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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 18/17-3

3:10 p.m., March 5, 2018

3. Nigeria—2018 Article IV Consultation

Documents: SM/18/33 and Correction 1, and Supplement 1, and Supplement 2, SM/18/34, and Correction 1,

Staff: Mati, AFR; Zeidane, SPR

Length: 1 hour and 7 minutes

Executive Board Attendance

M. Furusawa, Acting Chair

Executive Directors	Alternate Executive Directors
M. Mkwezalamba (AE)	
	M. Raghani (AF)
	D. Vogel (AG), Temporary
	C. Barron (AP)
	P. Fachada (BR)
	K. Lok (CC), Temporary
	E. Sanchez Rodriguez (CE), Temporary
	N. Feerick (CO), Temporary
	O. Bayar (EC)
	A. Castets (FF)
	K. Merk (GR)
	P. Dhillon (IN), Temporary
	I. Lopes (IT), Temporary
	Y. Saito (JA)
	M. Daïri (MD)
	P. Al-Riffai (MI), Temporary
	V. Rashkovan (NE)
	R. Bartkus (NO), Temporary
	M. Atamanchuk (RU), Temporary
H. Alogeel (SA)	
J. Agung (ST)	
	P. Inderbinen (SZ)
	T. Hemingway (UK), Temporary
	S. Vitvitsky (US), Temporary

C. McDonald, Acting Secretary
J. Morco, Summing Up Officer
M. Gislen, Board Operations Officer
M. McKenzie, Verbatim Reporting Officer

Also Present
World Bank Group: N. Fiess. African Department: M. Mati, M. Newiak, L. O'Sullivan, D. Owen, A. Selassie, C. Tsangarides. Communications Department: L. Mboto Fouda. Fiscal Affairs Department: O. Luca. Legal Department: W. Bergthaler, C. Ogada. Monetary and Capital Markets Department: M. Tamene. Strategy, Policy, and Review Department: A. Hosny, Z. Zeidane.

Executive Director: D. Sembene (AF). Alternate Executive Director: G. Lopetegui (AG), H. Razafindramanana (AF), K. Virolainen (NO). Senior Advisors to Executive Directors: M. Alle (AF), D. Cheong (BR), C. Collura (IT), E. Hagara (EC), H. Joshi (IN), O. Odonye (AE), E. Sishi (AE), A. Tivane (AE), F. Bellocq (FF). Advisors to Executive Directors: A. Abdullahi (AE), E. Amor (AP), X. Cai (CC), J. Garang (AE), S. Ismail (ST), M. Ismail (AE), M. Josic (NE), A. Nainda (AE), W. Nakunyada (AE), S. Potapov (RU), J. Suazo (CE).

3. Nigeria—2018 Article IV Consultation

Mr. Mkwezalamba and Mr. Odonye submitted the following statement:

Our Nigerian authorities thank staff for the constructive engagement during the Article IV consultation. They broadly concur with staff's assessment of the macroeconomic challenges facing the country and their policy recommendations.

Following five successive quarters of recession, the Nigerian economy has rebounded, driven by policy responses tailored to lay a strong foundation for inclusive growth and sustainable development. During the second quarter of 2017, economic activity picked up on the back of strong implementation of macro policies initiated under the Economic Recovery and Growth Plan (ERGP). The ERGP was developed in response to the recession, with the goal to fundamentally change the direction of national economic development. Its key priorities include stabilization of the macroeconomic environment and achieving low inflation, stable exchange rates, and sustainable fiscal and external balances.

Our authorities, however, wish to register their displeasure with the phrase "muddle through" outlook in the staff assessment and failure to appreciate government efforts despite several initiatives to strengthen the fiscal situation and promote growth. Equally, they find the reference to "pervasive/widespread corruption" in Nigeria inappropriate, given that corruption is relative across the globe, and it relies on Third Party Indicators (TPIs), some of which are questionable owing to the quality and reliability of their sources and methodologies. Going forward, the authorities request staff to correct the errors and use proper phrases to reflect actual situations.

Economic Developments and Outlook

The Nigerian economy posted a 0.8 percent growth in 2017, driven mainly by recovery in oil production and prices as well as rising agricultural performance. With steadfast implementation of the reform efforts under the ERGP, the authorities estimate that growth will reach 3.5 percent in 2018. It is further estimated that growth will rise substantially in the medium term following strong execution of the capital budget, a rebound in private sector investment supported by the implementation of structural reforms, and higher oil production.

Foreign exchange (FX) availability has improved, from $27.0 billion in 2016 to a four-year high of $39.2 billion in 2017, owing to greater exchange rate flexibility and a tighter monetary policy stance, and a rebound in oil exports. That said, the exchange rate has stabilized, and the parallel market premium declined from 60 percent in February 2017 to 20 percent in December 2017. At the same time, financial markets soared, gaining 60 percent in value from end-2016 to mid-January 2018.

On the other hand, inflation declined to 15.4 percent year-on-year by end-December 2017, from 18½ percent at end-2016. It has since moderated to 15.1 percent in January 2018, and maintained the trend indicating twelfth consecutive month of decline, and is expected to reach lower double-digit rates by the end of 2018.

Fiscal Policy

To address the fiscal deterioration occasioned by the sharp fall in oil prices, the authorities are determined to reduce dependence on oil revenue and create space for private sector investment. Going forward, they aim to implement structural fiscal reforms, focusing on increasing non-oil revenue. In this context, the 2018 budget presented to the National Assembly in November 2017 targets a significant fiscal consolidation and a reduction of the overall fiscal deficit from 4.3 percent of GDP in 2017 to 1.4 percent of GDP in 2018. This conforms with plans under the ERGP to progressively cut deficits and contain borrowing.

The authorities are making determined efforts to improve tax collection and strengthen tax administration, including widening the tax base. In this regard, they plan to implement measures to double the tax compliance rate to about 50 percent through undertaking tax audits, using e-filing, conducting data matching exercises to close collection loopholes, strengthening tax enforcement, and combating corruption in tax offices. In addition, the authorities are examining the need to focus on large taxpayers to boost collection and establish a more dependable revenue base. Further, proposals have been tabled in parliament to increase excises on tobacco and alcohol, review stamp duties, and introduce a registration threshold for VAT. Furthermore, the authorities are reviewing the requirements for publication of tax expenditures together with the annual budget as part of an effort to strengthen transparency. In a drive to comprehensively reform tax administration, current efforts would be supplemented by recommendations from the upcoming Tax Administration Diagnostic Assessment Tool (TADAT) exercise.

Implementation of the Voluntary Asset Income Declaration Scheme (VAIDS) is expected to positively impact revenue collections by end-March 2018. Going forward, the authorities plan to table before parliament a Finance Bill containing proposals to increase excise rates, reform the Value Added Tax (VAT) system by introducing registration thresholds and removing exemptions, and introducing stamp duties. Implementation of the Oil Asset Divestment Strategy, together with possible privatization of the Nigeria Petroleum Development Company, is expected to yield additional revenues. The authorities are also advancing efforts to complete the audit of the Nigerian National Petroleum Corporation (NNPC), to determine its financial position in respect of arrears and revenue due to government.

The authorities plan to maintain expenditures at budgeted levels, and savings from recurrent costs will offset the increase in planned capital investment. Further, they have no plans to reintroduce fuel subsidy in the budget. The authorities are also committed to the ongoing rationalization of current expenditures to create space for capital spending to close the infrastructure gap, and remain committed to improving public expenditure efficiency. In addition, they intend to improve public debt management, through closer coordination among the central financial agencies and reinforcing expenditure controls. Furthermore, a strategy to replace a portion of existing T-bills with Eurobonds will be pursued, while plans to strengthen the capital market will be implemented. The authorities have also stepped-up efforts in monitoring fiscal activities, including the identification of arrears and the requirement for state and local governments to provide financial reports regularly. Finally, the authorities are strengthening the implementation of the Treasury Single Account (TSA) mechanism to effectively utilize idle resources, and reduce domestic borrowing.

Monetary Policy

The Central Bank of Nigeria (CBN) has pursued a tight monetary policy stance since July 2016 when the monetary policy rate (MPR) was raised from 12 percent to 14 percent to address inflationary pressures. The CBN will continue to be vigilant, and anticipate any fiscal and liquidity pressures ahead of the 2019 elections. In this regard, the Monetary Policy Committee (MPC) will be proactive in managing liquidity to achieve CBN’s price stability objective, while implementing measures to strengthen financial sector stability and inclusive growth. The CBN will also continue to strengthen the transmission mechanism to enhance monetary policy impulse.

Some areas in the staff assessment need further clarifications. For instance, from its experience, the MPC would emphasize that an increase in the MPR at this stage would be unwarranted since monetary policy tightening has been directed at reducing pressures on the exchange rate, a key factor for Nigeria's inflation dynamics. This addresses the staff's recommendation that increasing the MPR to positive real levels would more transparently reflect the CBN's intentions, help anchor inflation expectations, and signal forward-looking policy. Consistent with CBN's experience and the staff's findings on the study to understand monetary policy in Nigeria (SIP: P.86), the MPC would continue to finetune the monetary policy framework while deploying a range of instruments, including the MPR, open market operations (OMO), and cash reserve ratio (CRR), to contain inflationary pressures.

On the CRR, the MPC has restated its position that the rate remains 22.5 percent on eligible deposits as reflected in the latest MPC communique issued in November 2017. Further, the MPC has reiterated that applying CRR on deposit flows has merits for Nigeria, which suffers from structural liquidity surpluses, as opposed to CRR on deposit stocks recommended by staff. Lastly, the CBN would maintain its commitment to the development finance mandate as provided in the Act, and were the change to happen, it will take a medium to long term for a parliamentary approval regarding the divestment of interest in development finance institutions (DFIs) advised by staff.

Exchange Rate

As encapsulated in the ERGP, the authorities are committed to the unification of exchange rates in the medium-term. In this regard, the CBN has started implementing measures to stabilize the exchange rate. These include encouraging increased flows from remittances through licensed international money transfer organizations (IMTOs), more CBN sales in the interbank market, and the establishment of the investor and exporter foreign exchange (IEFX) window. In addition, the CBN is monitoring convergence of the two major FX windows between the forward transactions in the wholesale/retail window and the IEFX rate. Prospects are strengthening and foreign reserves have risen to $42.8 billion as at February 2018 on the back of large rice production capacity promoted by the CBN anchor borrower program. Going forward, the CBN intends to remove restrictions in the FX market for the 40-category products, once reserve buffers improve to comfortable levels.

Financial Sector

Apart from rising non-performing loans (NPLs) in a few sectors, Nigeria's financial sector remains broadly stable. The banks are adhering to stricter standards for internationally active players than required under Basel II, and balance sheets remain strong. Capital buffers can withstand financial reporting at a more market determined exchange rate, including the January 2018 transition to IFRS9 on which bank examiners are expected to harmonize recommended provisions with bank impairment charge.

In response to the rising NPLs, commercial banks have implemented stricter adherence to revised repayment plans for restructured loans and moved out of the NPL territory, especially for loans to the oil, gas and power sector. The reference to banks resorting to "ever-greening" of potentially problematic loans is unsubstantiated since loan restructuring provides for recognition of macroeconomic effects on expected cash flows.

That said, in line with its guardianship role over the banking system, the CBN is further strengthening its supervisory oversight and deployment of early warning systems to identify vulnerabilities and manage emerging risks in the financial system.

Structural Reforms

Authorities have continued to make progress on implementing structural reforms as envisioned by the ERGP. To this end, they have prioritized the resolution of structural impediments and committed to building on the progress made to improve the business environment, accelerating the power sector reform, strengthening governance, and promoting financial inclusion and gender equality, among others. Progress under the Power Sector Recovery Plan (PSRP) has included increased power supply generation which reached a new peak of 5100MW in the grid in December 2017; appointment of new boards for sector agencies; appropriate budget provisions to ensure government agencies pay their electricity bills and enable the bulk trader to pay in full for generated power; and an off-grid electrification strategy. The ERGP Implementation Unit established in the Vice President's office is expected to accelerate delivery on policies to develop industrialization, agriculture, and power sectors. In this context, the authorities plan to approach international development partners to secure technical assistance.

One of the targets the government set for gauging its progress in creating an enabling environment for business was to achieve a positive movement in the World Bank Ease of Doing Business. According to a recent World Bank business index ranking, Nigeria moved 24 places to 145th position in 2017, and was among the top 10 reforming countries in the world.

To pursue a gender-sensitive, pro-poor and inclusive growth, the 2018 Budget appropriation plan has retained the social intervention program noted for creating jobs, supporting small businesses, and providing finance and economic opportunities to the vulnerable people. Relating to governance and transparency, the authorities have adopted the National Anti-Corruption Strategy (NACS) and have committed to digitizing public officials' asset declarations, and the publication of the first national money laundering and terrorist financing risk assessment report.

Authorities acknowledge the remaining shortcomings in the data and are working to close those gaps, including seeking TA support to state and local governments fiscal data, reduction in the balance of payments errors and emissions, and continuous enhancement of the Debt Management Office to extend coverage to private sector liabilities and foreign investments.

Conclusion

The Nigerian authorities reiterate their commitment to sustain implementation of ongoing reforms and implement urgent comprehensive policies to support durable and inclusive growth. Pursuing a growth-friendly fiscal policy that is complemented by tight monetary and flexible exchange rate policies to contain vulnerabilities in the economy remains the focus. Policies would be anchored on stronger execution of the capital budget, investment-sensitive structural reforms and higher oil production. Additional priorities include actions to boost non-oil sector activity, reduce inflation to the target range, contain emerging banking sector vulnerabilities, and address unemployment. Lastly, the authorities value Fund advice and technical assistance, which have helped shape the policy direction over the years.

Mr. Fachada and Mr. Cheong submitted the following statement:

We thank staff for the reports and Mr. Mkwezalamba and Mr. Odonye for their informative statement. Following the terms of trade shock, the Nigerian economy is in the midst of a nascent recovery, supported in part by the authorities' reform agenda. The authorities' draft 2018 budget rightfully seeks to strengthen the fiscal position, the monetary policy stance is appropriate and the Economic Recovery and Growth Plan (ERGP) is beginning to bear fruit. In this context and like Messrs. Mkwezalamba and

Odonye, we wonder whether staff's use of the phrase 'muddle through' outcome under current policies is helpful.

We welcome the consolidation efforts envisaged in the draft 2018 budget and the authorities' medium-term plans to increase non-oil revenues. Although staff assess the budget to be somewhat ambitious, the authorities' use of a conservative oil price in the budget as well as measures to contain expenditure and mobilize non-oil revenues are steps in the right direction. With regards to the latter, the authorities' plans to better manage fiscal arrangements with State and Local Governments (SLGs), enhance tax administration, increase excises and undergo VAT reform are commendable and consistent with staff's recommendations. Nevertheless, we encourage the authorities to consider the merits of staff's recommendations on these areas detailed in the Selected Issues paper, and also support staff's calls to strengthen public financial management, make better use of the Single Treasury Account and closely monitor the fiscal risks from SLGs.

In the context of still high inflation, the Central Bank of Nigeria's (CBN) tight monetary policy stance seems appropriate. To strengthen the monetary transmission mechanism and anchor inflationary expectations, we agree with staff that the CBN should better align money market rates with the monetary policy rate (MPR) and enhance its communication strategy. Additionally, although staff did not raise the issue of CBN financing of the budget in this year's report, we note that CBN's claims on the federal government (FGN) is projected to increase sharply over the forecast horizon (Table 7). Can staff comment on the projected increase in the CBN's claims on the FGN?

Plans in the ERGP to unify the exchange rate are welcome. Though not in-line with conventional approaches, the authorities' foreign exchange policies have helped Nigeria weather the fall-out from the terms of trade shock. The real effective exchange rate (REER) model suggests that the official exchange rate is overvalued by 12.0 percent, which implies that non-official exchange rates should be more in-line with fundamentals. We encourage the authorities to resolutely move towards unifying the exchange rate at a level consistent with Nigeria's fundamentals.

Although near-term prospects have improved, the authorities should remain vigilant against financial stability risks and avoid complacency. While banks in aggregate are profitable, capital adequacy indicators are near minimum thresholds and non-performing loans to total gross loans are significantly higher than a few years ago. We support many aspects of staff's recommendations to improve financial stability, but we also take note of the authorities’ views on regulatory forbearance.

We welcome the authorities’ commitment to the ERGP, and note that progress has been made on several fronts. In particular, improvements in the World Bank Doing Business rankings, the National Anti-Corruption Strategy, the adoption of the Petroleum Industry Governance Bill and the publication of the national money laundering and terrorist financing risk assessment report are commendable achievements. We encourage the authorities to work towards closing the infrastructure gap and continue to undertake critical elements of their structural reform agenda.

Mr. Saito and Mr. Naruse submitted the following statement:

We thank staff for informative reports and Mr. Mkwezalamba and Mr. Odonye for their insightful statement. It is encouraging that Nigeria’s economy is recovering, driven mainly by rising oil production. We positively note that the authorities initiated reforms under the Economic Recovery and Growth Plan. Going forward, we encourage the authorities to continue to implement comprehensive policies, such as measures to increase non-oil revenues, to narrow the infrastructure gap, to improve the business environment, and to contain corruption. As we broadly concur with the thrust of the staff’s appraisal, we will limit our comments to the following points:

Fiscal Policy

We agree with staff that increasing non-oil revenues is important. We welcome the authorities’ recent efforts towards revenue mobilization, including increases in exercises and the reform of the VAT. It is also encouraging that the authorities have taken steps to strengthen tax compliance, through measures such as increasing tax audits and using e-filing. We encourage the authorities to continue to improve collection through tax administration efforts.

We take note of the staff’s assessment that Nigeria’s public capital stock is low and of relatively low quality and that capital expenditures have been smaller and less efficient. In this light, we agree with staff that continuing to rationalize current expenditures to make room for much needed capital spending to close the infrastructure gap is important.

Monetary and Exchange Rate Policy

On monetary policy, we note that the Central Bank of Nigeria (CBN) has pursued a tight monetary policy stance to address inflationary pressures, and it is encouraging that the Monetary Policy Committee will be proactive to achieve CBN's price stability objective. On exchange rate policy, we take note of the ongoing convergence of exchange rate windows, and it is also encouraging that the authorities are committed to the unification of exchange rates.

Financial Sector Policy

We welcome the fact that the bank's liquidity resilience remains strong and that the maturity and interest rate mismatch between assets and liabilities is contained. On the other hand, we note that capital buffers have dwindled over the past two years. We therefore encourage the CBN to continue to monitor sectors with high nonperforming loans. Also, we note that recapitalizing the four undercapitalized banks is long overdue. We would welcome the staff's comments on the necessity of the CBN's capital injection into the four undercapitalized banks.

We agree with staff that enhancing banking supervision by strengthening the risk-based on-site inspections and the enforcement of prudential requirements is recommended. We also concur with staff that the resolution framework should be strengthened in line with international best practices to bolster confidence and minimize risks to the CBN's balance sheet.

Structural Reform

We take note of the staff's analysis that longstanding structural issues, such as a weak business climate and high corruption, hamper the recovery of the economy and export diversification. We welcome the improvement in the recent World Bank Doing Business Rankings due to the authorities' actions to improve the business environment. We are also pleased to see that the authorities have advanced anti-corruption measures, such as the adoption of the National Anti-Corruption Strategy. We look forward to seeing its effective implementation in the future.

Mr. Rashkovan and Mr. Josic submitted the following statement:

We thank staff for the interesting set of papers, as well as Messrs. Mkwezalamba and Odonye for their helpful buff statement. The

Nigerian economy is slowly recovering after a period of stagflation and the authorities' recent efforts, particularly on improving the business environment, are welcome. Nevertheless, structural weaknesses, corruption, elevated poverty and rising vulnerabilities require a steadfast and front-loaded policy reaction. We agree with the thrust of the staff appraisal, and would like to emphasize the following points.

The medium-term growth outlook is only half of what it was two years ago. We note that Nigeria is slowly recovering from the commodity price shock. However, staff's current projection for GDP in the medium-term is around 2 percent, compared to almost 4 percent two years ago, despite the increased oil prices, recent improvements in the business environment and some implemented reforms. Staff's comments on the significant drop in the growth outlook are welcome. In addition, could staff include estimates of the potential output and the output gap?

We agree with staff on the need for a steadfast implementation of growth-friendly fiscal consolidation based on the adjustment scenario. We acknowledge the authorities' efforts to improve the tax administration and to increase revenue mobilization, as emphasized in Messrs. Mkwezalamba and Odonye's buff statement. However, the federal government interest payments-to-revenue ratio has already reached an unsustainable level and fiscal deficits are projected to remain large. Against this background, we call on the authorities to implement staff's recommendations from the last two Article IV reports by increasing non-oil revenues and rationalizing current expenditures. In addition, we encourage the authorities to finally implement the automatic and independent price-setting mechanism for petroleum product prices.

The debt sustainability analysis (DSA) could be affected by the quality of the data. The risk assessment matrix points to a high likelihood of worsening of State and Local Government (SLG) finances with high impact. At the same time, we take note of staff's assessment that there is considerable room for improvement of SLG fiscal data, SOE fiscal operations and domestic arrears monitoring. Could staff be more specific about the data gaps and whether any PPP contingent liabilities are included in the DSA?

We support staff's recommendation to move to a unified exchange rate. This would help increase the credibility of the Central Bank of Nigeria (CBN), eliminate foreign exchange shortages and increase the resilience of the economy. At the same time, existing capital flow measures (CFMs) should be discontinued in line with the Fund's institutional view. However, to bear fruit, a coordinated action plan between all stakeholders will be required. Staff estimates that the real exchange rate (RER) is overvalued by about 12 percent, although most of this estimate is not explained (country specific), as evidenced in high residual. Staff's comments are welcome.

Addressing structural impediments is critical for long-term sustainable growth. We welcome the authorities' recent efforts on the implementation of the Economic Recovery and Growth Plan (ERGP) and the development of the National Anti-Corruption Strategy (NACS). However, more needs to be done as reform needs are large. The focus on export diversification should be reintroduced, tackling corruption should be accelerated and the business environment further strengthened. The ambitious infrastructural development agenda should be accompanied by strengthening the Public Investment Management (PIM) framework, aligning the laws on corruption with the UN Convention against Corruption and by transparent monitoring of these projects.

Poverty in Nigeria remains pervasive. Despite the impressive growth in the 2000s and a considerable number of social programs, not much has been done to effectively reduce poverty. According to the latest UNDP results, Nigeria is ranked low on the Global Human Development Index. The average years of schooling is only 6.0, for women only 4.9, while almost 70 percent of the population is, or is close to, multidimensional poverty. We therefore encourage the authorities to develop social safety net programs that will improve access to education, increase the labor participation of women and address the issue of gender and income inequality in line with the sustainable development goals. Addressing these structural impediments could significantly improve the productivity, boost potential output and accelerate GDP per capita convergence to its peers.

Mr. Inderbinen and Mr. Ahmadov submitted the following statement:

We thank staff for the good set of papers and Mr. Mkwezalamba and Mr. Odonye for their informative buff statement. We take good note of the recent recovery on the back of firmer oil prices, increased extraction, and recent reform efforts. These positive developments notwithstanding, non-oil growth has, apart from agriculture, not increased, unemployment is rising, poverty remains high and the humanitarian crisis in the North East is ongoing. The forthcoming elections underline the importance of not delaying the implementation of comprehensive reforms.

Decisive policy action is called for to address the significant distortions and reduce vulnerabilities. We welcome the initiated implementation of the authorities' Economic Recovery and Growth Plan, and the broad alignment of the ERGP with advice provided during the 2017 Article IV cycle. We also take good note of the establishment of a high-level implementation unit. As staff notes, consistent implementation of the Plan will be critical.

Fiscal adjustment will be essential. The significant correction envisaged under the 2018 budget is welcome. Sustained strengthening of Nigeria's fiscal position will hinge on measures to broaden the non-oil tax base and to increase overall revenue from its singularly low level. It is encouraging that the authorities and staff are in broad agreement on the measures that are called for in this regard, and that action is being taken to reform the VAT, strengthen tax administration, and improve transparency. We welcome the upcoming TADAT exercise, and would encourage the authorities to take further steps in accordance with its outcome. On the expenditure side, apart from the recommendations staff lists in paragraph 22 of the report, a review of fiscal transfers to the states would seem advisable. Is a review of the Budget Support Facility envisaged in the authorities' reform plans; and has staff engaged with the authorities on possible improvements to the current framework of fiscal federalism, beyond the TA requested to improve fiscal data at the local and state levels?

Clarifying the monetary policy framework would be beneficial. We note the differences between staff and the authorities on the adequacy of increasing the policy interest rate to a positive level in real terms. More broadly, we would argue for a clearer focus of the mandate of the Central Bank of Nigeria on price stability. This would involve a cessation of development financing by the central bank. We realize that this would necessitate legislative action. Also, CBN's direct lending to the government should be terminated.

We support staff's recommendation to rapidly unify the exchange rate. We note the convergence of rates under the two main forex windows. However, the current MCPs and the array of restrictions on current payments and capital flows continue to entail unnecessary distortions. We note the authorities' commitment to exchange rate unification, but would encourage them to bring corrective action forward.

We welcome the priority that the ERGP affords to structural reforms to strengthen the business environment and advance with the diversification of the economy. The adoption of the anti-corruption strategy is a welcome step. We encourage the authorities to take the recommendations that staff makes in the excellent Selected Issues Paper on strengthening transparency and governance under advisement, including criminalizing corruption in line with UNCAC, further increasing transparency in the oil sector, and strengthening the AML/CFT regime.

Mr. Merk and Mr. Rosenberger submitted the following statement:

We thank Mr. Mkwezalamba and Mr. Odonye for their insightful buff statement and staff for their comprehensive set of papers. We broadly concur with the thrust of the staff's appraisal.

The beginning economic recovery in Nigeria is encouraging. Both, higher oil prices and incipient dividends from reforms under the Economic Recovery and Growth Plan (ERGP) have contributed to a moderate pick-up in economic growth. Following a tighter monetary stance, inflation has declined somewhat but remains elevated. External reserves were strengthened and access to foreign exchange has eased but markets remain segmented. Higher fiscal deficits have contributed to larger financing requirements in the domestic market and a rise in public debt which, however, remains at relatively low levels. The banking system is facing rising vulnerabilities especially with regard to deteriorating asset quality. Taking note of the rather lacklustre economic outlook under current policies with substantial risks to the downside, we join staff's call for the upfront implementation of a comprehensive package of policy adjustments and structural reforms. Against this backdrop we would like to emphasize the following points on fiscal policy, monetary policy, financial sector, and structural reform agenda.

Staff projects debt service requirements to rise substantially under the baseline. Barring a determined policy change, interest spending is projected to reach unsustainable levels of well over 80 percent of federal government revenue by 2022. In order to avoid such a scenario, we join staff's call to frontload the necessary adjustment through additional fiscal consolidation. To this end, strengthening tax compliance and enforcement as well as reforming excise and VAT regimes will be essential to raise non-oil revenue. Amongst other important measures discussed extensively by staff, the authorities should further improve the composition of expenditures, rationalizing current expenditures to the benefit of high quality capital spending. While pushing ahead the necessary consolidation, we call on the authorities to ensure an adequate level of protection for the most vulnerable. Taking note of substantial deviations in economic assumptions and projections between staff and the authorities, we would welcome additional staff comments including on staff's forecast track record—which appears quite strong overall—and any efforts to improve outreach and communication of staff positions.

Tight monetary policies and a stronger emphasis on the central bank's core mandate of price stability will be essential to rein in the persistently elevated inflation. We recognize the CBN's efforts to tighten monetary policy by actively draining liquidity. However, we join staff in their call for a more institutionalized and transparent approach. Discontinuing the practice of unannounced special open market operations while raising the monetary policy rate (MPR) to appropriately positive real levels should help clarify communication, anchor inflation expectations and strengthen predictability by stabilizing money market rates and aligning them more closely to the MPR. In addition, we call on the authorities to strengthen the CBN's operational and institutional independence and refrain from further deficit financing. We concur with staff that measures to strengthen market forces on foreign exchange markets and increase flexibility in the exchange rate regime should be pursued decisively and in a timely manner.

We join staff in its call for comprehensive action to bolster resilience in the banking system. Against the background of a worrying deterioration in capital buffers and asset quality, a comprehensive and independent Asset Quality Review does not only appear advisable from a financial stability perspective, but could also help bolster investors' confidence, lower banks' refinancing costs and strengthen their lending capacity. Capital buffers should be raised where necessary while problematic loans should be adequately provisioned for and timely written-off.

Decisively tackling remaining structural impediments will be key to facilitate well-diversified, sustainable and inclusive growth. Progress has been reached in strengthening the business environment, reforming the energy sector and in strengthening anti-corruption and AML/CFT frameworks. However, important challenges persist, including remaining deficiencies in transparency and governance as well as in gender equality, which call for unwavering reform effort along staff's suggestions. The authorities' general commitment to continued structural reforms is encouraging in this regard.

Mr. Alogeel and Mr. Keshava submitted the following statement:

We thank staff for the comprehensive set of reports and Mr. Mkwezalamba and Mr. Odonye for their informative buff statement. We welcome the economic recovery in Nigeria, supported by the rebound in oil prices and the reforms initiated under the authorities' Economic Recovery and Growth Plan (ERGP). We are also encouraged by the significant narrowing of the parallel market exchange rate premium, reduced inflationary pressures, significant rise in international reserves, and improvement in the business environment. At the same time, Nigeria continues to face a number of challenges, as outlined in the staff report. It will therefore be important to pursue strong macroeconomic policies and implement further reforms to achieve robust and inclusive growth, address high unemployment and poverty, and enhance resilience. We are in broad agreement with staff's policy recommendations and would like to emphasize a few issues.

We are encouraged by the planned fiscal consolidation in the draft 2018 budget through significant non-revenue mobilization and rationalization of current expenditures. In this regard, it will be important to sustain efforts over the medium term to substantially increase non-oil revenue to create the necessary space for undertaking priority capital spending and for expanding social safety nets. Increased revenues over the medium term will also help in reducing federal government's interest payments-to-revenue ratio to the authorities' 30 percent objective by 2022 from the estimated 72 percent in 2017. In this context, the focus, as recommended by staff, should be on large taxpayers and more ambitious tax policy measures, including through reforming the VAT and rationalizing tax expenditures.

On debt management, we recall staff's response to the questions during last year's Article IV discussion that Nigeria practices sound debt management and a medium-term debt management strategy is in place. Against this background, we would welcome staff comments on what should be an appropriate long-term objective of external-to domestic-debt ratio, as staff seems to consider the authorities' goal of 40 percent to be high (paragraph 22, sixth bullet point).

Although inflation has moderated, it is still in double digits and we therefore agree that monetary policy should remain tight until inflation is within the CBN's 6 to 9 percent target range. We join staff in welcoming the progress made toward unifying some of the exchange rate windows and encourage the authorities to continue their efforts to move toward a full exchange rate unification. While international reserves are at a four-year high, it is important to further accumulate reserves to mitigate risks from external shocks. Enhancing banking sector resilience is also a priority in view of the declining bank solvency ratios and asset quality. In this connection, we are encouraged to note in the buff statement that the CBN is further strengthening its supervisory oversight and deployment of early warning systems to identify vulnerabilities and manage emerging risks in the financial system.

Finally, we welcome the progress on the structural front, including the improvement in doing business indicators, the adoption of the National Anti-Corruption Strategy, and the strengthening of the power sector. In line with the ERGP, the authorities should continue their efforts to advance their structural reform agenda.

With these remarks, we wish the authorities further success.

Mr. Ostros and Mr. Bartkus submitted the following statement:

We thank staff for a comprehensive set of papers and Messrs. Mkwezalamba and Odonye for an informative buff statement. Aided by higher oil prices and improved policies, the Nigerian economy is slowly emerging from recession, though substantial economic and policy challenges still prevail.

A growth-friendly consolidation is urgently needed to reduce debt service costs, focusing on non-oil revenue mobilization and phasing out fiscal dominance. The authorities shall also prioritize supply-side structural reforms, respond to building up financial stability risks, and develop a well-articulated and time-bound strategy to phase out exchange rate restrictions.

We commend staff for a thorough analysis in the selected issues paper that covers a broad set of macro-critical issues, ranging from revenue mobilization and distributional effects of fiscal policy to governance and transparency, term structure of interest rates, and monetary policy challenges. We particularly welcome a convincing analysis on gender inequality that provides evidence of economic and social costs of gender inequality.

The authorities’ macroeconomic and fiscal projections seem to suffer from a persistent optimistic bias that might complicate economic policy making. The 2017 growth outcome is broadly in line with that assumed by staff during the 2017 Article IV discussion and significantly below that of the authorities (0.8 percent versus 2.2 percent). Even under the adjustment scenario assumed by staff, the medium-term growth in Nigeria will stay significantly below 7 percent expected by the authorities.

The 2017 fiscal outturn was 1.5 percent of GDP lower than in the budget and the draft 2018 budget seems also overly optimistic, with significant consolidation based on assumed gains from improved tax compliance that are unlikely to materialize in the short-term. We would urge the authorities to err on the side of caution in their economic policy planning, considering broader tax policy changes as proposed by staff to make a viable progress on consolidation.

We welcome progress in improving the monetary policy consistency, with tighter monetary policy stance contributing to disinflation, narrowing exchange rate premium in the parallel market, and accumulation of reserves. At the same time, we echo staff's emphasis on the need to phase out the CBN's direct lending to the government, increase interest rates to positive level in real terms, and enhance the monetary policy transparency. The exchange rate unification and phasing out of multiple currency practices should be pursued as soon as possible, improving economic policy consistency will prove crucial in this regard.

We note concerns about reported signs of evergreening in the banking sector and support the key elements of the strategy to strengthen financial resilience as proposed by staff, notably the proposal for AQR, phasing out regulatory forbearance, strengthening bank capital buffers, and enhancing the regulatory and supervisory frameworks. We would appreciate a further update on the overdue recapitalization of four undercapitalized banks, specifically whether any steps have been taken to improve financial standing of these institutions?

We take note that the authorities implementation of the ERGP strategy has helped to make important strides in improving Nigeria's business environment and governance. Ranked 145th in the World Bank 2018 Doing Business report, Nigeria has significant scope for catchup and further determined efforts are needed to advance towards a more supportive business environment building on the progress so far.

Mr. Jin and Ms. Lok submitted the following statement:

We thank staff for the comprehensive reports and Mr. Mkwezalamba and Mr. Odonye for the informative buff statement. As Nigeria exits from recession, it continues to face a number of vulnerabilities which should be addressed through timely and steadfast actions by the authorities to improve economic resilience and promote sustainable and inclusive growth. In particular, we encourage the authorities to continue to implement the measures and policies under the Economic Recovery and Growth Plan

(ERGP). We broadly agree with staff's appraisal and would like to limit ourselves to the following comments for emphasis.

Strong efforts to mobilize non-oil revenue are critical to successful fiscal consolidation. We welcome the authorities' determination to reduce dependence on oil revenue, and note that staff have suggested some valid options for revenue mobilization in the Selected Issues Paper. The draft 2018 budget sets out some ambitious consolidation goals, relying heavily on the ability to mobilize non-oil revenue through various channels. The authorities' efforts to improve tax collection, strengthen tax administration, and broaden the tax base, should contribute to achieving these goals. Overall, we share staff's view that a broad-based and comprehensive set of reforms can help unlock Nigeria's revenue potential and create a more sustainable revenue stream.

Enhancements to the monetary policy and exchange rate frameworks should continue. With inflation still significantly above the Central Bank of Nigeria's (CBN) target range of 6 to 9 percent, there is a case for keeping monetary policy tight and strengthening the policy framework. We see merit in some of staff's suggestions for enhancing CBN's monetary policy framework, such as increasing transparency of operations and improving communication. We continue to welcome the authorities' commitment to a unified exchange rate, as underscored in the ERGP, and take positive note of the ongoing convergence of exchange rate windows

Banking sector resilience should be strengthened to safeguard financial stability. In the face of uncertainties surrounding both the domestic and external environments, efforts should be made to increase buffers in the banking sector to boost its resilience against potential shocks. Intensified supervision and a sound resolution framework will contribute further to this resilience. We are pleased to note that the authorities have taken staff's recommendation to conduct an Asset Quality Review on banks, and look forward to results from the review. We note from the Authorities' views in paragraph 34 that the CBN has asked banks to conduct stress testing scenarios. Could staff share information on the relevant test results, if any? Separately, according to staff, vulnerabilities persist in the banking system. What is staff's take on the recent stock market rally that is driven mainly by the financial sector, and do staff see any potential risks to financial stability?

Addressing structural impediments is key to achieving sustainable and inclusive growth. We are pleased to note that tackling structural issues are a priority for the authorities and the ERGP, and actions taken so far have resulted in a substantial improvement in Nigeria's Doing Business ranking by 24 places. Nevertheless, more efforts are needed to address issues including corruption, weak financial inclusion, and inequality. We welcome the adoption of the National Anti-Corruption Strategy and the authorities' commitment to digitizing public officials' asset declarations. To promote sustainable and inclusive growth, we encourage further efforts in narrowing the infrastructure gap, reducing gender inequality, and diversifying the economy. Enhancements to the efficiency of public institutions and investments will help maximize the benefits from these efforts.

Finally, noting the concerns raised by the authorities in the buff statement, we encourage that caution be exercised by staff in their choice of words in reports and use of Third Party Indicators.

With this, we wish the authorities every success with their endeavors.

Mr. Gokarn and Mrs. Roy submitted the following statement:

We thank staff for the reports on Nigeria and Mr. Mkwezalamba and Mr. Odonye for the informative buff statement.

Following five successive quarters of recession, the Nigerian economy has rebounded during the second quarter of 2017 on the back of strong implementation of macro policies initiated under the Economic Recovery and Growth Plan (ERGP). However, the need to boost non-oil sector activity, reduce inflation to the target range, contain emerging banking sector vulnerabilities, and address unemployment while pursuing a growth-friendly fiscal policy that is complemented by tight monetary and flexible exchange rate policies to contain vulnerabilities in the economy remains.

While economic conditions in 2017 show a tentative improvement on the back of recovering oil production and agriculture, non-oil, non-agricultural economic activity has yet to pick up. Given the experience of Nigeria after the oil price crash in 2014, when it suffered a recession along with weakening of external and fiscal buffers, a significant diversification of economic activities so as to provide cushion against sectoral shocks and employment opportunities for the general population is necessary. As unemployment is rising and poverty remains high, and as demographic trends imply that Nigeria could be the third most populous country in the world by 2050—it is necessary for the policymakers to look to diversify the economic structure for fostering faster growth, improve per capita incomes, and significantly reduce high unemployment and poverty. It is a matter of concern that export diversification has decreased in recent decades, reflecting long-standing structural issues which should be resolved to enhance economic efficiency and diversification. Given its large domestic population, even production for the domestic population in diversified sectors could result in gains. In which areas could Nigeria diversify its economic structure, given its natural endowments?

The federal fiscal deficit is running at 4.3 percent of GDP which is 50 percent higher than in 2016, and state and local governments' balance sheets remain fragile. Financing of this fiscal deficit and increased risk aversion on part of the banks has led to a decline in private sector lending. Monetary policy remains significantly tight with the CRR at 22.5 percent and the monetary policy rate (MPR) at 14 percent, unchanged since March and July 2016, respectively. Furthermore, liquidity draining operations have kept money market rates at, on average, twice the MPR. The staff report says that monetary policy would be tightened in the short-term to lower inflation to the CBN target range of 6–9 percent and loosened in the medium term once inflation has stabilized. Since supply factors are keeping inflation high and private borrowers are facing credit constraints, what steps could the authorities take to remove the supply constraints so that it would be possible for the central bank to loosen monetary policy and encourage investment and growth?

With bond issuances keeping yields high, the interest payments-to-revenue ratio for the federal government is estimated at 72 percent for 2017 as a whole and is projected to rise to 82 percent by 2023. This needs to be brought down from such high levels. The staff report states that this requires increasing non-oil revenues by 8 percentage points over the next five years to help reduce the interest-payments-to-revenue ratio to a more sustainable level. Given the lack of growth momentum in the non-oil sector mentioned earlier, how will greater revenue collection from the non-oil sector be possible?

Non-performing loans (NPLs) have increased from 5 percent of total loans in June 2015 to 15.6 percent in October 2017. While it is encouraging that about 82 percent of NPLs are fully provisioned, commercial banks pre-emptively restructured loans -particularly in the oil, gas and power sector – ranging between 2 and 30 percent of total loans (averaging 10 percent) for the largest banks. While the buff statement says that "Following the staff's recommendation, the CBN bank examiners and external auditors of banks have started the Asset Quality Review (AQR) and the results are expected in due course", the Authorities' views in the staff report states that the CBN has already asked banks to conduct their own stress testing scenario and does not believe an AQR is needed. Staff may like to clarify the exact steps being taken by authorities with regard to identification of NPL.

In recent months, foreign exchange availability has improved, the exchange rate has stabilized, and the parallel market premium declined from 60 percent in February 2017 to 20 percent in December 2017. However, according to the staff Report, foreign exchange market distortions are slowing efforts to attract long-term investment and diversify the economy. Removing distortions in the foreign exchange market, which should be unified and contribute to strengthening reserve buffers, would help boost investor confidence, raise growth, and reduce inflation to single digits. What would be the extent of positive impact on growth and inflation if the distortions in the foreign exchange market were removed?

With these remarks, we wish the authorities every success in their future endeavors

Mr. Beblawi and Ms. Al-Riffai submitted the following statement:

We thank staff for a comprehensive set of reports and Messrs. Mkwezalamba and Odonye for their informative buff statement. The Nigerian economy is still recovering from terms of trade shock which was exacerbated by the decline in oil production and policy challenges. An increase in oil prices and implementation of the authorities' Economic Recovery and Growth Plan (ERGP), including new foreign exchange measures, tighter monetary policy, and contained inflationary pressures, have been contributing to the economic recovery. However, vulnerabilities remain, as well as a large infrastructure gap, a dormant non-oil non-agriculture sector, and fiscal dominance, compounded by weak non-oil revenue generation and high interest payments-to-revenue ratio. We broadly concur with the staff report and have the following points to highlight:

We commend the authorities on their recent reform measures which have aimed to strengthen revenue collection, while concurring with staff that more still needs to be done, including broadening the tax base, closing loopholes and leakages, and doing away with exemptions. Nigeria has one of the lowest tax revenue-to-GDP ratios compared with peers, currently at 5.1 percent. Staff estimates additional revenue generation of 8 percent of GDP by 2023 is possible once Nigeria completes its tax reforms. The planned tax reforms are progressive, and we would like to underscore the importance of improving the efficiency, reach, and targeting of the social safety nets to mitigate the impact of the reforms on the most vulnerable.

Foreign exchange reforms have provided some liquidity to the foreign exchange market whose objective is to reach a unified rate under the ERGP. We commend the authorities on their efforts to achieve this goal and urge them to continue working towards achieving this objective. We understand that this has been a long-standing goal, and we would accordingly be interested in staff's assessment of the impediments to achieving it.

We note staff's assessment that there is considerable room for improving data on state and local governments (SLG) finances, SOE fiscal operations, and domestic arrears monitoring. At the subnational level, SLGs have political and fiscal autonomy, as well as varying regional socioeconomic disparities. We concur with staff on the importance of increasing SLG monitoring. This would help to reduce arrears accumulation and increase internally generated revenue, and we acknowledge the efforts to improve data in those areas, including through Technical Assistance. Given the efforts to date, we trust that the statistical infrastructure will be in place to successfully adhere to the reform timeline.

We take positive note of the numerous initiatives taken by the authorities to improve transparency and governance, including through a home-grown plan to strengthen fiscal discipline as well as the accountability framework of SLGs. We concur with staff on the need for SLGs to comply with the 22-point Fiscal Sustainability Plan (FSP) prior to receiving budgetary disbursements from the Federal Government. Can staff shed additional light on rationale for maintain the monthly transfers to some states despite their non-compliance with their FSP?

We wish the Nigerian authorities further success in their reform efforts.

Ms. Barron and Mr. Amor submitted the following statement:

We thank staff for their report and Mr. Mkwezalamba and Mr. Odonye for their helpful buff statement. We welcome the recent economic recovery in Nigeria, supported by recovering oil production and agriculture, and the authorities' ongoing reforms under the Economic Recovery and Growth Plan (ERGP). However, considerable issues remain to be addressed on all fiscal, financial and structural fronts, in addition to the ongoing security and humanitarian crisis in the Northeast. The authorities are taking measures to address vulnerabilities and we support the thrust of the staff's recommendations that continuing reforms are needed to support a durable economic recovery and address inequality.

Fiscal consolidation is needed to create the fiscal space necessary for growth-enhancing capital spending and poverty reduction. We commend the authorities' strong efforts on improving tax administration through audits, compliance enhancement and combating corruption, and their efforts on strengthening tax policy through ongoing excise and VAT reforms. Given the large development financing gap, we agree that more efforts are needed on both tax administration and policy enhancement with a focus on improving compliance and strengthening non-oil revenue. In parallel with the revenue measures, further efforts are needed to streamline fiscal spending, including through wage bill containment, incentives and fuel subsidies phase out, and better targeting social safety nets to protect the most vulnerable. We therefore appreciate the clarification in Mr. Mkwezalamba and Mr. Odonye's buff statement that the authorities have no plans to reintroduce the fuel subsidy in the budget. We support staff's policy recommendations, but noting that the authorities are already undertaking several fiscal initiatives, we seek staff's opinion on proper sequencing of the reforms in the short to medium term.

We support staff's position on tighter monetary policy and a unified, market-based exchange rate. The current tightening of monetary policy is necessary to help anchor inflation expectations and bring inflation gradually back to the target. A liberalized forex market will eliminate foreign exchange shortages, increase economic resilience to external shocks, and prevent deterioration of the international reserves position. We commend the authorities for unifying some of the exchange rate windows and encourage continued progress towards exchange rate unification, and full elimination of categorial foreign exchange access restrictions. We concur with staff's recommendation on not approving the exchange restrictions and MCPs. Can staff comment on their discussions with authorities regarding a timeline for removal of the exchange restrictions and MCPs?

We encourage the authorities to continue their efforts to enhance banking sector resilience and protecting financial stability through strengthening regulations and prudential requirements, close monitoring, and recapitalizing banks. We note positively in the buff statement that the authorities have started the Asset Quality Review process.

A durable economic recovery will require more efforts on structural reforms to develop economic infrastructure, improve human capital, and enhance the business environment. The progress under the ERGP is welcome and we encourage the authorities to sustain their efforts on improving governance and the business environment. Given the large infrastructure gaps and the need for strong fiscal consolidation, resource allocation should focus on growth-enhancing infrastructure projects in energy and transport, as well as pro-inclusive growth spending on education, health, and agriculture development. More efforts are also needed to address poverty issues. While we welcome the social safety net expansion program under the National Social Safety Nets Project, only 1 million households (10 percent of the poor) will benefit from it in the medium term. Increased scope may be constrained by limited resources, so we encourage authorities to ensure effectiveness, fairness, and transparency in the design and implementation of national safety nets to better attract additional support from donors.

We thank staff for the selection and high-quality assessment of the Selected Issues Papers. In particular, we appreciate the analysis on the interconnectedness between gender inequality and broader inequality and development issues. As noted in staff's paper, a reduction in gender inequality to regional levels could yield per capita GDP growth of 1¼ percent annually in Nigeria. This shows the significant economic benefit of addressing gender equality. While the ongoing efforts to address gender inequality by the authorities and civil society groups are commendable, we encourage authorities to actively pursue evidence-based solutions to gender inequality, including legal rights enforcement and improving access to health, education and financial services.

We encourage the authorities to implement their National Anti-Corruption Strategy without delay, and consider adopting staff's recommendations to further advance their anti-corruption policies. This will ensure that significant progress achieved on fiscal and structural reforms are not effaced by corruption practices. We note that staff's analysis does not rest solely on perceptions based on third party indicators but also draws heavily on the 2016 Corruption Survey undertaken by Nigeria's National Bureau of Statistics.

Mr. Lopetegui and Mr. Vogel submitted the following statement:

We thank staff for the reports and Mr. Mkwezalamba and Mr. Odonye for their helpful buff statement.

Nigeria will need to address substantial challenges and risks in the short and medium term and the recovery of oil prices provides a new opportunity for the country to pursue remedial measures and the needed structural transformations. The analysis presented in the staff report is eloquent in many respects. Although increasing from the past few years, the country's projected growth rates in the baseline scenario are still low and definitively insufficient to ensure healthy employment growth to absorb an increasing labor supply given Nigeria's demographic trends; at least for the next couple of years, non-oil GDP will be below the total GDP, which reflects the scarce dynamism of non-oil activities and the imperious necessity to diversify the country's economy. The overall fiscal situation is worrisome and among various problems, a very low tax collection ratio is clearly the most relevant. Fiscal dominance complicates the battle against inflation, leading to a tight monetary stance that poses additional obstacles to Nigeria's economic dynamism. Multiple exchange restrictions and rates generate distortions and undermine confidence and investment. Corruption remains high despite some progress in strengthening the legal framework.

We tend to agree with the staff's recommended policies, but we wonder if the proposed adjustment scenario is beyond realistic expectations. According to staff, in the adjustment scenario growth rates would be one percentage point higher in 2018 and two percentage points higher in 2019, amid a tighter fiscal position, tight money, and presumably some real depreciation that could hurt consumption. We agree about the necessity and urgency of implementing reforms on the tax system and revenue administration in line with staff's guidelines, but will the effect be so growth-enhancing and rapid as envisaged? Staff's comments are welcome. The Selected Issues' chapter on the distributional impact of fiscal reforms in Nigeria clearly shows the necessity to generate fiscal space in order to be able to respond to the country's social and infrastructure demands.

Despite the tight monetary policy stance, inflation continues to be at relatively high levels, indicating that this monetary stance will have to remain while mitigating fiscal dominance and significantly reforming Nigeria's exchange rate system. Although it illustrates the problems of having multiple objectives, the chapter on monetary policy provides sensible recommendations on monetary policies' instruments and framework, which should be much more transparent.

As the literature and, especially, empirical evidence show, a multitude of exchange rates constitutes a significant burden for a country's economy, not only in the short term, but particularly in the medium term where poor governance, corruption, and rent-seeking often accompany these kinds of systems. Therefore, we fully agree with staff on the urgent need to move toward a unified and free exchange rate system and welcome the fact that this critical transformation is included in the authorities' Economic Recovery and Growth Plan. We would like to have a further elaboration from staff on the eventual effects of the transformation of the exchange rate system on the banking system?

Banking sector risks should be reduced. Asset quality and capitalization have deteriorated, and enforcement of prudential regulation is not strict, leading to increased financial stability risks. It is important to enhance banking regulation and supervision and to undertake the necessary recapitalization of undercapitalized banks. The resolution framework needs to be upgraded along the lines suggested by staff.

We welcome staff's work on Strengthening Transparency and Governance in Nigeria. We congratulate the authorities for their progress on the new anti-corruption strategy and compliance measures. We encourage them to continue this path, including enacting reforms needed to ensure corruption is criminalized in line with the UNCAC, facilitating effective coordination among investigative agencies, and other measures suggested by staff in the Selected Issues paper. Against this background, we think that it is important to highlight that the overall regulatory framework appears to offer excessive discretion in economic policy matters, from tax policy exemptions and tax administration, to public financial management and personnel decisions, foreign exchange restrictions, financial regulation forbearance, and ad-hoc monetary policy operations.

We these comments, we wish Nigeria and its people every success in their future endeavors.

Mr. Sembene and Mr. Alle submitted the following statement:

We thank staff for an informative set of papers and Mr. Mkwezalamba and Mr. Odonye for their insightful buff statement.

The Nigerian economy is recovering from the 2016 recession owing to improved international oil market and the authorities' far-reaching reforms initiated under the Economic Recovery and Growth Plan (ERGP). Growth has turned positive for two consecutive quarters in 2017 and is projected to pick up in 2018. A number of other indicators have improved significantly, including those related to FX availability, inflation, financial sector activity, and reserve coverage. Significant steps have also been made in improving the business climate and governance. Yet, the economy is still facing various challenges which continue to hold it back from realizing its potential. We broadly concur with staff's assessment of the macroeconomic challenges facing the country and their policy recommendations.

We take good note of the improving outlook and encourage the authorities to firm it up by implementing the needed adjustment. We welcome the authorities' growth-friendly and revenue-centered fiscal adjustment. The financing of the high fiscal deficit has taken a toll on the development of the private sector and it is reassuring that the authorities have embarked on a significant fiscal consolidation. Attractive bond yields and banks' risk aversion have contributed to crowding out the private sector. We therefore see merit in the authorities' plan under the 2018 draft budget to reduce the Federal Government's overall fiscal deficit from 4.3 percent of GDP in 2017 to 1.4 percent of GDP in 2018. Furthermore, the bulk of the adjustment appropriately consists of non-oil revenue enhancing reforms. The two-pronged strategy of tax administration and tax policy measures, is appropriately crafted and should help Nigeria catch up with its peers in terms of revenue ratios. We particularly welcome the steps taken to enforce tax compliance, use e-filing, and combat corruption in tax offices. As regards tax policy, recent proposals to increase excises on tobacco and alcohol and introduce a registration threshold for VAT, are also welcome. Going forward, we encourage the authorities to consider staff recommendations, including: (i) broadening the pool of products subject to excises; (ii) undertaking a comprehensive reform of the VAT regime; (iii) broadening the tax base by removing exemptions, and increasing the VAT rate; and (iv) rationalizing tax incentives and exemptions. We also welcome the recent adoption of the Petroleum Industry Governance Bill, which would help improve transparency and mobilize more revenue in the oil and energy sectors. On the expenditure side, we are reassured by the savings made in recurrent spending while the capital budget is being doubled, thus supporting medium-term growth.

We note that Staff project a larger deficit in 2018, on the basis that expected surplus revenue from SOEs or privatization proceeds would not materialize, while foreseeing unbudgeted spending pressures. Could staff elaborate on the rationale provided by the authorities for not budgeting these spending pressures? We would also like to better understand the reason why staff doubt that the privatization process will come to fruition in 2018, as planned?

While taking good note of the positive developments in inflation and the FX market, we encourage the authorities to fine-tune monetary and exchange rate policies to sustainably address vulnerabilities. Maintaining a tight monetary stance has served the economy well; and we concur with staff that it should be continued in light of the still high inflation. Monetary policy should be supplemented by additional measures to address factors behind food price contribution to the headline CPI index. We welcome the authorities' efforts to move to a unified exchange rate as part of their strategy under the ERGP. Going forward, we encourage the authorities to give due consideration to staff's call for lifting existing FX and capital flow restrictions. Such a move will minimize risks of the development of parallel markets and ensure free capital flows in the medium term.

The banking system needs to be strengthened with adequate capital buffers and improved supervision. The aim to spur the non-oil growth warrants a sound banking system for adequate private sector lending. We therefore encourage the authorities to keep a close eye on the CBN's actions underway, including monitoring sectors with the highest NPLs and the six-months period given to banks to come up with plans to increase their capital. We also concur with staff that banking supervision should be enhanced, including by intensifying risk-based on-site inspections and strict enforcement of prudential requirements. Given the recent economic developments, we share the view that stress testing scenarios should capture the risk from the current strong sovereign-bank nexus and vulnerabilities to external shocks.

Structural policies should be stepped up to bolster the development of the non-oil economy. The recent recession has underscored the vulnerability of the economy to oil shocks. Enhancing its resilience therefore lies in further diversifying the economy with a view to broadening the export base. To this end, structural reforms should encompass: (i) further improving the business environment to boost investment; (ii) narrowing the infrastructure gap and boosting energy supply; (iii) enhancing financial inclusion; (iv) closing gender gaps and addressing inequality; and (v) combatting corruption. We welcome the setting of an ERGP implementation unit at the highest level and call for a swift implementation of the far-reaching reforms envisaged under the plan.

Mr. Psalidopoulos, Ms. Cerami and Ms. Lopes submitted the following statement:

We thank staff for an insightful set of reports, as well as Mr. Mkwezalamba, Mr. Mahlinza, and Mr. Odonye for their helpful statement. We broadly share staff assessment and would like to provide the following specific comments.

Rising oil prices and improved macroeconomic policies have driven up a moderate economic recovery that is expected to strengthen in the near to medium term. Contributing factors for these developments are a positive outlook for the oil sector, greater foreign exchange availability, authorities' commitment to carry forward a comprehensive package of fiscal, foreign exchange and monetary policies, and structural reforms. In this scenario staff expects growth to accelerate from 0.8 percent in 2017 to 2.1 percent in 2018, marking a significant increase, but short of the 3.5 percent foreseen by Nigeria's authorities as well as prevailing market forecasts. Given the magnitude of the gap, we would like to ask staff their views on these more optimistic forecasts.

We welcome the emphasis on further progress needed to reduce segmentation and distortions in the foreign exchange market by removing the remaining restrictions. The actions taken so far have been successful, however more needs to be done to achieve full foreign exchange flexibility and reap the benefits of increased foreign investments.

We note that, based on some valuations, the real exchange rate appears to be overvalued; at the same time, staff is encouraging greater issuance of foreign-denominated public debt with the aim of containing interest payments which are expected to reach 80 percent of government revenues. As foreign denominated debt is subject to foreign exchange risk, we consider stabilizing the foreign exchange market of paramount importance. The sequencing of foreign exchange reforms and public debt management is, therefore, also crucially important and should not be overlooked.

We appreciate the focus of staff on corruption and governance. However, our assessment on staff's approach is mixed. We look favorably at the way that recent initiatives and policy recommendations are portrayed in the report. Furthermore, we consider the level of details appropriate, as well as the granularity of staff's advice. However, and also acknowledging some of Mr. Mkwezalamba and Mr. Odonye's concerns, we find that in this case TPIs are not used according to best practices and in line with the outcome of the policy discussion of last November on this issue. For example, there are no robustness checks, no disclaimers, no presentation of the views of stakeholders, and, moreover, countries are ranked and targets are set using such indicators (see paragraphs 12, 13 and 14 of SIP).

Ms. Villa and Mr. Ismail submitted the following statement:

We thank staff for the comprehensive set of reports and Messrs. Mkwezalamba and Odonye for their insightful buff statement. Following five consecutive quarters of recession, we welcome the recent pickup in growth in the Nigerian economy on account of the authorities' policy responses and further boosted by recovering oil prices and production. However, the recovery remains fragile and vulnerabilities persist. Market confidence must be shored up, as this is a precursor to a more durable private sector presence. Against this background, we agree with staff that additional measures are needed to ensure a stable macroeconomic environment that will help to promote inclusive and sustainable economic growth, and overcome key developmental challenges. We broadly agree with the thrust of the staff report and offer the following for emphasis.

Concerted efforts to address structural issue will be key to the success of the Economic Recovery and Growth Plan (ERGP). As highlighted in the buff statement, the efforts to strengthen transparency and governance should be intensified as these are essential components in supporting Nigeria's developments towards a diversified private-sector led economy. The authorities should continue to pursue reforms that would lay the foundation for a conducive business environment including closing infrastructure gaps and the swift implementation of the power sector reform plan. Strategies to tackle gender inequality and fostering financial inclusion should also be reviewed and implemented. We welcome comments on the divergence in growth estimates for 2018 between staff and the authorities.

Reinforcing the ERGP with sound macroeconomic and financial policies will help to increase confidence, reduce vulnerabilities and boost growth prospects.

We welcome the authorities' fiscal consolidation efforts that focus on strengthening non-oil revenue mobilization and support the authorities' efforts to accelerate tax administration reforms to improve compliance and enforcement. We encourage the authorities to progressively initiate other structural tax measures such as through VAT reforms and rationalizing tax incentives that would further help lift Nigeria's revenue-to-GDP ratio relative to their peers. These measures, however, should be accompanied by complementary measures to protect the most vulnerable segments of society. At the same time, we share staff's concern on the higher financing needs owing to fiscal deficits and rising debt servicing costs. We invite staff to comments on the recourse for non-compliance with the Fiscal Rule and the effectiveness in its current design.

We concur with the authorities' stance of keeping the monetary policy rate at a level consistent with containing inflation. As the authorities noted, monetary policy tightening has been directed at reducing pressures on the exchange rate, which they consider a key channel for controlling inflation. Nevertheless, we agree with staff that maintaining price stability to support sustainable growth would require the authorities to strengthen the monetary policy framework. We note positively that the authorities would continue to fine tune the monetary policy framework while deploying a range of instruments to contain inflationary pressures. Current CBN practices that are beyond its core mandate suggest weak financial intermediation. Staff comments are welcomed. We also welcome the authorities' commitment to a unified FX market and take positive note that IEFX measures have contributed to better FX availability, the narrowing of the parallel market spread and helped strengthening external buffers. We encourage the authorities to assess the removal of MCP and the FX restrictions on goods which would further accelerate the unification process.

Prompt actions to address financial sector vulnerabilities are needed for the sector to play a role in supporting growth going forward. Growing sovereign exposures and accumulation of domestic arrears have magnified pressures to the banking sectors as evidenced in the high NPL and weakened solvency ratios. We are encouraged by the authorities' assurance to safeguard financial stability through strengthening its supervisory oversight and the conduct of Asset Quality Review as per staff recommendation.

With these comments, we wish the authorities every success in their future endeavors.

Ms. McKiernan and Mr. Williams submitted the following statement:

We thank staff for their comprehensive set of reports and Messrs. Mkwezalamba and Odonye for their informative buff statement. Nigeria's economy is experiencing a nascent recovery underpinned by better commodity prices and the authorities' policy actions under their economic recovery and growth plan (ERGP). Nevertheless, Nigeria still faces significant vulnerabilities. In this context, a lot more is needed to accelerate the growth momentum, raise potential growth, lower unemployment, and reduce poverty. As we broadly concur with staff's assessments and recommendations, we offer the following remarks for emphasis.

Revenue mobilization will be critical to safeguard fiscal consolidation while creating space to support growth-friendly public investment and expand the social safety net. In this regard, we welcome the pronouncements in the 2018 budget to ramp up non-oil revenue over the medium term. We remain concerned however that the planned fiscal improvement is heavily dependent on optimistic compliance efforts, and as highlighted in the SIP, these measures have not in the past delivered the expected outcome. While we support the actions to improve tax administration, we urge the authorities to supplement these with stronger tax policy measures along the lines recommended by staff to strengthen the revenue stream, support scaling up of public investment, and enable adherence to the fiscal rules. Can staff comment on the authorities' contingency plans in case the budgeted revenue flows do not materialize? Relatedly, enhancing the PFM framework, including through establishing and codifying a public investment management system, would significantly aid the fiscal consolidation thrust and boost potential growth. We also welcome the authorities' planned enhancement of the social safety net through the World Bank-supported National Social Safety Nets Project, which should go a far way in helping to alleviate poverty.

In light of the current high inflationary environment, a tight monetary policy is appropriate. That said, we are concerned about the multiple objectives of the Central Bank of Nigeria (CBN) and agree with staff that this could send conflicting signals to the market and impact policy credibility. Can staff comment on whether the authorities have articulated a plan to wind down some of the non-core central bank practices? Relatedly, the authorities' commitment to unify the exchange rates is welcomed and we urge them to eliminate the exchange restrictions and multicurrency practices subject to Article VIII as soon as possible.

The authorities' actions to contain financial sector risks are commendable. We nevertheless encourage them to remain vigilant to developments in the sector amid the recent rise in NPLs and the capital adequacy ratios falling close to Basel II regulatory thresholds.

Strong implementation of the structural reform agenda should accompany the fiscal and macrofinancial policies to deliver the authorities' development objectives. In this regard, the authorities should continue to build on and accelerate initiatives already underway to improve the business environment, combat corruption, and close the gender gap. Further efforts to enhance the country's infrastructure and improve power supply are important steps to induce greater private investment, reduce reliance on oil and bolster the country's resilience to shocks.

Mr. Sobel and Mr. Vitvitsky submitted the following statement:

Nigeria is the largest economy in Sub-Saharan Africa and one of the largest global oil producers. It is also projected to have the third largest population in the world by 2050. Meanwhile, the country faces significant challenges related to high levels of corruption, security risks, and very low revenue-to-GDP levels. Given its size and rising economic importance, building stronger foundations for the functioning of the state and a sound economic policy mix are critical to sustainable growth for Nigeria and the region, as well as to domestic social stability. In this context, we broadly agree with the recommendations laid out in the Article IV. We also praise authorities for beginning to implement their Economic Recovery and Growth Plan (ERGP), which addresses many of Nigeria's challenges, and encourage faster implementation.

Nigeria's economy is undergoing a slow recovery, hampered by weak non-oil, non-agriculture activity. Given its rapidly growing population and already high unemployment rate, stronger and more resilient growth is critical. As such, we agree with Fund staff that authorities should pursue sound macroeconomic policies, as well as policies to support education and healthcare, improve the business climate, and boost infrastructure. These steps would help increase productivity and potential output and support private-sector growth.

Despite a relatively low stock of public debt, we encourage greater fiscal realism and efforts to mobilize non-oil revenue. For a country of Nigeria's size and importance, its total revenue and non-oil and gas revenue are very low at 5.7 percent and 3.2 percent of GDP, respectively, one of the lowest levels in the region and the world, constraining economic growth. The interest payments-to-revenue ratio is also extremely high. We encourage the authorities to support the business environment by mobilizing resources to improve infrastructure, invest in education and health, and provide for young citizens' integration into the labor force. In particular, we support improving tax compliance and broadening the tax base as key measures that could mobilize non-oil revenue.

The draft 2018 budget appears ambitious in its scope and degree of fiscal consolidation, which relies heavily on a planned tripling of non-oil revenue. The Fund staff have significantly different projections on the fiscal deficit projection. Can staff elaborate on these differences? On a related matter, could staff comment on the fiscal risks stemming from state and local government finances and the degree of progress among the states toward meeting the 22-point Fiscal Sustainability Plan? Could staff also comment, based on its cross-country experience, if there are any lessons to be drawn about revenue-to-GDP levels for the foundations of the state for countries with similar per-capita income levels as Nigeria?

Additionally, we noted in the DSA that there is no data provision on contingent liabilities, so staff has used estimates of a possible banking sector bailout for the contingent liability stress test. Could staff comment on the type of data that would be useful for the authorities to provide to improve staff estimates of the magnitude of possible contingent liabilities? Is Fund staff confident in the comprehensiveness of data provided on sovereign domestic and external liabilities, including from official creditors?

Separately, we support staff's recommendations to unify exchange rates and remove restrictions on foreign exchange access. Both measures have created a high degree of economic uncertainty and lowered investor confidence in Nigeria, as well as created distortions in the private and public sectors. A tight monetary policy stance also appears appropriate given high headline and core inflation. That said, we encourage greater transparency of central bank operations and decision-making, as well as more transparent communication.

Finally, amid the Fund's ongoing work on governance, we praise staff for their excellent work on the impact of corruption in the Article IV and Selected Issues (SI) paper. The SI paper demonstrates how corruption is macro-critical in Nigeria, and we appreciate Fund staff's efforts to quantify the cost of corruption and its impact of government revenues. Staff lay out several policy recommendations to reduce corruption, including criminalization of corruption, asset declaration by public officials, and promoting transparency in beneficial ownership in the extractive industry, among others. We urge authorities to consider these recommendations, that together with other structural reforms, will support strong and sustainable economic growth and increase confidence in Nigeria's path.

Mr. de Villeroché, Ms. White, Mr. Hemingway, and Mr. Bellocq submitted the following joint statement:

We thank staff for this clear and compelling assessment, and Mr. Mkwezalamba and Mr. Odonye for the informative buff statement. We welcome the focus of detailed analysis in the Selected Issues Papers and the staff report on long-standing, structural issues in Nigeria, including on domestic resource mobilization, inequality, gender, and demographics. We also see the analysis of governance issues as a very valuable contribution. We encourage the authorities to consider this analysis as they continue their reform efforts. We also encourage them to continue engagement with the IMF and international community to inform and implement the most effective policy solutions.

Nigeria is experiencing a fragile recovery, which has been supported by external conditions and policy action. We believe that now is a critical time for Nigeria to “mend the roof,” putting in place conditions for sustainable and inclusive growth. We welcome the observation that recent reforms have been largely in line with past Fund advice, highlighting the value Fund analysis can have in its role as a trusted advisor. Nonetheless, staff projections highlight the need for further adjustment to put growth on a stronger, more sustainable and more inclusive footing. We broadly share staff assessment, and will focus our remarks issue that relate to Nigeria’s fiscal sustainability and business environment.

Fiscal Sustainability

Ensuring sustainable public finances is critical to Nigeria’s future economic performance. On the fiscal side, the revenue-to-GDP ratio is one of the lowest in the world. At 5.7 percent of GDP, public revenue is a major impediment to development expenditure funding and a major risk for debt dynamics. As perfectly highlighted in the Selected Issues paper, there remain many weaknesses in tax administration and tax compliance must be dramatically improved; according to the data provided by staff, the share of active taxpayers is just 1.9 percent for Personal Income Tax, 5.6 percent for Corporate Income Tax and 5.1 percent for VAT. Against this background, we urge the authorities to implement all the necessary measures to increase the compliance rate, including through tax audits, data matching between custom and tax administrations, and stronger focus on large taxpayers. Regarding the implementation of the Tax Administration Diagnostic Assessment Tool (TADAT) mentioned in the main report, we would be grateful to staff to indicate when the outcome of this assessment will be available.

Beyond tax administration issues, we believe a major tax policy reform is needed to increase non-oil revenue mobilization. We note the additional tax potential reaches 1 percent of GDP this year and more than 8 percent of GDP by 2023. We agree with the staff that a tax reform should be broad-based (covering VAT, CIT, Property tax and Excise) and sequenced over the medium term (2018-2023). We positively note that the authorities agree that a major fiscal reform should be implemented to increase non-oil revenue. Indeed, this is a stated objective under the ERGP (Economic recovery and growth Plan). In that regard, we would be grateful to the staff to indicate if the design and the implementation of a Medium-Term Revenue Strategy (MTRS) has been discussed with the authorities? Moreover, we would like the staff to indicate what is the level of ownership of the DRM agenda by the authorities?

We particularly appreciate the in-depth analysis provided in the Selected Issues regarding the way the authorities could mitigate the impacts of fiscal reforms on the poorest, which could a model going forward in other Article IV reviews. We agree with staff that higher domestic resources mobilization, notably through improved VAT compliance and higher VAT rates, would necessitate more effective social safety nets and a scale-up of transfers to the most vulnerable.

Despite low level of debt-to-GDP ratios, public debt dynamics is at risk. Indeed, the debt service-to-revenue ratio reached 72 percent last year and could reach 82 percent in the years to come in the baseline scenario. We encourage the authorities to implement the frontloaded non-oil resources mobilization measures proposed by staff to bring back the public debt service on a sustainable track. The implementation of the growth-friendly adjustment scenario proposed by staff this year would be a step in the right direction.

Improving the Business Environment

We commend the authorities on their business environment reforms to date and encourage them to continue to make it easier for the private sector to operate across Nigeria.

To do this, Nigeria should move towards a unified exchange rate as soon as possible. With Nigeria now out of recession and with more stable reserves, we strongly encourage Nigeria to act on the staff recommendations to move away from restrictions on foreign exchange access for 40 categories of goods and existing capital flow restrictions. The easing of import restrictions could encourage investments in certain industries, in particular, where banned items are used as intermediate goods. Reform should include unifying multiple exchange rate windows, consistent with the Fund’s policy on Multiple Currency Practices. We take note of Annex V on the impact of multiple exchange rate systems across countries, but observe this analysis is general, rather than Nigeria specific. We would welcome staff views on the historic impact on Nigeria of its decision to pursuing multiple currency windows and the probable impact of removing them. With regard to monetary policy, we agree with staff that the confirmation of the newly appointed Directors of the CBN Board of the MPC would strengthen the Central Bank independence and credibility.

Additionally, we strongly encourage the authorities to swiftly implement the National Anti-corruption strategy and support staff's recommendations regarding the adoption of further measures in that field.

Finally, Nigeria should address challenges related to private sector access to finance. We share staff assessment of important steps that need to be taken to help Nigeria avoid crowding out private sector finance and move away from subsidised lending and quasi-fiscal instruments from the Central Bank. We encourage the Nigerian authorities to consider a credible long-term strategy that sets out a balanced phase out to address the macro fundamentals whilst not immediately choking private sector finance.

Ms. Erbenova, Mr. Bayar and Mr. Hagara submitted the following statement:

We thank staff for their comprehensive reports and Messrs. Mkwezalamba and Odonye for their helpful buff statement. We broadly share staff's appraisal and would like to offer following comments.

Steadfast implementation of a comprehensive policy package remains a priority to bring the Nigerian economy back on a robust and sustainable track. Nigeria is the largest economy in Africa with rich resources and a large growth potential, underpinned by the strong population growth. The terms of trade shock the economy faced, coinciding with simmering vulnerabilities and inadequate policy reaction by the authorities not only drew the Nigerian economy into recession, but also had an adverse impact on other countries in the region. The higher oil prices now offer some valuable breathing space, but should not be seen as a reason for complacency, especially in the run-up to the general elections in 2019. We, thus, encourage the authorities to continue with the expedited implementation of the reform program and address cyclical and structural sources of vulnerabilities.

The authorities should decisively pursue a non-oil fiscal consolidation, centered around frontloaded revenue mobilization efforts. Despite higher oil receipts, the fiscal deficit increased due to higher expenditures and lower-than-projected non-oil revenues. Debt service costs continue to absorb a large share of revenues and crowd out the room for infrastructure investment, much needed in an economy with strong population growth, as well as pro-poor spending. We agree with staff that the authorities should accelerate and strengthen their tax revenue mobilization efforts, key for sustainable fiscal consolidation. In this vein, we welcome staff’s well-focused Special Issues Papers on options for tax revenue mobilization and the distributional impacts of fiscal reforms. The fiscal efforts should be reinforced by actions to rationalize expenditures and improve their efficiency, as well as a strengthened budgetary framework for state and local governments.

The monetary policy should be kept tight, reinforced by a stronger framework, while the steps to liberalize the exchange rate regime are continued. The monetary tightening and foreign exchange measures, reducing the parallel exchange rate premium, are welcome. Nevertheless, inflation remains above the CBN’s target, and we agree with staff’s call to keep monetary policy tight and strengthen the policy framework, including by implementing actions to increase the CBN’s independence and end monetary financing. We also encourage the authorities to continue moving towards a unified exchange rate as the multiple rates arbitrarily penalize the vibrant segments of the economy and undermine investor confidence. We continue to see merit in the development of a monitorable and time-bound plan to phase out exchange rate restrictions.

We support staff’s call for actions to safeguard the banking system’s resilience. The efforts to address risks from exposure to the oil sector and sovereign-bank nexus should be increased, including by improving the assessment of the asset quality and enhancing banking supervision. High NPLs and declining solvency ratios call for the long overdue recapitalization of undercapitalized banks along with strengthening the resolution framework. We also note in this respect the authorities’ view that the current practice of withholding dividends is sufficient to buttress capital buffers. Staff comments are welcome.

Continued commitment to governance reforms and the fight against corruption is essential to cement recent progress. We welcome the improvements in the business environment and the anti-corruption measures implemented by the authorities. Continued progress in this area is necessary and we fully support staff’s recommendations to streamline the legal and institutional frameworks; advance efforts to enhance transparency, particularly in the extractive sector in line with the EITI standard; strengthen the asset declaration regime; and continue enhancing the AML/CFT framework and its enforcement.

We encourage more clarity on staff's assessment of risks. We wonder about the consistency between the tone of the paragraph 16 of the Staff Report and the Risk Assessment Matrix (RAM). The RAM lists a number of negative risks, realization of five of those seen by staff as highly likely and having high impact. In contrast, paragraph 16 states that the risks are mostly balanced, on the account of possibly higher oil prices and faster implementation of infrastructure projects. We see the proper assessment of risks and its clear communication to the authorities and public as very important to ensure the right prioritization of policy responses. Staff's comments are welcome.

Mr. Palei and Ms. Atamanchuk submitted the following statement:

We thank staff for a set of informative reports and Mr. Mkwezalamba and Mr. Odonye for their helpful buff statement. Economic growth in Nigeria has started to rebound after the slowdown caused by a drop in oil prices and cuts in oil production. We welcome the reforms initiated under the authorities' Economic Recovery and Growth Plan, including convergence in exchange rates, improvements in tax administration, and positive developments in the business environment. At the same time, significant vulnerabilities remain, including double-digit inflation, persistent unemployment, and substantial fiscal deficit. Nigeria's economic projections are sensitive to a number of shocks that are well-described by staff in the RAM. In this context, we welcome the authorities' commitment to address vulnerabilities and boost non-oil activity.

In the fiscal area, the non-oil revenue accumulation together with an expenditure rationalization and debt management improvement are necessary to create the fiscal space and address infrastructure bottlenecks in Nigeria. Fiscal deficit remains relatively large and is estimated to exceed 5 percent of GDP in 2017. Even though Nigeria's public debt remains at a comfortable level, the authorities should address fiscal challenges from the medium-term perspective. Non-oil revenue accounts for only about 3 percent of GDP, while interest payments amount to about 70 percent of federal government revenue. We appreciate it that staff underline risks arising from a high level of interest payments, even though the DSA heat map does not show any red flags (page 53). Determined efforts are needed to raise non-oil revenues through improvements in revenue administration and broadening the tax base.

Monetary policy stance should remain tight, while the authorities need to strengthen their policy framework and further develop available instruments. We welcome the fact that broad money growth has declined and remained contained in 2017 and, at the same time, tend to agree with staff's views on the deficiencies of instruments used to contain this growth illustrated by the divergence of money market rates from the policy rate (Text Figure on page 7 and para 25). The CBN should consider streamlining the interest rate framework to better communicate its policy to the market participants and to better anchor inflation expectations.

On exchange rate policy, we welcome the fact that the authorities plan to move to a unified exchange rate and encourage them to remove without undue delays multiple currency practices and restrictions on FX access.

Banking system requires the authorities' continuing attention. We agree with the list of staff's recommendations in para 33 and encourage the authorities to conduct an AQR in line with best international practices, as well as to adopt a prudent approach to the treatment of risky loans and other items on banks' balance sheets.

On governance issues, the authorities have already achieved important progress. They also adopted the National Anti-Corruption Strategy. The SIP Chapter on Strengthening Transparency and Governance in Nigeria provides an overview of corruption issues, discusses strategies how to tackle corruption, and builds on the recent initiatives. Could staff elaborate on their country-specific assessment of the severity of corruption in Nigeria and explain why this topic warranted special attention in the Article IV report? Was this topic a major part of policy discussions between staff and the authorities? Why does the section on "the authorities' views" in the staff report have a reference that the authorities disagree with (as it is emphasized in the buff statement)?

We find the use of third-party indicators (TPIs) and related quantitative estimates in this SIP Chapter to be disappointing. First, staff's conclusions on corruption should not be primarily based on the perceptions of governance scores and perceptions of corruption measures, as well as on related regressions lacking credibility. Second, the use of questionable third-party indicators, especially those provided by private companies and perception-based, should be justified by staff. It is also paramount to include a disclaimer about substantial shortcomings of these indicators, as it was done, for example, in the 2017 Article IV report on Somalia. Third, the WGI are not produced by the World Bank, and they should not be misleadingly attributed to the World Bank in the IMF papers. If we recall correctly, the draft internal TPI Digest explicitly addressed the latter issue. We would appreciate staff's confirmation that the Fund-wide guidance clearly explains that the WGI are not "World Bank's indicators", as it was suggested in paragraph 1 on page 51 and Figure 2 on page 54 of the SIP chapter. The factual errors in the SIP should be corrected. Forth, the chapter on corruption did not mention the World Bank's ease of doing business indicators, although they are highly correlated with perceptions of corruption. Are staff aware of this close correlation?

In this respect, we note that Nigeria is among the top 10 economies showing the most improvement in the recent World Bank Doing Business Ranking, rising by 24 places last year. In addition to the information in the staff report, we would appreciate more details on Nigeria's progress in the Doing Business Ranking or Distance-to-Frontier Score over the past five years. We also note that the Nigerian authorities closely work with the World Bank on regional doing business indicators, which encourage the dissemination of best practices in the country. We congratulate the Nigerian authorities on making visible progress in simplification of procedures in the foreign trade area, as it should help in opening and diversifying the economy, as well as tackling corruption in a meaningful manner. We also welcome the establishment of the collateral registry as an important step toward strengthening protection of property rights.

To conclude, we encourage the Nigerian authorities to continue consultations with staff and wish them success in facing formidable challenges.

Mr. Hurtado and Ms. Sanchez Rodriguez submitted the following statement:

We thank staff for its report and Messrs. Mkwezalamba and Odonye for their candid buff statement.

Improvements in oil prices have provided some relief to the dire economic situation, allowing Nigeria to exit the recession. FX measures and tighter monetary policy have attracted capital inflows and helped improve the reserve position. At the same time, the non-oil non-agricultural sector is still contracting and the high level of unemployment is flat. Lack of more decisive action could lead to impoverished living standards for a country that is set to become the third most populated in the world by 2050. We have many doubts about the policy mix as it has been conducted in the past and urge the authorities to follow the path for reform recommended by staff.

The high percent of revenue that is now devoted to interest payments is concerning. We are encouraged to read that both the authorities and staff agree on the need to step up revenue mobilization efforts. The draft budget for 2018 aims at significant fiscal consolidation (from 4.3 percent in 2017 to 1.4 percent in 2018) assuming a tripling of non-oil revenue through improved compliance and enforcement, higher excises, SOEs savings and privatizations. While we see these consolidation efforts as commendable, the expected results seem overoptimistic, even more so when staff estimates an overall budget deficit of 3.6 percent for 2018. We concur with staff on the need for a comprehensive tax reform guided by a strengthened tax policy unit and consistent with IMF technical assistance.

In this context of fiscal dominance, we see merit in the tightening of monetary policy that has managed to reduce inflation which, at 15.4 percent, remains high. High interest rates have caused credit to contract and are crowding out the private sector; however, at the current juncture, no other course of action seems possible.

Greater exchange rate flexibility would have helped the economy to better cope with the 2016 terms of trade shock. We note that the parallel market premium has declined significantly, but a 20 percent gap persists. We urge the authorities to unify the exchange rate, as committed in the ERGP. The IEFX (window for exporters and investors) has helped stabilize the current account but we have many doubts on the appropriateness of such practices. We note that staff does not support the exchange measures either and ask staff to clarify what the next steps are under the IMF's multiple currency practices standards. Staff's comments are welcome.

The deterioration of the banking sector should be addressed, including through asset quality reviews and measures to strengthen capital, enforcement of prudential requirements and improvements in the resolution framework.

Finally, acknowledging the authorities' efforts as outlined in the Economic Recovery and Growth Plan, including strides for improving the business environment and fighting corruption, we call on them to pursue structural reforms, accelerate power sector reforms, and create the necessary conditions for a diversified private sector led economy.

Mr. Daïri and Mr. Sassanpour submitted the following statement:

We thank staff for a comprehensive set of papers, and Mr. Mkwezalamba and Mr. Odonye for their insightful buff statement. Recent policy initiatives under the Economic Recovery and Growth Plan (ERGP)– including increases in electricity and fuel prices, monetary tightening, depreciation of the Naira, and improvements in the business climate and governance–supported by a rise in oil output and prices, helped Nigeria emerge from a period of negative growth, improved foreign exchange availability, and facilitated a buildup of foreign reserves. These are welcome developments, but more forceful action is needed to address financial sector weaknesses, external vulnerabilities, and widespread unemployment and poverty in the face of a rapidly growing population. Nigeria has substantial potential for higher, more durable and inclusive growth, provided that comprehensive economic and structural policies enshrined in the ERGP are pursued vigorously, using the window of opportunity provided by rising oil income.

Government finances are clearly on an unsustainable path, with interest-to-revenue ratio reaching 72 percent in 2017, and expected to rise further under the staff's baseline scenario, which assumes oil output to recover gradually to recent peak levels, following domestic oil sector reforms. With nominal oil prices projected to weaken steadily in the coming years, we believe that Nigeria's future oil production will also be impacted by international market conditions. Staff comments are welcome. As borne by staff's analysis, Nigeria's non-oil revenue potential is severely underutilized, and an all-encompassing and frontloaded revenue mobilization effort, raising non-oil revenue-to GDP by 10 percentage points in 6 years under the "adjustment scenario", is seen as key to putting government finances on a sustainable footing. Would staff please elaborate on the feasibility of almost quadrupling of non-oil revenue/GDP ratio over a fairly short period? Staff also recommends rationalizing current expenditure (including wage restraint) and boosting capital spending. Capital spending doubled in 2017 and is budgeted to double again in 2018. While we recognize the urgent need to address the large infrastructure gap, it is important to improve the efficiency of spending under such a large scale up program, including by strengthening public investment processes and institutions. Bold reforms in this area could help achieve the higher growth under the adjustment scenario.

Staff recommendations involve a broad range of measures with potentially significant negative impact on population's welfare and yet priority social cash transfers are slated to increase to a token 0.2 percent of GDP over the medium term. Staff comments are welcome. Poverty headcount is very high in Nigeria, and income inequality has worsened over the past decade. We are of the view that more of the fiscal space being created by revenue measures package should be used to ensure that not only the vulnerable population is protected during the transition, but stronger efforts are made to reduce poverty as well as income and gender inequality.

Strengthening macroeconomic balances would facilitate the ultimate unification of exchange rates, and we are encouraged that such a move is already part of the ERGP. A frontloaded unification reduces the substantial costs and rents inherent in a multiple rate system, but it also requires that other economic and social considerations–including impact on poverty–are factored in. The tight monetary policy has helped reduce pressure on the exchange rate and allowed a buildup of reserves, but inflation has remained stubbornly high. Nonetheless, we see no urgency in tightening the nominal monetary conditions further at this juncture, as long as CPI inflation is largely driven by temporary supply factors and fiscal policy is sufficiently tight. However, there is a clear need for greater transparency in monetary operations and for strengthening the transmission mechanism and market signals. The banking system has weakened in the past two years, and loan quality is of concern. We welcome the authorities' follow up on the staff recommendation to conduct an Asset Quality Review.

Nigeria's output and export structures continue to be heavily dependent on oil. Stronger export diversification, as shown by staff analysis, would boost GDP per capita growth and mitigate output volatility. Rebuilding the economic and social capital is critical, but decisive action is also needed to improve the business climate and improve transparency and governance to boost private investment. The authorities' anti-corruption drive, including the adoption of the National Anti-Corruption Strategy and the publication of the first national money laundering and terrorist financing risk assessment report, are commendable and should be reinforced.

We wish the authorities all the success in their endeavors.

The Acting Chair (Mr. Furusawa) made the following statement:

Before opening the discussion, I would like to say a few words about the leak of the staff report. It has come to the attention of management that information concerning the characterization of the staff's view of the medium-term outlook for the Nigerian economy contained in the Article IV consultation staff report appeared in press dispatches issued in Abuja last Wednesday.

Until a staff report has been discussed by the Executive Board and published by the Fund, it remains confidential information. Management takes very seriously the leaking of the Fund's confidential information. Therefore, I would like to inform the Board that management has decided to refer this leak to the Office of Internal Investigations to undertake an investigation, and will report back to the Board in due course.

In the meantime, management would like to remind the staff, Executive Directors, their offices, as well as national authorities who received copies of the staff report through their relevant Executive Director's office, of the importance of respecting the confidentiality of Fund documents at all times.

Mr. Mkwezalamba made the following statement:

First, I would like to thank management for the swift decision taken to launch the investigation into the leak of the Article IV consultation report for Nigeria. The authorities remain concerned, given that this has happened for the second time in a row. They look forward to the launch and undertaking of the investigation, and hope that they will be updated on its progress.

We welcome the Acting Chair's comments regarding the need to maintain strict confidentiality for these reports and hope that others will abide that confidentiality, as has always been the case in the past.

Secondly, I wanted to comment on the discontent expressed regarding the use of certain language in the staff report, including the phrase "muddled through" in the outlook, as well as describing corruption as being pervasive and widespread.

We call upon staff to describe the situation as it is on the ground, instead of using language that may not be a true reflection of the situation. We are not surprised that in the article that the Acting Chair referred to, the words "muddled through" were the chosen as the headline.

Mr. Dairi made the following statement:

I thank the Acting Chair for the information about the action that management has taken regarding the leak. This should not be limited to information leaked before the Board meeting. It should be also encompass leaks of information provided on any non-published staff paper, whether the publication is authorized or not.

In this regard, I regret to say that in the case of Morocco, the level of overvaluation that was assessed as 7.2 percent in the staff report, and this figure was referred to in the media. Unfortunately, this happens more often than we think. We do not monitor all the leaks Fund-wide, and we should be extremely careful about the damage that this could do to the countries, especially when they are embarking on sensitive reforms.

I join Mr. Mkwezalamba’s comments on the leak and on the language used in the staff report. The language should remain respectful of the authorities’ policies and views, and should also carefully reflect the situation without using language that may be unjustified and where some assessment could be made without the need for somewhat offensive references.

Mr. Bayar made the following statement:

We thank the staff for comprehensive report and answers to our technical questions. We would like to emphasize three points.

First, as already pointed out by several Directors, there are discernible differences in the staff’s and the authorities’ estimates of the main macro parameters. We appreciate the staff’s written responses to technical questions, which have clarified their perspective of the Nigerian economy, vis-à-vis the views of the authorities. While they acknowledge the merits of the staff’s approach in the short run, we are somewhat puzzled by the growth dynamics in the longer run.

Nigeria is a resource-rich country and has one of the highest population growth rates in the world at about 2.6 percent per annum. Therefore, a long-run growth estimate of about 2 percent implies a negative total factor productivity and/or a negative capital formation rate at the steady state of the economy.

As daunting as it is, pinpointing potential output is a crucial task because all our diagnoses and advice on macro policies hinge on it. We would, therefore, appreciate further elaboration on the long-run growth dynamics of Nigeria.

Second, as we hinted in our gray statement, we view the message on risks as somewhat confusing. Clearly, Nigeria faces a complex set of challenges, the bulk of which could have negative consequences on the economic outlook. The staff has appropriately summarized their discussions on these risks in the risk assessment matrix on page 44. The realization of five risk factors is seen as highly likely and as having high impact. However, the tone of paragraph 16 of the main report is relatively more benign. In that paragraph, the staff argues that the risks are more balanced on account of possible upsides on oil prices and expedited delivery of infrastructure projects.

Taking all these into account, we clearly see the risks weighing on the downside and believe that our communication should be more coherent in this area.

Finally, we observe that the structural policy section of the staff report has benefitted from the use of several third-party indicators (TPIs). Being inspired by that discussion and perhaps going beyond the Nigerian case, we reiterate our call on the staff to provide a clear justification for the use of TPIs, and to choose suitable qualifiers for inferences and recommendations based on them. As such, we encourage the staff to use appropriate disclaimers when making reference to TPIs. That said, we will refrain from suggesting any particular wording here today.

Mr. Castets made the following statement:

We thank the staff for a comprehensive set of excellent reports. We also thank the staff for its answers to our technical questions. Having issued a gray statement with Ms. White, I will just highlight a few points for emphasis.

The economic and financial situation of Nigeria has improved somewhat since the last Article IV review but remains challenging. Along the lines of Mr. Bayar's intervention, we noted that the rapidly increasing population will mean that GDP per capita will not rise this year. We also have a question on the economic aggregates we should look at in the case of Nigeria, given the high level of inequality, the regional disparities, and the strong reliance on oil production. We wonder whether the aggregates we can use for some other economies are relevant in this case. We would appreciate if the staff could elaborate on this specific issue.

Our chair's main concerns are on the fiscal side. We believe that the very low level of tax revenues is unsustainable, and we note that the economic recovery and growth plan of the authorities aims at increasing domestic resources mobilization, but we expect concrete outcomes in that field by the next Article IV review.

Over the medium term, we encourage the authorities to increase dramatically tax compliance and implement a massive tax reform, covering all aspects of taxation tools. The staff includes some sensible proposals in its report—meaning VAT, personal and corporate income tax, excise, and property tax recommendations. This is crucial to put the public debt back on a sustainable path. The revised tax service-to-revenue ratio is projected to reach 82 percent in the years to come, and there is a baseline scenario. It is also crucial for the funding of development spending and will reduce the crowding out of bank credit to the private sector.

On the fiscal side, the current situation, as well as the baseline set up by the staff, does not appear sustainable, and we urge the authorities to take immediate and decisive action. In that regard, improving the VAT compliance and increasing VAT rates are among the low-hanging fruits that should be mobilized.

On domestic resource mobilization issues, we strongly encourage the authorities to assess the opportunity of engaging a medium-term revenue strategy in close collaboration with Fiscal Affairs Department (FAD) experts.

Lastly, I would like to highlight how much we have appreciated the selected issues paper presented by the staff with the Article IV report.

First, we value the fact that the staff took into consideration what could be the distributional impacts of tax reform in Nigeria and the way to mitigate such impacts for the poorest. The way the staff proposes a different scenario—illustrating that we could reach the two main objectives, which are raising more revenue but at the same time dedicating more revenue to social spending and growth-friendly investments—is a good example of what we would like to see in more Article IV reviews.

The paper on the macroeconomic cost of gender inequality is also insightful and demonstrates that the staff is strengthening its ability to deal with that kind of macro-structural issue. It is a promising avenue.

Last but not least, on the transparency and governance issues presented in the selected issues paper, while we hear Mr. Mkwezalamba's concern with some of the language that was used, and maybe there could be some refinement, like Mr. Sobel and Mr. Inderbinen, we appreciate the staff's effort to assess the macroeconomic cost of corruption, and we encourage the authorities to remain strongly committed to the fight against corruption.

It is also particularly interesting that in the selected issues paper, the staff refers to domestic data and analysis, which is relevant and also could be replicated.

Mr. Rashkovan made the following statement:

We thank the staff for the excellent set of papers, including the selected issues paper. We issued an extensive gray statement, so I will emphasize only one specific issue.

This chair believes that it is important to commend the authorities for recent improvements in the business environment, which have been also acknowledged by the rise in the overall Doing Business rankings.

We also welcome the introduction of the National Anti-Corruption Strategy. These steps send a strong message on the ownership of the reform agenda, and we urge the authorities to continue at the same pace. But this is only a starting point to tackle corruption seriously, both from the authorities' side but also the Fund's side.

Building institutions and implementing a zero-tolerance concept both for high-level and day-to-day corruption will be important for this strategy to bear fruit in the medium term. Therefore, we welcome the staff's attention to governance and the analytical work provided for the selected issues paper, taking into account its macro-criticality for stability and inclusive growth.

As we mentioned during the recent Board meeting on governance, it is important to admit the well-established concept that corruption could arise in industries' that tend to generate trends, like energy, infrastructure, communications, or natural resources.

Considering the Fund's strong focus on governance, further sound economic analysis by the Fund's staff could help in identifying and quantifying these variants, as well as suggesting economic policies for draining these variants and enhancing inclusive growth. We encourage the staff to perform these analyses not only for Nigeria but also to address these issues in all similar surveillance cases in other countries as well.

Ms. Lopes made the following statement:

We thank the staff for an insightful set of reports. I would like to focus on a point that we mentioned in our gray statement—namely, on the way governance and corruption were addressed in the report.

We welcome the focus on governance and corruption. A government's vulnerabilities and integrity issues can definitely hamper economic development. The report seems to make the right case for Nigeria. More generally, the staff's work on these issues is welcome, as long as the analysis is conducted in line with the policy guidance that has been provided by the Board.

In this respect, we appreciated the granularity of the staff's assessment of the policy measures already taken, as well as on the additional efforts still needed. Furthermore, like Ms. Barron and other Directors, we appreciated that the analysis also draws on the 2016 corruption survey undertaken by the National Bureau of Statistics.

However, we find that the use of TPIs in this case does not fully comply with the agreed policy. Notably, the views of other stakeholders are not adequately reflected in the report. Furthermore, a disclaimer, like the one used in Somalia's Article IV, would have been opportune.

Above all, ranking countries and establishing targets in terms of a more desirable level of a perception-based corruption indicator does not keep with the approach that was laid out in the Board's recent discussions on TPIs and on governance more generally.

We hope that the forthcoming guidance note on the use of TPIs will help avoid such episodes in the future. We also look forward to Board engagement on the guidance note, as envisaged in the summing up of the Board meeting on the review of guidance note on governance.

Lastly, we fully share the concerns expressed by management and by Mr. Mkwezalamba on the leak. These incidents undermine the Fund's role and need to be thoroughly investigated in order to avoid their repetition.

Mr. Inderbinen made the following statement:

In our gray statement, we encouraged comprehensive reforms to increase non-oil growth and decrease unemployment and poverty.

On the monetary side, we believe there is a lot of room to increase the clarity of the central bank's mandate on price stability. Like Mr. Merk and Mr. Ostros, we urge the Central Bank of Nigeria to cease direct government lending as soon as possible. We also acknowledge the authorities' commitment to unify the exchange rate but do encourage them to bring action forward in this regard.

On the fiscal side, like others, we noted that consolidation will be essential and that this will hinge on a substantial strengthening of the non-oil revenue, which is singularly low in terms of GDP.

We posed a written question on the expenditure side related to fiscal federalism. We did not see an answer in the staff's written responses. We are not sure whether it qualified as a technical question or not and trust that the staff will be discussing it, or we would appreciate some elaboration on it later.

We were intrigued by the fact that transfers are still made under the budget support facility to the states, although they do not comply with the fiscal sustainability plan. We were just wondering whether a reform is in train on this, and whether the staff engaged with the authorities on this issue. I would appreciate knowing if technical assistance was requested on this issue.

Mr. Fachada made the following statement:

I would like to start by associating myself with the comments made by Mr. Daïri regarding the confidentiality of information before and after Board meetings, as well as the comments of Mr. Bayar regarding risks, and the disclaimer for TPIs, an issue that Ms. Lopes has also raised.

Our chair welcomes the ongoing cyclical recovery in Nigeria in 2017 and the slightly improved growth prospects when compared to last year's staff report. The external account has also improved, international reserves have increased, and inflation has come down slightly.

While some of these improvements are associated with higher energy prices and increased oil production, the authorities' policies have also contributed to the recent improvement, as noted by Mr. Mkwezalamba and Mr. Odonye. Therefore, we are sympathetic to Mr. Mkwezalamba's comments on the inadequacy of the term "muddle through" used in the staff report.

The authorities have made progress on improving the ease of doing business, fighting corruption, and addressing the imbalance in the foreign exchange market. Further reforms are needed on several fronts, including on the foreign exchange market, and we welcome plans to unify the exchange rate.

On this specific topic, we note that in the staff's external sector assessment, the current account and the external sustainability approach implicitly use an effective exchange rate that reflects transactions across all foreign exchange windows. However, the real effective exchange rate approach is based on the official exchange rate that is only used for energy imports and government expenditures. We wonder whether the official exchange rate is relevant in this exercise. Indeed, it is no surprise that the real effective exchange rate model implies a real overvaluation relative to the official exchange rate, and that the other approaches, based on a more depreciated exchange rate, produce different results.

Lastly, as most Directors noted in the gray statements and oral interventions, there is a need for a concerted fiscal consolidation effort. This is no easy task, as reducing the deficit is complicated by Nigeria's large infrastructure gap, high poverty levels, large autonomy of the sub-national governments, and ongoing security concerns in the northern part of the country. While higher oil prices may provide some breathing space, Nigeria's consolidation efforts also hang on its ability to mobilize non-oil revenues.

Therefore, we encourage the authorities to strengthen their ongoing efforts and we broadly support the staff's recommendations in this regard.

Mr. Sobel made the following statement:

Nigeria is Africa's most populous country and one of its largest economies. It is a country of tremendous strategic importance with a rich resource base. A strong Nigerian economy could represent a powerful driver not only for its people but for the region as a whole. Against this background, we strongly support the staff's recommendations and its calls for sweeping reforms, particularly on the exchange rate and fiscal policy front. Some of my colleagues have already spoken to the details, so I will not add anything.

We also welcome staff's selected issues paper on governance and corruption. We urge the staff to speak forthrightly and be a ruthless truth-teller at all times.

I took note of text table 1 on the staff's proposed adjustment scenario. While I have no quibble with those who have suggested that the adjustment scenario is highly and perhaps exceedingly ambitious, I viewed the adjustment scenario in light of the staff's answer to question 10, which we had posed.

In question 10, the staff indicates that, based on work in the Fiscal Affairs Department (FAD) led by Vitor Gaspar, a minimum tax-to-GDP ratio of 12 to 13 percent of GDP is associated with a significant acceleration in growth and development in state capacity. That contrasts with the staff's baseline scenario, which points to 7 percent of GDP total revenue and grants in 2022.

This issue strikes us as remarkably pertinent for a country such as Nigeria, which is facing security challenges and widespread poverty.

Separately, we are pleased, per the staff's answers to our technical question, that Nigeria has relatively strong debt management capacity. This is an increasingly important topic that merits the attention of all mission chiefs throughout the region, particularly as official lending from non-traditional creditors grows.

Along these lines, we encourage Fund staff to be more explicit in reports on their confidence in the debt management and data-recording capacity of authorities. The staff's assessment in question 7 that reporting of debt data is timely, comprehensive, and publicly available could have been included in the Article IV report. Alternatively, when data reporting is not as thorough and timely in other countries, Fund staff should also state so in their assessments.

Ms. Barron made the following statement:

I would like to join with Mr. Castets in congratulating the staff on the excellent selected issues papers.

In particular, the papers on the distributional impact of fiscal reforms, gender inequality, and strengthening transparency in governance all fall within what are sometimes referred to as emerging issues, and distinguished by some from the core mandate of the Fund. The analysis in these papers demonstrates that, for Nigeria, those issues fall well within the core mandate of the Fund. The link to macroeconomic outcomes is made clearly and strongly.

The modeling result, that reducing gender inequality to regional levels could increase GDP per capita by 1¼ percent annually, is as critical a macroeconomic outcome as we are likely to find.

The analysis in the papers draws on a wide range of national sources, as well as those from collaborating with the World Bank and other relevant agencies, and their recommendations fall in areas in which the Fund has expertise. I would like to commend the staff on the high quality of these papers, both as a vehicle to improve our understanding of the Nigerian economy and its development challenges, and just as importantly, to provide a template for how to consider these issues where they are relevant in other member countries.

Ms. Atamanchuk made the following statement:

We share Mr. Mkwezalamba’s concerns and Mr. Daïri’s concerns about the leak, which were supported by many other Directors.

We issued a gray statement on Nigeria, and we welcome the reforms initiated by the authorities under the economic recovery and growth plan, including convergence in exchange rates, improvements in tax administration, and positive developments in the business environment.

I would like to make a point on the use TPIs and their treatment in the staff report. We believe that TPIs, especially perception-based TPIs, should be justified by the staff. As we noted in our gray statement, which has been supported by Ms. Lopes, Mr. Bayar, and Mr. Fachada, it is important to include a disclaimer about the substantial shortcomings of these indicators, as was done in the last report on Somalia.

Mr. Alogeel made the following statement:

We welcome the recent economic recovery in Nigeria, supported by a rebound in oil prices and reforms initiated under their economic recovery and growth plan. On the structural front, we are encouraged by the progress that has been made, including the improvement in Doing Business indicators and the adoption of a National Anti-Corruption Strategy. The authorities should continue their efforts to advance their structural reform agenda to promote diversification and strengthen the country’s medium-term prospects.

On the use of the TPIs in Fund reports, in the discussion we had on the issue, we underscored the need to include an appropriate disclaimer whenever TPIs are used. In this regard, we agree with many other Directors that it is important to always include a proper disclaimer in the staff report, which should include a description of the substantial shortcoming of these indicators. As mentioned by Mr. Palei, this was done in the 2000 Article IV report on Somalia, which was a good disclaimer.

Mr. Sembene made the following statement:

We welcome the recent economic recovery in Nigeria. With Nigeria being the largest economy in the Economic Community of West African States (ECOWAS) we welcome this development that not only benefits the country but also has positive spillovers on neighboring countries, including countries in our own constituency. We commend the authorities for their policy response, the steps they have taken, and their contributions to this welcome development. We encourage the authorities to continue with sound policymaking in order to accelerate the recovery.

On the issue of governance and corruption, we welcome the anti-corruption initiative that the authorities have implemented in recent months and years, which has earned them improved rankings in the World Bank's Doing Business indicators. This was well-documented in the staff report, and we welcome the commitment of the authorities to pursue these anti-corruption initiatives.

That being said, we also support increased focus on those governance and corruption issues in staff reports, and we believe that should be done in a transparent and evenhanded manner to make sure that no naming and shaming is taking place. We emphasize that this new focus on corruption and governance should be done according to the principles that the Board has reiterated in recent meetings on this issue.

We agree that the staff needs to be candid in their report, but at the same time, they also need to be respectful and use words that are in line with the spirit of this institution. I support Mr. Mkwezalamba's comments on this issue. We can report whatever weaknesses exist in the governance framework of a country without being disagreeable, and that is what we should aim to do. It is a failure when the authorities feel like that basic expectation from Fund staff has not been met. We hope that this will not be repeated.

That being said, whenever it is warranted, the staff has to address these issues and address them in a respectful manner.

Lastly, I associate myself with what Mr. Palei and others have said about making sure that the use of TPIs is in line with the principles the Board agreed on recently. This includes making sure that we include appropriate disclaimers whenever those indicators are used. That would be a good step forward. We cannot actually not use those TPI. We need them, and we see scope for the staff to continue using them. But we have to make sure that when they do so, they do it in line with the agreed principle, as illustrated in the guidance note on the use of TPIs.

The staff representative from the African Department (Mr. Mati) made the following statement:[1]

[1] Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these minutes.

We have provided written answers to technical questions raised by Directors. My remarks will focus on the outlook and I will intertwine some of the new questions in my answers on fiscal policy, monetary and exchange rate policy, and I will conclude by addressing the governance issue.

On GDP, under current policies, the growth outlook in the medium term will remain flat, low relative to historical standards, and negative in GDP per capita terms. That is what we characterized as a “muddle through outcome.” That was a discussion that we also had with the authorities during the mission. In the end, “muddle” was a word that was left, and there was no discussion on that particular term. But we take note of the latest reactions.

Regarding oil production over the medium term, our baseline projections provide a production path that is close to Nigeria’s production capacity, given currently proven reserves and confirmed investment. These are largely independent from developments in oil prices, although persistent oil prices could make future investments less attractive, therefore, lowering the upside potential from increased production.

In terms of the question raised about the forecast, they mainly differ with respect to the pickup in non-oil activity and in terms of reform implementation. That was the staff’s best understanding of current policies and the impact, and given what has happened with the crisis, namely, that some of the capital was lost, it will take time for it to be accumulated and get to the potential that it used to have. Hence, we have scenarios. The baseline under the current policy is where the growth will go to about 2 percent or 2.5 percent, and non-oil economic activity will pick up by about 2 percent of GDP from the current 0.4 percent; and in an adjustment scenario where all the reforms being implemented, growth will get closer to potential, which is about 5 percent on non-oil.

On the risks, we consider the risks balanced because if the reform implementation does pick up, and if oil prices go up, that could compensate for some of the downside risks, whereas the risk assessment matrix actually focuses more on those downside risks that have the high probability of materializing. Our stance is that, under our baseline scenario, the risks are balanced.

As to the question about what priority sectors could drive growth, the authorities’ focus on sectors under the economic recovery and growth plan, in particular on agriculture where a large share of the population is employed, is appropriate. However, independently from the sectoral focus, policies that address structural weaknesses will allow the private sector to strive, and it is that coherent policy package that will be needed to increase growth.

On the fiscal front, one of the questions concerned the feasibility of the revenue mobilization objective. I would like to note that at 5.1 percent of GDP in total revenue in 2017, Nigeria is well below its potential and that of its comparator countries. A tripling is possible, but it is very much conditioned on key ingredients. These include parallel implementation of revenue administration and tax policy measures, broadening of the tax base for both direct and indirect taxes, and using excise taxation for short-term gain. A recent FAD study highlighted successful examples of revenue mobilization that were sustainable over short- and medium-term periods.

A case in point was Georgia, which doubled its revenues by 12 percent of GDP, from 12 to 24 percent of GDP; and Liberia by 6 percentage points of GDP over a two-year period.

On the level of ownership of the domestic revenue mobilization agenda, we would like to reiterate that this is a priority of the authorities. As part of the economic recovery and growth plan, the authorities want to increase the tax-to-GDP ratio from 5 percent to 15 percent of GDP by 2020. A difference with the staff's projections in that area is that the initial focus is on tax administration and less on tax policy, which is also part of the authorities' agenda but not as immediate.

On the sequencing of fiscal reforms, the staff is of the view that they should proceed in parallel, both at the revenue level and on the spending side. On the revenue side, tax administration efforts will be parallel in the short term by a broader use of excises and by placing a moratorium on new business tax holidays. Efforts should then be made to transition in the medium term toward a broad-based consumption VAT at the higher rat—the current VAT rate in Nigeria is only 5 percent—and rationalizing tax expenditures, reforming the personal income tax, and property taxation.

On the spending side, efforts to reinforce the Treasury single account, rationalize current spending, and strengthening expenditure controls should also be pursued.

There was a question on the fiscal rule and the non-compliance. It is important to remember that it only applies to the federal government, which needs to respect a 3 percent of GDP fiscal deficit. That ratio has always been respected by the authorities in the proposals. It has also been respected in the budget reporting, but there is a difference with the staff because of some classification of revenue and spending items. Ongoing improvements in public financial management, government finance statistics (GFS) budget classification, are expected to improve reporting and monitoring of the compliance requirements. Strengthening the revenue forecasting capacity will also help make the budget more credible.

As to risks from state and local governments, most of the commercial bank borrowing by states was restructured through the first financial assistance package by the federal government, and there has been little new bank borrowing by states, and the total debt of state and local government is about 3.8 percent of GDP. The greater concern is that states still rely on federal government assistance to finance their spending, and they are running up arrears. This is the reason the finance ministry expanded the budget support facility disbursement by an additional five months in 2017 and has recently tightened enforcement of the implementation of its fiscal sustainability plan as conditions for disbursements.

The World Bank has a US$750 million package that will focus on helping states in these areas. This is an operation that is expected to be presented to the World Bank Board later this summer.

Turning to monetary policy, with regard to the central bank mandate, the staff is not aware of any discussions on revising the mandate. The Central Bank of Nigeria noted that it remains committed to its overriding mandate of price stability. While some current practices lie outside its core mandate, the central bank believes some of these policies were necessary to boost economic growth. For those non-core activities, there are no plans to wind them down.

On foreign exchange policy, the staff recommends removing the multiple currency practices and restrictions on foreign exchange access for 40 categories of goods, as well as unifying the exchange rate as quickly as possible. This will help remove market distortions and facilitate private and public decision-making with positive implications for the economy.

What will be the impact? The analysis approach conducted by the staff for sub-Saharan African countries shows that inflation is about 2.5 percentage points higher in countries with multiple exchange rate systems. There was no statistically significant effect found for growth. A more comprehensive empirical investigation would be needed to establish such a causal relationship for Nigeria.

As for the removal of restrictions, the authorities argue that these are appropriate to increase the competitiveness of local industries and reduce imports. A unified exchange rate is part of the authorities' strategy, although they argue that such a move would first require reaching more comfortable reserve levels.

To answer the question about the timetable, the authorities have not elaborated on the targeted level of reserves that will constitute the trigger to remove the restrictions or to move toward a unified exchange rate.

Before concluding with a question on governance, I would like to answer the point on the real effective exchange rate. On the appropriateness of the exchange rate overvaluation, this is why we report on all three methods, with two of the methods using the effective exchange rate in the economy, in which we find no overvaluation. We tried to be as clear as possible with the real effective exchange rate method by noting that this is with respect to the official exchange rate of 305 naira per dollar, as opposed to one of the other windows.

I will conclude with the question regarding governance, and I would like to reiterate that the staff's country-specific assessment on the extent of corruption is aligned with that of the government, which has highlighted corruption as one of the key challenges facing the country in its economic recovery and growth plan. In line with the authorities' focus on corruption, the staff assessed that improving governance and transparency is macro critical, thus, warranting special attention. An expert from the Legal Department also came as part of the mission to help us look at this issue.

Key elements of the assessment and policy recommendations were discussed with the government, including during the meetings that concluded the Article IV mission, and with the wording provided, and with no objection from the authorities.

As to the TPIs, the staff issued corrections in the selected issues paper to clearly indicate that Worldwide Governance Indicators are not World Bank official indicators. The selected issues papers and the staff report also included a footnote noting a disclaimer about the relative ranking.

Importantly, as noted by some chairs, we do not solely rely on TPIs but make extensive use of the 2016 corruption survey undertaken by the Nigerian National Bureau of Statistics. This survey in itself illustrates the Nigerian government's commitment to improve transparency, including by clearly highlighting the population's perception of corruption.

The staff representative from the Strategy, Policy, and Review Department (Mr. Zeidane), in response to questions and comments from Executive Directors, made the following statement:

> I would like to comment on TPIs, governance and corruption. We take note of the request for disclaimers. We need to be consistent with the policy that was approved by the Board.
>
> The paper was issued before our discussion last Friday, so the charts in this selected issues paper that show relative ranking will not appear anymore in the staff paper. We are working on clear guidance on that.
>
> That being said, we will continue to provide a score with confidence intervals, so people can see whether this country is different from another country. The benchmarking will continue to be done but not on a ranking basis, because we need to continue to benchmark. We will always provide the confidence intervals, because in some of these reports, we will say this country is more corrupt than the others, but if one looks to the confidence interval, one will see that these are overlapping and one cannot say clearly that there is a difference between the two countries. We will try to improve the way we do the presentation. There will be no ranking, and much more consistent implementation of the policy taking into account uncertainty around these estimates.
>
> I would also like to raise the importance of having national data on corruption. If every country moves toward national data, the discussion around the TPI on corruption may not be relevant anymore. The fact that Nigeria had its own survey demonstrates that it is a big issue, because if more than 50 percent of the population says this is an issue, and it is more important than healthcare or infrastructure, then one should think about a way to address this issue.
>
> This is a good development in the case of Nigeria, and we would hope that as the Fund works more with countries on governance and corruption issues, we will see more countries taking the same approach as Nigeria, collecting their own data and making the discussion around the TPI less relevant.

Mr. Daïri made the following statement:

In my earlier intervention this afternoon, I forgot to recognize the high quality of the staff's work.

In some circumstances, it is better to use one word instead of the other without undermining the candidness of the staff's assessment and advice. I fully agree with Mr. Sobel on the importance of maintaining true and candid assessments. This is what we want to do.

I also thank the staff for the response on the issue of revenue mobilization. I agree completely with the staff and Mr. Sobel that reaching 7 percent of GDP by 2023 is insufficient. They need to do much more than that. But asking them to do 7 percentage points more than what is in the baseline—a 7 percent of GDP increase in the revenue-to-GDP ratio—is not only challenging, it is raising the bar too high. We have to recognize the capacity constraints but also the political economy factors in Nigeria. Even with the authorities' best intentions, they may not be able to implement these reforms to the extent suggested by the staff.

The staff should try to find middle ground with the authorities, and more significant effort should be aimed at the medium term without reaching this very ambitious level. It would be helpful to build ownership of the reform process, even if we do not meet the best solution that we want. Sometimes the perfect is the enemy of the good.

It is important to engage the authorities so they will have greater ambitions, and so they will own this objective, and if the situation improves in two or three years, they may raise the bar even more. But for the time being, we should seek something less ambitious than the current objective, which may not be easy to implement.

Mr. Merk noted that the discussion on TPIs might be one-sided since many Directors did not comment on the issue. His chair supported the use of TPIs.

Mr. Mkwezalamba made the following concluding statement:

On behalf of my Nigerian authorities, I wish to express my sincere appreciation to Directors for their frank, constructive, and invaluable advice and policy recommendations, the implementation of which will assist in laying a strong foundation for inclusive growth and sustainable development in Nigeria. The advice and policy recommendations will be conveyed to the authorities.

Directors took careful note of the recent economic recovery in Nigeria, underpinned by higher oil prices and progress in implementing the Economic Recovery and Growth Plan. Owing to an undiversified economic base, higher fiscal deficit and interest payments, double-digit inflation, and structural impediments, Directors saw vulnerabilities in the economy and called for implementation of comprehensive policy actions to promote sustainable and inclusive growth.

I wish to assure Directors that the authorities share their views of the challenges that lie ahead and that urgent policy actions are needed. They are already implementing measures and actions that have begun to yield dividends. For instance, domestic revenue mobilization in Nigeria has improved in the past few years. I take note of the concerns that have been highlighted in relation to the lower tax-to-GDP ratios following implementation of tax reforms that increased the tax base. In addition, the implementation of the Voluntary Assets and Income Declaration Scheme is expected to positively impact revenue collections. Going forward, the authorities plan to implement several other measures aimed at improving tax collection and strengthening tax administration, as highlighted in our buff statement and also by the mission chief. Furthermore, they plan to maintain expenditures at budgeted levels and remain committed to the ongoing rationalization of current expenditures to create space for capital spending.

To curb accelerating inflation, Directors encouraged the Central Bank of Nigeria to maintain a tight monetary policy stance and enhance the monetary policy framework. Additional measures included the unification of the exchange rate and removal of exchange restrictions. The authorities concur that, absent these measures, liquidity flow will remain constrained and borrowing premia elevated, thereby hampering private investment and economic growth. In this regard, the central bank remains committed to pursuing a tight monetary policy stance and ensuring more exchange rate flexibility while working toward removing any obstacles to liquidity flows.

Directors also reiterated the need to address financial sector vulnerabilities, including by ensuring adequate capital buffers of banks and undertaking an asset quality review. In view of the importance of addressing this critical issue, the central bank has reaffirmed its commitment to ensuring resilience in the banking system through vigilance in its oversight and resolution of nonperforming loans, strengthening asset quality, and tackling credit concentration, among others. That being said, the central bank urges the Fund to restrict its evaluation to the issue of solvency and be mindful of the side effects of emphasizing that banks are stressed and kept afloat by central bank lending to avoid speculation and contention, which runs counter to the cause of stability.

Regarding implementation of structural reforms, the authorities continue to improve the business environment, accelerate power sector reforms, strengthen governance, and promote financial inclusion and gender equality, among others, in line with the Economic Recovery and Growth Program, and plan to continue implementing the reforms.

In conclusion, I thank the mission chief, Mr. Mati, and his team for their hard work and active engagement with our authorities and for their responses to the issues raised by Directors. My Nigerian authorities value the Fund's advice and technical assistance, which have helped shape the policy direction over the years. They also look forward to the speedy launch of the investigation.

The Acting Chair (Mr. Furusawa) noted that Nigeria is an Article XIV member, but no longer maintained any restrictions under that Article. It maintained exchange restrictions and multiple currency practices subject to Fund approval under Article VIII, Section 2(a) and 3 but no decision was proposed.

The following summing up was issued:

Executive Directors agreed with the thrust of the staff appraisal. They welcomed Nigeria's exit from recession and the strong recovery in foreign exchange reserves, helped by rising oil prices and new foreign exchange measures. They commended the progress in implementing the Economic Recovery and Growth Plan, including the start of a convergence in foreign exchange windows, tight monetary policy, improvements in tax administration, and significant strides in improving the business environment. Directors noted, however, that important challenges remain, as growth in the non-oil, non-agricultural sector has not picked up; inflation remains high and sticky; unemployment is rising; and poverty is high. To address these vulnerabilities, they stressed that comprehensive and coherent policy actions remain urgent.

Directors emphasized the need for a growth-friendly fiscal adjustment, which frontloads non-oil revenue mobilization and rationalizes current expenditure to reduce the ratio of interest payments to revenue to a more sustainable level and create space for priority social and infrastructure spending. In addition to ongoing efforts to improve tax administration, Directors underlined the need for more ambitious tax policy measures, including through reforming the value-added tax, increasing excises, and rationalizing tax incentives. The implementation of an automatic fuel price-setting mechanism, sound cash and debt management, improved transparency in the oil sector, increased monitoring of the fiscal position of state and local governments, and substantially scaled-up social safety nets should support the adjustment.

Directors commended the central bank's tightening bias in 2017, which should continue until inflation is within the single digit target range. They recommended continued strengthening of the monetary policy framework and its transparency, with a number of Directors urging consideration of a higher monetary policy rate, a symmetric application of reserve requirements, and no direct central bank financing of the economy. A few Directors urged confirmation of the appointments of the central bank's board of directors and members of the monetary policy committee.

Directors commended the recent foreign exchange measures and recent efforts to strengthen external buffers to mitigate risks from capital flow reversals. They welcomed the authorities' commitment to unify the exchange rate and urged additional actions to remove remaining restrictions and multiple exchange rate practices.

Directors stressed that rising banking sector risks should be contained. They welcomed the central bank's commitment to help increase capital buffers by stopping dividend payments by weak banks. They called for an asset quality review to identify any potential capital need. They noted that an enhanced risk-based banking supervision, strict enforcement of prudential requirements, and a revamped resolution framework would help contain risks.

Directors emphasized that structural reform implementation should continue to lay the foundation for a diversified private-sector-led economy. They noted that, building on recent improvements in the business environment, implementing the power sector recovery plan, investing in infrastructure, accelerating efforts to strengthen anti-corruption and transparency initiatives, and updating and implementing the financial inclusion and gender strategies remain essential.

Directors welcomed the continued improvement in the quality and availability of economic statistics and encouraged further efforts to address remaining gaps.

It is expected that the next Article IV consultation with Nigeria will take place on the standard 12-month cycle.

APPROVAL: April 17, 2020

JIANHAI LIN
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Outlook

1. Given the magnitude of the gap, we would like to ask staff their views on these more optimistic forecasts. We welcome comments on the divergence in growth estimates for 2018 between staff and the authorities. We would welcome additional staff comments including on staff's forecast track record—which appears quite strong overall—and any efforts to improve outreach and communication of staff positions.

- Forecasts mainly differ with respect to the pace of (i) the pick-up in the non-oil economy, (ii) reform implementation, (iii) impact of reforms on growth—with staff taking a more conservative stance with respect to these factors. Faster than expected reform implementation, as flagged in the staff report, is an upside risk that would reduce the gap between the short-term forecasts significantly. Similarly, outcomes under the recommended adjustment scenario are significantly closer to outcomes envisioned by the authorities.

- Staff's projections have tended to somewhat err on the optimistic side (as is the case for the average emerging and developing country) but have been appropriate in the recent past (e.g., the projection on real growth of 0.8 percent in 2017 has just been confirmed).

- Regarding outreach, besides intensive discussions during missions, staff's views are regularly discussed with various stakeholders through the Senior Resident Representative/Mission Chief in the field.

2. Staff's current projection for GDP in the medium-term is around 2 percent, compared to almost 4 percent two years ago, despite the increased oil prices, recent improvements in the business environment and some implemented reforms. Staff's comments on the significant drop in the growth outlook are welcome. In addition, could staff include estimates of the potential output and the output gap?

- The drop in growth in 2016 has been sharper than projected two years ago, (-1.6 percent compared to the more than 2 percent forecast at the time), and the economy recovered to just 0.8 percent in 2017 (compared to a 3.5 percent projection 2 years ago). These revisions also have implications for the expected speed of the recovery going forward.

- In addition, while oil prices have recovered from their 2016 trough, they are expected to remain significantly below pre-shock levels, making a full recovery to pre-shock growth rates more challenging, particularly as firms are still repairing their balance sheets.

- Estimates of the current output gap, using standard IMF templates, are around -2½ percent of potential GDP. In the medium term, staff considers non-oil growth of at least 5 percent achievable under an adjustment scenario where the policies recommended by staff are pursued.

Fiscal and Debt Sustainability

3. ***The Fund staff have significantly different projections on the fiscal deficit projection. Can staff elaborate on these differences? Could staff elaborate on the rationale provided by the authorities for not budgeting these spending pressures? We would also like to better understand the reason why staff doubt that the privatization process will come to fruition in 2018, as planned?***

- Differences arise mainly from: (i) the authorities assuming a significant increase in public enterprises' surplus revenue, which staff expects to remain in line with historical patterns (a 0.8 percent of GDP difference); (ii) inclusion by the authorities of privatization proceeds of oil divestment as revenue and gains from the review of the fiscal regime for oil Production Sharing Contracts (a 0.7 percent of GDP difference); and (iii) lower oil revenue assumptions by staff to reflect implicit retail fuel subsidies (0.5 percent of GDP).

- Based on the experiences of past privatization procedures and discussions with Ministry of Petroleum experts, staff believes that it is likely that the privatization process will take at least 18 months to be completed.

- The authorities consider that only the costs of the power sector reform that are directly financed by the budget should be budgeted. For the salary arrears clearance, they consider these can be covered within the existing wage bill. Staff expects these spending pressures to be offset by lower execution of the capital budget.

4. We agree about the necessity and urgency of implementing reforms on the tax system and revenue administration in line with staff's guidelines, but will the effect be so growth-enhancing and rapid as envisaged? Staff's comments are welcome.

- The effect of changes in fiscal policy on output depends on the composition of fiscal adjustment: cutting public investment has a larger effect on output than cutting public consumption or raising revenue. As discussed in the literature on multipliers (and work by Fund economists e.g. Spilimbergo et al. 2009 SPN/09/11; Batini et al. IMF/WP/14/93), spending multipliers tend to be larger than revenue multipliers.

- Hence, the increases in public expenditure and tax revenue projected over the period 2018-23 would result in a cumulative increase in growth of about two percentage points after two years, and three percentage points in the medium term.

5. ***Can staff comment on the authorities' contingency plans in case the budgeted revenue flows do not materialize?***

- If no financing is available, contingency measures would include cutting non-essential recurrent spending or reviewing budgeted investment plans.

6. ***Given the lack of growth momentum in the non-oil sector mentioned earlier, how will greater revenue collection from the non-oil sector be possible?***

- The current non-oil revenue collections are below potential on account of inefficiencies in tax administration and of a tax policy design that can still be significantly improved (see a full discussion in the SIP on revenue mobilization).

7. ***Could the staff be more specific about the data gaps and whether any PPP contingent liabilities are included in the DSA? Could staff comment on the type of data that would be useful for the authorities to provide to improve staff estimates of the magnitude of possible contingent liabilities? Is Fund staff confident in the comprehensiveness of data provided on sovereign domestic and external liabilities, including from official creditors?***

- Apart from revenue transfers, there is little information on internally generated revenue, spending, and arrears of state and local governments (SLGs). SOEs fiscal operations could be strengthened by more regular data on revenues/spending and guarantees provided.

- The authorities report the size of contingent liabilities in their medium-term fiscal framework (about 1.5 percent of GDP). The quantification could still be improved to account fully for the power sector contingent costs or other government guarantees.

- The DSA does not explicitly include contingent PPP liabilities. Nevertheless, the DSA analysis assumes a contingent liability shock of 10 percent of financial assets plus a shock to growth of about 3 percentage points increase in the nominal debt-to-GDP ratio. The latter is considered sufficient to cover additional potential contingent liability risks, such as those arising from PPPs.

- FGN reporting of debt data is timely, comprehensive and publicly available. Publication of data includes debt stock and debt service from all external sources including official creditors.

8. ***Regarding the implementation of the Tax Administration Diagnostic Assessment Tool (TADAT) mentioned in the main report, we would be grateful to staff to indicate when the outcome of this assessment will be available*?**

- The outcome of this assessment is expected to be available by mid-June 2018.

9. We would be grateful to the staff to indicate if the design and the implementation of a Medium- Term Revenue Strategy (MTRS) has been discussed with the authorities?

- Some of the preliminary assessments necessary for an MTRS—TADAT and a preliminary review of tax expenditures—have been launched. Once completed, and if the data quality improves, it will be possible for the authorities to request an engagement with the Fund on an MTRS.

10. Could staff also comment, based on its cross-country experience, if there are any lessons to be drawn about revenue-to-GDP levels for the foundations of the state for countries with similar per-capita income levels as Nigeria?

- While we do not have direct lessons from the experience of countries with similar income levels as Nigeria, recent research based on a broader sample of countries (Gaspar at all, 2016) suggests a minimum tax-to-GDP ratio of 12 ¾ percent is associated with a significant acceleration in the process of growth and development, and likely with changes in social norms of behavior and state capacity.

Monetary Policy

11. Can staff comment on the projected increase in the CBN's claims on the FGN?

- CBN financing of FGN has been considerable in the past. Projections of CBN financing reflect this pattern, which is driven by the underlying fiscal policy stance.

12. Since supply factors are keeping inflation high and private borrowers are facing credit constraints, what steps could the authorities take to remove the supply

constraints so that it would be possible for the central bank to loosen monetary policy and encourage investment and growth?

- Measures to reduce distortions in the FX market, such as the immediate removal of the ban on accessing FX on 40 groups of items, would decrease import costs for these items and ease price pressures from the import side.

- Going forward, removing structural constraints, including through addressing the large infrastructure gap, would reduce disruptions in transportation, thus easing inflationary pressures from such supply shocks.

Financial Sector

13. ***We would like to have a further elaboration from staff on the eventual effects of the transformation of the exchange rate system on the banking system?***

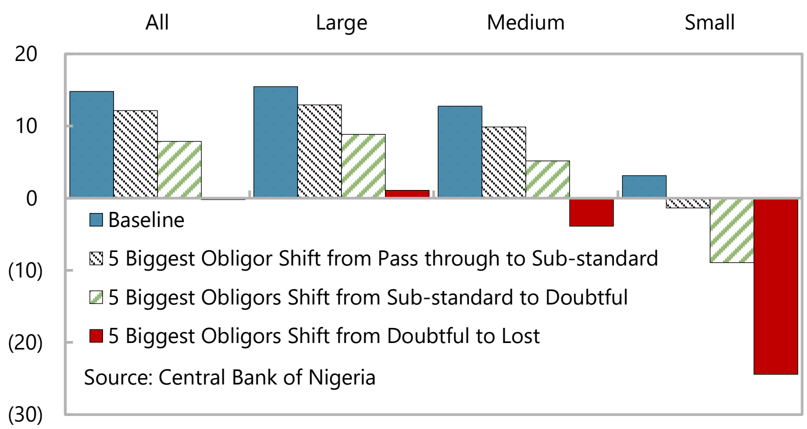
- Staff estimate that a 10 percent depreciation of the naira could amplify corporate and financial sector vulnerabilities, increasing the banking sector's NPLs net provision to capital and reducing the overall CAR by 3 and 1 percentage points, respectively.

- However, existing limits on foreign currency exposure—on FX borrowing and Net Open FX Position—combined with the policy of encouraging banks to lend in foreign currency only to those customers with foreign currency revenue would mitigate the impact of the depreciation on banks' balance sheets.

14. Could staff share information on the relevant [banking] tress test results, if any?

- Details of the stress testing that is going to be undertaken are not yet available. Based on the most recent financial stability report (December 2016), which includes stress testing results, medium and small-sized banks are the ones most at risk. Such findings are expected to remain valid under the updated stress test.

Nigeria: Banking Sector Sensitivity Test Capital Adequacy Ratio



Source: Central Bank of Nigeria

15. ***We also note in this respect the authorities' view that the current practice of withholding dividends is sufficient to buttress capital buffers. Could the staff comment?***

- As noted in Supplementary Information, implementation of CBN's new circular prohibiting banks with low solvency ratios or high NPLs from paying a dividend, will be necessary to help prop up banks' capital buffers in an environment of rising non-performing loans.

- However, it is necessary for banks to increase their capital position further to support private sector lending.

16. ***We would welcome the staff's comments on the necessity of the CBN's capital injection into the four undercapitalized banks. We would appreciate a further update on the overdue recapitalization of four undercapitalized banks?***

- At the time of the discussions for the Article IV consultation, the four undercapitalized banks were given six months to come up with plans to restore their capital position. The recommendation is not for the CBN to inject the needed capital. Staff will follow up on progress in this area in the coming weeks.

External Sector Assessment

17. ***Staff estimates that the real exchange rate (RER) is overvalued by about 12 percent, although most of this estimate is not explained (country specific), as evidenced in high residual.***

- The residual in the EBA methodology largely reflects data gaps (large swings in reported errors and omissions) and the presence of FX restrictions in Nigeria.

- Further improvements in BOP statistics are ongoing with the help of Fund technical assistance.

Structural

18. ***We wonder about the consistency between the tone of the paragraph 16 of the Staff Report and the Risk Assessment Matrix (RAM). Could the staff comment?***

- Risks with high likelihood and impact mentioned in the RAM are highlighted in paragraph 16. An uptick in oil prices is not a standard input in the RAM, but could substantially support internal and external buffers and boost both oil and non-oil growth.

- Overall, we see risks as balanced given the current internal and external environment.

19. In addition to the information in the staff report, we would appreciate more details on Nigeria's progress in the Doing Business Ranking or Distance-to-Frontier Score over the past five years.

- Details of the Ease of Doing Business results can be found in the World Bank Doing Survey database. As the methodology of assessment changes over time, not all ranking/DTFs are comparable over time, so we will be happy to exchange on this at the technical level. The text table provides an evolution of distance to the frontier and Doing Business rankings over the past five years.

Text Table: Doing Business in Nigeria

Year	Rank global as published (not possible changes in methodology in other years)	DTF global (DB17-18 methodology)	DTF global (DB16 methodology)	DTF global (DB15 methodology)	DTF global (DB10-14 methodology)
DB2018	145	52.0			
DB2017	169	48.2			
DB2016	169	47.6	47.5		
DB2015	170		46.4	50.3	
DB2014	175*			46.7	48.4

*not actually published ranking but adjusted to make comparable with 2015 methodology
Note: DTF=Distance to Frontier