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Public Expenditure Profile and Economic Growth in Nigeria: A Cointegration Approach

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Background of the Study

Governments, the world over expend resources in the economy to achieve certain macro-economic objectives. Prime issues are the provision of infrastructure, which enhances employment and productivity and improvement in the general well being of the people to catalyse the economy towards optimal growth level.

The expenditure incurred by public authorities like Federal, state and local governments for the provision of public goods to satisfy the collective social wants of the people is known as public expenditure. It can be referred to as the funds expended by local, state and federal government and its agencies and distinct from that of households and firms. Anyafor (1996) referred to expenditure as an actual payment or the creation of obligation to make a future payment for some benefits, items or service received. Expenditure can be classified into two broad categories: Capital Expenditure and Recurrent expenditure.

Capital Expenditure are expenses on capital projects like roads airports education, telecommunication, electricity generation, etc., while Recurrent Expenditure are government spendings on administration in the form of wages and salaries, interest on loans maintenance, transfer payments and so on. Public expenditure is vital in the process of macro economic stability because it is an important fiscal tool and can be used to manipulate or manage the economy (Begg et al (1984).

In Nigeria government expenditure has nominally been on the increase due to oil revenue which is now the mainstay of the Nigerian economy. This over dependence on extractive industry and commodity export (traditional capital) characterize not only the Nigerian economy but also other sub-Saharan Africa. This reinforces the need to review the public expenditure structure in these countries since the success of government fiscal policy implementation depends upon efficient public expenditure management and also the effectiveness of Government's fiscal measures/operations is seen against the back drop of the extent to which they help in achieving the macro-economic objectives.

A cursory look at the expenditure profile in Nigeria reveals that the proportion of recurrent expenditure to the total expenditure stood at 68%, 60% and 70% in 2007, 2008 and 2009 respectively while apportioning very poor proportion to capital expenditure. This poor public expenditure management seems to account for unemployment, high level of poverty lack of visible development in terms of physical infrastructure, and other facilities that aid economic growth. Ogwuru (2008) suggested a reduction in the funds allocated to recurrent expenditure in order to reduce unemployment in Nigeria. The spate of complaints of poor infrastructure relative to the huge oil revenue in Nigeria has led to the question concerning the benefit of public expenditures in this country. Nevertheless, this study sets out to determine empirically the extent of public expenditure impact on the growth of Nigerian economy.

Trends in Nigeria's Public Expenditure

Government expenditure in Nigeria has been increasing very significantly since 1960. This increase has been due to a number of social, political and economic factors which greatly increased the level of government activity. During the 1950's the total government expenditure was on the average about 8.17 per cent of the GDP but with the coming of political independence in 1960, (between 1959 and 1962) total government expenditure rose to an average of about 15 percent of GDP. For the whole period of 1960s, it was 11.4 percent, 16.1 percent in 1970s and 41.8 percent between 1980 and 1985 (Okpara, 2008).

Apart from the role of civil war financing in increasing public expenditure, the oil boom of 1970s raised the ability of the government to finance its expenditures. Thus, growth of public expenditure that time became rapid. For the first time in Nigeria, total government expenditure exceeded revenue in 1971. By 1972, the budget deficits of the federal government as a proportion of total estimate revenue became 32.7 percent.

Phenomenal increases in expenditure occurred between 1973 and 1976 and these increases were 70 percent in 1975 and 47 percent in 1976. Consequently, the average growth rate of government expenditure rose about 19 percent in the 1970. This, however, declined to about 12.8, 1983 and 1984. Between 1980 and 1985, the budget deficits of the federal government as a proportion of total estimated revenue rose to an average of 37.6 percent. For the whole period, there was no year the government was able to balance its budget (see Okpara, 2008). Thus, from 1980 till the recent day, the expenditure trend is on the increase. Every component of the expenditure structure has an upward trend that most often, government spending exceeds its revenue.

However, the consistent growth of government expenditure has been at a reducing rate relative to GDP growth that has been increasing at an increasing rate. This development accounts for fluctuations in the government expenditure-GDP ratio in Nigeria. On the average, the ratio of expenditure to GDP from 1970 to 1979 stood at 21% which it still maintained in the period 1980 to 1989 but dropped to 19.6% in 1990 to 1999 and further reduced to 13.1% between the year 2000 to 2010. The trends of the GDP at current basic prices, recurrent and capital expenditure, total expenditure and the ratio of expenditure to GDP are presented in table 2.2 as follows.

Table 1: PUBLIC EXPENDITURE AS A RATIO OF GDP

	GDP AT CURRENT BASIC PRICES	RECURRENT EXP.	CAPITAL EXP.	TOTAL EXP.	RATIO OF EXPENDITURE TO GDP
1970	5281.1	716.10	187.8	903.90	17.1 %
1971	6650.9	823.6	173.6	997.20	15%
1972	7187.5	1012.30	451.3	1463.60	20%
1973	8630.5	963.50	565.7	1529.20	18%
1974	18823.1	1517.10	1223.5	2740.60	15%
1975	21475.2	2734.90	3207.7	5942.60	28%
1976	26655.8	3815.40	4041.3	7856.7	29%
1977	31520.3	3819.20	5004.6	8823.8	28%
1978	36540.1	2800.00	5200.0	8000.0	22%
1979	41974.7	3187.20	4219.5	7406.7	18%

1980	49632.3	4805.20	10163.4	14968.6	30%
1981	47619.7	4846.7	6567.0	11413.7	23%
1982	49069.3	5506.0	6417.2	11923.2	24%
1983	53107.4	4750.8	4885.7	9636.50	18%
1984	59622.5	5827.5	4100.1	9927.6	16%
1985	67908.6	7576.4	5464.7	13041.1	19%
1986	69147.0	7696.9	8526.8	16223.70	23%
1987	105222.8	15646.2	6372.5	22018.70	20%
1988	139085.3	19409.4	8340.1	27749.50	19%
1989	216797.5	25994.9	15034.1	41028.30	18%
1990	267550.0	36219.6	24048.6	60268.20	22%
1991	312139.7	38243.5	28340.9	66584.40	21%
1992	532613.8	53034.1	39763.3	92797.40	17%
1993	683869.8	136727.1	54501.8	233806.50	34%
1994	899863.2	89974.9	70918.3	160893.20	17%
1995	1933211.6	127679.8	121138.3	248768.10	12%
1996	2702719.1	124491.3	212926.3	337217.60	12%
1997	2801972.6	158563.5	269651.7	4828215.20	15%
1998	2708430.9	178097.8	309015.6	487113.40	17%
1999	3194015	449662.4	498027.6	947690	29%
2000	4582127.3	461600.0	239450.9	701059.40	15%
2001	4725086.0	579300.0	438696.5	1017996.50	21%
2002	6912381.3	696800.0	321378.1	1018178.10	14%
2003	8487031.6	984300.0	241688.3	1225988.30	14%
2004	11411066.9	1032700.0	351300.0	1384000	12%
2005	14572239.1	1223700.0	519500.0	1743200	11%
2006	18564594.7	1290201.9	552385.8	1042587.7	9%
2007	20657317.7	1589270.0	759323.0	2348593	11%
2008	24296329.3	2117400.0	960900.0	3078300	12%
2009	24712669.9	2131906.0	1152796.6	3254702.6	13%
2010	29,108,000	3109000	883900.00	3992900	13%

Source: Computed from statistical bulletin and CBN annual and statement of account 2010.

Review of Related Literature

Public expenditure represents the funds expended by government for its own maintenance, the maintenance of the society and the running of the economy in general. It also includes amounts incurred for helping other countries. (Okpara, 2002). The basic rationale for government expenditure is associated with the existence of market failure. Without market failure, there will be no reason to assume that additional public sector investment would be more productive than the private sector investment (Teshome, 2006). Musgrave and Musgrave (2010) in articulating the basis of the public sector intervention in the management of the economy for sustainable economic growth and development argued that market mechanism alone cannot perform economic functions. The public sector was expected to fund, from the public treasury, the social overheads necessary to make the life of its citizens easier.

Barro (1990) categorized government expenditure as productive and non productive. Productive government spending would include the resources devoted to property rights reinforcements, as well as activities that enter directly into production function. On the other hand those expenditures that could not enter into production function (e.g. government consumption services) are considered unproductive. Following Barro's approach, Bleaney et al (2001) classified general public service expenditure such as defence expenditure, educational expenditure, health expenditure, housing expenditure, and transport and communication expenditure as productive expenditures. Health and Education spending is treated as investment because they add to the quality of human capital stock. They further classified social security and welfare expenditure, expenditure on recreation, and expenditure on economic services as unproductive expenditure.

Okpara (2002) however noted that another area where government expenditure is deployed is the payment for factor services. Heavy financial outlays are used yearly by government to buy factor services. It has been noted that the public sector in the developing economies are major employers of labour. He pointed out that this phenomenon is not strange in Nigeria where it has been observed that personnel component of the annual recurrent expenditure is very high (Okpara 2002). Addition to value is done by personnel who are therefore productive and as such recurrent expenditures are also productive. A cut in investment spending on productive new capital projects or reduction in outlays for maintaining the existing capital stock may reduce growth prospect in the economy (Ke-Young Chu et al, 1999). Another way to view expenditure cut, is in civil service salary reduction.

A sharp cut in real wages in the public sector can lower the productivity of the public sector work force and are unlikely to be sustainable. The outcome of such wage cuts may be absenteeism, low performance at the work place, dereliction and other vices that are inimical to the growth of the economy.

Maku (2009) observed that the mechanism through which government spending on public infrastructure is expected to affect the pace of economic growth depends largely on the precise form and size of total public expenditure allocated to economic and social development projects in the economy. He however believed that public expenditure on social and economic infrastructure in education, health, transportation, communication, waste disposal, water, electricity, and sanitation etc., can contribute to the performance of the economy in the following ways;

- Promotion of infant industries in the country
- Reduction in the unemployment rate
- Stabilization of the general prices in the country
- Reduction in the poverty rate and increase in the standard of living of the people
- Promotion of higher productivity through efficient utiliza tion of factor inputs

Ram (1986) using cross section data for a larger sample of 115 countries and time-series data (1960-1980) for 17 individual countries to see the effect of government size on economic growth and employing OLS on the premise of a first-order auto-regressive disturbance term (AR1) for some countries from time series data arrived at the following major results: firstly, the overall impact of government size on growth is positive in almost all cases; secondly, the (marginal) externality effect of government size is generally positive; thirdly, although the number of time series observations for each country is relatively small, there is a broad harmony between the estimates obtained from cross section and time-series data; and fourthly, it is possible that the positive effect of government size on growth is stronger in lower income contexts.

Ram (2008) who carried out a panel data study of 154 countries from 1960 -2000 and found significant effect of public expenditure on goods and services, once country size is controlled. Ghosh and Gregoriou (2008) analysed panel data from fifteen developing countries for twenty eight (28) years and found that current spending exerts positive impact on growth, while capital spending impacted on growth negatively.

Empirical results have however presented mixed results on the impact of government expenditures on economic growth.

Devarajan and Vinay (1993) using panel data for 14 developed countries (1970-1990) and applying method of OLS on 5-year moving average while taking various functional types of expenditure (health, education, transport, etc) as explanatory variables found that health, transport and communication have significant positive effect while education and defense have a negative impact on economic growth.

Alexander (1990) applied OLS method for sample of 13 Organization for Economic Cooperation and Development (OECD) countries panel (1959-84) and found that the growth of government spending and inflation have significant negative impact on economic growth. Also Landau (1983), Uwatt (2006), and Baro (1991), in their study discovered a negative relationship between government size and economic growth.

Mitchell (2005) evaluated the impact of government spending on economic performance in developed countries. He assessed the international evidence, reviewed the latest academic re-

search, cited examples of countries that have significantly reduced government spending as a share of national output and analyzed the economic consequences of these reforms and eventually concluded in his empirical study that a large and growing government are not conducive to better economic performance.

Schaltergger and Torgler (2007) carried out studies on the relationship between government size and economic growth between 1981 and 2001, using Switzerland as a test case and found a negative relationship between government size and economic growth. Afonso and Gonzalez-Alegre (2008) empirically examined the relationship between the composition of expenditure and revenue and economic growth for a sample of twenty seven (27) European Union (EU) members from 1971 to 2005. The results from their study indicate that there were differences in the relationship between government spending and growth, among the EU members.

In Nigeria studies also abound on government expenditure and economic growth. For example Oyinlola (1993), reported that there is a positive impact of government expenditure on defence and economic growth. Ogiogoi (1995), carried out a study of Nigeria and discovered a long term effect of government expenditure on economic growth. He equally found out that recurrent expenditure impacted economic growth more than capital expenditure.

Olukayode (2009) undertook a study of government expenditure and economic growth in Nigeria using time series data to analyse Ram (1986) model, he developed variants of Ram (1986) model regressing Real GDP on private investment and consumption spending, human capital investment, Government investment and consumption spending at absolute level and found out that private and public investments have insignificant effect on economic growth during the period under review, which is 1977 to 2006.

Okpara (2009) observed that increases in expenditure had immediate and inevitable influence on the level and structure of aggregate demand and consequently increased the overall level of employment and prices. Deducing from his empirical analysis, he concluded that increased government expenditure may lead to provision of social goods and services and thereby increasing aggregate output to circumvent supply shortages and reduce inflation. He also submitted that government expenditure in the form of subsidies and indirect expenditures in the form of tax holidays are capable of boosting output of goods and services to curtail supply shortages and reduce inflation.

Abu, et al (2010), observed that rising government expenditure has not translated to meaningful development as Nigeria still ranks among the poorest countries. However, Olapede (2010), viewed public expenditure and economic growth through a different prism. He investigated impact of government expenditure on economic growth and development using Nigeria as a test case, and noted that despite huge amounts of funds allocated to capital expenditure such as infrastructural facility in education sector like the Universal Basic Education projects, road construction and maintenance; there has been little to show for the huge allocation, especially in the southern states. Udah (2010) equally observed that government size did not compliment private investment initiative in Nigeria.

Ogwuru (2009) in his study of government expenditure and unemployment problem in Nigeria concluded that capital expenditure was significant in reducing unemployment while recurrent expenditure was not. He noted that, that was an indication that the large sum of funds allocated to recurrent federal government expenditure did not have a reducing effect on unemployment.

3.0 Methodological Framework

The study sourced data on government expenditures and gross domestic product (GDP) from the statistical bulletin of the Central Bank of Nigeria. To circumvent the possibility of spurious results, stationarity test was carried out using the Augmented Dickey Fuller unit root test.

Non stationary data are not asymptotically consistent with the notion of convergence which is necessary for the series to be non-spurious. The use of non-stationary variable(s) in a given model then leads to the "spurious regression phenomenon" discussed by Granger and Newbold (1974), and Phillips (1986). Since most macroeconomics time series variables exhibit non-stationarity behaviour, capable of invalidating the quality of empirical inference drawn from such estimates if appropriate measures were not taken, it becomes imperative that the unit root test which is an instrument for guarding against the pitfall of spurious regression result arising from non-stationary time-series variables is used (Isu and Okpara, 2013). The cointegration and error correction model techniques were employed for determination and evaluation of the parameter estimates of the variables.

The model and its error correction model for the analysis are formulated in implicit and explicit forms as follows:

GDP=G(GovtExp, HEXP, EDEXP, TCEXP, DEXP) (1)
GGovtExp, GHEXP, GEDexp, GTCExp, GDExp > 0
GDP = λ0+λ1GovtExp+λ2HEXP+λ3EDEXP+λ4TCEXP+λ5DEXP+ECTt-1+u1t (2)
GGovtExp, GHEXP, GEDexp, GTCExp, GDExp > 0

Government expenditure and its components as indicated under each of the functional relationship are by a prori positive to GDP. In other words, each component is expected to exert positive impact on the growth of the economy.

Where:
GDP = Gross domestic product
ExpHealth = health expenditure
EXPEdu = education expenditure
TransCmExp = transport and communication expenditure
ExpDefence = defence expenditure
G,P,I, = Functional notations
λs = Parameters to be estimated
ECT = error correction term
u1t = stochastic term

The unit root tests for the variables are presented in table 2 as follows.

Table 2. Unit Root Test For Nigeria

	Max. Lag	Coefficients	ADF critical values		
	Based on SIC	ADF test 1st difference	1 Percent	5 Percent	Remark
GDP	4	-9.124675	-3.831511	-3.029970	Stationary
Public Expenditure	4	-4.266373	-3.831511	-3.029570	Stationary
ExpEdu	4	-5.232487	-3.83151	-3.029970	Stationary
ExpHealth	4	-5.678935	-3.857386	-3.040391	Stationary
ExpDefence	4	-5.934406	-3.831511	-3.029970	Stationary
TransCmExp	4	-3.728054	-3.831511	-3.029970	Stationary

In order to determine whether there exist any cointegrating vector supporting the existence of long run relationship between

GDP, per capital income and the explanatory variables, the researcher further subjected the variables to Johanson cointegration tests. The results of the cointegration test are presented in table 3 below.

Table 3. Cointergration for GDP

Hypothesise	Trace	0.05			
No. of CE(s)	Eigenvalue		Statistic	Critical	Value rob.**
None*	0.968261		143.8466	95.75366	0.0000
At most1*			0.867269	78.29285	69.81889 0.0090
At most 2	0.596468		39.92367	47.85613	0.2253
At most 3	0.480362		22.68116	29.79707	0.2621
At most 4	0.317739		10.24333	15.49471	0.2625
At most 5	0.145108		2.978820	3.841466	0.0844

Trace test indicates 2 cointegrating eqn(s) at the 0.05 level
*denotes rejection of hypothesis at the 0.5 level
**Mackinnon – Haug-Michelis (1999) p-values

The test shows the presence of two cointegrating equations at 5% critical level for GDP model.

Having established that the variables are stationary and therefore integrated of order I(1) , and also have long run relationship, to capture the short run deviations that might have occurred in the long run cointegrating equations, the researchers estimated the error correction model, which their parsimonious results are presented in table 4 below.

Table 4. Parsimonious Result for Error Correction Model

Dependent Variable: GDPCUS$NIGERIA Method: Least Squares Date: 10/05/12 Time: 07:40 Sample(adjusted): 1993 2010			
Included observations: 18 after adjusting endpoints			
Variable	Coefficient	Std. Error t-Statistic	Prob.
D(GDPCUS$NIGERIA PUBLICEXPENDCUS	1.302809 13.56488	0.307284 4.239760 6.367529 -2.130320	0.0133 0.1002
D(PUBLICEXPENDCU EXPEDU	19.76443 24.19043	6. 683187 2.957336 42.65955 0.567058	0.0417 0.6010
D(EXPEDU(-1)) D(EXPEDU(-2)) EXPHEALTH	47.07843 11.04210 -61. 35555	51.91340 0.906865 30.05116 0.367443 43.44977 -1.412103	0.4158 0.7319 0.2308
D(EXPHEALTH(-1)) D(EXPHEALTH(-2)) EXPDEFENCE	-249.7363 182.1475 159.4798	99.21303 -2.517172 84.97189 -2.143620 70.82996 2.251586	0.0656 0.0987 0.0875
TRANSCMEXP	224.1375	98.87723 2.266826	0.0860
D(TRANSCMEXP(-2)) ECT(-1) C	-62.81524 0.342655 100519.2	39.36257 -1.595811 0.427640 0.801270 61921.37 1.623337	0.1858 0.4679 0.1798
R-squared Adjusted R-squared S.E. of regression Sum squared resid Log likelihood Durbin-Watson stat	0.975755 0.896960 20089.45 1.61E+09 -190.3473 2.120570	Mean dependent var S.D. dependent var Akaike info criterion Schwarz criterion F-statistic Prob(F-statistic)	99405.28 62584.23 22.70526 23.39777 12.38340 0.013105

Source: Computed from Data set for Nigeria

3.1 Discussion of findings.

The above parsimonious result shows that the total public expenditure exerts positive and significant impact on the growth of GDP. A 1% increase in government expenditure brings about 19.76% increase in the growth of GDP. The components of the expenditures such as expenditure on education, health, defence, transport and communication are generally positively related to GDP but could not individually exert significant influence on GDP. The coefficient of determination (R2 = 97.58%) shows that the model is highly fitted. In other words, the explanatory variables, public expenditure and its components, explain about 97.58% of the variations in the dependent variable. The overall regression (F = 12.38) is significant as the probability of 1.3% is less than 5% (1.3% < 5%). The Durbin Watson statistic is approximately 2 which by the rule of thumb indicates absence of autocorrelation.

In the light of the above results, we conclude that the growth of GDP is a positive and significant function of total government expenditure. This finding contradicts the findings of Olukayde (2009), Olapede (2010), Uwatt (2006), and Baro (1991), but corroborates the findings of Oyinlola (1993), Ogiogoi (1995), and (Okpara 2009).

Conclusion

Government expenditure is a tool for providing social overheads and improving the welfare of the society. When government increases its purchase of goods and services, it not only pumps additional funds into the income stream of economic agents but also provides additional infrastructure to the economy. Invariably, this is the aim of the expenditure profile. The achievement of this depends on the way and manner by which the government finances its expenditure. Besides the appropriateness of the choice of financing government expenditure, whether tax financing is appropriate for the economy, money creation financing or debt financing, there is always a challenge of the budgeted expenditure being actually or properly expended. Under normal circumstances therefore, government expenditure is a positive and significant function of the growth of GDP and the general well being of the economy. Our empirical finding lends credence to this assertion. Government in order to impact on the growth and socio-economic well being of its country, should design the appropriate source of financing its expenditure while making sure that the implementation of the expenditures are not distorted by the prevailing evil wind named corruption.

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