

Financial Market Development and Fiscal Deficit Financing In Nigeria

By

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ABSTRACT

This study examines the implications of financing fiscal deficit from domestic sources on the development of the Nigerian financial markets. Specifically, the study attempts to establish whether there is a significant relationship between fiscal deficit financing options and the development of the country's financial markets in the short run and long run. The study also seeks to establish causality between fiscal deficit and financial markets. In addition, the study assessed whether domestic debt crowd out or crowd in private sector investment in Nigeria. A modified Keynesian Twin-Deficit Model was used to capture the empirical relationship between fiscal deficit financing and financial market development. The model was estimated using ARDL in order to capture the long run equilibrium relationship between the variables. The results showed that there is long run association running from fiscal deficits to financial market development. More specifically, budget deficit, domestic debt and government expenditure significantly impacted on the development of the Nigerian financial markets. Besides, in the long-run, budget deficit impact did not stimulate (improve) financial development. Another observation is that domestic debt significantly impacted negatively on private sector investment lending credence to the hypothesis that domestic public debt crowds out private sector investment in Nigeria. The findings indicate that fiscal policy in Nigeria has a strong role in macroeconomic stabilization. The government is advised to curtail the massive and persistent budget deficit. Fiscal policies should play a more neutral role in the effort to stimulate private sector entrepreneurship and investment in the economy.

JELCodes: E44, E52, E62, H62

Keywords: Budget Deficit, Domestic Debt, Private Credit, Financial Development, ARDL

1.0 Introduction

The Nigerian government has engaged in both domestic and external financing of its debts arising from budget deficit. Economic theory and empirical literature has demonstrated that both sources have implication on the overall macroeconomic conditions. The experience of Nigerian government with external debt obligation had led the government to engage more in domestic financing than external financing in its budget deficit. Financing budget deficit through domestic financial market has implications on both the financial intermediation and stock market development. While several studies have investigated the effects of external debts on the Nigeria economy, less attention has been paid to the consequence of financing budget deficit domestically on domestic financial market.

The Nigerian government has engaged in monotonous recurrent expenditure which is has been virtually fiscal deficit for decades. With the exception of the periods 1971, 1973, 1974, 1979, 1995, and 1996, there were overall deficits in the federal government budgets each year since 1970 to date. Even the budget surpluses so claimed by the Federal Ministry of Finance for 1995 and 1996, may actually turn out to be deficits when exposed to more appropriate accounting and budgetary procedures (Adedotun, 1997).

The country has had a very unpleasant sojourn into external borrowing which culminated in being highly indebted to the London and Paris Club between 1960 and 2000. The high extension external debt stock in the country which started as mere US \$69.7 million in 1960, rose to US 246.0 Million in 1970, representing 252 percent increase, and then to 3,146.0 million in 1977. Although the total debt stock declined in 1975 and 1976 by 10.3 and 20.7 percent, the average growth of debt between 1970 and 1977 was 5.9 percent. The external debt stock rose from US \$8,934.0 million in 1980 to US \$12,954.0 million in 1982, and US \$19,550 million in 1985 (Anyanwu et al 1997). The total external debt outstanding as at 31st December 2004 stood at US\$35.94 billion as against US\$32.92 billion in December 2003, indicating an increase of US\$3.03 billion or 9.20 percent. As was the case in the year 2003, the increase in the debt stock was largely as a result of the interest component of additional payment arrears that accumulated, and continued depreciation of the US dollar against other currencies in which the debts were denominated. According to Iyoha (2005), "it is obvious that even if we managed to pay the interest and charges alone, there was no way in which we could ever hope to pay the principal, this is why it is the "Debt Trap", The country suffered the severe consequence of debt overhang until the regime of President Obasanjo managed to lift the unpleasant burden off the shoulders of the Nigerian people in 2007 when he paid off a substantial portion of Nigeria's external debt and the country exited both the Paris and London Clubs. The Nigeria's external debt position had

been brought down from N2.70 trillion in 2005 to N431m in 2007 by the Obasanjo's administration. In March 2015, owing to the Jonathan's administration, the country was owing external debts in excess on N2 trillion. Many writers have argued that huge external debt stock slows down economic growth in the poor countries of the world as it consumes valuable resources in debt service obligations and principal repayment (World Bank (1989), Iyoha (1990), Kenen (1990) and Adams (2001)). The unpleasant experience in the sojourn of external borrowing has made it imperative for the Nigerian governments to look inwards for domestic sources of financing fiscal deficits in the country.

The issue of domestic debt in Nigeria has taken centre stage in Nigeria as the source for government to finance projects and grow the economy in recent times. This is achieved by issuing debt instruments to the Nigerian public through existing financial institutions and markets. As the Nigerian economy developed after independence and with the problems encountered with external borrowing, successive governments started to borrow internally to finance fiscal deficits. Nigeria's domestic debts are denominated in the country's local currency (Naira). Federal government domestic debt which stood at N11.2 billion in 1981 had risen to N84 billion in 1990 (increase of 750%). In the year 2000, domestic debts had risen to N898 billion and to N4.13 trillion in 2007. In 2012 Nigeria's domestic debts were N6.6 trillion. As at March 2015, Nigeria's short term and long term domestic debts stood at N8.5 trillion. This figure does not compare favourably with total credit to private sector which stood at N18.6 billion for the same period of March, 2015.

There have been various sentiments express by parties on the growing domestic debt position of the Nigerian economy. For instance, Former Coordinating Minister of the economy put Nigeria's total debt stock at \$63.7 billion (Okonjo-Iweala, 2015). She noted that \$9.7 billion or 15 per cent is external while \$54 billion or 85 per cent represents domestic debt. Even with this figure, the former minister noted that Nigeria still has one of the lowest fiscal deficits in the world with debt to GDP ratio of about 1.5 per cent of the budget. The country's Gross Domestic Product (GDP) for December 2014 was estimated at 568.51 billion US dollars.

African Development Bank (AfDB, 2015), in its African Economic Outlook 2015 cautioned against Nigeria's rising public debt profile which it puts at \$67.7 billion as at December 2014. The body observed that total public debt level, which represents a five per cent increase from end-2013, was driven largely by the 10 per cent rise in the domestic debts of the federal and state governments. They contend that the "Increased domestic public debt has a tendency to raise interest rates, resulting in crowding out of the private sector from the local credit market. Anecdotal evidence suggests that increased public domestic debt is the major driver of the high

lending rate in the country coupled with high monetary policy rate. Federal Government bonds and Nigerian treasury bills are the dominant instruments in the country's domestic debt, accounting for over 95 percent of total domestic debt stock", the report noted.

However, beyond consideration of maximum acceptable Debt-GDP ratio of 30% (for a developing country like Nigeria) a more critical consideration for the development of the country is the financial market absorptive capacity which might be quite low given the threshold. Domestic debt is therefore a topic to examine at this point of the country's national development when unemployment is critically high and the global economic crisis is far from being resolved. The trend of government borrowing from the domestic market may therefore raise three issues;

First, has fiscal deficit financing from the nation's domestic sources contributed to the development of financial markets?

Second, does the country's fiscal deficit cause financial market development, or, is it the other way round?

Third, does the country's domestic debt stock rise the profile of interest rate?

Fourth, does fiscal deficit financing from the domestic financial market crowd out or crowd in private sector investment in Nigeria?

Several studies have been conducted on Nigeria's public debt (local and foreign) and their impact on the country's economic growth and development. The existing literature is scanty on the link between fiscal deficit financing and the effects on the country's financial markets. This study intends to determine the impact of fiscal deficit financing on the development of country's financial markets. The study also desires to assess the impact of public domestic debt on private sector investment in the country. The scope of study covers the period of 1981 to 2013.

The paper is divided into five sections; the first section gives a general introduction to the topic of financial market development and fiscal deficit financing in Nigeria therefore serving as background to the study stating its problems, objectives, research questions and justification. Section 2 looks into the review of existing related literature and empirical studies on the topic, while section 3 presents the theoretical framework, model of analysis and definition of variables for the study. Section 4 discusses the estimation strategy and presentation of results. Section 5 discusses the conclusions and policy recommendations.

2.0 Literature review

Fiscal deficit may be defined in terms of loan financing and drawing down on cash balances. One of the most important aspects of fiscal policy is the management of the public sector's fiscal deficit. Such fiscal deficit simply refers to the excess of the public sector's spending over its revenue (The World Bank, 2005). The concept of fiscal deficits have been at the forefront of macroeconomic adjustment – purposeful and coherent set of measures used to respond to (often severe) imbalances in the economy both in developing and developed nations (Anyanwu, 1997). More specifically fiscal deficit may be considered a practice in which a government spends more money than it receives as revenue. In other words, budget deficit refers to a gap between public revenues and expenditures. Revenues normally come from taxation and public property while expenditures may cover development projects as well as current expenses of running government. Budget deficit has to be bridged by increasing revenues, reducing expenditures, internal borrowing from public, commercial banks and central bank, and by external borrowing. Public borrowing has become a major feature of contemporary economies in both developed and developing countries.

Gardner Patterson defines deficit financing as the net increase in the amount of money in circulation where such an increase results from a conscious governmental policy designed to encourage economic activities which would otherwise not have taken place (Oluwabukola and Falowo, 2013). Prudently used, deficit financing could be a very powerful tool of capital formation. He identifies traditional methods of financing the deficit as including net borrowing from the Central Bank, the commercial banking system, non-banking financial intermediaries, and depletion of cash balances.

Jhingan (2007) also defines deficit financing along similar lines; deficit financing refers to the financing of the deliberately created gap between public revenue and public expenditure or a budgetary deficit, the method of financing being one that results in the net addition to national outlay or aggregate expenditure.

Fischer and Easterly (1990) identify four ways of financing the government fiscal deficit:

- 1) Printing money (ways and means)
- 2) External borrowing

3) The use of foreign reserves

4) Domestic borrowing

Broadly speaking, the existing two major methods of financing the budget deficit include monetary financing and debt financing. Macroeconomic variables could, therefore, be regarded as the economic fundamentals or preconditions that must be fulfilled without which investment cannot take place. Deficit usually occurs as a result of government inability to match revenue and expenditure (Paiko, 2012). The deficit is financed either through borrowings (domestically or foreign) or use of foreign reserve to settle the deficit. By borrowing it means the government has to agree on the terms payments which usually are attached with strange regulations.

The sources of domestic borrowing can be categorized into four (Oluwabukola and Falowo, 2013):

1) Borrowing from the Banking System

2) Borrowing from the non-banking public

3) Borrowing from the Central Bank through the issuance of new currency

4) Drawing from the reserves of the Central bank

Borrowing from the Banking System: This is carried out by issuing government bonds and securities directly to the banking institutions. The banks use their excess reserves to purchase such securities. This method is also referred to as bond financing. The implication of this is a reduction in the credit creation capacity of banks through the depletion of external reserves.

Borrowing from the Non-banking public: In this case, government bonds and securities are sold to the public, who in turn transfer a part of their resources to the government. This leads to reduction in the general level of saving, thereby affecting the level of private investments.

Issuance of New Currency (Ways and Means): Deficits are financed by the creation of new currency or printing of new money by the Central Bank. This tends to increase the money supply/growth in the economy and has an inflationary impact. The quantity theory of money by the classical economists says that inflation is driven by money growth. Under this theory, changes in money supply are proportional to changes in prices with no impact on output and employment. This will lead to inflation (as too much money chasing too few goods will increase

demand and raise prices). This brings a twist to Friedman statement that “inflation is everywhere a monetary phenomenon”. Inflation might be a monetary phenomenon, but money is a reflection of fiscal policy and not of monetary policy.

Drawing from Central Bank Reserves: Deficits are financed from funds generated by the central bank through its banking functions. Funds such as those meant for the purchase of foreign exchange are lent to the government for its expenditure operations (Nwaogwugwu, 2005).

On the development models of public expenditure which primarily is the works of Musgrave (1974) and Rustow (1971) anchors on the fact that the countries of the world must pass through different stages before they could develop, and that these different stages requires varied proportion of Government spending to total investment in the economy will be large since most of her activities center on capital formation bordering on roads, housing, telephone, education and health care, among others in preparation for takeoff in to the middle stage.

When government borrows from foreign sources to finance budget deficit it means the nation has to agree on the terms payments which usually are attached with strange regulations. Hence, this may perpetrate the deficit as more money would be spent by government on servicing the debt. External borrowing usually causes appreciation of real exchange rate, deepening current account deficit, increases of foreign debt and loss of foreign reserves. Extreme and very serious result of this foreign borrowing can be currency crises, for which this scenario is very common (Hakkio, 1996). The situation could degenerate to induce more expenditure and further deficit to service the debt. Persistence of this may result to high and variable inflation with crowding out of investment and may lead to stunted growth and macro - economic imbalance (Osuji and Ozurumba, 2013).

Persistent borrowing from external sources to finance budget deficit could result to high extension debt stock which could mean a huge debt burden on the nation. This may have a dampening effect on macroeconomic investment mainly through the “debt overhang” effect, arising from crowding out effect and credit rationing effect. **Debt overhang** is the condition of an organization or government that has existing debt so great that it cannot easily borrow more money, even when that new borrowing is actually a good investment that would more than pay for itself. **Credit rationing** refers to situation in which a highly indebted country is likely to face credit constraint in international capital market and this would lead to reduction investment.

Increasing taxes could serve as an internal source of funds for government to finance a budget deficit situation. This source of financing is only viable where the citizens of the country are viable enough to afford the increase in taxes.

But in a country, where a majority of people are living on the subsistence level, the margin between income and consumption is very low so that the citizens may not be buoyant enough to absorb tax increases. However, there have been attempts by governments in developing countries to increase the funding for projects by raising additional taxes. During the last few years, taxes have been gradually increased developing countries in the effort to mobilize resources for development activity (Mascagni, 2014). Yet because there is extreme poverty among the great mass of the people, additional taxation beyond a point raises difficult problems. In Nigeria, attempts at upward revision of tax rates have made governments unpopular such that the effort has become politically inexpedient. Therefore, in the anxiety to implement development schemes in developing countries, the governments are compelled to resort to other sources of financing the resulting budget deficit situation.

In developing countries where the option to increase tax rate might not serve to as a viable financing arrangement to meet a budget deficit situation, the likely most feasible option might be to raise funds through the domestic financial markets. The choice to raise funds through the domestic financial markets could end up being more enduring as all foreign debts (and accumulated interest) would eventually be paid up from domestic sources.

2.1 Empirical Literature

The related studies that have been reviewed in this study could be categorized into three. The first set of studies concern the relationship between of fiscal budget deficits and private sector investment while the second set of studies would relate fiscal deficits with economic growth. The third set of literature would relate financial sector development to fiscal deficit financing.

Looney E. Robert (1995) examined public sector deficits and private investment while testing the crowding-out hypothesis in Pakistan's Manufacturing industry. He deployed the modified granger causality test and suggested that expanded public investment in infrastructure led to a situation that dampened the flow of private capital borrowing into the important large scale manufacturing sector. He concluded that financial crowding-out of private investment was a

strong possibility (though not simply a straight forward process) that resulted from the expanded public sector investment in infrastructure. The weakness of the study lies in the fact that even the modified granger causality test is not enough to justify the extent the crowding-out hypothesis.

Ahmed Badawi (2003): attempts to address the issue of complementarity and substitutability of state capital to private sector investment activities in a neoclassical growth framework. He employs a co-integrated vector autoregressive model to account for potential endogeneity and non-stationarity problems. The results suggest that both private and public capital spending have stimulated economic growth in Sudan over the period 1970-98. The impact of private investment on real growth has been more pronounced than that of public sector investment. Public sector investment appears to have deleteriously impacted private sector physical capital expansion, implying that the impact of crowding-out categories of public sector investment has been large enough to offset any crowding-in effects. Such crowding out effect weakened the favourable positive effect that public sector's investment has exerted on growth by jeopardising private sector capital undertakings.

Samah and Ahmed (2014) Driven by the observed growing budget deficit and the heavy reliance on debt-financing from the banking sector, this study sets to test the lazy banking hypothesis for Egypt. According to this hypothesis, government borrowing crowds out private investment through its dampening effect on private credit. The study estimates a VAR model using quarterly data spanning for almost four decades. The estimated model has unearthed a number of interesting results. As the government issues more debt instruments to finance its deficit, banks shift their portfolio away from risky private loans and opt for lazy behavior characterized by a shrinking overall credit tilted more and more toward government debt-instruments. This behavior not only limits their exposure to the private sector, hence reducing private investment, but also adversely affects investment and hence overall growth potential. In addition, evidence shows that output growth positively impacts the willingness of the banking sector to extend more credit to both the government and the private sector. Finally, and consistent with the lazy bank model, impulse response functions show that the effect of a government borrowing shock is contractionary (as opposed to the effect of private credit shock which is slightly expansionary) with regard to the overall banking sector credit.

Sinevičienė (2013) examined the relationship between government expenditure and private investment in the case of small open economies. She had in mind that governments could promote private investment increasing government expenditure, but increase of government expenditure can both crowd out and crowd in private investment. In order to assess relationship between government expenditure and private investment in the chosen countries, cross-correlations and Granger causality tests are applied using data of Bulgaria, Estonia, Latvia, Lithuania and Slovenia during 1996 – 2012. The results showed that impact of government expenditure increase on private investment is very weak, but negative impact of government expenditure increase on private investment dominates, except in the case of Bulgaria; whereas the impact of private investment increase on government expenditure is very different in analyzed countries.

Shetta and Kamaly (2014) observed the growing budget deficit in Egypt and the reliance on debt financing from the banking sector. The effort was to test the hypothesis that government borrowing crowd out private investment through the dampening effect on credit to the private sector. The study employs a VAR model using quarterly data spanning four decades. They found out that as government issues more debt instruments to finance deficit, banks shift their portfolio away from risky private loans and opt for government debt-instruments. This behavior limited banks' exposure to the private sector and adversely affected general level of investment and the potential for growth in the economy.

Njiforti and Muhammad (2010) investigated the relationship between public sector borrowing and deficit financing on the one hand, and private sector saving and investment on the other, in the Nigerian economy. Multiple regression technique was utilized on Nigerian economy data spanning 1992 to 2007. Deficit financing in Nigeria is observed to crowd-out private saving and investment and due to inability to influence savings deposit rate upward.

Paiko (2012) examined the relationship between deficit financing and private sector investment in Nigeria. Employing multiple regression techniques, the result showed that a negative relationship between deficit-financing and investment in the period under review i.e deficit financing in Nigeria crowds out private investment.

Ezeabasili and Nwakoby (2013) studied the relationship between government expenditure and private sector investment in Nigeria. They paid specific attention to budget deficit and crowding

out effect of private sector investments. The employed cointegration and error correction model in their analysis. While confirming the relevance of the accelerator principle to Nigeria, it was observed that improvement in national income engenders increase in private investment. In addition, it was observed that fiscal deficits had a depressive effect on private investment in the country. The results also showed that Nigeria's debt profile has had strong and negative impact on private investment in Nigeria.

Adesuyi and Falowo (2013) studied the relationship between fiscal deficit and the performance of the Nigerian economy. Their analysis entailed the utilization of multiple regression technique on data that spanned between 1981 and 2010. The study concluded that fiscal deficit had made significant impact in the growth and performance of the Nigerian economy. The study did not cover the impact of fiscal deficit on private investment in the economy.

Ekpo (1994) investigates the impact of government expenditure on economic growth in Nigeria between 1960 and 1992, using ordinary least square technique. The study confirms that government spending on infrastructure as well as investments in agriculture crowd in private investment, while spending on manufacturing crowds out private investment. The study concludes that public sector investments in infrastructure complements the private sector and implicitly enhances growth.

Maduka and Onwuka (2014) investigated both the long run and short run relationships between financial structure and economic growth using time series data. The presence of a unit root in the time series data was tested using Augmented Dickey – Fuller and Philips – Perron tests. The long run relationship among the variables is estimated using Johansen and Juselius (1990) maximum likelihood procedure. While the vector error correction model is used to estimate short run the dynamic coefficients. The main results reveal that financial market structure has a negative and significant effect on economic growth based on Nigeria data. This suggests a low level of development of the country's financial sector. The paper therefore recommends that there is a need to put appropriate financial policies in place that will encourage the growth per capita GDP.

Running public fiscal deficits typically reduces national savings, and lower national savings, in turn, leads to reduced investment and reduced net exports (Ball and Mankiw, 1995). Investment is curtailed because a drop in national savings restricts the supply of loanable funds, forcing interest rates higher. In the long run, the fall in investment lowers the capital stock, reducing

productive capital and output. The crowding out of investment and capital also lowers productivity growth and hence real wages.

Ahmad and Malik (2009) used panel data for 35 developing countries over the period of 1970 – 2003, analyzing the role of financial sector development in economic growth and domestic and foreign capital accumulation. They found that financial development affects per capita GDP mainly through its role in efficient resource allocation, rather than its effects on capital accumulation. Furthermore, they contend that it is the domestic rather than foreign capital accumulation that is instrumental in increasing per worker output and hence promoting economic growth in the long-run. Furthermore, foreign capital also does not stimulate domestic capital accumulation, while domestic capital plays a significant role as a complementary factor in attracting foreign capital.

Jamshed Y. Uppal (2011) studied government budget deficits and the development of bond market in Pakistan. He sought for ways to improve market performance through institutional checks and balances and discipline. He examined the role of political institutions and budgetary process in the fiscal policy process of the country. The study concludes that the installation of a comprehensive fiscal discipline process remains the long-term solution to an improved, active and liquid bond market. He recommended strong political will and raising public awareness as additional measures required the planned reforms in the country's financial markets. The study did not give precise measures on the relationship between fiscal spending and the development of the country's bond market.

Jen-Te, Hwang et al (2011) used panel data of 20 high external debt countries selected from Asia and Latin-America to investigate the financial sector development-debt-growth nexus within the framework of an endogenous growth and financial development mechanism. First, they found that among 20 high external debt countries, the external debt-to-GDP ratio is significantly negatively correlated with economic growth rates, indicating that excessive debt is detrimental to the growth of an economy. Second, they introduced the simultaneous GMM equations between financial sector development and economic growth to evaluate the interaction effects among economic growth, external debt, and financial sector development. In empirical results, they found that the negative impact of high debt on growth appears to operate through a strong negative effect, in terms of compulsion to resort to financially repressive policies. In addition,

they also find a two-way relationship between financial sector development and economic growth.

2.2 Overview of the Nigerian Financial Sector

The Nigerian financial system comprises of various institutions, instruments and regulations. According to Central Bank of Nigeria (1993), the financial system refers to the set of rules and regulations and the aggregation of financial arrangements, institutions, agents that interact with each other to foster economic growth and development of a nation. The financial system plays a key role in the mobilization and allocation of savings for productive purposes. It also assists in the reduction of risks faced by firms and businesses in their production processes, improvement of portfolio diversification, and insulation of the economy from external shocks (Nzotta, 2004). In addition, the system provides linkages for different sectors of the economy and encourages a high level of specialization and economies of scale.

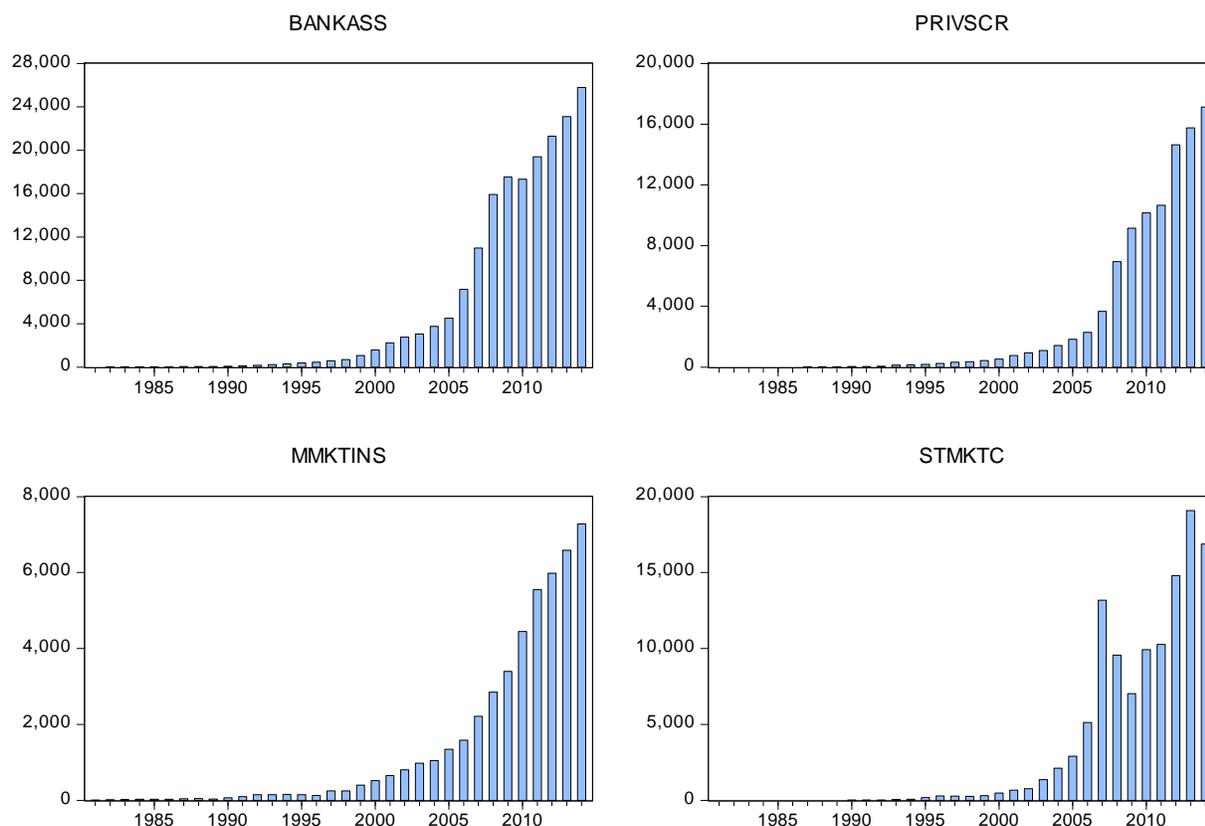
The Nigerian financial system can be divided into two sub-sectors; the formal and informal sectors. The informal sector has no formalized institutional framework, no formal structure of rates and comprises the local money lenders, thrift collectors, savings and loan associations and all forms of 'Isusu' associations (Nzotta and Okereke, 2009). According to Olofin and Afangideh (2008), this sector is poorly developed and not integrated into the formal financial system, therefore, its exact size and effect on the economy remain unknown and are a matter of speculation. The formal sector on the other hand comprises of bank and non-bank financial institutions. Bank financial institutions are the deposit taking institutions. As financial intermediaries, they channel funds from surplus economic units to deficit units to facilitate trade and capital formation.

They include; central bank, commercial banks, development banks, co-operative and commerce banks, etc. while, the non-banks financial institutions include; the money markets, capital markets, insurance companies, pension funds, etc. These institutions are not deposit taking institutions, but some of them perform intermediation functions of channeling funds from surplus to deficit units for economic activities, for instance, money and capital markets. The regulatory institutions in the financial system are; the Federal Ministry of Finance, Central Bank of Nigeria as the apex institution in the money market, the Securities and Exchange Commission (SEC) as

the apex institution in the capital market, Nigeria. Deposit Insurance Corporation (NDIC), National Insurance Commission (NAICOM) and the National Pension Commission (PENCOM).

Since independence, business activity in the Nigerian financial sector has been on the increase. Over the years, the financial sector has witnessed several reforms in the effort to strengthen the size and depth of the markets. The most ambitious financial sector reform in Nigeria was implemented in 2004 by the Olusegun Obasanjo's administration. The implementation of the 2004 banking reforms triggered various mergers which reduced the number of deposit banks in Nigeria from 89 to 25. In an attempt to meet up with the new capital regulatory capital base requirements (raised from N2 billion to N25 billion), the banks raised an equivalent of \$3bn from domestic capital markets and attracted about \$652m of foreign direct investment (FDI) into the Nigerian Banking System. This reform was also introduced to enable Nigerian banks to become active domestic and global players in the financial markets. Other financial institutions like merchant banks, insurance companies, finance companies etc have also been growing. Also included in the reform exercise are specialized banks such as industrial development banks, agricultural and rural development banks and mortgage banks. The financial sector has been liberalized in Nigeria. The efforts of that singular reform produce some very commendable improvement in the Nigerian financial markets. The impact could be witnessed from the trends revealed in figure 1. It can be seen that Total Commercial Banks Assets (BANKASS) from about N32 billion in 1985 grew to N83 billion in 1990 and then to N385 billion and N1.6 trillion in 1995 and 2000. Subsequently, it grew to N4.5 trillion, N17.3 trillion, and N25.8 trillion in the years 2005, 2010 and 2014 respectively. From the figure, other money market variables like Private Sector Credit (PSCR, from Commercial Banks) and Money Market Instruments (MMKTINS) grew in a similar fashion. During the period of analysis, a lot of performance variables experienced growth in the Nigerian financial markets. For instance, Stock market capitalization from N6.6 billion in 1985, it grew dramatically to N16.3 billion and N180.4 billion in 1990 and 1995 respectively. Furthermore, the variable continued its upward trend from N472.3 billion and N2.1 trillion respectively in 2000 and 2005 to N9,9 trillion and N16.9 trillion in 2010 and 2014 respectively.

Figure 1 – Overview of the Nigeria’s Financial System



Sources: Based on Data from the Central Bank of Nigeria (CBN)

However, despite the impressive growth records of banks and non-bank financial institutions in Nigeria during the period, coupled with the financial liberalization policy, the Nigeria financial system is still considered to be fragile and shallow in depth (Maduka, 2013 and Moyo 2014).

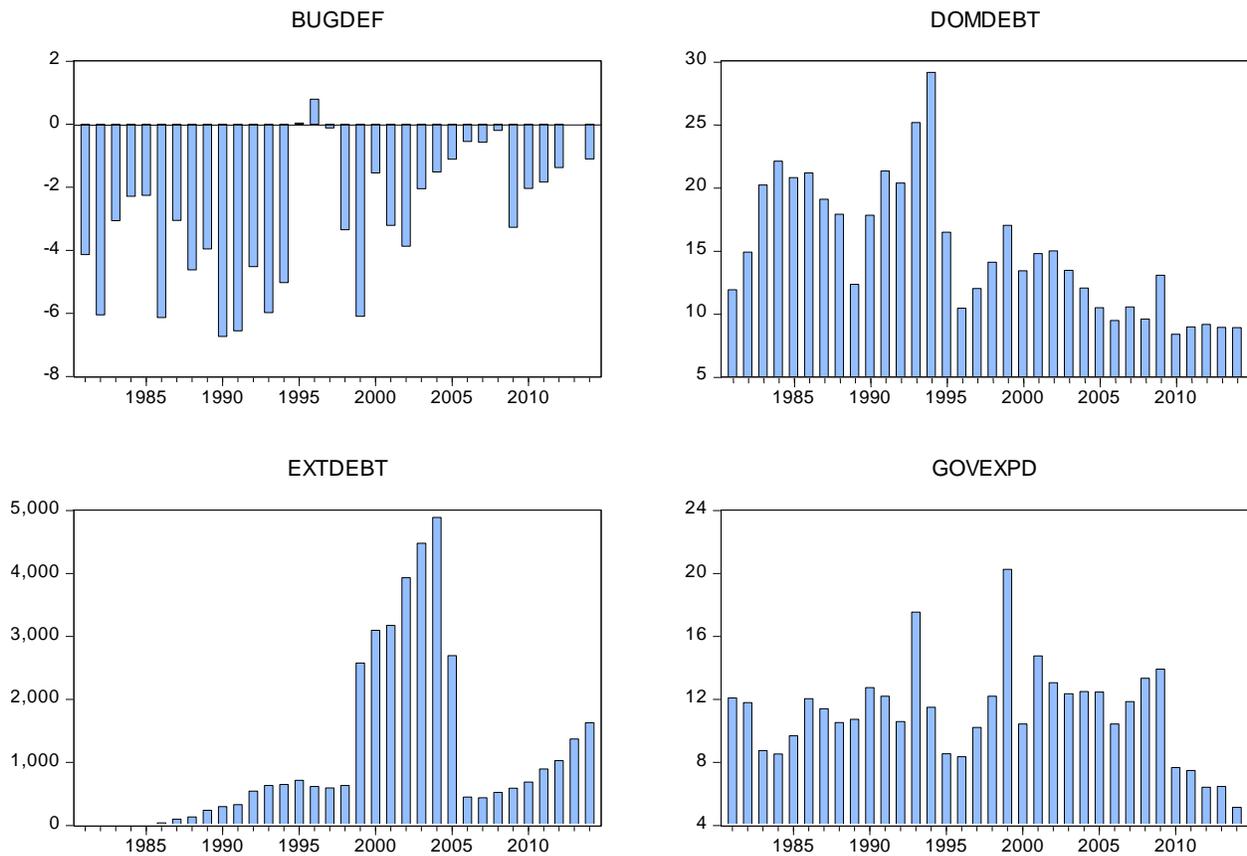
2.3 Public Expenditure and Public Debt in Nigeria

The international oil market glut of early 1980s (which marked the end of the Arab-Israeli War), coupled with the Nigerian government zeal to continue maintaining its planned expenditure level at the face of falling revenues, resulted into chronic budget and BOPs deficits and huge debt burdens (Adubi et al, 1994). An analysis of the fiscal operations of the Nigerian government have shown a continued huge deficit as its main features since the late 20th century (NCEMA, 1991) as cited by Adubi et al (1994). Thus, the trends in figure 2 show the Nigerian government ran a deficit budget for our entire period of analysis. Except for 1995 and 1996 when the budget

became negative, government budgets for the entire period of analysis were basically negative. The highest point of budget deficit was in 1990 with over N6 trillion. However, lowest point was in 1996 with a positive of about N800 million.

In the course of trying to finance the deficit budgets during the period, the Nigerian government embarked on public sector borrowing from both domestic and foreign sources. Domestic debt in Nigeria grew from N11.8 trillion in 1981 to N20.7 trillion in 1985. In 1990 it was N17.8 trillion but got to an all time high in 1994 with N29.1 trillion. By the year 2000 it has dropped to N13.4 trillion. It kept on dropping on the average recording N9.9 trillion and N8.8 trillion in 2012 and 2014 respectively. Nigeria's external debts were virtually non existent till the early 80's when it grew to N17.3 billion. It maintained an upward swing and got to N716.9 billion in 1995. External debts in Nigeria came down briefly and started another climb in 1998 with N633.8 billion. The upward movement got to a peak in 2004 with N4.9 trillion. The Olusegun Obasanjo's administration negotiated and paid off the country's major lender (London Club and Paris Club) between 2005 and 2006. In 2007, the country's external debts were N438.9 billion. The trend commenced a gradual build up from N523.3 billion, to N689.3 billion and finally N1.63 billion for the years 2008, 2010 and 2014 respectively.

Figure 2



Sources: Based on Data from the Central Bank of Nigeria (CBN)

Government total expenditure in the country has merely been fluctuating without any definite pattern. From N12.1 billion in 1981 government expenditure came down gradually to reach a turning point N9.6 billion in 1985. The highest point on government expenditure is N20.3 billion in 1999 and the lowest point is N5.2 billion in 2014.

3.0 Theoretical Framework

Theoretically, the issue of deficit financing has been at the center of debate between the three main schools of economic thought: classical economists, Keynesian and the Ricardian Equivalence Hypothesis.

The classical economists suggest keeping public undertakings such as borrowing as minimum as possible due to crowding-out of private investment effect. In their view by borrowing public

authority accumulates resources for its own use leaving private sector with less. This phenomenon is popularly termed as crowding-out of private investment. According to them, as public expenditure is less productive than private expenditure, the increased output as a result of the loan-financed public expenditure does not fully offset the negative impact of the crowding-out of investment on output, thus reducing GDP (Njiforti and Muhammad, 2010).

The Keynesians see no harm in public borrowing in case of necessity. The Keynesian argument was based on the principle of the multiplier effect that explains how a change in the public expenditure generates a greater change in output. They however, were not unaware of the crowding-out effects of public borrowing (Alauddin, 2007). Keynes (1936) himself hinted at such effects in “The General Theory” by mentioning the multiplier limitation arising from possible adverse reactions on private investment, “confused” business psychology, and a tendency of the marginal propensity to consume to decline with rises in employment. However, their treatment of the crowding-out effect is quite different from that of the classicals. While the Keynesians consider the issue for ensuring the smooth and optimum performance of the borrowing activities of government, the classical economists, by contrast, raise the issue against undertaking any extent of public borrowing. It is noteworthy that in the two frameworks conclusions were drawn under different set of assumptions. For instance, in the classical approach, resources of an economy are assumed to be fully employed at all times and wages and prices are highly flexible. There is no room for any unemployment in the long run for the classical framework. The Keynesian paradigm, on the other hand, allows existence of unemployment in economy even in the long-run. The extent to which the assertion of one or the other school will be replicated in the real world depends upon how close the actual situations are to the background assumptions.

However, **the main contribution of Keynes on the issues of fiscal deficit has to do with the Twin-Deficit Theory.**

This theory focuses on the relationship between the budget deficit and the current account deficit. The current account is one of the components of the balance of payment account, which according to Bo Sodersten, is merely a way of listing receipts and payments in international transactions for a country (Jhingan, 2010). The current account also referred to as the balance of

According to the Keynesian school of thought, budget deficit has a significant impact on the current account deficit.

Keynes has argued that if the government increases its outlays through deficit financing, people will have more money on hand, feel wealthier, and therefore begin to spend more on consumption, leading swiftly to increased output and employment. In conventional Keynesian macro-economics, government bonds were commonly treated as net wealth to the private sector. Assuming that government spending is constant, an increase in government debt would therefore increase consumption. He therefore viewed budget deficit as expansionary.

The Mundell-fleming model suggests that an increase in the budget deficit will exert upward pressure on domestic interest rates, thereby causing capital inflows, and the exchange rate to appreciate, which in turn deteriorates the current account balance. The Keynesian approach argues that a rise in the budget deficit will increase domestic absorption via import expansion, causing a current account deficit.

The Ricardian Equivalence Hypothesis (REH) is third theoretical approach to the Fiscal Deficit Analysis. This hypothesis looks at two principal ways for increasing government expenditure, namely to tax current generations or to issue government debt in the form of government bonds, the interest and principal of which has to be paid later. The REH therefore, argues that, while tax financing and deficit financing are equal, deficit financing just serves as a means of postponing the inevitable tax given the fact that taxes will still be collected in future to repay the principal and interest rate on any bonds that have been issued (Muhammad, 2012). In essence, the hypothesis basically says that financing the deficit through debt or debt financing has no impact consumption, output, and employment because rational economic agents adjust their saving in expectation of future taxes that will be used to pay off the debt.

There have been some arguments in the literature as regards the justification of the proposition contained in the Ricardian Equivalence Hypothesis (REH).

First, the writings of Ricardo himself did not suggest his personal conviction in preference of his own REH (McCulloch 1888). The writings of Ricardo betrayed his preference for tax financing. He wrote about how to finance a war with annual expenditure of \$20 million and asked whether it makes a difference to finance the \$20 million via current taxes or to issue government bonds

$G - T = \text{Budget Deficit}$

GC = Central Bank claims on the government

GB = Commercial bank holding of government securities

GP = Non-bank public holding of government securities

K = Capital inflows through loans, grants, etc., including inflows through sale of government securities.

Thus any change in government expenditures must be financed by a change in tax revenue, government debt, or the monetary base. The budget deficits, however, cannot be financed by tax changes; hence recourse must be made to creation of money and the creation of public debt.

Since government securities are held in money and capital markets, they would constitute the basis for credit (money market) and stock exchange transactions (capital market).

$$GC + GB + GP = (G - T) - K$$

Basically, GC + GB + GP constitutes, credit and liquidity in money and capital markets hence:

Our Models for estimate for purposes of testing the hypotheses in the study would be equations 8 and 9 as follows:

$$FSD = f(\text{BUDD}, \text{GOVXP}, \text{DOMD}, \text{INTR}, \text{FDI}) \quad - \quad - \quad - \quad - \quad - \quad - \quad (9)$$

$$\text{PSCR} = f(\text{BUDD}, \text{GOVXP}, \text{DOMD}, \text{INTR}, \text{FDI}) \quad - \quad - \quad - \quad - \quad - \quad - \quad (10)$$

Where:

FSD : Financial Sector Development – Measured as $\text{PSCR}/\text{GDP} + \text{SMKTC}/\text{GDP}$ (defined in Jen-Te, Hwang et al, (2010))

PSCR : Private Sector Credit – Measured as PSCR/GDP

BUDD : Budget Deficit – Measured as BUDD/GDP

GOVXP : Government Expenditure – Measured as GOVXP/GDP

DOMD : Domestic Debt - Measured as DOMD/GDP

INTR : Interest Rate - Minimum Rediscount Rate / Monetary Policy Rate

FDI: Foreign Direct Investment - Measured as FDI/GDP

For the purpose of data testing, equations 8 and 9 can be written as follows:

$$FSD = \alpha_0 - \alpha_1 BUDD + \alpha_2 GOVXP + \alpha_3 DOMD - \alpha_4 INTR + \alpha_5 FDI + \mu_1 \quad - \quad - (11)$$

$$PSCR = \gamma_0 - \gamma_1 BUDD + \gamma_2 GOVXP + \gamma_3 DOMD - \gamma_4 INTR + \gamma_5 FDI + \mu_2 \quad - \quad - (12)$$

Equation (11) is designed to measure the relationship that exists between financial markets development and fiscal deficit and other independent variables. This is to see how those fiscal deficit variables influence financial markets in the economy. In line with a priori expectations, the expected signs of the coefficients are: $\alpha_1 < 0$; $\alpha_2 > 0$; $\alpha_3 > 0$; $\alpha_4 < 0$; $\alpha_5 > 0$. The sign (> 0) implies a positive relationship between financial markets and the coefficients of the fiscal deficit variables while (< 0) connotes a negative relationship. Equation 11 is designed to test our first hypothesis

Equation (12) is designed to estimate the responsiveness of Private Sector Credit to government fiscal deficit in the economy. In line with a priori expectations, the expected signs of the coefficients are: $\gamma_1 > 0$; $\gamma_2 > 0$; $\gamma_3 > 0$; $\gamma_4 < 0$; $\gamma_5 > 0$. The sign (> 0) implies a positive relationship between financial markets and the coefficients of the fiscal deficit variables while (< 0) connotes a negative relationship. Equation (12) is set to test our second hypothesis.

4.0 Estimation Strategy

The estimation technique for this study consist of four steps procedures. The first step is the unit root test which involves the determination of the stationarity property of the time series variables, using the Augmented Dickey-Fuller (ADF) (Dickey & Fuller, 1981). The second step is the Distributed Lag Model. This is necessary to determine the existence of long-run relationship between the variables of study. The third step is impact estimation, using Least Squares multiple regression method (including a constant term). The fourth step is the Granger Causality Test to determine the direction of causality between the financial development variables and fiscal deficit variables. Tests are run over the sample period (with quarterly data) 1981-2014. Data was collected from CBN Annual Statistics for 2014 Report.

4.0 Analysis of Result

4.1.1 Stationarity Test

From the ADF test statistics, the results in Table 1 show that FSD, PSCR, GOVXP, DOMD, INTR, FDI were integrated at order one, that is I(1) i.e. or they became stationary at first difference. But BUDD was integrated at order zero I(0). Comparing the variable integration levels with their (the ADF unit root test statistic) various probabilities, the test statistics show that the variables were statistically significant at, 5% and 10% critical values at level and first difference.

Table 1 – ADF Unit Root Test

Method	Statistic	Prob.*
ADF - Fisher Chi-square	28.2213	0.0133
ADF - Choi Z-stat	-2.76449	0.0029

Series	t-stat	Prob.	Order of Integration	Max Lag	Obs
FSD	-11.4632	0.00000	I(1)	1	135
PSCR	-11.4526	0.00000	I(1)	1	135
BUDD	-3.58114	0.04550	I(0)	1	135
DOMD	-11.4991	0.00000	I(1)	1	135
GOVXP	-8.57712	0.00000	I(1)	1	135
INTR	-11.4490	0.00000	I(1)	1	135
FDI	-8.08353	0.00000	I(1)	1	135

Test critical values:	1% level	-4.027463
	5% level	-3.44345
	10% level	-3.146455

It means that the Johansen cointegration test is not plausible on grounds of the varying levels of integration at orders I(0) and I(1). The adoption the ARDL bound testing exercise would constitute the logical method to examine the variables in the models for long-run equilibrium relationship. The arguments for using ARDL bound testing technique in this study are well documented. According to Pesaran and Shin (1995), unlike the conventional method which uses multiple equations system, ARDL uses reduced form equation and is therefore parsimonious. More importantly, Duasa (2007), points that ARDL is applicable irrespective of whether the regressors are purely I(0), purely I(1) or a mixture of both and this makes Johansen Cointegration

unsuitable for our case in which the order of integration of our variables is mixed. The existence or absence of cointegration is tested using the Wald F Statistic against Pesaran and Shin (1995) lower and upper bound critical values. Prior to the test, Optimum Lag Selection for the ARDL Model was carried out using the Akai and Schwaz Criteria and produced the following output.

4.1.2 ARDL Test

Table 2 shows results of the lag selection. Both criteria (Akaike and Schwaz) choose lag 2 and we used the lag in out Bound Testing exercise and Error Correction Model

Table 2 - ARDL Lag Selection

Lag	Akaike	Schwaz
0	4.645545	4.884354
1	4.537585	4.972224
2	4.465934*	4.768694*
3	4.593100	5.160925
4	4.682506	5.184845

* indicates the chosen lag order under each criteria.

The Wald Test calculated F Statistic is compared against the Pesaran and Shin (1995) lower bound [I(0)] and upper bound [I(1)] critical values at 1%, 5% and 10% level of significance. At all levels of significance, the F Statistic of 5.2347 is greater than the corresponding upper bounds critical values.

Table 3 - Bound Test for Cointegration

Test Statistic	Value	K	Level of Significance	Bound Critical Values	
				I(0)	I(1)
	7.2347	5	1%	3.93	5.23
F - Statistic	7.2347	5	5%	3.12	4.25
	7.2347	5	10%	2.75	3.79

This implies that the null hypothesis of no cointegration cannot be accepted at all levels therefore signifying that there exist a long run equilibrium relationship running from Budget Deficit, Domestic Debt, Government Expenditure, Interest Rate and Foreign Direct Investment. The nature of the long run association was established by estimating the error correction of the

ARDL model. Specifically we did this to determine the speed of convergence of the system back to equilibrium.

4.1.3 Error Correction Model

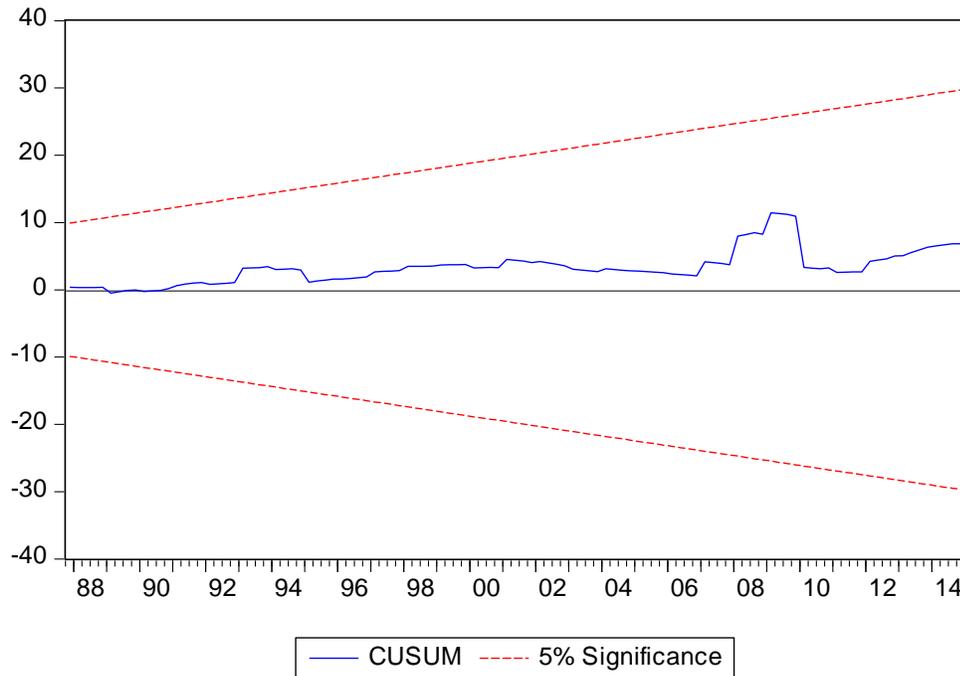
Table 4 shows the error correction model results. The long run dynamics in the model is shown by the error correction term ECT (-1), which measures the convergence of the model to equilibrium. The error correction term is negative (-0.306387), less than zero and statistically significant with t-statistic (-2.773687) and probability value (0.0064).

Table 4 - Error Correction Model result (Dependent Variable is FSD)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.174569	0.408089	-0.427771	0.6696
@TREND	0.003706	0.005225	0.709263	0.4796
D(BUDD(-1))	0.024581	0.28924	0.084984	0.9324
D(BUDD(-2))	0.024638	0.289246	0.085181	0.9323
D(DOMD(-1))	0.065075	0.151107	0.430653	0.6675
D(DOMD(-2))	0.065088	0.151109	0.430735	0.6674
D(GOVXP(-1))	0.059287	0.175155	0.338485	0.7356
D(GOVXP(-2))	0.059454	0.175176	0.339398	0.7349
D(INTR(-1))	-0.220721	0.289086	-0.763512	0.4467
D(INTR(-2))	-0.220513	0.289072	-0.762828	0.4471
D(FDI(-1))	-0.019706	0.175158	-0.112502	0.9106
D(FDI(-2))	-0.019743	0.175158	-0.112714	0.9104
D(FSD(-1))	0.166127	0.258228	0.643333	0.5213
D(FSD(-2))	0.165838	0.258225	0.642225	0.522
ECT(-1)	-0.306387	0.110462	-2.773687	0.0064
R2	0.147891			
Adjusted R2	0.123464			
D. W Test	2.068143			

This shows evidence of long run causality from the explanatory variables to the dependent variable. The coefficient of -0.306387 shows the level of convergence to equilibrium. If Private Sector Credit is in disequilibrium, the system converges back to equilibrium at a speed of 30.6%. The value of Durbin Watson (2.068143) shows that model does not suffer from autocorrelation. The stability of the model can be observed from the test on the recursive estimates of the model shown in

Figure 1. - CUSUM Test



Further diagnostic tests were conducted on the error correction model to detect serial correlation and stability problems using the Breusch-Godfrey Serial Correlation Test (Table 5) and the Recursive (CUSUM) Estimates (Figure 1) respectively.

Table 5 - Breusch-Godfrey Serial Correlation Test

Dependent Variable: Residuals

Breusch-Godfrey Serial Correlation Test			
Test Statistic	Value	Probability	Decision
F-Statistic	2.165892	0.1193	Do not Reject H_0

The probability value of 0.1193 is greater than 0.05 hence we cannot reject H_0 that there is no serial correlation on the error correction model. Therefore the model is free of serial correlation. Stability test results are shown on Fig.1 on CUSUM Test. The CUSUM Estimates line is between the 5% Significance Level implying that the error correction model is stable. After establishing that long run association do exists among the variables in the model and determining the speed of adjustment to equilibrium, we then proceeded to run the OLS of the model and obtained the following results.

4.1.4 Multiple Regression Model

A view of the result in table 6 shows that all the explanatory variables in the model are significant in explaining the trend in the dependent variable – Financial Sector Development (FSD). In addition, FSD displayed positive relationship with BUDD, GOVXP and FDI while DOMD and INTR exhibited negative relationship with FSD. The R-squared and Adjusted R-squared did not indicate good fit. From the values of R-Squared, about of the variation in FSD is explained by the variation in the independent variables. The F Statistic (26.82105) is greater than 5 and the F probability of 0.0000 means that collectively, the explanatory variables have been statistically significant in explaining the trend in financial sector development (FSD) over the period of study.

Table 6 - OLS Long Run Model Results

Dependent Variable: FSD				
Method: Least Squares				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	49.23972	5.491762	8.966105	0.0000
BUDD	1.992187	0.78683	2.531916	0.0125
DOMD	-1.462152	0.291745	-5.011752	0.0000
GOVXP	1.970398	0.473258	4.163479	0.0001
FDI	2.100201	0.596336	3.52184	0.0006
INTR	-1.924666	0.325932	-5.905112	0.0000
R-squared	0.507772	Mean dependent var		25.29413
Adjusted R-squared	0.48884	S.D. dependent var		17.56676
S.E. of regression	12.55944	Akaike info criterion		7.941936
Sum squared resid	20506.13	Schwarz criterion		8.070436
Log likelihood	-534.0517	Hannan-Quinn criter.		7.994155
F-statistic	26.82105	Durbin-Watson stat		2.09868
Prob(F-statistic)	0.00000			

Substituted Coefficients:

=====

$$\text{FSD} = 49.2397199984 + 1.99218744269*\text{BUDD} - 1.46215164333*\text{DOMD} + 1.97039811858*\text{GOVXP} + 2.10020084808*\text{FDI} - 1.924665649*\text{INTR}$$

Further analysis of the estimated result shows that if Budget Deficit (BUDD), Government Expenditure (GOVXP) and Foreign Direct Investment (FDI) are increased by 1%, Financial Sector Development (FSD) will increase by 1.99%, 1.97%, and 2.1% respectively. The result also shows that if Domestic Debt (DOMD) and Interest Rate (INTR) and are increased by 1%, FSD will decrease by 1.4%, and 1.9% respectively. The F-Statistic probability result shows that

An examination of the relationship between Financial Sector Development (FSD) with Government Expenditure (GOVXP) and Foreign Direct Investment (FDI) falls in line with our apriori expectations and confirm that government action develops the market. However, Budget Deficit (BUDD) has a direct relationship with Financial Sector Development. This implies that deficit budget financing by government has a depressing overall effect on the country's domestic financial market.

This position is reinforced when we look at the results of the test of our second hypothesis. The result in table 7 tests the crowding-out hypothesis. All explanatory variables in the model are significant in explaining the variation in Private Sector Credit (PSCR) except Budget Deficit (BUDD).

Table 7 - OLS Long Run Model Results

Dependent Variable: PSCR				
Method: Least Squares				
Included observations:136				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	23.12625	2.286286	10.11521	0.0000
BUDD	-0.145396	0.327567	-0.443868	0.6579
DOMD	-0.528915	0.121457	-4.35476	0.0000
GOVXP	0.41446	0.197023	2.103614	0.0373
INTR	-0.81467	0.135689	-6.00393	0.0000
FDI	0.932215	0.248262	3.754966	0.0003
R-squared	0.365498	Mean dependent var	12.63556	
Adjusted R-squared	0.341094	S.D. dependent var	6.441354	
S.E. of regression	5.228642	Akaike info criterion	6.189295	
Sum squared resid	3554.031	Schwarz criterion	6.317795	
Log likelihood	-414.8721	Hannan-Quinn criter.	6.241514	
F-statistic	14.97701	Durbin-Watson stat	2.29945	
Prob(F-statistic)	0.0000			

Substituted Coefficients:

$$\text{PSCR} = -0.145396412396\text{BUDD} - 0.528915005012*\text{DOMD} + 0.414459860642*\text{GOVXP} - 0.814669695707*\text{INTR} + 0.932214677424*\text{FDI} + 23.126254025$$

The analysis shows that 1% change in Budget Deficit (BUDD), Domestic Debt (DOMD) and Interest Rate (INTR) would be accompanied by 0.15%, 0.53% and 0.82% (respectively) change in Private Sector Credit (PSCR) in the inverse direction. Similarly, a 1% change in Government

Expenditure (GOVXP) and Foreign Direct Investment (FDI) would induce 0.41% and 0.93% respective change in Private Sector Credit. It means that Domestic Debt crowds-out Private Sector Credit (**Samah Shetta and Ahmed Kamaly, (2014)**)

4.1.5 Granger Causality Test

The result of our Granger Causality Test is contained in our appendix1. The important findings in the test are: i) Budget Deficit (BUDD) granger cause Private Sector Credit (PSCR); ii) Domestic Debt (DOMD) granger cause PSCR and Private Sector Credit (PSCR) granger cause Interest Rate (INTR). This position confirms a unidirectional causality running from fiscal deficit to financial market development.

5.0 Conclusion

The main objective of this study is to empirically examine the impact of fiscal deficits on financial market development. Using Bound Testing approach to Cointegration and Error Correction Model developed within the context of the Auto-Regressive-Distributed-Lag (ARDL) framework developed by Pesaran and Shin (1995, 1999) , the study investigated whether a long-run equilibrium relationship exist between financial development and fiscal deficits in Nigeria. In addition, we examined the strength of the long run association and convergence to equilibrium. We then adopted the multiple regression analysis to establish the long-run responsiveness of financial market development to fiscal deficit variables.

The results show that there is long run association running from Fiscal deficits to financial market development. More specifically, budget deficit, domestic debt and government expenditure significantly impacted on the development of the Nigerian financial markets. Besides, the long-run budget deficit impact did not stimulate (improve) financial development as expected. This is in line with the study of Ball and Mankiw (1995). It means that persistent budget deficit ultimately depressed financial development.

Another observation in the study from the granger causality test is that short-run causality ran from fiscal deficit to financial market development variables. This position further reinforced our earlier position that fiscal deficit impacted on the development of the country's financial markets.

To test the crowding-out hypothesis, we examine the impact of domestic debt on private credit. The results showed that domestic debt significantly impacted negatively on Private sector credit. This is important evidence that domestic debt crowds out private sector credit. This position is

supported by Shetta and Kamaly (2014). This situation portends a note of caution for the Nigerian government that wishes to stimulate the private sector to play the leading role in the country's enterprise and development process. Furthermore, it clearly stimulates the debate on which sector would better utilize the available financial market loan facilities in favour of the country's long-term development objective: is it private sector or public sector?

The findings indicate that fiscal policy in Nigeria has a strong role in macroeconomic stabilization. The government should reduce the massive and persistent budget deficit. Fiscal policies should play a more neutral role in the effort to stimulate private sector entrepreneurship and investment in the economy.

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Appendix 1

Pairwise Granger Causality Tests

Date: 08/16/15 Time: 18:10

Sample: 1981Q1 2014Q4

Lags: 2

Null Hypothesis:	Obs	F-Statistic	Prob.
PSCR does not Granger Cause FSD	134	3.06970	0.0498
FSD does not Granger Cause PSCR		11.4084	3.E-05
BUDD does not Granger Cause FSD	134	1.91831	0.1510
FSD does not Granger Cause BUDD		1.01389	0.3657
DOMD does not Granger Cause FSD	134	2.04227	0.1339
FSD does not Granger Cause DOMD		1.70705	0.1855
GOVXP does not Granger Cause FSD	134	0.40579	0.6673
FSD does not Granger Cause GOVXP		0.46842	0.6271
INTR does not Granger Cause FSD	134	0.11489	0.8916
FSD does not Granger Cause INTR		2.21733	0.1130
FDI does not Granger Cause FSD	134	0.16941	0.8444
FSD does not Granger Cause FDI		0.03747	0.9632

BUDD does not Granger Cause PSCR PSCR does not Granger Cause BUDD	134	3.27785 0.60230	0.0409 0.5491
DOMD does not Granger Cause PSCR PSCR does not Granger Cause DOMD	134	2.97794 1.48692	0.0414 0.2299
GOVXP does not Granger Cause PSCR PSCR does not Granger Cause GOVXP	134	0.45449 2.22206	0.6358 0.1125
INTR does not Granger Cause PSCR PSCR does not Granger Cause INTR	134	0.33902 2.66359	0.7131 0.0435
FDI does not Granger Cause PSCR PSCR does not Granger Cause FDI	134	0.67658 0.26707	0.5101 0.7660
DOMD does not Granger Cause BUDD BUDD does not Granger Cause DOMD	134	0.16816 1.41152	0.8454 0.2475
GOVXP does not Granger Cause BUDD BUDD does not Granger Cause GOVXP	134	0.02632 0.16903	0.9740 0.8447
INTR does not Granger Cause BUDD BUDD does not Granger Cause INTR	134	0.14701 0.19018	0.8634 0.8270
FDI does not Granger Cause BUDD BUDD does not Granger Cause FDI	134	0.17803 0.07146	0.8371 0.9311
GOVXP does not Granger Cause DOMD DOMD does not Granger Cause GOVXP	134	0.11288 0.03726	0.8934 0.9634
INTR does not Granger Cause DOMD DOMD does not Granger Cause INTR	134	0.92794 0.13427	0.3980 0.8745
FDI does not Granger Cause DOMD DOMD does not Granger Cause FDI	134	0.50241 0.43012	0.6063 0.6514
INTR does not Granger Cause GOVXP GOVXP does not Granger Cause INTR	134	0.54367 1.26374	0.5819 0.2861
FDI does not Granger Cause GOVXP GOVXP does not Granger Cause FDI	134	0.01995 0.47586	0.9802 0.6224
FDI does not Granger Cause INTR INTR does not Granger Cause FDI	134	0.62245 3.61206	0.5382 0.0298