

# Economic Update

Nigeria | Economy | Fiscal Operations | September 07, 2016

PAC RESEARCH

## 2Q'16 Fiscal operations: Increasing fiscal deficit poses a downside risk

In the second quarter to June 2016, gross federally-collected revenue stood at ₦1,159 billion, down by 51.3% compared with budgeted revenue of ₦2,380 billion. The revenue in the review quarter is lower than ₦1,269 billion in the first quarter of 2016 and ₦1,397 billion in the second quarter of the previous year by 8.7% and 17.0% respectively. The decline in the revenue was a result of shortfall in receipts from both oil revenue and non-oil revenue; oil revenue was down by 39.2% compared with the budgeted estimates of ₦884 billion for the quarter. Also, the oil receipts is lower than ₦666 billion and ₦839 billion in the first quarter of 2016 and the corresponding quarter of the previous year by 19.3% and 36.0% respectively.

The weakness was a result of the low prices of crude oil in the international market and the hostility in the oil producing region which has led to destruction of oil and gas infrastructures in the region. Crude oil production in the quarter stood at an average of 1.69 million barrel per day (mbpd), lower by 19.9% and 17.6% compared with an average of 2.11 mbpd and 2.05 mbpd respectively in the first quarter of 2016 and the corresponding quarter of the previous year. Also, the review quarter's oil production is lower by 19.1% compared with 8-quarter average of 2.09 mbpd. On the other hand, Brent crude oil traded at an average price of US\$48.38 per barrel in the review quarter, down by 30.6% against an average price of US\$69.69 per barrel in the corresponding period of the previous year. Consequently, the decline affected the revenue accrued to the government from the sale of crude oil in the period.

Overall, revenue from oil and gas contributed 46.3% to total collected gross revenue relative to 52.5% in the first quarter of the year and 60.0% in the second quarter of 2015. Furthermore, crude oil and gas sales was down by 47.9% y/y to ₦112 billion compared with ₦215 billion in the previous year, but higher by 36.6% against ₦82 billion in the first quarter of 2016. Similarly, petroleum profit tax and royalties declined by 34.5% y/y and 32.2% q/q to ₦213 billion compared with ₦325 billion and ₦314 billion accordingly.

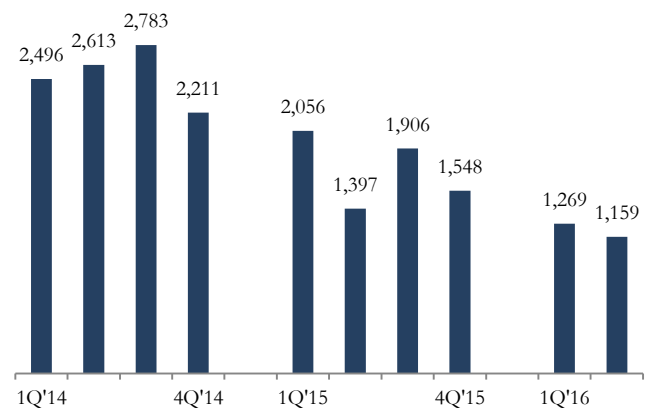
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**Table 1: Gross Federation Account Revenue (₦ billion)**

	1Q'15	2Q'15	3Q'15	4Q'15	1Q'16	2Q'16
Federally-collected revenue (gross)	2,056	1,397	1,906	1,548	1,268	1,159
Oil revenue	1,211	839	949	831	666	537
Non-oil revenue	845	558	956	717	602	622

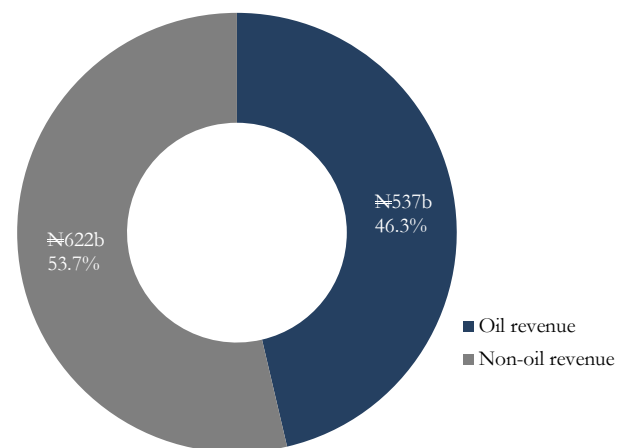
Source: CBN, PAC Research

**Fig. 1: Gross federation account revenue (₦ billion)**



Source: CBN, PAC Research

**Fig. 2: Oil revenue and non-oil revenue in 2Q'16**



Source: CBN, PAC Research

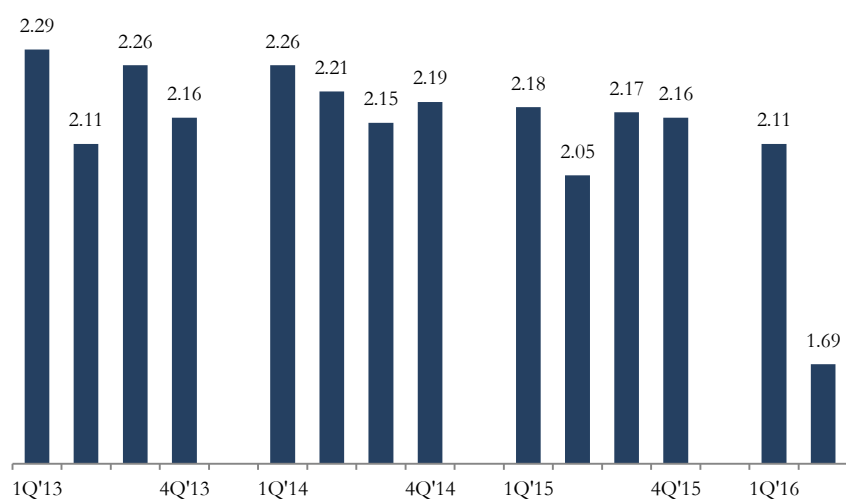
In our view, if the on-going dialogue among the relevant stakeholders in the oil producing region can yield positive results, then the hostility in the region which has led to production shock can be brought under control. Consequently, the destruction of oil and gas infrastructures might come to an end and the revenue from the sector is expected to improve subsequently.

Fig. 3: Prices of Brent crude oil (US\$ per barrel)



Source: Bloomberg, PAC Research

Fig. 4: Crude oil production (mbpd)



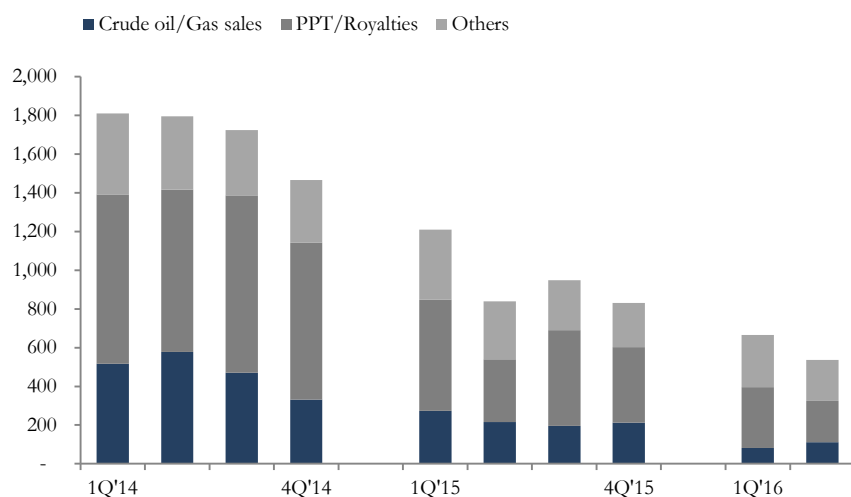
Source: CBN, PAC Research

Table 2: Components of gross oil revenue (₦ billion)

	2Q'14	3Q'14	4Q'14	1Q'15	2Q'15	3Q'15	4Q'15	1Q'16	2Q'16
Oil revenue	1,795	1,723	1,466	1,211	839	949	831	666	537
Crude/gas sales	577	491	331	274	215	196	213	82	113
PPT/Royalties	839	916	810	573	325	495	389	314	213
Others	379	336	325	363	299	258	229	270	212

Source: CBN, PAC Research

Fig. 5: Components of crude oil revenue (₦ billion)

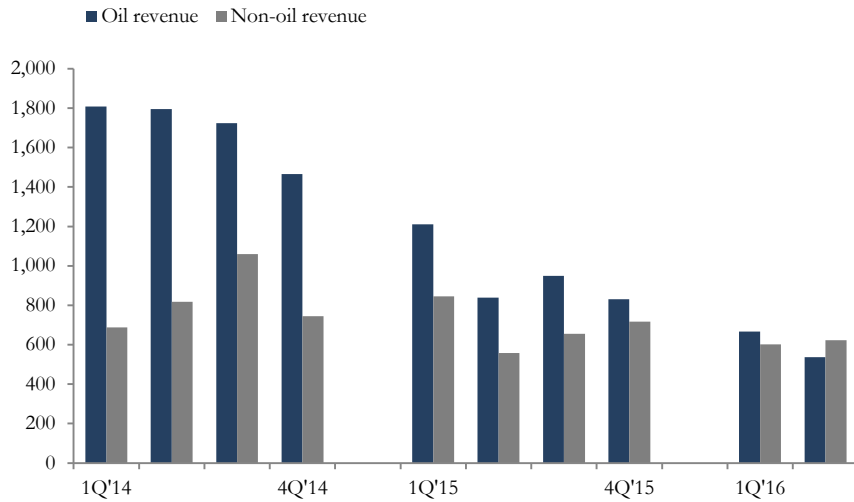


Source: CBN, PAC Research

**Non-oil revenue increases by 3.2% q/q and 11.5% y/y on the back of a higher revenue from FGN independent revenue sources.** In the review period, receipts from non-oil revenue sources improved to ₦622 billion, up by 11.5% y/y and 3.2% q/q compared with ₦558 billion in the second quarter of 2015 and ₦603 billion in the first quarter of 2016. The improvement was on the back of an increase in the revenue from independent sources by 119.1% to ₦149 billion against ₦68 billion in the corresponding quarter of the previous year. However, the revenue was lower than the budgeted estimates of ₦1,495 billion for the quarter by 58.4%. On the contrary, revenue from Value Added Tax (VAT) was down by 3.9% y/y and 1.0% q/q to ₦195 billion compared with ₦203 billion in 2Q'15 and ₦197 billion in the first quarter of the year. Also, revenue from customs and excise duties stood at ₦107 billion, down by 16.4% and 20.7% compared with ₦128 billion in the second quarter of the previous year and ₦135 billion in the preceding quarter of the year respectively. The decline in the revenue was a result of dwindling in the level of importation of goods consequent to the persistent scarcity of foreign exchange. In addition, revenue from companies income tax and other taxes declined by 2.3% q/q but it increased by 8.2% y/y to ₦172 billion against ₦176 billion respectively in 1Q'16 and ₦159 billion in 2Q'15.

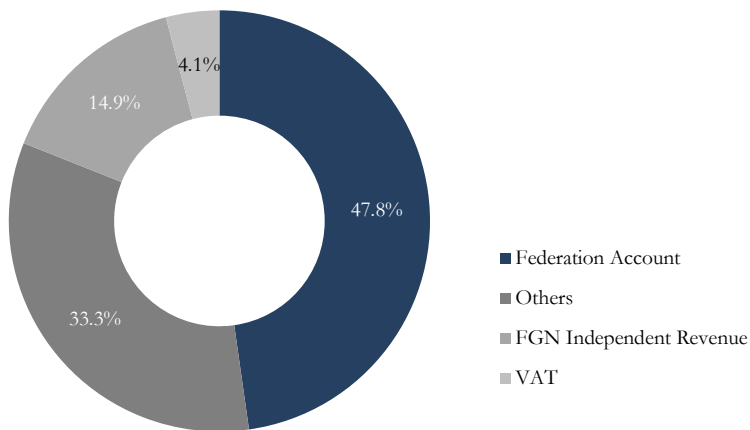
*In the review period, receipts from non-oil revenue sources improved to ₦622 billion, up by 11.5% y/y and 3.2% q/q...*

Fig. 6: Oil revenue and non-oil revenue (₦ billion)



Source: CBN, PAC Research

Fig. 7: Components of Federal Government retained revenue in 2Q'16



Source: CBN, PAC Research

Fig. 8: Components of gross non-oil sector revenue (₦ billion)



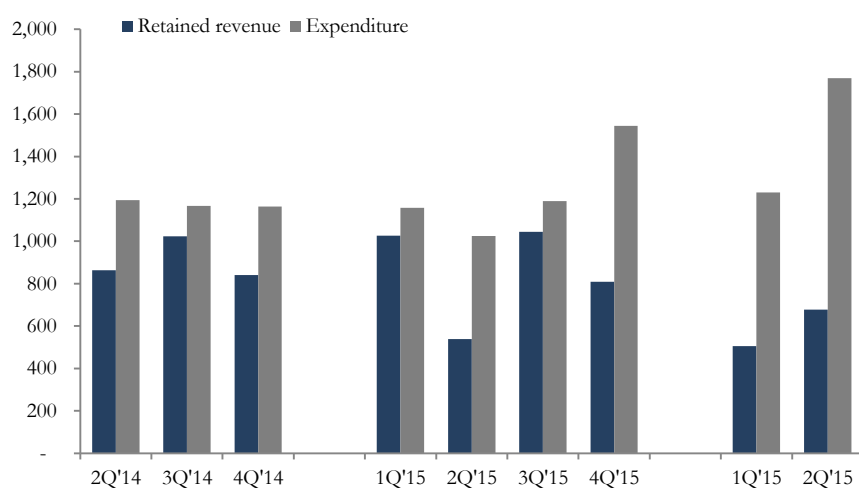
Source: CBN, PAC Research

**Table 3: Components of gross non-oil revenue (₦ billion)**

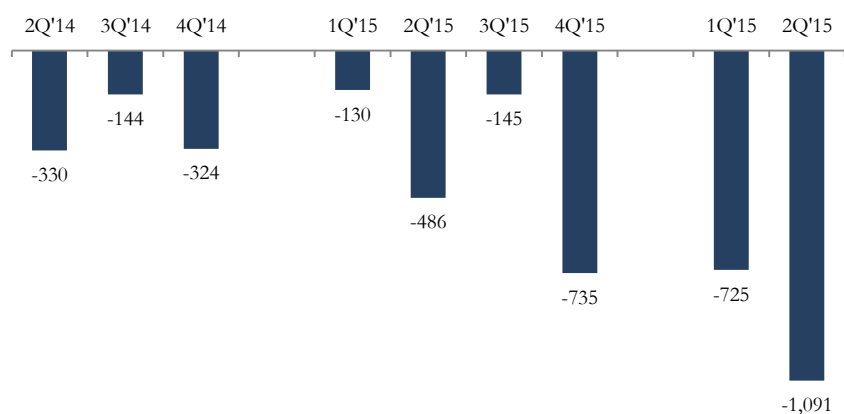
	2Q'14	3Q'14	4Q'14	1Q'15	2Q'15	3Q'15	4Q'15	1Q'16	2Q'16
Non-oil revenue	818	1,060	745	845	558	956	717	602	622
Value-added tax	194	194	193	196	203	202	178	197	195
Companies income tax	404	423	202	175	159	416	279	176	172
Customs & excise duties	136	151	157	138	128	139	142	136	107
Others	83	293	193	336	68	200	119	94	149

Source: CBN, PAC Research

**Federal Government expenditure in the review quarter exceeds budgeted estimate by 12.8%.** For the second quarter of 2016, total expenditure of Federal Government stood at ₦1,769 billion, higher than budgeted estimates of ₦1,568 billion by 12.8%. Also, the expenditure is higher by 72.6% and 43.8% compared with ₦1,025 billion and ₦1,230 billion respectively in 2Q'15 and 1Q'16. Consequently, in the review quarter deficit of ₦1,091 billion was recorded, up by 124.5% and 50.5% compared with the deficit of ₦486 billion in 2Q'15 and ₦725 billion in 1Q'16 in that order. In our view, if the trends continue in the quarters ahead, the total deficit by the end of the fiscal year may be in excess of ₦3 trillion.

**Fig. 9: Federal Government's retained revenue and expenditure (₦ billion)**

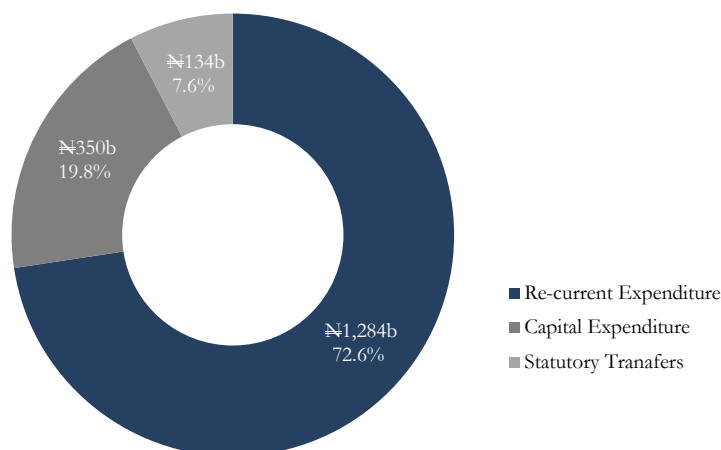
Source: CBN, PAC Research

**Fig. 10: Federal Government's fiscal deficit (₦ billion)**

Source: CBN, PAC Research

Further analysis revealed that re-current expenditure amounted to ₦1,284 billion representing 72.6% of the total expenditure while capital expenditure (₦350 billion) and statutory transfer (₦134 billion) represented 19.8% and 7.6% respectively. The increase in expenditure relative to the budgeted estimates was attributed to the rise in both re-current expenditure and capital expenditure in the period. Furthermore, non-debt component of re-current expenditure represented 73.4% while debt service accounted for 26.6%.

Fig. 11: Proportion of components of Federal Government expenditure in 2Q'16



*The increase in expenditure relative to the budgeted estimates was attributed to the rise in both re-current expenditure and capital expenditure in the period.*

Source: CBN, PAC Research

Table 4: Federal Government's fiscal operations (₦ billion)

	3Q'14	4Q'14	1Q'15	2Q'15	3Q'15	4Q'15	1Q'16	2Q'16
<b>Retained revenue</b>	<b>989</b>	<b>840</b>	<b>1,027</b>	<b>539</b>	<b>1,045</b>	<b>808</b>	<b>505</b>	<b>678</b>
Federation account	766	638	601	430	590	483	412	324
VAT account	28	28	28	29	29	26	28	28
FGN Independence revenue	133	62	280	10	17	62	40	101
Others/SURE-P	96	110	84	84	408	248	24	226
<b>Expenditure</b>	<b>1,252</b>	<b>1,164</b>	<b>1,157</b>	<b>1,042</b>	<b>1,175</b>	<b>1,544</b>	<b>1,230</b>	<b>1,769</b>
Re-current	905	870	1,033	814	1,013	945	896	1,284
Capital	237	193	60	163	72	463	221	350
Statutory transfers	111	101	64	48	90	136	114	135
<b>Deficit</b>	<b>-264</b>	<b>-324</b>	<b>-129</b>	<b>-503</b>	<b>-131</b>	<b>-736</b>	<b>-725</b>	<b>-1,091</b>

Source: CBN, PAC Research

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