view of possible resistance from the banks and could be sub-optimal for overall tax compliance by incentivizing cash transactions. In terms of administration, there is also need for more clarity on who should be the competent authority to administer transactions between individuals.

Reforms of corporate income tax (CIT) can seal loopholes without raising the tax burden on compliant corporations, potentially raising revenue by 0.7 percent of GDP

In the current environment, in which raising CIT rates could suppress economic growth, targeting compliance and rationalization of tax expenditures provides an avenue for CIT-related growth: (1) An anti-fragmentation rule could be included in the Corporate Income Tax Act (CITA) to prevent medium and large companies from fragmenting business activity into multiple companies to take advantage of the exemption for small companies with turnover of less than ₦25 million. (2) The definition of "dividends" should be revised to include "disguised" dividends to prevent companies from funneling corporate profits to shareholders without paying tax. In the medium term, a technical diagnostic review of the CITA will be necessary to identify loopholes and technical deficiencies in current law and to rationalize costly tax incentives. Any progress toward more compliance in the current environment is likely to be sticky, however, persisting beyond the COVID-19 induced economic crisis.

VAT reforms introduced in the Finance Act 2019 can raise 0.4 percent of GDP in revenue, and another 1.4 percent could come from better compliance

While raising VAT rates is not viable in the short term due to the financial burden it would impose on the poorest Nigerians, broadening the VAT base and improving compliance would significantly raise VAT revenue. The Finance Act 2020 introduced VAT taxation of cross-border business-to-consumer digital supplies to align with the CIT digital tax introduced in Finance Act 2019. Proper application of this provision would significantly boost VAT revenues and open up room for future revenue growth as cross-border consumption of digital products continues to grow. In addition, an anti-fragmentation rule should be introduced to prevent splitting of business operations into small companies in order to fall below the VAT filing threshold introduced in Finance Act 2019.

In the medium term, the current 7.5 percent VAT rate, one of the lowest in SSA, can be raised to international levels of 10–15 percent. The limited input tax credit mechanism means that the Nigerian VAT operates more like a turnover tax applying at all levels of production and distribution. The mechanism should be reviewed and reformed, with the long-term goal of a broad-based VAT regime with a single rate and a comprehensive input tax credit mechanism. This would be the most efficient way to collect VAT revenue.

In the medium term, tax concessions should be rationalized to reduce market distortions

How governments deploy tax expenditures is critical, especially in the current economic context. Selective and targeted use of concessions can provide a lifeline

Table 3.1. In 2019 more than ₦1.1 trillion was lost in CIT expenditures.

Four main CIT concessions

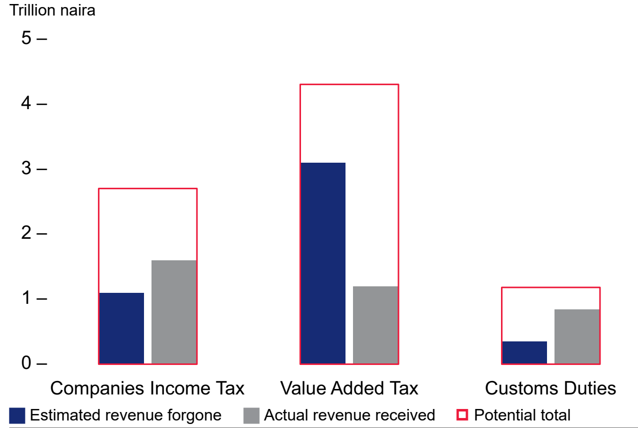
₦ billion

Main CIT Concession Claimed	*Tax Expenditure (Billion NGN)*
Interest on loans for agriculture, fabrication and cottage industry	999.7
Interest on securities	57.7
Research and development	34.1
Deductibles under S.23(1) CITA	17.8
Total TEs from four main concessions	**1,109.4**

Source: World Bank staff calculations.

Figure 3.17. Reviewing tax expenditures alone can double current revenues.

Cost of tax concessions in 2019



Source: World Bank staff calculations.

for struggling entities, especially those hit hardest by COVID-19. Rationalization could also greatly ease perennial revenue losses by closing loopholes in order to foster healthy market competition between corporations. The Nigerian tax system includes many concessionary measures intended to achieve various policy goals, but that can only come at the cost of lower tax revenues. These tax expenditures influence choices and create incentives for persons and businesses to alter economic behavior. For more efficient use of tax expenditures, the policy objectives for underlying individual tax expenditures must be clearly defined and the associated costs monitored.

There has been progress: in 2020 the government for the first time published a Tax Expenditures Statement (TES). The TES supplements the government's Annual Budget by providing data for analyzing the cost, benefit, and effectiveness of individual tax expenditures in achieving policy goals. Ultimately, the TES will allow for greater transparency, and will also inform discussion of the equity and efficiency of the tax system. According to World Bank estimates, ₦1.1 trillion in CIT, ₦3.1 trillion in VAT, and ₦347 billion in customs duties were forgone.

During crises, improving tax administration by fixing compliance gaps can bridge the revenue gap caused by low economic activity

A central lesson from the COVID-19 pandemic has been that it is critical for revenue administration authorities to maintain operations and business continuity[23] during a crisis. Before any revenue authority can tackle tax administration issues in times of crisis, it must first remain viable. Achieving this not only depends on the availability of reliable ICT platforms but also on good processes to enhance decision making in a rapidly changing environment in order to keep staff and taxpayers safe while still offering critical services to both taxpayers and the government. Nigeria's revenue agencies, FIRS and NCS, are working to accelerate the move to digital revenue administration. The goal is to provide taxpayer-friendly, world-class online services, characterized by efficient, paperless operations, and enhanced by ICT-enabled enforcement to optimize revenue.

With critical operations in place, investment in VAT compliance is likely to provide the best returns. A 2019 World Bank analysis of the VAT gap in 2019 found it to be as wide as ₦3.1 trillion. It estimated that

23 OECD, "Covid-19: Revenue Administration Implications, The World Bank Group, April 2020; CIAT/IOTA/OECD (2020), Tax Administration Responses to COVID-19: Business Continuity Considerations, OECD, Paris.

Table 3.2. VAT revenue potential.

₦ million

Focus Area	*Value*
Total VAT reported for 2010 (NBS)	560,998
Total VAT reported for 2019 (NBS)	1,188,581
Growth	2.12
Compound average growth rate (CAGR)	8.70%
Rate used (2019)	5%
Potential VAT revenue, assuming no policy or administrative leakage	4,323,381
Total leakage calculated	3,134,799
Potential VAT on capital under current policy	1,089,278
Revenue gain potential factor	3.6
Potential VAT revenue from tax on capital	92%

Source: World Bank staff calculations.

one-third was due to policy gaps, such as exemptions, and two-thirds to compliance gaps. The 2020 increase in the VAT rate from 5 to 7.5 percent is likely to widen the VAT compliance gap by at least 50 percent, and perhaps more if rising inflation is taken into consideration. Gains from improved compliance can allow the government to sustain critical spending without overburdening taxpayers in economic downturns.

Adopting a digital transformation strategy for an ICT-driven FIRS and enhancing its organizational efficiency will allow FIRS to weather future crises better

Done well, digital transformation of FIRS operations may be a positive consequence of the pandemic. Considering the drop in revenue collection since the onset of COVID-19, FIRS is crafting a digital transformation strategy to establish a strong ICT backbone for the tax authority. The three-year Strategy (2021–23) intends to align IT priorities to FIRS business needs, highlight areas to be supported for stable operations in future, identify application and IT service development priorities, and provide a framework for continuous improvement of IT service delivery within the FIRS and a roadmap to achieve its objectives.

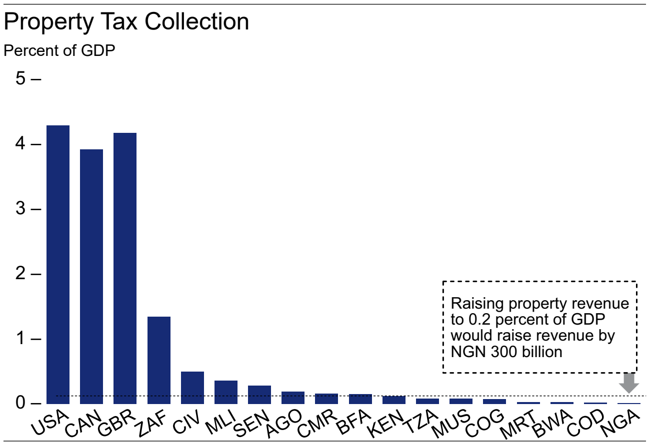
While physical infrastructure, such as ICT equipment, is important, equally critical is organizational efficiency. Currently, efficiency is obstructed by overlapping management structures, lack of standard operating procedures, and inconsistent work processes. These challenges can be resolved in large part by redesigning the organization, improving and digitalizing business processes, standardizing work procedures, and building capacity and otherwise improving human resources (HR) management. Staff should be trained and regularly retrained to improve both efficiency and retention. Over the long term, appropriate HR policies, planning, and processes need to be put in place, supported by robust monitoring and evaluation. Reforms underway should be periodically evaluated, using standard tools like the World Bank Group's DIAMOND assessment methodology.

Reforms to state tax administration can supplement federal revenue collection efforts, internally generated revenue (IGR) being the third largest source of non-oil revenue after VAT and CIT

A significant part of the fiscal challenge in Nigeria stems from the distribution of tax administration between Federal and State levels. While there are political and constitutional constraints on what taxes can be collected, it is still possible to make improvements that can materially affect the amount of revenue collected. Of note is the revenue potential from personal income tax (PIT) and property taxes.

The PIT collected by states is low due to tax evasion; certain classes of taxpayers escape the income tax net entirely. A major problem is underreporting by high-net-worth individuals (HNWIs) and unincorporated business. There is also a large informal sector, with many small-scale traders and businesses that do not report income. While enforcement should be conducted in all these areas, resources would be best used in pursuit of high-potential areas such as taxing HNWIs. Income data may be limited but it is possible to estimate HNWI income based on third-party sources of information, such as property cadasters, land use charge records, and other third-party sources, such as financial intermediaries and shareholder registers. Foreign income can be identified from the Automatic Exchange of Information data available through international initiatives.

Figure 3.18. Nigeria collects less in property tax revenue than its SSA peers.



Source: IMF, Government Financial Statistics, 2017; except Nigeria: World Bank estimate.

In addition to PIT, recurrent immovable property tax is a stable source of revenue for subnational and local governments all over the world. In advanced countries such as the US, Canada, and UK, as much as 3 percent of national GDP annually is collected through this tax instrument. This tax generates significant revenues in some Sub-Saharan African countries, notably South Africa, where it generates more than 1 percent of national GDP. Based on information collected from Nigerian states, total property tax revenue is estimated at 0.01 percent of national GDP, with most collecting less than ₦400 per capita.

Significant revenue can be generated from land use charges (LUC) to complement state IGR. This can be done by broadening the tax base, creating a database of properties and LUC payers within a geographic information system (GIS), improving the information on taxable properties, revising the assessment basis for the LUC, reviewing the current tariff structure, strengthening supporting legislation, and simplifying tax compliance. However, several factors make reforming this revenue source daunting.

1. **Incomplete or inaccurate records on potential taxpayers and insufficient information on properties do not support effective property taxation.** In several states and administration is carried out using manual approaches, paper-based property files, maps, and other legal documents. Lack of a computerized database of properties severely impedes tax administration and does not allow states to leverage the efficiencies of technology. A few states (notably Kaduna, Edo, Nasarawa, and Lagos) have set up GIS Administration Agencies to help them identify property records.

2. **In transfer deeds, property values are often not accurately stated, in part to reduce stamp duty liability, in part due to lack of laws to enforce honest disclosure.** Because property values are under-reported, the properties are under-taxed. Where states prescribe valuation of properties, the assessment methods for the LUC are not able to capture market values because market data is not reliable. Several states have therefore resorted to setting low, flat rates per property, even when the revenue collected is relatively small.

3. **Some states lack the legislation necessary to support the LUC levy.** In others, the legislation is not fully compliant with the Constitution. Where there is legislation, it is poorly enforced, lowering collection rates.

4. **Cumbersome compliance requirements** necessitate several visits to banks and government offices. Because LUC revenue is low, it should be possible to make payments via mobile money and other nontraditional mechanisms, especially when taxpayers do not have bank accounts.

Key policy options to mobilize revenues in a time of crisis

Why reforms are needed	*Which reforms are critical and when could they be carried out*			*What the impact of reforms would be*
	Reforms that can be carried out in 1–6 months	*Reforms that can be carried out within 18 months*	*Structural initiatives and institutional reforms that can put on a firm footing in the next 3 years*	
Non-oil revenues have been stagnant due to a sub-optimal VAT system, extensive use of tax incentives, lack of effective enforcement, and the high costs of tax compliance.	• Reform excise tax rates. • Implement the Electronic Money Transfer levy. • Launch VAT compliance improvement initiatives. • Craft the Digital Transformation Strategy for ICT in FIRS, laying the foundation for a tech-driven, efficient tax administration. • Build capacity in the audit and taxation of large business.	• Fully implement VAT and CIT compliance programs. • Make desk audits more effective. • Review CIT law; bring international tax rules in line with global good practices with emphasis on the practical. • Rationalize ineffective tax incentives. • Improve how Customs administers VAT, duty. and excises	• Build the capacity of federal tax and customs administration to improve compliance. • Establish a modern, digital ICT-based tax administration that uses Big Data effectively and is powered by risk engines to ensure smart enforcement.	✓ Tax policy and administration reforms can help increase Nigeria's tax-to-GDP ratio in the medium term from 4 to 7 percent, thus helping to reduce the fiscal deficit, and increase fiscal space for investments in human capital and the infrastructure needed to connect farmers and firms to markets and youth to jobs. ✓ Advance health and environment policy goals by capturing more of the negative externalities of consumption of harm goods. ✓ Increase non-oil revenues from excise, EMT levy, VAT, incentives, and international tax reforms.
	Adopt a **public engagement strategy** that links revenue mobilization to increased investment in infrastructure and human capital.		Enhance FIRS efficiency by supporting reforms to the structure of the organization, ensuring that management approaches and standard operating procedures are consistent and, supported by effective HR management.	
	✓ Improve state level PIT and improve state-Federal cooperation in tax administration.	✓ Introduce a well-designed, progressive and properly administered property tax expand electronic tax payments and stop cash payments.	✓ Establish consolidated state revenue accounts as part of state TSAs.	✓ State IGR reforms would: provide taxpayer clarity and reduce double-taxation; reduce leakages from IGR sitting in individual MDA accounts; induce more efficient land use and provide revenue to states and local governments.

Why reforms are needed	*Which reforms are critical and when could they be carried out*			*What the impact of reforms would be*
	Reforms that can be carried out in 1–6 months	*Reforms that can be carried out within 18 months*	*Structural initiatives and institutional reforms that can put on a firm footing in the next 3 years*	
Tax design is impeding business growth by (1) increasing working capital requirements; (2) the high cost of compliance, with no simplification measures yet available for small business, which makes the tax policy regressive.		• Streamline the VAT, eliminating unnecessary frictions that impinge on productivity, and avoiding tax cascading. • Ensure prompt VAT refunds, after putting in place strong controls. • Establish a valuation database of high-value urban properties for the LUC.	• Record and harmonize IGR policies and administration across states and minimize double taxation in terms of federal policies.	✓ More post-tax profits available for investment. ✓ Lower compliance costs for SMEs that give them an incentive to become formalized. ✓ Paperless operations, equipped with sharp, ICT-enabled risk-based enforcement. ✓ High working capital requirements obviated.
Inefficient Customs Administration reduces trade and tax collection	• Improve NCS administration of border entries and reduce processing times. • Simplify tax assessment and payment mechanisms as part of ICT development in FIRS.		• Modernize the FIRS and NCS to create a taxpayer-friendly organization providing world-class online services.	✓ Improved tax morale because of more clarity about taxes by reducing double taxation incidents, negative experiences with tax officials, and lack of how taxes are used.
Shadow economy is estimated at over 50 percent.	• Focus on HNWIs for PIT enforcement. • Introduce well-designed simplified PIT regimes for SMEs; SMEs operating as companies are exempted from CIT.	• Pilot internal cooperation with one state IRS (Lagos) to strengthen PIT, CIT and VAT enforcement.	• Successfully embed a Compliance Risk Management system based on objective risk criteria.	✓ The demonstration effect of HNWIs being subject to taxation will improve voluntary compliance and widen the tax base.

Nigeria: Key Economic Indicators

Economy	*2015*	*2016*	*2017*	*2018*	*2019*	*2020e*
Real GDP Growth (percent yoy)	**2.7**	**-1.6**	**0.8**	**1.9**	**2.2**	**-1.8**
Nominal GDP (naira tr)	95	103	115	129	146	154
Oil Production (mb/d)	2.1	1.8	1.9	1.9	2.0	1.9
Oil Price (Bonny light, US$/bbl)	54	45	55	72	65	42
Inflation (percent average)	9.0	15.6	16.5	12.1	11.4	13.2

Real sectoral growth (percent yoy)	*2015*	*2016*	*2017*	*2018*	*2019*	*2020e*
Real GDP Growth	2.7	-1.6	0.8	1.9	2.2	-1.8
Agriculture	3.7	4.1	3.4	2.1	2.4	2.2
Industries	-2.2	-8.9	2.1	1.9	2.3	-5.8
Industry-Oil	-5.4	-14.4	4.7	1.0	4.6	-8.9
Industry-NonOil	0.1	-5.0	0.6	2.4	0.9	-3.9
Services	4.8	-0.8	-0.9	1.8	2.2	-2.2
Oil GDP	-5.4	-14.4	4.7	1.0	4.6	-8.9
Non-Oil GDP	3.7	-0.2	0.5	2.0	2.1	-1.3

GDP Composition (percent)	*2015*	*2016*	*2017*	*2018*	*2019*	*2020e*
Total GDP	100.0	100.0	100.0	100.0	100.0	100.0
Agriculture	20.9	21.2	21.1	21.4	22.1	24.4
Industries	20.4	18.4	22.5	26.0	27.7	28.6
Industry-Oil	6.4	5.3	9.1	10.5	8.6	6.7
Industry-NonOil	14.0	13.1	13.4	15.5	19.1	21.9
Services	58.8	60.4	56.4	52.6	50.2	47.0
Oil GDP	6.4	5.3	9.1	10.5	8.6	6.7
Non-Oil GDP	93.6	94.7	90.9	89.5	91.4	93.3

Source: Nigerian authorities and World Bank calculations.

Monetary and Financial Sector (percent yoy, end of period, unless indicated otherwise)	*2015*	*2016*	*2017*	*2018*	*2019*	*2020e*
Money Supply (M2)	-2.9	11.8	-5.4	5.5	5.0	31.0
Narrow Money	1.1	21.7	-10.3	-4.4	-7.0	51.7
Net Foreign Assets	-24.0	41.5	45.3	22.4	-22.8	26.4
Net Domestic Credit	6.2	23.5	-1.9	0.6	28.8	17.6
Credit to Government	53.6	23.8	-9.9	-18.1	87.0	30.8
Credit to Private Sector	3.2	23.5	1.4	1.9	17.6	12.9
Monetary policy parameters:						
Monetary Policy Rate (absolute rate, end of period)	11.0	14.0	14.0	14.0	13.5	11.5
Liquidity Ratio (absolute rate, end of period)	30.0	30.0	30.0	30.0	30.0	30.0
Cash Reserve Requirement (absolute rate, end of period)	20.0	22.5	22.5	22.5	22.5	27.5

Financial Market Indicators (end of period)						
Stock Market (NSE) Index	28,642	26,875	38,243	31,431	26,842	40,271
Fitch Sovereign Long Term Foreign Debt Rating	BB-	B+	B+	B+	B+	B
Moody's Sovereign Long Term Foreign Debt Rating	Ba3	B1	B2	B2	B2	B2
S&P Sovereign Long Term Foreign Debt Rating	B+	B	B	B	B	B-

External Sector	*2015*	*2016*	*2017*	*2018*	*2019*	*2020e*
Exchange rate - official (₦/US$, end of period)	197	305	306	307	307	380
Exchange rate - parallel (₦/US$, end of period)	267	490	363	363	362	465
Real effective exchange rate index (end of period)	67	86	99	87	79	79
Current Account Balance (percentage GDP)	-3.2	0.7	2.8	1.0	-3.8	-4
Current Account Balance (US$ bn)	-15.4	2.7	10.4	3.9	-16.7	-17.0
Exports of Goods and Services (US$ bn)	49.0	38.4	50.8	66.0	69.9	40.0
o/w oil and gas exports (US$ bn)	42.4	32.0	42.3	56.6	54.5	31.4
Imports of Goods and Services (US$ bn)	71.9	47.0	50.9	71.6	100.8	72.1
Net Income (US$ bn)	-12.7	-8.6	-11.5	-14.7	-12.5	-5.8
Net transfers (including remittances) (US$ bn)	20.2	19.9	22.0	24.1	26.4	21.0
Net Direct Investment (US$ bn)	1.6	3.1	2.2	0.6	1.8	2.7
Net Portfolio Investment (US$ bn)	0.9	1.7	3.7	-7.2	9.0	-3.6
Net Other Investment (US$ bn)	-9.2	-4.9	-5.2	-9.7	0.3	4.3
External Reserves (US$ bn, end of period)	29.1	25.8	38.8	43.1	38.6	36
Equivalent months of imports of G&S	4.8	6.6	9.1	7.2	4.6	6

Source: Nigerian authorities and World Bank calculations.

Nigeria: General Government Fiscal Summary - preliminary						
Actual (percentage GDP)	*2015*	*2016*	*2017*	*2018*	*2019*	*2020e*
Total revenues	**7.5**	**5.9**	**6.7**	**8.1**	**8.2**	**6.5**
Federally collected	6.4	4.8	5.4	6.6	5.9	5.2
Oil and gas revenues	3.2	1.6	2.3	3.6	3.0	2.0
Non-oil revenues and other revenues	3.2	3.1	3.1	3.0	2.9	3.1
Independent and other revenues	1.1	1.2	1.3	1.5	2.3	1.4
Total expenditure	**10.7**	**9.7**	**10.7**	**12.3**	**12.7**	**11.9**
Overall balance (general government)	**-3.2**	**-3.8**	**-4.0**	**-4.2**	**-4.6**	**-5.4**
Public Debt (net)	**14.2**	**17.3**	**18.9**	**19.3**	**21.7**	**24.1**

Source: Nigerian authorities and World Bank calculations.
Notes: /1 After budgeted and discretionary deductions, but before derivation. /2 Includes Solid Minerals, NLNG Dividend, and Signature Bonus; exchange rate difference, excess petroleum profit tax.

Nigeria: Federal Government Fiscal Accounts - preliminary						
Actual (percentage GDP)	*2015*	*2016*	*2017*	*2018*	*2019*	*2020e*
Total Revenue	**2.7**	**2.0**	**2.4**	**3.0**	**3.2**	**2.2**
Share of federally collected revenues	2.5	1.7	2.0	2.5	2.4	1.8
Oil, Gas and Mineral Revenue (incl. signature bonus)	1.5	0.7	1.0	1.5	1.4	0.8
Non-Oil Revenue	1.0	1.0	1.0	1.0	0.9	1.0
FG Independent revenues and grants	0.3	0.3	0.4	0.6	0.9	0.3
Total Expenditure	**5.0**	**4.7**	**5.7**	**6.3**	**6.8**	**6.8**
Recurrent Expenditure	4.4	3.9	4.4	4.8	5.1	5.8
Personnel Cost (including Pensions)	2.2	1.8	1.8	1.8	1.8	2.1
Overhead Cost	0.1	0.1	0.2	0.1	0.2	0.5
Other recurrent (incl. COVID-19 intervention and power sector)	na	0.7	1.1	1.2	1.5	1.0
Interest payments	1.1	1.2	1.4	1.7	1.7	2.2
Capital Expenditure (incl. COVID-19 intervention)	0.6	0.7	1.2	1.5	1.7	1.0
Overall Fiscal Balance	**-2.2**	**-2.7**	**-3.3**	**-3.2**	**-3.6**	**-4.7**

Source: Nigerian authorities and World Bank calculations.
Notes: The reported revenue and fiscal balance figures differ from the published Federal Government budget figures as the World Bank excludes the non-revenue items under international classification. Total expenditure for some years differs from the Federal Government reports as the World Bank excludes debt amortization payments from expenditure. Figures exclude government-owned enterprises and donor funding. /1 Includes other extractives revenues. /2 The actual capital spending reported for the calendar year. /3 Other Outflows include irregular items.

Nigeria Development Update
June 2021

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Vision and Mission
by ***Odeyemi Oluwaseun***

Odeyemi Oluwaseun was born in 1989 and is a native of Ogun State in Nigeria. In 2015 he obtained his National Diploma in fine art from the Polytechnic Ibadan, and in 2019 his Bachelor of Arts in fine and applied art at Obafemi Awolowo University. He continued to sharpen his skills with industrial training at Universal Studios of Art. Oluwaseun's work spans different styles including oil, pastel, Conte, charcoal, acrylic, and watercolor paintings. His works in both local and international collections are managed by the MastersofArt Gallery in Lagos, Nigeria. He has participated in different exhibitions, including the So Far, Nosa, and Infectivity exhibitions, Artcom's 70th international cultural exposition of arts, Mydrim art fair, La grand bazart, Limcaf Charity Art, and Union Bank's art competition where he won the student price in 2017. His mixed media on canvas "Vision and Mission" shows the intensity of ambition and the journey of life. In Oluwaseun's words, "there are many alternatives or distractions along the way but stay staying true to the ladder will lead you up."

People forge ideas, people mold dreams, and people create art. To connect local artists to a broader audience, the cover of this report and following editions will feature art from Nigeria.