ECONOMIC REPORT ON NIGERIA

NIGERIA COUNTRY OFFICE

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This is the second in the series of our new analytical tool: The Economic Report on Nigeria (ERN). As expressed in the maiden edition, this analytical tool was necessitated by the need to pursue the deliverables contained in the Bank’s Nigeria Country Strategy Paper (CSP): 2013 – 2017. Since the publication of the first report in September, the Nigeria Country Office has been upgraded to a full department status following a fine-tuning of the Bank organizational structure.

As the first field-based office with a Departmental status in the history of the Bank, the Nigeria Country Office (ORNG) has been given expanded mandate to deepen its analytical and policy work with a view to strengthening its advisory role for a sound policy environment and policy implementation in Nigeria. This new edition of ERN reflects to some extent the renewed commitment to the implementation of the Bank Ten Years Strategy.

It reports on developments through the third quarter of 2013. The first part of the report provides a panoramic view of key developments in the macro-economy, with focus on the real economy, monetary, fiscal and international issues. Next, the report discusses key ongoing structural reforms featuring the energy sector. Lastly, the thematic part concentrates on strengthening the public-private partnership initiative to improve infrastructure development in Nigeria. Specific lessons for Nigeria are drawn from global best practices and successful PPP projects around the world.

This report was produced by a team from ORNG led by Eric Kehinde Ogunleye (Consultant Macroeconomist), with contributions from Ben Obi (formerly Consultant Economist), Barbara Barungi (Lead Economist) and Andoh Mensah (Chief Country Programme Officer), under the overall guidance of the Country Director, Dr. Ousmane Dore. The report benefitted from very useful insights provided through review and comments from colleagues both within and outside the Bank.
1.1 Overview of the Economy

Nigeria sustained its impressive growth performance, settling at 6.8% at the end of Q3 and hopefully would achieve the projected growth of 6.75% at the end of the year. The non-oil sector remained the major growth driver at 7.7 percent compared with a negative growth of 0.7% for the oil sector.

Delayed passage of the PIB may be contributing to poor performance of the oil and gas sector as a result of possible postponed investment by prospective investors.

Monetary authorities maintained its tight monetary policy stance that has been very helpful in taming inflation to single digit at 8% in Q3. This has been reinforced by agriculture reform that appears to have positively contributed to reducing food inflation, the major driver of headline inflation.

Investor confidence appears to be gradually restored with the values of stock market capitalization increasing from N15.8 trillion in Q2 to N17.7 trillion in Q3 2013 and All Share Index by 1.16 percent from 36,164 in Q2 to 36,585 in Q3 2013, thus gravitating toward the pre-crisis level.

The link between domestically mobilized financial resources and the real sector activities is yet weak and demands policy focus.

The hitherto quarterly declining revenue was reversed during the quarter with significant increase by 14.4 percent over the previous quarter, driven largely by non-oil revenues while oil revenue continues to trend downwards.

Despite the increased retained Government revenue during the quarter, fiscal spending takes a long-term perspective with a scale back in fiscal expenditures and concomitant improvement in overall fiscal balance.

Revenues and expenditures for the rest of the year is expected to mirror the current pattern given the spirited efforts of the government in fighting oil theft, illegal oil bunkering and pipeline vandalism.

Oil theft and pipeline vandalism is seriously impinging on exports and foreign reserves with decline during the quarter under review.

The partial petrol subsidy removal and close monitoring of the subsidy regime seems to have led to significant decline in imports. This is reinforced by government import substitution policy interventions.

The slowdown in investment may not be unconnected with perceived risks attached to the upcoming General Elections and delayed passage of the PIB since significant foreign investment goes to the oil and gas sector.
1.2 Real Sector

Nigeria has sustained strong growth that stood at 6.8% at the end of Q3 and hopefully would achieve the projected growth of 6.75% at the end of the year. The non-oil sector remained the major growth driver at 7.7 percent compared with a negative growth of 0.7% for the oil sector.

Delayed passage of the PIB may be contributing to poor performance of the oil and gas sector.

Nigeria continues to maintain its impressive economic growth despite the challenges posed by the poor performance in the oil sector. Real GDP growth for the third quarter remains robust at 6.8 percent, following the impressive growth in previous quarters and better than the 6.75% projected for the year (Chart 1). The near term outlook for real GDP growth remains positive, projected at 6.75% and 7.3% in 2013 and 2014, respectively. The medium-term prospects are also promising. As in previous quarters, growth was driven by non-oil sector that grew by about 7.7 percent during the period under review. Agriculture, wholesale and retail trade, telecom, building and construction, hotel and restaurants, solid minerals, real estate and services were the main drivers (Chart 2). Given the labour intensive nature of these activities, diversifying the economy in this direction holds high promise for improving inclusive growth in the country.

This remarkable performance raises optimism on the growth performance of the economy with strong indications that the economy may exceed growth projections for the year. This view is anchored on the usual increased economic and business activities in the last quarter of the year in preparation for the yuletide season when consumption is usually higher. Hence, growth in the last quarter is expected to be higher than the previous quarters. However, the downside is the poor performance of the oil sector that recorded a negative growth of 0.7 percent. Oil theft, pipeline vandalism, and illegal bunkering estimated to be around 80,000 barrels per day (bpd) that has resulted in divestment, force majeure and production shut in by oil majors are mainly responsible. Hence, the problem may persist in 2014 if more pragmatic actions are not taken. There are also limited investment flows into exploration in the upstream oil activities as no new finds have been recorded in 2013 up till the third quarter. The continued delayed passage of the Petroleum Industry Bill may be exacerbating the situation as recent concerns have shown (Box 1).

![Chart 1. Real GDP Growth (%)](chart1.png)

Source: National Bureau of Statistics (NBS)
Box 1: Delayed Passage of the PIB and Petroleum Sector Performance

There are heightened concerns that the delayed passage of the PIB may be hurting the economy, starving it of the needed investment. One of the most powerful unions in the oil and gas industry, the Petroleum and Natural Gas Senior Staff Association of Nigeria (PENGASSAN) recently expressed concern that the situation poses serious challenge to investments in the sector by International Oil Companies (IOCs) with unrealized investment worth about $100 billion in the upstream sub-sector as a result of the risk-averse nature of most investors.

The PIB proposes a new legal, fiscal and regulatory framework for the oil and gas industry and has been praised by some for its focus on ensuring better returns for Nigeria and Nigerians from their oil and gas endowments. The Bill has been undergoing development and subsequent consideration by the National Assembly for the past 12 years with limited progress toward its passage. Several promises have been made in the past about its passage, including the promise to pass it before the end of 2013. However, its passage is still being awaited. There are several issues around contents, provisions and importance of the PIB that have led to arguments and counter-arguments by different stakeholders and interest groups. The concerns that the delayed passage may be hurting the economy are not unfounded given the poor performance of the sector with negative growth that stood at 0.74% at the end of the third quarter 2013. The lack of new discoveries in 2013 is a possible by-product of lack of investment in exploration. In fact, production stood at 1.9 million barrels per day (mbpd) compared to the budgeted estimate of 2.53 mbpd for 2013. Chances that the country would meet the 2.39 mbpd projected for 2014 is very slim. Added to this is the risk of expected increased fiscal spending as a result of the upcoming General Elections.

There are real and potential negative effects of developments in the oil and gas sector on outlook for the economy. ORNG will closely monitor these developments and their effects and engage national authorities in the effective dialogue for managing them.

Despite its poor performance, there were some interesting noteworthy developments in the sector during the quarter. Average daily production improved over the previous quarter at 2.26 million bpd, an increase from 2.11 million bpd in Q2. Also, restoration of 400,000 bpd production during the quarter due to re-opening of three major pipelines (Trans Niger, Nembe creek and Tebidaba-Brass pipelines) contributed to improving the situation in the sector.
Government efforts toward economic diversification and sustained implementation of the ongoing reform interventions in key sectors are expected to contribute to improved economic performance. Despite the threat from the discoveries and development of shale oil in the United States and oil theft in the domestic economy, Nigeria’s economy has been resilient due to proactive policies especially in the non-oil sector. Therefore sustenance of these efforts is necessary to sustain and/or increased growth in the future.

1.3 Monetary Policy

Monetary authorities maintained its tight monetary policy stance that has been very helpful in taming inflation to single digit at 8% in Q3. This has been reinforced by agriculture reform that has further reduced food inflation, the major driver of headline inflation.

Investor confidence appears to be gradually restored with the values of stock market capitalization increasing from N15.8 trillion in Q2 to N17.7 trillion in Q3 2013 and All Share Index by 1.16 percent from 36,164 Q2 to 36,585 over the same period, thus gravitating toward the pre-crisis level.

The link between domestically mobilized financial resources and the real sector activities is yet weak and demands policy focus.

Inflation continues to decelerate on the back of tight monetary policy stance of the Central Bank and other fiscal and reform measures (Chart 3). The year-on-year headline inflation which fluctuated between 15.1 and 10.2 percent since Q2 2008 declined to 8.0 percent at the end of the Q3 2013. Food and non-food inflation stood at 9.4 percent and 7.4 percent, respectively. While upward pressure on prices is usually expected for food items during the first half of the year which is usually a planting period, Q3 is a period of harvest, putting further downward pressure on the food sub-index. The programs of the Agricultural Transformation Agenda and other interventions seem to have ensured good harvest. There was a marked increase in non-food prices as a result of increases in prices of books and stationeries as school resumes for another academic year and the services of accommodation/apartments. Given the measures put in to moderate inflation, general prices are expected to remain in the single digit at end of the year.

However, two risks to sustainability of current sanguine monetary policy are identifiable, namely upcoming General Elections and imminent change in CBN leadership. As previous experiences have shown, election years are characterized by high fiscal spending that may consequently make it harder for the CBN to mop up excess liquidity in the system and ensure stable inflation rate. The second major risk is the upcoming change in leadership of the CBN that may possibly result in emergence of a leader that does not favor pursuing the current tight monetary policy stance.

Interest rates appear to be easing, suggesting that the financial inclusion policy of government and other lending initiatives may have begun to have positive impact. The slight rise in interbank lending rate to 14 percent in the quarter under review against 11.7 percent in the previous quarter is possibly a visible manifestation of the increase in CRR on public funds to 50 percent. One would expect, however, that raising average terms and lending rate would be an appropriate action to help improve savings mobilization that would help accommodate the constraint imposed by the increased CRR on public funds.
Investor confidence appears to be gradually restored in the capital market. This is apparent from the stock market capitalization that increased in value from N15.8 trillion in Q2 to N17.7 trillion in Q3 2013 and the Nigerian Stock Exchange (NSE) All Share Index (ASI) rising by 1.16 percent from 36,164 in Q2 to 36,585 in Q3 2013. The growing investor confidence underpinning this good performance may have been engendered by improved regulatory environment and improved financial results of listed companies as well as the country’s strong macro-economic fundamentals. However, there is a concern, that there is a weak link between the growing domestic financial resources mobilized and the real sector of the economy (Box 2).

**Box 2: Pension Fund and the Real Economy**

The Nigerian Pension Fund has witnessed phenomenal growth from a deficit of N2.6 trillion ($16.3 billion) before the take-off of the scheme in 2004 through N265 billion ($1.7 billion) in 2006 to N3.7 trillion ($23.2 billion) in 2013. The Fund is projected to reach $100 billion by 2020. However, there are concerns that the channels for deploying the Fund to benefit the real economy is highly limited and non-existent, in some cases. Also of concern is the possibility that the fund may result in asset bubbles in the medium term given the fund’s level and growth potential as the regulatory authorities make efforts to bring in the informal sector under the pension fund. This brings to the fore the delink between the financial and real sector of the economy.

The Pension Reform that began in 2004 has been highly successful with the Nigerian pension industry witnessing a dramatic revolution as demonstrated by the unprecedented growth in pension fund from 1.4% of GDP shortly after take-off in 2006 to its current level of 8.5% of GDP. There are two key implications of this growth. First, the Fund is growing faster than the available investment instruments that are growing at $2.5 billion a year, or approximately 1% of GDP per annum, raising concerns about possible asset bubbles in the medium-term since fund managers are increasingly chasing the few existing assets. Indeed, since there is provision that up to 70% of the pension fund can be held in government fixed income securities, the fund may be one of the main drivers of the rising appetite for government securities. Second, there are limited instruments such as corporate bonds, infrastructure bonds, private equity, and real estate investment trusts for channeling the Fund to the real sector. Pension Fund holds high potential for addressing two main constraints facing the Nigerian economy: infrastructure deficiency and limited structural transformation. However, this would be achieved only if managers of the economy are able to develop additional instruments for channeling the Fund to real sector activities. There is need to create additional private sector financial intermediaries and instruments such as specialized banks, private equity, venture capital funds, leasing companies, insurance funds, and micro-credit providers. Government also has a role to play in removing the risks and macroeconomic challenges associated with the financial sector. The AfDB is supporting national authorities in strengthening financial intermediation and link between the financial and real sector by supporting the proposed Development Finance Institution in the country. In addition, some of the bank’s ongoing private sector lending to deposite money banks also target SMEs and assist them to develop and deploy additional financial instruments for channeling financial resources to the real sector.
1.4 Fiscal Policy

The hitherto declining fiscal revenue was reversed during the quarter with significant increase by 14.4 percent over the previous quarter, driven largely by non-oil revenues while oil revenue continues to trend downwards.

Despite the increased retained Government revenue during the quarter, fiscal spending takes a long term perspective with a scale back in fiscal expenditures and concomitant improvement in overall fiscal balance.

Revenues and expenditures for the rest of the year is expected to mirror the current pattern given the spirited efforts of the government in fighting oil theft, illegal oil bunkering and pipeline vandalism.

1.4.1 Revenues

The previous quarterly declining revenue was reversed during the quarter with significant improvement of 14.4 percent, driven largely by non-oil revenues. The gross federally collected revenue for the third quarter 2013 fell short of its budgetary estimate and below the corresponding quarter in 2012 by about 4.2 percent and 1.6 percent, respectively. Total revenues for the quarter stood at US$17.3 billion compared to the US$17.7 realized in the 2012 corresponding quarter (Chart 4). However, when compared to the previous quarter where total revenue worth US$15.1 billion was realized, total federally collected revenues witnessed an improvement by 14.4 percent. This is a landmark achievement given the consistent decline in total quarterly federally collected revenues since Q4 2012. It is noteworthy that non-oil revenue is the source of the improved fiscal revenues during the quarter being reviewed.

The improved performance in total federally collected revenues mirrors improvement in non-oil revenues which experienced a leap to over 40 percent of total revenues, compared to 23.9 percent and 23.6 percent during the corresponding quarter in 2012 and previous quarter, respectively. Indeed, non-oil revenues increased by almost 100 percent in the quarter under review over the previous quarter. With this achievement, it is possible that the efforts of the Federal Government to diversify fiscal revenue sources may have started to yield some concrete results as the improved non-oil revenue sources can be traced mainly to company income and other corporate taxes that increased by almost 160 percent and other taxes that include education taxes which increased by almost 280 percent over the previous quarter (Chart 5). This is the highest ever recorded quarterly non-oil revenue performance in recent past. It is expected that this impressive non-oil revenue performance would continue given the ongoing Federal Government pursuance of improved revenue diversification.

Source: Central Bank of Nigeria
In contrast to the improved non-oil revenue performance, total realized oil revenues continue to slide, following the pattern that began in Q4 2012. During the quarter under review, oil revenues declined by 10.5 percent over the previous quarter and 16.2 percent over the corresponding quarter in 2012. Juxtaposing this outturn with the trend over the recent quarters, it appears that the oil theft, illegal oil bunkering and pipeline vandalism that has been the main source of declining oil revenues are yet to be contained by the Federal Government. Indeed, there are speculations that this would continue in 2014. If this trend persists and the improvement in non-oil revenues are not sustained, this would pose serious fiscal risks to the economy and could hamper the country’s development programs as enunciated in the Transformation Agenda. (See Box 3 for the 2014 proposed budget).

Chart 5. Non-Oil Revenue Sources

Source: Central Bank of Nigeria
The 2014 Budget proposal was recently presented to the National Assembly for debate and approval. The budget focuses on “Jobs and Inclusive Growth” and is underpinned by the following assumptions: GDP growth target of 6.75%; oil production of 2.3883 million barrels per day; crude oil benchmark price of $77.5; and exchange rate of N160/US$. It has a planned expenditure of N4.642 trillion ($29 billion) compared to total expenditure of N4.987 trillion ($31.2 billion) in 2013. However, recurrent expenditure has risen to 74.4% as compared to 67.5% in 2013. The Government therefore has the difficult balancing act of maintaining fiscal consolidation at the same time as creating policy space for jobs and inclusive growth.

Maintaining fiscal consolidation in the face of declining fiscal revenues, increasing job creation and social inclusion are the core challenges being addressed in the budget. The special intervention programmes, especially SURE-P and YouWin will be more effectively implemented to ensure more jobs are created. The proposal also outlined a focus on critical social sectors and infrastructure projects. In addition, new policy measures are also being initiated. First is the promotion of social protection and social safety net schemes with a view to reducing inequality and vulnerability. The North East Zone also receives special attention worth N5 billion ($32 million) through the Federal Initiative for the North East (FINE). A wholesale Development Finance Institution (DFI) is also proposed to improve medium to long-term financing for SMEs and agriculture with expectation that this initiative will be supported by the AfDB and the World Bank.

The forthcoming General Elections may present fiscal challenges as previous experiences have shown significant rise in expenditures during election cycle. Indeed, most of the election spending would be done this year since most elections would hold early 2015. That the fiscal deficit would worsen in 2014 is acknowledged in its downward revision to -1.9% compared to -1.85% of GDP in 2013. However, the fiscal deficit position may perform less than projected with possible supplementary budget proposal in the course of the year. Increasing recurrent expenditures driven by the bloating public sector wage bill at the expense of capital expenditure is additional challenge the government has to grapple with. The structure of the proposed budget is a cause for concern given the lack of political will to undertake public sector reforms that will reduce wage bill.

The government effort at promoting jobs and inclusive growth is laudable in the face of revenue shortfalls and other fiscal constraints. The focus on key labor-intensive and poverty-reducing activities in the social sectors, agriculture, SMEs, and providing incentives to the private sector are commendable. If well implemented, the budget would enable job creation and promote inclusive growth.

1.4.2 Expenditures

Despite the increased retained Government revenue during the quarter, fiscal spending takes a long term perspective with a scale back in fiscal expenditures and concomitant improvement in overall fiscal balance. The Federal Government retained revenue during the quarter under review increased by approximately 9 percent over both the previous and corresponding quarters in 2012 (Chart 6). Following the Federal Government’s fiscal consolidation plan, the increased retained revenue did not induce increased expenditure but rather resulted in improved overall fiscal balance by almost 60 percent and 80 percent over the previous quarter and corresponding quarter of 2012, respectively. Indeed, despite the increased retained revenues, total expenditures and all its components decreased when compared to the previous quarter.
While there is significant progress in the Federal Government’s expenditure restructuring toward capital expenditure relative to recurrent expenditure to 24 percent during the period under review compared to 16.5 percent in the corresponding quarter of 2012, a slight slide of about 0.5 percent was recorded over the previous quarter. This suggests need for the fiscal authorities to watch more closely the expenditure pattern to ensure the target to reduce recurrent expenditure to 60 percent while raising capital expenditure to 40 percent of total spending by 2015 is achieved.

On outlook for the rest of the year, there are expectations of relative revenue stability around the current level. This emanates from the expected positive effects of government fight against oil theft, illegal oil bunkering and pipeline vandalism. The outlook is also anchored on the expectation that the global oil price will be stable in the immediate term. The improving global economy, especially of Nigeria’s oil buyers such as the US, Euro Zone and China suggests that the demand for oil would strengthen in the medium term. These factors are expected to reinforce themselves to increase oil exports and revenues. The general budget performance is expected be below target, with capital component performing worse because capital expenditures bears the brunt of the accommodative expenditures given the shortfall in revenues since recurrent expenditures are sensitive to adjustments.

1.4.3 Debt and Composition

The concern about the rising Federal Government domestic debt remains valid as the figure increased by 2.7 percent in the quarter under review over the previous quarter and almost 11 percent over the corresponding quarter of 2012 (Chart 7). This is indicative that the domestic debt now appears to be increasing at a suppressed rate compared to what it was until recently. As mentioned in earlier report, the fiscal authorities are engaging in ongoing initiatives that focus on correcting this trend. It is expected that as the ingenious fiscal consolidation interventions begin to yield results, the trend in domestic debt is expected to further ease.

Source: Central Bank of Nigeria
External debt profile is trending upwards and appears to be structurally evolving in favour of commercial debt. External debt stood at US$8.3 billion or 19.4 percent 31.3 percent increase over the preceding quarter and corresponding quarter in 2012, respectively (Chart 8). The percentage share of multilateral debt in total external debt increased from 70 percent in the previous quarter to 80 percent in the current quarter. Conversely, commercial debt that represented 7.7 percent of total external debt in the preceding quarter now accounted for 18.5 percent in the quarter under review. While this is not yet alarming, there is need for the debt management and fiscal authorities to be wary of this creeping tendency and make concerted effort to nip it in the bud. Otherwise, debt servicing growth and payments may gradually erode the fiscal space engendered by the soft nature of bilateral and other concessionary loans that had dominated the country’s external debt profile. The need to keep watchful eye on reversing the emerging trend in external debt remains valid.
1.5 External Sector

- Oil theft and pipeline vandalism is seriously impinging on exports and foreign reserves with both declining during the quarter under review.

- The partial petrol subsidy removal and close monitoring of the subsidy regime seems to have led to significant decline in imports. This is reinforced by government import substitution policy intervention.

- The slowdown in investment may not be unconnected with perceived risks attached to the upcoming General Elections and delayed passage of the PIB since significant foreign investment goes to the oil and gas sector.

1.5.1 Trade

Nigeria experienced a decline in total trade of around 7 percent in the third quarter when compared with the previous quarter and the pattern is becoming a bit more unpredictable (Chart 9). As pointed out in the previous report, while the poor performance in oil exports may be a factor responsible for the observed trade performance, trade facilitation also plays a very important role. To illustrate, while Nigeria performs better than the averages of Sub-Saharan African (SSA) and lower middle income countries on information availability in the OECD trade facilitation indicators, its performance in automation, streamlining of procedures and internal border agency co-operation falls below the SSA and lower middle income countries. This suggests that efforts need to be directed toward improving the country’s trade facilitation capacity.

The decline in total imports during the quarter under review is driven largely by the decrease in oil imports by 38 percent over the previous quarter because non-oil imports increased by 10 percent (Chart 10). Continued strengthening and monitoring of the petrol subsidy system appears to be the factor responsible for the declining oil imports. Strenuous efforts are ongoing to further tighten the system to prevent leakages as a result of activities unscrupulous businessmen.

**Chart 9. Total Trade**

Source: Central Bank of Nigeria
One important feature of non-oil imports composition in Nigeria that calls for attention is the very high share of manufacturing imports as a percentage of total merchandise imports. This suggests that value added products, especially manufactures, are in high import demand. This is a reflection of the weak manufacturing base in the country and a manifestation of weak firm-level value addition. This demands attention and could be corrected through focused implementation of the industrialization policy being developed. The market potential of the economy is very large. Such focused policy on improved domestic manufacturing would provide local substitution to the large imports of manufactures. Scaling up on this with time will also provide opportunity for exports, beginning with the ECOWAS market.

Oil production losses and theft unarguably determines the pattern of exports in Nigeria since it accounts for quarterly average of about 97 percent of total exports (Chart 11). Hence, once the oil sector sneezes, total exports catches cold. This further reiterates the level of exposure of the country to external shocks given the economy’s high trade concentration. Export diversification is surely the way out. But there is need for specific national policy on diversification. Currently, there are sectoral and activity-specific interventions to boost non-oil activities. This is discernible in the Agriculture Transformation Agenda that focuses on developing agribusiness and value chain around agriculture in different parts of the country. Several activities are also ongoing to promote industrialization and, SME activities. These include the National Enterprise Development Programme (NEDEP), National Automotive Policy, National Competitiveness and Consumer Protection Policy, etc. The challenge, though, is that these policy initiatives appear to be functioning in silos and need better coordination. There is compelling reason, therefore, for the country to develop a National Economic Diversification Policy that will be comprehensive and integrative of all these sector- and activity-specific interventions.
To improve trade performance in the economy, policy efforts need to focus on improving trade facilitation, especially with the ECOWAS member countries. This will help to improve bilateral flow of trade between Nigeria and the rest of the world. Specific actions in this direction would include lowering trade costs, with specific focus on reducing trade formalities. This would require streamlining trade procedures and documentation and spearheading harmonization of these across the ECOWAS member countries. Nigeria has high trade potential and except there is a significant unexpected backlash from the oil theft challenges facing the country, trade performance is expected to end on a relatively stable level that is not significantly different from the recent quarters. This is especially so given the fact that the last quarter of the year is usually marked by increased trade activities in preparation for the December yuletide season.

1.5.2 Investment

Nigeria is experiencing slowdown in portfolio and FDI inflows based on investor expectations and risk perception of existing and potential investors (Chart 12). Foreign investment is declining and should be considered a cause for concern since this is happening in two consecutive quarters. Nigeria has consistently been the number one investment destination in Africa in 2011 and 2012. Moreover, portfolio investment has been rising in emerging market, making one to wonder why Nigeria should not have similar experience. It, therefore, appears that investors may be a bit cautious about the Nigerian market.
This declining trend in investment, especially the portfolio component may be motivated by perceived political risks by investors based on the upcoming General Elections in 2015. Hence, this trend is expected to continue in the next few quarters up until after the elections. In addition, since the bulk of FDI inflows goes to the oil and gas sector, the delayed passage of the Petroleum Industry Bill may be accountable for the reduced FDI inflows.

1.5.3 External Reserves

The Nigerian external reserves have been trending downward over the last one year (Chart 13). See Box 4 for detailed exposé on this development and the possible link with the oil theft phenomenon.
1.5.4 Balance of Payments

The overall BoP position of the country has significantly worsened over the last two quarters, recording a negative balance of 4.5 percent and 1.5 percent, respectively, compared to the surplus balance of 6.8 percent in the first quarter of the year (Table 1). The declining trend in the current account and capital account balances reflect the weak trade and investment performance in the recent quarters. CBN foreign exchange management continues to yield good results with the nominal effective exchange rate remaining stable around N157 to a dollar.

Box 4: Oil Theft and External Reserves in Nigeria

The continued drop in Nigerian external reserves has heightened concerns as it has now dipped below the 12-month low of $44.2 billion in mid-December. As at December 18, the external reserves had dropped to $44.16 billion from the recent peak of $48.86 billion in May 2, 2013, corresponding to about 10% decrease. At $44.26 billion at the end of 2012, the country’s external reserves finished $6 billion below the government’s target. The continuous depletion of the foreign reserves is taking place against the back drop of oil theft in the country that has impacted negatively on oil exports, revenues and foreign reserves accumulation. This has forced the country to lower its production target for 2014 to 2.383 million barrels per day (mbpd) from its 2.53 mbpd target for 2013.

The continuous depletion of the Nigerian foreign reserves can be traced mainly to the combined effect of oil theft and pipeline vandalism resulting in shutdown and force majeure by some international oil majors. The direct effect of this is decline in oil exports and consequently foreign exchange inflows. Official estimates by the Federal Ministry of Finance puts the loss to be around 80,000 barrels per day while a Chatham House report has $38 billion as annual loss. In addition, production shut in as a result of oil theft is estimated to further cost the country about one-fifth of its total production output.

While Nigerian foreign reserves remain strong and adequate measured by months of import cover (over 6 moths), there is need to ensure the rate of depletion is addressed. This is more expedient because there are projections that the ongoing oil theft and pipeline vandalism that reduces oil exports may persist in the coming year. The discovery of alternatives to crude oil such as shale gas may lead to significant reduction in the global demand for the product and consequently reducing its price. Additionally, investment in electric and hybrid automobiles may reinforce the discovery of alternatives to crude oil to further force down the price of crude oil. Policy focus on economic diversification and deeper structural transformation of the economy would provide a way out of this conundrum. Otherwise, this phenomenon may impact on the prospect for the present good sovereign credit and risk rating the country currently enjoys. It may also have serious implication for inclusive growth through decline in fiscal expenditures on key growth-enhancing priority sectors and capital projects since the country depends largely on oil revenues for these activities.
### Table 1: Balance of Payments

<table>
<thead>
<tr>
<th></th>
<th>Q1 2012</th>
<th>Q2 2012</th>
<th>Q3 2012</th>
<th>Q4 2012</th>
<th>Q1 2013</th>
<th>Q2 2013</th>
<th>Q3 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Account Balance (% GDP)</td>
<td>7.9</td>
<td>3.1</td>
<td>13.5</td>
<td>7.3</td>
<td>10.8</td>
<td>14.0</td>
<td>12.7</td>
</tr>
<tr>
<td>Capital &amp; Fin Account Balance (% GDP)</td>
<td>8.2</td>
<td>-5.2</td>
<td>-11.9</td>
<td>-8.9</td>
<td>-3.6</td>
<td>2.8</td>
<td>1.5</td>
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<tr>
<td>Overall Balance (% GDP)</td>
<td>4.3</td>
<td>0.4</td>
<td>7.8</td>
<td>4.7</td>
<td>6.8</td>
<td>-4.5</td>
<td>-1.3</td>
</tr>
<tr>
<td>External Reserves Stock (Billion USS)</td>
<td>35.20</td>
<td>35.41</td>
<td>40.64</td>
<td>43.83</td>
<td>47.88</td>
<td>44.96</td>
<td>44.11</td>
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<tr>
<td>External Reserves (Months of Imports Equivalent)</td>
<td>6.7</td>
<td>6.9</td>
<td>12.0</td>
<td>10.7</td>
<td>12.5</td>
<td>9.5</td>
<td>10.2</td>
</tr>
<tr>
<td>External Debt Stock (Billion USS)</td>
<td>5.99</td>
<td>6.04</td>
<td>6.30</td>
<td>6.53</td>
<td>6.67</td>
<td>6.92</td>
<td>8.26</td>
</tr>
<tr>
<td>Effective Central Exchange Rate (N/$)</td>
<td>156.7</td>
<td>156.1</td>
<td>156.1</td>
<td>156.0</td>
<td>156.0</td>
<td>156.0</td>
<td>156.1</td>
</tr>
<tr>
<td>Average Exchange Rate (N/$)</td>
<td>157.9</td>
<td>157.3</td>
<td>157.4</td>
<td>157.3</td>
<td>156.0</td>
<td>157.3</td>
<td>157.4</td>
</tr>
</tbody>
</table>

Source: Central Bank of Nigeria
The oil and gas sector is beset by several challenges, notably unsustainable subsidy payments, delayed passage of the Petroleum Industry Bill, oil theft, illegal bunkering and pipeline vandalism.

These challenges are evident in negative growth performance of the sector, acting as a drag on growth and weak investment, especially in upstream activities.

Key reform interventions include the Presidential Amnesty Programme for ex-Niger Delta militants, local content development, full subsidy removal of subsidy on diesel and partial removal of petrol subsidy.

Key evidence of positive effects of reform in the sector is the renewed domestic and foreign investor interest in upstream economic activities, petroleum refineries and petroleum value chain

To consolidate on gains, efforts must be made to complete the process of passing the PIB into law and effectively address the ongoing oil theft and pipeline vandalism that currently characterizes the sector.

The oil and gas industry is the most important sector in Nigeria’s economy as the main source of fiscal revenues, exports and foreign exchange earnings. With proven oil reserve of about 37.14 billion barrels and gas reserves of about 5,118 billion cubic metres, Nigeria is in the top ten countries with largest crude oil and gas reserves in the world. Petroleum and gas account for annual average of approximately 95 percent of total foreign exchange earnings and about 85 percent of total fiscal revenues. Production is dominated by joint ventures between the state-owned oil company, Nigerian National Petroleum Corporation (NNPC) and oil majors accounting for 95% of total production while independent firms operating in the marginal fields account for the balance.

However, the sector is beset by several challenges that tend to militate against harnessing its full potential in contributing toward sustainable inclusive economic growth in Nigeria. First, there is limited domestic capacity to manage the sector. Hence, upstream activities, including supplies, services and fabrication are dominated by foreign firms. Second, youth militancy and agitation for increased resource control in the Niger Delta resulting in kidnaps of expatriates, production disruptions has resulted in challenging operating environment. Third, there is negative environmental effect of oil exploitation activities, spills and gas flaring. Fourth, poor investment in exploration, leading to low discoveries and no new finds in 2013. Lastly and more recently, crude oil and petroleum product theft has negatively affected the sector, fiscal revenues by $38 billion per annum and foreign earnings and consequently excess crude account and foreign reserves. Federal Ministry of Finance estimated a daily loss of 80,000 barrels per day while a Chatham House report estimated annual loss to be $38 billion.
These developments have had significant negative effect on the oil and gas sector. One, the sector has been experiencing negative growth in recent times that stood at 0.74% at the end of the third quarter in 2013. Two, limited investment in the sector has resulted in lack of new discoveries, especially in 2013. Three, oil production has been dwindling, with production reducing by estimated daily average of 80,000 barrels per day and daily production revolving around 1.9 million barrels per day (mbpd) compared to the budgeted estimate of 2.53 mbpd for 2013. Four, fiscal revenues has declined by estimated $38 billion per annum, foreign reserves and the excess crude account have been declining, with reserves falling from a recent peak of $48.86 billion in May 2, 2013 to $43.6 billion at the end of 2013.

The determination of the Federal Government to address these challenges and their obvious effects has motivated significant reforms in the sector. The reforms are motivated by the need to: develop the country’s energy resources that would guarantee the achievement of diversified energy sources; guarantee an efficient and cost effective consumption pattern of petroleum products; and improve local content and capacity in the operations and management of the sector. To actualize these, several targeted reform actions have been taken in the past to address the perceived challenges in the sector. The three main ones are the Local Content Development, the Presidential Amnesty Programme (PAP) for former youth militants in the Niger Delta, and partial subsidy removal on petrol.

The Local Content Policy aims at championing the course for higher indigenous participation and value addition in the country’s oil and gas industry. One of the major thrusts of the policy was to promote higher participation of Small and Medium-sized firms within the industry. To drive the process, the regulatory and administrative framework was developed through articulation of the Nigerian Oil and Gas Industry Content Development Act 2010 and establishment of the Nigerian Content Development and Monitoring Board in 2010 the same year to supervise, guide, monitor, coordinate and implement the provisions of the Act. The key mandates of the institution include: increasing indigenous participation in the oil and gas industry; building local capacity and competencies; creating linkages to other sectors of the national economy; and boost industry contributions to the growth of our National Gross Domestic Product. Some of the key achievements of this reform include establishment of the Nigerian Content Development Fund to the tune of $350 million; attraction of $5 billion worth of investments into the economy; creation of about 38,000 jobs between 2009 and 2013. Challenges remain, though, that require urgent attention. These are: ineffective supervision, cumbersome prequalification requirements, and inadequate financing for the domestic firms.

The PAP for the ex-Niger Delta militants focuses on restoring peace to the hitherto troublesome Niger Delta region. The Niger Delta youth militancy started in 2006 as a result of grievances against perceived poverty and underdevelopment, poor regulation of the oil industry resulting in environmental pollution, and the desire for more involvement of the local people in the management of oil resources. The activities of the militants led to significant loss in oil production from 2.6 mbpd to 1.7 mbpd. Commencing in 2010, the PAP seeks to rehabilitate and reintegrate into the society over 30,000 militants that surrendered their arms and renounced militancy by offering them monthly allowances and training. Many of them were sent to local and foreign universities and vocational institutions to learn skills that would help them get easily integrated into the society. The achievements of this intervention include reduction in abductions of oil workers, reduced attacks on oil facilities and increased oil production. It has also resulted in community empowerment and increased local capacity in oil and gas-related activities in the oil producing areas. However, there are concerns that this could become a slippery slope as crafting an exit strategy could become a political issue and may thus become difficult to implement.

The complete removal of the petrol subsidy that has been ongoing for a very long time was attempted on January 1, 2012, following earlier successful complete removal of subsidy on diesel. Over the years, payments for fuel subsidy have gradually become a fiscal Albatross. Between 2006 and August 2011, total government expenditures on petroleum
subsidies amount to N3.7 trillion, increasing from N261 billion in 2006 to N673 billion in 2011, representing about 160 percent rise. About $8 billion was spent in 2011 alone on petrol subsidy payments, accounting for 30 percent of the fiscal spending, about 4 percent of GDP and 118 percent of capital budget. Hence, the petrol subsidy became an unsustainable fiscal burden while simultaneously restraining investment in the downstream petroleum sector. Indeed, the subsidy regime benefited unscrupulous businessmen engaging in oil imports. However, the policy attempt led to serious resistance that finally resulted in partial removal of the subsidy with the pump price increasing from around $0.40 to $0.60. The partial subsidy removal has resulted in substantial fiscal savings that has been deployed to the Subsidy Reinvestment and Empowerment Programme (SURE-P). This programme has become the channel for deploying the petrol subsidy savings into improving education, maternal and child health, power, roads and bridges, mass transit, water resources and agriculture. Through the savings, the Federal Government has also engaged in capacity building through: Graduate Internship Scheme; Vocational Studies; Public Works; and Community Service, Women and Youth Empowerment Programme.

In recent times, there has been gravitation toward ensuring that the oil and gas sector reform is encapsulated in the Petroleum Industry Bill (PIB). The Bill seeks to establish the required effective legal, regulatory and institutional framework for efficient operations of the petroleum industry. It also stipulates guidelines for operations in the upstream and downstream activities (see Box 5).

**Box 5: The Petroleum Industry Bill**

The Nigerian oil and Gas industry is undergoing series of reforms. Going forward, the reform agenda for the sector is being driven through the Petroleum Industry Bill (PIB). The PIB currently undergoing legislative processes at the National Assembly establishes the legal and regulatory framework, institutions and regulatory authorities for the Nigerian petroleum industry. It also stipulates guidelines for operations in the upstream and downstream sectors.

The objectives of the PIB are therefore as follows: enhance exploration and exploitation of petroleum resources; significantly increase domestic gas supplies especially for power and industry; create competitive business environment for the exploitation of oil and gas; establish fiscal framework that is flexible, stable and competitively attractive; create commercially viable national oil company; create strong and effective regulatory institutions; promote Nigerian content; and promote and protect health, safety and environment.

The proposed reforms in the PIB can broadly be divided into two; non-fiscal and fiscal reforms. Non-fiscal reforms relate to institutional and policy re-orientation. At the heart of the PIB is the separation between policy, regulation and monitoring and commercial operations. Based on this innovative idea, the PIB seeks to build institutions around these core principles. Under this, the Ministry of Petroleum Resources has responsibility for the evolution of policy in the oil and gas sector. Under the Ministry are the Regulatory Institutions charged with regulation and monitoring while the National Oil Company is responsible for commercial operations. The building blocks of these institutional and policy reforms are: the Unbundling of NNPC as presently constituted through the creation of a National Oil Company that promotes indigenous operational capacity development; creation of an Asset Management Limited, a limited liability company to manage the joint venture assets on behalf of the federation; and the excision of Nigerian Gas Company (NGC) from NNPC as a separate partially privatised entity to cater for domestic gas marketing and gas infrastructure development. The intention here is to accelerate national gas infrastructure development for effective gas supply to power industrial sector of the economy. This is expected to be realized through private equity participation of up to 49%.

The PIB represents the largest overhaul of the government petroleum revenue system in the last four decades. This overhaul has four central objectives: simplify the collection of government revenues; cream off windfall profits in case of high oil prices; collect more revenues from large profitable fields in the deep offshore waters; and create Nigerian employment and business opportunities, by encouraging investment in small oil and gas fields.
The Bill appropriately delineates roles among the various institutions in the industry and crafted to stimulate the much talked about overall reform of the oil and gas sector. The bill combines a multitude of laws and regulations into a single consistent piece of legislation that modifies the fiscal regime; overhauls the national oil company and other key executive and regulatory agencies; sets the stage for deregulation of downstream activities; and introduces measures to improve transparency and accountability. The proposed restructuring is based on the need to create a vibrant industry where the private sector plays a prominent role. It is expected that all funding issues would be resolved. It would pave way for the removal of all bureaucratic bottlenecks, minimize undue government interference and guarantee effectiveness and result-oriented performance.

The Bill has been undergoing development and subsequent consideration by the National Assembly for the past 12 years without significant progress toward its passage. Several promises have been made in the past about its passage, including the promise to pass it before the end of 2013. However, none of these were actualized. Different stakeholders appear to have with the BIP around contents, provisions and its importance, leading to arguments and counter-arguments by different stakeholders and interest groups. Concerns that the delayed passage may be hurting the economy are becoming heightened.

The reforms in the oil and gas sector have yielded significant results. One of the noticeable projects in the reform was the launch of 'Project Aquila' by the management of the Petroleum Equalization Fund Management Board. The project is an electronic monitoring of petroleum products distribution which resulted in an increase in products availability in depots and outlets from 40 per cent in 2010 to almost 95 per cent in 2013 thus eliminating diversion and incessant scarcity characterizing petroleum products in the past. The project has also improved promptness of claims payments to marketers.

Renewed interest by both domestic and foreign investors in domestic petroleum refineries and value chain. As a result of improved confidence in the sector, about N53 billion investments, 1000 new retail outlets and 800 new trucks were recorded between 2010 and 2013. The highlight of these is the plan by an indigenous investor, Dangote Group to invest $9 billion in greenfield investment in petroleum products value chain that include refineries, petrochemicals and fertilizer. MoUs have also been signed with some Chinese firms for investment in greenfield refineries in the country. Hence, the country may soon become a net exporter of refined petroleum products.

Increased domestic gas supply and reduced gas flaring. Under the reforms, the initiated Nigeria Gas Master Plan and Gas Revolution has resulted in increased domestic gas production supply and revenue. The Nigeria Gas Company has increased its sales and transmission throughput from722 mmcsf/d in 2011 to about 800 mmcsf/d in 2012.

Increased domestic participation in the upstream oil and gas activities. The Local Content Act has resulted in many indigenous businesses securing contractual services jobs from the international oil companies (IOCs). For instance, Marine vessels of various categories wholly owned by Nigerians increase from 54 in 2011 to 180 by the end of 2012 with further increase to 208 by the first quarter 2013. Nigerian companies are now forming partnerships for deep-water rig ownership. Recently, several Nigerian indigenous firms bought large oil facilities from oil majors, thus increasing their operations in the sector.

Increased job creation and improved technical know-how for indigenes.

According to estimate from the NCMDB, indigenous investments in critical oil and gas infrastructure in creating employment for 30,000 Nigerians, creating wealth and increasing technical Know-how for technology transfer.

Despite these achievements, challenges to sustainability of the oil and gas sector remain. The greatest and most pressing of these is the delayed passage of the PIB. There are heightened concerns that this may be hurting the economy through investment scale back by risk averse investors. In addition, the recent phenomena of oil theft and pipeline vandalism have devastated effect, not just on the performance of the sector, but also on the macro-economy through decline in fiscal revenues. Local capacity, technical know-how, participation, job creation and integration of the sector with other sectors of the economy remain weak. These are the key areas that demand serious attention if the gains from the reforms so far are to be consolidated and delivered to majority of Nigerians.
1. Introduction

Nigeria is characterized by high infrastructure deficiency with limited fiscal resources to meet the needs, thus necessitating finding alternative infrastructure development financing sources.

PPP is a desired alternative source of infrastructure funding because of its cost effectiveness, delivery of better value for money, sustainability, and increased funding synergy.

Infrastructure Concessionary and Regulatory Commission (ICRC) Act 2005, establishment of ICRC and development of the National Policy on PPP provide the regulatory and institutional framework for PPP operations in Nigeria.

Some of the key challenges facing PPP in Nigeria include weak regulatory and enforcement powers, limited capacity to drive PPP process, poor planning and coordination between public and private partners involved in PPP projects, and weak cooperation and collaboration among MDAs on PPP-related activities.

To succeed in using PPP to drive infrastructure development in Nigeria, there is need for political commitment, effective overall coordination, protection of interest of all parties by ensuring that all agreements are enshrined in law, involving the private sector early in project conceptualization and development, and realistic expectations from private partner by public partner.

Nigeria has high infrastructure development needs. Infrastructure deficiency is unarguably a major challenge facing the country today. Infrastructure needs for roads, ports and railway networks tend to constrain businesses and limit the potentials of the country through increased cost of transportation and trade. In a recent estimate, the government plans to spend $2.9 trillion through its 30-year Nigeria Integrated Infrastructure Master Plan (Usman 2013). Similarly, the AfDB in its Infrastructure Action Plan for Nigeria estimated total expenditures of $350 billion between 2011 and 2010. It is a fact that government alone cannot raise this huge sum of money, thus necessitating the need to explore alternative funding sources. One of which is public-private partnership (PPP).

International experiences from successful PPP countries such as China, India, Indonesia, and Korea have shown that the benefits of PPP infrastructure provisioning are numerous. They include cost effectiveness and better value for money, sustainability, and increased funding synergy. It also allows the government to focus on its primary role of a regulator rather than service provider. In all, PPP offers the opportunity to provide infrastructure through allocating and transferring financial, technical and
management risks to the private sector that is best placed to manage this process within a reasonable time and at the least cost and acceptable quality. There are snags, though, that have equally been identified as shortfall to the use of this infrastructure development model. They are: more expensive method of funding capital projects due to the profit component for the private firms involved and serving as potential the additional borrowing costs; lengthy tendering process; and conduit for corruption and diversion of public funds.

Several years back, Nigeria experimented with this method of infrastructure provision. For example, the development of Dolphin Estate in Lagos in the 1980s was through PPP between Lagos State Government and HFP Construction Limited. The project was a tremendous success. The current reforms involving strategies for infrastructure development has led to re-consideration of PPP as an option (Zenith Bank 2008). While this option has since been adopted, meaningful progress and impact are yet to be felt.

This section focuses on the state of PPP in Nigeria. It reviews the existing regulatory, institutional and administrative framework for PPP in the country and documents the perceived challenges that have moderated success. The section further looks at the lessons from the experiences of successful countries that could be useful as Nigeria explores this potential strategy for bridging its infrastructure gap.

2. Institutional, Regulatory and Administrative Framework for PPP in Nigeria

The renaissance of PPP as a global best practice for infrastructure development and the decision to embrace this strategy require establishment of an institutional, administrative and regulatory framework for ensuring smooth operation of the system. To this end, the Federal Government established the Infrastructure Concessionary and Regulatory Commission (ICRC) in 2005 to serve as the umpire agency to regulate, monitor and supervise the contracts on infrastructure or development projects in the country. Hence, establishment of the ICRC is a major milestone in the emergence of PPP process in Nigeria.

The core objective of ICRC includes the following: to implement and establish effective PPP process; take custody of every concession agreement made under the enabling Act and monitor compliance with the terms and conditions of such agreement; build a pipeline of public infrastructure investment projects using the Ministries, Departments and Agencies (MDAs) that are operating in high priority sectors with a view to attracting private sector investment; and ensure the development and consistent implementation and application of a robust, transparent, efficient and equitable processes for managing the selection, development, procurement, implementation and monitoring of PPP projects. The sectoral focus of the agency covers all infrastructure activities, prominent among which are power, transport, ports, water supply, education and health facilities, housing, and solid waste.

To strengthen its position to effectively deliver on its mandate, the agency has developed a National Policy on Private Public Partnership to serve as a guide for all PPP engagements in the country. The policy document outlines a clear and consistent procedural guides for all aspects of PPP project identification, initiation, evaluation, selection, procurement, operation, maintenance and performance monitoring.

One of the major interventions by the government to strengthen the institutional, regulatory and administrative framework for PPP in Nigeria was initiation and execution of an IDA-funded “Nigeria PPP Programme” through an Adaptable Programme Loan (APL) facility. The loan valued US$315 million was signed in 2011 with the World Bank to support the ICRC to develop a national PPP project. The first phase of the programme that runs over six years involved spending a total sum of US $115 million for Capacity building in two core areas of project development and transaction advisory services to ICRC and MDAs that are active in developing PPP projects. The second phase worth US $200 million focuses on two key areas: providing seed funds for the development of long-term financing instruments in the country’s Financial Market and assisting the Federal Government to establish a Structured Viability Gap funding scheme to support its infrastructure PPP projects.
However, establishment of the ICRC, development of the National Policy on PPP that aim to provide creative financing and asset management to infrastructure development and the strengthening the PPP framework have not significantly changed the landscape of PPP infrastructure development process in Nigeria. Since its history, the agency has only succeeded in developing one project, namely, urban infrastructure development in Katampe and Mabushii both in the FCT.

Indeed, several PPP projects are beset by challenges that have made them unsuccessful. Some of the unsuccessful projects are the Lagos-Ibadan Expressway concession to Bi-Courtney Nigeria Ltd, Guto-Bagana Bridge Contract involving the Concessionaire (Digital Toll Ltd), the Project Contractor (Nairda Ltd), the Project Consultant (Siraj Nig. Ltd), and the public partners (Federal Ministry of Works, Kogi State Government and Nasarawa State Government. There has been several disputes on concessions, particularly between Bi-Courtney Ltd and FAAN on the MMA2 contract, Bi-Courtney Ltd and Federal Ministry of Works on Lagos-Ibadan Expressway, Seaport Terminals, Lekki Toll Road, and Aulic Nigeria Limited and Lagos international Trade Fair Complex (LITFC) Management Board on the LITFC and Lagos State Government.

3. Challenges facing PPP in Nigeria

The general failure of PPP projects in Nigeria suggests existence of some challenges militating against their success. Some of these challenges are highlighted below.

First, the regulatory and enforcement powers of ICRC is weak, as evident in the Act establishing the agency. The ICRC enabling Act focuses more on concession contracts and less on PPP process. Even the focus on concession contracts is weakened by the fact that no provision is made in its Act for the contracts that were operational prior to establishing the agency. In addition, the agency lacks enforcement powers on PPP contracts with no clear provision in its Act to enforce real and potential dispute resolution system. There is also the issue of overlap between the mandates of ICRC and some regulatory agencies engaged in similar activities such as the Bureau of Public Enterprises (BPE) and Bureau of Public Procurement (BPP). These challenges emanating from its Act limits the capacity of the agency to provide effective oversight of PPP initiatives. Hopefully, the ongoing review of the Act would help identify these inherent weaknesses and address them.

Second, there is limited capacity to drive PPP process in Nigeria. Capacity in this very important area is still emerging at both private and public levels. Most MDAs and even private investors do not have full understanding of what PPP involves and its modus operandi. Also, MDAs do not have the required capacity to undertake meaningful economic project appraisal that would lead to development of long-term PPP investment strategy. Therefore, there is real need for focused intervention in developing adequate facility to correct this. This would require advocacy and sensitization of all stakeholders involved in the partnership. It appears that sufficient advocacy was not done prior to commencement of PPP process. ICRC needs to be more active in this regard through the use of innovative outreach mediums. This should be combined with capacity development for all stakeholders, especially Ministries, Departments and Agencies (MDAs). This would require strengthening the PPP units in the MDAs.

Third, poor planning and coordination between public and private partners involved in PPP projects. The case that illustrates this is the Lekki Toll Road Concession Project between the Lagos State Government and Lekki Concession Company Ltd. There appears to be an apparent challenge with the project as evidenced in the delay in completion and operationalizing the project.

Fourth, risks on return on investment for prospective private sector partner. Private investors engaged in PPP projects are interested in safety of their funds and payback period of their investment (Delmon 2009). However, there are several factors that characterize the operating environment that limit certainty of this. The high cost and short borrowing tenor imply that private investors may not be able to generate sufficient returns to cover their cost and make profits within a reasonable period of time. Political risks also come into play where a change in government...
may lead to non-honoring of the terms of the contract by the new government. It is a common knowledge that once a new government comes into office, most existing contracts and agreements signed by previous office holders are subjected to scrutiny, review and probes. There is also the weak legal environment where contract enforcement is yet weak and may take a long process. Knowledge of the existence of these risks forces prospective private sector investors to shudder from undertaking PPP projects (Bayliss 2009).

**Fifth, existence of weak long-term finance for infrastructure.** Long-term financing is imperative for successful PPP. This requires effective mobilization and utilization of domestic and foreign financial resources. Success will be limited if the country rely on building roads with 25% interest from deposit money banks. There is, therefore, need to develop a framework for the deployment of long-term funds such as pension, etc, to mobilize resources for PPP. Applying short-term fund to long-term PPP projects is a serious mismatch that need to be corrected.

**Sixth, mismatch between PPP transaction life cycle and national budget cycle.** The PPP lifecycle ranges between 12 and 36 months compared to the national budget cycle of approximately 12 months. This mismatch implies that many PPP projects cannot be accommodated in the budget cycle. Efforts to accommodate PPP projects that have longer gestation period may lead to cutting corners and sacrificing the required detailed process for the projects. Such tardy project development process may mean developing PPP projects that are dead on arrival.

**Seventh, weak cooperation and collaboration among MDAs on PPP-related activities.** The success of PPP depends largely on cooperation among MDAs and the regulatory agency since the infrastructure activities cover all sectors of the economy. In some instances, the regulatory agencies has received cold shoulder with regard to its request to concerned institutions provide it with adequate information on legacy PPP projects and other concession contracts entered into. This limits the capacity of the agency to effectively discharge its mandate that include compliance monitoring and enforcement of the terms of the contract.

Eight, PPP project could serve as conduit for exploiting taxpayers. There are concerns that PPP projects sometimes serve as a conduit for corruption and siphoning public funds into private pockets. Hence, while the public takes the risks, the private partners get all the profits. This occurs through engagements in unscrupulous activities by the private sector partner over invoicing, deliberate miscalculations, and passing undisclosed costs to the public partner.

4. **Evolving Effective PPP: Lessons for Nigeria**

The poor performance of PPP in the country emanating from the myriads of challenges facing it despite the significant real need for infrastructure development and the existence of a regulatory institution to drive the process is worrisome and needs some attention. Lessons from successful countries and projects would provide guide and direction on the way forward.

**Government must demonstrate political commitment by assuming leading role at the formative and development stages of PPP.** This is important because PPP concept is a new phenomenon with very limited knowledge and understanding on the process and mode of operation. The GMR Group and Government of India PPP projects in Delhi and Hyderabad International Airports provides a classical example in this respect. The political will and weight thrown behind the project provides the needed groundwork for the success with respect to its acceptance and successful management and operations. At the development stage of the Athens International Airport, the Greek Government assisted the private sector partners to secure funds through EIB loans and made this available for 50% of total construction costs with a total maturity of 25 years. Also in the Attiki Odos motorway project in Greece, the government ensured that all the required permits for the design, construction, financing, operation, exploitation and maintenance of the project were issued promptly to assure effective and smooth development and operation of the project.

**Integrate the needs of all parties and ensure all PPP contracts are enshrined in law to protect all partners involved in the project.** Most investors are risk-averse and are
interested in the security of their investment. Public partners interested in ensuring value for money and protection of taxpayers money. To achieve these, agreements on PPP contracts must be properly documented such that should conflict arise, there are grounds for redress. For example, the 30-year concession between the Greek Government and the Athens International Airport Company for the management of the Athens International Airport was coded in the Law, clearly stating the exclusivity of the rights of the private partner in the design, financing, construction, completion, commissioning, maintenance, operation, management and development of the airport. With such well defined partnership agreement, the private partner is assured of its role and framework for the partnership is clear.

Overall coordination is important to overcome challenges associated with PPP projects. There is no perfect PPP project anywhere, not even in the most successful countries. The only way to overcome the real and potential emerging challenges is proper coordination. For example, the Nottingham Express Transit Tram Line One project between Nottingham City Council and Nottinghamshire County Council and Transdev European faced several challenges and delays during the development and design phases. Milestones were missed, commissioning time was significantly reduced and inspectorate approval to operate and hence scheduled start of operations were extended. This resulted in additional costs to the construction element of the project. However, proper coordination of the process among the government and the private sector partners that include sponsors, contractors and operators helped achieve the needed success in the management of the delays.

Involve the private sector early in project conceptualization and development. This helps provide the needed commercial due diligence and assurance that a bankable and deliverable proposal is developed. Involvement of private sector operators would ensure development of sound feasibility and viability appraisal. This will, in turn, promote funding either from domestic and foreign investors and help avoid risk allocation challenges. This would also require setting up a small project team with the needed complementary skills at a very early stage of the project. Such team should be appropriately empowered financially and technically to take important decisions in the course of developing the project. This was the success factor in the Kirklees Metropolitan Council and United Waste Services Limited in the UK’s Kirklees Metropolitan Solid Waste project.

Assure transparency and integrity at the planning stages through frank and open discussions with prospective investors. In the case of the Kirklees Metropolitan Solid Waste project, the procurement method was not sufficiently clear. At the end, success was achieved because the process was made more transparent, effectively managed and best solution was openly negotiated through post tender dialogues and discussions.

Encourage private sector innovation. There is no need limiting the scope of use of appropriate technology in the execution of the project. Hence, the public partner should allow the private partner to be imaginative in the application of new technology that could lead to significant cost saving. The advantage of this is that it could help save public funds and achieve better value for money. This lesson is illustrated by the Norfolk Street Lighting where evaluation methodology maintained an appropriate balance between quality/technical specification and cost.

The public sector should be realistic on its expectations from the private partner. Public sector should neither demand nor expect too much from the private partner in their project partnerships. This includes recognizing the needs and constraints of the private party. Additionally the requirements of external financiers need to be integrated at an early stage so as to reduce time delay and cost at later stages. These highlight the need for a partnership based on mutual understanding and a certain amount of trust and agreement on each other’s objectives.

Ensure that projects are demand-driven and highly responsive to specific needs of the society. All successful PPP projects in whatever sector conceivable are based on need. This implies existence of ready market and use of the activities being undertaken. They are either private service or product providing activities or social services provision. The bottom line is that such projects must focus on meeting existing demands and needs.
Other lessons are: development of proper project financing strategy; good framework for contractor selection; effective information dissemination and communication system throughout the life of the project; continuous project monitoring, evaluation and control; and absence of political pressure.

5. Conclusion

Globally, Governments are increasingly relying on PPP model as a creative financing mechanism to maintain and improve national, regional and local infrastructure in all facets of the economy for both hard and soft infrastructure. This becomes a viable option given budgetary challenges in the face of competing needs for the use of fiscal revenues. Many countries have successfully tapped into this innovative infrastructure finance option. This is yet the case in Nigeria.

To achieve this and join the league of successful countries, tapping into the experiences of these countries is imperative. To ensure accelerated smooth transition to PPP, there is need to restructure state-owned enterprises and strengthen the regulatory framework (AfDB 2010). Among other things, government must: ensure demonstrated political commitment; develop efficient and sound framework for initiating, developing, implementing and operating PPP projects; develop capacity of both the private and public sector players in this new area with respect to procurement, negotiations, monitoring and evaluation of PPP projects; collaborate with the private partner to undertake effective costing of projects including real and potential risks; ensure accessible and sustainable source of financing; promote transparency and trust between both partners throughout the life of the project.

Through its engagements with the Nigerian authorities, the African Development Bank will continue to dialogue with the government through its Infrastructure Action Plan on mainstreaming PPP as a viable infrastructure development option for the country.


