



Proshare **Confidential**



States and the Rising Weight of Debt

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ECONOMY

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Executive Summary

The dip in oil price coupled with relatively low production led to erosion in government revenue. This dislocation exposed the weakness in Nigeria's revenue pool. Interestingly, these structural fault lines rubbed on the states, as they had increased their debt levels, just like the Federal Government while the boom was on. Thus, the high dependency ratio on statutory allocation and weak internal generated revenue became inevitable.

The anti-clockwise movement in the cycle left the finances of states hard pressed, thereby leading to an automatic fall in consumption. Certainly states are limited with respect to fiscal multipliers, as they are not totally risk free. High oil prices had masked both the weak productive level of many states and the low taxable population. At the same time it brought to public consciousness, the size of total debt held by states.

Taking a clinical view at the productive level of each state have become necessary, so as to determine the productive capacity of each state of the federation. Moreover, it gives an insight on how resources are managed by each state over the years. A study of the size of public debt of each states and the trajectory of such debt

is carried out in this edition of our Proshare Confidential Report.

In this edition, the debt of individual states is weighed against their level of productivity, as a measure of their fiscal sustainability. It also determines the chunk of total debt held by states to the aggregate credit over a 5 year period. Even though states are not totally risk free, they still enjoy preference over corporates on the risk ladder.

We also studied the external debt of states both prior to devaluation and post devaluation, to ascertain the needed hint on the direction and distribution of total external debt among states.

As a follow up to the study, projected revenue of each states and their composition is made available. Thus it allows the study determine:

- The Average dependency ratio by states on statutory allocation.
- The States which are below that have their gross revenue below 50%.
- The Index capture of expenditure.
- The Internally Generated Revenue contributed per individual.

Measures were provided on how best to reduce debt and shore up revenue in the short term. The study also pointed out that states that are quick to identify their competency and improve competitive advantage will end up increasing their output. States that are able to hewn their value added tax's properly and improve rural roads will reduce the dependency ratio.

The study further made a case for improving the quality of human capital, as a tool to improve output and increase its taxable population.

States which have addressed poverty by improving human capital, increasing opportunity and reducing poverty are less vulnerable to dependency.

Certainly the study presented the macro picture of the economy and the threat of a secular stagnation, if policy recalibration is not taken. Adhering to tradition foreign tit-bits was provided but this time we focused on Argentina by accessing the reforms and trade-offs made in the face of political headwinds – which is important in a region where ideological battle fronts are vivid.

Introduction

Recently, the Debt Management Office stated that 23 states of the federation had exceeded their borrowing limits, in accordance with the Fiscal Responsibility Act of 2015. Furthermore, 20 out of 23 states had exceeded their 50% gross and net allocation. The statement jolted economic agents, given the possible trickle-down effect.

Moreover, in certain states of the federation, the impact of a low oil price has led to bitter spill experience already. Eventual bankruptcy will compound such harsh experiences felt by civil state workers in these states. The ripple effect on the financial system could be huge, thereby culminated into further depressing aggregate demand.

Obviously a scenario of debt defaults and rising contractor arrears in any of the states is an up risk to the fragile recovery and could further dampen an already dented human indicator. Moreover, the ripple effect could lead to deteriorating financial stability.

Puerto Rico and Detroit in the United States of America provides a vivid picture of states struggling under such burden. States once preferred for their economic activities have been reduced to ghost towns as debt defaults has led to a flight in human capital.

In this edition, shedding light on the individual economies of each state is inevitable in order to enrich the study.

In scenarios when states which have tipped in bankruptcy are locked out of the capital market. Revenue is blunted further by shrinking in both taxable population and corporates; potential productivity of such dwindles as exodus in human capital goes on.

Therefore such alarm bells rang by the Debt Management Office is timely, so as to prevent a capitulation in the cycle. Certainly studying the fiscal position of states and the GNI of each state has become a necessity. The study will provide solution on appropriate fiscal management measures needed in order to decelerate debt consumption.

In all, there are limitations to bail outs provided through the Federal Government and debt restructuring process. Without states “pruning down their pumps” in a manner that leaves room for growth with relatively thinner state government intrusion, increased investment in productive asset and improved conditions for doing business.

Statement of the Problem

- Relatively low oil prices compare to 2014 has affected the revenue capacity of the states.
- Heavily resource dependent states like Bayelsa are under pressure due to high debt and leaner revenue.
- Deposit money banks have become more reluctant to lend to states due to more sharpened risk.
- Rising recurrent expenditure has become the elephant in the room
- States workers are owed salaries, which has led to dampen demand in such state.
- Growth in recurrent expenditure has outpaced IGR in many states.
- There is an erosion in fiscal sustainability in most states.
- States are gradually been locked out of the capital market due to high loans and leaner revenue.
- Presence of poor fiscal management and uncoordinated policies in some states.
- There is relatively weak net foreign inflow in most states.
- Political consideration always take prominence ahead of commercial decision.
- Social unrest and agitation in certain states has affected their revenue base.
- At the same time fiscal policy is also crowding out viable states from sourcing funds in the capital market.
- Relatively weak productive activity in most states have made tax's revenue lean
- The weak economic cycle has affected indirect taxes like customs and VAT, thereby affecting the statutory income of states.
- States with huge external debt are struggling under the weight of higher interest expense.
- The poor land regulation and quality of land administration in most states has affected their competitiveness.

Objective of the Study

- The study will provide the macro picture of the economy.
- The study will provide a GNI of each state.
- The study will capture the economy on the sub national level.
- This study will provide an index capture of each state.
- It will provide an insight into the revenue base of each state, factoring the internal generated revenue and the other revenue stream.
- An analysis of the trajectory of domestic debt of the states will be provided.
- The study will determine the fiscal sustainability of each state both in terms of debt to gross service, debt to revenue and debt to internal generated revenue.

Methodology and Data interrogation

In carrying out this study, secondary data from reputable sources such as the Central bank, National Bureau of Statistics, Economic Associates State Report, IMF and many

others were used. At the same time primary data was also used to enrich the study. Essentially, data hybrid was employed as a method in this study.

Background to the Study

Macro-Picture

Table 1: Macroeconomic Variables

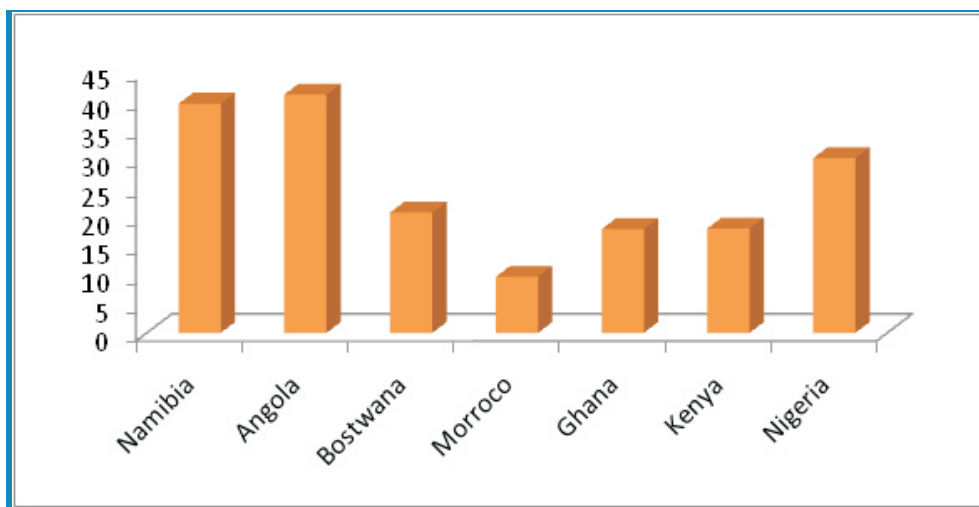
Variable	Present	Previous
Fiscal Deficit Or Surplus	N(397) billion as at May 2017	N(344.6) billion as at April 2017
Total Public Debt	N19.39 trillion, which is \$64.19 billion As at June 2017.	N19.159 trillion, which is \$62.87 billion as at march 2017
(FAAC)	N638 billion for the month of September 2017	N437 billion in the month of August 2017
External Debt	\$15.047 Dollars as at July 31 2017	\$13.87 billion as at March 2017
External Debt Servicing	\$54.24 millions	\$127 million
Capital Importation	\$1.792 billion	\$0.908 billion
Foreign Direct Investment	\$ 0.211 billion in Q2	\$ 0.275 billion in Q1
Inflation	15.98% in August 2017	16.01% in August 2017
Food Inflation	20.32 % in September 2017	20.25% in August 2017
Exchange Rate (Official)	N305.45 to a dollar as at June 30 (Q2)	N306.35 to a Dollar as at March 31 (Q1)
Parallel Market	N366 to a dollar as at June 30 (Q2)	N455 to a dollar As at march 31 (Q1)
External Reserve	\$33.4 billion as at 20 th October 2017	\$32.49 billion at the end of December 2017
PMI	55.0 in October 2017	53.3 in September 2017
GDP Growth	0.55%	-0.90%

Source: NBS, CBN

Economy at a Glimpse

- Inflation maintained a downward trend as core inflation and month on month inflation continued to dip.
- Food inflation reversed earlier slip in August, as it rose to 20.32%. Push factors such as rising energy cost and poor infrastructure has consistently driven the price of food northwards.
- Month on month inflation dwindled largely to 0.78 in the month of June, due to the tight monetary policy.
- Purchasers manufacturing index has maintained successive months of expansion, as it expanded from 55.3 in September to 55 in October 2017.
- The recovery in the Naira has led to improvement in the import PMI, thereby eroding the balance of payment slightly.
- Federal allocation to the 3 tiers of government in the month of September rose by 46% compared to the previous month of August. The accretion in FAAC was due to the strengthening in oil price.
- External reserve has grown by 1.3% compared to the previous month of September
- Total deposit with the Central bank in the month of August 2017 rose from N15.63 trillion to N17.27 trillion, the rise is attributed to 31% and 13.4% increase in federal and other deposits.

Fig 1: Bloomberg Misery Index



Source: Trading Economics, Proshare Research

- Using the Bloomberg misery Index, Nigeria's misery index stood at 31.8 at the end of September 2017.
- Certainly quantitative variables such as balance of payment,

PMI and the currency are far healthier.

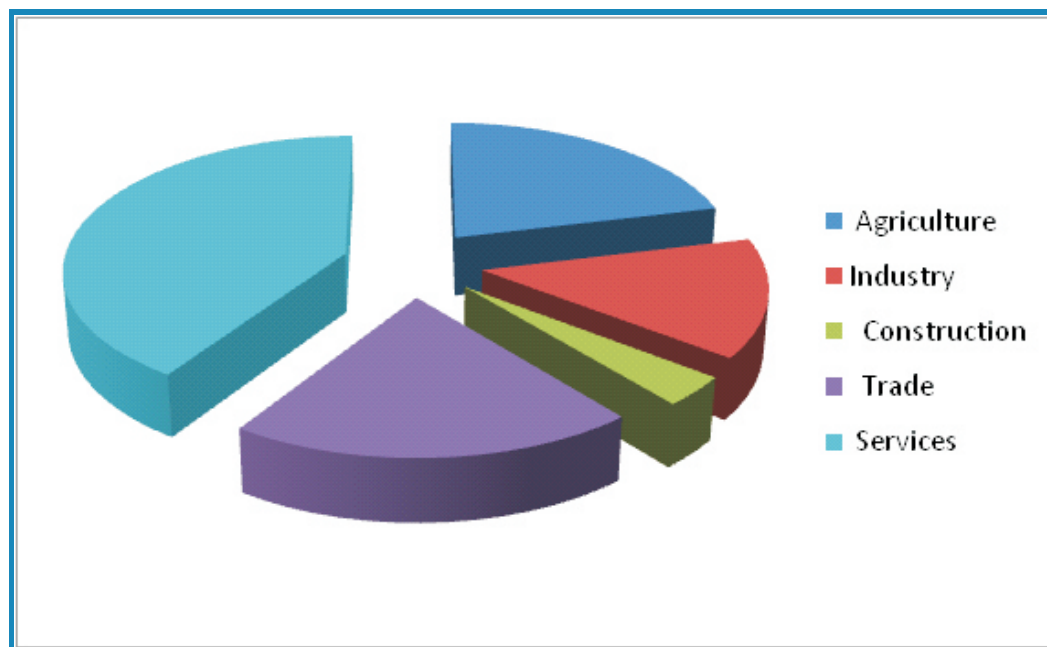
- Per capital income remained relatively weak compare to other countries.

Table2: GNI for Some Selected Countries

Country	Per Capital Income
Botswana	6,510
Morocco	3,040
Algeria	4,870
Angola	4,180
Nigeria	2,820
Chile	14,060
Egypt	3.34
Gabon	9,210

Source: World Bank, Proshare Research

Fig 2:Nominal GDP- Per Sector



Source: CBN, Proshare Research

Running Ex-Ante

- The persistent slack in the construction PMI still remain a drag to growth.
- It is expected that Naira recovery will boost labor productivity in dollar terms
- Recovery in the naira will ensure lighter implicit price deflator and a stronger Real Effective Exchange Rate (REER).
- is expected that ongoing inflation inertia will persist as push factors remain a concern to price stability.
- Expectedly, the present oil price will support an accretion in external reserve; moreover the Kurdish crisis is a tail wind to oil prices.
- Remittances are expected to increase as the festive period draw closer.
- The weakness in the individual PMI of export of manufacturing and export to non-manufacturing will continue.
- Emasculation of monetary supply will continue as we move closer to the festive period.
- We donot see any change in monetary policy till next year 2018
- The macro economy will experience a combination of low growth, high unemployment and high inflation, largely referred to as secular stagnation.

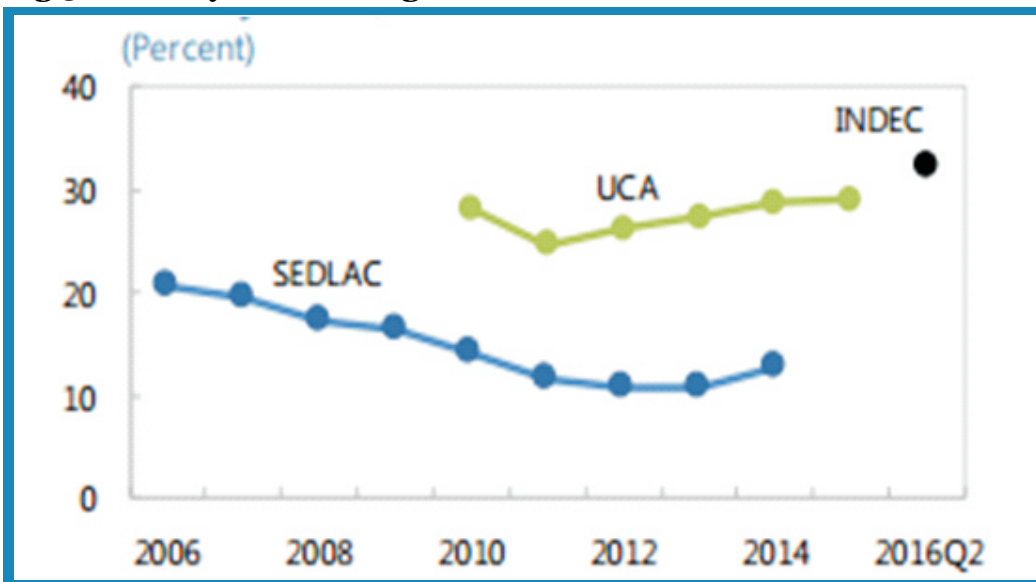
Foreign Tit-Bits

Argentina: Cheering a Gradualist Approach

At the end of the Krishna era, Argentina's economy was left in tatters as reforms became inevitable. The trio of rising inflation, currency crisis and rising unemployment, validated the picture of an economy in tatters. Moreover Argentina in its ability to reach a consensus with its creditor locked it out of the capital market.

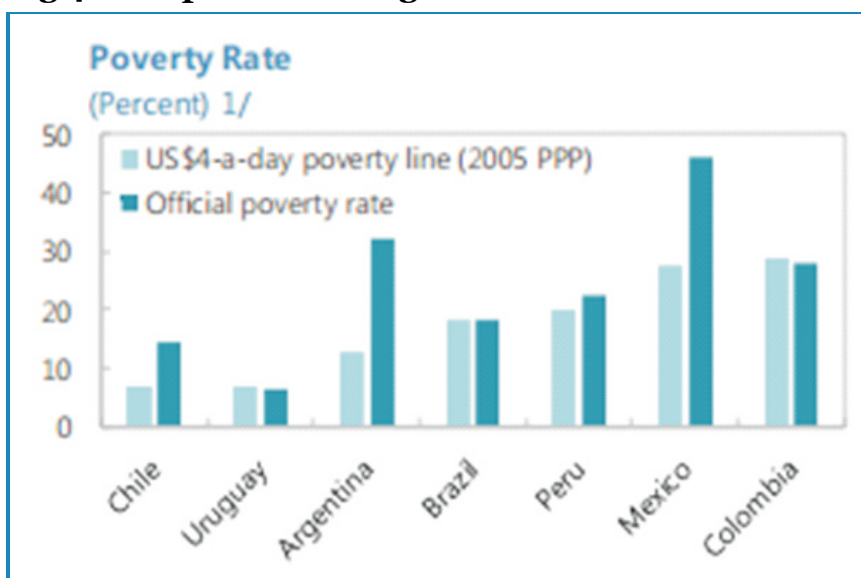
The Krishna era had pushed consumption beyond unsustainable levels, eroding drastically the potential growth level and drying up investment. Such policy reflected how extreme Keynesian policy with complete disregard for monetary policy always end up been a Trojan horse.

Fig 3: Poverty Rate in Argentina



Source: IMF

Fig 4: Comparison of Argentina other South American Countries



Source: IMF

At the same time, earlier policies of nationalization have led to a famine foreign investment, thus slowing down drastically the gross capital formation of Argentina. The present administration of Mauricio Marci had its fingers full, given the pyramid of problems Argentina was faced with. Argentina was in need of a lot of structural reforms on both the fiscal and monetary end.

The dilemma was to either prescribe a big bang pill, whereby reforms will be taken at a single dose. However disregarding the short term effect will further embolden poverty and unemployment, such negligence of the short term effect will be catastrophic. Eventually, the fall out effect will be an aggregate demand dampened largely left behind even when growths begin to emerge.

The internal economy will fail to meet supply since supply is reliant on external demand.

On the other hand the gradual pill will prevent an inflammation in poverty even as structural reform goes on. The up risk is that residue of structural restrains always remain, thereby not allowing potential growth to recover fully.

No doubt adjusting the macro environment in such a manner that supply is better off is necessary; neglecting the possible long term dent on demand could also be injurious e.g. Euro.

Moreover for a region where the battle lines between command and market economy are rife, good intentions might be fraught with a possible doom. More than anywhere else, the existing political dynamics limits the pace of reforms.

bound. Therefore setting targets and providing the right signals to investors in terms of commercial and macro interest. It started by:

- Unshackling the peso from capital control, eventually floating the nominal currency
- Removing export tax's
- Ensuring VAT reform

- Reduction in provisional transfers

- Reduction in subsidy and tariff social

- An overhaul of the national statistical agency, so as to bring credibility to data

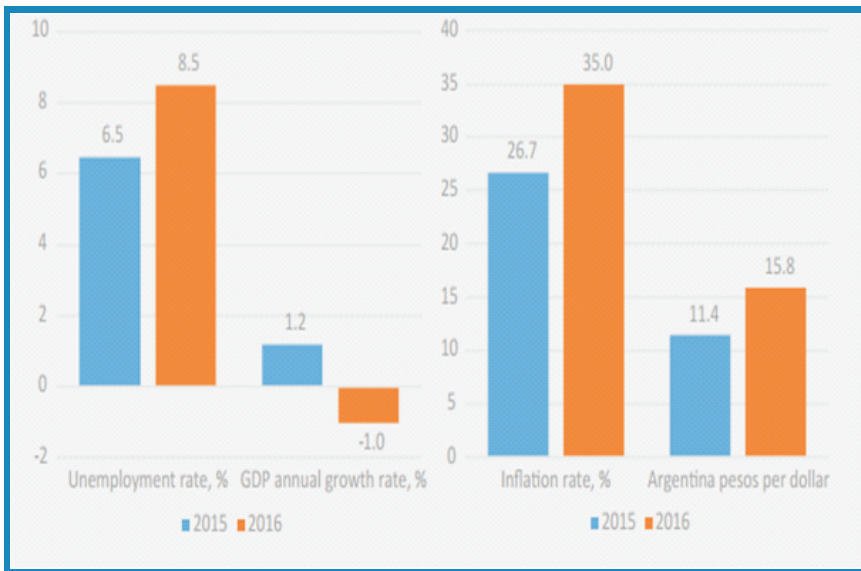
- Tax amnesty

Even with a gradualist approach, inevitably Argentina slipped into a recession in 2016. Output and industrial production fell by 2.6% and 8%, while unemployment roved around 9%.

The downturn proved that a big bang prescription would inflame poverty too quickly and domestic investment would dwindle sharply: thus triggering an astronomic increase in poverty and unemployment. Politically this could lead to unwinding reforms.

One must admit finding social economic mobility and structural reform on the short to medium never come easy. Moreover in a society like Argentina, where free markets must consistently provide room for equality even on the short run.

Fig 5: Unemployment and Growth in Argentina



Source: IMF

Macro management policies to demand were taken such as increase in unemployment benefit regardless certain gains were made.

- Settle debts that emanated from the currency board of 2001
- Repatriated \$100 billion of funds held back by creditors
- Increase in foreign portfolio investors - the Argentine Merval has enjoyed a 65.2% YTD. The highest in the world
- Unemployment has begun to fall, as it stands at 8.2%. However, higher than the Kirchner era.
- Argentina has emerged from a recession but with an 0.7% growth. Unarguably such growth remains too little too small to address Argentina's poverty rate.

- The floating of the Argentina peso has led to an accretion in reserves, providing more monetary maneuvering space.

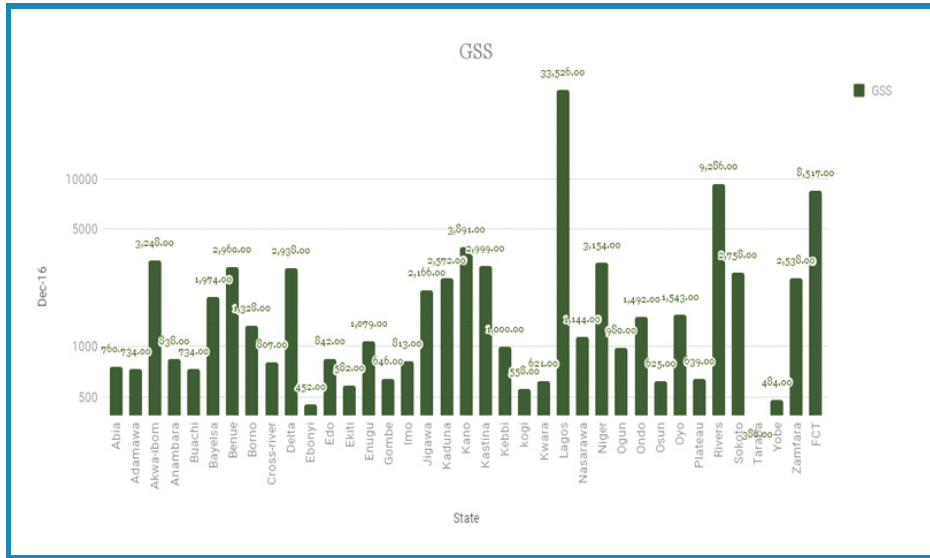
The policy transition so far has led to higher debt to GDP, at the same time inflation inertia is still a problem. Providing an accommodation for demand in such styled led reform does come with their cost, fiscal consolidation come in bits.

Given the political headwinds faced by Argentina, a multi targeted approach can only sustain such reform. Anything else in a region where sympathy to big government holds sway, such could jeopardize the reform. The opium about big government shed off on the medium term as market efficiency replaces socio-political equality. Evidently monetarist must be patient with Argentina in order to give free markets a chance on the long run.

Economy of States

Sub-National Economy

Fig 6: Gross Service Sector of States



Source: EA Associates

Table 3: States Distribution

No	States Services Below 500	<500>1000	<1000>5000	<5000>10000	>10000
1	Ebonyi	Abia	Akwa-ibom	Rivers	Lagos
2	Taraba	Adamawa	Bayelsa	FCT	
3	Yobe	Anambara	Benue		
4		Bauchi	Borno		
5		Cross-river	Delta		
6		Edo	Enugu		
7		Ekit	Jigawa		
8		Gombe	Kaduna		
9		Imo	Kano		
10		Kogi	Kastina		
11		Kwara	Kebbi		
12		Osun	Nasarawa		
13		Plateau	Niger		
14			Oyo		
15			Sokoto		
16			Zamfara		
Total	3	13	16	2	1

Source: EA Associates, Proshare Research

The total amount of gross service produce by states stands at N101 trillion. Lagos state alone accounts for 32.1% of the gross service. Rivers state alone accounts for N9.28 trillion worth of services, which makes it 9.13% of the total gross service produced.

Sixteen (16) states which include Kano, Oyo, Akwa-Ibom, Bayelsa, Benue, Borno Delta, Enugu, Jigawa, Kaduna, Kastina, Kebbi, Nasarawa, Niger, Sokoto and Zamfara produce N35.68 trillion of services, accounting for 35% of the total gross service produced.

Thus underlining the loop-sided production, moreover some of those states are producing below their potential output.

The remaining states produced N10.1 trillion worth of services.

Our Take-Away

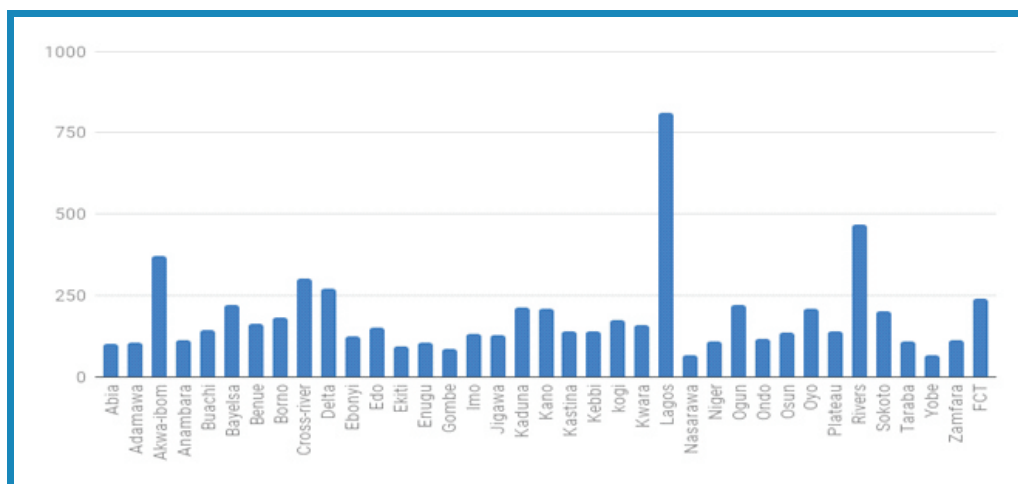
- The low productivity in many states have led to a supply delinquency.
- Most states have a slack level of competitiveness due to poor land administration.
- States with relatively low gross service, have low private participation making them prone to high recurrent expenditure.
- States which produce below N500 billion, state governors are the

Thus making it 10% of the total services produced and far less than Lagos state: As their productivity levels account for just 31% of Lagos GSS.

major employer of labour in such places.

- States with low productivity levels have low taxable population, which negatively affects the IGR.
- High unemployment levels fused with weak GNI are present in with low productivity.

Fig 7: Revenue Projections by Each State For 2017



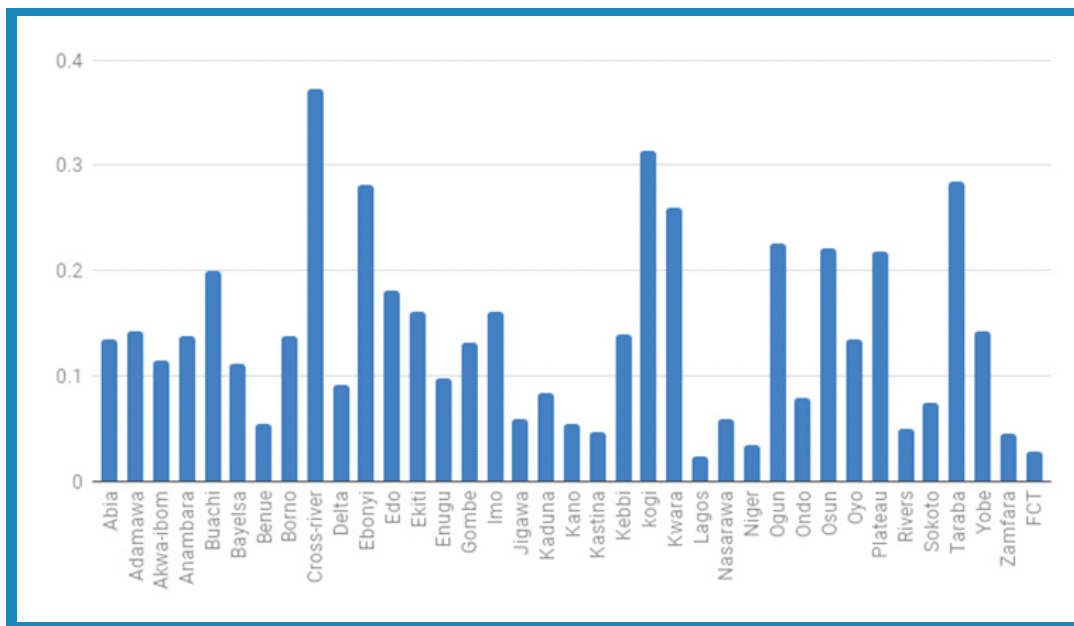
Source: EA Associates, Proshare Research

Table 4: Distribution of Projected Revenue of States

Below 100 Billion	From 100 to 150 Billion	From 150 to 250 Billion	From 250 to 350 Billion	From 350 to 500 Billion	Above 500 Billion
Ekiti	Abia	Bayelsa	Cross-River	Akwa-Ibom	Lagos
Gombe	Adamawa	Bayelsa	Delta	Rivers	
Nasarawa	Anambra	Benue	FCT		
Yobe	Buachi	Borno			
	Ebonyi	Edo			
	Enugu	Kaduna			
	Imo	Kano			
	Jigawa	Kogi			
	Kastina	Kwara			
	Kebbi	Ogun			
	Niger	Oyo			
	Ondo	Sokoto			
	Osun				
	Plateau				
	Taraba				
	Zamfara				

Source: EA Associates, Proshare Research

Fig 8: Projected Revenue to GSS



Source: EA Associates, Proshare Research

State Debts

Trailing Domestic Debt Consumption

Table 5: State Debt as at 2011 and January 2017

No	State	Million(N)	% of the Total	Million(N)	% of the Total
		2011		Jan. 2017	
1	Abia	24,202.24	1.9	53,525.31	0.018
2	Adamawa	25,954	2.1	61,157.54	0.021
3	Akwa-ibom	41,253.91	3.35	155,431.51	0.053
4	Anambara	6,403.32	0.52	3,993.89	0.001
5	Bauchi	18,345.73	1.49	69,988.36	0.024
6	Bayelsa	162,822.65	13.2	140,177.08	0.047
7	Benue	16,631.14	1.35	63,526.70	0.022
8	Borno	1,684.56	0.14	30,929.43	0.011
9	Cross-river	90,750.05	7.36	128,142.09	0.043
10	Delta	90,843.57	7.37	241,231.44	0.082
11	Ebonyi	40,239.94	3.26	28,057.14	0.01
12	Edo	39,044.30	3.17	45,091.94	0.015
13	Ekiti	23,667.51	1.92	85,049.68	0.029
14	Enugu	10,887.17	0.88	48,417.54	0.016
15	Gombe	7,170.42	0.58	48,312.48	0.016
16	Imo	25,419.40	2.06	93,267.76	0.032
17	Jigawa	1,590.54	0.13	19,005.55	0.006
18	Kaduna	34,771.71	2.82	63,276.47	0.021
19	Kano	5,867.29	0.48	93,715.18	0.032
20	Kastina	2,059.88	0.17	21,449.60	0.007
21	Kebbi	7,291.05	0.59	20,650.99	0.007
22	Kogi	34,122.12	2.77	71,381.26	0.024
23	Kwara	25,547.47	2.05	38,136.72	0.013
24	Lagos	157,536.16	12.77	311,755.80	0.105
25	Nasarawa	5,336.06	0.43	59,033.75	0.02
26	Niger	16,975.15	1.38	31,984.10	0.011
27	Ogun	30,143.97	2.44	75,921.43	0.026
28	Ondo	48,369.00	3.92	53,159.72	0.018
29	Osun	5,464	0.44	147,069.97	0.05
30	Oyo	5,463.64	0.39	115,886.55	0.039
31	Plateau	20,908.12	1.7	110,340.67	0.037
32	Rivers	83,978.39	6.81	142,424.09	0.048
33	Sokoto	4,902.05	0.4	22,450.25	0.008
34	Taraba	17,974.66	1.46	38,868.70	0.013
35	Yobe	2,088.40	0.17	13,581.29	0.005
36	Zamfara	12,968.38	1.05	58,321.02	0.02
37	FCT	85,568.90	6.94	152,804.61	0.052
	Total Debt	1,234,246.49		2,957,517.61	

Source: NBS

- As at December 2011, the total debt held by states stood at N1,234 billion, which was 2.2% of gross domestic product and 7.67% of money supply

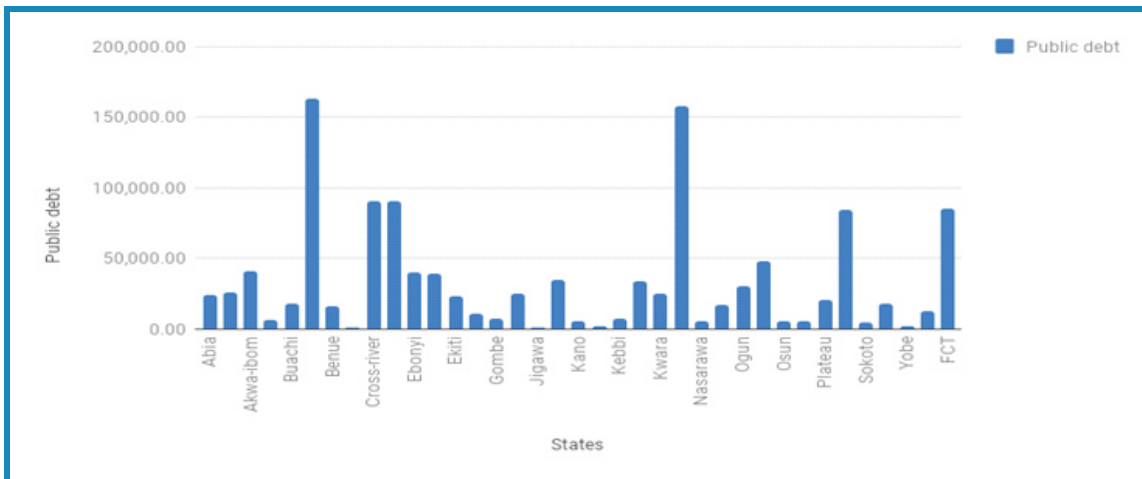
- Average debt per state stood at N33.35 billion

- Bayelsa state and Lagos state accounted for the highest chunk of debt, each with N162 billion and N157 billion. Thereby standing at 13.2% and 12.77%, of the total debt universe respectively.

- Jigawa is the least indebted with N1.59 billion, which was 0.13 % of the total debt held by states.

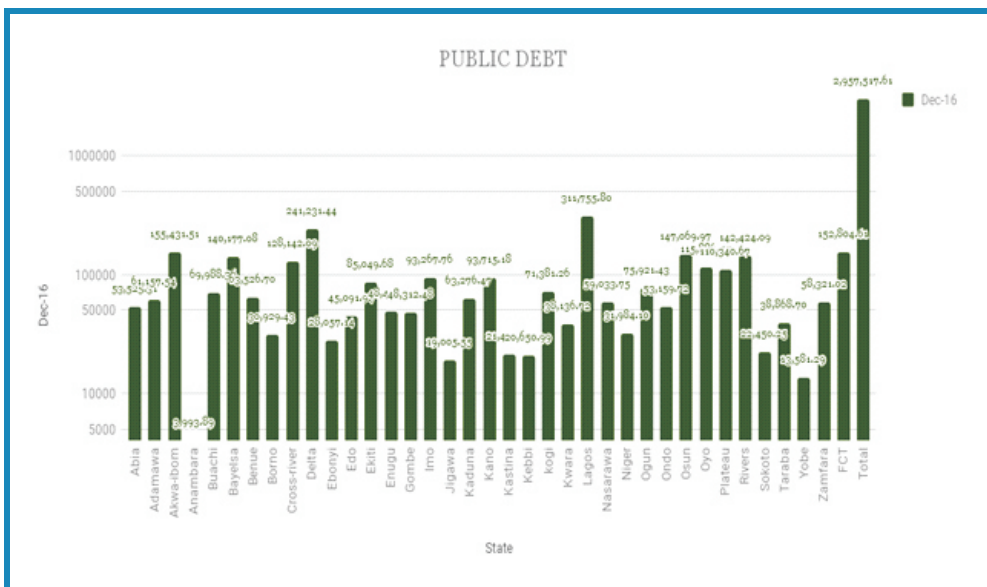
- Total oil receipts for 2011 stood at \$40.11 billion and the Naira was N155.85 to a Dollar.

Fig 9: Debts of States as at December 2011



Source: NBS

Fig 10: Public Debt As At Jan 2017



Source: DMO

- Total debt held by state stood at N2.95 trillion, which is 2.9% of GDP. Thus, revealing that debt accumulation have grown faster than GDP

- Avenge debt per state stood at N77.9 billion , reflective of a 133% growth

- Total debt of states to money supply stood at 12.59%

- Lagos holds the higher chunk of debt at N330 billion, which is 10.5% of the total state debt.

- Jigawa state is least exposed to debt, with N19 billion, but with one of the highest growth, given its low base.

Fig 10: Public Debt As At Jan 2017



Source: CBN, Proshare Research

** Total debt include capital market sourced credit such as bond

Although total state debt to aggregate credit to the economy have risen from 9.6% to 10.5%, regardless amplified risk to states due to the crash of oil triggered a softening in ratio compared a year ago. At the same time

sub national are not totally risk free but still enjoy preference on the risk ladder ahead of corporates.

Regardless state bonds make up a relatively lower chunk compare to contractors arrears and commercial loans.

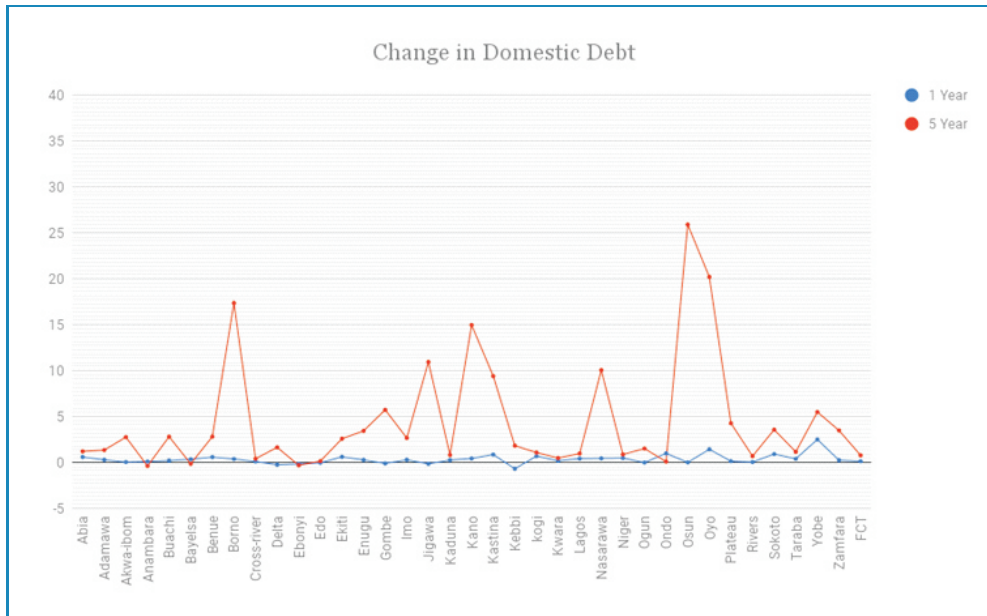
Table 6: State bonds

State	Interest rate	Amount	Credit Rating
Bauchi	15.5	15	Bb+
Bayelsa	13.75	13	Bb+
Delta	14	50	A
Edo	14	25	A-
Ekiti	14.5	25	
Ekiti	14.5	5	
Gombe	15.5	20	Bb+
Gombe	16	5	Bb+
Lagos			A+
Lagos	13.75	87	Aa-
Lagos	14.5	80	Aa-
Lagos	16.5	47	Aa-
Niger	14	12	A-
Niger	14	9	A-
Ondo	15.5	27	A-
Osun	14.75	30	Bbb-
Osun	14.75	11.4	Bbb-
Oyo	16.5	4.8	A-
Plateau	17.5	28.2	Bb
Zamfara	17.7	7	Bb

Source: Augusto Ratings

What are the percentiles telling us?

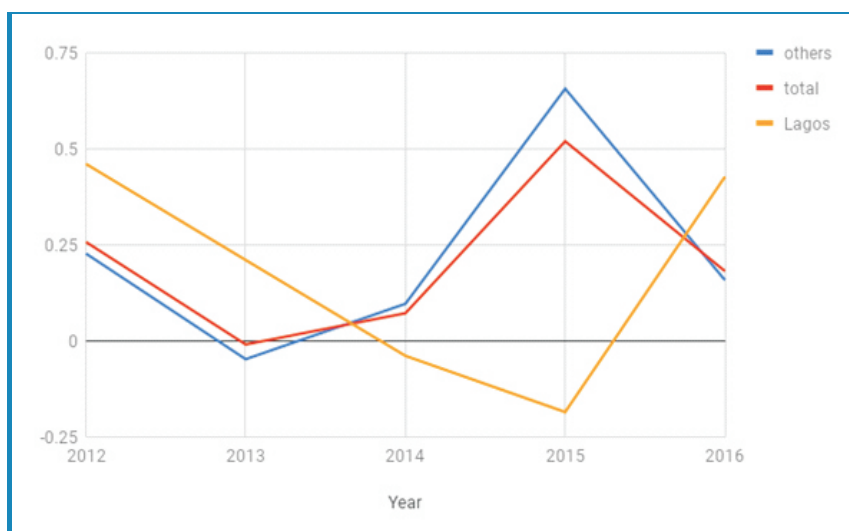
Fig 11: Change in domestic debt over the previous year and 5 year



Source: DMO

- States like Oyo, Osun and Kano have the highest debt growth at 20times, 25.9times and 14times, respectively.
- The average debt consumption over the last 5 years has been 4times the initial level in 2011. The average debt accumulation over the last one year period is 0.37, suggesting a deceleration in debt consumption.
- States like Anambra, Delta and Ebonyi have decongested their debt position compare to 2015
- Lagos debt growth over a 5 year period is 0.97, regardless its high base mask its divergence compare to other states.

Fig 12: Lagos and Others



Source: DMO

In recent times there has been a sharp accretion in domestic debt by Lagos state. Debts of other states have substantial correlation with total debt of states. Thereby sustaining a more dispersed distribution of debt, moreover there has been a deceleration in debt consumption by other states.

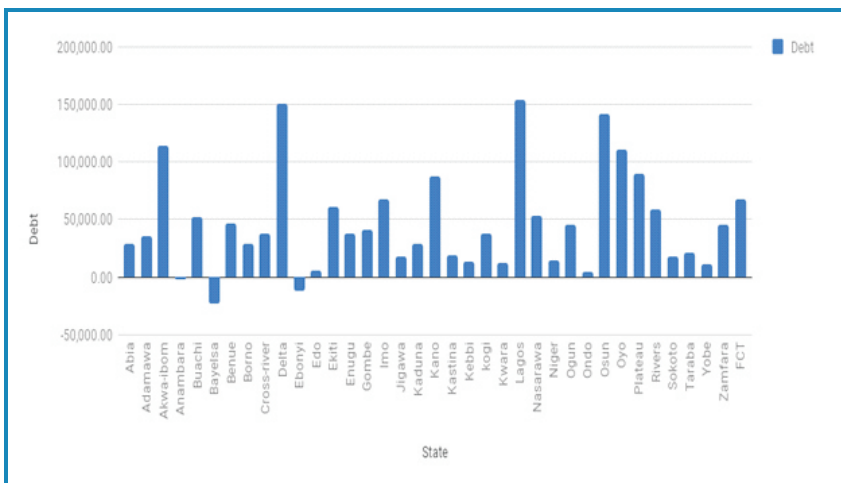
- Especially in states like AkwaIbom, Adamawa and Delta have borrowed more than N100billion over the last 5years.

- At the same time states like Ondo, Edo have low debt levels in absolute terms.

- Comparatively, Jigawa's debt level still remain minimal, highlighting the offshoot in its debt due to its low base.

- States like Anambra, Bayelsa and Ebonyi are best suited as their percentile align with their absolute value

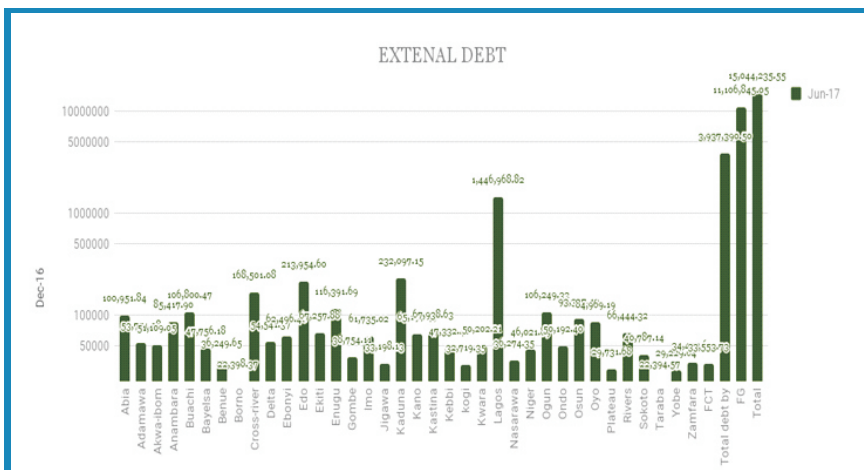
Fig 13: Change in Absolute Terms



Source: DMO

External Debt

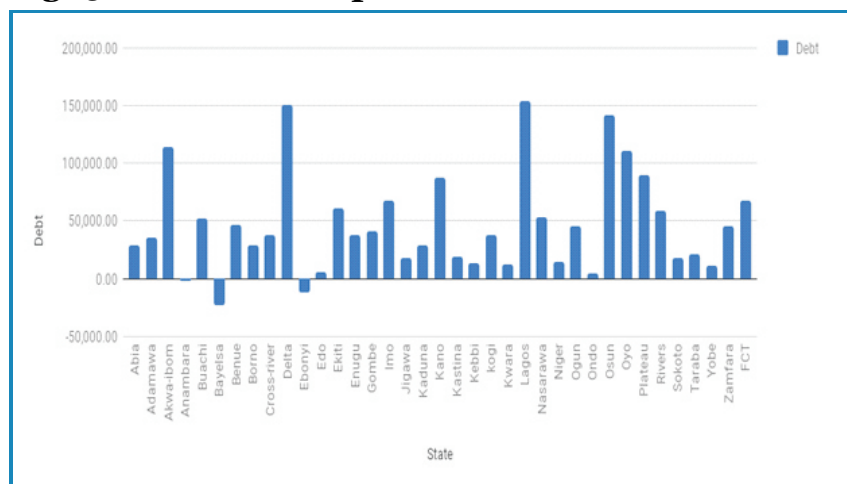
Fig 14: External Debt As At 2017



Source: DMO

- The total external debt held by states stands at \$3.97 billion.
- The external debt held by states stands at 0.9% of GDP.
- Over a 5 year period, external debt has grown by 58%. Thereby reflective of a leaner growth in external debt compared to domestic debt.
- The average external debt per state is \$109 million.
- Bauchi, Cross-river, Enugu, Kaduna, Lagos and Ogun's external debt levels are higher than the sub national average.
- Lagos has the highest amount of external debt, of \$1.4 billion, making it 36% of total external debt held on the sub national level: the rise in external debt makes Lagos more prone to external shocks compare to other states.
- Borno has the least amount of debt; the security situation in the state has shielded it from foreign inflow.
- Plateau, Yobe and Taraba have low external debt exposure.
- Cross River has a huge chunk of external debt, which streams from investment on tourism like Tinapa.

Fig 15: External Debt per Individual in Each State



Source: DMO

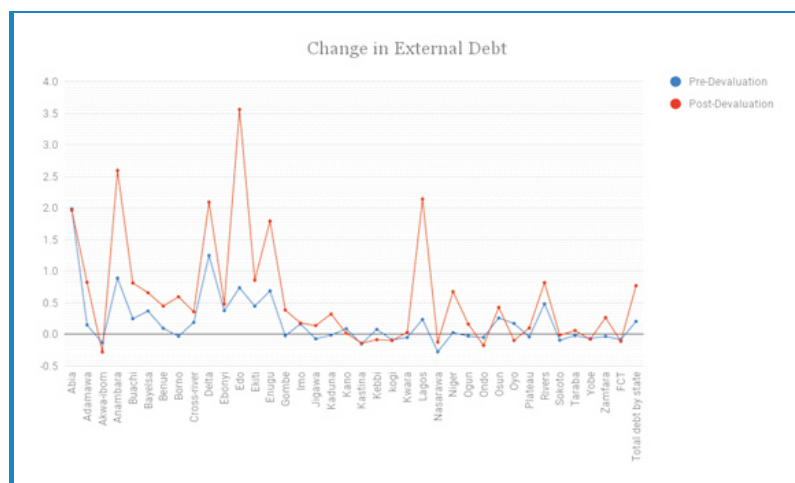
In most circumstances the dilution from high population base will trigger lower ratio, when measured on an individual basis. Expectedly, the debt per ratio slips is not far off from the sub national average.

Lagos runs contrary to this rule of thumb, rather each individual in Lagos is indebted to a tune of \$131 on the sub national level. At the same time 668% higher than the sub national average of \$ 19.68 per individual, other states like Cross river

their per external debt ratio higher than the sub national average. On the short to medium, Lagos state external

debt won't create ripples but on the long: ceteris peribus it might generate credit shocks.

Fig 16: Changes in External Debt across States



Source: DMO

- Obviously given Lagos their huge output, such as providing Lagos access to the capital market when compared to other states.
- States like Kebbi and Kogi have decongested their external debt position, compared over a 5 year period.

- At the same time states like Abia which has a relatively limited output below a trillion coupled with revenue below N150 billion stands the risk of inflaming its debt to both output and revenue: given the rise in external debt.

Revenue

Internal Generated Revenue (IGR)

Internally generated revenue is income sourced independent of the federal government. They play an important role in buffering up already existing revenue to states. Moreover, it reduces the level of dependency on the federal government and improves the viability of states.

Strong internal generated revenue is also a representation of high private participation, facilitated by the state. Internal generated revenue comprises of 5 major items.

- PAYE
 - MDA's revenue
 - Direct assessment
 - Road taxes
 - Other taxes
- Robust internal generated revenue is also a product of an effective tax system. At the same time it is determined by certain factors such as
- Fiscal capacity.
 - Efficiency of the state's tax institution.
 - The degree of poverty.
 - Industrial and agricultural development.

Table 7: Net Internally Generated Revenue As At 2011 & 2016

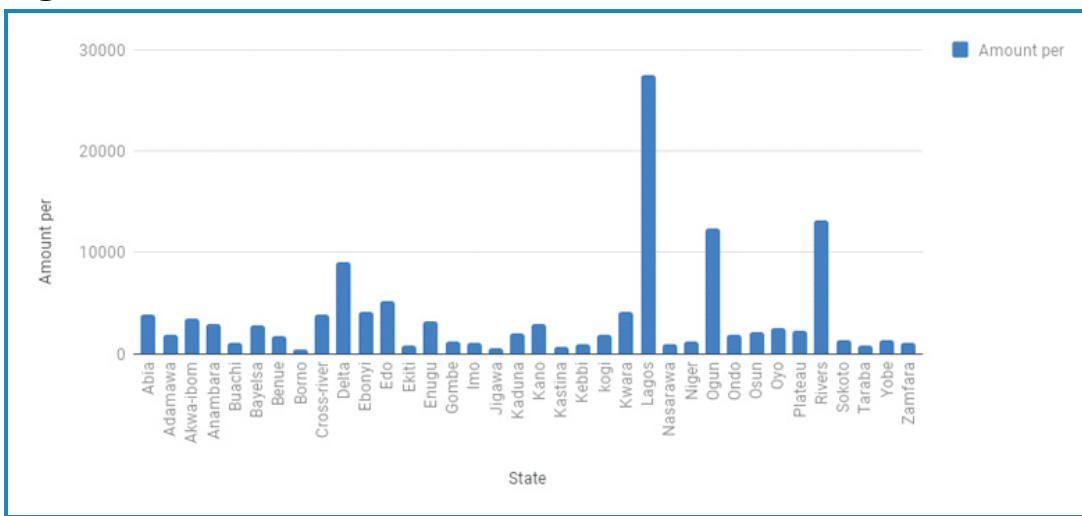
State	IGR as at 2011 Billion (N)	IGR as at 2016 Billion (N)	Ratio to Total IGR (2016)	Change (%)
Abia	11.76	13.35	0.016	0.13
Adamawa	4.11	7.59	0.0097	0.84
Akwa-ibom	11.67	16.59	0.021	0.42
Anambra	6.15	14.79	0.019	1.4
Bauchi	3.791	6.22	0.0079	0.64
Bayelsa	3.66	7.41	0.0094	1.02
Benue	11.13	8.88	0.0113	-0.2
Borno	2.82	2.52	0.0032	-0.11
Cross-river	9.16	13.54	0.017	0.48
Delta	34.75	44.89	0.057	0.29
Ebonyi	2.298	11.03	0.014	3.8
Edo	17.69	20.67	0.026	0.17
Ekiti	2.48	2.38	0.003	-0.04
Enugu	7.29	12.67	0.016	0.74
Gombe	3.15	3.57	0.0045	0.13
Imo	5.806	5.43	0.0069	-0.065
Jigawa	1.482	3.34	0.0042	1.25
Kaduna	9.78	15.5	0.019	0.58
Kano	6.62	34.46	0.044	4.2
Kastina	4.239	5.51	0.007	0.299
Kebbi	4.472	3.13	0.0039	-0.3
Kogi	2.84	7.58	0.0096	1.6
Kwara	8.82	16.46	0.02	0.86
Lagos	202.76	301.92	0.38	0.48
Nasarawa	4.13	2.094	0.0026	-0.49
Niger	3.79	5.76	0.0073	0.52
Ogun	10.83	56.28	0.0716	4.1
Ondo	8.01	7.78	0.0099	-0.029
Osun	7.39	8.96	0.0114	0.21
Oyo	8.95	15.66	0.02	0.74
Plateau	4.52	9.09	0.011	1.01
Rivers	52.71	82.101	0.1	0.56
Sokoto	4.185	6.22	0.0079	0.48
Taraba	2.86	4.105	0.0052	0.434
Yobe	2.49	3.8	0.0048	0.53
Zamfara	1.714	4.25	0.0054	1.5

Source: DMO

- Total internal generated revenue at the end of 2016, stood at N 785 billion
- Internal generated revenue grew 60% compare to 2011
- Total IGR makes up 3% and 0.7% of money supply and GDP, respectively.

- Lagos state internal generated revenue makes up 38% of total internal generated revenue
- States like Kebbi, Ondo, Nasarawa, Bayelsa, Borno, Ekiti and Imo have had their IGR dampened compared to 2011

Fig 17: IGR Contributed Per Individual in Each State



** The population figure as at 2014, is used in the study

- Borno state has the lowest IGR contribution per population as it stands at N500.
- Lagos state has the highest IGR contribution per population as it stands at N27,424.
- The average IGR contribution per population stands N3,603, whereby 27 states of the federation

have their IGR contribution per population below the average.

At the same time, states like Lagos and Ogun that have a robust payas you earn revenue base are more likely to have strong IGR contribution per population compared to the likes of Osun and Kaduna state.

Fig 17: IGR Contributed Per Individual in Each State

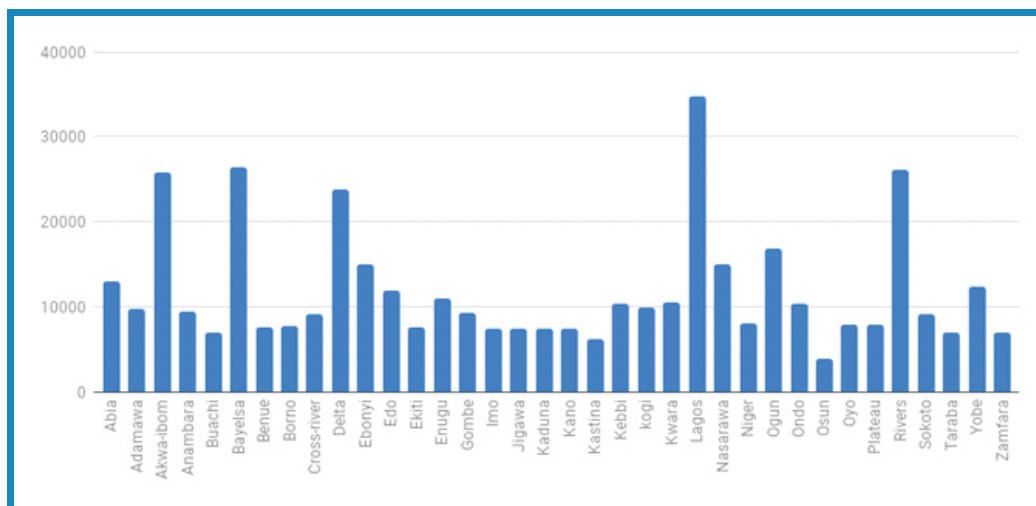
State	Net FAAC (Billion)	Total Revenue (Billion)	Net FAAC to Total Revenue	Competency and Potential
Abia	30.86	44.21	0.698	Manufacturing and trade
Adamawa	29.87	37.46	0.8	Trade route, mining and Agriculture
Akwa-ibom	104.97	121.56	0.864	Agriculture and oil production
Anambara	32.82	47.61	0.69	Trade, agriculture and manufacturing
Buachi	32.78	39	0.84	Agriculture and Mining
Bayelsa	60.5	67.91	0.89	Agriculture and oil production
Benue	30.36	39.24	0.774	Crop production and mining (coal)
Borno	37.06	39.58	0.936	Trade , agriculture and oil exploration
Cross-river	18.24	31.78	0.574	Tourism, Agriculture and oil production
Delta	73.32	118.21	0.62	Agriculture and oil production
Ebonyi	28.56	39.59	0.721	Agriculture, crop production; rice
Edo	26.21	46.88	0.559	Agriculture and mining (bitumen)
Ekiti	19.51	21.89	0.891	Agriculture, crop production; tubers
Enugu	31.07	43.74	0.71	Mining (coal) and agriculture
Gombe	23.15	26.72	0.867	Agriculture and Mining
Imo	30.26	35.69	0.848	Agriculture and oil production
Jigawa	36.322	39.662	0.916	Agriculture, crop production
Kaduna	40.118	55.618	0.721	Tourism, Agriculture and mining
Kano	50.68	85.14	0.595	Trade and Agriculture
Kastina	38.58	44.09	0.875	Agriculture, crop production (perishables)
Kebbi	31.919	35.049	0.91	Agriculture and Mining
kogi	32.07	39.65	0.808	Mining and agriculture
Kwara	25.97	42.43	0.612	Mining, oil production and Agriculture
Lagos	81.097	383.017	0.212	Tourism, manufacturing and oil production
Nasarawa	32.77	34.864	0.94	Agriculture and mining
Niger	32.77	38.53	0.85	Agriculture and mining
Ogun	20.25	76.53	0.264	Manufacturing and service
Ondo	35.69	43.47	0.821	Mining, oil production and Agriculture
Osun	6.92	15.88	0.436	Agriculture and mining
Oyo	33.4	49.06	0.681	Agriculture and mining
Plateau	21.56	30.65	0.703	Mining, tourism and agriculture
Rivers	83.64	165.741	0.504	Agriculture, oil production and agriculture
Sokoto	34.5	40.72	0.847	Mining and agriculture
Taraba	27.53	31.635	0.87	Agriculture, tourism and mining
Yobe	31.3	35.1	0.892	Agriculture
Zamfara	23.54	27.79	0.847	Agriculture and mining

Source: NBS, Proshare Research

- The total revenue accrued by states was N2.11 trillion in 2016
- The total net federal allocation accrued to N1.3 trillion in 2016

- The total revenue generated by states makes up 8.9% and 2.07% of money supply and GDP, respectively.

Fig 18: State Revenue per Individual



Certainly the state governors in places like Lagos, Akwa-ibom, Bayelsa and Rivers are bequeathed with larger revenue pool to address developmental concerns; however the cost of living and the quality and efficiency of spending by state governors play a critical factor on

how resource distribution affects the lower end of the pyramid and consistently grease the participation of private sector.

Fiscal Sustainability

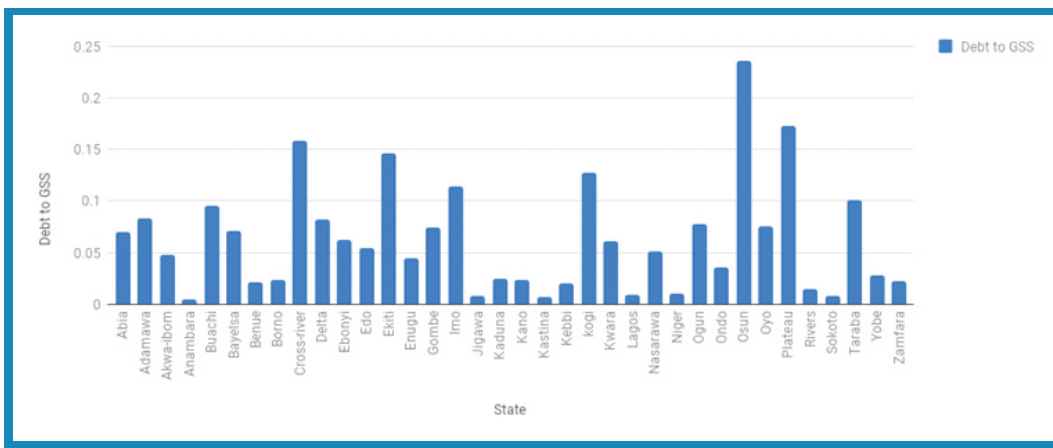
Output Indicator

One of the measures of fiscal sustainability is matching the debt of the individual or economic entity against the value of the asset owned by that economic entity. Popularly referred to as the asset to debt ratio, the general threshold for a tipping point is 40%. Thus, when debt to asset ratio is 40%, the sustainability of such is in doubt: For most sub-nationals within a sovereign the 40% threshold might be deceptive because:

- Nigeria's debt to GDP threshold is less than 40%.
- Economic sub-set like sub-nationals do have a lower threshold than the mother bird (nation).

- The domestic debts of states are not risk free.
- Most states do have different competencies, some tend to be more resilient than the other.
- A large chunk of the debt are not state bond, some are bank credits and contractors arrears.
- The debt mix between external and domestic.
- The dynamics of the domestic debt, especially between the trio of state bonds, contractors arrears and bank credits.

Fig 19: Debt to GSS



Source: DMO, EA Associates
 ** Public debt was only weighed against GSS

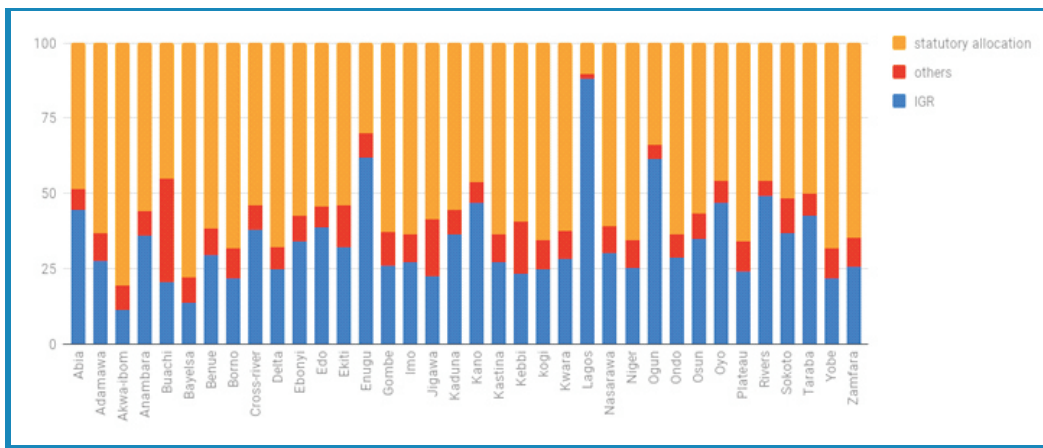
- The average debt to output ratio is 6.3%.
- Osun state's debt to GSS is the highest at 22% and higher than the National debt to GDP ratio of 19%.
- Osun state's fast absorption and relatively high debt to GSS ratio puts debt sustainability on a back foot.
- Relatively states like Cross River and Plateau have high debt to GSS ratio: obviously the sudden rise in debt puts gross revenue under pressure.
- Even though Lagos has high debt absorption, regardless Lagos state's debt to GSS ratio remains low.
- States with relatively stunted output but fast growing debt especially in areas where they are either agitations like Bayelsa, Yobe, Borno and Plateau are at risk of diminished fiscal sustainability.
- At the same time states like Ekiti and Cross- River have debt levels which are not sustainable.

Liquidity Indicator

The liquidity indicator unlike the output indicator matches revenue to interest expense. It tends to assume a more secured obligation to short term instrument. Especially when asset are slow in revenue generation and fiscal sustainability is under duress.

Moreover in a country where revenue is largely cyclical, studying the revenue basket of states will give a hint on how resilient such states are in terms of liquidity.

Fig 20: Revenue Basket of Each State



Source: NBS

- On the average, IGR and statutory allocation constitute 33.3% and 56.65% of the revenue basket of states.

- 27 states have their internal generated revenue below the total state average, reflective of high concentration of their individual income pool.

- Therefore in a cycle whereby oil prices have shed their value by half and debt levels have doubled. The gross income of states are under pressure.

- Presence of a concentrated income pool put their fiscal sustainability under duress.

- Most states which are oil producing areas have a concentrated revenue pool. At the same time states like Akwa-Ibom and Delta which has experienced substantial growth in their debt portfolio, stand the treat of diminished fiscal sustainability.

- States with revenue below 100 billion such as Ekiti, Gombe and Nasarawa have exceeded their borrowing limit.

- Another measure of liquidity is the index capture of expenditure. This measure captures the relationship between internal generated revenue and expenses. In specifics it weighs internal generated revenue against the recurrent expenditure.

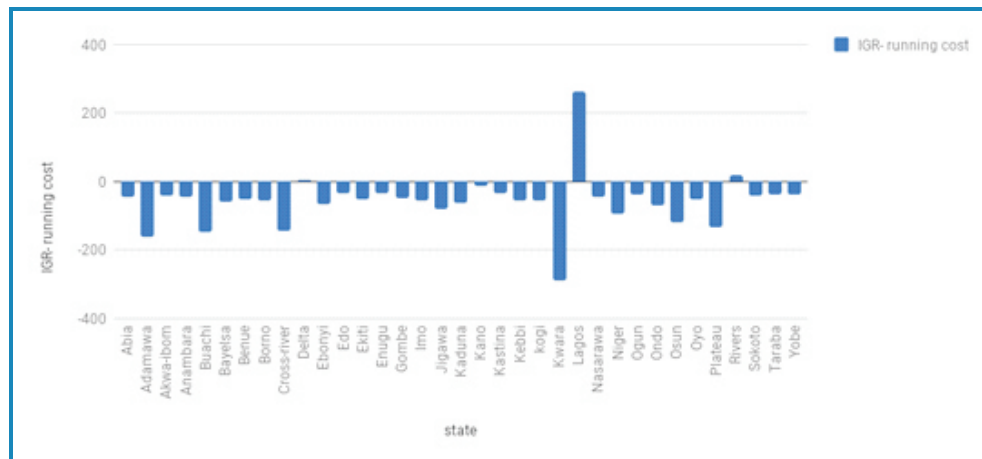
- It explains the strength of state governments to meet their fiscal obligation, especially interest expense in the absence of statutory allocation. The index also captures the strength of internal shock absorber, in scenario where the center is a cash crunch. It forms part of the matrix on how risk premium is determined on the sub national level.

Table 9: Recurrent and IGR across States

State	Recurrent Expenditure Billion (N)	2016 IGR Billion (N)	IGR minus Recurrent expenditure Billion (N)
Abia	57.36	13.35	-44.01
Adamawa	169.32	7.59	-161.73
Akwa-ibom	56.64	16.59	-40.05
Anambara	58.8	14.79	-44.01
Bauchi	155.16	6.22	-148.94
Bayelsa	66.36	7.41	-58.95
Benue	59.64	8.88	-50.76
Borno	56.76	2.52	-54.24
Cross-river	158.04	13.54	-144.5
Delta	40.2	44.89	4.69
Ebonyi	76.56	11.03	-65.53
Edo	55.08	20.67	-34.41
Ekiti	55.2	2.38	-52.82
Enugu	46.92	12.67	-34.25
Gombe	53.76	3.57	-50.19
Imo	61.92	5.43	-56.49
Jigawa	83.52	3.34	-80.18
Kaduna	79.44	15.5	-63.94
Kano	47.76	34.46	-13.3
Kastina	40.2	5.51	-34.69
Kebbi	58.68	3.13	-55.55
Kogi	64.32	7.58	-56.74
Kwara	305.28	16.46	-288.82
Lagos	38.64	301.92	263.28
Nasarawa	48	2.094	-45.906
Niger	102	5.76	-96.24
Ogun	95.16	56.28	-38.88
Ondo	75.84	7.78	-68.06
Osun	127.56	8.96	-118.6
Oyo	69.36	15.66	-53.7
Plateau	141	9.09	-131.91
Rivers	62.4	82.101	19.701
Sokoto	49.32	6.22	-43.1
Taraba	41.88	4.105	-37.775
Yobe	41.04	3.8	-37.24

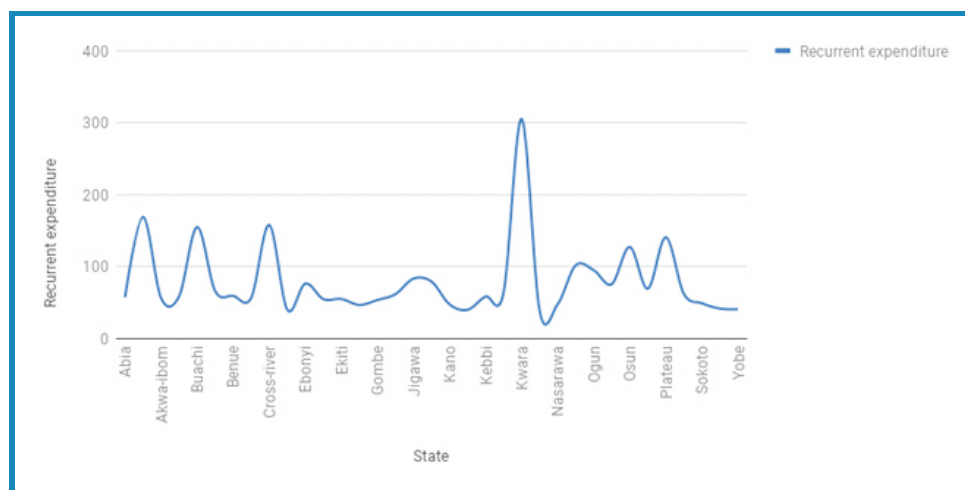
Source: OAF, Budget IT

Fig21: Index's Capture of Recurrent Expenditure



- Only states like Lagos, Rivers and Delta can survive in the absence of federal allocation, evidently 33 states cannot be ran without federal government support
- The index capture validate the earlier position that states with limited private participation are vulnerable to high recurrent expenditure, especially personnel cost.
- The growth in recurrent expenditure has outpaced the growth of IGR in most states
- It not surprising that Lagos and rivers state have lower risk premium compare to the other states
- Lastly states with a negative index capture have higher risk of defaulting on their interest obligation: thus reflective of a low fiscal sustainability
- At the same time the measure reinforces the position that limited private presence in states ends up into higher recurrent expenditure. As state governments try to fill the vacuum, with regards job creation.

Fig 22: Recurrent expenditure across states



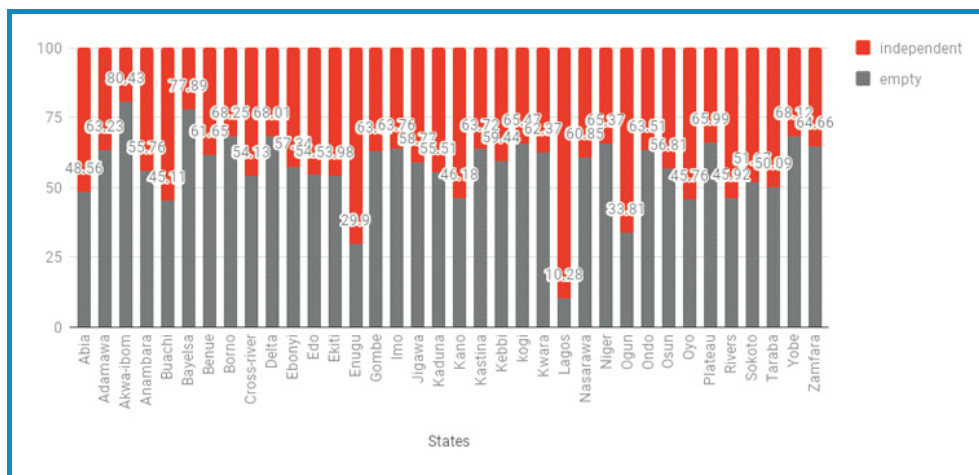
Key Findings

- Output across most states are low, which underlines relatively low private participation in most states.
- There is a more disperse distribution of domestic debt compare to the external debt; A third of external debt is held by Lagos alone.
- Osun states has the highest debt to output at 22%, higher than the national debt to GDP.
- States likes Cross-river and Ekiti have debt levels which are not sustainable, given its tax's base.

- The size of recurrent expenditure in Kwara state reduces room for capital expenditure, measure that requires deflating recurrent expenditure are needed expeditiously.

- There is a divergence between the trajectory of Lagos debt and all the other states

Fig 23: Dependency Level



Source: NBS

- The average dependency ratio on statutory allocation by all states is 56.6%

- The average dependency ratio in oil producing areas is 61.83%, except Rivers which has a 45% dependency on federal allocation

- State debts have grown faster than both GDP and money supply

- Rivers state still have room to boost its income, given the size of its output. The oil sector just comprises 21.74% of Rivers economy; it still has huge taxable income untapped.

- Certainly, revenue generation remains weak as VAT base is largely fallow: moreover recurrent have

grown faster than IGR.

- Statutory allocation just make up 10.8%, making it largely immune to shocks from statutory allocation

- States which have their debt to revenue below the total state average have both reached their borrowing limit and have gone beyond the net income threshold.

- States where there are limited private presence like Ekiti and Jigawa have a lean taxable population.

- The index capture reflects weak fiscal management and widely dented revenue quality across most states.

- Even though external debt to GDP stand low, however the still stand exposed to inflaming debt levels due to currency shocks.

- The states have limited fiscal multipliers, automatically fiscal adjustment take off when resources

are limited. The nonpayment of salaries justifies such position and more importantly they rely on the center to provide an automatic stabilizer.

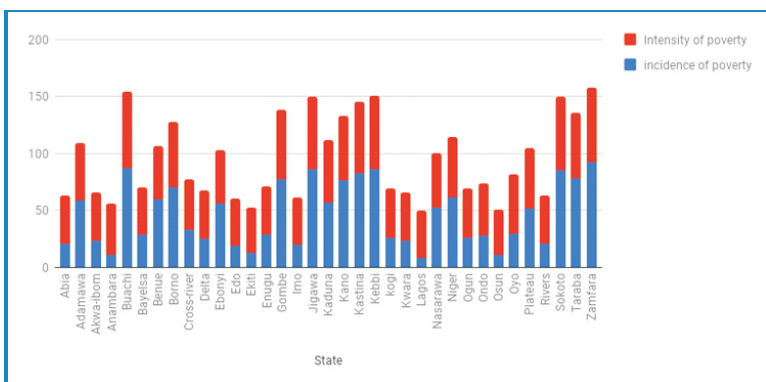
Measures

Short – Medium

- States with low output need drastic measures to drive output, by addressing individual structural constrains.
- There is a need to increase revenue by improving their IGR pool.
- States need to identify and improve their competitive advantage.
- States like Osun have to reduce its debt levels, at the same time improve private participation in the state.
- States where their economies are agriculture driven like Sokoto, Jigawa, Benue, Zamfara and Ekiti need to improve rural roads. As a catalyst for improved productivity.
- Cross river has a high debt to revenue, regardless it has the potential of been a frontier state: improving its agricultural potential in rice coupled with leveraging on it tourism would make it a frontier status.
- States like Akwa- Ibom, Ondo, Bayelsa and Delta need to improve their agricultural sector. Especially areas with huge potential in rubber and palm.
- Plateau, debt consumption is huge and it dependency ratio is high. Plateau has huge potential for tourism, solid mineral and Agriculture. Restoring the city to old self as a haven of peace can only assure any form of progress.
- Rivers state has not leveraged enough on its potential VAT pool. States which are agricultural drive have deficiency in taxes generation.

Medium to Long

Fig 24: Multidimensional Poverty Index (MPI) Across States as at 2017



Source: Oxford Depart For International Development

Lastly state governments have to take issues of poverty with more attention by improving their human capacity and widening existing scope of opportunity. States with relatively lower poverty tend to have higher taxable population and lower probability of a dependency ratio.

Moreover, resources are better managed and output improves over time, especially when opportunities are created. In reality the huge dependency and weak revenue in certain states cannot be disconnected from the quality of human capital and poverty rate in such states.

Conclusion

The fall in oil prices exposed the structural fragility of states in terms of revenue generation and their heavy dependence on government. The rise in interest expenses due to currency shocks fused with lean internal revenue, inevitably led to a fall in the gross revenue of most states. Many states find themselves in a scenario, whereby they are struggling with huge debt weight, thus making it hard to spend on productive assets.

It is important that states become more inward looking in order to identify their competencies and improve its competitive advantage. In addition, states such as Ebonyi, Taraba are in desperate need to improve the output capacity.

The combination of high dependency ratio on statutory allocation fused with stunted internal generated revenue has affected the quality of income generated by states. In the short term, states have to improve their IGR and pay more attention to VAT, especially in an economy that is consumption driven. Properly hewed VAT could reduce the gap.

In the long run, states must begin to invest in human capital, research and development and reduce poverty rate. Such policies increase the taxable population, resource management and improve output.

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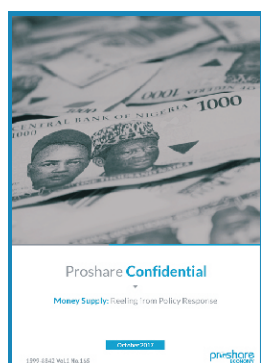
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