ACCESSING LONG-TERM FUNDS FROM THE CAPITAL MARKET FOR PUBLIC SECTOR PROJECTS IN NIGERIA

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Abstract

This paper discusses the various capital market instruments, which the three tiers of government in Nigeria employ to augment the financing of public sector projects. Such instruments include the Federal Government Development Stocks, Treasury Bonds and Municipals. The major finding of the paper is that the use of these instruments by the various governments in Nigeria helps to free-up monthly allocations from the Federation Account for other pressing needs, and also instill financial prudence and accountability into public sector managers, as funds sourced from the capital market are usually project-tied.

Introduction

Between the 16^{th} and the 18^{lh} centuries, nationalism and consolidation held sway; small provinces joined together to form larger countries. Consolidation implied the unification of laws of contract, the establishment of common currency and system of tariffs, and a coordinated infrastructure (i.e., communications, water supply, etc). That period was also accompanied by mercantilism, that is, the state regulation of production, commerce and trade. In contrast, the 18^{th} and 19^{th} centuries saw the removal of many mercantilist regulations.

The world depression of the late 1920s, however, brought many changes in international relations and increased government intervention into domestic economic relations. The post-war period of the 1940s onwards marked a significant departure from the liberal economic policies of previous ages. Governments now intervene in economic affairs on an unprecedented scale unknown and unthought-of in earlier periods. Hence, virtually all economies of the world today are ‘mixed economies’ with large proportion of their gross national products (GNPs) originating in the public sector. Correspondingly, a significant share of their GNPs is collected in taxations in order to finance these public outputs. Interestingly, these shares have been growing over time as governments now provide a variety of goods and services that cut across all the sectors of the economy.

One may wish to ask, why is this the case? The answer seems not far-fetched! The outputs of the goods and services of the economy and the set of prices for these outputs were determined competitively in the market place in accordance with consumers’ preferences and incomes. The market outcome was assumed to be Pareto-efficient in the sense that, given the set of factor prices, a reallocation of factor inputs could not increase total output and, given the initial distribution of incomes, it was not possible, by reallocating final output between individuals, to make one person better off without making another worse off. These results depended upon the usual assumptions of perfectly competitive markets. Thus, it could be reasoned that government intervention in economic and social affairs emanated from market failure - situations in which the conditions necessary to achieve the market efficient solution fail to exist or are contravened in one way or another (Odufalu, 1977).

Given the presence of market failure, one possible role for government is to intervene in the allocative function of the market and thus correct the market failure or introduce policies that would cushion its effects. In this sense, it could be inferred that the days of the “invisible hand” of government in correcting the economy are over, while the days of the “mighty and visible hand” of the government to regulate the economy have come to stay with us. In the new dispensation, government can establish projects in addition to its traditional function of defending the territorial integrity of the country, providing security over life and property, and administering justice. A public project is an undertaking established by government or its agency to produce those goods or services, which the private sector players are not willing or able to produce either because of its capitalintensiveness or its inability to pay back its initial capital outlay within a reasonably short period.

The thrust of this paper is to discuss the various capital market instruments, which the three tiers of government in Nigeria use to finance public sector projects. The remainder of the paper is organized as follows: section 2 reviews the literature; section 3 explores the capital market instruments available to the governments in Nigeria; section 4 heralds the problems of public sector projects in Nigeria; while the summary and concluding remarks of the paper are contained in section 5

Review of Related Literature

Various definitions have been accorded "project" in the extant literature. For example, King, Jr. (1967) defines project as "a proposal for capital investment to develop facilities to provide goods and services. The Project Management Body of Knowledge (PMBOK, 1996), defines project as "... a temporary endeavour undertaken to create a unique product or service. ***Temporary*** means that every project has a definite end. ***Unique*** means that the product or service is different in some distinguishing way from all similar products or services". The United Nations (1958), defines a project as "the compilation of data, which will enable an appraisal to be made of the economic advantages and disadvantages attendant upon the allocation of a country's resources to the production of specific goods and services. The Webster's New Collegiate Dictionary defines the word "project as "a specific plan or design; a scheme; an idea; a planned undertaking". Turner (1963), defines project as "... an endeavour in which human (or machines), materials and financial resources are organized in a novel way to undertake a unique scope of work, of a given specification, within the constraints of costs and time, so as to deliver beneficial change defined by quantitative and qualitative objectives". Bruce (1982), defines a project as "a discrete package of investment, inputs and activities designed to remove or alleviate various development constraints in order to achieve one or more outputs/benefits in terms of increasing productivity and improving the quality of life of a group of target beneficiaries over a given time-span, that is, it is time-bound". Baum (1977). defines project as "a discrete package of investment policies (institutional and other actions) designed to achieve a specified development objective or a set of objectives within a designated period". Little and Mirles (1974), on their part, define project as "any scheme or part of a scheme for investing resources, which can reasonably be evaluated and analyzed as an independent unit".

From the foregoing definitions, a project can be conceptualized as the beneficial change, which uses the project management techniques to plan and control the scope of work in order to produce and deliver a good or service designed to satisfy consumers' and other stakeholders' aims and expectations.

We may need to make haste to point out at this juncture that no matter how laudable a given project may seem, if its funding or financing is inadequate, it is likely to make nonsense of itself and meaningless or worthless to its intended beneficiaries. Hence, finance can be considered as the outstanding life-blood running through the arteries of project execution. The capital market represents one of the major funding sources for public sector projects in Nigeria.

Capital Market Instruments and Public Sector Projects in Nigeria

Conventionally, a capital market represents a network of financial institutions and facilities that interact to mobilize and allocate long-term savings in the economy (Odoko, et al 2004). Such savings are exchanged for financial assets issued by borrowers or traded by holders of outstanding eligible instruments. Thus, the capital market provides services that are essential to a modem economy by contributing to capital formation through financial intermediation, financial advisory services and managerial skills development. Additionally it facilitates portfolio diversification that allows savers to maximize returns on their assets and reduce risks. Consequently, an efficient capital market optimizes the amount of savings that finances investment at any level of saving.

In Nigeria, the capital market provides funds to industries and governments to meet their long-term capital requirements for fixed investments such as buildings, plants and other public utilities and infrastructure. Until relatively recently, the capital market in Nigeria has been characterized by low contributions to the level of capital mobilization and investment as demonstrated by the low market capitalization over the years. For example, the value of stock which stood at only N57.7 million in 2001 jumped to N225.8 million in 2004, and further to N242.9 million in 2005. See table 1 for a clearer picture of the transaction at the Nigerian Stock Exchange for a period covering 2001 to 2005.

Table 1: Transactions at The Nigerian Stock Exchange, 2001 - 2005

Item	2001	2002	2003	2004	2005
Volume of stock ('000)	5,930,186.0	6,614,048.0	13,304,211.9	19,210,000.0	26,672,765.7
Number of Deals	426,163	451,850	621,717	973,526	1,021,966.0
Value of Stocks (Million)	57,683.8	59,406.7	120,402.6	225,820.0	262,935.8
Market Capitalization (million)	648,449.8	747,599.8	1,324,898.0	1,925,937.5	2,900,062.1
Index (1984 = 0)	10,965.0	12,137.7	20,128.9	23,844.5	24,085.8

Source: The Nigeria Stock Exchange.

This sub-section examines the various capital market instruments which the three-tiers of government in Nigeria use to finance public sector projects. Specifically, it undertakes an analysis of the performance of the bonds market within the capital market wherein the different levels of government in Nigeria commonly access long term capital for their project implementation.

Bond (Debt) Market in Nigeria

The need to augment internally generated revenues has prompted governments to look outwards for additional sources of funding public sector projects in order to close their resource gaps. In the circumstance, the bond market offers itself as a good option especially as the banks are not the ideal sources for long term funds. A bond is a debt obligation or "IOU", representing a promise by the borrower to pay the interest elements periodically and the principal at some specified future date. It carries either a fixed or floating coupon rate with a maturity period ranging from 1 to 30 years. In effect, a bond constitutes a loan by the bondholder to the bond issuer. Bond issues secured by specific pledge against the issuer's assets are called "debenture bonds". Bond issues available to the Federal Government of Nigeria include: The Federal Government Development Stocks (FGDS) and the Federal Government Treasury Bonds (FGTBs).

The Federal Government Development Stocks (FGDS)

These are stocks issued for development purposes and are project-tied. They are gilt-edged stocks with fixed interest rates and maturity dates. The FGDS are frequently issued in tranches and the interest paid semi-annually. The history of the Nigerian Bonds Market dates back to 1946, when the Federal Government issued a N600,000.00(3 ***'A*** %) Federal Government Stock. The primary objective of the stock was to promote development finance for all tiers of government while its tenor was between 7 and 25 years.

At the initial stage of the Nigerian capital market, the FGDS dominated the traded securities both in volume and value, accounting for 17 out of the 19 securities traded on the Nigerian Stock Exchange. This dominance was largely attributable to the attractive interest rates of between 5 and 12.5 per cent. The share of government stocks in the capital market continued its dominance until 1979/80 when it firmed at N512.3 million or 97.9 per cent of total trading activities on the market (Odoko, et al, 2004). However, the share of government stocks in the total trading activities on the Nigerian Stock Exchange has been declining drastically and persistently until it settled at an all time low 0.01 per cent in 1998. This scenario could be ascribed to Federal Government's recourse to other sources of financing outside the capital market as well as the unattractive returns and volatile macroeconomic indicators, which have characterized the Nigerian economy since the mid-1980s. Consolidation of holdings of FGDS figures for 1990 to 2003 is shown in Table 2.

Table 2: Nigeria: Holdings of Development Stocks, 1990 — 2003

Years	Banks (N million)	Others (N million)	Total (N Million)
1990	163.5	8,193.2	8,356.7
1991	39.9	8,163.1	8,203.0
1992	33.1	7,911.9	7,945.0
1993	159.0	7,457.8	7,716.8
1994		7,338.0	7,338.0
1995	14.7	7,155.3	7,160.0
1996	471.1	2,908.3	3,379.4
1997	14.0	2,826.0	2,840.0
1998	170.8	2,452.3	2,623.1
1999	4.0	2,466.0	2,470.0
2000		2,110.0	2,110.0
2001		2,110.0	2,110.0
2002	2,692.7	9.194.0	11.706.7
2003	32,504.9		32,504.9

Source: The Nigerian Stock Exchange,

The Federal Government Treasury Bonds (FGTBs)

The Central Bank of Nigeria introduced the FGTBs in 1996 with the objective of minimizing its debt service obligations. The bonds are non-tradable with coupon rates of 5 to 10 per cent and tenor of 10 to 25 years. The bonds grew from the conversion of Treasury Bills that had been used to cover the Ways and Means Advances granted the Federal Government by the Central Bank of Nigeria at end-December every year. Since their introduction on 16lh March, 1996, Treasury Bonds have become an attractive instrument of financing Federal Government Projects. The value of the instruments has grown tremendously; for example, the value of Treasury Bonds outstanding was N430.6 billion at end-December, 2003. (Central Bank of Nigeria, 2004). This Figure represented 42.3 per cent of Federal Government total domestic debt.

State and Local Government Bonds

Other tiers of government in Nigeria (i.e., State and Local Governments) also source funds from the capital market to execute some of their projects, which are considered to have direct and indirect benefits on their respective areas of jurisdiction. The bonds included in this category are commonly referred to as ***municipal securities.*** State and Local Governments and/or their agencies such as: Town Planning & Property Development Authority, Education Boards, Water Boards, etc formally issue municipal securities. In issuing these securities, these tiers of government distinguish between short term and long-term municipals. Here, we concern ourselves with long-term municipals.

Long-term municipals are used primarily to finance capital projects, which are expected to yield benefits over long periods so that future taxes that should cover the interest and principal payments would be transferred to those who benefit. Generally, long-term municipals are categorized into general obligation bonds (GOBs) and revenue bonds (RBs). Interest and principal payments on GOBs are backed by the full faith, credit and taxing power of the issuer. In fact, this backing represents the strongest commitment a government can make in support of its debt. At the extreme, governments promise to raise taxes, attach real property, and issue new debt to meet promised debt service payments.

On the other hand, revenue bonds (RBs) are issued to finance projects whose revenues are the primary source of repayment. An example is a bond issued to finance the development of a University dormitory that is supported by the fees payable by students. The label "fees payment" can identify the revenue source of this hypothetical bond. RBs exhibit greater default risk than do GOBs.

The State and Local Governments that have issued municipal securities in Nigeria are shown in

Table 3.

Year	Government	Amount and Project
1978	Bendel State Government	N50 million
1987	Ogun State Government	N30 million revenue bonds for Abeokuta Water Scheme
1987	Lagos State Government	J430 million revenue bonds for Lekki Peninsula
1989	Kaduna State Government	N50 million revenue bonds for Ginger Processing Plant)
1990	Lagos State Government	N90 million revenue bonds for Lekki Peninsula
1992	Lagos Island Local Government	W100 million revenue bonds for the .construction of a Shopping Centre
2001	Edo State Government	£J1 billion revenue bonds for Ogba Housing Estate

Source: Central Bank of Nigeria.

Obviously, certain advantages accrue to those State and local Governments that issue municipal securities. Such advantages include, among others, the following:

i. freeing-up monthly allocations from the Federation Account for other pressing needs;
ii. instilling financial prudence and accountability into public sector managers as funds sourced from municipals are usually tied to specific projects and hence repayment is well monitored by trustees and regulatory authorities;
iii. enhancing public sector savings as it is definitely a cheaper source of capital through cheaper costs; and
iv. helping to provide more goods and services to economic agents and at the same time generating more job opportunities thereby reducing unemployment rate

Problems and Prospects of Public Sector Projects in Nigeria

There were high expectations that the policy measures initiated in the National Development Plans and the Structural Adjustment Programme including the Rolling Plans would lead to rapid industrial development, export diversification and extensive transformation of the Nigerian economy. In spite of the huge resources committed to the pursuit of these goals, very little has been achieved. The following are some of the major constraints that could be attributed to the rather low performance of most public sector enterprises in Nigeria:

i. **Deficient Infrastructural Facilities**

The activities of public sector enterprises in Nigeria are constrained by frequent disruptions in electric power and water supply and poor roads and other transportation problems. The adverse effects of the infrastructural facilities on the activities of these projects have thus necessitated private provisioning of such facilities by these projects. This has inevitably resulted in escalating production costs and uncompetitive prices of the goods and services provided by these enterprises in both the domestic and international markets;

ii. **Bureaucratic Controls and Poor Funding of Investments**

The mining sub-sector of the Nigerian economy has been plagued by various problems, which have tended to undermine its optimal development over the years. For example, Power Holding Company of Nigeria (PHCN), Ajaokuta and Aladja Steel Complexes and the Nigerian National Petroleum Corporation (NNPC) are controlled by their respective Supervisory Ministries. Consequently, these public sector enterprises lack autonomy, as a result of which decision-making is often bureaucratic and unnecessarily delayed. Therefore, the operations of public sector enterprises are characterized by inefficiency, which manifest itself in low capacity utilization, power destruction and marketing of final outputs, and frequent delays in the payment of cash call or counterpart funds to joint

iii. **Political Instability**

Political instability has been a major problem for most public sector enterprises in Nigeria. Since independence, several regimes (both civilian and military) have come on board rather frequently. These frequent changes in government have led to unnecessary cash denials for public sector enterprises or outright phase out. For example, the two steel complexes in Nigeria were completely abandoned for over 25 years before construction works commenced again few years ago. This is in spite of the enormous role these enterprises are expected to play in Nigeria's industrialization process.

iv. **Low Level of Technology**

This is perhaps the greatest constraint militating against the productivity of public sector enterprises in Nigeria, as developments in technology and innovation are the primary forces of industrialization today. New processes and procedures of doing business, driven by automation, have revolutionalized the industry and its productivity in industrialization.

Unfortunately, many Nigerian public sector enterprises have not been able to acquire the modem plants and machines that would make a significant impact on their processes. Most of them especially the NNPC, PHCN and the Steel Complexes are producing with machines and equipment procured in the 1960s and 1970s, which experience frequent breakdowns and low rates of capacity utilization. The result of all this is an excessive dependence on imports and very low local value- added inputs.

The constraints outlined above tend tohaveserved tolimit government'saccess to external funds from the capital market for its projects.Added to these is the rather low quoted rates of government securities in the capital market.

Prospects for Public Sector Enterprises in Nigeria

Nigeria's vast natural resources, including oil, gas and solid minerals coupled with the enormous potentials in electric power resources; a large human population forming a very big market; and substantial idle capacity in all industrial sectors, indicate that there are great potentials for growth in output, value added, export capacity and employment opportunities for public sector projects. Higher and coordinated investments in gas, oil and solid minerals sub-sectors will boost local production of raw materials and intermediate goods, which will enhance the capacity utilization rates of public sector enterprises as well as generate export earnings that will even surpass current revenue from crude oil export. The rehabilitation and expansion of the power system through private sector participation to enable it provide uninterrupted electricity will boost industrial and commercial operations, conserve the foreign exchange currently used in importing generators. Increased mining operations, and enhanced electricity supply and the privatization of the core industrial projects will have salutary effects on the industrial sector and ultimately lead to higher national income, through increased value added, greater export capacity and the generation of more employment opportunities.

Summary, Recommendations and Conclusion

Summary

In this paper, an attempt has been made to identify and discuss the various capital market instruments, which the government uses to source funds for its public sector projects in Nigeria. The paper started by revealing that the period from the sixteenth to the eighteenth century was a time of nationalism and consolidation when small provinces came together as a single country by unifying their laws of contract, establishing common currency and system of tariffs and a coordinated infrastructure. By the eighteenth and nineteenth century, however, liberalism was embraced by nations and this saw many mercantilist regulations associated with nationalism and consolidation. The world depression of the late 1920s engendered international relations and increased intervention into domestic economic relations. Thus, governments have been intervening in economic affairs by going ahead to participate in the production of goods and services to enhance the overall welfare of the society. This marked a departure from the days of classicals' "invisible hand" of the government and paved the way for the "mighty and visible" hand of government at regulating the economy and, hence, public sector projects.

The next substantive section of the paper conducted an in-depth survey of the literature with the singular objective of examining the various definitions accorded the term "project". The outcome of that survey indicated that no one universally accepted definition for the term "project" exists in the extant literature despite the numerous and extensive theoretical and empirical studies carried out by experts. However, we worked with the definition put forward by Bruce (1982) that a project is a discrete package of investment, inputs and activities designed to remove or alleviate various development constraints in order to achieve one or more outputs/benefits in terms of increasing productivity and improving the quality of life of a group of target beneficiaries over a given time- span, that is, it time-bound".

The bond (debt) market arm of the Nigerian capital market serves as the window through which the three tiers of government source funds for public sector projects in Nigeria. This arm of the market offers itself as a good option especially as the banks are usually not the right source for long term funds. The Federal Government of Nigeria uses Development Stocks and Treasury Bonds to source funds for their projects while the State and Local Governments use municipals to source funds for their projects in the capital market.

Some of the problems or constraints militating against the optimal performance of public sector projects in Nigeria include low level of technology, deficient infrastructure, bureaucratic controls and poor funding of investments, and political instability.

Policy Recommendations

For the various layers of government in Nigeria to source long term funds for their projects from the capital market, they need to formulate appropriate industrial strategies, which must be anchored on macroeconomic stability, export promotion, fortification of infrastructural facilities, improved technology and privatization and commercialization.

Macroeconomic Stability

Macroeconomic stability is desirable because it shapes the overall investment climate and determines the level of confidence investors have in an economy. Stability aids planning and enables the business community forecast, reasonably, future returns on current investment. Stability therefore promotes capital market activities, which is a ***sine qua non*** for long-term capital intermediation. In particular, the achievement of a sustainable macroeconomic stability requires the re-establishment of price stability. Maintenance of a market-based stable foreign exchange rate policy, adoption of market determined interest rate through the application of indirect tools of monetary policy, fiscal prudence, transparency and accountability; restoration of law and order to protect lives and property, that is, political stability and good governance.

Export Orientation

The changing roles for public sector enterprises must in the first instance be import substitution and ultimately export orientation. Experience from the South East Asian countries has shown that export orientation of local enterprises brings about international competitiveness, product efficiency and an increasing market for domestically produced goods and services.

Privatization and Commercialization

A proper rationalization of the role of government in the development process at this point in time is essential. Most public investments in the productive sector in Nigeria are public monopolies, while others complete with rather than complement private sector investment. This has led to inefficiency on the part of public sector projects. It is strongly recommended, therefore, that government should not make new investments in commercial and industrial projects in which the private sector has proved to be more efficient. In particular, government should gradually remove all monopolistic hindrances and divest its equity holdings in the oil and gas projects, steel plants and the fertilizer company through privatization. This could be done over a period of ten to fifteen years. Such commercial enterprises as electricity and water supplies and railway services should be partially privatized with the private sector providing the much needed competition, which will induce efficiency.

Rehabilitation of Basic Infrastructure

Having substantially reduced involvement in business enterprises, government should then concentrate on its primary responsibilities. These include adequate prevision of social and economic infrastructure such as education, health, electricity, water and transportation system. It will also devote more resources to the maintenance of law and order, focusing on protecting lives and property. Adequate and efficient infrastructures as well as an effective administration of law and order are necessary conditions for promoting investments and industrialization.

Conclusion

The major factors that influence government's access to long-term funds in the capital market are macrocosmic stability, export orientation, rehabilitation of ailing public infrastructure, privatization/"and commercialization, and political stability. When these factors are properly laid on the economic foundations of a nation, activities in the capital market will increase and hence will become efficient in its intermediary role as the allocator of long-term savings within the economy. If all Nigeria's ongoing reform programmes encapsulated in the National Economic Empowerment and Development Strategy (NEEDS) are efficiently prosecuted, the nation's capital market will become deep, broad, efficient and resilient, such that it can provide the required long-term capital for both public and private investments.

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