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Challenges of Fiscal Policy as an instrument of Economic Stability in Nigeria

[1] Yusuf, M. Senusi,[*] [2] Jibrin Bappah, [3] Hassan D. Aliyu, & [4] Abubakar Ammani

[1] Department of Economics, Federal University, Kashere, Gombe – Nigeria
[2] Federal College of Education (Tech) Gombe, Gombe State – Nigeria
[3] Department of Arts & Social Sciences Education, Federal University Kashere, Gombe – Nigeria
[4] Hassan Usman Katsina Polytechniq, Katsina State - Nigera

[*] Corresponding Author's; E – mail:

Abstract

Fiscal policy as one of the instruments of macroeconomic policy seeks at achieving economic stability of a country It concerns with how government generate taxes and spend such income in order to bring desirable changes in the patterns of governance The purpose of this study was basically to examine the challenges of fiscal policy in ensuring economic stability. This paper employs basically the descriptive method to examine the concept of fiscal policy. It equally identifies the objectives and roles of fiscal policy. The paper further examines fiscal policy as a tool for economic stability. The paper reveals that there are underlining challenges facing fiscal policy. The paper concludes that all the fiscal policy variables need to be effectively employed so as to ensure stability, as without that, the goal of macro-economic stability will be a mirage. The study recommended among others that, the government should ensure a viral and stable economy by adjusting its fiscal instrument to suit current realities.

Keywords: Challenges, Fiscal Policy. Instrument, Economic Stability
JEL Classification:

Contribution to/Originality Knowledge

1.0 Introduction

Nigeria and other countries comparable have continuously predicted for economic stability as a must attained macroeconomic policy in recent times in administering government fiscal policy, taxation and expenditure become central to government. It is a known fact that taxation to a country is inevitable since it helps in attaining certain levels of production, consumption, investment, employment and allocation of socio infrastructure to the public, redistribution of income as well and controlling inflation. In view of the above, taxation becomes a prominent tool of economic stability. On the expenditure, it helps to direct demand and supply towards economic equilibrium among the populace. In the view of Samuelson & (2005), fiscal policy has developed an array of instrument to handle different facets of the economics of the public sector. They further stressed that by the existence of multiplicity of goals it is often bedeviled by inherent conflict of objectives between long term growth and short term stability, between social welfare and economic growth and between redistribution and production incentives. Fiscal policy uses taxation and expenditure its main instrument of stability. Being a non-monetary instrument of stability, Nigeria as a growing economy has not strategized its fiscal policy yield the revenue. One could say that the instrument over the years has been weak in achieving its goal.

Fiscal policy entails revenue generation and expenditure in such a manner that macroeconomic goals of full employment, price and economic stability, high level and sustainable economic efficiency are enhanced. To this end, all economic activities are visited by the government. Fiscal policy is complementary to monetary policy in price stability, reduced production cost, increased private investment and profitability of firms among other variables. The goal of fiscal policy is to enhance socio-economic development by pursuing a policy stance that ensures a sense of balance between taxation, expenditure and borrowing and proper functioning of the economic sectors. Fiscal policy works well in a business environment and Nigeria by virtue of its abundant human and material resources should keep tract with fiscal expectations. However, the continuous negligence and adverse government policy has led to underutilization of these resources. The fundamental elements of economic stability such as full employment, low inflation rate, business boom, prosperity, fall in poverty, availability of economic facilities, are yet to gain improved levels which mostly stemmed from political intolerance rather than human capital. Most of government grandiose policies are nebula in implementation simply because of lack of sincerity of purpose One could say that the government over the years has not translated these tools into meaningful development since taxation and public expenditure have failed in achieving the objectives of proper allocation of resources, controlling inflation, checking of balance of payments, redistribution of income, growing unemployment among others. The paper therefore attempts to examine some of the challenges that constraint the effective use of fiscal policy to enhance economic stability.

2.0 Statement of the Problem

Fiscal policy is means by which a government adjusts its level of spending in other to monitor and influence a nation's economy. It is used along with the monetary policy which the Central Bank of Nigeria to manipulate money supply in the Nation to achieve desirable changes and economic prosperity As it is today in Nigeria, stability is not yet attained. This can be blame to the poor conduct of the fiscal instrument. In support of above, Adewunmi (2012) said the tax process was further exacerbated by poor coordination of fiscal policy among the three tiers of government. He further posits that, there is a weak revenue base arising from high marginal tax rate with very narrow tax base resulting in low tax compliances. As a result of these and other factors such as corruption, poor supervision, serious macroeconomic imbalance has emerged in Nigeria. The study was undertaken to suggest ways that will enhance economic stability having identified the challenges of fiscal policy in Nigeria.

2.1 Theoretical Framework and Literature Review

Various researchers have written different aspects of fiscal policy especially as it relates and affects the macroeconomics of the country. Fiscal policy is defined as the means by which a government adjusts its levels of spending in order to monitor and influence a nation's economy. According to Reem (2009) fiscal policy is based on the theories of British economist John Magnard Keynes whose theory basically states that governments can influence macroeconomic productivity levels by increasing or decreasing tax levels and public spending. This influence, in turn, curbs inflation, increases employment and maintains a healthy value of money.

Various researchers have written on different aspects of fiscal policy especially as it relates to macroeconomic productivity levels. The studies of the effect of public expenditure on the economy has shown a positive relationship Ranjan and Sharma (2008), found negative relationship. However, kormendi and Megure (1995) could not find any relationship.

Adefeso and Mobalaji (2010) wrote on the fiscal-monetary policy and economic growth in Nigeria. Their major objective was to re-estimate and re-examine the relative effectiveness of fiscal and monetary policies on economic growth in Nigeria using annual data from 1970-2007. The Error correction mechanism co- integration technique were employed to analyze the data and draw policy inferences their result showed that the effect of monetary policy is much stronger than fiscal policy. They suggested that there should be more emphasis and reliance on monetary policy for the purpose of economic stabilization in Nigeria. In the same vein. Olawunmi and Ayinka (2007) examined the contribution of fiscal policy in the achievement of sustainable economic stability in Nigeria using slow growth model estimated with the use of ordinary least square method. It was found that fiscal policy has not been effective in the area of promoting sustainable economic stability in Nigeria. They however, stated that factors such as wasteful spending, poor policy implementation and lack of feedback mechanism for implemented policy evident in Nigeria which are indeed capable of hampering the effectiveness, of fiscal policy have made it impossible to come up with such a conclusion.

Omitogun and Ayinla (2007) examined empirically the contribution of fiscal policy in the achievement of sustainable economic growth in Nigeria. They used Solow growth model estimated with the use of ordinary least square method and found out that fiscal policy has not been effective in the area of promoting sustainable economic growth in Nigeria. They suggested that Nigerian government should put a stop to the incessant unproductive foreign borrowing, wasteful spending and uncontrolled money supply and embark on specific policies aimed at achieving increased and sustainable productivity in all sectors of the economy Anerbach (2009) suggested that for fiscal discretionary policy to be practiced on a large-scale attention must be paid to policy design. Fiscal policy can be described as the use of parameters such as taxation, expenditures, budget and national debt that will influence government revenue and spending with a view to achieving macroeconomic objectives which monetary policy also stands to achieve. Anyanwu (2007), refer to fiscal policy as part of government policy concerning the raising revenue through taxation and other means and deciding on the level and pattern of expenditure for the purpose of influencing economic activities or attaining some desirable macroeconomic goals. In essence, fiscal policy is adopted by government primarily to balance the use of resources of the public and private sector and by so doing curtail inflation, unemployment, balance of payment deficits, income disequilibrium and poor allocation of resources among sectors. However, this policy is manipulated, the objective is to ensure stability in economic growth and development and the general price level that could balance between consumption and supply sides of the economy. Fiscal policy according to Siyan and Adebayo (2005) is the one of most powerful tools used by the government to achieve macroeconomic stability of the economy of most developing countries.

In the view of Jhingan (2003), fiscal policy can be seen as a deliberate spending and taxation actions undertaken by government in order to achieve price stability, to dampen the seeing of business circle and to bring about national output and employment to desired levels that can guarantee economic stability. Fiscal policy involves the use of government spending, taxation and borrowing to influence the pattern of economic activities and also the level and growth of aggregate demand, output and employment Fiscal Policy entails government of the economy through the manipulation of its income and spending power to achieve certain desire macroeconomic objectives. (Medee 2011). Olawunmi & Ayinla (2007) opined that fiscal policy has conventionally been associated with the use taxation and public expenditure to influence the level of economic activities.

Economic stability requires a balance on both the demand side and supply side of an economy. The broad objective of macroeconomic policy is to contribute to economic and social wellbeing in an equitable and sustainable manner. Continued and sustained economic growth is not only a precondition for employment generation, but also provides countries the fiscal space to address other critical social concerns such as access to health services, sanitation and safe drinking water among others. Once these are achieved, stability of an economy is sure. Steady and stable economy must be accompanied by low inflation, low interest rates, low unemployment and sound & sustainable public finances to enable government raise investment.

2.2 Objectives of Fiscal Policy

Anyanwu, and Oaikhenan (1995) summarized the objective of fiscal policy in Nigeria to include:

1. Generation of significant revenue for the government with which can provide other services that benefit the entire society.
2. Diversification of revenue sources away from crude oil the entire revenues.
3. Reduction in the tax burden on individuals and organizations.
4. Maintenance of economic equilibrium, particularly to control inflationary pressures, accelerate economic growth, equilibrium balance of payment and full employment.
5. Substantial reduction and elimination of government.
6. Promotion of self-reliance.
7. Effective protection of domestic industries budget deficit.
8. Reduction of the heavy debt on loans, reduction of inequality in incomes and wealth modify consumption pattern and living standards which tend to undermine efficiency.
9. To ensure high productivity in agriculture and high utilization of industrial products.
10. Improving the ensuring transparency and accountability in management of finances.

2.3 Role of Fiscal Policy

Fiscal policy is a veritable tool by which funds are raised to finance socioeconomic infrastructures such as health, education, roads, water, industries and security which when provided can raise the standard of living of both the private and public sectors of the economy.

Taxation as instrument of fiscal policy influences key governance measures ranging from Transparency, accountability, corruption free and more effective expenditures of revenues in budget (Todaro and Smith 2009) they further Stressed that, domestic resource mobilization in the form of progressive tax can strengthen all the economic productive aspects and ultimately tackle the structural causes of poverty. Musgrave & Musgrave (2004) outline the role of fiscal policy to include:

i. The level of taxation affects the level of public savings and thus volume of resources available for capital formation.
ii. Both the level and the structure of taxation affect the level of private savings.
iii. The system of tax incentives and penalties may be designed to influence efficiency of resource utilization.
iv. The distribution of tax burden along with the expenditure benefits play a large part in promoting equitable distribution of incomes.
v. The pattern of taxation on imports and exports relative to that of domestic production will affect the foreign trade balance.
vi. The tax treatment of investment from abroad may affect the volume tax capital inflows and rate of earnings.
vii. Public investment is needed to provide infrastructure type of investment which fiscal policy is an appropriate tool.

2.4 Fiscal Policy Economic Stability in Nigeria

Government taxation and expenditure form bulk of government responsibility t the public. Most stabilization attempts have concentrated on cutting government expenditure to achieve budgetary balance. To achieve this, revenue mobilization to finance government public developmental projects must not be ignored. In the absence of well-organized and locally controlled money market, Nigeria has to rely on fiscal measures so as to stabilize the economy and to mobilize domestic resources. Public expenditure and taxation policies have implications for scope and incidence of government services, for growth and income distribution. There is a consensus that macroeconomic stability is a necessary condition for economic growth and development. Despite substantial increase in public expenditure over the years, the rate of stability has been very low and sluggish to the level one would, say that, sustainable economic growth and stability has remained a mirage. Changes in fiscal policy, or even in monetary policy for that matter, have little potential for stabilizing the economy. Instead, inevitable delays in recognizing economic disturbances, in enacting a fiscal response, and in the economy's reacting to the change in policy can aggravate, rather than diminish, business-cycle fluctuations. The trend can only be change if the variables are properly identified and tackled

2.5 Challenges of Fiscal Policy in Nigeria

Fiscal policy in Nigeria and developing economies over the years have suffered poor implementation, in light of the above, Usman (2008) posits that, the past failure of fiscal policy in Nigeria in contributing to stable economic growth, wealth creation and poverty reduction can better by analyzed within the framework of a common term Natural Resource curse'. This subscribed to the fact that Nigeria is blessed will the resources but fails to translate such wealth to meaningful utilization. In her submission, Zhattau (2013), there is no strong commitment by both the government and there citizen to their mutual responsibilities and so the ability of the tax structure to yield substantial revenue is significantly reduced due to:

- Weak administration capacity for tax collection.
- Widespread corruption in tax collection
- Absence or dearth of public service benefits for previous tax payments which serve as a disincentive to continue tax payments.
- Perceived mismanagement of public funds.
- Unfavorable attitudes towards paying tax multiplicity of tax and levies at the three tier of government.

The precarious condition of Nigeria fiscal policy has led to undue real exchange rates appreciation with detrimental effect on investment and growth. There has been inefficiency and leakages in both current and capital budget of Nigeria which in the end yield unproductive results. These huge spending on unproductive ventures has hampered with the stability of the Nigeria economy.

Many less developed countries always experience fiscal deficit as a result of excess expenditures over revenue. These arise due to internal and external factors. In support of the assertion. Todaro and Smith (2009), conclude that rising debt burden, falling commodity prices, growing trade imbalance, and declining foreign private- public investment inflows have forced most developing economies to fiscal retrenchment. They further suggest that government should cut down expenditures and raise revenue through increased tax.

Efficient tax system and expenditure are crucial for economic stable growth of a country. The need to address the difficulties associated with fiscal policy has led to several reforms. Reforms have been undertaken over the years on existing fiscal policy in order to achieve some improvement on economic stability, but these reforms have not yielded anything tremendous for the country; this failure to achieve desired goals of stability in Nigeria stemmed from lack of recognition on the part of policy makers and their relationship between fiscal activities and macroeconomic variables. Zhattau (2013) advised that, stabilization policy requires that, policy makers can determine feasible target with a reasonable knowledge of the working of instrumental variables with the view effectively controlled these variables and acquire desired results.

Fiscal policy has not effectively promoted sustainable economic stability in Nigeria. Factors responsible policy inconsistency, high level of corruption, wasteful spending, poor policy interpretation and implementation and weak mechanism. If these problems are not properly and adequately checked, achievement of economic stability goals will continue be a night mere. In recent, Nigeria's fiscal policy has failed to address the exchange rate problems and the price hike of commodities have hampered with Nigerian economic stability. However, if changes in fiscal policy are going to exert a stabilizing effect on the economy, they must be timed correctly. Proper timing of fiscal changes is difficult. There will be a time lag between when an economy is dipping into a recession and when policy-makers figure out what is happening and what to do. It will also take time to develop a fiscal package on which the majority will agree and pass it through Congress. The ability to forecast when the economy is about to dip into a recession or experience an economic boom is extremely limited. Therefore, in a world of dynamic change and unpredictable events, macroeconomic policy-making is a little bit like throwing a stone at a target that often moves in unforeseen directions.

4.0 Conclusion

Nobody can dispute that fact that, for economic stability and of Nigeria be achieve, the individuals, corporate bodies and government need to play their roles Instability in Nigeria can be traced to political instability corruption, weak fiscal apparatus, external shocks, price disruption poor implementation of policies, unemployment and inequitable distribution of income among others. Once these problems are not checked and addressed, decades of fiscal policies would continue to change but will not yield anything substantial to economic stability. This is because stability ensures equilibrium in all facets of life that provides a level ground for all citizens.

5.1 Recommendations

Attaining equilibrium and achieving macroeconomic goals are inevitable for a country. The only problem is that the variables that could result to such balances need to be addressed. In view of that, the following recommendations are made;

1. Government should ensure economic stability by adjusting the level and allocation of taxes and expenditures. Fiscal policy should be designed to level the business cycle and achieve full employment, price stability and sustained economic growth.
2. The administrative machinery should be function effectively in their implementation of taxation policies that are geared towards desired goals.
3. Government should put in place a new, open and transparent framework for macroeconomic policy by defining clear policy objectives and division of responsibilities which give proper accountability.
4. Tax principles and systems should not leave a devastating incidence on the citizens. Efficient and fair fiscal policies are essential for promoting democracy and state legitimacy and since tax payers tend to hold their government accountable, the government should build a strong fiscal social contract between citizens and their government at all levels to encourage tax compliance.

5. More staff should be employed to help in tax assessment, interpretation awareness and implementation. Once these are addressed, the administration of tax will not be complicated and over burden.

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