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EFFECT OF EXTERNAL DEBT ON ECONOMIC GROWTH IN NIGERIA (1981-2024)

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Abstract

This study examines the effect of external debt on Nigeria's economic growth from 1981 to 2024. It evaluates the effects of external debt stock and debt servicing on Gross Domestic Product (GDP), while considering inflation, exchange rate, interest rate, and government expenditure. Data were obtained from the CBN Statistical Bulletin and Debt Management Office reports. The study employed the Augmented Dickey-Fuller test, Engle-Granger cointegration test, and Ordinary Least Squares method. Findings indicate that rising external debt stock negatively affects economic growth, while external debt servicing does not significantly impair growth. The study recommends investing borrowed funds in productive sectors, expanding Nigeria's export base, and adopting favourable debt repayment arrangements to improve debt sustainability.

Keywords: External Debt, Economic Growth, Gross Domestic Product, ADF.

Introduction

It is generally expected that developing countries, facing a scarcity of capital, will acquire external debt to supplement domestic saving (Malik et al, 2010; Aluko and Arowolo, 2010). Besides, external borrowing is preferable to domestic debt because the interest rates charged by international financial institutions like International Monetary Funds (IMF) is about half to the one charged in the domestic market (Pascal, 2010). However, whether or not external debt would be beneficial to the borrowing nation depends on whether the borrowed money is used in the productive segments of the economy or for consumption. Adepoju et al (2007) stated that debt financed investment need to be productive and well managed enough to earn a rate of return higher than the cost of debt servicing The main lesson of the standard "growth with debt" literature is that a country should borrow abroad as long as the capital thus acquired produces a rate of return that is higher than the cost of the foreign borrowing.

In that event, the borrowing country is increasing capacity and expanding output with the aid of foreign savings. The debt, if properly utilised, is expected to help the debtor country's economies (Hameed et al, 2008) by producing a multiplier effect which leads to increased employment, adequate infrastructural base, a larger export market, improved exchange rate and favourable terms of trade. But, this has never been the case in Nigeria and several other sub-Saharan African Countries (SSA) where it has been misused (Aluko and Arowolo, 2010). Although the growth rate of the economy has been inconsistent in the post-debt relief period as it plunged from 6.5% in 2005 to 6% in 2006 and then increased to 6.5% in 2007 (CBN, 2008), it could have been worse if the debt had not been cancelled. Before the debt cancellation deal, Nigeria was to pay a whopping sum of $4.9 billion every year on debt servicing (Aluko and Arowolo, 2010). It would have been impossible to achieve exchange rate stability or any meaningful growth under such indebtedness.

The effect of the Paris Club debt cancellation was immediately observed in the sequential reduction of the exchange rate of Nigeria vis-à-vis the Dollar from 130.6 Naira in 2005 to 128.2 Naira in 2006, and

then 120.9 in 2007 (CBN, 2009). Although the growth rate of the economy has been inconsistent in the post-debt relief period as it plunged from 6.5% in 2005 to 6% in 2006 and then increased to 6.5% in 2007 (CBN, 2008), it could have been worse if the debt had not been cancelled. 10 However, the benefits of the debt cancellation, which was expected to manifest after couple of years, was wiped up in 2009 by the global financial and economic crisis, which was precipitated in August 2007 by the collapse of the sub-prime lending market in the United States. The effect of the crisis on Nigeria's exchange rate was phenomenal as the Naira exchange rate vis-à-vis the Dollar rose astronomically from about N120/$ in the last quarter of 2007 to more than N150/$ (about 25% increase) in the third quarter of 2009 (CBN, 2009). This is attributable to the sharp drop in foreign earnings of Nigeria as a result of the persistent fall of crude oil price, which plunged from an all-time high of US$147 per barrel in July 2007 to a low of US$45 per barrel in December 2008 (CBN, 2008).

The huge external debt stock and debt service payments of African countries and Nigeria in particular prevented the countries from embarking on larger volume of domestic investment, which would have enhanced growth and development (Clements, etal. 2003).

External debt became a burden to most African countries because contracted loans were not optimally deployed, therefore returns on investments were not adequate to meet maturing obligations and did not leave a favourable balance to support domestic economic growth. So, African economies have not performed well because the necessary macro-economic adjustment has remained elusive for most of the countries in the continent.

The main interest of this study then is to empirically investigate the effect of external debt on the economic growth of Nigeria. The study will focus on the following objectives: (i) Empirically investigate the effect of external debt on the growth process of the country; (ii) To determine the impact of external debt service payment on economic growth of Nigeria.

The findings from the study will be of utmost importance because policy recommendations will be given on the basis of its findings. The next section reviews various literatures, section three deals with the methodology, section four presents the data analysis and interpretation while the last section provides the conclusion and recommendations.

Literature Review

Nigeria is characterized by inadequate internal capital formation arising from the vicious circle of low productivity, low income, and low savings. This scenario calls for technical, managerial and financial support from abroad to bridge the resources gap. The accesses to external finance strongly influence the economic development process of nations. It is an important resource needed to support sustainable economic growth.

According to Owasanoye (2005), the establishment of debt management office (DMO) is regarded in contemporary times as a best practice in view of the importance of external debt management to development. He maintained that a new approach to debt 24 management is needed.

This will ensure that borrowing is resorted to only when necessary and excessive borrowing should be avoided, the legislature should wake up to its duty to set the expenditure limits in collaboration with the executive, something similar to what obtains in US a debt ceiling is set for government by the congress. It should also insist that all request regarding borrowing is accompanied with a cost benefit analysis, conduct public hearings on requests for the borrowings and ensure that borrowed funds are judiciously invested in purposes for which the approval was sought.

Muoghalu et al (2007) investigated how and the extent to which investment burden is affected by exchange rate conditions and external debt crisis in Nigeria, in the light of international oil prices movements using two different methods namely; the OLS and exact maximum likelihood (EML)

techniques. They found that a positive association exists between external debt and investment burdens. They, therefore concluded that it will not be an appropriate policy for a developing economy such as Nigeria to lavishly encourage both foreign investment participation (and associated remittances) and increased accumulation of external debt (and attendant burden). They recommended that policy makers must have to strike a balance between the two and determine the optimal levels and timing of both activities in order not to unnecessarily increase the overall external sector burdens.

2.1 HISTORY OF NIGERIA'S DEBT CRISIS

The phenomenon of external debt by Nigeria dates back to the colonial period precisely in 1958 when the sum of US$28 million was contracted for railway construction (Adepoju et al, 2007). Between 1958 and 1977, debts contracted were the concessional debts from bilateral and multilateral sources with longer repayment periods and lower interest rates constituting about 78.5 per cent of the total debt stock (Adepoju et al, 2007). AFRODAD (2007) noted that Nigeria's external debts have been increasing over time because of a proportional shortage of foreign exchange to meet her developmental needs. The fall in oil prices in the late 1970s had a devastating effect on government expenses. It therefore became necessary for government to borrow in 1978 for balance of payment support and project financing. As a result of this, government promulgated Decree No.30 of 1978 which limited the external loans the Federal Government could raise to 5billion Naira. In the same year government made the first "jumbo loan" of US$1 billion from the International Capital Market. This increased the nation's debt profile to US$2.2 billion (AFRODAD. 2007). Given this, Nigeria's external debts skyrocketed from the million-dollar category to that of billion dollars. Nigeria's external debt stock increased 16 to US$13.1 billion in 1982 (CBN, 2003). Two factors led to this sharp increase: one, the entrance of state governments into external loan obligation and two, there was a substantial decline in the share of loans from bilateral and multilateral creditors and a consequent increase in borrowing from private sources at stiffer rates.

Nigeria's inability to settle her import bills resulted in the accumulation of trade arrears amounting to US$9.8 billion between 1983 and 1988. The insured components were US$2.4 billion while the uninsured were US$7.4 billion (Adepoju et al, 2007). The insured component was rescheduled at the Paris Club, while the uninsured was reconciled with the London Club. This reconciliation which took place between 1984 and 1988 reduced the amount to US$3.8 billion (Adepoju et al, 2007). The accrued interest of US$1.0 billion was recapitalised. This brought the amount to US$4.8 billion in 1988 and the debt was eventually refinanced. In 1990, Nigeria's external debt rose again to US$33.1 billion (CBN, 2003). After a brief decline to US$27.5 billion in 1991, it rose steadily to US$32.6 billion at the end of 1995. As at 1999, Nigeria's external debt stock was US$28.0 billion. 73.2 per cent of this was owed to the Paris Club while the rest was owed to the London Club, the multilateral creditors, promissory note holders and others. (CBN, 2003).

Furthermore, servicing and rescheduling of debt became problematic for Nigeria from around 1985 when its external debt rose to up to US$19 billion. Before then, Nigeria had experienced boom in oil revenue which was followed immediately by an unexpected decline. In 1980, Nigeria earned $25 billion from oil export. In 1982, it declined to $12 billion and further to $6 billion in 1986 (CBN, 2003). Government spending had remained high within this period and much of the projects were financed 17 through external borrowing. Since Nigeria was an OPEC member, it was not qualified for the soft-loan financing provided by multilateral and bilateral aid agencies to other countries at that time. As at the end of 2004, Nigeria's debt stock had reached almost $36 billion out of which $31 billion was owed to the Paris Club of Creditors while the rest was owed to multilateral, commercial and other non-Paris Club of creditor (Riefel, 2005). According to AFRODAD, (2007) debt service payment for Nigeria's debts started on a soft, tolerable level in 1958 until it became a hard bargain years later. Matters came to a head in 2003 when one of Nigeria's creditors, the Paris Club, demanded $3 billion annually for debt service payment. Dr. Ngozi Okonjo-Iweala considered the payment economically unsustainable (Semenitari, 2005). She therefore negotiated with the club. The $18 billion debt cancellation for Nigeria in 2005 by The Paris Club

and subsequent settlement of some outstanding debts reduced the total external debt of the country substantially.

2.2 EXTERNAL DEBT MANAGEMENT IN NIGERIA

2.2.1 External Debt Management Strategies

In the 1980, the management of the external debt became major responsibility of the Central Bank of Nigeria (CBN). This necessitated the establishment (setting up) of a department in collaboration with Federal Ministry of Finance to the management of external debt. Although, the debt management strategies and measures varied from time to time since the early 1980s when the external debt became pronounced. The following measures were used by the Government as guidelines to external borrowing. Economic sector should have positive Internal Rate of Return (IRR) as high as the cost of borrowing i.e. interest. External loans for private and public sectors projects with the shortest rate of return should be sourced from the international capital market while loans for social services or infrastructure could be sourced from confessionals financial institutions. -

State Government, Parastatals, Private sectors borrowing receive adequate approval from the Federal Government so as to ensure that the borrowing conforms to the national objectives. Projects to be financed with external loan should be supported with feasibility studies which include loan acquisition, deployment and retirement schedule. State Governments and other agencies with borrowed funds should service their debts through the foreign exchange market and duly inform the Federal Ministry of Finance for record purposes. Any default will attract deduction (in Nigeria equivalents) at source before the release of statutory allocations. Private sector, industries that are export oriented are expected to service their debt from their export earnings while others should utilize the Foreign Exchange Market facilities for debt servicing.

The government over the years adopted the under listed strategies and measures to deal with the debt problem. They include: Embargo on new Loans and Directives to State Government to restrict external borrowing to the barest minimum: The embargo was to check the escalation of total debt stock and minimize additional debt burden. However, these have not been particularly effective as indiscriminate quest for external loans have not been adopted. Although rescheduling has conferred short term relief or debt service obligations, the debt overhang has however hardly been abated as the debt stock has continued to increase significantly.

2.2.2 Nigeria External Debt Servicing

The major challenge faced by the debt management office is ensuring that a reasonable level of resources earmarked for debt servicing to avoid the risk of default and to maintain conducive relations for debt relief negotiations with the creditors. Also, the DMO faces the challenge of ensuring that budget resources are release in time to effect debt service payment since much of Nigerian’s debt stock build – up was accounted for by the capitalization of interest arrears and penalties for default. Debt service payments to the World Bank are due every 15 days while ADB (African Development Bank) service payments occur frequently. The debts are not subject to debt relief or rescheduling and in case of default, they carry stiff consequences with sanctions coming 30 days after due date.

The implications for default include. I. Prohibition of borrower/guarantor from signing new loan or guarantee agreement with the background. II. Suspension of disbursement in respect of all Bank group loans granted to the borrower/guarantor and lastly. III. Suspension of the granting of any new loans by the Bank group to the borrower/guarantor. The impositions of the above sanctions adversely affect the credit – worthiness of a Country as well as access to further foreign credits or loans. It is therefore to be avoided by all means. A.Paris club: Failure of our debt service obligation will undermine Nigerian’s effort to obtain substantive debt relief over the medium term coupled with the inability to benefit from normal credit facilities as Export credit agencies in Paris club creditor countries in default of debt service payment. Also business and government agencies from such debtor countries seeking to import goods

and services are required to pay the full 100% upfront, even against deliveries that will take several months and at times years. B.Bilateral: Defaulters in this category incur penalty charges in the form of late interest, which are usually about 1-3% above the normal interest charged.

C.London Club: The consequences of defaulting are stiff as the instruments carry legal obligations e.g. If par bonds on promissory notes payment is not received as at when due, creditors could acquire the assets of the Central Bank of Nigeria CBN and Nigerian National Petroleum Corporation NNPC anywhere in the world, as Nigeria has expressly waived her sovereign immunity under the terms of the agreement. In line with the desirable consequences of default in debt service payments the best arrangement must be put in place from time to time in response to changes in the economy and the polity. In order to facilitate the implementation of a new debt service arrangement, the DMO has agreement with the debtors on the nation's external debt stock and debt service obligation so that levels of government and their agencies that contracted the loans would know their respective stock of debt and the required amount for servicing.

2.2.3 Nigerian External Debt Rescheduling and Restructuring

Debt Rescheduling involves the postponement, extension and re-orderings of the repayment of the existing debt. An agreement between creditors (government authorities and the commercial banks acting as a group) and the debtor to roll over payment due to the former from the later over a certain period and under new terms and conditions falls under either debt rescheduling or refinancing. This involves the provision of new money to replace maturing debt. The four elements of loan restructuring are: I Rescheduling of the principal of a part or all of an existing loan by postponing repayment i.e. rearranging maturities and grace periods involves the rescheduling of the interest payments. Il Refinancing of an existing loan by raising fresh or complementary fund to meet existing obligation that is making provision for new credits with proceeds to be used to repay outstanding loans; Ill Restoring of trade –related bank credit lines; and IV Persuading the financial community to restore inter-banks lines of credit to a certain minimum level. Official debt restructuring under Paris club- This involves the rescheduling of both official medium term and long- term debt falling due in a given period including those in arrears. The rescheduling terms under Paris Club are generally non-concessionary. Moreover, Paris Club is extremely reluctant to reschedule payments on short term debt with an initial maturity of one year or less.

In Nigeria efforts on debt rescheduling, the country held a first round of talks with the Paris club on rescheduling of her debt in October, 2000 while the second help in December 2000 resulted in an agreement to reschedule Nigeria's debt under Houston Terms. Rescheduling of Nigeria's Paris club debt totaling US$20.5 Billion in 2000 over an 18-20year period. Credits are to be rescheduled over 20 years at concessional interest rates and enjoy 10 year's grace periods. Commercial credits are to be rescheduled over 18 years at market-based interest rates, including a three years moratorium interest of about US $1.063 Billion which was capitalized. It was agreed that debt service payment in 2001 should be kept at $1 billion. Nigeria made bilateral negotiations with about fourteen creditor countries on the specific details of each agreement. Nigeria confirmed her stand with the Paris club in the Agreement minute in Dec. 2000 for a further negotiation after July 31, 2001 the agreement was however subject to a good track of record in implementing the IMF –supported stand; negation of as follow-up medium term programme supported by the IMF and lastly satisfactory implementation of the 2002. Paris club agreed minutes including timely debt servicing.

However, Nigeria's debts, like that of most other developing countries, appeared to be on a ceaseless and perpetual increase. The more we paid, the more it seems we owe. Doubtful deals, dud projects (white elephants) and dubious debts; Nigeria was neck-deep in the debt trap. Debt became a burden on Nigeria's neck, jeopardized her economic growth; undermined the capital market development and compromised her social development. The country spent a lion's share of her national income servicing debts leaving little money for social services and infrastructural developments, and even still much less for investment. In the process, we have paid more than we originally borrowed, yet our debt – like a cruel virus – continues to multiply Nigerians, victims of many years of belt-tightening and austerity measures

are worried stiff while President Olusegun Obasanjo cried himself hoarse appealing to the Western creditors to loosen the debt noose through outright cancellation, interest forgiveness and debt-for-development assistance-swap. Before the debt cancellation, with an external debt of over $US30 billion, servicing of debt was a major economic challenge and a critical development issue. Nigeria was spending about one third of its budget, three times its sectoral budget for education and nine times its health budget on servicing outstanding debts. This saddled away investable fund that would have been available in the economy. The chapter shall be devoted to different views on external debt and its impact on growth and development.

2.3 EFFECT OF EXTERNAL DEBT ON ECONOMIC GROWTH

There have been several attempts to empirically assess the external debt-economic growth link - the debt overhang and crowding out effects - mainly by using ordinary least square (OLS). Most of the empirical studies include a fairly standard set of domestic debt policy and other exogenous explanatory variables. The majority find one or more debt variables to be significantly and negatively correlated with investment or growth (depending on the focus of the study). Hameed et al, (2008) opined that too much of external debt could dampen growth by hampering investment and productivity growth because of the fact that when greater 26 percentages of reserves (foreign currency) are consumed in meeting debt service, exchange rates fall and creditworthiness erodes; causing reduction in access to external financial resources. Boyce and Ndikumana (2002) noted that the inability of many SSA countries to meet their social needs and escape from debt is, to a large extent, a result of the fact that the borrowed funds have not been used productively.

Instead of financing domestic investment or consumption, a substantial fraction of the borrowed funds was captured by African political elites and channeled abroad in the form of capital flight, they revealed. They argued that in order to prevent diversion of borrowed fund through capital flight, there is need for greater accountability on the creditor side as well as the establishment of mechanisms of transparency and accountability in the debtor countries' own decision-making processes with regard to foreign borrowing and the management of borrowed funds. Were (2001) noted that Sub Sahara Africa countries were plagued by their heavy external debt burden. He argued that the debt crisis, compounded by massive poverty and structural weaknesses of most of the economies of these countries made the attainment of rapid and sustainable growth and development difficult. It then became widely accepted that the heavily-indebted countries require debt relief initiatives beyond mere rescheduling to have a turn-around in their economic performance and fight against poverty.

Sun (2004) opined that completion point countries will continue to face a dilemma given their large priority financing needs for development on the one hand, and the need to maintain long-term debt sustainability on the other. To achieve debt 27 sustainability, he advised that they should maintain macroeconomic stability and deepen reforms to improve policy and institutional frameworks, strengthen debt management, mobilize domestic revenues, and create an environment conducive to attracting foreign direct investment and diversifying exports. He concluded that the mix between debt and grant financing must be closely monitored by both borrowers and creditors to ensure that the potentially large financing needs associated with meeting the Millennium Development Goals do not give rise to a renewed excessive buildup of debt. Ngassam (2000) argued that debt obligations can be eased temporarily by rescheduling. He however, noted that African countries that are undergoing external debt crisis may improve their situation by: liberalizing their economies in order to bring competitive pressures on domestic private business activities, adjusting the exchange rate so that exports are encouraged and imports are restrained, and reducing inflation through strong policies of fiscal and monetary adjustment. He concluded that because of the structural difficulties facing most African countries, a comprehensive policy package for managing external debt has to aim at addressing not only demand management issues, but also the structural problems

According to Yilanci and Ozcan, (2008) external debt sustainability is a country's ability to meet its foreign debt obligations. Ajayi (1991), after analyzing the external debt of Nigeria within a general

macroeconomic framework, found that the country had macroeconomic policies that led to the accumulation of debt in excess of what was sustainable as judged by her export performance. He found out that for the entire period 25 between 1970 and 1988, macroeconomic policy coupled with inadequate trade policy led to a rate of borrowing that was not sustainable by Nigeria.

Adepoju et al (2007) further noted that a huge external debt without servicing as it was the case for Nigeria before year 2000 constituted a major impediment to the revitalization of her shattered economy as well as the alleviation of debilitating poverty. They revealed that the needed inflow of foreign resources for investment stimulation, growth and employment were hampered because without credit cover, Nigerian importers were required to provide 100 percent cash covers for all orders and this therefore placed them to a competitive disadvantage compared to their counterparts elsewhere.

Clements etal. (2003) argued that debt affect growth via its effect on the efficiency of resource use, rather than through its depressing effect on private investment. It was also found that the stock of public debt does not appear to depress public investment debt service does. Annual time series data from 1981 to 20024 was obtained to examine the dynamic effect of GDP, debt service, capital stock and labour-force on her economic growth. The study concludes that debt servicing burden has a negative effect on the productivity of labor and capital, thereby adversely affecting economic growth.

METHODOLOGY

Data sources and method of analysis

The study employed data that are secondary in nature. The annual time series data was obtained from the Central Bank of Nigeria Statistical Bulletin and Debt Management Office from 1981 to 2024. The methods of analysis or estimation techniques include Ordinary Least Square (OLS) method, Augmented Dickey Fuller (ADF) Unit Root test, Johansen Cointegration test and Error Correction Method (ECM).

MODEL SPECIFICATION

The study hypothesized that external debt does not have a significant effect on the economic growth of Nigeria. The model proxied Gross Domestic Product (GDP) as the endogenous variable to measure economic growth while External Debt (EXD), Ratio of External debt to Exports (EXD/X), Inflation (INF) and Exchange Rate (EXR) represent the exogenous variables.

Model I

$logGDP_t = \beta_0 + \beta_1 EXD_t + \beta_2 INF_t + \beta_3 EXRVOL_t + \beta_4 EXDR_t + \mu t$, ……(1)

Where $logGDP_t$ - Gross Domestic Product at time t.

EXD_t - External debt stock at time t.

INF_t – Inflation at time t.

$EXRVOL_t$ - Exchange rate volatility at time t.

β_0, β_1, β_2 and β_3- Parameters,

$EXDR_t$- External debt ratio at time t.

μ_t - Error term

Model II

$logGDP_t = \alpha_0 + \alpha_1 EDS_t + \alpha_2 GEX_t + \alpha_3 INT_t + e$ ……..(2)

Where $logGDP_t$ - Real Gross Domestic Product at time t.

EDS_t - External debt service payment at time t.

GEX_t - Government expenditure at time t.

INT - Average interest rate at time t.

β_0, β_1, β_2 and β_3- Parameters,

μ_t - Error term.

RESULTS AND DISCUSSION

This section deals with the analysis of data and interpretation of findings. The method of data analysis employed the Ordinary Least Square (OLS) method, Augmented Dickey Fuller (ADF) Unit Root Test, Johansen Cointegration Test and the Error Correction Method. The logarithms of the variables were obtained so as to bring the time series data on the variables.

Table 1: Unit root test.

VARIABLE	ADF	CRITICAL VALUE(5%)	P.VALUES	STATIONARY	REMARKS
GDP	6.774006	-2.938987	0.0313	I(1)	Stationary
EXD	-5.89598	-2.938987	0.0000	I(1)	Stationary
INF	-5.324450	-2.935001	0.0000	I(0)	Stationary
EXRVOL	-5.89598	-2.936942	0.0145	I(0)	Stationary
EXDR	-4.87972	-2.954202	0.0000	I(1)	Stationary
EDS	-4.373564	-2.936642	0.0003	I(1)	Stationary
GEX	-7.819631	-2.943427	0.0000	I(0)	Stationary
INT	-6.688910	-3.456883	0.0406	I(1)	Stationary

Note: Probability value are stated in parenthesis and (*) means significant at 5% level of significance.

Source: Authors Computation (2025).

4.2 JOHANSEN COINTEGRATION TEST

The cointegration test establishes whether a long run equilibrium relationship exist among the variables. To establish cointegration, the likelihood ratio must be greater than the Mackinnon Critical Value @ 1% and 5% levels of significance and the cointegrating equation is chosen from the normalized cointegrating coefficient with the lowest log likelihood.

Table 2: Johansen cointegration test.

Maximm eigen value	Trace statistics	5% critical value	1% critical value	Hypothesized no: CE(s)
0.5869	8.623	8.53	5.08	r =0**
0.4196	5.8390	6.21	5.48	r <1*
0.3390	3.6600	2.36	3.65	r<2*
0.259	1.5010	1.44	0.04	r<3*
0.1596	6.87	3.78	6.61	R<4**

Source: Authors Computation (2025).

This asterisk (*) denotes rejection of the hypothesis at 5% significance level and (**) denotes rejection of the hypothesis at both 1% and 5% significance levels. Using the trace statistics, it indicates five cointegrating equations at 5% significance level which implies that long run relationship exists among the variables. This led to the rejection of the hypothesis of no

cointegration. The cointegrating equation chosen from the Normalized cointegrating coefficients is;

GDP =1.390662EXD + 1.200221EXD/X + 0.607099INF + 0.617005EXR (0.15249) (0.11566) (0.14304) (0.20466)

Note: Standard Error statistics are stated in parenthesis from the cointegrating equation, all the exogenous variables except EXD has a positive relationship with GDP in the long run. In the long run, a unit increase in EXD/X, INF, and EXR leads to a rise in GDP by 1.200221, 0.607099, and 0.617005 units respectively while an increase (decrease) in EXD will cause GDP to decrease (increase) by 1.390662 unit.

4.3 ECM Results

Table 3: Short run results

ECM TEST RESULT

VARIABLE	COEFFICIENT	STD.ERROR	T-STATISTICS	PROB.
D(GDP)	6.777080	3.041825	2.227965	0.0351
D(EXD)	-0.059487	0.032600	-1.824773	0.0800
D(INF)	-0.038184	0.059666	-0.639947	0.5267
D(EXRVOL)	0.114519	0.0072198	1.586177	0.1253
D(EXDR)	2.474759	1.829577	-9.242890	0.0000
ECT(-1)*	-0.438289	0.155610	-9.242890	0.0000
ECT(-1)**	-0.861437	0.172592	-5.744404	0.0000
R-Squared				0.761213
Adj. R-Squared				0.731365
D.W Stat				2.345919

Source: Authors Computation (2025).

The coefficient of ECM in the model is -0.438289, implying that 43.8289% of the disequilibrium in the model is corrected every year. In model 2, the coefficient of ECM is -0.861437, implying that 86.1437% of the disequilibrium in the model is corrected every year. These results suggest that the speed of adjustment is higher in model two than in model one.

4.4 EVALUATION OF RESULT

4.4.1 Evaluation Based on Economic “A priori” Criteria, this test is carried to ascertain if the parameter estimates conform with what economic theory states in terms of sign and magnitude. The test is summarized in the table below;

VARIABLE	EXPECTED SIGN	OBSERVED SIGN	CONCLUSION
EXD	NEGATIVE	NEGATIVE	CONFORMS
INF	NEGATIVE	POSITIVE	DOES NOT
EXRV	POSITIVE	POSITIVE	CONFORMS
EDS	NEGATIVE	POSITIVE	DOES NOT
GEX	POSITIVE	POSITIVE	CONFORMS
INT	NEGATIVE	POSITIVE	DOES NOT

Source: Authors Computation (2025).

Muoghalu et al (2007) found that a positive association exists between external debt stock and investment burdens. This also conforms to the result of the “a priori” test.

CONCLUSION AND RECOMMENDATIONS.

External debt plays a crucial role in an economy. The optimal utilization of external debt by the government would avoid debt overhang and crowding out of investments. The bane of the study has been to examine the effect of external debt on the economic growth of Nigeria. The study employed the Johansen cointegration test and Error Correction Method. The cointegration test shows the existence of long run equilibrium relationship among the variables.

The error correction method reveals that the lagged error correction term in the overparameterized and parsimonious models is significant judging from its negatively signed coefficient. The high coefficient of multiple determination (R2) in the overparameterized model (88.7%) and the parsimonious model (87%) led to the overwhelming rejection of the null hypothesis which states that external debt does not have a significant effect on the economic growth of Nigeria. Also, the F-statistics shows that the time behaviour of external debt, ratio of external debt, inflation, and exchange rate all put together cause a significant change on the Nigerian economy.

Based on the findings in the study, recommendations were made. Firstly, the government should ensure economic and political stability in order to enjoy the benefits of external debt and make the debt burden minimal. Secondly, government should acquire external debt largely for economic reasons rather than social or political reasons. This would increase the productivity of the nation. Thirdly, government should diversify the nation's export base so as to increase export earnings and promote industrialization in order to reduce import dependency. Also, the government through its monetary authorities should put measures in place to curtail the inflationary trend in the economy. Furthermore, stability in the exchange rate should be pursued and depreciation in the Naira should be avoided by the government. Lastly, government should press for permanent debt relief so as to avert debt overhang problem.

Since 1985, Nigeria has been engaged in debt servicing, rescheduling and buy back with its creditors. Yet its debt stock as at the end of 2004 was $36 billion dollars after having paid about $35 billion to its creditors on $15 billion which it actually borrowed.

The situation could be blamed on two factors: (1) compound interest accrued to the actual loan within these years; and (2) the disposition of the Paris Club of Creditors towards the restructure of Nigerian debt for political reasons. The major findings of this study are highlighted below: i. It was found that there is a general increase in the external debt stock of the country over the years mostly due to accrued volatile compound interest and the ever-increasing appetite of various governments to secure loan for dubious projects.

ii. It was also found that the external debt of Nigeria has been unproductive in terms of its contribution to the growth process of the country due to corruption and challenges of debt sustainability. The effect of the debt service payments was not found to impair economic growth thereby not eroding the gains of the external debt.

Nigeria's debt crisis can be attributed to both exogenous and endogenous factors such as the nature of the economy, economic policies, dependency on oil, dwindling foreign exchange receipts etc. The origin of Nigeria's external debt dates back to 1958. Debt service payments were within manageable limits until 1982, but became unmanageable in 1983 because of the preference for private lending.

However, Nigerian political leaders need to develop homegrown policies to enhance the country's competitive advantage in the international market in this era of globalization. Besides, conscious efforts must be made to secure total exit from all forms of commercial debts that exposes the country to another regime of debt overkill. Nigeria must also explore and develop more export products outside crude oil.

Based on the findings of this study, Nigeria can only avoid future debt management problems if only they take the following recommendations. Nigeria should ensure that debt service obligations do not rise

rapidly than foreign exchange earnings. Loans contracted should be invested in profitable ventures, which will generate a reasonable amount of money for debt repayment. External finance should be used only for projects of highest priority such as mineral resources, education and agricultural projects.

The composition of the external debt should be regularly checked in order to forestall problems associated with the bunching of debt service obligations. Adequate safeguards should be put in place to cope with the sudden or unexpected shortfalls in earnings from exports or anticipated expenditures on imports.

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