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What about the 2015 Budget?

"A budget is telling your money where to go instead of wondering where it went." – Dave Ramsey

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In Brief

The 2015 Budget of the Federal Government of Nigeria (FGN) was presented to the National Assembly on 17 December 2014. Described as "A Transition Budget", the focus will be on "managing the revenue challenge in a manner that protects the most vulnerable while safely transiting to broader based non-oil driven economy".

Highlights	2015	2014	Change
Crude oil indices:			
- Price per barrel (benchmark price)	$65.00	$77.50	-16.1%
- Daily production (mbpd)	2.28	2.39	-4.6%
Aggregate Revenue FGN (₦ billion)	**3,602**	**3,731**	**-3.5%**
Expenditure Profile:			
- Recurrent (non-debt)	2,616	2,469	6.0%
- Capital (including SURE P)	634	1,120	-43.4%
- Debt service	943	712	32.4%
- Statutory transfers	412	409	0.7%
- Subsidy reinvestment program (SURE P)	103	268	-61.8%
Aggregate Expenditure FGN (₦ billion)	**4,358**	**4,725**	**-7.8%**
GDP Growth rate (budgeted)	5.50%	6.20%	-11.3%
US$ Exchange rate	165	160	3.1%
Fiscal deficit (% of GDP)	-0.79%	-1.24%	-36.3%

Why is budgeting so important?

When you fail to plan then you are invariably planning to fail. Without a plan of expected revenue from various sources and the allocations between competing demands, it is impossible to run a successful government. While planning does not guarantee success, failure to properly plan guarantees failure. According to the American financial author - Dave Ramsey, a budget is telling your money where to go instead of wondering where it went.

Where does the money come from?

Government revenue comes mainly from oil and taxes. Nigeria relies heavily on crude oil revenue to fund government spending. For the federal government (FG) only, the Budget proposal has aggregate revenue of ₦3.602 trillion made up of oil revenue of ₦1.918 trillion and non-oil revenues of ₦1.684 trillion (implying a ratio of 53% oil revenues to 47% non-oil). The oil revenue is made up of proceeds from Nigeria's crude sale as well as royalty and petroleum profit taxes from oil companies. Non-oil revenue which is mainly other taxes includes companies income tax, capital gains tax, share of value added tax and customs duties.

Total revenue collection is over N10 trillion (including amounts to be shared to states and local government). For states, their revenues come from share of oil revenue and internally generated revenue mostly personal income tax and land taxes. Due to the heavy reliance on revenue sharing from the centre, the decline in oil revenue has significant implications for states. Unfortunately we do not pay sufficient attention to budgeting at the states level. Who knows what crude oil benchmark they based their 2015 budgets on?

Where does the money go?

The FG has proposed an aggregate expenditure of ₦4.358 trillion for 2015. This expenditure figure consists of ₦412 billion for Statutory Transfers (for the National Assembly, Judiciary etc.), ₦943 billion to service debts, ₦2,616 billion for Recurrent (personnel cost and running expenses) and ₦634 billion for Capital Expenditure (development projects inclusive of SURE-P). The broad expense headings are similar at the states level.

Compared to 2014, total expenditure is down by 8% while recurrent expenditure is up by 6.5% and a significant decline in capital expenditure by 43%.

Government plans to curb recurrent expenditure through cuts in international travels and training, reduce nonessential administrative expenditure, and rationalisation of agencies. It was reported that ₦185.4 billion has been saved from these measures and over 60,450 ghost workers have been weeded from 359 ministries, departments and agencies.

Although these are commendable steps, more drastic measures are required to make a real impact and reverse the trend of increasing recurrent expenditure and decline in capital expenditure. This will require making difficult decisions and reassessing the expenditure profiles of all arms of government especially the Executive and the Legislature.

The proposed increase in debt service expenditure is 32.4% compared to 20.3 % in the 2014 Budget estimate. The cost of servicing debt has been on the increase in the past three years and is expected to gulp about 26% of 2015 aggregate revenue of the federal government. The national Debt Management Office attributed the high debt profile to six factors: Inefficient trade and exchange rate policies, unfavourable exchange rate movements, unfavourable interest rate movements, poor lending and inefficient loan utilisation, poor debt management practices, and accumulation of arrears and penalties.

Given that the budget deficit as currently proposed (₦755 billion) is more than the capital expenditure budget (₦ 633 billion), this means government will have to borrow to fund even part of recurrent expenditure.

Even though Nigeria's overall debt to GDP ratio is well below the global benchmark, it is a source of concern to see that debt service to projected government revenue for 2015 is about 26%. Put differently, we will spend about a quarter of our earnings (₦943 billion) to service debt, much more than the entire budget for capital expenditure of ₦633 billion. In my view this is the true measure of Nigeria's debt burden and a reflection of our capacity or lack thereof to increase borrowing. We really should not be comparing ourselves with other countries on the basis of debt to GDP ratio given that many of those countries borrow at close to 0% interest rate and therefore have lower debt burden.

What are the assumptions?

The FG projected a GDP growth rate of 5.5% for 2015 down from over 6% from 2014. Despite the significant decline in oil prices from about $115 per barrel in June 2014 to now below $50 per barrel, the 2015 Budget is still based on a benchmark of $65 per barrel on the expectation that crude oil prices are expected to average about $65 to $70 in 2015. Oil prices continue to fall but that is not the only concern, daily production is estimated at 2.28 mbpd down from 2.39 mbpd estimated for 2014. This is further compounded by production failures, spillages and high bunkering and theft placing downward pressure on volumes. Some reports say Nigeria currently has unsold cargoes no thanks to the heated oversupply in the global market and cooling demand fundamentals.

In terms of exchange rate, the CBN devalued the Naira by about 8% moving the midpoint from ₦155/US$ to ₦168/US$. The exchange rate in the 2015 Budget is however pegged at ₦165 to USD 1 compared to ₦160 in the 2014 Budget. It is not certain how the Naira can be sustained within the target exchange rate band considering current rate of about ₦190/US$ and a possible further decline in oil prices.

Can we raise more money from tax?

Possibly! Nigeria's tax to GDP ratio is reported as 6% (excluding oil) in the Budget presentation compared to over 20% in most countries. To close the tax gap, government plans to review existing tax waivers and exemptions especially pioneer status. In addition, the Debt Enforcement and Special Prosecution Unit of the FIRS has been very active resorting to tax raids and arrests to enforce full tax compliance. There are plans to increase VAT rate to at least 10% and government wants to ensure that various agencies remit funds collected by them.

And there is luxury tax imposed on certain items by way of special levies. Details of these surcharges are as follows:

- Purchase of new Private Jets will be subject to a 10% import surcharge
- Purchase of luxury Yachts will be subject to a 39% import surcharge
- Purchase of luxury cars will be subject to a 5% import surcharge
- Purchase of champagnes, wines and spirits will be subject to a 3% luxury surcharge
- 1% FCT Mansion Tax on residential properties with value of ₦300 million and above
- There will also be a surcharge on Business and First Class tickets on Airlines.

To truly raise tax revenue, government must adopt a broad base approach that simplifies the tax system, encourages voluntary compliance, expands the tax base and sanctions defaulters regardless of their status in the society.

Government should have taken advantage of the low oil prices to fully deregulate the sector. This will help address the much talked about subsidy corruption and rather than the recent reduction in the regulated pump price of petrol which only benefits the middle class and the rich with little or no impact on the poor as savings are not passed on to consumers by way of lower fares and prices of goods and services. Any measure that enriches only the middle class and the rich but leaves out the poor is unequitable because it increases inequality.

Where do we go from here?

There is no doubt that government at all levels will have less money to spend in 2015. However, the good news is that the most impactful changes do not require money – what they require is common sense and a political will. For instance when GSM was introduced, not only did it cost government close to nothing, it generated billions of Naira in revenue into government coffers.

This is the time for genuine reforms in various sectors to improve the ease of doing business from 170 out of 189 countries according to the World Bank and Nigeria's competitiveness from 127 out of 144 according to the World Economic Forum. Different areas requiring reforms to truly diversify the economy include Agriculture, Power, Transportation, Housing, Insurance, Manufacturing, Tourism, Oil & Gas, Solid Minerals, Creative Industries, Information and Communication Technology.

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