Fiscal Policy and Economic Stability in South East, Nigeria from 2015-2023

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ABSTRACT

This study examined fiscal policy and economic stability in South East, Nigeria from $2015 - 2023$. Specifically the study is design to; ascertain the extent taxation (T) has affected unemployment rate (UR) in the South East Nigeria, assess the extent to which government spending (GS) have impacted on unemployment rate (UR) in South East, Nigeria. The study adopted Ordinary Least Square (OLS) research design and made used of secondary data sourced from CBN statistical bulletin, CBN Annual Report and Statement of Accounts 2023. The findings of the study revealed that the coefficient of the constant term is 13.07545 and assumes a positive sign. It is statistically significant at 0.0003 levels, while the employment rate (UR) has a negative sign and hence shows a negative relationship with taxation (T). The findings also revealed that Taxation (T) has a negative sign and sows a negative relationship with Unemployment Rate (UR) and Government Spending (GS) which is statistically significant at 0.0540, while Government Spending (GS) has a positive sign and shows a positive relationship with Unemployment Rate and Taxation. The findings imply that while Taxation (T) has no significant relationship with Unemployment (UR), Government Spending (GS) has a positive significant relationship with Unemployment Rate (UR) and Taxation (T). Based on the findings; the following recommendations where made; government spending should be channeled more on human capacity building in order to reduce the rate of unemployment, high tax tariff on indigenous industry should be discourage in order to encourage job creation through indigenous industries, the government should avoid frivolous public spending which will lead to public debt and exacerbate unemployment rate.
Keywords: Unemployment Rate, Government Spending, Taxation and Fiscal Policy

INTRODUCTION

The Nigerian economy has been plagued with several challenges over the years. In spite of many and frequently changing fiscal, monetary and other macroeconomic policies, Nigeria has not been able to harness her economic potentials for rapid economic development [1-4]. According to [5] the debate on the effectiveness of fiscal policy as a tool for promoting growth and development remains inconclusive, given the conflicting results of current studies. Over the last decade, the growth impact of fiscal policy has generated large volume of both theoretical and empirical literature. However, most of these studies paid more attention to developed economies and the inclusion of developing countries in case of cross-country studies were mainly to generate enough degrees of freedom in the course of statistical analysis [6-7]. Fiscal policy are inextricably linked in macroeconomic management; developments in one sector directly affect developments in the other. Undoubtedly, fiscal policy is central to the health of any economy, as government's power to tax and to spend affects the disposable income of citizens and corporations, as well as the general business climate. Fiscal policy can contribute to macroeconomic stability through three main channels. The first is the automatic reduction in government saving during downturns and increase during upturns, cushioning shocks to national expenditure [8]. Such automatic stabilization occurs because tax revenues tend to be broadly proportional to national income and expenditure, whereas public spending reflects government commitments independent of the business cycle and entitlement programs specifically designed to support spending during downturns, including unemployment benefits.2 Also, to the extent that government consumption is less volatile than other components of GDP, the public sector contributes to output stability through a mere composition effect of domestic expenditure. Second, governments can deliberately change public spending and tax instruments to offset business cycle fluctuations. Finally, the

structure of the tax and transfer system can be designed to maximize economic efficiency and market flexibility, thereby enhancing the resilience of the economy in the face of shocks.

The notion of fiscal stabilization pertains to the first two channels

The public's demand for government-induced stability reflects a number of factors that may vary over time and across countries, including the inherent resilience of the economy and the existence of alternative stabilizers, such as an effective monetary policy and unrestricted access of individual agents to financial instruments. During the recent crisis, the perceived need for fiscal stabilization has been unquestionably high: the resilience of national economies was impaired by the depth and the global nature of the shock, agents faced either limited access to or high cost of self-insurance through credit markets and financial institutions, and the firepower of monetary policy was constrained by the zero-bound on nominal interest rates. The focus of this paper is examining the stabilizing role of fiscal policy on the economy of south east Nigeria from 2015 − 2023. Specifically the study is design to; ascertain the extent taxation (T) has affected unemployment rate (UR) in the South East Nigeria, assess the extent to which government spending (GS) have impacted on unemployment rate (UR) in South East, Nigeria [8-9].

Statement of the Problem

To realize macroeconomic stability, there is the need to harmonize the fiscal policies to solve the macroeconomic problems of the Nigeria economic stability. It is the awareness of these problems that trigger off the study in order to examine ways and means in which the fiscal policy strategies can be used to the best advantages. To this end, this study intends to assess the extent to which fiscal policies affect economic stability in Nigeria.

RELATED LITERATURE REVIEW
Conceptual
Concept of Fiscal Policies

Fiscal policy refers to the use of government spending and taxation to influence the economy. It is one of the two main tools that governments use to manage their economies, with the other being monetary policy. Fiscal policy is primarily concerned with the government's revenue and expenditure decisions and their impact on the overall economy. Here are some key aspects and components of fiscal policy: Government Spending: Governments can stimulate or restrain economic activity by adjusting their levels of spending. When the government increases its spending on public projects, such as infrastructure development, healthcare, education, or defense, it can boost economic growth by creating jobs and increasing demand for goods and services. Conversely, reducing government spending can have a dampening effect on economic activity [10-11].

Taxation: Taxation is another crucial tool in fiscal policy. Governments can adjust tax rates and policies to influence consumer and business behavior. For example, cutting taxes on individuals and businesses can encourage spending and investment, which can stimulate economic growth. On the other hand, raising taxes can reduce disposable income and curb excessive spending, helping to control inflation.

Budget Deficits and Surpluses: A fiscal deficit occurs when a government's expenditures exceed its revenues, leading to borrowing to cover the shortfall. Conversely, a fiscal surplus occurs when revenues exceed expenditures, allowing the government to pay down debt. The management of budget deficits and surpluses is an essential aspect of fiscal policy [12-13].

Automatic Stabilizers: Certain fiscal policies are designed to automatically stabilize the economy during economic downturns or booms. For instance, unemployment benefits and progressive tax systems help buffer the impact of economic fluctuations.

Cyclical vs. Structural Policy: Fiscal policies can be designed to address either short-term economic fluctuations (cyclical) or long-term economic challenges (structural). Cyclical policies aim to counteract recessions or overheating in the economy, while structural policies focus on issues like long-term economic growth, income inequality, and workforce development.

Public Debt Management: Governments often need to borrow money to finance deficits or long-term investments. Managing public debt levels is a critical aspect of fiscal policy to ensure that debt remains sustainable and does not lead to a fiscal crisis.

Political and Economic Considerations: Fiscal policy decisions are influenced by political factors, economic conditions, and the priorities of the ruling government. Different political parties and leaders may have varying approaches to fiscal policy.

Fiscal policy can be expansionary or contractionary depending on the government's goals and the economic conditions. Expansionary fiscal policy involves increasing government spending and/or reducing taxes to stimulate economic growth, while contractionary fiscal policy involves reducing spending and/or increasing taxes to control inflation or rein in an overheated economy.

The effectiveness of fiscal policy depends on a variety of factors, including the timing of policy changes, the size of the fiscal measures, and the overall economic environment. It is often used in conjunction with monetary policy to achieve macroeconomic stability and promote sustainable economic growth [13-15].

Economic Stability

Economic stability indicators are measures used to assess the overall health and stability of an economy. These indicators help policymakers, investors, and the general public gauge the economic conditions within a country or region. Economic stability is essential because it contributes to a higher quality of life, sustainable growth, and the well-being of a nation's citizens. Some key economic stability indicators include:

Gross Domestic Product (GDP): GDP measures the total economic output of a country. Stable and growing GDP indicates a healthy economy, while a declining GDP may suggest economic instability.

Inflation Rate: Inflation measures the rate at which the general price level of goods and services rises, causing a decrease in the purchasing power of a currency. Moderate and stable inflation is generally preferred to hyperinflation or deflation.

Unemployment Rate: The unemployment rate reflects the percentage of the labor force that is unemployed and actively seeking employment. A high and increasing unemployment rate can be a sign of economic instability.

Balance of Payments: The balance of payments accounts for a country's trade and financial transactions with the rest of the world. A stable balance of payments is crucial for long-term economic stability.

Interest Rates: Central banks often use interest rates as a tool to control inflation and stabilize the economy. Stable and predictable interest rates can contribute to economic stability.

Exchange Rates: Exchange rates measure the value of a country's currency relative to other currencies. Exchange rate stability is important for international trade and investment.

Government Debt: The level of government debt relative to GDP can indicate the fiscal health of a country. High and rapidly increasing government debt can raise concerns about economic stability.

Consumer and Business Confidence Indices: Surveys of consumer and business sentiment provide insights into the optimism or pessimism about the economic outlook. High confidence levels can support economic stability by encouraging spending and investment.

Financial Market Indicators: Stock market indices, bond yields, and credit spreads can provide information about investor sentiment and the overall health of financial markets, which are closely linked to economic stability.

Housing Market Indicators: The stability of the housing market, including indicators like home prices and mortgage delinquency rates, can reflect broader economic stability.

Labor Force Participation Rate: This rate measures the percentage of the working-age population that is either employed or actively seeking employment. A declining participation rate can signal labor market challenges.

Foreign Exchange Reserves: A country's foreign exchange reserves indicate its ability to manage external shocks and maintain exchange rate stability.

Income Inequality: While not a direct economic stability indicator, high income inequality can lead to social and political instability, which can, in turn, affect economic stability.

These indicators are often analyzed together to provide a comprehensive assessment of an economy's stability. Governments, central banks, and international organizations use this data to make informed policy decisions and take actions to maintain or restore economic stability when necessary.

IMPACT OF FISCAL AND ECONOMIC STABILITY

The impact of taxation on Economic Stability

Fiscal policy, as a part of state's economic policy is characteristic by its basic aims among which definitely belongs the stimulation of economic growth. This policy is usually executed by changing the amount or structure of government spending and taxes. [7], state that the impact of fiscal variables on economic growth is ambiguous and depends on their nature. Concretely, the impact of distortion and non-distortion taxes, or productive and unproductive spending on economic growth. Distortion taxes and unproductive government spending decrease economic growth. Productive government spending will have a pro-growth effect only if they are financed by non-distortion taxes.

Government spending and its impact on economic Stability

Within the impact of government spending on economic growth it is necessary to realize that their impact depends on the fact if productive or unproductive government spending prevail [5-8]. [10-14] among productive government spending incorporate e.g. investment into education and human capital, spending on defense, infrastructure or healthcare. Unproductive government spending are mainly social security contributions. Further, it is necessary to mention the work of [8] explaining "Wagner's law". Wagner's law states that economic growth can lead to increased demand for government services and "welfare spending". According to this law, in fully developed countries government spending raise from three main reasons. (1) socio-political: e.g. social and health insurance; (2) economic: thanks to the science and technology the increased engagement of the state in technological projects is required; (3) historical: growth of government spending lead in the end to the government debt increase. Therefore, if these spending suppress investments or government spending into education, then the impact of total government spending cannot be pro-growth.

But only a very few studies research the productivity of government spending in the case of different institutional conditions. E.g. [4], evaluate the influence of government spending on economic growth, where they study how the government effectiveness influences the efficiency of government spending. They do not classify government spending into productive and unproductive a priori, but they divide countries into two groups according to the effectiveness/ineffectiveness of government institutions. The first finding is that government consumption has a negative growth effect for certain groups of countries. The negative pro-growth effect of this spending can be seen especially in developing countries with inefficient governments, whereas in developing countries with efficient governments this impulse is insignificant. Second finding is that capital spending have a positive pro-growth effect in developing countries with inefficient governments and also in developing countries as a whole. Generally, these two results mean that government efficiency (efficiency of government institutions) is an important determinant of the economic growth in developing countries.

Theoretic Framework

[6] the effects of fiscal policy on economic growth Fiscal policy is of great importance in the development of the economy. In Kosovo and other countries, fiscal policy plays a key role in economic growth. The state of affairs and the prudence of fiscal policies are essential for the preservation of macroeconomic stability. Fiscal policy relates to government actions in changing the composition of public revenue and expenditure by managing aggregate demand to maintain a steady economic growth with relatively high employment without creating an inflation and without increasing public debt and a satisfactory balance of payments. Methodologically, this study makes a critical review to check whether the fiscal policy in Kosovo has achieved its purposes, such as reducing economic inequality, reducing regions of inequality, environmental progress, etc. The study shows that fiscal policy did indeed have an important role in economic growth and inequality reduction.

Empirical Review

[5] conductor a study Monetary – Fiscal Policy Mix: A Tool for Economic Stabilization in Nigeria. The study examined empirically the relationship between monetary-fiscal policy mix and Nigeria's economic stability. The Johansen co-integration technique complemented with VECM were employed to achieve the objective of the study. The result of the descriptive statistics revealed that the variables were normally distributed and the degree of variability of them was good as evident from the Jarque-Bera statistics and standard deviation. The Johansen and Juselius co-integration results revealed that both the trace statistic and maximum Eigenvalue statistic confirmed the existence of co-integrating equations among the variables of interest. It was evident that the trace test indicated six co-integrating equations while maximum Eigenvalue test revealed four co-integrating equations in the model, as the null hypothesis of no co-integration was rejected. These results suggested that there was a unique long run equilibrium relationship among the variables. The VECM result indicated that there was a long run relationship between the variables concerned. The result further showed that monetary-fiscal indicators have not made much significant contributions to the growth of the Nigerian economy as well as economic stabilization in Nigeria. The study recommended the entrenchment of fiscal discipline as a result of destabilizing effect of government's fiscal activities due to its fiscal irresponsibility in Nigeria. Also recommended was that monetary policies should be structured to lower lending interest rate and raise interest rate on saving deposits so as to increase the availability of loanable funds which will in turn boost investment and stimulate economic growth.

The Monetarist: Monetarism's essence can be stated in the form of a few central propositions where the over-whelming influence of money is the center piece. Monetarists assign causal role to money, and since money is treated by them as exogenous, it is possible to control disturbance or disequilibrium in the economy by controlling the money supply, and hence money matters. To them, fiscal policy is very complicated and difficult to execute in timely manner and given the constancy of the rate of interest over a long period, suggesting horizontal curve (indicating infinitely elastic demand for new investment) and constant money supply, an increase in government investment will correspondingly reduce private investment, and this crowding out' will reduce the efficacy of fiscal policy. As a result of this crowding out, the effect of fiscal policy on normal income will be zero, provided the LM curve is vertical. An increase in taxation and 'crowding out' will raise the rate of interest to decrease the investment. Thus, to them, fiscal policy may change income, velocity, interest rate and so on but its expansionary effect is likely to be minor and transitory (temporary) on aggregate income and price levels. Thus, a pure fiscal policy does not matter for aggregate demand, nominal income price level.

The St-Louis multiplier has been used to show that pure fiscal policy has no effect on nominal income. Fiscal policy impact depends on how the government deficit is financed. Finance by money creation (a monetary action) is seen to be more expansionary than what is possible by the manipulation of fiscal tools. Thus, according to monetarism, what matters is the quantity of money created and not how it is created. Monetarists are of the view that money and income are directly correlated. Monetary change affects long-run stock of real capital and hence output. Fluctuation in money, national income is attributed largely on monetary policy whose effect is transmitted to national income both through the bond field and other channels. Thus, the long-run economic activity and nominal income are essentially the function of the stock of money and flows themselves adjust to the stock. The

adjustment to change in money involves substitution between money and different types of asset, thus, while wealth effect of a change in money is not of any empirical importance, the substitution effect appears to be given the tendency to assume that money is the only asset, the real balance effect and the wealth effect are also assumed to be tantamount. The monetarists concede a direct nexus between money supply and price level, which is proportional in the long-run. In effect, in long-run, proper growth rate of money stock is crucial for stable growth path of output and prices.

METHODOLOGY

The estimation method adopted in this study is the ordinary least square (OLS). Time series data over the period 2015 to 2023 were used. The data used were secondary in nature sourced from CBN statistical bulletin, CBN annual report and Statement of accounts.

Model Specification

1. To ascertain the extent taxation (T) have affected unemployment rate (UR) in the South-East, Nigeria
2. To assess the extent government spending (GS) have impacted on unemployment rate (UR) in the South-East, Nigeria in the South-East, Nigeria

$UR = F(T, GS)e_t$--------------- (1)
This can be econometrically modeled thus:
$LUR = a_0 + a_1LT + a_2LGS + e_t$--- (2)
Where:
e_t --- represents stochastic term
$a_1 - a_2$ = Parameter Estimate
LUR = Log of Unemployment Rate
LT = Log of Taxation
LGS = Log of Government Spending
As stated in this study, economic stability i.e. UR, has a functional relationship with Taxation (T) and Government Spending (GS)

DATA PRESENTATION AND ANALYSIS

Method: Least Squares
Date: 29/09/23 Time: 22:58
Sample (adjusted): 2015 − 2023
Included observations: 22 after adjusting endpoints

Variables	Co-efficient	Std. Erro	t-Statistic	Prob.
C	13.07545	3.641763	3.590417	0.0030
LUR	-0.3590047	0.225180	-1.594489	0.1331
LT	-1.429438	0.679593	-2.103373	0.0540
LGS	0.135748	0.233911	0.580339	0.5709

R-squared	0.655873	Mean dependent var		6.068384
Adjusted R-squared	0.483809	S.D. dependent var		0.499886
S.E. of regression	0.359150	Akaike info criterion		1.065137
Sum squared resid	1.805847	Schwarz criterion		1.4618805
Log likelihood	-3.716507	F-statistic		3.811805
Durbin-Watson stat	1.149481	Prob(F-statistic)		0.015878

Source: E-views 7

From the result presented above the following facts emerged prominently. The equation has UR, Taxation (T), and Government Spending (GS), as independent variables. The coefficient of the constant term is 13.07545 and assumes a positive sign. It is statistically significant at 0.0003 levels. UR has a negative sign and shows an inverse relationship between and T. Taxation has a negative sign and shows an inverse relationship between UR and GS. It is statistically significant at 0.0540. Government spending has a positive sign and shows positive relationship between UR and T. It is statistically significant at 0.5709.

The F statistics tell us if the model will be accepted or not. Decision rule: For the model to be accepted the F statistics must be relatively high and positive. For this model the F statistic is 3.811805, therefore it is accepted.

CONCLUSION

Monetary – Fiscal Policy mix: a tool for economic stabilization in Nigeria is the title of this study while the specific objective is to determine the long run relationship between monetary - fiscal policy mix and economic stabilization in Nigeria. The study uses annual data from Nigeria for a period of 32 years covering 1986-2017. Descriptive statistics, Johansen co-integration and Vector error correction model (VECM) techniques were employed to achieve the said objective. The result of the descriptive statistics revealed that the variables were normally distributed and the degree of variability of them was good as well. These were evident from the Jarque–Bera statistics and standard deviation respectively. The Johansen and Juselius co-integration results showed that both the trace statistic and maximum Eigenvalue statistic confirmed the existence of co-integrating equations among the variables. It was evident that the trace test indicated six co-integrating equations while maximum Eigenvalue test revealed four co-integrating equations in the model, as the null hypothesis of no co-integration was rejected. These results suggested that there was a unique long run equilibrium relationship among the variables of interest. The VECM result indicated that there was a long run relationship between the variables concerned. The result further showed that monetary-fiscal policy indicators have not made much significant contributions to the growth of the Nigerian economy as well as economic stabilization in Nigeria. However, fiscal policy variables have much impact on economic stabilization than the monetary policy variables. The study recommended the entrenchment of fiscal discipline as a result of destabilizing effect of government's fiscal activities due to its fiscal irresponsibility in Nigeria. Fiscal and monetary policies are inextricably linked in macroeconomic management; developments in one sector directly affect developments in the other. Undoubtedly, fiscal policy is central to the health of any economy, as government's power to tax and to spend affects the disposable income of citizens and corporations, as well as the general business climate. Today, monetary and fiscal mix is both commonly accorded prominent roles in the pursuit of macroeconomic stabilization in both developed and developing countries. To realize macroeconomic stability, there is the need to harmonize monetary and fiscal policies to solve the macroeconomic problems of the economy. It can therefore be concluded that fiscal and monetary policies are complementary and re-inforcing in ensuring economic stabilization of the Nigerian economy.

RECOMMENDATIONS

Arising from the empirical findings of this study, the following recommendations are made as a matter of necessity

1. Government spending should be channeled more on human capacity building in order to reduce the rate of unemployment,
2. High tax tariff on indigenous industry should be discourage in order to encourage job creation through indigenous industries,
3. The government should avoid frivolous public spending which will lead to public debt and exacerbate unemployment rate.

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