



POLICY BRIEF

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Reducing the Cost of Governance: Alternative Policy Options for Economic Sustainability

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Summary

The Nigerian government has proposed to harmonise the salaries of civil servants as a measure to control the high costs of governance amidst the shrinking revenue base. While the harmonisation of salaries across MDAs is a reasonable idea, it is unclear how that would help to achieve government's objective of cost reduction.

- However, the government may also consider other known alternative measures such as reforming the fuel subsidy regime, merging and consolidating MDAs, placing a limit on the number of political appointees and aides, scrutinising the budget to eliminate duplicated and frivolous expenditure, and revising the indicators for measuring fiscal responsibilities.
- Achieving the above will require the National Assembly to,
 - (i) collaborate with relevant stakeholders to reform the fuel subsidy regime;
 - (ii) amend or totally repeal the Acts establishing affected MDAs by the consolidation reform;
 - (iii) sanction MDAs that include repetitive or frivolous items in their budget;
 - (iv) amend the Fiscal Responsibility Act to include additional indicators of fiscal responsibility such as recurrent expenditure-total expenditure ratio.

Introduction

The Nigerian economy has been faced with numerous challenges in the past few years. One of the major challenges facing the country's economic management is the

high cost of governance. Over the years, recurrent expenditure has consistently accounted for about 70% of the budget, leaving only 30% for investment in productive infrastructural projects. The



current situation will perpetuate a state of social and economic underdevelopment.

The Federal Government, through the Federal Ministry of Finance, Budget and National Planning, has been devising measures to reduce the cost of governance and create a sustainable fiscal path for the economy. This brief re-examines some of the alternative policy options for cutting the cost of governance.

Main Issues

The situation of the Nigerian economy is currently unsustainable. The economy is highly vulnerable to global economic disruptions. The COVID-19 pandemic, fall in oil prices, Boko Haram insurgency, herders and farmers' conflict, pushed the economy into recession in 2020. According to the National Bureau of Statistics (NBS), the economy contracted by 3.62% in the third quarter of 2020. The economic vulnerability is further reflected in the decline in total government revenue in 2020 due to oil price plunge caused by the COVID-19 pandemic. However,

government expenditure continues to rise, as planned expenditure in the 2021 budget is estimated at ₦13.08 trillion¹. The increases in expenditure is mainly driven by increases in recurrent expenditure relative to capital expenditure. Analysis of government expenditure between 2017 and 2021 reveal that government spending on capital project has been very low (see Fig. 1). Government currently spends an average 30% of the total budget on capital projects with the highest percentage of 39% in 2018. In contrast, recurrent expenditure as a percentage of total expenditure on average is 70% with the highest of 77% in 2020. The low proportion of capital expenditure could undermine investment in critical infrastructure required to eliminate absolute poverty. 79 million Nigerians currently live in extreme poverty, which accounts for 20% of the people living in poverty in Sub-Saharan Africa²; and massive investment in capital expenditure is critical to reversing the poverty trend.

¹ 2021 Appropriation Act. Budget Office of the Federation.

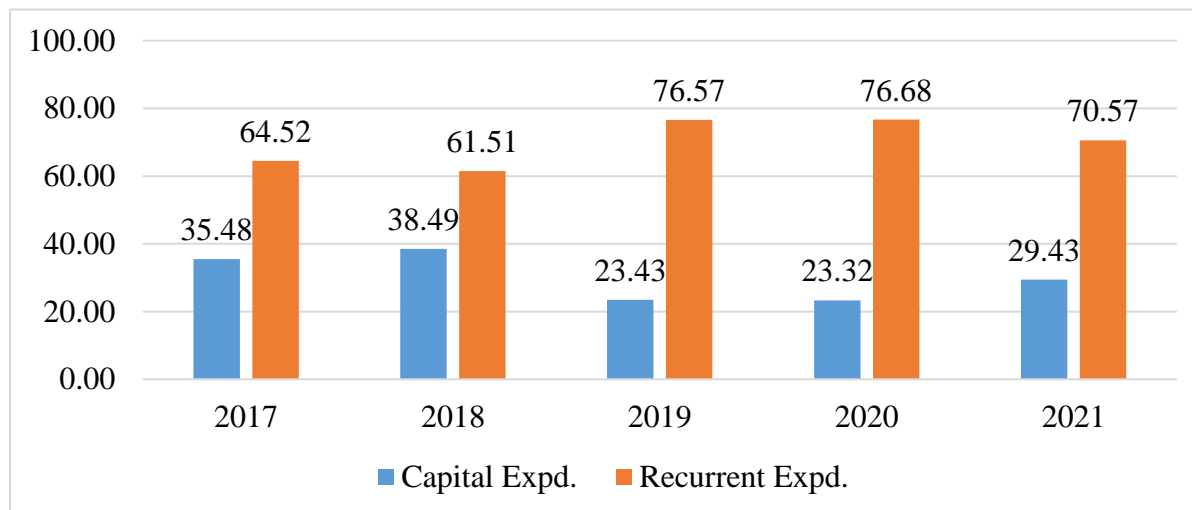
<https://www.budgetoffice.gov.ng/index.php/resource>

[es/internal-resources/budget-documents/2021-budget](https://www.budgetoffice.gov.ng/index.php/resource)

² CSEA, (2021). Nigerian Economic Update. Center for the Study of Economies in Africa. Issue 14



Fig. 1: Share of Capital and Recurrent Expenditure in the Budget, % (2017-2021)



Source: Author's compilation using data from NBS

Increasing deficit and debt has necessitated the need to reduce the cost of governance. Fiscal deficit as percentage of GDP increased from 4.3% in 2019 to 5.2% in 2020 while total public debt stood at \$85.9 billion (25% of GDP) on 30 June 2020³. Hence, the Federal Government through the Minister of Finance, Budget and National Planning, Mrs Zainab Ahmed, has proposed measures to reduce the costs of governance. Some of the measures proposed as reported in the media⁴ include harmonisation of salaries of civil servants across Ministries, Departments and Agency (MDAs),

reduction in the number of federal agencies, and removal of superfluous items from the national budget.

According to the Minister of Finance, Budget and National Planning, the goal of salary harmonisation is to ensure that the salaries of workers in the same grade level across MDAs are similar. This is likely to be achieved in either two ways. First, the salaries of some workers will be increased to close the gap across MDAs. If this is done, the higher salaries would further increase the cost of governance, which could undermine the stated goal of reducing

³ AfDB (2021). African Economic Outlook 2021. From Debt Resolution to Growth: The Road Ahead for Africa.

African Development Bank. Abidjan, Côte d'Ivoire.
⁴ <https://dailypost.ng/2021/05/05/buhari-govt-to-cut-civil-servants-salaries-minister/>



the cost of governance. Second, the salaries of some workers may be reduced to close the gap with those currently earning lower salaries. But this may also be counterproductive to the goals of the government.

Given the high dependency ratio, reducing the salaries of civil servants may increase the poverty rate. According to the 2019 NBS Poverty and Inequality in Nigeria Report, 40.1% of the population, or almost 83 million Nigerians live below the country's poverty line⁵. Income and non-income inequality is also high. Inequality, measured using the Gini coefficient, increased from 0.356 in 2004 to 0.391 in 2016. Considering the high cost of living, driven by the current inflation rate of 18.12% (overall inflation) and 22.72% (food inflation), reducing the salary of civil servants will amount to lower standards of living and may result in high poverty rates. This is partly because the 2019/2020 NBS/World Bank Living Standard Measurement Surveys shows that low-income Nigerians spend a larger proportion of their income on food. Also, an increase in the poverty rate will force the

government to spend more on social investment programmes (SIPs), which is self-defeating given that the government aims to cut spending.

Furthermore, it is unclear how harmonisation of salaries may help to cut the cost of governance. Hence, other policy alternatives may also be carefully considered. The Federal Government needs to consciously set targets for reducing the cost of governance and bridging the gap between revenue and expenditure by adopting aggressive spending reduction programs that include reforming entitlement programs, eliminating low-priority programs, and adopting commercial best practices in its operations.

A major option that could be considered is total elimination of the fuel subsidy regime. Although there have been competing claims about the existence of fuel subsidy, report by the NNPC shows the government spends approximately \$300 million monthly on fuel subsidy⁶, which translates to ₦1.3 trillion a year. Put in perspective, the annual spending on fuel subsidy is about 10% of the 2021 budget. Also the amount is way more than the 2.82% budgeted for health,

⁵ NBS, (2019). 2019 Poverty and Inequality in Nigeria: Executive Summary. National Bureau of Statistics. Abuja, Nigeria.

⁶ Bloomberg.com/news/articles/2021-03-25/nigeria-fuel-subsidy-hits-nearly-300-million-a-month-nnpc-says. Accessed 26 May, 2021.

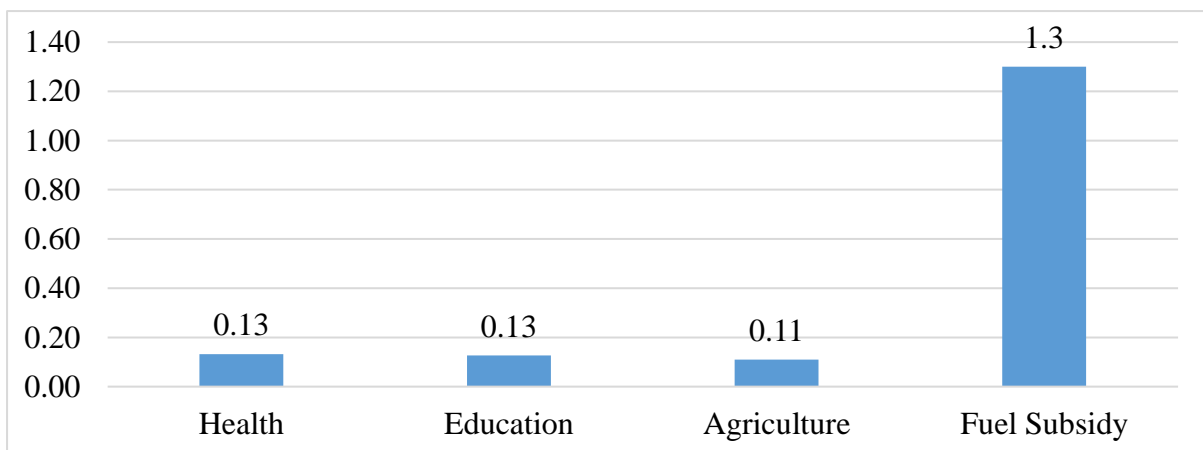


education and agriculture sectors combined in the 2021 budget (see fig. 2). Hence, reforming the subsidy regime is not only a necessity but it is an efficient way to reduce non-productive spending and the cost of governance. It would also remove its distortionary effects on the economy and boost private investment in the sector. The latter would create opportunities for government to generate tax revenue. To mitigate the effects of the subsidy reforms on the poor, the government could implement targeted and efficient subsidy scheme, which would have lesser financial implications than the current bloated subsidy regime.

Another key alternative route to cutting the cost of governance is by merging and

consolidating MDAs with related responsibilities. According to a media report in The Guardian Newspaper⁷, over 700 MDAs have similar and overlapping functions and responsibilities. The costs associated with the daily operations of MDAs are enormous. For example, the personnel and overhead costs of MDAs in the 2021 budget is ₦3 trillion and ₦330 billion respectively. The Oronsaye’s report noted the proliferation of irrelevant MDAs, and suggested the need to scrap some MDAs, merge those with related responsibilities, and encourage others to become financially self-sufficient in order to free up funds for capital expenditure and infrastructural development.

Fig. 2: Estimated government spending on fuel subsidy vs budget allocations to key sectors, 2021 (trillion Naira)



Source: Author’s compilation using data from *Budgit*

⁷ <https://guardian.ng/opinion/need-to-merge-federal-agencies/>. Accessed 26 May, 2021



Cutting the number of political appointees and aides is another option for reducing the cost of governance. One of the contributors to high cost of governance, especially personnel cost, is the large number of political appointees. While political appointees and aides are essential to the effective performance of government activities, there are cases of politicians having unnecessarily large number of aides. It is reported that some elected officials have over a thousand aides⁸. Paying the salaries and allowances of these aides constitute a significant proportion of personnel cost and overall government spending.

Eliminating the practice of duplicated and frivolous expenditure in the expenditure framework is critical for cutting the cost of governance. A report by Budget shows that about 316 projects worth ₦39.5 billion are duplicated in the 2021 budget⁹. It is also common to have ambiguous budget classification such as “consultancy”, “capacity building”, etc. in the annual budget. Preventing the duplication of projects and the associated costs should be one of the measures to be considered by the

government in its attempt to cut the cost of governance.

Another major gap in the quest to promote fiscal responsibility is the over-reliance on the deficit-GDP ratio in the Fiscal Responsibility Act (FRA). The existing indicator in the FRA measures fiscal responsibility using the deficit-GDP ratio, benchmarked at 3.26%. This might not be a fully reliable indicator, as the GDP figure is largely unknown as at the period the budget is being scrutinised. It is therefore important to consider other measures. For example, the fiscal responsibility rule could contain a limit on recurrent expenditure-total expenditure ratio to restrict over-bloated recurrent expenditure in the budget.

Areas for Legislative Considerations

The need to scale down on unnecessary expenditure and to monitor expenses on developmental projects that would impact positively on the lives of the citizenry have been highly talked about over the past years. Given the recent economic challenges, the government has proposed to harmonize salaries across MDAs. Although, the proposal is reasonable, it is not clear how this would help to achieve government’s goal of cutting the cost of

⁸ <https://guardian.ng/features/huge-number-of-political-appointees-causes-stir-in-cross-river-state/>

⁹ <https://www.vanguardngr.com/2021/05/2021-budget-316-projects-worth-n39-5bn-duplicated-budget/>



governance. Given the urgent need to reduce the costs of governance, it is important to emphasize some known policy options.

1. The National Assembly may collaborate with the executive to attempt a transparent reform of the fuel subsidy regime. This is a known major challenge, but efforts should be intensified to scrutinise the subsidy regime
2. Also, the National Assembly may consider the implementation of the recommendations of the Oronsaye's report. On its part, this may require amendments or total repeal of the Act establishing the affected MDAs.
3. In addition, the National Assembly may refuse to approve projects that appeared repetitive or frivolous until they are appropriately justified. There may be sanctions and penalties for MDAs that knowingly include such projects in

their budget. It is equally imperative that restrictions or ceilings be placed on the number of political appointees and aides that government officials and federal political office holders are allowed to employ.

4. More importantly, the Fiscal Responsibility Act may be amended to include additional indicators of fiscal responsibility such as recurrent expenditure-total expenditure ratio. A certain ceiling should be set over which recurrent expenditure in the annual budget is not allowed to exceed.

Conclusion

This brief assesses the proposed measures of the Federal Government to cut the cost of governance via harmonising of the salaries of civil servants. There is no clear evidence that this will ultimately reduce the cost of governance. Hence, the government may consider other measures to cut the cost of governance.



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