Resolving Nigeria's Debt Through a Discounted Buyback

Center for Global Development

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April 2005

CGD Notes

Nigeria has $33 billion in external debt. The government has been trying unsuccessfully for years to cut a deal with creditors to reduce its external obligations but to date has only managed to gain non-concessional restructuring. The major creditors also have good reasons for wanting to seek a resolution, yet agreement has been elusive. Fortunately, there is a brief window of opportunity in 2005 to find a compromise that can meet the needs of both sides. This note briefly outlines a proposal for striking such a deal through a discounted debt buyback.

Why Nigeria is in debt

The vast majority of Nigeria's $33 billion in external obligations is owed to a handful of bilateral creditors (Table 1). Indeed, just four (UK, France, Germany, and Japan) account for 65% of Nigeria's total debt. Unlike many indebted poor countries, Nigeria's debts are not from massive over-borrowing and then wasteful spending. The initial loans to Nigeria were fairly small amounts and undertaken by the civilian Shagari government in the early 1980s. The subsequent escalation of debt stock is primarily the result of accrued arrears, interest, penalties, and export credit defaults accumulated by the military governments that ruled the country from 1984-99. The current Obasanjo administration came to power in May 1999 and has since sought unsuccessfully to reduce these inherited debts. It had hoped to receive treatment similar to Paris Club 'Naples terms,' which implies a 67% stock reduction. Nigeria was also excluded from even consideration for HIPC because of its IDA status.[1] But it has failed to reach agreement with the Paris Club for anything beyond a non-concessional restructuring in December 2000.

Debt overhang impedes reforms

The debt impasse has had a severely negative effect on the ability of the Obasanjo government to enact reforms. Perceptions in parliament of unfair treatment by creditors have created resistance to allocating debt service in the budget, further alienating the creditors and, in turn, emboldening nationalist legislators. The debt issue has, in effect, immensely complicated the government's ability to push though the reforms necessary for the government to promote non-oil economic activity and reduce poverty.

Table 1: Nigeria's External Creditors, end 2003

Creditor	Debt Stock (US$ bn)	Share of Total (%)
UK	7.0	21%
France	5.6	17%
Germany	4.6	14%
Japan	4.2	13%
Italy	1.8	6%
Netherlands	1.4	4%
USA	0.9	3%
Other Paris Club	1.9	6%
Total Paris Club	*27.5*	*83%*
Multilateral Creditors	3.0	9%
Private Creditors	2.4	7%
Other Bilateral Creditors	0.1	0%
Total Debt Stock	32.9	100%

Source: Nigerian Debt Management Office

A rare opportunity

Fortuitously, Nigeria is experiencing a revenue boom from high oil prices and its foreign reserves have climbed to $17 billion by December 2004. Obasanjo's economic team, led by finance minister Ngozi Okonjo-Iweala and central bank governor Charles Soludo, also have put forward an ambitious reform plan, but its success is far from certain. A debt deal could help to tip the balance in the reformists favor; failure to reach a deal could undermine their efforts and waste a crucial opportunity to get Nigeria back on track.

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The proposal: Buy back all bilateral debt at steep discount

Nigeria could offer to pay off its entire bilateral debts this year, but at a steep discount. A fair discount might be in the range of 20-33 cents per dollar of face value, or roughly on par with the discounts inherent in Naples terms and the Iraqi Paris Club debt agreement (but creditors would have the bonus of receiving all repayment immediately rather than over an extended period). This proposal is also within the range of the recent Argentine commercial debt offer.

Such a deal would cost the Nigerians about $6-9 billion, or about the recent increase in their foreign reserves from the oil windfall (Table 2). Even if this only covered the Paris Club creditors, it would leave Nigeria with only about $5.4 billion in debt and create pressure on the remaining multilateral and private creditors for a similar discount deal.

Table 2: Estimated costs to Nigeria of debt offers to the Paris Club

	Offer scenarios (US$ billions)		
	20c Iraq discount	25c Argentina offer	33c Naples discount
UK	1.4	1.7	2.3
France	1.1	1.4	1.8
Germany	0.9	1.2	1.5
Japan	0.8	1.1	1.4
Italy	0.4	0.5	0.6
Netherlands	0.3	0.3	0.5
USA	0.2	0.2	0.3
Other Paris Club	0.4	0.5	0.6
Total cost to Nigeria	5.5	6.9	9.1

Source: author calculations

Benefits of this proposal for Nigeria

- ✓ Effectively a Naples-like debt reduction—or better
- ✓ Nigeria would finally erase the majority of its debts
- ✓ It would be an efficient and non-inflationary use of the oil windfall
- ✓ The deal is affordable now, but might not be soon
- ✓ Huge reduction in costs of debt management and administration
- ✓ A deal would help to give the reform program political momentum
- ✓ More reform could pave the way to warmer relations with creditors and eventually renewed borrowing

Benefits of this proposal for creditors

- ✓ Creditors would receive payment greater than the actual commercial value of the debt, and likely greater than their own internal valuation
- ✓ Much of the debt may be otherwise uncollectible
- ✓ Gain credit for wiping the debt in Africa's most populous country and the home of nearly 100 million people living below the poverty line
- ✓ Help bolster reformers within the government
- ✓ A show of support for a fragile nascent democracy
- ✓ Some payback for Obasanjo's leadership on peacekeeping, conflict resolution, and other regional issues, such as his personal interventions in Liberia and Togo.

A one-time offer

The Nigerian government should make a one-time offer to pay off its debt at a steep discount and the creditors should accept. In 2005 Nigeria has an unusual amount of cash on hand and an opportunity to finally resolve its debt problem. The creditors also have solid political, strategic, and humanitarian reasons to cut a deal. Missing this opportunity not only will lose creditors their best chance to collect this debt but could also threaten the economic and democratic reforms in one of Africa's largest and most pivotal countries.

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[1] See Todd Moss, Scott Standley & Nancy Birdsall (2004), "Double-Standards, Debt Treatment, and World Bank Country Classification: The case of Nigeria," Working Paper Number 45, Center for Global Development, Washington DC, November.

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