Nigeria

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- **Nigeria's first 50 years were characterised by weak per-capita income growth**
- **Over the next 50 years, the demographic dividend should finally set in**
- **We assess the reform environment to see if enough is in place to make this happen**

Time for the demographic dividend

Nigeria comes of age

Nigeria's population continues to grow rapidly, but the demographic dividend, which depends on the age structure of the population, is only just setting in

Nigeria's 50th post-independence anniversary provides an opportunity to take stock. The population has grown rapidly, to over 150mn today from 45mn in 1960, and is expected to stabilise eventually between 250mn-300mn. Yet due in part to this rapid population surge, and in part to a chequered growth history prior to recent reforms, Nigerian per-capita income has performed poorly. The 1980 level (USD 885) was only reached again in 2005, following an oil-price boost to GDP. For much of the 1980s and 1990s, per-capita income languished between USD 200-300. The recent record has been more encouraging, with per-capita income now at USD 1,370. Optimistically, it is projected to rise to USD 1,840 in five years' time. By then, Nigeria will have added another 23mn to its population.

Declining youth dependency and a higher working-age population should boost Nigerian growth in the years ahead

This increased growth optimism lies partly in Nigeria's expected demographic dividend. Given its traditionally high youth dependency, Nigeria's rapid population growth has not always supported economic growth. But with evidence of falling fertility rates as incomes rise, the age structure of the population is set to change positively in the years ahead. Dependency ratios will decline, with the working-age population making up a larger proportion of the total population. Over the next 50 years, demographic factors alone should start to make a much more meaningful contribution to GDP growth, reinforced by faster urbanisation. There is much at stake. This could be Nigeria's moment – a time when growth accelerates and the economy experiences positive structural change. Alternatively, if the necessary institutional and economic backdrop is not in place, there may be a high threat of social exclusion stemming from demographic change. Below, we assess key reforms for clues on where we might be heading.

The ability to provide meaningful employment to an expanding labour force will be key; labour-intensive manufacturing will require a power sector that works

Power-sector reforms. If there were a single 'make or break' factor driving growth, it would be planned power-sector reforms. Nigeria's current power-generating capacity is estimated at less than 6,000MW; as a result, much of the country's manufacturing capacity is idle. In order to make more of its demographic dividend, Nigeria will need to generate many more jobs to absorb excess labour. With a rapidly urbanising population, growth in agriculture alone will not deliver what is needed. The resource sector is too capital-intensive to make a difference. But with increased power supply, manufacturing firms might run multiple shifts, potentially tripling the number of people employed. Recent reforms allowing for greater private involvement in the power sector are potentially significant. Powerful vested interests have so far resisted any meaningful change, and with elections on the way, many observers will want to see evidence that 'reforms' go beyond the near-term opportunity for increased political patronage. So far, the signs are encouraging.

Nigeria (con'd)

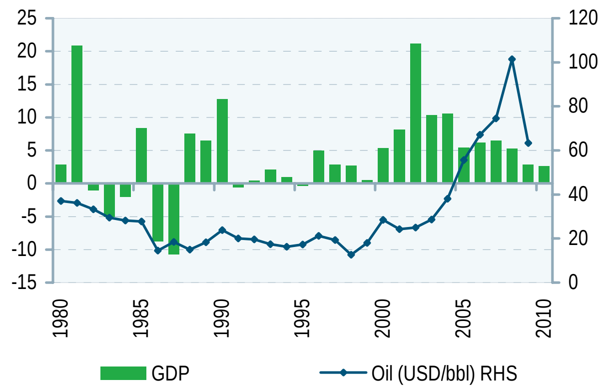
After significant fiscal slippage, efforts to institutionalise oil savings are encouraging, but Nigeria needs to do much more to boost non-oil revenue

Saving the oil windfall for future generations. Nigeria's record on fiscal policy has been mixed. While measures put in place in 2004 to save oil windfalls were positive, the depletion of 'excess crude' savings following the global crisis was not. Some argue that this was a necessary counter-cyclical rebalancing, preventing much larger deficits, but oil is not a renewable resource, and the spending created little lasting benefit. With the federal government budget alone now over USD 30bn, the quality of spending remains important. Private spending is thought to account for 90% of total spending on health and education. Nigeria's human development indicators (HDI) are poor, with the country ranking 167th out of 176 states on life expectancy. Under Nigeria's 13% derivation principle, oil-producing states get a higher share of revenue per capita, but their HDI results are particularly weak, and compare unfavourably with states that are more reliant on other internally generated revenue. Efforts to look more closely at the quality of spending, set a ceiling on the monthly 'FAAC' allocation (revenue shared by the three tiers of government), and institutionalise the savings of future oil windfalls by establishing a sovereign wealth fund are potentially encouraging.

Growth in Nigeria's pension savings provides a significant pool of investible funds; pension reforms will allow a proportion of these savings to be allocated directly to the real economy for long-term lending

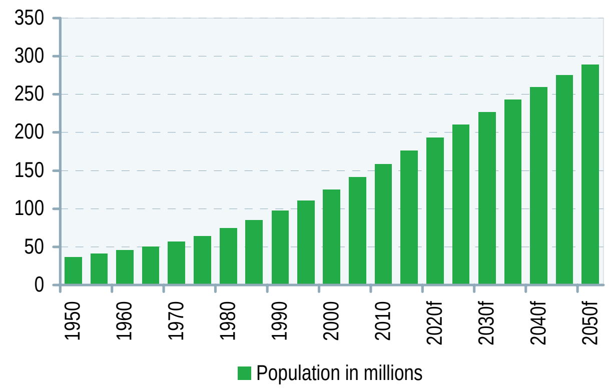
Banking, pension and other regulatory reforms. Banking-sector consolidation (ostensibly to facilitate bank regulation) and higher minimum capital requirements did not prevent the onset of a banking-sector crisis within 3.5 years of these reforms taking effect. There is little evidence that Nigeria's 'one size fits all' capital requirement worked, and excessive capital possibly contributed to excessive risk-taking by some institutions. With only 20% of Nigerians estimated to have access to financial services today, the end of universal banking – and the introduction of different minimum capital requirements for different types of financial institutions – may be a step in the right direction. A tighter regulatory framework to restore depositors' confidence in banks should also pay dividends in the longer term, although it will not – on its own – overcome the greater risk aversion currently gripping the sector. From this perspective, reforms to make a proportion of Nigeria's rapidly growing pension-sector assets available for long-term financing are positive, as is the recent effort to tighten regulation of the country's capital markets.

Chart 1: Oil booms and Nigerian growth



Source: IMF

Chart 2: Nigeria's population growth



Source: UN