**External Debt Stock and Economic Growth in Nigeria, 1981 – 2020**

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**Abstract:** This study analyzed external debt stock and macro-economic performance in Nigeria for the period 1981-2020. The macro-economic performance indicators used in the study included real gross domestic product, exchange rate and unemployment rate. External debt stock was the primary explanatory variable. Three models were formulated with external debt stock being constant variable in all the three variables while the macro-economic indicators were the control variables in each of the three models. The data were sourced from the Central bank of Nigeria Statistical Bulletin 2020 edition and analyzed using the Ordinary Least Square regression technique. The variables were found to be integrated at first difference but not cointegrated meaning that they have no long run relationship. The findings revealed that external debt stock decreased economic growth significantly. It also increases exchange rate significantly and decreased unemployment rate but not significantly. The study concluded that the decreasing effect of external debt stock on the economy and the fact that external debt stock exerted more strain on the exchange rate puts the Nigerian economy in a tight corner. It was recommended that the Nigerian government should as a matter of urgency decrease Nigeria’s external debt profile by seeking alternative means of funding. The increasing external debt profile has been empirically proven to decrease growth as this situation might be worsened in the long run. There is need to providing foreign exchange to the real sector for foreign trade to ease the strain on exchange rate and as well investing more of the borrowed funds in export goods rather than on consumption.

**Keywords** – External Debt Stock, Economic growth, Exchange Rate, Unemployment Rate, Real Gross Domestic Product

1. **INTRODUCTION**

The attainment of sustained economic growth, low inflation rate, positive balance of payment position, etc. remains a key focus for any country especially the developing countries which have been identified to have low capital formation due to low levels of domestic investment and savings. Aluko and Arowolo, (2010); Safdari and Mehrizi, (2011); Sulaiman and Azeez, (2011) argued that expectedly when these developing countries are faced with capital scarcity, they tend to seek for external loans in order to augment their domestic savings.

According to Soludo (2003), countries borrow in order to increase the growth of the economy and reduce the level of poverty. He argued that debt begins to have negative effects when it reaches certain level, and also debt servicing becomes a huge burden and which moves countries on the wrong side of the debt-laffer curve, where debt crowds out investment and growth. The debt service burden has worked against the rapid economic growth and development and worsened the social-economic problem of Nigeria.

Excessive external borrowing constitutes an impediment to sustainable economic growth, reduction in the inflation rate, a favourable balance of payments and reduction of poverty etc. Those who are of the view that external debt has a positive effect on the economy base their argument on the fact that external debt will increase capital inflow and when used for productive ventures accelerate macroeconomic performance. The capital inflow includes technical expertise, technology, managerial know-how, including access to the foreign market. The above view is in tandem with the Keynesian school of thought that capital accumulation is a catalyst for economic growth. However, Eduando 1989 asserted that external debt may negatively affect investment through debt overhang and credit- rationing problem. The debt overhang phenomenon is a situation where huge resources are used in servicing the debt which then stifles the performance of the macroeconomic growth indicators. It becomes a tax on domestic production which hinders reasonable economic growth activities in that it lowers available resources to the government for the implementation of economic policies that will enhance economic growth

Accumulation of excessive foreign loan does not necessarily result to a slow economic growth; it is the failure of the nation to meet its debt service payments coupled with lack of adequate information relating to the structure, nature, and volume of the debt in question (Were, 2011). This is one of the major challenges faced by the Nigerian economy. The inability of the country to promptly meet its debt servicing obligations resulted in high debt service burden for the country. The impact of this burden of debt service created more problems for the nation as it led to the increase in the fiscal deficit which is driven by the increase in the levels of debt servicing. This created a major problem to the economy because a great part of the earned revenue of the country was now being used up.

The origin of external debts in Nigeria dates back to 1958 when the country first borrowed the sum of $28million from World Bank to prosecute a railway extension (Nnamocha, 2002). In 1964 Nigeria took the first loan form the Paris Club of creditors. Between that time and 1970, Nigeria borrowed moderately despite the civil war that took place in the country from 1967 to 1970. However, in 1978, the ‘jumbo loan’ of US$1bn was borrowed from the international capital market (ICM) and this opened the floodgate of foreign borrowing in Nigeria. During this period (1971 to 1981), Nigerian leaders borrowed unsustainably in spite of high oil revenues to finance post war reconstruction and other state projects and infrastructure. From then on as a result of decline in crude oil prices and poor macroeconmic management by the Nigerian government, the external debt proile of the country began an upward movement. Thus from an external debt of N2.33 billion in 1981, the external debt stock of the country increased to N298.61 billion in 1990 and shut up to N3,097.38 billion in 2000. It then peaked at N4,890.27 billion in 2004 before declining to N2,695.07 billion in 2005 and then declined sharply to N451.46 billion in 2006 due to the debt relief Paris Club gave to the country.

The external debt of the country have continued to rise since after receiving the debt relief with the figure standing at N9,022.42 billion in 2019. However, the huge debt profile of the country has not reflected on the economic growth and other macroeconomic fundamentals of the country. Rather, the country is faced with high rate of insecurity and militancy which is as result of high rate of unemployment among the active labour force, high rate of poverty, lack of infrastructure, high rate of inflation and many others even amidst available resources. The question then becomes; why has external loan not stimulated the rate of the economic growth of the country? What then could still be crowding out investment and growth in Nigeria even after the debt relief and still drive the government into more indebtedness? This is reason why the study intends to investigate the impact of external debt on economic growth in Nigeria from 1981 to 2020.

**Objectives of the Study**

The broad objective of this research is to examine the impact of external debt on macroeconomic performance in Nigeria between 1981- 2020.

The specific objectives are to;

1. Assertain the extent to which external debt stock has contributed to economic growth in Nigeria;
2. Investigate the relationship between external debt stock and exchange rate in Nigeria;
3. What are the effects of external debt stock on unemployment rate in Nigeria

**Research Questions**

The study considered the following research questions relevant:

1. To what extent has external debt stock contributed to economic growth in Nigeria?
2. What is the relationship between external debt stock and unemployment rate in Nigeria?
3. What are the effects of Nigeria’s external debt stock on exchange rate in Nigeria?

**2. LITERATURE REVIEW**

**2.1 Conceptual Framework**

**Debt:** Debt is when something, particularly [money](https://en.wikipedia.org/wiki/Money), is owed by one person, who is the [debtor](https://en.wikipedia.org/wiki/Debtor) or borrower, to another person, who is the [creditor](https://en.wikipedia.org/wiki/Creditor) or lender. Debt is a chain of payments which is owed in the future or deferred payment, which is what, makes it different from an immediate purchase. The debt may be owed by a country, state government, [local government](https://en.wikipedia.org/wiki/Local_government), an individual or a company. It is a situation where a person owes another or has entered into an obligation which is enforceable through legal action in order to make payment of money. Countries resort to external loan for two major reasons; macro-economic reason (higher investment higher consumption i.e. health and education) or to finance balance of payment deficit in order to reduce nominal interest rates from foreign lenders due to lack of long term domestic credit or to avoid budget constraint (Soludo, 2003).

Debts can be categorized in terms of the time limit of their payment. We have the short-term debts and the long-term debts. The short-term debt refers to those debts, which are repayable within a year of incurring them. The loans that are taken by the corporate organizations from the banks are an example of short-term debt. The current liabilities of various business entities which have to be paid to the suppliers and creditors within one year are also a type of short-term debts. Debts can also be classified as deadweight or productive debt. A loan is classified as productive when it is obtained to purchase some sort of asset such as money borrowed for the acquisition of factories, electricity, and refineries, etc. On the other hand, money borrowed to for current expenditures or to prosecute a war is deadweight debt.

There are two sources of debt in any nation, namely;

1. Internal or Domestic Source
2. External or Foreign Source
3. **Internal or Domestic Debt**

Emerenini (2005) noted that this is the type of debt that is owed to individuals, organisations or corporate bodies in a given country by the government of that country. It carries different degrees of maturity, terms and conditions. The government may borrow internally with the use of securities in the financial market. Internal or domestic debt is contracted from the following instruments – treasury bills, treasury certificates, revenue bonds, etc.

1. **External or Foreign Source**

External or foreign debt is that part of a borrowing of a country, (private and public) which is sourced from abroad such as like government foreign corporations,re or financial institutions other than the country residents and it is repaid in foreign currency.

**External Debt:** External debt is that part of the debt of a country which was borrowed from lenders abroad that includes commercial banks governments or international financial institutions. It is a medium used by countries to augment their domestic savings and realize the funds required to carry out economic growth and developmental projects that will improve the living standards of the citizens of the country and promote sustainable growth and development. Ogbeifin (2007) opined that external debt arises as a result of the gap between domestic savings and investment and the gap between the value of export and that of import. As the gap increases, debt increases and thereby making the country to resort to borrow increasing amounts so as to stay afloat. He also described the external debt of Nigeria as that potion of the debt owed by the public and private sectors of the Nigerian economy to non-residents and citizens which is repaid in foreign currency, goods and services and arises due to the gap between domestic investment and domestic savings. Arnone et al (2005) defines external debt as that part of the debt of a country which is borrowed from foreign sources such as foreign corporations, government or financial institution.

Udoka and Anyingang (2010), defined external debt as the term that explains the financial relationship between a debtor country and the lender country. It usually refers to debt incurred which is repaid in other currencies apart from that of the country that borrowed the money. In principle, external debt comprises short-term debts, such as trade debts which mature between one and two years or whose payment would be settled within a fiscal year in which the transaction is conducted. Both developing and developed countries seek for foreign loans to improve their macroeconomic performance because external debt is generally believed to improve the growth and development of an economy (Osinubi & Olaleru, 2006. According to Nnamocha (2002), external debt can be classified to the purpose for which they are incurred such as;

1. Trade Arrears: These debts arises when a country is unable to pay completely for its external purchases and or services
2. Balance of payment support debts: These are debts incurred to correct adverse balance of payment of any country
3. Project-tied Debts: These are loans for particular projects which are usually self-liquidating such as the loans Nigeria has borrowed from China to finance airport and railway projects
4. Loans for socio economic needs: These are debts from loans used to provide socio-economic needs of the country.

**Exchange Rate:** Exchange rate is the rate at which one currency of a country will exchange for that of another country. For example how many US dollars does it take to but one Naira. Osadume (2018) stated that exchange rate could be regarded as the price of one country’s currency relative to another and that exchange has been necessitated due to the globalization and need for international trade settlements. Exchane rate plays an important role in an economy that is dependent on international trade as it connects the price system of two different currencies thereby facilitate trade between individuals, organizations and government of one country and that of another. It also helps traders to directly compare prices of traded goods. Countries use exchange rates as policy for macroeconomic control and for attainment of macroeconomic objectives in most economies. For instance, if foreign exchange is obtained at low cost, similarly, the prices of imported goods will be low. On the other hand, if the exchange rate appreciates, for example, an increase via devaluation, prices of imported goods will increase and the general level of prices in the economy will increase. Nations from time to time introduce exchange rate policies in their pursuit of macroeconomic objective of a healthy external balance.

**Unemployment:** Unemployment according to Briggs (1973) is the difference between the numbers of labour employed at current wage rates and working conditions, and the number of labour not hired at these levels. According to Gbosi (1997) unemployment is a situation where people that are willing to work at the prevailing wage rate cannot find jobs. The International Labour Organization (ILO) defined an unemployed as a member of the economically active population, who are without work but available for and seeking for work, including people who have lost their jobs and those that have left work voluntarily (World Bank, 1998). Unemployment takes place when people who are able to work cannot find a suitable paid job for a tangible period of time. Available statistics from the Bureau of Statistics indicates that 38% of the population that falls within the employable age are unemployed while 65% of Nigerian youth face unemployment as at September 2016.

**Types of Unemployment**

1. **Frictional Unemployment**: This type of unemployment is caused by industrial friction. There are jobs but people are unable to fill them because they do not possess the skills or are not aware of the existence of the jobs. This occurs as a result of lack of information, immobility of labor, shortage of raw materials, and machine breakdown.
2. **Residual Unemployment**: This type of joblessness is caused by old age, physical or mental disability, irresponsible attitude towards the job and inadequate training.
3. **Structural Unemployment**: This type of unemployment is caused by the shift in the country's economy causing a mismatch between the skills required by employers and the skills proposed by employees.
4. **Cyclical Unemployment**: It is as a result of a decrease in the demands for goods and services. It is usually caused by the economic recession or situation that forces companies to terminate a number of workers so as to cut their costs.
5. **Technological Unemployment**: It is caused by the constant technological changes that have increased mechanization of production. This results in low demand for man-power and displacement of human labor

**Economic Growth:** Economic growth is the sustained rise in the market value of the goods and services that is produced by an economy over a given period of time after adjusting for inflation. Conventionally, it is measures as the rate of increase in real gross domestic product, or real GDP, usually in per capita terms (IMF, 2012). Economic growth can also the referred to as the rise in the ability of an economy to produce goods and services, compared from one period of time to another. It can be measured in real terms, ie after adjusting for inflation or in nominal terms. Simply put, economic growth refers to an increase in aggregate productivity. Most often, the total gains in productivity are related with the increase in average marginal productivity. This implies that the average laborer in a given economy becomes more effective on the average. It is also possible to achieve aggregate economic growth without an increased average marginal productivity through extra immigration or higher birth rates (Investopedia, 2017).

Ajayi (1996) viewed economic growth as the increase in the real output of goods and services of a country over a period of time. Schumpeter in Todaro and Smith see economic growth as gradual and continuous change in the long-run which comes about by a steady rise in the savings rate and population (Klein, 2009). Thus, economic growth is akin to the quantitative and continuous increase in the per capita output of a country or income which is accompanied by an increase in its level of consumption, labor force, volume of trade and capital. It means a rise in the country’s real gross domestic product over a period of time usually one fiscal year.

**External Debt and Economic Growth in Nigeria**

There is a general agreement in economic theory that rational amount of borrowing by developing countries like Nigeria are expected to improve its economic growth. When economic growth is improved (at least more than 5% growth rate), the poverty situation of the economy will likely be positively affected. This will also lead to improvement in the unemployment rate, reduce inflation rate and also positively affect other macroeconomic variables. Most developing countries like Nigeria in order to support economic growth resort to external borrowing so as to augment their domestic savings and investment. This is because of the control little stocks of capital and which will make these countries to likely have investment opportunities with rates of return that are higher than that of other countries in developed economies. This becomes effective if the funds that are utilized properly for productive investment, and are not amenable to macroeconomic instability, policies that hinder economic incentives, or sizeable adverse shocks.

***Figure 1 External Debt and Economic Growth in Nigeria from 1981-2019***



***Source: Researcher’s Computation using Data from CBN Statistical Bulletin, 2019.***

From figure 2.5 above the external debt experienced the highest growth rate in 1999 with a growth rate of 307.16% while the lowest growth rate was in 2006 when the growth rate declined by 496.97% following the debt relief given to Nigeria by the Paris Club of Creditors. During this period in 2006 the GDP growth rate was only 8.6% as against 11.5% in 2005. The GDP witnessed the highest growth rate in 1995 with a growth rate of 64.24% and the lowest growth rate of 4.53% in 1984.

**Profile of Nigeria’s External Debt**

Nigeria has two major groups of external creditors which are; official and private creditors. The official creditors are made up of the following oraganisations;

* The African Development Bank (ADF),
* The International Bank for reconstruction and development (IBRD),
* The African Development Bank (AFDB),
* Economic Community of West African States (ECOWAS) fund
* The International Fund for Agricultural Development (IFAD), and
* The European Investment Bank.

The above-mentioned institutions are the multilateral creditors of Nigeria which also include International Monetary Fund (IMF) and the World Bank which were very active lenders in the 1970s/1980s. The Paris Club and Non-Paris Club creditors make up the bilateral creditors. The Paris Club is an informal group of official creditors which was established to assist debtor countries going through repayment challenges to find endurable and lasting solutions to their debt problems. Also, parts of the external debt profile of Nigeria were provided by private creditors and these are made up of London Club group of creditors and holders of promissory notes.

Available statistics from the Debt Management Office (DMO) indicates that the total outstanding volume of external debt as at December 2004 was $35.94 billion. This outstanding debt stock was made up of; Paris Club 85.82%, London Club 4.01%, multilateral creditors 7.86%, Non-Paris Club 0.13% and Promissory notes 2.18% (DMO, 2012). The figures above clearly indicate that the Paris Club group of creditors was owed the largest proportion of the external debt of Nigeria.

**Table 1: The Sources of the External Debt in Nigeria from 1981 - 2019**

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Years** | **Multilateral (N’ bn)** | **Paris Club (N’ bn)** | **London (N’ bn)** | **Prom Notes (N’ bn)** | **Bilateral (N’ billion)** | **Euro Bond (N’bn** | **Diaspora Bond (N’bn)** | **Others (N’ bn)** | **Total (N’ bn)** |
|
| 1981-1985 | 3.84 | 25.54 | 15.19 | 2.98 | 2.98 | 0 | 0 | 3.31 | 53.84 |
| 1986-1990 | 79.52 | 436.16 | 126.47 | 63.28 | 63.28 | 0 | 0 | 46.51 | 815.21 |
| 1991-1995 | 404.29 | 1,479.11 | 219.12 | 316.69 | 316.69 | 0 | 0 | 135.64 | 2,871.54 |
| 1996-2000 | 1,032.18 | 5,201.76 | 433.68 | 412.72 | 412.72 | 0 | 0 | 27.97 | 7,521.03 |
| 2001-2005 | 1,817.99 | 15,051.86 | 994 | 607.17 | 607.17 | 0 | 0 | 94.66 | 19,172.85 |
| 2006-2010 | 2,330.73 | 0 | 0 | 64.83 | 89.43 | 0 | 0 | 208.89 | 2,693.88 |
| 2011-2015 | 5,170.39 | 0 | 0 | 0 | 907.5 | 941.2 |  | 35 | 7,054.10 |

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| 2016-2019 | 13,078.97 | 0 | 0 | 0 | 3,513.93 | 9,173.18 | 281.70 | 0 | 26,048.04 |

**Source: Author’s computation from Central Bank of Nigeria Statistical Bulletin (2019)**

Table 2.2 shows the major sources of foreign borrowing in Nigeria from 1981 to 2018. The table reveals that from 1981 up-till 2001-2005, Paris club has been the major source of external borrowing in Nigeria. Thereafter, the debt owed the Club decline drastically as a result of the debt relief granted to the country by Paris Club creditors. This reason for this as reported by the Debt Management Office (DMO) (2005) was that the Paris Club of creditors was the only lender that consented to grant a debt relief of $18 billion (60 percent) to Nigeria out of an outstanding debt of $30.84 billion owed to them as at December 31, 2004. The multilateral lenders have remained the major source of external debt in Nigeria since 2006 to 2018. This was followed by bilateral sources from 2001 to 2010 and then Euro Bond from 2011 to 2019.

**2.2 Theoretical Framework**

**The Dual-gap theory:** Omoruyi (2005) asserted that reason why most economies resort to foreign borrowing is to enable the country to fill the gap between the level of domestic savings and investment. This gap according to Chenery 1966, is the reason for foreign borrowing which is to resolve the lack of savings and investment in a nation. The rise in the domestic savings and investment would vis-à-vis lead to a rise in economic growth and other macroeconomic growth indicators (Hunt, 2007). The framework of dual-gap analysis indicates that the development of any country is dependent on investment which needs domestic savings and this domestic savings is not adequate to enable that development take place (Oloyede, 2002). The dual-gap theory is derived from the national income accounting framework which stipulates that excess investment expenditure (investment-savings gap) is equal to the excess of imports over exports (foreign exchange gap).

The dual gap analysis stated that the economic development of any country is a function of investment, and that investment is an important product of domestic savings, which most times is not enough to finance development. In this situation, government resort to borrowing from abroad the money that can be invested in the economy, and this amount is usually equal with the amount that is saved. Furthermore, the local resources are to be supplemented with resources from abroad, in such a way that will result to excess of import over export i.e. M>E.

I – S

M – E

Hence, I – S = M – E

Surplus of investment over domestic saving in the national income account is equal to the excess of import over export.

Income = Consumption + Import + Savings

Output = Consumption + Export + Investment

Income = Output

That is, Investment – Savings = Import – Export. (I – S = M - E)

This is the basis of dual gap analysis; it shows that savings investment gap exists if the available domestic saving is not adequate to realize the targeted rate of growth, and thus borrowing is induced to cover the shortfall. Similarly, if the maximum import required to achieve the growth expectation is larger than the maximum possible level of export, then there is an export- import exchange gap.

**Debt Overhang Hypothesis**

Debt Overhang effect is one of the major means through which high debts impact macroeconomic performance (Krugman 1988; Sachs 1989). A high debt burden shrinks investments, due to the fact that the returns from the investment are taken away through tax by the foreign lenders. It is because of this that if there is the probability that debt of a country will exceed her ability to repay with some likelihood in the future, expected debt service is likely to be an increasing function of the level of output of the country. This then implies investment from current lenders from abroad and other investment by domestic and new foreign investors will be discouraged as some of the returns from investing in the domestic economy will be effectively ‘taxed away’. (Claessens*et al*. 1996). Therefore, the debtor nation will have to let go some multiplier-accelerator effects of investment, which dampens the economy’s rate of growth, and further raises its dependence on external finance (Metwally and Tamaschke 1994).

Debt overhang could also dis-incentivize investments in new technologies and human capital, as well as the willingness of the government to engage in structural reforms and fiscal adjustments, leading to a poverty trap (Sachs 2002).

A number of studies have been carried out to test the debt overhang theory, and some of them include Borensztein (1990), Cohen (1993), Sachs (1989) and Warner (1992). Others are Pattillo et al. (2002), Clements et al. (2003), Elbadawi et al. (1997), Chowdhury (2004) and Fosu (2007). Very few studies have focused on the channels through which external borrowing affects macroeconomic performance in general and capital formation in particular. However, Pattillo et al. (2004) inferred that the impacts of external debt are felt mainly through investment and total factor productivity. Many of the studies paid specific attention to developing countries, while others focused on relatively low-income economies. All of these studies described debt overhang as the additional negative impacts of the accumulation of debt on economic growth which strongly lowers the macroeconomic performance of an economy through deterrence due to the fear of future tax burden and macroeconomic volatility.

The overhang relationship between debt and growth is usually represented by an inverse U-shaped curve, where the peak (maximum) represents the level where the beneficial impact of debt constitutes a drag on the growth process. A graphical illustration of this theory became known as the debt Laffer curve. Economists redirected their focus towards finding the optimal debt stock for any country in order to find a solution to the debt overhang problem, which has been clearly explained by the existing theories. This would be the sustainable level of debt of a country where it would not have any debt overhang problem or in other words without being trapped in the debt cycle.

**The Solow Growth Model**

The Solow-growth model was published in 1956 as a seminar paper on economic growth and development under the title, “A contribution to the theory of economic growth”. Solow growth model like most economic growth theories is predicated upon some assumptions which includes;

* Countries will produce and consume only a single homogenous good.
* In the short run, technology is exogenous.

The growth model of Solow was introduced based on a Cobb - Douglas production function which is given by the form:

Y = f(K, L) = Ka L1-a (i)

Where

Y = output

K = Capital input

L = Labor input

α and 1-α are output elasticities of capital and labor respectively and α is a number between 0 and 1.

The capital accumulation equation is the other important equation of the Solow growth model which is expressed in the form:

Ḱ = sY – dK (ii)

Where:

Ḱ = change in capital stock

sY = gross investment

dK = depreciation during the production process

With mathematical manipulation Solow derives the capital accumulation equation in terms of per worker i.e. ḱ = sy – (n+d)k . This means that the change in capital per worker is a function of investment per worker, depreciation per worker and population growth. Of these three variables only investment per worker is positively related with change in capital per worker

**2.3 Empirical Review**

Omodero and Alpheaus (2019) studied the effect of foreign debt on the economic growth of Nigeria using ordinary least square and secondary data for 21 years to examine. The results showed a significant negative relationship between foreign debt and economic growth while while a strong and significant positive relationship exists between foreign debt servicing and economic growth. The other factors were insignificant in explaining economic growth under this scenario.

Agwu, Ohaegbu, and Nnodim (2019) used multiple regression statistical technique to study on the Impact of External Debt on Economic Growth in Nigeria from 2014 to 2018. They used the following variables; GDP (as dependent variable), while external debt, exchange rate and external debt service were the independent variables. The results revealed a positive relationship between external Debt and Gross Domestic Product, while external debt service had a negative relationship with Gross Domestic Product; and Exchange Rate had a negative relationship with GDP.

Odubuasi et al. (2018) investigated the impact of external debt on the economic growth of Nigeria from 1981 to 2017 using Augmented Dickey Fuller (ADF), Granger Causality and Error Correction Model. The results of their study revealed that there exists a significant positive relationship between external debt, capital expenditure and economic growth, while debt servicing cost did not have any impact on economic growth.

Solomon (2016) used secondary date and applied the regression and granger causality methods of analysis to examine the impact of external debt on the Nigeria economya. The results revealed that external debt and external debt service have negative relationship with GDP and the granger causality test shows that GDP had a unidirectional causal relationship with external debt service which runs from GDP to external debt service. It equally showed that uni-directional causality existed between external debt and GDP which runs from external debt to GDP.

Afolabi et al. (2017) used error correction model and granger causality test to examine the long and short term relationship between external debt and economic growth in Nigeria from 1980 to 2014. Their findings showed that there was a negative relationship between external debt and economic growth in Nigeria. The study recommended that government should use the external debt judiciously for the provision of projects and infrastructures that will boost economic growth and development in the country

Ndubuisi (2017) analysed the impact of external debt on economic growth in an emerging economy using evidence from Nigeria. The data used were external debt services, gross domestic product, external debt stock, exchange rate and external reserve over the period 1985 to 2015. The data were analysed using the ordinary least square regression. Augmented Dick Fuller Unit Root Test, Co-integration and Error Correction Model were used in conducting the diagnostic tests. Findings revealed that there was a negative and insignificant relationship between debt service payment and Nigeria’s economic growth while external debt stock had positive and significant impact on the growth index of Nigeria. External reserve and exchange rate were used as control variables and they had positive and significant effect on growth.

Matthew and Mordecai (2016) used annual time series data from 1986 to 2014 to examine the impact of public debt on economic development of Nigeria. The study utilized the following econometric tools; the Augmented Dickey-Fuller test, Johansen co-integration test, Error Correction Method (ECM) and the Granger Causality test. Findings from the study revealed an insignificant negative relationship between external debt stock, external debt servicing and economic development in Nigeria. It further showed that a direct significant relationship existed between domestic debt stock and economic development while domestic debt service payment had significant but inverse relationship with economic development in Nigeria.

Amaefule and Umuaka (2016) examined the effects of Government Borrowing on Nigerian Infrastructural development using OLS. It was revealed from their findings showed that the variables have a short-term relationship among themselves. The study further reveals the existence of a positive relationship between the capital expenditure of the federal government and domestic debt; while there was no significant relationship between capital expenditure and foreign debt.

Utough (2016) using annual time series data from 1981 to 2014 examined the impact of external debt on economic growth in Nigeria. The study utilized the following econometric tools; the Augmented Dickey-Fuller test, Johansen co-integral ion test, Vector Error Correction Method (ECM) and the Granger Causality test. The findings revealed that external debt service has a significant and negative relationship with economic growth in Nigeria while external debt stock impacted positively to the development of the Nigerian economy at 5% level.

Utomi (2014) investigated the impact of external debt on economic growth in Nigeria from 1980-2012 using include Augmented Dickey Fuller (ADF) test, Johansen Co-integration, Vector Error Correction Mechanism and Granger Causality econometric techniques. The results revealed an insignificant long run relationship and a bi-directional relationship between external debt and economic growth in Nigeria. The study recommended that external debts should be contracted solely for economic reasons and not for social or political reasons. Also, the responsible authorities for managing the external debt of the country should adequately monitor the debt payment obligations and ensure that the debt are not be allowed to pass a stated limit in order to avoid debt overhang.

Faraji and Makame (2013) examined the impact of external debt on economic growth of Tanzania from 1990-2010. The study made use of time series data on external debt and economic performance and assumed that external debt was utilized by developing countries to augment their domestic savings in meeting developmental needs. The results from the study revealed that a significant relationship existed between external debt, debt service and GDP growth. The debt service payment had a negative effect of about 28.52 while total external debt stock had a positive effect of about 0.37. The study recommended that in taking external debt, counties should ensure that they are put in productive use and the rate of return of debt is higher than the service payment rate.

Mukolu, and Ogodor (2012) examined how external debt relates with macroeconomic performance in Nigeria from 1975 to 2005 using ordinary least square technique (OLS). They expressed two macroeconomic variables of gross domestic product and interest rate each as a function of external debt and debt servicing. The study found a significant and positive relationship between external debt and Nigeria’s Gross Domestic Product while the debt charges paid on this debt, and the debt serviced by the government have a negatively impact economic growth in Nigerian.

Faraglia et al (2012) employed dynamic stochastic general equilibrium (DSGE) to examine the impact of government debt maturity on inflation. They used Fiscal Insurance, Fiscal Sustainability, Government Debt, Inflation, Interest Rates and Maturity as variables. The result revealed that the volatility and continuity of inflation is predicated on the size, sign and maturity profile of government debt and was significantly incomplete even with long bonds and inflation which is not significant in realizing sustainability of debt. They concluded that issuance of long term debt does help governments in utilizing inflation more to realise fiscal sustainability. The effect of the inflation was more volatile and persistent with longer maturity of debt.

Atique and Malik (2012) examined the impact of domestic and external debt on the economic growth of Pakistan from 1980-2010 using ordinary Least Square approach (OLS) to co-integration. The result revealed a significant inverse relationship in both, that is, inverse relationship between domestic debt and economic growth, and external debt and economic growth.

Suleiman *et al* (2012) used annual time series data from 1970 to 2010 to carry out a study on the effect of external debt on the economic growth in Nigeria. The study used econometric techniques of Ordinary Least Squares (OLS), Augmented Dickey-Fuller unit root test, Johansen co-integration test and error correction model (ECM) in the empirical analysis. The Johansen co-integration test showed that there was a long-run relationship amongst the variables and findings from the error correction model revealed that external debt has a positive relationship with the economic growth of the Nigerian economy.

Ohwofasa, Nana and Kumapayi (2012) carried out a study on external debt management and macroeconomic performance of Nigeria from 1986 – 2011. The study employed Ordinary Least Squares (OLS) technique and modeled four equations using unemployment, per capita income, literacy rate and external debt as dependent variables. External debt, balance of payment, foreign direct investment and debt service payment were the independent variables. Their findings revealed that debt service, external debt, and balance of payment impacted negatively on per capita income while FDI had a positive relationship with per capita income. Also, debt service, external debt, and balance of payment positively affected unemployment rate while that of FDI on unemployment was negative. The results from the findings further showed that the impact of debt service, FDI, and external debt on literacy rate was positive while there was a negative relationship between literacy rate and balance of payment. Finally, FDI and terms of trade impacted negatively on external debt while a positive relationship existed between GDP, exchange rate and external debt. The study recommended that government should ensure that all transactions with the London and Parish Clubs and other creditors should be ones that will promote greater trade and investment in Nigeria.

Ogunmuyiwa (2011) also investigated whether external debt promotes economic growth in Nigeria used time series data from 1970 to 2007. He employed econometric techniques such as Augmented Dickey-Fuller test, Granger causality test, Johansen co-integration test and Vector Error Correction Method (VECM) to estimate the regression equation. The study found out that there was no existence of causality between external debt and economic growth in Nigeria.

Safdari and Mehrizi (2011) employing vector autoregressive model (VAR) technique of estimate and time series date from 1974 to 2007, carried out a study on the impact of external debt on economic growth in Iran. The study observed the balance and long-term relation of five variables (GDP, private investment, public investment, external debt and imports). From their it was discovered that external debt negatively affected the GDP and private investment while pubic investment had a positive relationship with private investment.

**3. METHODOLGY**

The research adopt *ex-post-facto* research design and the choice of this research design was due to the fact that the study utilized secondary data for the analysis and that the secondary data are not subject to manipulation from the researcher. The data were obtained from the Central Bank of Nigeria (CBN) Statistical Bulletin (2020) Edition. In addition, we obtained data on other variables from the National Bureau of Statistics (NBS) Annual Statistical Publications.

**3.1 Model Specification**

In an attempt to study the effect of external debt stock on the Nigeria’s macro-economic performance**,** we take a cue from empirical evidence which have established a vector relationship between selected macro economic performance indicators and external debt variables. The specification of Agwu, *et al* (2019) is modified to suit our purpose. It is important to note here that this study used a more specific and direct model by including only external debt stock and using three macro economic performance indicators. Consequenbtly, we have three models and formulate a linear relationship following the multiple linear regression model thus:

***RGDP = f(EDSK, EXR, UNEM) …(i)***

***EXR = f(EDSK, RGDP, UNEM) …(ii)***

***UNEM = f(EDSK, EXR, RGDP) …(iii)***

The above model specifies three linear equations where each of the macro economic performance indicator is used as the dependent variable with the other macro economic performance indicators used as the control variable in each of the equations. This is aimed at carrying out a more specific analysis of the relationship between the variables since other studies have explored the vector relationship amongst these variables. Putting the specifications in *equations (i) – (iii)*, in a a multiple regression equation format, the variables are connoted as:

**RGDPt = α0 + α1\*EDSKt + α2\*EXRt + α3\*UNEMt + ε1t­ *…(iv)***

**EXRt = β0 + β1\*EDSKt + β2\*RGDPt + β3\*UNEMt + ε2t­ *…(v)***

**UNEMt = λ0 + λ1\*EDSKt + λ2\*EXRt + λ3\*RGDPt + ε3t­ *…(vi)***

Where:

RGDP = Real gross domestic product at 2010 constant price

EDSK = External debt stock

EXR = Exchange Rate (Naira to US dollar)

UNEM = Unemployment rate (% of active population that are not employed)

**α0,** β0 and **λ0** = Intercepts of the models

α1 – α4, β1 – β4 and λ1 – λ4 = Unknown parameters of the model to be estimated

εt’s = Stochastic Error terms at time “t”

The ***a-priori*** expectations of the three models is such that the coefficient of external debt stock is expected to have positive sign i.e. α1, β1, λ1 > 0. Also, the macro economic variable are all expected to have positive coefficients except unemployment rate which is expected to have inverse or negative relationship with the other macro economic variables i.e. α2 > 0, α3 < 0, β2 > 0, β3 < 0 and λ2 > 0, λ3 < 0.

In this research study, the data were analyzed based on three criteria: Economic, Statistical and Econometric criteria. The Economic criterion examined the econometric parameters and how they conform to economic a-priori expectation.

The statistical criterion used statistical tools with the aid of E-views 9 econometric software to obtain the parameter estimates. The estimated parameters were analyzed and also discussed in line with the economic criteria.

The econometric criterion investigated the causal relationship between the variables and if there were violations of classical Econometric assumptions of no autocorrelation and heteroskedasticity. The data were interpreted after the estimation of the parameters from the E-views 9 software.

The Ordinary Least Square (OLS) regression technique was used in analyzing the data and estimating the model. Egbulonu (2020) asserts that the Ordinary Least Square regression can be used to estimate econometric models that are integrated at first order but not cointegrated. The Ordinary Least Square multiple regression estimates the parameters of the variables that are integrated at first order (Pesaran, Shin and Smith, 1999).

# 4. Data Analysis and Discussion of Findings

**4.1 Data Analysis**

The unit root test otherwise called the stationarity test was carried out using the Augmented Dickey Fuller (ADF) unit root test approach. The stationarity test indicates that the variables real gross domestic product (RGDP), exchange rate (EXR), unemployment rate (UNEM) and external debt stock (EDSK) all achieved stationarity at first difference, which implies that the variables are integrated of order one, I(1). This further confirms that the statistical properties of the data are constant and do not vary over the period of study. Therefore, the data can be used for predictive purposes

.

**Table 1: Summary of Unit Root Test**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **ADF Test statistics** | |  | |
| **Variable** | **At Level** | **1st Difference** | **Decision Rule** | **Order of Integration** |
| RGDP | -0.1953 | -3.4588 | Stationary at 1st difference | I(1) |
| EXR | -1.2184 | -5.5218 | Stationary at 1st difference | I(1) |
| UNEM | -1.3803 | -6.2482 | Stationary at 1st difference | I(1) |
| EDSK | -2.1399 | -4.3721 | Stationary at 1st difference | I(1) |
| *Critical value at 5% level = -2.9678* | | | |  |

*Source: Computed from E-Views 9.0*

The Table 1 above confirms that the variables are all 1(1) series, therefore, we proceed to the test for long run relationship using the Johansen cointegration test. As summarized in Table 2 below, the Trace and Max-eigen statistics indicated no cointegrating equation at the 5% level.

# 

# Table 2: Summary of the Johansen Cointegration Test

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| **Trace Statistic** | | | | | **Max-Eigen Statistic** | | |
| **No of CE (S)** | **Eigen-Value** | **Trace stat.** | **5% CV** | **Prob\*\*** | **Max-Eigen stat.** | **5% CV** | **Prob\*\*** |
| None | 0.3992 | 48.131 | 63.876 | 0.4995 | 19.361 | 32.118 | 0.7019 |
| At most 1 | 0.3063 | 28.769 | 42.915 | 0.5758 | 13.897 | 25.823 | 0.7312 |
| At most 2 | 0.2144 | 14.872 | 25.872 | 0.5852 | 9.1744 | 19.387 | 0.7064 |
| At most 3 | 0.1392 | 5.6978 | 12.517 | 0.4996 | 5.6978 | 12.517 | 0.4996 |

*Source: Computed from E-Views 9.0*

The Table 2 above shows that none of the probability values were significant at 5% level. This means that there is no long-run relationship between external debt and Nigeria’s macro economic performance.

Since the variables were stationary at first difference but not cointegrated, we proceeded with the estimation of the model coefficients using the Ordinary Least Square regression. The OLS estimates for each of the three models are summarized below in Table 3 below

**Table 3A: Estimation of the Ordinary Least Square Regression (Model One)**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  |  |  |  |
|  |  |  |  |  |
| **Variable** | **Coefficient** | **Std. Error** | **t-Statistic** | **Prob.** |
|  |  |  |  |  |
|  |  |  |  |  |
| C | 32.38092 | 0.945835 | 34.23526 | 0.0000 |
| LNEDSK | -0.116990 | 0.038308 | -3.053887 | 0.0042 |
| LNEXR | 0.343782 | 0.048315 | 7.115494 | 0.0000 |
| LNUNEM | 0.223193 | 0.059909 | 3.725522 | 0.0007 |
|  |  |  |  |  |
|  |  |  |  |  |
| R-squared | 0.902631 | Mean dependent var | | 31.03803 |
| Adjusted R-squared | 0.894517 | S.D. dependent var | | 0.582858 |
| F-statistic | 11.92622 | Akaike info criterion | | -0.396311 |
| Prob(F-statistic) | 0.000000 | Durbin-Watson stat | | 1.598875 |

*Dependent variable = RGDP*

*Source: Computed from E-Views 9.0*

The Table 3A above shows the relationship between real GDP and external debt stock with exchange rate and unemployment rate as the control variavbles. The estimates reveasls that external debt stock has a negative relationship with economic growth (RGDP) decreasing it by 0.1169 units. This means that a unit change in external debt stock of Nigeria decreases econonmic growth by 0.1169 units annually. The probability value of 0.0042 is an indication that the decrease in real GDP as a result of change in external debt stock was a significant decrease. Also, exchange rate and unemployment rate significantly increased growth by 0.3438 and 0.2232 units respectively.

The model has a coefficient of determination of 0.8945 meaning that about 89.45% of the changes in real GDP are being accounted for by external debt stock and other variables. The F-statistic value of 11.12 shows that the variables have joint significant effect on real GDP while the Durbin Watson value of 1.599 indicates that the model has negative autocorrelation.

**Table 3B: Estimation of the Ordinary Least Square Regression (Model Two)**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  |  |  |  |
|  |  |  |  |  |
| **Variable** | **Coefficient** | **Std. Error** | **t-Statistic** | **Prob.** |
|  |  |  |  |  |
|  |  |  |  |  |
| C | -62.34035 | 6.363949 | -9.795860 | 0.0000 |
| LNEDSK | 0.494208 | 0.048504 | 10.18899 | 0.0000 |
| LNRGDP | 1.700034 | 0.238920 | 7.115494 | 0.0000 |
| LNUNEM | -0.069523 | 0.156388 | -0.444554 | 0.6593 |
|  |  |  |  |  |
|  |  |  |  |  |
| R-squared | 0.951674 | Mean dependent var | | 3.620902 |
| Adjusted R-squared | 0.947646 | S.D. dependent var | | 1.839792 |
| F-statistic | 23.63118 | Akaike info criterion | | 1.202085 |
| Prob(F-statistic) | 0.000000 | Durbin-Watson stat | | 1.479278 |

*Dependent variable = EXR*

*Source: Computed from E-Views 9.0*

External debt stock has a positive effect on exchange rate as shown in the Table 3B above. The positive coefficient of 0.4942 means that a unit change in external debt stock increases exchange rate by 0.4942 units. The probability value of 0.0000 indicates a very significant and positive effect of external debt stock on exchange rate in Nigeria for the period. Also in the second model, real GDP increased exchanbge rate significantly by 1.700 units while unemployment rate had a negative relationship with exhcnage rate decxreasing it by 0.0695 units, though the decrease was not significsnt.

The model has 94.76% fitness since the adjusted R-squared value was 0.9476. This means that about 94.76% of the changes in exchange rate are being accounted for by external debt stock and other variables. The F-statistic value of 23.63 shows that the variables have joint significant effect on exchange rate while the Durbin Watson value of 1.479 indicates that the model has negative autocorrelation.

**Table 3C: Estimation of the Ordinary Least Square Regression (Model Three)**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  |  |  |  |
|  |  |  |  |  |
| **Variable** | **Coefficient** | **Std. Error** | **t-Statistic** | **Prob.** |
|  |  |  |  |  |
|  |  |  |  |  |
| C | -35.04242 | 11.55763 | -3.031974 | 0.0045 |
| LNEDSK | -0.028693 | 0.101480 | -0.282747 | 0.7790 |
| LNEXR | -0.078531 | 0.176652 | -0.444554 | 0.6593 |
| LNRGDP | 1.246726 | 0.334645 | 3.725522 | 0.0007 |
|  |  |  |  |  |
|  |  |  |  |  |
| R-squared | 0.634282 | Mean dependent var | | 2.592572 |
| Adjusted R-squared | 0.603806 | S.D. dependent var | | 0.710796 |
| F-statistic | 20.81219 | Akaike info criterion | | 1.323927 |
| Prob(F-statistic) | 0.000000 | Durbin-Watson stat | | 1.779967 |

*Dependent variable = UNEM*

*Source: Computed from E-Views 9.0*

Unemployment rate is the dependent variable in the third model. The Table 3C above shows that external debt stock has a negative effect on unemployment rate decreasing it by 0.0287 units. However, the was not significant as the p-value of 0.7790 was not significant at 5% level. Similarly, exchange rate decreased unemployment rate but not significantly by 0.0785 units while increase in real GDP increased unemployment rate significantly by 1.2467 units (*p-value* = 0.0007).

The explanatory variables in the third model explains up to about 60.3% of the changes in unemployment rate annually. This means that external debt stock, exchange rate and real GDP account for up to 60.3% of the variations witnessed in unemployment rate movements in Nigeria for the period reviewed. The F-statistic value of 20.812 shows that the variables have joint significant effect on unemployment rate while the Durbin Watson value of 1.779 indicates that the model has negative autocorrelation.

**4.2 Discussion of Findings**

The effect of external debt on macro economic performance of Nigeria has been studied by numerous researchers. One interesting aspect of the many research on this topic of sudy is the variety in the findings. Some studies have found positive effect of external debt on growth while others have found negative effect (See empirical evidence in sub-section 2.3 above). This study adds to the body of empirical literature by formulating three models using three macro economic performance indicators namely real GDP, exchange rate and unemployment rate to analyze their relationship with external debt stock for the period 1981-2020.

The three models were analyze dusing the Ordinary Least Square regression technique. The findings from the first model revealed that external debt stock decreased growth significantly over the period studied. This means that the more Nigeria takes external loans, the more the country’s external debt profile increases and this hinders growth of the economy.

The negative effect of xetrnal debt stock on growth corroborates earlier findinsg by Ohwofasa, *et al* (2012), Matthew & Mordecai (2016) and Ndubuisi (2017). These studies found that external debt stock negatively impacted on growth and the negative impact was significant. However, other studies like Faraji & Makame (2013) and Mukolu & Ogodor (2012) found positive effects of external debt on growth. These studies may have been limited in time scope as the inclusion of current and up-to-date trends in Nigeria’s external debt stock may have been the reason for the disparity in their findings.

Furthermore, external debt stock was found to have positive and significant effect on exchange rate but affects unemployment rate negatively but not significantly. What this entails is that increasing Nigeria’s external debt stock puts more strain on the country’s exchange rate as it increases in realtion to the US dollar thereby causing harmful effects on the economy. Also, there is decrease in unemployment rate occasioned by ncrease in external debt stock. This is expected because of the possible utilization of the funds to enhance human capital.

**5. Conclusion and Recommendations**

The study showed strong contrasting evidence that external debt has decreased Nigeria’s economic growth significantly on one hand, and has also decreased unemployment rate on the other hand. However, the decreasing effect of external debt stock on the economy and the fact that external debt stock exerts more strain on the local currency puts the Nigerian economy in danger. This may be the reason many economic stakeholders are calling for a halt in the current external borrowing spree as this will have long term adverse effect on the economy. External debt stock decreased unemployment but not significantly. In reality, the externally borrowed funds may not be utilized for the purpose they are meant. This is one of the limitations of the data collected as published by the Central Bank of Nigeria. Econmetric analysis may show positive effect on the macro economy but in reality, the funds were not utilized judiciously.

Notwithstanding, the study made useful and sightful findings out of which the following recommendations were made:

The Nigerian government should as a matter of urgency decrease Nigeria’s external debt profile by seeking alternative means of funding. The increasing external debt profile has been empirically proven to decrease growth as this situation might be worsened in the long run.

External debt stock can be used to strengthen the local currency exchange rate by way of providing foreign exchange to the needy sectors through preferential disbursements. The increasing effect of external debt stock on exchange rate can also be checked by investing more of the borrowed funds in export goods rather than on consumption.

The positive effect of external debt stock on unemployment rate is an expected development. However, this should be transformed to reality by investing these externally borrowed funds into human capital development projects which will provide the needed impetus for repayment of these debts.

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