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ECONOMIC POLICY AND ECONOMIC STABILITY IN NIGERIA

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ABSTRACT
The ability of an economy to support a defined level of economic production indefinitely and the country desire for minimal fluctuations in the macro-economy is a function of government policies and actions policy making institutions. Hence, this study examines the impact of economic policy (monetary policies, fiscal policies and trade policies) on economic stability. With the use ARDL approach to cointergration to analyze data 1981-2016, the study found that economic policy has a significant effect on economic stability therefore the usefulness of economic policy cannot be over-emphasized in the contribution to the Economic stability of the country.
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Keywords: Fiscal policy, Trade policy, Monetary policy, Economic Policy, Economic Stability

1. INTRODUCTION

The ability of an economy to support a defined level of economic production indefinitely and the desire for the country to have minimal fluctuations in the macro-economy is a function of the policies of the government and actions of its Central Bank. Nigeria economy dropped into recession in 2016 after more than two decades, showing negative economic shocks, conflicting economic policies, and security problems (African Economic Outlook; 2017)[3] .

The Nigerian government periodically sets policies as corrective measures for the volatile economy. The Federal Government and the Central Bank of Nigeria are taxed with setting policies to fit all aspect of government, ministries and industries with important economic component, while the Central Bank of Nigeria develops monetary policies for the financial sector, the Federal Government in conjunction with relevant agencies formulates other relevant policies for the industries

The Nigerian economy has faced the problem of excess liquidity, slow growth in gross domestic product (GDP); unpredictable inflation rate, periodic variation in external reserves, exchange rate inconsistency, yearly budget deficit and untapped revenue sources aside revenue from crude oil-causing different system of monetary and fiscal policies to evolve in Nigeria (Musasa, 2012) . Contractionary and expansionary methods are mostly used to stabilize prices, though growth has not been continuous, poverty and underdevelopment still persist in the country (Akinjare, Babajide, Areghan, and Okafor, 2016).

This study stems from the current financial turmoil which reminds that economic shock is not in smooth process. This is to determine the process through which economic policy influence the entire economy. The effectiveness of economic policies is evaluated using positivist economics which endeavours to describe how the economy and economic policies work without resorting to value judgments about which results are best. Economic policies for the purpose of this study are viewed in terms of macroeconomic stabilization policy and trade policies. Macroeconomic stabilization policies are developed with the intent of stabilizing money supply so it does not result in excessive inflation, and to unwind the business cycle. Trade policies are tariffs, trade agreements and

other policies that are developed to help promote trade by working conjointly with supply side policies which endeavour to increase productivity.

In this view, this study investigates the impact of economic policy on economic stability in Nigeria between 1986 and 2016.Specifically, the study seeks to examine the relationship between economic policies indicators and economic stability indicators in Nigeria while also measuring the impact of economic policies on economic stability in Nigeria. Hence, the paper is structured with the second Section on literature review; Section 3 presents materials and methods, Section 4 presents the results and discussion, and finally Section 5 is on conclusion and recommendation.

2. LITERATURE REVIEW

Economic policies are activities and responses meant to impact the performance of the economy which are consistently implemented and administered by the government. Economic policy is the term used to describe government actions that are intended to influence the economy by directly impacting market data (Buckley, Clegg, Voss, Cross, Liu, and Zheng; 2018 ; Moynihan and Titley; 2001 ,). On a wide view, economic policies are formulated and implemented to enhance economic efficiency, improve economic security, promote economic stability (full employment and the absence of inflation), and ensure economic growth. Generally, a policy is directed to achieve specific objectives; monetary policies are often used in combination with fiscal policies and trade policies, to influence the direction of the economy and achieve economic goals (Baker, Bloom, and Davis, 2016) .

Monetary policy is a combination of methods used by monetary authority to manage the liquidity or controls the supply of money of a country in other to create economic growth (Amadeo, 2017) . Monetary policies are actions by the monetary authorities to influence the national economic objectives by controlling the quantity and direction of money supply, target interest rate, credit and cost of credit in order to achieve the major economic goals of optimal price stability, full employment, economic growth and development and creating a broad and continuous market for government securities (Stiglitz, 2018 ; Okpara, 2010 and Salawu, 2005).

Monetary policy can equally be contractionary or expansionary methods and instruments used by the policy makers and are changed or adjusted over the years. In Nigeria, the Central Bank of Nigeria place monetary policy emphasis on market mechanisms Since1986 CBN (2017) . The policy tools commonly exploited to achieve price and financial system stability are Monetary Policy Rate (MPR), Open Market Operations (OMO), Discount Window Operations, Cash Reserve Ratio (CRR) and Foreign Exchange Net Open Position (NOP) limit (Ozsoz, Akinkunmi, Ay, and Bamidele, 2017) .

Fiscal policy on the other is the means by which a government adjusts its spending levels and tax rates to monitor and influence a nation's economy fiscal policy can be expansionary and contractionary (Speer, 2018) . Expansionary fiscal policies are formulated in periods of recession to trigger the economy. It involves the government spending more money, lowering taxes, or both so as to reduce unemployment or increase business cycle (De Grauwe; 2018) .

Trade policies are formulated to boost the nation's international trade; such trade policy includes taxes imposed on import and export, inspection regulations, and tariffs and quotas (Cadot, Gourdon, Kathuria, Malouche, and Sattar, 2016) . Trade policies are known as commercial policy or international trade policy since they are directed towards economic transactions across international borders.

Abata, Kehinde and Bolarinwa (2012) opined that fiscal and monetary policies are inextricably linked in macro-economic management and as such developments in one sector directly affect developments in the other. They further concluded that, fiscal policy is central to the health of any economy, since government's power to tax and to spend affects the disposable income of citizens and corporations, as well as the general business climate.

Shuaib, Ekeria and Ogedengbe (2015) submitted that while there is a direct relationship between fiscal policy and economic growth, the need for both monetary policy and fiscal policy to complement each other cannot be overemphasized for a stable economic growth. Abdurrahman (2010) in Sudan found that monetary policy had little impact on economic activity during the period under consideration.

Srithilat, Sun, and Thavisay, (2017) investigated the impact of monetary policy on the economic development between 1989-2016 using the Johansen Cointegration and Error Correction Models Results indicated money supply, interest rate, and inflation rate negatively effect on the real GDP per capita in the long run and only the real exchange rate has a positive sign. The error correction model result indicates the existence of short-run causality between money supply, real exchange rate and real GDP per capita.

Oboh, (2017) utilised the Set Theoretic Approach (STA) to examine the relationship between monetary and fiscal policies in Nigeria from 1981 to 2015. Results indicated a weak level of policy regulation estimated to be

17%. A further disaggregation of the results showed that the highest level of coordination of 36.4% occurred during the period of low growth and high inflation. There was no indication of regulation during periods of high GDP growth and inflation. Similarly, Itodo, Akadiri, and Ekundayo, (2017) studied the relationship and role of monetary policy in stabilizing price level in Nigeria using Vector Autoregressive (VAR) model and results showed that money supply has no significant relationship with price level in Nigeria. While Nwankwo, Kalu, and Chiekezie, (2017) highlighted the contribution of government fiscal policy to economic growth, and they showed that aggregate government expenditures results in a rise in government revenue, with revenue plunging than expenditures. Investment expenditures descend faster than recurrent expenditures resulting in the destitute economy.

Monetary policy function in a developing country is crucial in controlling money supply, promoting economic growth and price stability. Exchange rate, interest rate and money supply impact the Nigerian economy significantly while inflation does not. Monetary policies are to provide friendly investment environment by promoting the emergency of market based interest rate and exchange rate regimes that appeal to domestic and foreign investors, creating new jobs, promoting non-oil export and underutilized reviving industries (Akinjare, Babajide, Areghan, and Okafor; 2016)3

According to Pettersson-Lidbom, (2001) government debt becomes a strategic variable used by each policymaker to influence the choices of his successors. Results of the model analysis showed the equilibrium level of government debt is broad and influence the current fiscal policies in the United States and in several other countries. Alesina and Passalacqua (2016) further reviewed literature to emphasise reasons governments accumulate more debt than it would be consistent with the prescriptions of optimal fiscal policy. Kondo (2016) theoretically examined how the critical level depends on the fiscal policies, and reveals some merits of consumption taxation. As the consumption tax rate increases, so income taxation and cutting public spending become more effective in sustaining public debt. Debt policy gives rise to stability if the reaction of the primary surplus to higher public debt is sufficiently large. A strongly regressive consumption tax rate over a certain range, multiple balanced growth paths may emerge (Greiner, and Bondarev, 2015) .

Using ordinary least squares method; Onyeiwu, (2012) analysed the impact of monetary policy on the Nigerian economy between 1981 and 2008. Finding revealed monetary policy presented by money supply exerts a positive impact on GDP growth and balance of payment but negative impact on rate of inflation. Sulaiman and Migiro (2014) evaluated the nexus between monetary policy and economic growth in Nigerian by measuring economic growth using gross domestic product and monetary policy using cash reserve ratio, monetary policy rate, exchange rate, money supply, and interest rate. The co-integration test result shows that the variables are co integrated with one other and the test for causality indicates that monetary policy has a noticeable influence on the growth of the economy, while economic growth does not influence monetary policy equally significantly. This suggests that the monetary policy transmission mechanism enhances economic growth in Nigeria.

Ngerebo (2016) proxies monetary policy as monetary policy rate, treasury bill rate, savings rate, prime lending rate, maximum lending rate, growth of narrow money supply, growth of broad money supply, among others and used inflation as a proxy for economic development. The results show that monetary policy rate, treasury bill rate, prime lending rate are not statistically significant, while growth of narrow money supply, growth of broad money supply are statistically significant in relation to growth. Result depleted that monetary policy instruments are effective in managing growth while others are not.

3. DATA AND METHODOLOGY

3.1 Data

This study employed both qualitative and quantitative design with descriptive and inferential statistics. Secondary data was sourced from World Development Indicator (WDI) for a period of 36 years from 1981 - 2016. The data and their statistical properties were evaluated using both descriptive statistics and inferential statistics.

3.1 MODELLING AND ANALYSIS

The model used in this study is adapted from the study of Itodo, et al., (2017)16, Nwankwo, et al., (2017), Srithilat, etal., (2017)14, and Abataetal., (2012) with the inclusion of trade policy instruments (Import and Export) which is intended to capture the effect of trade policy on economic stability.

$$GR_t = f(TR_t, DB_t, RIR_t, MS_t, TE_t, TI_t) \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots 1$$

$$GR_t = \beta_0 + TR_t + DB_t + RIR_t + MS_t + TE_t + TI_t \ldots\ldots\ldots\ldots\ldots\ldots 2$$

where:

GR_t= Gross Domestic Product Growth Rate at time t

TR_t =Tax Revenue at time t

DB_t= Government Debt at time t

RIR_t= Real Interest Rate at time t

MS_t= Broad money supply at time t

TE_t= Total Export of goods and services at time t

TI_t= Total Import of goods and services at time t

$\beta_{0=}$ Intercept of the model

μ_t is the error term.

Note: All the independent variables are expressed as a ratio of GDP

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Table 1 Operational measurement of Variables

Variables	Proxy	Empirical studies
Economic stability	GDP growth Rate	Moynihan and Titley, (2001), Baker, Bloom, and Davis (2016)
Fiscal policies	Tax Revenue	Kondo (2016), Alesina and Passalacqua (2016), Greiner and Bondarev (2015)**Error! Bookmark not defined.** Alesina, and Tabellini, (1990)
	Government Debt	
Monetary policies	Real Interest Rate	Ngerebo-A (2016), Sulaiman and Migiro (2014), Onyeiwu (2012). Gavin (2017), Keynes (2016), Belongia and Ireland (2015), Galindo and Méndez (2014).
	Broad money supply	
Trade policies	Export of goods and services	Costinot, Donaldson, Vogel, and Werning (2015), Moïsé and Sorescu (2013), Rodriguez and Rodrik (2000), Corden (1997).
	Import of goods and services	

Source: Authors Compilation (2017)

3.3. RESULTS

Table 2 Descriptive Analysis of Data

	GR	TR	DB	MS	RIR	TE	TI
Mean	0.0444	0.0427	0.2582	0.1737	-0.0010	0.2252	0.1459
Median	0.0475	0.0365	0.1558	0.1693	0.0322	0.2213	0.1481
Maximum	0.1460	0.1310	0.6317	0.3795	0.2528	0.4959	0.2597
Minimum	-0.0757	0.0256	0.0126	0.0857	-0.4357	0.0662	0.0444
Std. Dev.	0.0439	0.0187	0.2335	0.0579	0.1659	0.1143	0.0539
Skewness	-0.2074	3.0549	0.3588	1.5965	-0.9387	0.4541	-0.0207
Kurtosis	3.3559	14.7250	1.4668	6.7547	3.7806	2.3963	2.181311
Obs	36	36	36	36	36	36	36

Source: Authors Compilation (2017)

Table 2 shows the descriptive statistics of the variables used in this study. The mean value of all the variables is positive except for real interest rate (RIR) which depicted a negative value. Gross domestic product growth rate (GR) on the average is 4.4%, suggesting that from 1981-2016, the economy grew at an average of 4.4%. The size of tax revenue as a ratio of the gross domestic product (TR) is about 4.2% suggesting that the level of

financing of the economy by the amount of tax generated is about 4.2%. Similarly, the level of debt financing in the economy is about 25%, this suggest that the government depends on debt for effective functioning of the economy. While the level of financial depth as measured using money supply as ratio of GDP (MS) shows that it is about 17 % while total export (TE) and import (TI) contributes about 22% and 14% to the economy. This suggests that the Nigerian economy depends more on debt and exportation.
Furthermore, all the variables are relatively stable given their standard deviation while total export (TE) is unstable and volatile, this suggest that government should not over rely on proceeds from exportation as they are prone to fluctuation. It was also discovered that all the variables are positively skewed except for GDP growth rate (GR), real interest rate (RIR) and total import (TI) while government debt (DB), total export (TE) and total import (TI) produces less extreme outliers based on the kurtosis value.

Unit Root Test

Before testing for causality or co-integration, it is essential to determine the order of integration for each of the variables series; hence, this study conducts the unit root test to determine the order of integration of the series. The Augmented Dickey-Fuller (ADF) tests are reported in Table 2.

Table 3 Unit root Test

Variable	T-Stat	5% Critical Value	Prob.	Order
GR	-3.1449	-2.2944	0.0323	I(0)
TR	-3.9775	-2.9484	0.0041*	I(0)
DB **D(DB)**	-1.4271 -4.4570	-2.2944 -2.9511	0.5574 0.0012*	I(1)
MS **D(MS)**	-2.0702 -5.5513	-2.9484 -2.9511	0.2573 0.0001*	I(1)
RIR	-5.8922	-2.2944	0.0000*	I(0)
TE **D(TE)**	-1.6046 -5.8145	-2.9484 -2.9511	0.4696 0.0000*	I(1)
TI **D(TI)**	-2.4646 -9.5259	-2.9484 -2.9511	0.1325 0.0000*	(1)

Sources: Authors' Computation (**Note:** significant level: * 1%. ** 5%, ***10%)

Table 3 above shows that DB, MS, TE AND TI are not stationary at level stationary but at first difference while GDP, TR and RIR are stationary at level. This implies that the variables are multileveled integrated and integrated of order one and zero. Hence, a long-run linear relationship is suspected the variables. Auto-Regression Distributive Lag (ARDL) to co-integration was used to capture the long run effect among the variables. The choice of the ARDL is consistent with the statistical properties that are integrated of order one with few that are stationary at level. There is no I(2) series that could make difficult the interpretation of the value of the F-statistics developed by Pesaran et al., (2001).

Table 4 Bound Test

Test Statistics	Value	K	Pesaran Critical Value Bound 5% 10 Bound	II Bound
F-statistics	13.58879	6	3.79	4.85

Sources: Authors' Computation

Table 4 shows the bound test carried out to investigate the long run effect of economic policy on economic stability in Nigeria. The value of the F-statistic is 13.5887and lie above the upper bound critical value 4.85 at 5% level of significance suggesting that a long run relationship exist between government economic policy and economic stability.

Table 5 Long Run Coefficients

Dependent Variable: GR				
Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.**
C	-0.006178	0.018829	-0.328100	0.7453
TR	1.203106	0.411469	2.923927	0.0068*
D(DB)	-0.071697	0.062710	-1.143316	0.2626
D(MS)	-0.413735	0.250795	-1.649697	0.1102
RIR	0.064667	0.062534	1.034123	0.3099
D(TE)	0.044894	0.124778	0.359793	0.7217
D(TI)	-0.165820	0.188843	-0.878084	0.3874
R-squared	0.326742	**Mean dependent var**		0.044526
Adjusted R-squared	0.182472	**S.D. dependent var**		0.044625
S.E. of regression	0.040349	**Akaike info criterion**		-3.405662
Sum squared resid	0.045584	**Schwarz criterion**		-3.094592
Log likelihood	66.59908	**Hannan-Quinn criter.**		-3.298281
F-statistic	2.264798	**Durbin-Watson stat**		1.414984
Prob(F-statistic)	0.065985***			

Note: Significant level: * 1%. ** 5%, ***10%

Table 5 revealed the extent to which economic policy affects economic stability in Nigeria in the long-run. As shown above, DB, MS, TI depicted negative coefficients, implying that in the long run, they have adverse effect on economic stability. This suggests that the policies set up by government in the area of money supply, government debt and importation will not result in stable economy in the long run. This is similar to the recent findings of Itodo, Akadiri, and Ekundayo, (2017)16who found no significant relationship between money supply and economic growth.

Similarly, Srithilat, Sun, and Thavisay, (2017)14also found that money supply negatively effect on real GDP per capita in the long run.

On the other hand, TR, RIR and TE depicted positive coefficients with only TR been significant at 1%. This suggest in the long run, the economic policies been implemented as related to tax generation, interest rate and exportation will yield positive result as it will enhance economic stability. Nwankwo, Kalu, and Chiekezie, (2017)17posit that government fiscal policy promotes economic growth, however, when investment expenditures descend faster than recurrent expenditures it results to a destitute economy.

While the value of r-squared shows that the independent variables bring about 32% variations in economic stability in Nigeria, this suggests that in the long run, economic policy accounts for about 32% changes in economic stability. Also, the F-statistics also suggest that in the long run, economic policy has significant effect on economic stability in Nigeria.

Table 6 Error Correction Model

Dependent Variable: GDP				
Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.***
C	-0.012242	0.013602	-0.900052	0.3807
GDP(-1)	1.314247	0.266372	4.933875	0.0001*
TR	0.050560	0.343985	0.146982	0.8849
D(DB)	-0.008661	0.055589	-0.155807	0.8780
D(DB(-1))	0.152194	0.055517	2.741368	0.0139**
D(MS)	-0.339538	0.188097	-1.805115	0.0888***
D(MS(-1))	0.391006	0.226200	1.728588	0.1020
RIR	0.119510	0.051383	2.325869	0.0327**
RIR(-1)	-0.127573	0.051613	-2.471708	0.0243**
D(TE)	0.255508	0.104872	2.436378	0.0261**
D(TE(-1))	-0.107530	0.104376	-1.030211	0.3173
D(TE(-2))	0.238114	0.115731	2.057488	0.0553***
D(TI)	-0.280240	0.170710	-1.641615	0.1190
D(TI(-1))	0.080156	0.199622	0.401540	0.6930
D(TI(-2))	-0.355121	0.175202	-2.026927	0.0586***

ECM(-1)	-1.174913	0.311357	-3.773525	0.0015*

Note: Significant level: * 1%. ** 5%, ***10%

The coefficient of the ECM is correctly signed and statistically significant, suggesting that approximately 1.17% of disequilibria from the previous year's shock converge back to the long-run equilibrium in the current year, hence, there is short run significant effect of economic policy on economic stability. Srithilat, Sun and Thavisay (2017) also indicated the existence of short-run causality between money policy and economic growth. Furthermore, the result shows that a period lag of GDP growth rate (GR); government debt (DB), money supply (MS) and total import (TI) contributes positively to economic stability in Nigeria in the short-run. This suggests that government policy on debt, money supply and total import in the previous year has the capacity to enhance economic stability. This study also confirms the study of Sulaiman and Migiro (2014) that monetary policy transmission mechanism enhances economic growth in Nigeria while Ngerebo (2016) also asserted that monetary policy instruments are effective in managing economic growth. Onyeiwu, (2012)22also revealed that monetary policy exerts a positive impact on economic growth.

On the other hand, a period lag of total export (TE) and real interest rate (RIR) has inverse effect on economic stability in Nigeria, implying that the previous year government policy on total export and real interest rate result to economic instability in the short run. While a two period lag of total export (TE) brings about a significant positive effect on economic stability, a two period lag of total import (TI) on the other hand has a significant negative effect on economic stability in the short run. Similarly, the present policies by government on tax revenue (TR), real interest rate (RIR) and total export (TE) contributes positively to economic stability while the present policies on government debt (DB), money supply (MS) and total import contributes negatively to economic stability in Nigeria. However, based on the ECM parameter, the study concludes that economic policy has a significant effect on economic stability in the short run.

Akinjare, Babajide, Areghan, and Okafor; (2016)3 opined that monetary policies provides friendly investment environment by promoting the emergency of market based interest rate and exchange rate regimes that appeal to domestic and foreign investors, hence, creating new jobs, promoting non-oil export and underutilized reviving industries. Similarly, Abata, Kehinde and Bolarinwa (2012)11opined that fiscal policy is central to the health of any economy, since government's power to tax and to spend affects the disposable income of citizens and corporations, as well as the general business climate. While Shuaib et al., (2015) also submitted that a direct relationship exists between fiscal policy and economic growth and there is need for both monetary policy and fiscal policy to complement each other to have a stable economic growth.

Table 7 Post Diagnostic Test

	F-statistic	**Prob**
Normality Test: Jarque-Bera	0.6269	0.7308
Breusch-Godfrey Serial Correlation LM Test:	1.2677	0.3100
Heteroskedasticity Test: Breusch-Pagan-Godfrey	0.7663	0.6950

Source: Authors Compilation, (2017)

The result of the Jarque-Bera Statistics suggests that the residuals are normally distributed given the probability value of 73% while the Breusch-Godfrey Serial Correlation Test shows that the probability value of F-statistic is not significant at 5% (0.31) as such we reject the null hypothesis that there is presence of serial correlation among the variables. Thus, the diagnostics indicate that the residuals are normally distributed, homoscedastic and serially uncorrelated which implies that the result of this study is not spurious and can be relied on for policy-making.

4. CONCLUSION

This study empirically examined the impact of the economic policy on the Economic stability of Nigeria from (1981-2016) so far the issue of economy policy has been restricted to monetary and fiscal policies. Previous studies empirical researched the impact of monetary and or fiscal policies on economic growth or economic stability. This study contributed to existing literature by expanding the concept of economic policies from monetary and fiscal policies by including trade policies into the economic policies.

The study concluded that the present policies by government on tax revenue, real interest rate and total export contributes positively to economic stability while the present policies on government debt, money supply and total import contributes negatively to economic stability in Nigeria. However, based on the ECM parameter, the

study concludes that economic policy has a significant effect on economic stability in the short run. On the long run, economic policy has significant effect on economic stability in Nigeria therefore the usefulness of economic policy cannot be over-emphasized in the contribution to the Economic stability of the country.

Based on the results from findings, the study recommends that policy makers should implement policies that promote lending like lowering economic policy rate to lower the rate of inflation through effective application of monetary policy, and growth in output should be formulated as these would lead to credit expansion and invariably returns and profitability of commercial banks that could impact on the economy positively. Government should implement sustainable macroeconomic policies that will promote sustainable growth, business friendly and conducive environment that will enhance capacity utilization of industries, improve import and export trade so as to allow for high level of credit demand and absorption in the economy. Policy makers should also strive to have a stable tax policies implement policies that will promote stable income for the government and fiscal policies should be implemented in line with the current economic position of the nation to maintain economic stability.

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