Nigeria's Fiscal Deficits: A History of its Colonial Foundations, 1899 – 1959

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Abstract
In the last thirty years, deficit financing has become a major impediment to fiscal balance in the administration of public expenditure in Nigeria. From the middle of the 1980s up to the present, the federal government has consistently overspent its actual revenue accruals and have even borrowed in the pursuit of projects for which she has too little revenue backing. In fact, since the beginning of democratic rule in the current fourth republic, government has increasingly failed to balance its budget with grave consequences for price levels, interest rates, inflation and macro-economic stability. This paper shows that deficit financing of public expenditure by the Nigerian government is however not a recent issue and that it can be traced to the formative years of Nigeria's public finance in the colonial period. The paper however argues that unlike the current practice, deficit financing was driven more in the colonial period by the need to build an infrastructure base for the economy rather than on personnel and overhead expenses manifested in the lopsided allocation of the greatest proportion of public revenues to the recurrent budget as it is the practice in Nigeria today.

Introduction

Budget Deficit Financing: Some Empirical Evidence

Nigeria has had to contend with the adverse effects of deficit financing of its budget for many years. From 1980 up to 2008, the federal government has balanced its budget only in four out of the 32 years within the period, the exceptional years being 1980, 1981, 1995 and 1996 when government current account balances were +₦0.603billion, +₦0.118 billoin, +₦1.01 billion and +₦32.05 billion, respectively

(Ogunyemi, 2008: 302, 373). But in cumulative terms, no regime at the federal level of governance in Nigeria since 1979 has succeeded in balancing its total expenditure with its aggregate revenue even when unexpected but positive variances occur in the revenue budget far in excess of approved estimates. It has been elaborately shown in a recent study that from the time of President Shehu Shagari (1979-83) to that of General Abdulsalami Abubakar (1998-99) the federal government overspent its aggregate revenue by a cumulative sum of ₦728,860.7 million (or about ₦728.861 billion) (Ogunyemi, 2008: 430-434). This accounted for, on the average, some 26.23% of the total expenditure of government in those years. Experts have described a situation where government spends more than it earns or plans to spend in excess of its revenue as budget deficit financing (Yekini, 2001, Ram, 1986, Grossman, 1988). They conclude that it is a dangerous path of economic growth and one most likely to subvert the course of development if allowed to exceed 4% of the Gross Domestic Product (GDP) of any state (Okongwu, 1986, Ariyo, 1996b, Egwaikhide, 1996b). This study attempts a reconstruction of the growth-path and the history of Nigeria's deficit financing in the colonial period. The purpose is to show that the deficit problems which the country did experience from the 1980s up to 2008 had its antecedent parallel in the colonial period. This is to show that the accepted orthodoxy that colonial finance was always balancing its budget (Hazzlewood, 1956, Helleiner, 1966) needs a re-examination in the light of the fact that even during the alien rule, huge fiscal deficits were recorded in Nigeria's account books.

It has been shown that the Federal Government of Nigeria overspent its revenue from 1980 to 1993 by ₦259.491 billion and that during the regimes of General Ibrahim Babangida alone (1985-1999),, total deficit financing of government expenditure was a whopping ₦246.270 billion (Ogunyemi, 2008). As vividly shown in **Table 1** below, the eras of Generals Sani Abacha and Abdulsalami Abubakar (1993-1999), budget deficit financing was more than ₦460.894 billion. In other words, beginning in era of General Olusegun Obasanjo in 1976 up to the time of General Abubakar/President Obasanjo in 1999, the federal government did not, at any time, balance its budget (Ogunyemi, 2008: 338), rather, it consistently overspent its revenue by billions of naira.

Table 1: Budget Deficit financing in Nigeria, (1980 – 1999) (in ₦ millions)

Administration	Period	Total Federally Collected Revenue	Federal Govt. Share	% Fed Govt Share	Total Expenditure	Deficit	Deficit as % of expenditure
General Obasanjo	1976/77-1979/80	34,952.0	26,452.0	75.68	34,927.0	-8,475.0	-24.3
President Shagari	1980-83	35,999.0	29,845.0	82.90	37,366.0	-7,521.0	-20.1
General Buhari	1984-85	24,400.0	17,260.0	70.74	22,960.0	-5,700.0	-24.8
General Babangida	1986-93	441,230.0	271,270.0	61.48	517,540.0	-246,270.0	-47.6
General Abacha	1994-98	2,228.490.0	1,486,570.0	66.70	1,662,360.0	-175,790.0	-10.6
General Abubakar/ President Obasanjo	1999	949.187.90	662,585.3	69.80	947,960.0	-285,104.7	-30.0
Total		**3,713,701.9**	**2,493,982.3**	**71.21**	**3,223,113.0**	**-728,860.7**	**26.23**

Sources: (a) *Report of the Accountant General of the Federation Together with Financial Statements* (Various years).

(b) Central Bank of Nigeria, *Statistical Bulletin.* vol. 11, No. 2, December, 2000.

Scholars are agreed that deficit financing may be due to many causal factors. First, it may be due to government's dominance in the economic affairs of a state by way of huge public spending which "crowds out" the private sector (Robinson, 1977, Ram, 1981, Provopolous, 1982). It may also be a reflection of an improperly anchored macro-economic policy. A plethora of conflicting arguments exists on the propriety of large government spending and its dominant participation in economic activities (Keynes, 1936, Sweezy, 1942, Haines, 1961, Landau 1983, 1986)). While some views have consistently stuck to the arguments which frown at the intervention of the state in economic activities via the use of fiscal and monetary policies, especially those of taxation and transfers in coercing the economy into a predetermined route of motion; other views have continued to insist on the necessity for the use of fiscal and monetary policies in the allocation of scarce resources. For instance, Ram (1986) believes that government fiscal and monetary policies such as taxes and transfers distort market prices and discourage economic activities such as savings and investment. Wijimbergen (1994) however, disagrees with this view. His argument is that the government needs to stimulate effective demand within the economy in order to create jobs and this can be done only by using appropriate fiscal measures such as deficit spending to create more output and hence, employment.

It appears therefore that within the body of literatures on deficit financing, there exists two diametrically opposed theoretical positions. That is, those who favour the Keynesian economic model and who therefore believe that the key to economic growth particularly in a developing economy is the high incidence of state intervention in economic matters and huge government spending directed at rapid growth. Those who share this view are congregated in a school of thought known as the "Developmental School" (Keynes, 1936). There is an opposing line of thought shared by those who advocate a minimal level of government involvement in economic matters, identified as the "Neo-classical School" (Smith, 1776).

Ikhide (1995) looks into the measures that may be deployed in the financing of budget deficit and the possible effect of this on developing economies. His findings suggest that the issue at stake in

developing African economies is not so much the choice between alternative measures of financing deficits, as the effect of the measures on the general price level. For, the study shows that, whether the financing of deficits is done through money creation by the central bank or by borrowing from commercial banks or securing bilateral or multilateral financial assistance from abroad, the recurring decimal in developing African economies has always been the rise in price level. Hence, the study suggests that the most reasonable method of achieving a reduction in the inflation rate and enhancing the value of income to each stakeholder within the developing African economy is to reduce the level of budget deficit.

It appears that budget deficit necessarily correlates with increase in price levels and that this leads to a reduction in the value of real income especially in the less developed states of the world. When a government plans to and actually spends more than it earns, the ultimate effect is a system awash with excess liquidity that is not backed by a corresponding quantum of productivity. No wonder Ndung'U (1995), using a multivariate *Granger-Non Causality test* embarked on a study designed to examine and measure where possible, the correlation between the variables of fiscal deficits and their effects on the inflation rate and growth in money supply vis-à-vis direct money printing by the central bank and the rate of inflation. The result of the study was not any significantly different from those of Ikhide's (1995) or Marshall and Schimidt-Hebbel's (1991). It was revealed that budget deficit correlates perfectly with the rate of money growth and that links exist between money creation and the rate of inflation and ultimately the rate at which interest rates grow. From the backdrop of Ndung'U and Ikhide's studies, Osoro (1997) attempted to test the hypothesis that large fiscal deficit causes more public spending. His study showed that high fiscal deficits is a causal factor in increased public spending and that in the particular case of Tanzania, huge public spending since the 1980s has been encouraged by a high incidence of fiscal deficits.

Origin and causes of budget deficit in colonial Nigeria

Deficit financing in Nigeria dates back to the colonial period. As early as 1900, loans and advances from foreign financiers were secured by

the country's colonial masters for several economic purposes (Lawal, 1979). First, for "opening up the interior for trading penetration and for administrative control" (Pim, 1946, Perham, 1948) and second, in building infrastructure, especially transport infrastructure such as the railway, ports, harbours, etc (Lawal, 1994, Olukoju, 2003). Since the early years of colonisation (189-1920) it was discovered that local financial capacity had not expanded enough to finance major civil works which the economy needed, such as the railway and telecommunication, resort was had to foreign loans was made by the colonial authorities. This meant that the government at the time planned to and actually spent more than it earned (Helleiner, 1966, Lawal, 1979). For example, the first loan contracted by the colonial government in 1899 for ₤792,500 was raised by way of borrowing from private financiers in England by the Imperial Treasury, (Helleiner, 1966:228). This created for the first time, a major case of deficit financing for the newly acquired Nigerian territories which even in strict political terms, was yet to be constituted into a single vassal state under British hegemony.

Nevertheless, the assets and liabilities of the imperial railway were inherited by the unified Nigeria in 1914. But even by that year, evidence has shown that the practice of borrowing to provide for major infrastructural projects had just begun. Southern Nigerian government which by this time was administratively and financially autochthonous successfully negotiated a series of loan advances from British lenders in 1905, 1908 and 1911 amounting to ₤10 million (Helleiner, 1966:228). The loans were secured for the building of bridges, harbours, water supply plant in Lagos and for dredging purposes. The orgy of borrowing in millions of pounds at a time when the total income of the country was still less than ₤100 million continued in the 1930s. By 1931, the total foreign debt stock of the country had reached ₤28,350.582 (Helleiner, 1966:228). The result was heavy debt servicing charges which though was 7.6% of the value of total exports in the 1920s climbed rather significantly to 19.1% in 1934 (Helleiner, 1966:228-229), representing some 32.8% of the total Federal Revenue in the same year.

One event that worked rather adversely to make the debt burden and consequently the margin of deficit to become rather worrisome to the colonial government in the inter-war years was the great world economic depression of the late 1920s to the early 1930s (McElvaine, 1984). The depression led to a huge decline in export revenue from where the bulk of national revenue came (Perham, 1948). The depression further increased the need for deficit financing as it affected nearly 50% of total revenue that accrued to the national government. In fact, from the 1927-31 fiscal years, deficit financing had caused the national revenue account to be overdrawn to the tune of £7.3 million (Helleiner, 1966:23), necessitating a major review of the structure and relations of fiscal system between the Nigerian national government and its numerous Native Authorities. It is interesting to note that though the central administration at this time found it difficult to balance its budget, the Native Authorities had surplus budget (Philipson, 1947, White, 1981). The reason was not far-fetched. Whereas Native Authorities had a legion of local taxes from where they could finance their activities especially after the quasi-federal experiment introduced by the Arthur Richards Constitution of 1946, the central government had rather limited sources, the most important of which was export tax which the depression had adversely curtailed.

The colonial administration attempted to solve this obvious fiscal imbalance between the central and Native Administrations by embarking on three major steps: (a) transferring some public work duties from the central government to the Native Administration (b) reducing the share of the vertical fiscal transfer marginally from the national treasury from 70% to 60% in favour of the central administration (Phillipson, 1947:57) and by drawing down the country's foreign reserve to solve the pressing liquidity crisis in the national revenue budget (Helleiner, 1966:234-235).

Apart from the reason of decline in export revenue which induced deficit financing of government activities, increase in wages, salaries and allowances paid to colonial officials, serving and retired, also constituted a major factor of high government expenditure necessitating deficit. Helleiner (1966:232) reports that between 1939 and 1949, wage rates "more than doubled" while "still more dramatic

wage rates were registered in the 1950s and early 1960s". Okigbo (1962: 20-21) has also shown that the huge increase in administration cost as well as public expenditure on goods and services between 1950 and 1957 should also be blamed for the deficit financing of expenditure by the colonial government. The consequences of the high administration/recurrent cost on government, Helleiner maintains, was a disproportionate increase in expenditure vis-à-vis revenue, thus allowing public expenditure to rise by about 62% in the decolonization years up 1959 (Helleiner, 1966:232).

That government wage rate increases and expenditure on administration had such a significant impact on public treasury was symptomatic of the huge involvement of the state in economic matters. The Nigerian government, whether in pre-independence, decolonization and post-colonial periods has always had a recurring feature of heavy participation in economic matters. This participation has been in the form of government direct involvement in production, distribution and service economies, infrastructure building, wage increases, etc. All these have continued to have significant impact on public treasury. The importance of this point can be seen in the quantum of government share of the funds earmarked for the country's five development plans starting from 1946. For example in the 1946-56 'Colonial Welfare Plan', to which was committed the sum of £55 million (₦110 million), government/public sector was responsible for 75% of the sum. Although the plan was dismissed as "no-plan at all" due to its abysmal failure, the fact that the public sector still accounted for the largest share of the sums invested in it still shows the high level of public spending that the government had to bear in the course of Nigeria's development (Dean, 1972, Tomori and Fajana, 1979). The same high level of public expenditure was done for the first indigenous plan of 1962-68, and others such as the 1970-74 plan, the 1975-80 plan, and the 1980-85 plan in which public share of the committed funds were: ₦132 million, ₦43.3 billion and ₦82.2 billion, respectively (Ihimodu, 1994:99-122).

In sum, we may draw a tentative conclusion that budget deficit financing neither began in Nigeria with the post-independence balance of payment problems witnessed in the 1980s nor was it entirely new to Nigeria's public finance structure in the immediate

post-independence era, rather it originated in the colonial period. After independence in 1960, Nigeria's national leaders continued with budget deficit financing as an instrument of infrastructural development and this was manifested in the programmes of development they set for the country and implemented. But, a most heart-warming fact was that such deficits which between 1914/16 and 1927/31 grew from about £800,000 to ₤4.5 million and specifically in the 1931/32 fiscal year to ₤7.3 million, were properly managed in such a way that in spite of the liquidity squeeze in the depression years of the world economy (1929-34), Nigeria did not become bankrupt, neither was her expansion of the public sector significantly slowed down or halted.

Management of Deficit

Budget deficit financing necessarily implies that the economy is being overdrawn in relation to cash. A negation of this will obviously lead to a pursuit of budget surplus or balanced budget in which available cash balances will be in excess of expenditure or at least, be equal to it. However, the reality of fiscal deficits is beyond this simplistic description of the scenario. For, budget deficit financing can be a macro-economic instrument of achieving expansionary fiscal policy in an economic setting needing appropriate "reflation" along the philosophy already well established by Maynard Keynes (Keynes, 1936, Musgrave and Musgrave, 1973: 109-24). This may be to provoke all productive enterprises in order to make them increase on their output levels. Hence, budget deficit is not necessarily bad economics because any attempt to cure the imbalance between revenue and expenditure must be carefully managed in order to avoid jeopardising the advantages derivable from expanding productivity within the private sector. It is in the light of this background that we discuss here the medley of fiscal and monetary tools employed by the colonial administration of Nigeria in the management of Nigeria's budget deficit situations.

There are diverse measures by which fiscal deficit in an economy can be managed. The measures may be contractionary, expansionary or inflationary. First, policy makers may increase taxes to meet the vacuum between revenue and expenditure. That is an inflationary measure since it has the tendency to lead to a general rise in price

levels. The government may embark on the creation of money i.e. by printing money by the central bank or issue bonds and securities through which it may borrow from the investing public to finance public projects. This latter measure is necessarily expansionary because it will ultimately lead to increase in money supply within the system. The first time that kind of measure was used was in May 1959 when bonds in the sum of ₤2.3 million were issued by the Central Bank of Nigeria (CBN) to finance further expansion of the railway and Lagos harbours (Helleiner, 1966:229). Again, the government may decide to deliberately cut expenditure, most usually capital expenditure. This is a contractionary fiscal policy since public spending and hence money supply will be reduced. Finally, the government may embark on a draw-down of the country's foreign reserves to finance rising domestic expenditure, a measure which has the very serious effect of increasing the external debt stock and consequently huge debt service burden on a country.

The colonial government of Nigeria used the combination of all the above measures to combat deficit problems between 1914 and 1960. For example, government borrowed from abroad and from internal sources to finance its expenses in the areas of infrastructure and administration especially in policing services and the judiciary. The first domestic loan contracted was in the sum of ₤300,000 in 1946 at 3½% interest rate offered to the public by way of securities (Helleiner, 1966:229). This was followed in 1959 by a ₤2.3 million loan at 5.6% (Helleiner, 1966:229). From 1959-64 government borrowed from the public each year, creating a pool of locally sourced development loan which by year end 1964, totalled ₤54,355,360 (Helleiner, 1966:229-289). The Nigerian Central Bank which began operation in 1959 held only about 30% of the development stock, the balance went to private individuals and corporate bodies domiciled in Nigeria.

However, the government did not borrow during the great depression, preferring instead to freeze wage increases and to cut significantly, total annual expenditure by ₤4.5 million in the 1930/31 fiscal year and by ₤3.8 million in the 1933/34 fiscal year (Pim, 1948:249). This affected mostly those expenditure classified as "Development expenditure" especially under the public works

department while expenditure on debt-servicing and transfer increased (Helleiner, 1966:234, Pim, 1948:250). Debt repayment alone was as large a proportion of expenditure because it accounted for 19.6% in the depression years of 1933/34 (Pim, 1948:252). The shift in expenditure emphasis from development to repayment of debt had an unmistakeable effect on the fiscal conditions of the country. For example between 1930 and 1934 total financial commitment to development expenditure declined from 40.4% to 32.5%, while that on debt increased from 16.8% to 19.6% and this further increased between 1938-39, (the after-shock of the depression) to 27.3% of total expenditure (Helleiner, 1966:233). These expenditure figures however excluded those of railway, colliery, electricity, posts and telegraphs, extra-ordinary and miscellaneous expenses which, as at that time in Nigeria's financial history, were separately accounted for in national revenue accounts (Okigbo, 1962: 180).

Apart from internal borrowings from the domestic market, the government equally borrowed from abroad (Pim, 1948, Phillipson, 1947). We have earlier shown that the Nigerian Railway's first loan of ₤792,500 was negotiated and secured by the Imperial Treasury in England in 1899. Other borrowings followed between 1919 and 1930 and debt service charged from 1931 onwards consumed a chunk of national revenue (22.0% in 1929) and was further worsened by the depression which pushed the percentage share of transfer on foreign debt to 32.8% of total revenue in 1934 and 19.1% of total value of exports. (Frankel, 1938:182).

The Central Bank of Nigeria did not come on board as an institution for financial management in Nigeria until 1959. Hence, the deficit management measures of money printing could not be used for the management of Nigeria's budget deficit prior to independence. Although, money printing is necessarily inflationary because of its capacity to make the economy awash with excess cash, it has remained since the creation of the bank an alternative measure by which increased public spending could be supported (CBN, 2000: 100-101)

Recourse to a draw-down on the foreign reserves of the country was also made as a way of financing deficit spending during the colonial period. This was done pursuant to the redemption of foreign loans and retirement benefit claims of colonial officials who were at that time domiciled in Britain (Ogunyemi, 2008: 171). This remained the position of things until independence in 1960 when even an the rate at which Nigeria's indigenous elite sought for additional funds for development projects from abroad continued unabated (Okotie-Eboh, 1963: 36-37, 47; 53). By the mid 1950s, however, the impact of using foreign reserves in support of deficit financing soon began to dawn on the government. By 1956 Nigeria's foreign reserves which was put at ₤260 million (UN, 1965) and which was adequate to support two years import had been drawn so low that it recorded a negative growth rate of -12.6% in 1959 (Langley 1968:153-155). The adequate, safe and reasonable ratio of reserve to imports are usually calculated in terms of the capacity of the reserve to conveniently finance imports for a continuous period of four months. By 1959 however, it could no longer support imports for a period more than three months. The reserve was not re-built until the advent of Nigeria's oil wealth in the early 1970s under General Yakubu Gowon. The most notable effect of the management of the deficit was that the colonial authorities were able to checkmate its spiralling effect from destroying the revenue base of the country by avoiding at all costs, all imprudent expenditure that could lead to bankruptcy. In fact, what the colonial government handed over to the indigenous elite at the country's independence in 1960 was a robust rather than a weak financial base devoid of debt servicing obligations which was in excess of the capacity of the economy to conveniently amortise.

Conclusion

The Nigerian colonial government did not have all the financial resources as at the time it set to work in Nigeria. British authorities were not disposed to permitting any of its dependencies from endlessly depending on it for financial support and this partly explained why the financially weak Northern Protectorate of Nigeria was merged with the financially buoyant Southern Protectorate and the Colony of Lagos in 1914. But, even from that year until independence, situations arose several times, that made the colonial government of Nigeria seek for and obtain other sources of finance

from the private investors in Nigeria and foreign financiers as well. The need to seek for more funds by the government was necessitated by its plan of building basic transport infrastructure in the country in order to permit for more opportunities of trade in the interior and the consolidation of imperial rule. This forced the government to exceed in many instances, its revenue budget and to embark on deficit financing of its expenditure plans. Recourse was made to foreign borrowing, issuance of development bonds within Nigeria and, deliberate reduction of the recurrent expenditure in order to free more funds for critical projects.

All these began in 1899 and continued until the country became independent of colonial rule in 1960. The lesson is that deficit financing though became intense and most destabilising to macroeconomic management of Nigeria in the 1980s, it actually did not begin in those years. Its colonial root had been firmly laid even before the constitution of Nigeria into a single unified state under imperial Great Britain in 1914. The main difference however has been the style and effect of its management. Whereas during colonial rule, deficit financing accounted for, at most, only one-third of the budget, in the post colonial era and especially during military rule, deficit financing has grown so big as to account for more than 45% of total expenditure of government (FOS, 1996: 20-21). Again, whereas the colonial government embarked on deficit financing in order to provide funds for capital projects, post-colonial government did this principally to finance consumption through lopsided devotion of the greatest proportion of government revenues to the recurrent expenditure. The result has been utterly destabilising to economic planning and has continued to fuel inflation and a fall in real income in post-colonial Nigeria.

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